IFRS: An Introduction (2nd ed.)

By Needles & Powers

Solutions to Assignments

(The authors appreciate receiving suggestions for improvements in these solutions)

CHAPTER 1

1. **What international organization began the movement toward international** accounting standards and when and how did the United States become involved?

The establishment of the International Accounting Standards Committee (IASC) in 1973 began the movement toward international accounting standards.

The FASB in the United States first formally expressed interest in international standards when it issued a plan for a global focus on standard setting in 1991. The FASB began to collaborate with the IASC and became a founding member of the G4 + 1. The G4 + 1 was a working group consisting of standard setters in the United Kingdom, Canada, the United States, and Australia, plus the IASC.

2. **What is the IASB; when was the IASB formed; and why is its structure important?**

The initiative of the G4 + 1 led eventually to formation of the IASB in 2001.

". . . the SEC and the FASB were deeply involved in the establishment of the restructured IASB, and the structure, governance, and independence of the IASB are largely modeled on the FASB's." said by IASB chair. Because IASB doesn't represent any particular country or interest of entities, the goal of IASB is to offer standards of financial reporting accepted by worldwide.

3. **Briefly, what is the process followed by the IASB for issuing an IFRS?**

IASB and staff will set an agenda of possible issues and study the worthiness of discussions. After the research, the issue will be brought for public discussion. After considering all comments from its discussion paper, exposure draft is issued to receive more comments. After all, IASB will publish a final IFRS; but IASB still continue to receive further suggestions.

4. **Why is each of the following important and how does each relate to the concepts of convergence and adoption?**

   a. Memorandum of Understanding (MOU) between the FASB and the IASB

b. The SEC Roadmap

a. MOU in 2002 laid out the joint commitment of cooperation between FASB and the IASB working toward convergence. Through it, two parties can build up and maintain the compatibility of IFRS and GAAP.

b. The SEC Roadmap is set up for the adoption of IFRS. The Roadmap is published for public comment, leading to the adoption of IFRS by U.S. issuers. The SEC can follow the roadmap and decide whether to mandate IFRS for U.S. public companies.

5. What conditions must the IASB meet in order for adoption of IFRS by the United States in 2011? List one or two conditions that will be the most difficult to accomplish.

Potential implementation of the mandatory use of IFRS

6. In your opinion, what are the two most important arguments in favor of allowing IFRS for U.S. public companies?

(1) IFRS would enhance transparency and comparability among companies globally, thus, enabling investors and other users to more readily assess performance and to make comparisons among companies

(2) IFRS presents opportunities for global U.S. companies to lower costs through standardization of financial reporting, centralization of processes, improved controls, and better cash management

(3) U.S. companies would benefit financially from adoption of IFRS, resulting in improvements in liquidity, valuation and cost of capital

(4) The adoption of IFRS increases U.S. companies competitiveness in global capital markets and lower their cost of capital

(5) Public companies, private, non-public companies receives same option on adopting IFRS

7. In your opinion, what are the two most important arguments against allowing IFRS for public U.S. companies?

(1) U.S. GAAP have a longer history and is more comprehensive than IFRS. Differences between IFRS and U.S. GAAP are significant

(2) Some U.S. standards that differ from IFRS may be difficult to change

(3) IASB needs strengthening as an independent, global standard setter

(4) Continued existence of European IFRS undermines global comparability

(5) Significant changes to the U.S. reporting infrastructure are needed

(6) U.S. accountants and educators need to be trained in order to adapt to IFRS

(7) Elimination of U.S. GAAP for U.S. companies contradicts the general sentiment in the United States that by maintaining control of setting accounting standards, the influence of the FASB, SEC and other U.S. organizations would be limited or nonexistent.

8. *Class or group discussion*: Should the SEC require U.S. public companies to use IFRS?

Yes. IFRS would enhance transparency and comparability among companies globally, thus, enabling investors and other users to more readily assess performance and to make comparisons among companies. U.S. companies would benefit financially from adoption of IFRS, resulting in improvements in liquidity, valuation and cost of capital. In order to be global leader, U.S need to get more involved into the trend of international accounting standards. Even though the adoption or convergence.

9. *Exercise*: State the name of each of the organizations represented by the acronyms listed below and give a brief statement to the organization's importance to IFRS:

a. IASC: International Accounting Standard Committee, IASC work with FASB to found G4+1, which is the initial formation of IASB.

b. IAS: International Accounting Standards, IAS was issued by IASC. Due to receiving many criticisms, IASC work on revise IAS in order to come out a set of core standards, which are IFRS.

c. IASC: ??? same as a. u mean IFAC?

d. IASCF: IASC Foundation, appointing and overseeing the IASB. It's a not-for-profit, private sector body consisting of a geographically and professionally diverse group twenty-two trustees.

e. IFRIC: International Financial Reporting Interpretation Committee, issuing interpretations of IFRS when there is doubt about the appropriate accounting treatment.

f. SAC: Standards Advisory Council, which consists of a wide-range of representative from user groups, financial analysts, auditors, regulators, advises the IFRS on a broad range of issues.

10. Case:

Yes, because adoption of IFRS allows the company investors easily compare the companies with others, lower costs through standardization of financial reporting, results in improvements in liquidity, valuation and cost of capital. As a CFO, I definitely should let the company adopt the IFRS; then Off-Shore Jewelry Inc is able to expand the services in Europe.

No, because Off-Shore Jewelry Inc. is based in U.S. The company is still a private company, which doesn't need to offer the comparability and transparency for the global investors. Moreover, the company also needs to report to U.S government, instead of Europe. The adoption of IFRS will bring more cost to the company. Therefore, the adoption is not recommended.

CHAPTER 2

1. **What are IFRS and how do they relate to IAS?**
   IASB achieves its objectives primarily by developing and publishing IFRS and promoting the use of those standards in general purpose financial statements and other financial reporting. To aid in the development of future IAS and in the review of existing IAS, the IASC issued the *Framework for the Preparation and Presentation of Financial Statements* for external users. The IASB continues to rely on the framework in setting IFRS.
2. **What is the objective of financial statements and what two assumptions underlie them?**
   The objective of financial statements is to provide information about the financial position, performance, and changes in financial position of an entity that is useful to a wide range of users in making economic decisions.
   Two assumptions underlying financial statements are accrual accounting and going concern.
3. **Why are qualitative characteristics important?**
   Qualitative characteristics are the attributes that make the information provided in financial statements useful to users. Therefore, the four principal qualitative characteristics, understandability, relevance, reliability, comparability enhance the usefulness of financial statements.
4. **What is the difference between understandability and relevance?**
   Information has the quality of understandability if users readily understand it. Users are assumed to have a reasonable knowledge of business, economic activities, and accounting as well as a willingness to study the information with reasonable diligence. Information has the

quality of relevance when it influences users' economic decisions. However, relevant information about complex matters should not be excluded merely on the grounds that it may be too difficult for certain users to understand.

5. **Is reliability the same as accuracy?**

   Information has the quality of reliability when it is free from material error and bias and can be depended upon by users to represent faithfully that which it either purports to represent or could reasonably be expected to represent. Reliability does not imply precise measurements of the elements of financial statements. Accuracy means the financial statements are totally free from errors. Reliability could not guarantee the accuracy, but definitely could provide the readers the confidence of dependability.

6. **What are the characteristics of reliability?**

   The characteristics of reliability are: faithful representation, substance over form, neutrality, prudence.

7. **What is comparability and to what does it apply?**

   The quality of comparability means users may compare the financial statements of an entity through time in order to identify trends and also compare the financial statements of different entities in order to evaluate their relative financial position, performance, and changes in financial position.

8. **What are assets, liabilities, and equity? Define each.**

   Asset: A resource controlled by the entity as a result of past events and from which future economic benefits

   Liability: A present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.

   Equity: The residual interest in the assets of the entity after deducting all its liabilities.

9. **What are venues and expenses? Define each.**

   Income: The increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants.

Expenses: Decreases in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrence of liabilities that result in decreases in equity, other than those relating to distributions to equity participants.

10. **What are measurement, recognition, and derecognition? Define each and tell how they relate to each other?**

Recognition is the process of incorporating in the balance sheet or income statement an item that meets the definition of an element and satisfies the following criteria: It is probable that any future economic benefit associated with the item will flow to or from the entity; and the item has a cost or value that can be measured with reliability.

Derecognition is the removal of a previously recognized asset or liability from an entity's statement of financial position.

Measurement is the process of determining the monetary amounts at which the elements of the financial statements are to be recognized and carried in the balance sheet and income statement.

So accountants have to measure value of items, and the recognize them the financial statements. If there are no more future economic benefits made by this item, accountants need to derecognize it from the financial statements.

11. **List the five sections that all proposed financial statements should contain.**

All statements will be divided into five categories as follows:

Business: Includes line items related to operating and investing activities.

Financing: Includes line items related to financing activities.

Income taxes

Discontinued operations

Equity

12. **How does the balance sheet under proposed IFRS differ from U.S. GAAP?**

GAAP and IFRS have pretty similar format in balance, which IFRS named as statement of financial position. IFRS do not prescribe a format for the statement of financial position. IFRS require the separation of current and non-current assets, and current and non-current liabilities and that they be listed in order of liquidity. In contrast to U.S. practice, IFRS specifically prohibit "deferred tax assets/liabilities".

13. **What is the proposed new name for the income statement and why does it have this name?**

    The new name is Statement of Comprehensive Income. The title includes the words comprehensive income, indicating it will include items that previously were disclosed separately as other comprehensive income.

14. **How does the proposed IFRS statement of cash flows differ from the way most of these statements are prepared in the United States?**

    In a significant difference from U.S. GAAP, IFRS exclude non-cash investing and financing activities from the statement of cash flows. Entities disclose the relevant information related to these transactions in the notes to financial statements.

15. **What does the proposed schedule in Exhibit 5 reconcile and why is it useful?**

    The reconciliation can clearly show the five sections in all of financial statements, Business, financing, Income Tax, Discontinued operations, Equity. Then accountants can easily see what goes into each category and explains its choices in the accounting policy note to the financial statements.

16. **Class or group discussion: Is historical cost or fair value more in line with the qualitative characteristics of the conceptual framework and why?**

    Fair value underlies the measurement of all items under IFRS. Fair value underlies the measurement of all items under IFRS. Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable parties in an arm's length transaction. A measure of value used in accounting in which the price of an asset on the balance sheet is based on its nominal or original cost when acquired by the company. Based on the historical-cost principle, under U.S. GAAP, most assets held on the balance sheet are to be recorded at the historical cost even if they have significantly changed in value over time. Therefore, in order to fitting into the neutrality, comparability characteristics in IFRS, Fair value is more appropriate.

17. ***Class or group discussion*: Define the concepts of *conservatism* under U.S. GAAP and *prudence* under IFRS. How are they similar and how are they different? Do they represent a significant difference between U.S. GAAP and IFRS? Give an example of how they might differ in their application.**

The principle of conservatism in GAAP provides that accounting for a business should be fair and reasonable. Accountants are required in their work to make evaluations and estimates, to deliver opinions, and to select procedures. They should do so in a way that neither overstates nor understates the affairs of the business or the results of operation. In IFRS, to be prudent, a degree of caution in the exercise of the judgments is needed in making the estimates required under conditions of uncertainty, such that assets or income are not overstated and liabilities or expenses are not understated. They do not represent a significant difference between GAAP and IFRS. They both mean the cautious side in accounting area. I didn't quite see the difference.

18. ***Exercise*****: Match the selected sections of IASB-proposed financial statements (letters) with their respective components (numbers):**

1) E 2) D 3) G 4) B 5) A

6) E 7) F 8) C 9) D 10) A

11) F 12) C 13) G 14) A

19. ***Exercise:*** **Match the selected sections of IASB-proposed statement of comprehensive income statement (letters) with their respective components (numbers).**

1) B 2) F 3) I 4) B 5) E

6) C 7) D 8) F 9) D 10) G

11) D 12) I 13) H 14) D 15) B

16) I 17) A

20. ***Exercise:*** **Match the selected sections of IASB-proposed statement of financial position (letters) with their respective components (numbers).**

1) D 2) F 3) A 4) C 5) E

6) A 7) C 8) A 9) G 10) H

11) A 12) B 13) G 14) C 15) B

16) G 17) C

21. ***Case:*** **Assume you work for a company that has used the U.S. GAAP practice of valuing Buildings at historical cost less accumulated depreciation. Your company is considering revaluing the building annually based on fair value. Based on the concepts underlying the IFRS framework, how does fair value differ from historical cost. (Use the example of fair value presented in the text as a starting point.)**

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable parties in an arm's length transaction. According to one former member of the IASB, fair values

- Are *relevant*
- Have *predictive value*
- Can be *faithful representations* of assets and liabilities
- Are *neutral*
- Are *timely*