COMPANY FINANCIAL STATEMENTS AND COMPARMENT BETWEEN U.S.GAAP AND IFRS

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Abstract:
The paper is a overview if you prepare financial statements in accordance with U.S. Generally Accepted Accounting Principles (GAAP) or International Financial Reporting Standards (IFRS). International Financial Reporting Standards (IFRS) are now required for consolidated financial reports for all European Union exchange-listed companies. Other countries have also adopted IFRS or IFRS-equivalent financial reporting standards. IFRS differ from U.S. Generally Accepted Accounting Principles (GAAP) in many key areas. The International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) are working on various convergence projects designed to reduce or eliminate differences between the two sets of reporting standards.

Key words: *financial statements, accounting U.S. GAAP, IFRS, FASB, IASB*

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Differences in accounting principles

A most frequent method applied to measure economic activity is different among the countries around the world. Country's legal, economic, political and educational system; stages of technological development; tradition and culture; and various other socioeconomic factors all influence the development of accounting standards and the accounting profession in that nation. All the deference's brought us to significant diversity in accounting standards from one nation to another. The lack of a uniform set of accounting standards generates problems for firms, prepares and users. Some countries develop their accounting principles based on the information needed by the taxing authorities. Other countries have accounting principles designed to meet the needs of the central government economic planners. U.S. accounting standards focus on the information needs of the common stockholder or the creditors.

Another major financial reporting model is in the process of being developed by the International Accounting Standards Board (IASB). The IASB has a mandate to establish a set of international financial reporting standards and to encourage adoption of those standards globally. There are 14 members of the IASB, of whom 12 are full time members (i.e., employed only by the IASB). The IASB requires that its membership be composed of the followings: five formal auditors, three former preparers of accounts, three former users of accounts, and one academic. The remaining two members may have any of these or other backgrounds.

IASB repaced International Financial Reporting Standards (IFRS). Prior to the formation of the IASB, Financial Reporting Standards (IFRS) were issued by the International Accounting Standards Committee. IAS's were issued between 1973 and 2001. The IASB adopted all IAS's and continued their development, calling new standards IFRS's. Although IAS are no longer produced, they are still in effect unless replaced by an IFRS. IFRS's are used in many countries around the world, including Singapore, Hong Kong, Russia, Australia, Romania, and South Africa. The European

Commission has required all publicly listed companies in the European Union (EU) to provide their consolidated financial statements using IFRS's beginning with the year 2005. Prior to 2005 there where around 350 publicly listed companies that used IFRS's; as of 2005, the number has grown to around 7.000. The IASB Website presents a list of the countries that require or allow IFRS for securities filings in that country.

When measured by market capitalization, U.S. GAAP is used by more than half of the world's companies. IFRS's are now also relatively widely used, given their adoption by the European Union and others. Many feel that a single set of high-quality global accounting standards would improve investor confidence in the market and serve to increase market efficiency by allowing investors to draw better comparison among investment options from different countries

The proposed balance sheet, or as it is formally called, the "Statement of Financial Position," exhibits a number of striking features. First, the Statement of Financial Position isn't organized into the traditional sections of assets, liabilities, and equity. Rather, it is organized into five sections: Business, Financing, Income Taxes, Discontinued Operations, and Equity. The Business section of the Statement of Financial Position presents both assets and liabilities that are related to the reporting entity's "business activities," i.e., the operating and investing activities through which the entity creates value. The Financing section lists assets and liabilities that relate to how the reporting entity funds or finances its business activities from *no owner* sources of capital. Financing from *owner* sources is detailed in the Equity section.

The Financial statements section contain the assets and liabilities associated with the reporting companies continuing operations, and assets and liabilities associated with discontinued operations are contained another section. One of the exceptions regards the income-tax assets and liabilities. These are presented separately in the section of the Income Taxes.

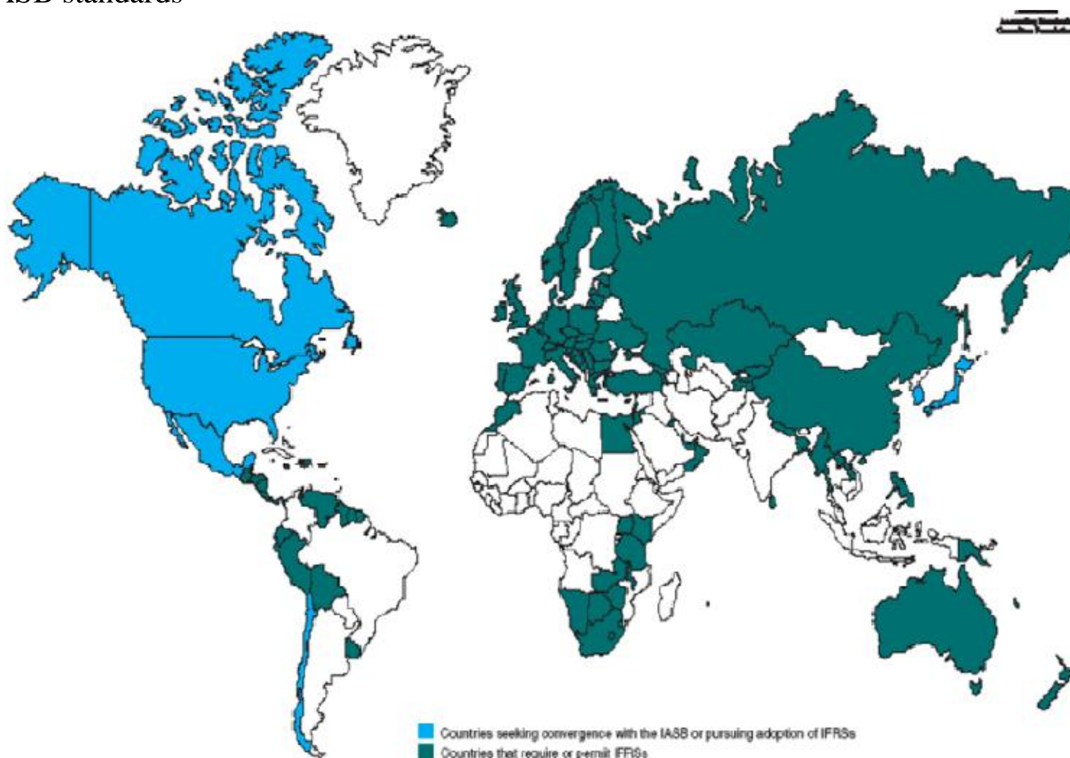
This method becomes more apparent, in what regards the Statement of Comprehensive Income, statement which is organized into five sections—Business, Financing, Income Taxes, Discontinued Operations, and Other Comprehensive Income—that largely parallel the sections presented in the Statement of Financial Position. The Business and Financing sections of the Statement of Comprehensive Income present items of income and expense relating to the firms ongoing activities regarding business and financing. The effects of the income-tax of those activities on comprehensive income are presented in a section separately, meanwhile incomes and expense items related to discontinued operations are presented on their own on an after-tax basis. The elements of the Other Comprehensive Income are presented separately from the traditional components of Net Income or Profit or Loss.

The main structure of the Statements of Financial Position and Comprehensive Income are repeated in the Statement of Cash Flows. This is specific to the Statement of Cash Flows which is organized into Business, Financing, Income Taxes, Discontinued Operations, and Equity sections. In a traditional fashion the distinction between operating and investing cash flows is preserved within the Business section, reveling a new distinction that's made between operating and investing items from the Business section of the Statements of Financial Position and Comprehensive Income. If we try separating cash flows associated with income taxes, discontinued operations, and transactions with equity holders in their own categories is a significant difference from the current practice. The Statement of Cash Flows would be made on a direct basis, which is currently recommended by both the FASB and the IASB but are very rarely applied in practice.

The remaining principal financial statement, the Statement of Changes in Equity, won't change and will continue to be required as part of a complete set of financial

statements. There are many additional changes that the FASB and the IASB have proposed; however, relating to all of the financial statements, and those changes will be explored next month. But before I conclude this month's column, a few words are in order about why the Boards are proposing such profound changes to the most visible and most fundamental elements of the financial reporting supply chain.

There are more than 100 countries which use IFRS's or are convergent with IASB standards



Some differences between IFRS and US GAAP highlighted in the financial statements

International Financial Reporting Standards (IFRS) are now required for consolidated financial reports for all European Union exchange-listed companies. Other countries have also adopted IFRS or IFRS-equivalent financial reporting standards. IFRS differ from U.S. Generally Accepted Accounting Principles (GAAP) in many key areas. The International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) are working on various convergence projects designed to reduce or eliminate differences between the two sets of reporting standards.

IAS 1, Comparative prior year financial statements

IFRS: One year comparative financial information is required.
US: US GAAP states that comparatives are "desirable". SEC regulations generally require three years of comparative financial information (balance sheet two years).
IAS 1, Classification of liabilities on refinancing

IFRS: Noncurrent if refinancing is completed before balance sheet date.
US: Noncurrent if refinancing is completed before date of issue of the financial statements.
Status: FASB exposure draft proposing the IASB approach is expected
IAS 2, Method for determining inventory cost

IFRS: LIFO is prohibited.
US: LIFO is permitted.

IAS 7, Classification of interest received and paid in the cash flow statement

IFRS: May be classified as an operating, investing, or financing activity.

US: Must be classified as an operating activity.

IAS 8, Change in depreciation method for existing assets

IFRS: Change in estimate (prospective).
US: Change in accounting policy (cumulative effect in net profit or loss).
Status: FASB has issued an exposure draft proposing to adopt the IASB approach
IAS 12, Recognition of taxable temporary differences that arise from the initial recognition of an asset or liability in a transaction that is (a) not a business combination and (b) does not affect accounting profit or taxable profit

IFRS: Deferred tax not recognized. Nor are changes in this unrecognized deferred tax asset or liability subsequently recognized.

US: No similar 'initial recognition exemption'.
Status: FASB and IASB are addressing some IAS 12/SFAS 109 differences in their short-term convergence projects.
IAS 16, Basis of property, plant, and equipment
IFRS: May use either revalued amount or historical cost. Revalued amount is fair value at date of revaluation less subsequent accumulated depreciation and impairment losses.
US: Generally required to use historical cost.
Status: Revalued amount continues to be an accounting policy choice under the IASB's 2003 revisions to IAS 16.
IAS 16, Gains and losses on exchanges of similar non-current assets

IFRS: Gain or loss recognized.
US: Gain or loss recognition is prohibited.
Status: FASB has issued an exposure draft proposing to adopt the IASB approach.
IAS 23, Income on temporary investment of funds borrowed for construction of an asset

IFRS: Reduces borrowing cost eligible for capitalization.

US: Generally does not reduce borrowing cost eligible for capitalization.
IAS 27, Accounting for investments in subsidiaries in parent-company financial statements

IFRS: Either cost method or use IAS 39, but not equity method.
US: Equity method is allowed.
Status: December 2003 revision to IAS 27 prohibited the equity method.
IAS 27, Presentation of minority interest

IFRS: In equity.

US: Outside of equity, between liabilities and equity.

Status: FASB is reconsidering this issue as part of its convergence project.
IAS 28, Accounting for investments in associates in parent-company financial statements

IFRS: Either cost method or use IAS 39, but not equity method.
US: Equity method is allowed.
Status: December 2003 revision to IAS 28 prohibited the equity method.
IAS 29, Adjusting financial statements of an entity that operates in a hyperinflationary economy

IFRS: Adjust using a general price level index before translating.

US: An entity that operates in a hyperinflationary economy must use the functional currency of its parent, rather than its own hyperinflationary currency, to prepare its financial statements.
IAS 31, Investments in joint ventures

IFRS: May use either the equity method or proportionate consolidation.
US: Generally use the equity method (except in construction and oil and gas industries).
IAS 33, Disclosures of earnings per share

IFRS: Basic and diluted income from continuing operations per share and net profit or loss per share.
US: Basic and diluted income from continuing operations, discontinuing operations, extraordinary items, cumulative effect of a change in accounting policy, and net profit or loss per share.
Status: IASB considered this as part of its Improvements Project.
IAS 36, Level of impairment testing for goodwill

IFRS: Cash generating unit (CGU) or group of CGUs that represent the lowest level at which goodwill is monitored for internal management purposes – but not larger than a business or geographical segment.
US: Reporting unit – either a business segment or one organisational level below.
IAS 36, Calculating impairment of goodwill

IFRS: One-step: compare recoverable amount of a CGU (higher of (a) fair value less costs to sell and (b) value in use) to carrying amount.
US: Two steps: 1. Compare FV of the reporting unit with its carrying amount including goodwill. If FV is greater than carrying amount, no impairment (skip step 2). 2. Compare implied FV of goodwill with carrying amount.
IFRS 3, Combinations of entities under common control

IFRS: Outside the scope of IFRS 3, though merger accounting (pooling of interests method) is generally used in practice.
US: Pooling of interests method is required.
Status: This is included in the scope of Phase II of IASB's business combinations project.

Conclusions

The IASB and the FASB are working on a joint project on discontinued operations. The Boards intend to converge the definition of 'discontinued operations' and the disclosures for components of an entity that have been disposed of. Exposure drafts from both Boards are expected in the third quarter of 2008.

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