

IFRS – EU experiences and implications

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1 IFRS came to Europe



What will IFRS bring to Europe?

“The International Accounting Standards Regulation will introduce a new era of transparency and put an end to the current Tower of Babel in financial reporting. It will help European firms to compete on equal terms when raising capital on world markets and allow investors and other stakeholders to compare companies’ performance against a common standard.”

Frits Bolkestein, EC Internal Markets Commissioner

IFRS will

- harmonise corporate reporting
- introduce comparability and consistency
- and transparency and reliability
- widen access to capital markets
- increase market efficiency...
 - ...and hence reduce the cost of capital...
 - ...and hence improve competitiveness...
 - ...and hence boost growth



2 Experience to date and key lessons learned



Experience to date

1. Amount of work to convert to IFRS depends on starting point of **local GAAP**, but also **application thereof and consistency**.....
2. Differences between local GAAP and IFRS range from simple **re-classification** to complex **measurements** to significant additional **disclosure** requirements
3. There will be **industry specific** accounting matters
4. IFRS may need to be reconciled to **standards for local regulators** such as local accounting standards board, tax authority, listing authorities, statutory law setters
5. Companies have reacted differently:
 - **Tactical** approach *versus* **strategic** approach
 - **Early** preparation for conversion *versus* **last minute** projects
 - **In house** projects *versus* extensive use of **external consultants**



IFRS Conversions - Key Success Criteria

Companies that are successful in their IFRS conversion have paid regard to:

Project Organisation Structure

- Up front top management buy-in and ownership
- Dedicated IFRS project team – project manager, project team at Head Office and also at subsidiaries
- Project governance appropriate for organisation – Steering committee, regular project meetings
- Use external consultants where required – project guidance, specialist accounting technical issues, valuations, actuaries

Project approach

- Establish Project Plan which is monitored and practical
- Project may start at Head Office but must reach out to Group companies and local ownership
- Involve auditors along the way
- Managed stakeholders - investors, lenders, internal departments etc.
- Implement internationally recognised version of IFRS - Europe
- View IFRS Conversion Project as the start the on-going IFRS reporting framework

Timing

- **Start early!**



3 Conversion concerns



Time to convert to IFRS

PwC conducted a survey of 667 companies across Europe (“IAS in Europe – the views of over 650 CFOs”) taken in 2000 and 2002 (=3 years before IFRS was required for listed companies in the EU) with updated results in 2005.

- In 2002 about 85% of companies had yet to convert to IFRS.
- Awareness was high with 95% of the CFOs aware of IFRS regulations coming into force.
- 9 out of 10 respondents, not currently using IFRS, are confident that they will be able to meet the 2005 deadline with only 3% saying they will not be able to convert in time.
- However, around 65% of these companies had not started planning yet.
- **Hence IFRS conversion took longer than expected for 43% of the companies overall (and even 64% for financial services companies).**



Time to convert to IFRS

Companies in the survey generally acknowledged the benefits of IFRS:

- 71% of those using IFRS are very positive about the benefits of IFRS transition for their company.
- 62% of the companies surveyed believe that IFRS will help to establish a pan-European debt and equity market and 78% believed this market to be very beneficial to Europe.
- 81% of CFOs even wanted the freedom to adopt IFRS before 2005.

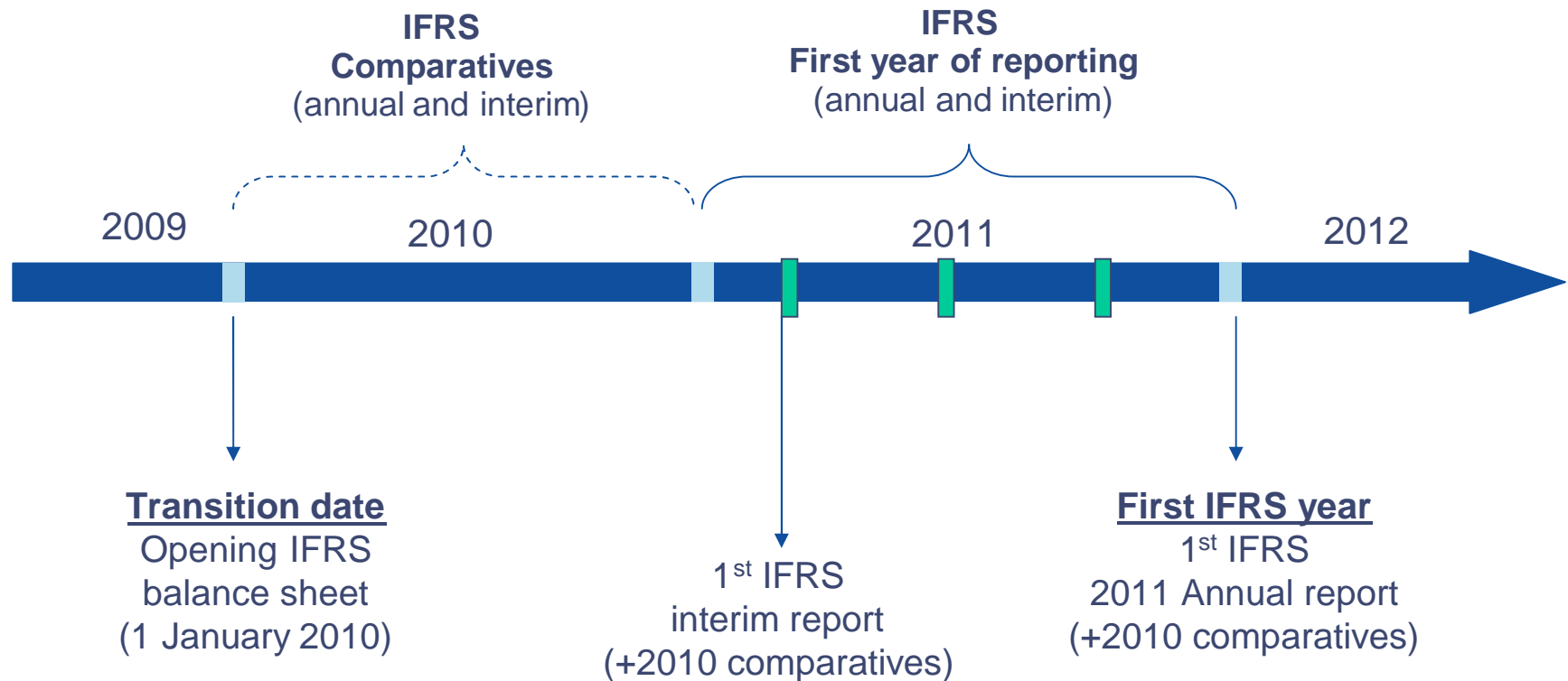
But they also mentioned:

- **“You need to make a realistic plan for conversion. It may take more than one accounting year before you get the full effect.”**
- “The IFRS project should be given top-level backing and adequate resources should be allocated to get it right first time.”
- “Build knowledge internally and do not underestimate the impact of IAS on many different aspects of the business.”
- “Conversion will require a lot of knowledge and competence at both the parent and subsidiary level.”



Timeline for IFRS conversion project – required 2011

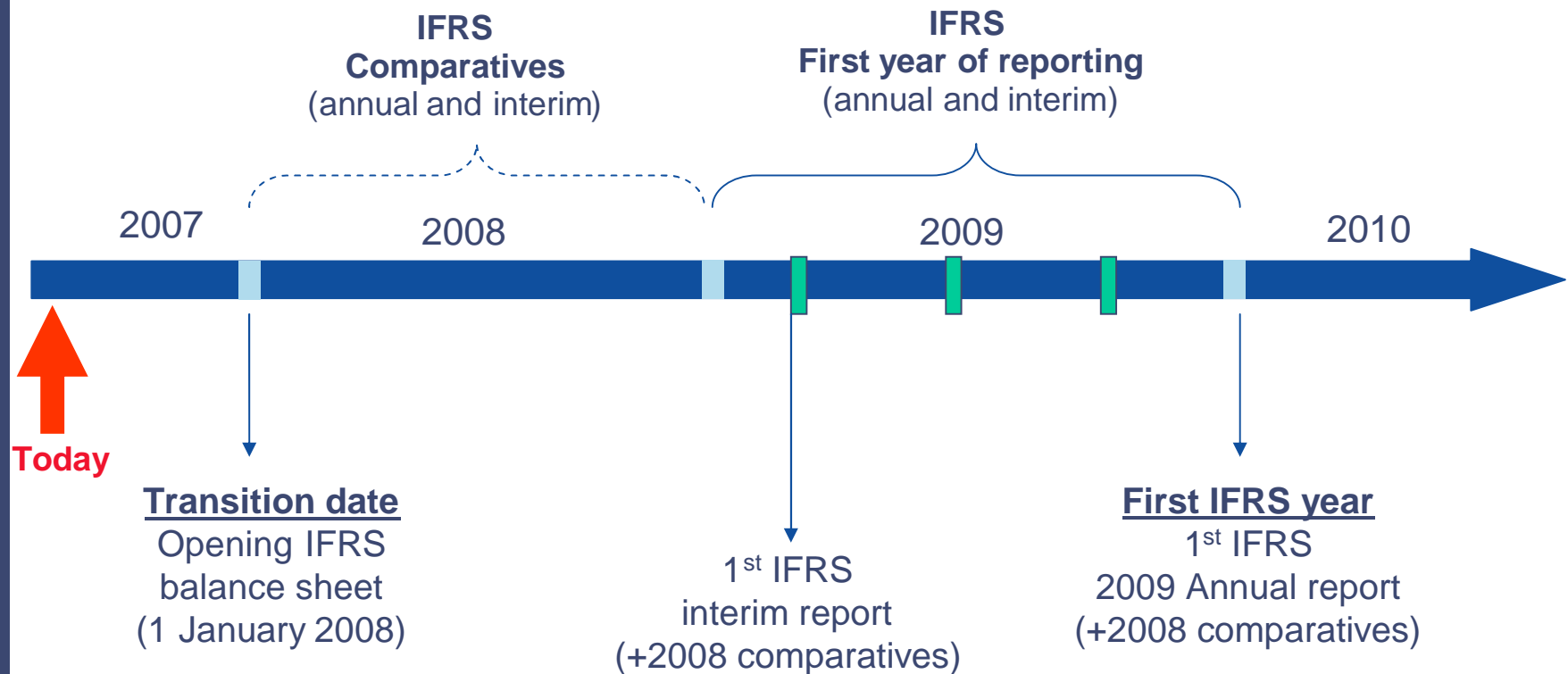
Korean companies are required to produce 2011 IFRS financial statements with 2010 as comparatives. For a 31 December year end company, the timeframe is as follows:





Timeline for IFRS conversion project – optional 2009

A company may convert voluntarily earlier and produce 2009 IFRS financial statements with 2008 comparatives. For a 31 December year end company, the timeframe is as follows:





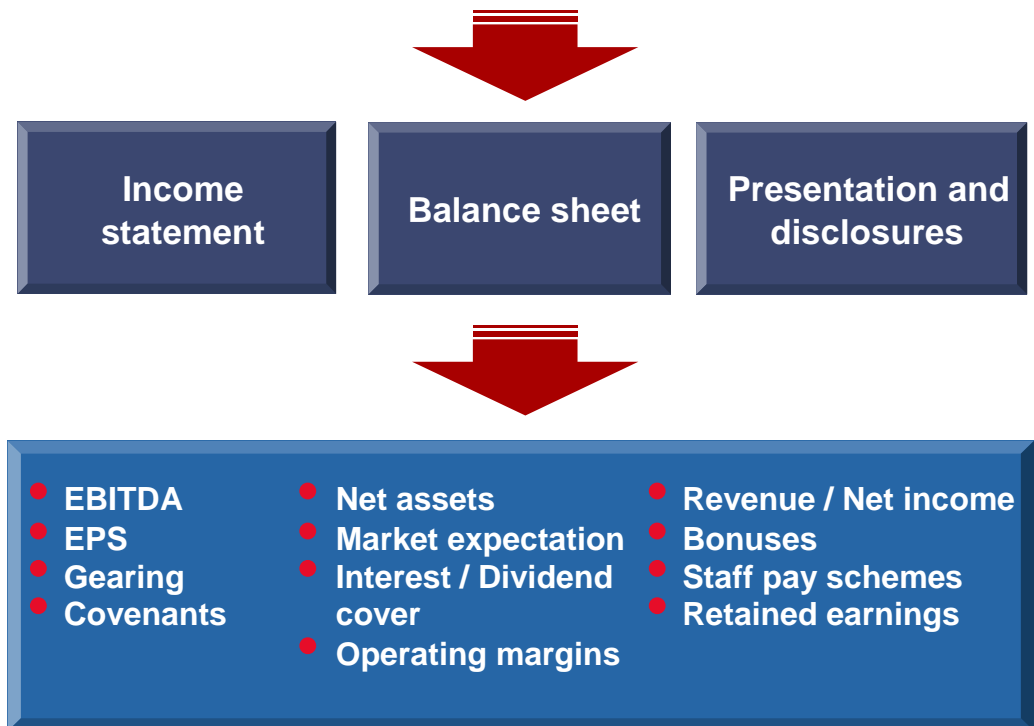
Implications of IFRS conversion – impact on Financial Statements

IFRS conversion is not just about accounting differences. The accounting differences may have a significant impact on the **Financial Statements** of a group as well as of individual entities.

Impact on Financial Statements

Some potentially major technical differences

- Revenue recognition
- Leased asset / Lease obligation
- Derivatives / Hedge accounting
- Functional currency concept
- Share based payments
- Pensions
- Deferred tax
- Intangibles





Examples of Major Impacts on Ratio's

	EBITDA/ EBIT	Net debt	Working capital
Accounting for stock options	X		(X)
Accounting for retirement liabilities (Pension)	X		
Broader notion of consolidation perimeter (notion of control)	X	X	X
Elimination of provisions of a general nature	X		
Discounting of receivables	X	X	X
Hybrid debt: split between debt and shareholders' funds		X	
Financial debt issuance costs		X	
Preferred stock		X	
Goodwill/Other intangibles	X		
Capitalization of R&D costs	X		
Capital versus operating lease classification	X	X	
Financial instruments/derivatives	X	X	
Revenue recognition	X		X



Implications of IFRS conversion - Practical

The accounting differences may also require changes to be made to reporting infrastructure of companies. Based on our experience, we have grouped such changes under the headings of **Process, Systems and People**.

Practical Implications of IFRS conversion



PROCESS

- Accounting policies & procedures
- Update & new controls
- Reporting packs
- New valuations
- Impairment modelling
- Hedging a/c requirements
- Increase data collection
- Management reporting
- Budgeting process

SYSTEMS

- Accounting and consolidation systems enhancement
- Data gaps
- New systems / modelling required – e.g.: valuation
- Update chart of accounts
- New procedures
- Training

PEOPLE

- Communication strategy
- Training strategy
- Project Management support
- Language conversions
- Resource / skills to manage the change
- Corporate governance
- Embedding knowledge – new policies and processes



4 Practical implications for companies going forward



Experiences to date

Based on our reviews of companies who have just reported IFRS for the first time:

- **Processes and controls not updated to produce numbers regularly / accurately nor to manage future transactions**
- **Implementation appears to be tactical – IFRS adjustments are made at Head Office with limited pushdown to business level**
- **Companies use spreadsheets rather than systems solutions**
- **There is time lag between producing Statutory IFRS financial results and implementing IFRS into management reporting / budgeting**
- **Sense that “we’ll make it....just”**
- **To repeat the whole process again will be painful**



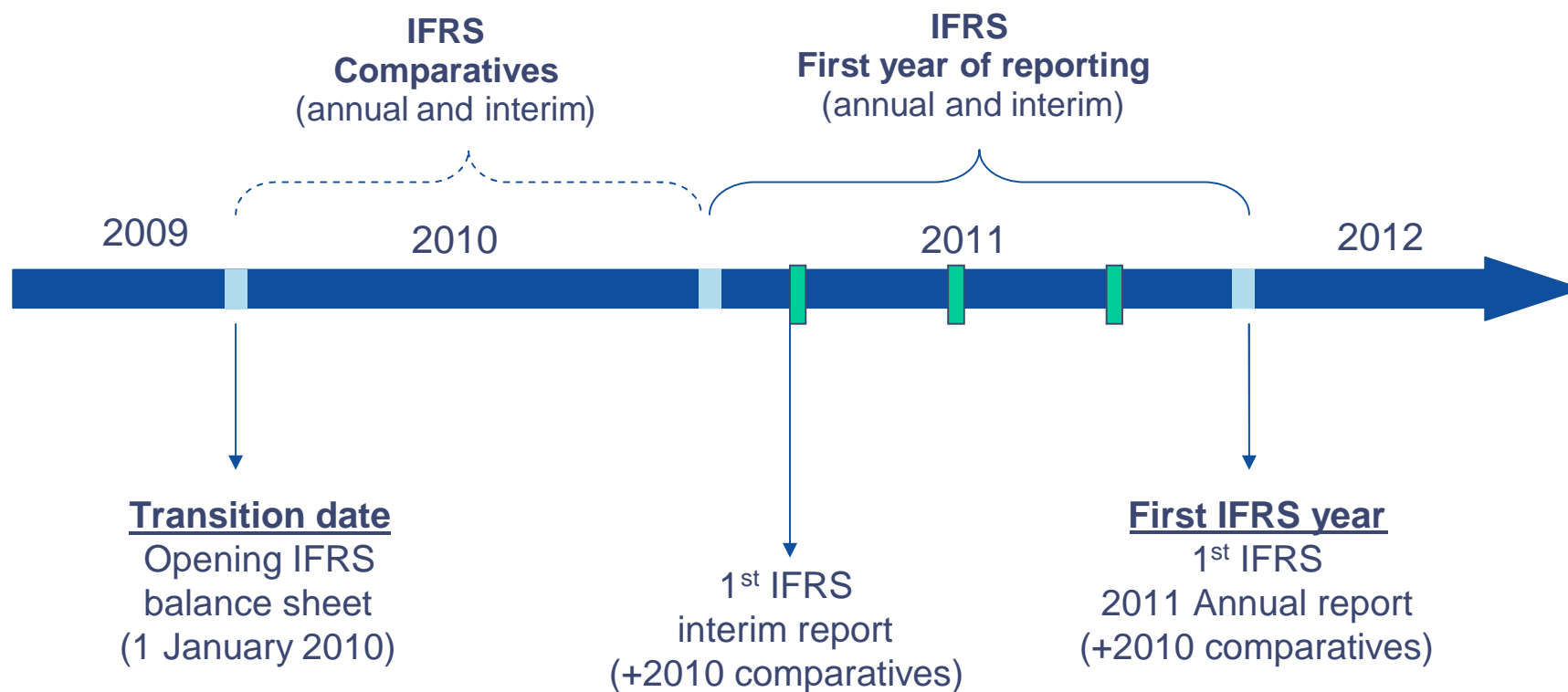
Developing a sustainable reporting model





Key Message – required conversion 2011 year end

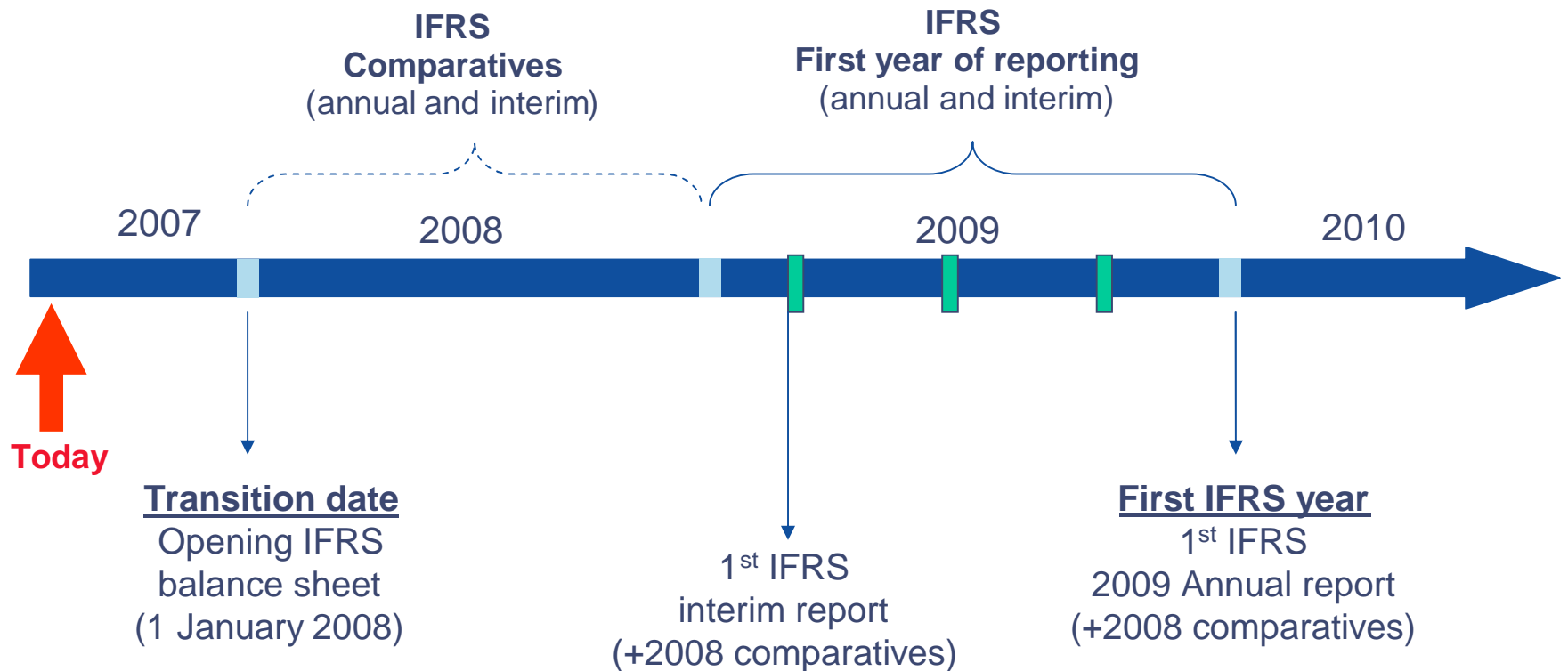
Start Early!





Key Message – optional conversion 2009 year end

Start Now!





What can go wrong?

- **Start late** - Company A (UK) – started not with the IFRS conversion until the third quarter of 2004. As a result Company A had to delay the publication of the Q1 2005 IFRS report by two months. This resulted in a 10% decrease of the share price!
- **Limited scope** - Company B (France) – started the IFRS conversion in Q4 of 2003. However Company B focused only on 5 IFRS standards and not on all the other. During the audit of the first IFRS financial statements (2005) the auditor found several other differences between local GAAP and IFRS. As a result the Q1, Q2 and Q3 reports that had been issued earlier had to be restated.

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