Includes summary of key provisions
U.S. GAAP vs. IFRS

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2010 Interpretation and Application of International Financial Reporting Standards

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PREFACE

IFRS: Interpretation and Application of International Financial Reporting Standards provides detailed, analytical explanations and copious illustrations of all current accounting principles promulgated by the IASB (and its predecessor, the IASC). The book integrates the accounting principles promulgated by these standard setters and by their respective bodies responsible for responding to more narrowly focused issues, the current International Financial Reporting Interpretations Committee (IFRIC), and the former Standing Interpretations Committee (SIC). These materials have been synthesized into a user-oriented topical format, eliminating the need for readers to first be familiar with the names or numbers of the salient professional standards.

IFRS have been adopted or adapted by well over one hundred nations for mandatory or optional financial reporting by public and/or private entities, with many more adoptions scheduled to occur over the next very few years. A key event signaling the growing recognition of the primacy of IFRS was the decision by the US Securities and Exchange Commission in 2007 waiving its former requirement for foreign registrants to reconcile key financial statement captions to amounts computed under US GAAP. Now, for those submitting financial statements that fully comply with IFRS, this is no longer required.

Another important event, having worldwide implications, occurred in 2008 when the SEC granted permission for qualified "early adopters" to file annual financial reports for 2009 based on IFRS, with a concomitant promise to decide in 2011, based on early experience, whether to entirely phase out US GAAP in favor of IFRS. Universal adoption of IRFS appears to now be a virtual certainty, probably within the near term, although the originally promoted target of 2014 to 2016 might conceivably slip one or a few years.

The primary objective of this book is to assist the practitioner in navigating the myriad practical problems faced in applying IFRS. Accordingly, the paramount goal has been to incorporate meaningful, real-world-type examples in guiding users in the application of IFRS to the complex fact situations that must be dealt with in the actual practice of accounting. In addition to this emphasis, a major strength of this book is that it does explain the theory of IFRS in sufficient detail to serve as a valuable adjunct to, or substitute for, accounting textbooks. Much more than a reiteration of currently promulgated IFRS, it provides the user with an understanding of the underlying conceptual basis for the rules, to enable the reasoning by analogy that is so necessary in dealing with a complex, fast-changing world of commercial arrangements and structures using principles-based standards. Since IFRS is by design less prescriptive than many national GAAP, practitioners have been left with a proportionately greater challenge in actually applying the rules. This book is designed to bridge the gap between these less detailed standards and application problems encountered in actual practice.

Each chapter of this book, or major section thereof, provides an overview discussion of the perspective and key issues associated with the topics covered; a listing of the professional pronouncements that guide practice; and a detailed discussion of the concepts and accompanying examples. A comprehensive checklist following the main text offers practical guidance to preparing financial statement disclosures in accordance with IFRS. Also included is an up-to-date, detailed, tabular comparison between IFRS and US GAAP, which remains the second most commonly encountered financial reporting standards, keyed to the chapters of this book. The book features copious examples of actual informative disclosures made by companies currently reporting under IFRS.

The authors' wish is that this book will serve practitioners, faculty, and students as a reliable reference tool, to facilitate their understanding of, and ability to apply, the complexities of the authoritative literature. Comments from readers, both as to errors and omissions and as to proposed improvements for future editions, should be addressed to Barry J. Epstein, c/o John Wiley & Sons, Inc., 155 N. 3rd Street, Suite 502, DeKalb, Illinois 60115, prior to May 15, 2010, for consideration for the 2011 edition.

Barry J. Epstein
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Dr. Epstein is a widely published authority on accounting and auditing. His current publications include *Wiley GAAP*, now in its 26th edition, for which he serves as the lead coauthor. He has also appeared on over a dozen national radio and television programs discussing the crises in corporate financial reporting and corporate governance, has presented hundreds of educational programs to professional and corporate groups in the US and internationally, and has had scores of articles published in legal, accounting, and other professional journals. He previously chaired the Audit Committee of the AICPA's Board of Examiners, responsible for the Uniform CPA Examination, and has served on other professional panels at state and national levels.

Dr Epstein holds degrees from DePaul University (Chicago—BSC, accounting and finance, 1967) University of Chicago (MBA, economics and industrial relations, 1969), and University of Pittsburgh (PhD, information systems and finance, 1979). He is a member of American Institute of Certified Public Accountants, Illinois CPA Society, and American Accounting Association

Eva K. Jermakowicz, PhD, CPA, has taught accounting for over twenty-six years and has served as a consultant to prominent international organizations and businesses. She is currently a Professor of Accounting and Chair of the Accounting and Business Law Department at Tennessee State University, Nashville, and held previous positions on the faculties of the University of Southern Indiana and Warsaw Tech University in Poland, and she has taught accounting courses in several additional countries. In 2003-2004, Dr. Jermakowicz was a Fulbright scholar under the European Union Affairs Research Program in Brussels, Belgium, where her project was "Convergence of National Accounting Standards with International Financial Reporting Standards." She was also a Fulbright scholar in Poland in 1997. Dr. Jermakowicz has consulted on international projects under the auspices of the World Bank, the United Nations, and Nicom Consulting, Ltd. Her primary areas of interest are international accounting and finance.

Dr. Jermakowicz has had numerous articles published in academic journals and conference proceedings, including *Abacus, Journal of International Accounting, Auditing & Taxation, Journal of International Financial Management & Accounting, Multinational Finance Journal, Journal of Accounting and Finance Research, Bank Accounting & Finance, Financial Executive, Strategic Finance, CPA Journal,* and *Butterworths Journal of International Banking and Financial Law*. She is a member of the American Accounting Association, European Accounting Association, American Institute of Certified Public Accountants, the Tennessee Society of CPAs, and the Institute of Management Accountants, and other professional organizations.

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1 INTRODUCTION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

The year 2005 marked the beginning of a new era in global conduct of business, and the fulfillment of a thirty-year effort to create the financial reporting rules for a worldwide capital market. For during that year's financial reporting cycle, as many as 7,000 listed companies in the 27 European Union member states, plus many others in countries such as Australia, New Zealand, Russia, and South Africa were expected (in the EU, required) to produce annual financial statements in compliance with a single set of international rules—International Financial Reporting Standards (IFRS). Many other business entities, while not publicly held and not currently required to comply with IFRS, also planned to do so, either immediately or over time, in order to conform to what is clearly becoming the new worldwide standard. Since there are about 15,000 SEC-registered companies in the USA that prepare financial statements in accordance with US GAAP (plus countless nonpublicly held companies also reporting under GAAP), the vast majority of the world's large businesses are now reporting under one or the other of these two comprehensive systems of accounting and financial reporting rules.

There were once scores of unique sets of financial reporting standards among the more developed nations ("national GAAP"). However, most other national GAAP standards have been reduced in importance or are being phased out as nations all over the world have embraced IFRS. For example, Canada announced that Canadian GAAP (which was modeled on and very similar to US GAAP) is to be eliminated and replaced by IFRS in 2011. China required that listed companies employ IFRS beginning with their 2007 financial reporting. Many others planned to follow this same path.

2007 and 2008 proved to be watershed years for the growing acceptability of IFRS. In 2007, one of the most important developments was that the SEC dropped the reconciliation (to US GAAP) requirement that had formerly applied to foreign private registrants; thereafter, those reporting in a manner fully compliant with IFRS (i.e., without any exceptions to the complete set of standards imposed by IASB) do not have to reconcile net income and shareholders' equity to that which would have been presented under US GAAP. In effect, the US SEC was acknowledging that IFRS was fully acceptable as a basis for accurate, transparent, meaningful financial reporting.

This easing of US registration requirements for foreign companies seeking to enjoy the benefits of listing their equity or debt securities in the US led, quite naturally, to a call by domestic companies to permit them to also freely choose between financial reporting under US GAAP and IFRS. By late 2008 the SEC had begun the process of acquiescence, first for the largest companies in those industries having (worldwide) the preponderance of IFRS adopters, and later for all publicly held companies. A new SEC chair took office in 2009, expressing a concern that the move to IFRS, if it were to occur, should perhaps move more slowly than had previously been indicated. In the authors' view, however, any revisiting of the earlier decision to move decisively toward mandatory use of IFRS for public company financial reporting in the US will create only a minor delay, if any. Simply put, the worldwide trend to uniform financial reporting standards (for which role the only candidate is IFRS) is inexorable and will benefit all those seeking to raise capital and all those seeking to invest.

It had been highly probable that nonpublicly held US entities would have remained bound to only US GAAP for the foreseeable future, both from habit and because no other set of standards would be viewed as being acceptable. However, the body that oversees the private-sector auditing profession's standards in the US amended its rules in 2008 to fully recognize IASB as an accounting standard-setting body (giving it equal status with the FASB), meaning that auditors and other service providers in the US may now opine (or provide other levels of assurance, as specified under pertinent guidelines) on IFRS-based financial statements. This change, coupled with the promulgation by IASB of a long-sought standard providing simplified financial reporting rules for privately held entities (described later in this chapter), has probably increased the likelihood that a broad-based move to IFRS will occur in the US within the next several years.

The impetus for the convergence of historically disparate financial reporting standards has been, in the main, to facilitate the free flow of capital so that, for example, investors in the United States will become more willing to finance business in, say, China or the Czech Republic. Having access to financial statements that are written in the same "language" would eliminate what has historically been a major impediment to engendering investor confidence, which is sometimes referred to as "accounting risk," which adds to the already existing risks of making such cross-border investments. Additionally, the permission to list a company's equity or debt securities on an exchange has generally been conditioned on making filings with national regulatory authorities, which have historically insisted either on conformity with local GAAP or on a formal reconciliation to local GAAP. Since either of these procedures was tedious and time-consuming, and the human resources and technical knowledge to do so were not always widely available, many otherwise anxious would-be registrants forwent the opportunity to broaden their investor bases and potentially lower their costs of capital.

The authors believe that these difficulties are soon coming to an end, however. The historic 2002 Norwalk Agreement—between the US standard setter, FASB, and the IASB—called for "convergence" of the respective sets of standards, and indeed a number of revisions of either US GAAP or IFRS have already taken place to implement this commitment, with more changes expected in the immediate future. These changes are identified in the following table:

Financial Reporting Topic	*US GAAP Converged to IFRS*	*IFRS Converged to US GAAP*
Share-based payments	FAS 123 adopted aspects of IFRS 2	
Business combinations	FAS 141(R) adopted elements of IFRS 3	Revised IFRS 3 adopted aspects of FAS 141(R)
Inventory costs	FAS 151 adopted elements of IAS 2	
Exchanges of nonmonetary assets	FAS 153 adopted approach used by IAS 16	
Accounting changes and corrections of errors	FAS 154 adopted requirements under IAS 8	
Fair value option for reporting financial instruments	FAS 159 adopted option under IAS 39	
Reporting noncontrolling interests in consolidated financial statements	FAS 160 converges with IAS 27	IAS 27 conforms with FAS 160
Subsequent events reporting	FAS 165 brings guidance formerly in the auditing literature into US GAAP requirements	IAS 1 requirements had always included guidance on reporting of subsequent events
Transfers of financial instruments	FAS 166 converges with IFRS guidance	
Special purpose/variable interest entities	FAS 167 converges with IFRS guidance	
Noncurrent assets held for sale and reporting of discontinued operations		IFRS 5 largely conforms with FAS 146 under US GAAP
Reporting segments of the business		IFRS 8 conforms to FAS 131
Income taxes		Proposal currently outstanding largely converges on FAS 109 and other US GAAP literature
Construction period interest		Revised IAS 23 adopts mandatory capitalization per US GAAP
Leases	Joint project will result in convergence	Currently outstanding Exposure Draft will result in convergence

Several other convergence projects are still under joint development by IASB and FASB. The completion date for all these projects has now been set at no later than June 2011. It thus is anticipated that by that date all or virtually all distinctions between US GAAP and IFRS will be eliminated, even if US GAAP remains an independent set of financial reporting rules, notwithstanding that there remain challenging issues to be resolved before full convergence can occur. For one very important example, while IFRS bans the use of LIFO costing for inventories, it remains a popular financial reporting method under US GAAP because of a "conformity rule" that permits entities to use the method for tax reporting only if it is also used for general-purpose external financial reporting. In times of increasing costs, LIFO almost inevitably results in tax deferrals and is thus widely employed. US-based companies will be reluctant to fully embrace IFRS if it means that this tax strategy must be abandoned.

Origins and Early History of the IASB

Financial reporting in the developed world evolved from two broad models, whose objectives were somewhat different. The earliest systematized form of accounting regulation developed in continental Europe, starting in France in 1673. Here a requirement for an annual fair value statement of financial position was introduced by the government as a means of protecting the economy from bankruptcies. This form of accounting at the initiative of the state to control economic actors was copied by other states and later incorporated in the 1807 Napoleonic Commercial Code. This method of regulating the economy expanded rapidly throughout continental Europe, partly through Napoleon's efforts and partly through a willingness on the part of European regulators to borrow ideas from each other. This "code law" family of reporting practices was much developed by Germany after its 1870 unification, with the emphasis moving away from market values to historical cost and systematic depreciation. It was used later by governments as the basis of tax assessment when taxes on business profits started to be introduced, mostly in the early twentieth century.

This model of accounting serves primarily as a means of moderating relationships between the individual company and the state. It serves for tax assessment, and to limit dividend payments, and it is also a means of protecting the running of the economy by sanctioning individual businesses that are not financially sound or were run imprudently. While the model has been adapted for stock market reporting and group (consolidated) structures, this is not its main focus.

The other model did not appear until the nineteenth century and arose as a consequence of the industrial revolution. Industrialization created the need for large concentrations of capital to undertake industrial projects (initially, canals and railways) and to spread risks between many investors. In this model the financial report provided a means of monitoring the activities of large businesses in order to inform their (nonmanagement) shareholders. Financial reporting for capital markets purposes developed initially in the UK, in a common-law environment where the state legislated as little as possible and left a large degree of interpretation to practice and for the sanction of the courts. This approach was rapidly adopted by the US as it, too, became industrialized. As the US developed the idea of groups of companies controlled from a single head office (towards the end of the nineteenth century), this philosophy of financial reporting began to become focused on consolidated accounts and the group, rather than the individual company. For different reasons, neither the UK nor the US governments saw this reporting framework as appropriate for income tax purposes, and in this tradition, while the financial reports inform the assessment process, taxation retains a separate stream of law, which has had little influence on financial reporting.

The second model of financial reporting, generally regarded as the Anglo-Saxon financial reporting approach, can be characterized as focusing on the relationship between the business and the investor, and on the flow of information to the capital markets. Government still uses reporting as a means of regulating economic activity (e.g., the SEC's mission is to protect the investor and ensure that the securities markets run efficiently), but the financial report is aimed at the investor, not the government.

Neither of the two above-described approaches to financial reporting is particularly useful in an agricultural economy, or to one that consists entirely of microbusinesses, in the opinion of many observers. Nonetheless, as countries have developed economically (or as they were colonized by industrialized nations) they have adopted variants of one or the other of these two models.

IFRS are an example of the second, capital market-oriented, systems of financial reporting rules. The original international standard setter, the International Accounting Standards Committee (IASC), was formed in 1973, during a period of considerable change in accounting regulation. In the US the Financial Accounting Standards Board (FASB) had just been created, in the UK the first national standard setter had recently been organized, the EU was working on the main plank of its own accounting harmonization plan (the Fourth Directive), and both the UN and the OECD were shortly to create their own accounting committees. The IASC was launched in the wake of the 1972 World Accounting Congress (a five-yearly get-together of the international profession) after an informal meeting between representatives of the British profession (Institute of Chartered Accountants in England and Wales—ICAEW) and the American profession (American Institute of Certified Public Accountants—AICPA).

A rapid set of negotiations resulted in the professional bodies of Canada, Australia, Mexico, Japan, France, Germany, the Netherlands, and New Zealand being invited to join with the US and UK to form the international body. Due to pressure (coupled with a financial subsidy) from the UK, the IASC was established in London, where its successor, the IASB, remains today.

The actual reasons for the IASC's creation are unclear. A need for a common language of business was felt, to deal with a growing volume of international business, but other more political motives abounded also. For example, some believe that the major motivation was that the British wanted to create an international standard setter to trump the regional initiatives within the EU, which leaned heavily to the Code model of reporting, in contrast to what was the norm in the UK and almost all English-speaking nations.

In the first phase of its existence, the IASC had mixed fortunes. Once the International Federation of Accountants (IFAC) was formed in 1977 (at the next World Congress of Accountants), the IASC had to fight off attempts to become a part of IFAC. It managed to resist, coming to a compromise where IASC remained independent but all IFAC members were automatically members of IASC, and IFAC was able to nominate the membership of the standard-setting Board.

Both the UN and OECD were active in international rule making in the 1970s but the IASC was successful in persuading them to leave establishment of recognition and measurement rules to the IASC. However, having established itself as the unique international rule maker, IASC encountered difficulty in persuading any jurisdiction or enforcement agency to use its rules. Although member professional bodies were theoretically committed to pushing for the use of IFRS at the national level, in practice few national bodies were influential in standard setting in their respective countries (because standards were set by taxation or other governmental bodies), and others (including the US and UK) preferred their national standards to whatever IASC might propose. In Europe, IFRS were used by some reporting entities in Italy and Switzerland, and national standard setters in some countries such as Malaysia began to use IFRS as an input to their national rules, while not necessarily adopting them as written by the IASC or giving explicit recognition to the fact that IFRS were being adopted in part as national GAAP.

IASC's efforts entered a new phase in 1987, which led directly to its 2001 reorganization, when the then-Secretary General, David Cairns, encouraged by the US SEC, negotiated an agreement with the International Organization of Securities Commissions (IOSCO). IOSCO was interested in identifying a common international "passport" whereby companies could be accepted for secondary listing in the jurisdiction of any IOSCO member. The concept was that, whatever the listing rules in a company's primary stock exchange, there would be a common minimum package which all stock exchanges would accept from foreign companies seeking a secondary listing. IOSCO was prepared to endorse IFRS as the financial reporting basis for this passport, provided that the international standards could be brought up to a quality and comprehensiveness level that IOSCO stipulated.

Historically, a major criticism of IFRS had been that it essentially endorsed all the accounting methods then in wide use, effectively becoming a "lowest common denominator" set of standards. The trend in national GAAP had been to narrow the range of acceptable alternatives, although uniformity in accounting had not been anticipated as a near-term result. The IOSCO agreement energized IASC to improve the existing standards by removing the many alternative treatments that were then permitted under the standards, thereby improving comparability across reporting entities. The IASC launched its *Comparability and Improvements Project* with the goal of developing a "core set of standards" that would satisfy IOSCO. These were complete by 1993, not without difficulties and spirited disagreements among the members, but then—to the great frustration of the IASC—these were not accepted by IOSCO. Rather than endorsing the standard-setting process of IASC, as was hoped for, IOSCO seemingly wanted to cherry-pick individual standards. Such a process could not realistically result in near-term endorsement of IFRS for cross-border securities registrations.

Ultimately, the collaboration was relaunched in 1995, with IASC under new leadership, and this began a further period of frenetic activities, where existing standards were again reviewed and revised, and new standards were created to fill perceived gaps in IFRS. This time the set of standards included, among others, IAS 39, on recognition and measurement of financial instruments, which was endorsed, at the very last moment and with great difficulty, as a compromise, purportedly interim standard.

At the same time, the IASC had undertaken an effort to consider its future structure. In part, this was the result of pressure exerted by the US SEC and also by the US private sector standard setter, the FASB, which were seemingly concerned that IFRS were not being developed by "due process." While the various parties may have had their own agendas, in fact the IFRS were in need of strengthening, particularly as to reducing the range of diverse but accepted alternatives for similar transactions and events. The challenges presented to IASB ultimately would serve to make IFRS stronger.

If IASC was to be the standard setter endorsed by the world's stock exchange regulators, it would need a structure that reflected that level of responsibility. The historical Anglo-Saxon standard-setting model—where professional accountants set the rules for themselves—had largely been abandoned in the twenty-five years since the IASC was formed, and standards were mostly being set by dedicated and independent national boards such as the FASB, and not by profession-dominated bodies like the AICPA. The choice, as restructuring became inevitable, was between a large, representative approach—much like the existing IASC structure, but possibly where national standard setters appointed representatives—or a small, professional body of experienced standard setters which worked independently of national interests.

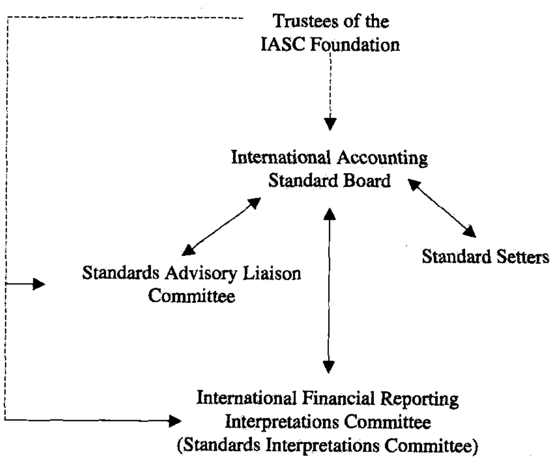
The end of this phase of the international standard setting, and the resolution of these issues, came about within a short period in 2000. In May of that year, IOSCO members voted to endorse IASC standards, albeit subject to a number of reservations (see discussion later in this chapter). This was a considerable step forward for the IASC, which itself was quickly exceeded by an announcement in June 2000 that the European Commission intended to adopt IFRS as the requirement for primary listings in all member states. This planned full endorsement by the EU eclipsed the lukewarm IOSCO approval, and since then the EU has appeared to be the more influential body insofar as gaining acceptance for IFRS has been concerned. Indeed, the once-important IOSCO endorsement has become of little importance given subsequent developments, including the EU mandate and convergence efforts among several standard-setting bodies.

In July 2000, IASC members voted to abandon the organization's former structure, which was based on professional bodies, and adopt a new structure: beginning in 2001, standards would be set by a professional board, financed by voluntary contributions raised by a new oversight body.

The Current Structure

The formal structure put in place in 2000 has the IASC Foundation, a Delaware corporation, as its keystone. The Trustees of the IASC Foundation have both the responsibility to raise the $19 million a year currently needed to finance standard setting, and the responsibility of appointing members to the International Accounting Standards Board (IASB), the International Financial Reporting Interpretations Committee (IFRIC) and the Standards Advisory Council (SAC).

The Standards Advisory Council (SAC) meets with the IASB three times a year, generally for two days. The SAC consists of about 50 members, nominated in their personal (not organizational) capacity, but are usually supported by organizations that have an interest in international reporting. Members currently include analysts, corporate executives, auditors, standard setters, and stock exchange regulators. The members are supposed to serve as a channel for communication between the IASB and its wider group of constituents, to suggest topics for the IASB's agenda, and to discuss IASB proposals.



The International Financial Reporting Interpretations Committee (IFRIC) is a committee comprised mostly of technical partners in audit firms but also includes preparers and users. It succeeded the Standards Interpretations Committee (SIC), which had been created by the IASC. IFRIC's function is to answer technical queries from constituents about how to interpret IFRS—in effect, filling in the cracks between different rules. In recent times it has also proposed modifications to standards to the IASB, in response to perceived operational difficulties or need to improve consistency. IFRIC liaises with the US Emerging Issues Task Force and similar bodies liaison as standard setters, to try at preserve convergence at the level of interpretation. It is also establishing relations with stock exchange regulators, who may be involved in making decisions about the acceptability of accounting practices, which will have the effect of interpreting IFRS.

The liaison standard setters are national bodies from Australia, Canada, France, Germany, UK, USA, and Japan. Each of these bodies has a special relationship with a Board member, who normally maintains an office with the national standard setter and is responsible for liaison between the international body and the national body. This, together with the SAC, was the solution arrived at by the old IASC in an attempt to preserve some degree of geographical representation. However, this has been somewhat overtaken by events: as far as the EU is concerned, its interaction with the IASB is through EFRAG (see below), which has no formal liaison member of the Board. The IASB Deputy Chairman has performed this function, but while France, Germany and the UK individually have liaison, EFRAG and the European Commission are, so far, outside this structure.

Furthermore, there are many national standard setters, particularly from developing countries, that have no seat on the SAC, and therefore have no direct link with the IASB, despite the fact that many of them seek to reflect IASB standards in their national standards. At the 2002 World Congress in Hong Kong, the IASB held an open meeting for national standard setters, which was met with enthusiasm. As a result, IASB began to provide time concurrent with formal liaison standard setters' meetings for any other interested standard setters to attend. While this practice was not enshrined in either the Constitution or the IASB's operating procedures, both remain under active review as of late 2009.

Process of IFRS Standard Setting

The IASB has a formal due process which is set out in the *Preface to IFRS*, revised in 2001. At a minimum, a proposed standard should be exposed for comment, and these comments should be reviewed before issuance of a final standard, with debates open to the public. However, this formal process is rounded out in practice, with wider consultation taking place on an informal basis.

The IASB's agenda is determined in various ways. Suggestions are made by the Trustees, the SAC, liaison standard setters, the international audit firms and others. These are debated by IASB and tentative conclusions are discussed with the various consultative bodies. The IASB also has a joint agenda committee with the FASB. Long-range projects are first put on the research agenda, which means that preliminary work is being done on collecting information about the problem and potential solutions. Projects can also arrive on the current agenda outside that route.

The agenda was largely driven in the years immediately after 2001 by the need to round out the legacy standards, to ensure that there would be a full range of standards for European companies moving to IFRS in 2005. Also, it was recognized that there was an urgent need to effect modifications to many standards in the name of convergence (e.g., acquisition accounting and goodwill) and to make needed improvements to other existing standards. These needs were largely met by mid-2004.

Once a project reaches the current agenda, the formal process is that the staff (a group of about 20 technical staff permanently employed by the IASB) drafts papers which are then discussed by IASB in open meetings. Following that debate, the staff rewrites the paper, or writes a new paper which is then debated at a subsequent meeting. In theory there is an internal process where the staff proposes solutions, and IASB either accepts or rejects them. In practice the process is more involved: sometimes (especially for projects such as financial instruments) individual Board members are delegated special responsibility for the project, and they discuss the problems regularly with the relevant staff, helping to build the papers that come to the Board. Equally, Board members may write or speak directly to the staff outside of the formal meeting process to indicate concerns about one thing or another.

The process usually involves: (1) discussion of a paper outlining the principal issues; (2) preparation of an Exposure Draft that incorporates the tentative decisions taken by the Board—during which process many of these are redebated, sometimes several times; (3) publication of the Exposure Draft; (4) analysis of comments received on the Exposure Draft; (5) debate and issue of the final standard, accompanied by application guidance and a document setting out the *Basis for Conclusions* (the reasons why IASB rejected some solutions and preferred others). Final ballots on the Exposure Draft and the final standard are carried out in secret, but otherwise the process is quite open, with outsiders able to consult project summaries on the IASB Web site and attend Board meetings if they wish. Of course, the informal exchanges between staff and Board on a day-to-day basis are not visible to the public, nor are the meetings where IASB takes strategic and administrative decisions.

The basic due process can be modified in different circumstances. If the project is controversial or particularly difficult, IASB may issue a discussion paper before proceeding to Exposure Draft stage. It reissued a discussion paper on stock options before proceeding to IFRS 2, *Share-Based Payment*. It is also following this pattern with its financial statement presentation project and its project on standards for small and medium-sized entities. Such a discussion paper may just set out what the staff considers to be the issues, or it may do that as well as indicate the Board's preliminary views.

IASB may also hold some form of public consultation during the process. For example, when revising IAS 39, *Financial Instruments: Recognition and Measurement,* in 2003, IASB held round table discussions. Respondents to the Exposure Draft were invited to participate in small groups with Board members where they could put forward their views and engage in debate.

Apart from these formal consultative processes, IASB also carries out field trials of some standards (as it recently did on performance reporting and insurance), where volunteer preparers apply proposed new standards. The international audit firms receive IASB papers as a result of their membership on IFRIC and are also invited to comment informally at various stages of standard development.

Constraints

The debate within IASB demonstrates the existence of certain pervasive constraints that will influence the decisions taken by it. A prime concern has, heretofore, been achieving *convergence.* In October 2002, the IASB signed an agreement with the FASB (the so-called Norwalk Agreement) stating that the two boards would seek to remove differences and converge on high-quality standards. This agreement set in motion short-term adjustments and both standard setters subsequently issued a number of Exposure Drafts and final standards changing their respective standards in order to converge with the other on certain issues. The agreement also involved a commitment to the long-term development of joint projects (business combinations, performance reporting, revenue recognition, etc.).

The desire for convergence was driven to a great extent by the perception that international investment is made riskier by the use of multiple reporting frameworks, and that the global capital market would benefit from the imposition of a single global reporting basis—but also specifically by the knowledge that European companies that wished to be listed in the US needed to provide reconciliations of their equity and earnings to US GAAP when they did this. Foreign companies registered with the SEC are required to prepare an annual filing on Form 20-F that, until late 2007—unless the reporting entity prepared its financial statements under US GAAP—required a reconciliation between the entity's IFRS or national GAAP and US GAAP for earnings and equity. This reconciliation was said to be costly to prepare, and resulted in companies reporting, in effect, two different operating results for the year, which was not always understood or appreciated by the capital markets. As of year-end 2007, this requirement was eliminated, provided that the foreign private issuers (i.e., SEC registrants) complied fully with IFRS. Note that IFRS as adopted by the European Union contains departures from IFRS as promulgated by the IASB, and thus reconciliation has not been (thus far, at least) waived.