EMBEDDING INTERNATIONAL FINANCIAL REPORTING STANDARDS IN ORGANISATIONS

A Paper Presented by:

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Highlight of the presentation

- Overview of IFRS/Financial Reporting Framework
- Overview of stages in IFRS conversion
- Rules and Principles relating to first time adoptions
- Practical considerations for the adoption of IFRS

What are IFRSs

IFRSs are Standards and Interpretations issued by the International Accounting Standards Board (IASB).

They comprise:

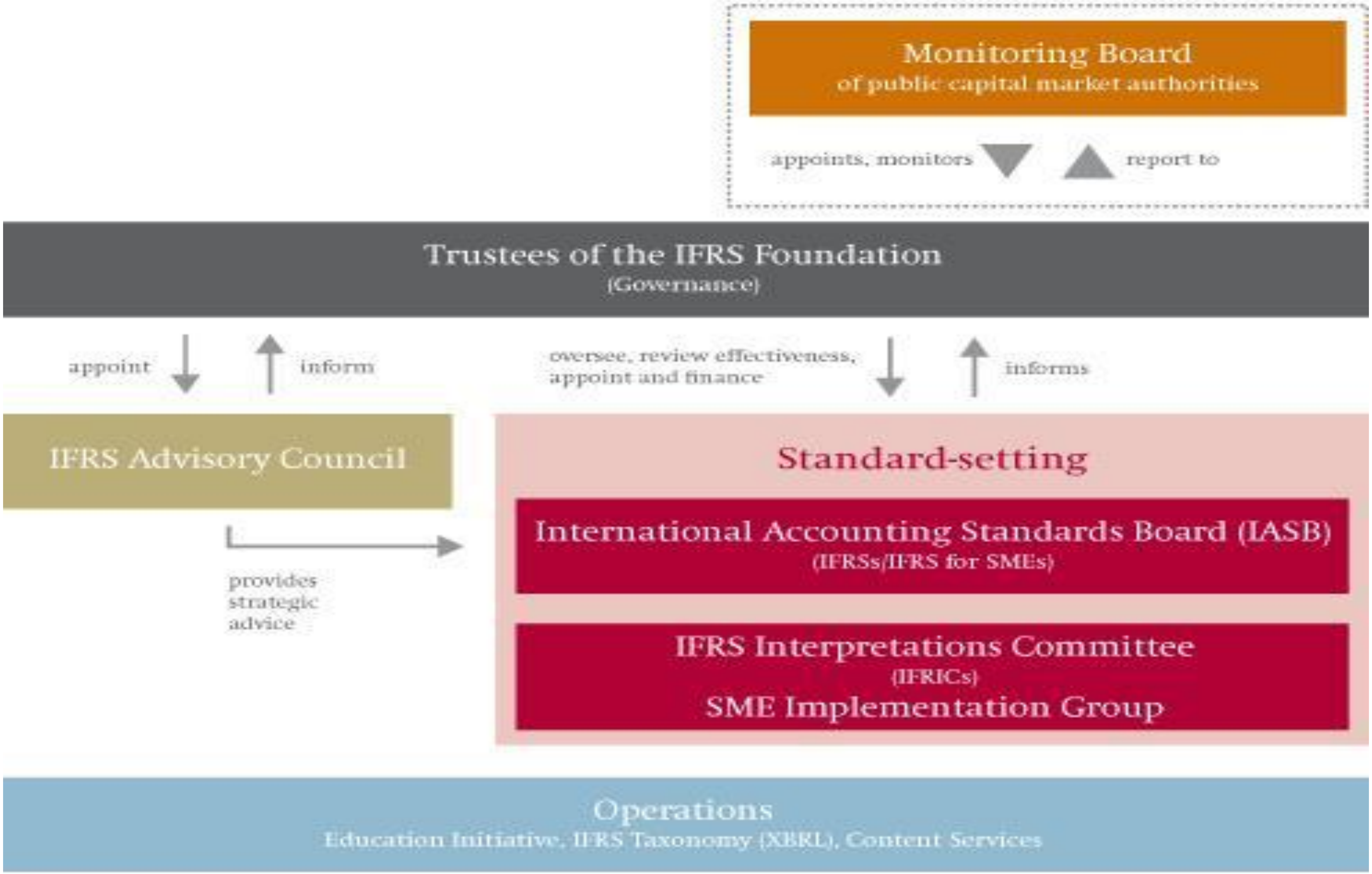
- International Financial Reporting Standards (IFRS);
- International Accounting Standards (IAS); and
- Interpretations originated by the International Financial Reporting Standards Interpretations Committee (IFRSIC) or the former Standing Interpretations Committee (SIC).

IFRS are "principles based" set of standards that establish broad rules as well as dictate specific treatments. There is an increasing acceptance and use of IFRS in major capital markets all over the world.

Since 2001, almost 130 countries have required or permitted IFRSs.

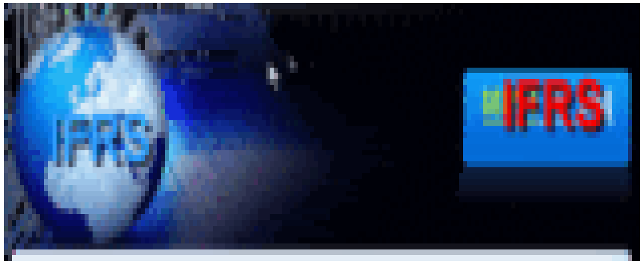
All major economies have established time lines to converge with or adopt IFRSs in the near future.

The IFRS Foundation



Source: www.ifrs.org

8,000 listed companies in 25 countries since 2005



- The World is going IFRS

Benefit of Implementing IFRS

Fundamental to getting to a high quality global reporting system

Attracting investment through transparency

Reducing the cost of capital

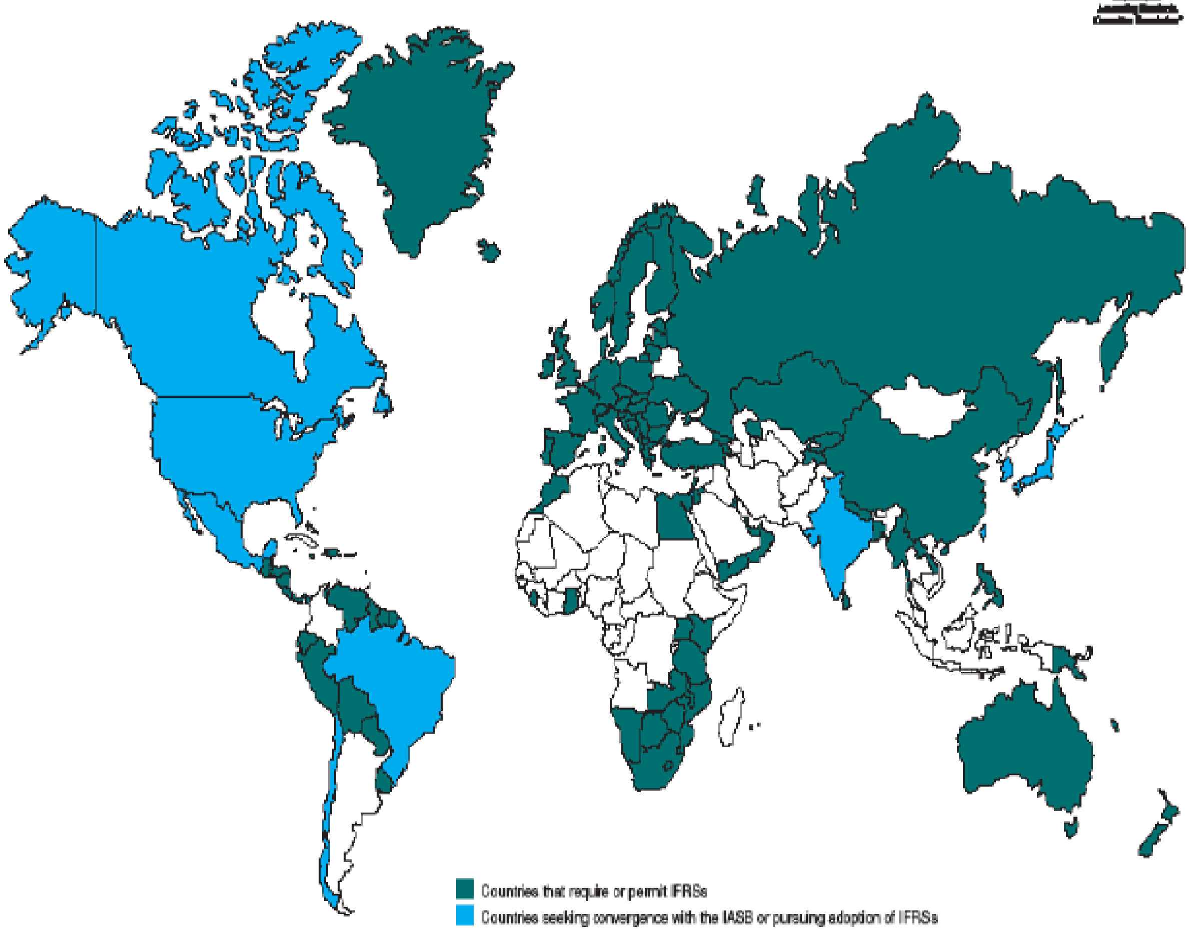
Increased comparability

Elimination of Multi GAAP reporting

Enhanced knowledge of global financial reporting standards by the Nigerian Accountant

THE MOMENTUM TOWARDS GLOBAL IFRS ADOPTION

More than 100 countries require or permit the use of International Financial Reporting Standards (IFRSs), or are converging with the IASB's standards.

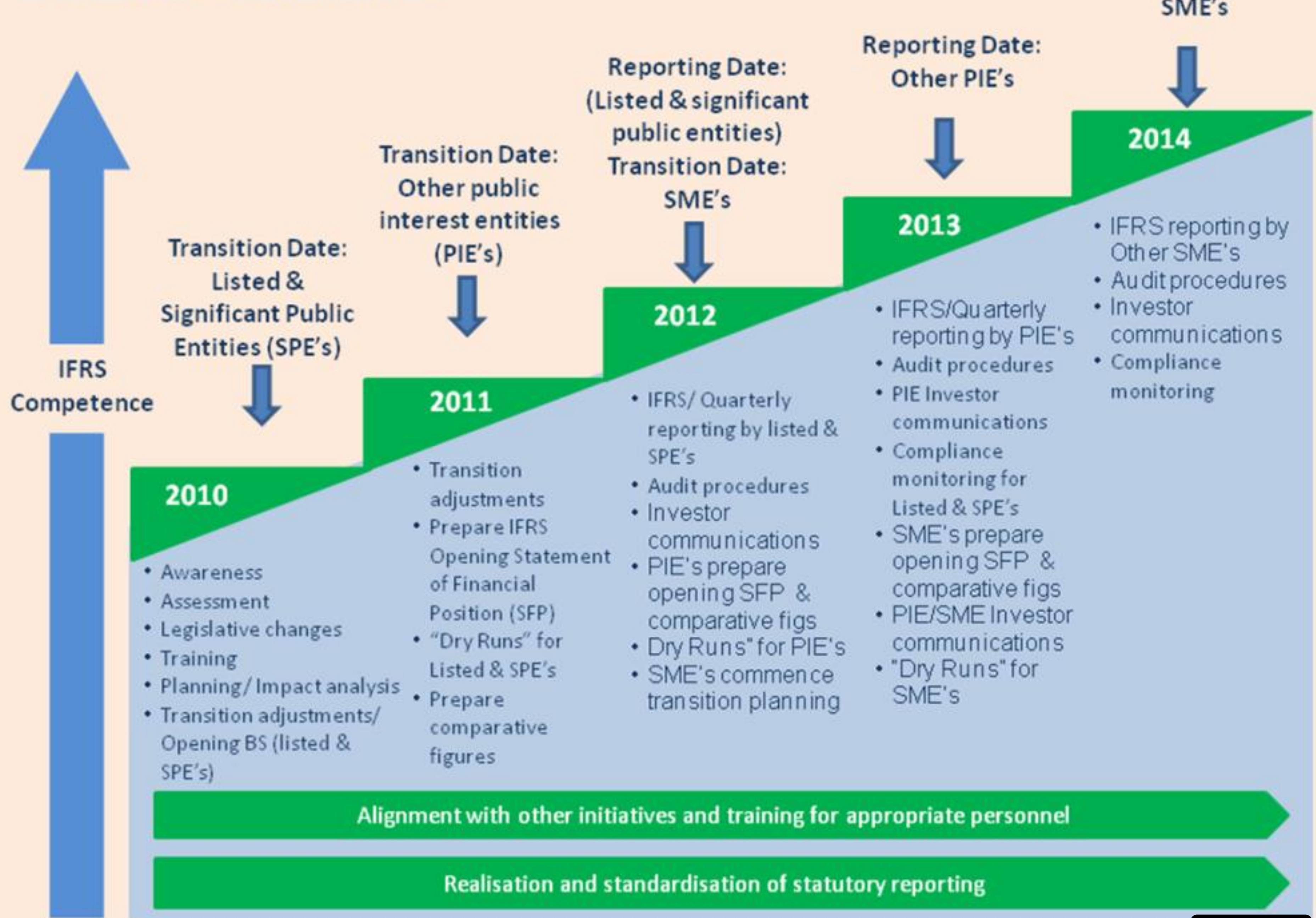


Source: www.ifrs.org

IFRS – Which Way Nigeria ?

- Cross-border listings in some Nigerian PLCs
- Bankers' Committee – an initial agreement
- CBN attempted to enforce Bankers Committee's agreement that all Banks should adopt IFRS by December, 2010.
- A Road map committee was inaugurated on October 22, 2009.
- The Road Map committee's report was submitted January 26, 2010.
- *Government took a decision on July 28, 2010 to adopt IFRS effective January 1, 2012 .*

Roadmap to IFRS conversion



Significant public interest entities

“means government business entities, all entities that have their equities or debt instruments listed and traded in a public market (a domestic or foreign Stock Exchange or an Over the Counter market, including local and regional market), and such other organisations, though unquoted, required by law to file returns with regulatory authorities and this excludes private companies that routinely file returns only with Corporate Affairs Commission and the Federal Inland Revenue Service. Examples of entities meeting these criteria include financial and other credit institutions and insurance companies.” - *FRC Road-Map Guideline*

Other public interest entities

“refers to those entities, other than listed entities (unquoted, private

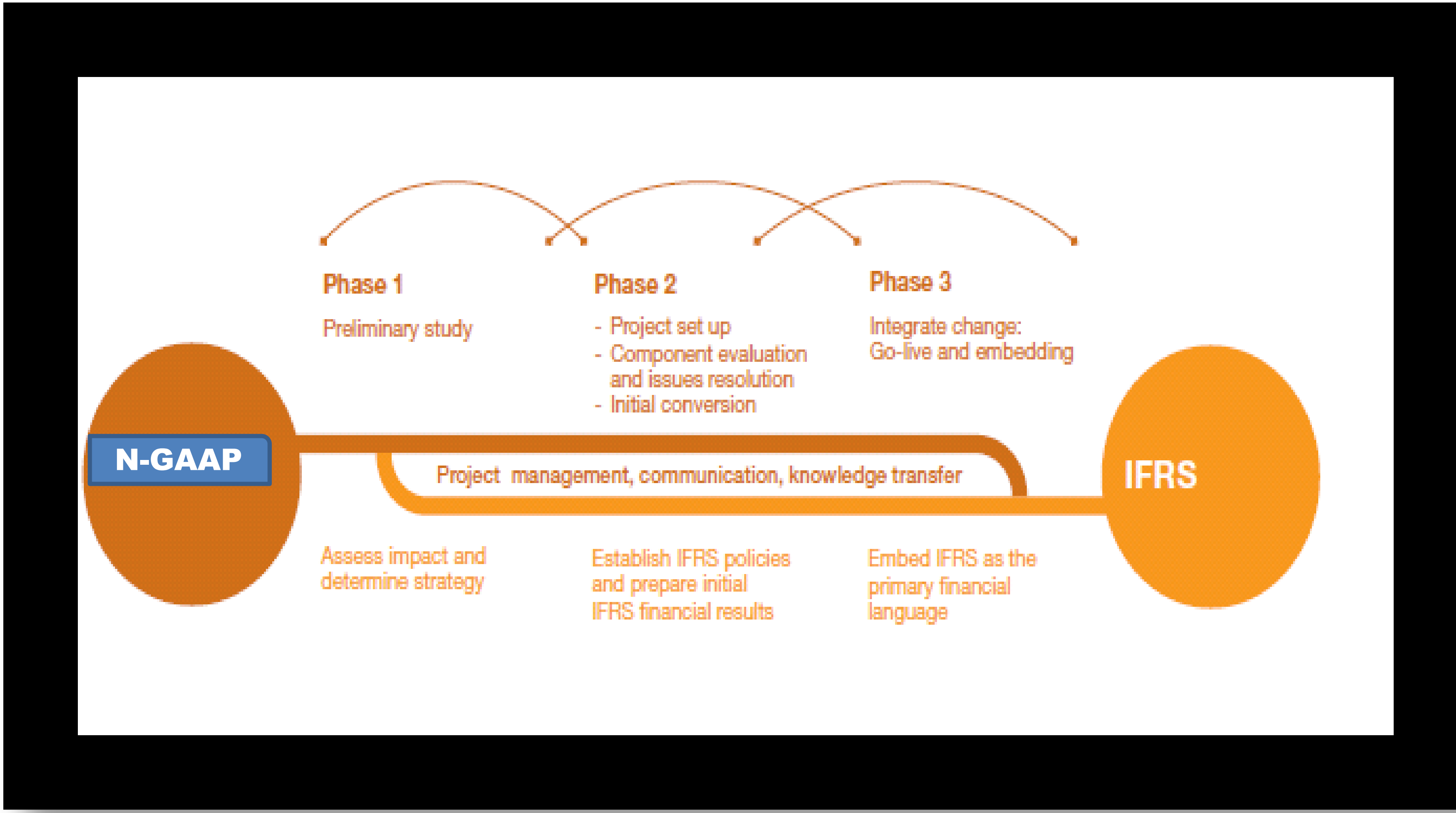
- companies), which are of significant public interest because of their nature of business, size, or number of employees or their corporate status which require wide range of stakeholders. Examples of entities meeting these criteria are large not for profit entities such as charities and pension funds and may include publicly owned entities and other entities where there is a potentially significant effect on financial stability” - *FRC Road-Map Guideline*

Small and Medium-sized Entities (SMEs)

"entities that may not have public accountability and:

- their debt or equity instruments are not traded in a public market;
- they are not in the process of issuing such instruments for trading in a public market;
- they do not hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses
- the amount of its annual turnover is not more than N500 million or such amount as may be fixed by the Corporate Affairs Commission
- its total asset value is not more than N200 million or such amount as may be fixed by the Corporate Affairs Commission
- no Board members are an alien,
- no members are a government or a government corporation or agency or its nominee, and
- the directors among them hold not less than 51 percent of its equity share capital." - *FRC Road-Map Guideline*

Transition to IFRS Methodology



Source: www.pwc.com

IFRS conversion impacts your entire business

Which are the essential differences in accounting and disclosures between IFRS and Local GAAP?

What is the impact on systems and processes – quick fix or major overhaul?

What are the effects on
- **company results and equity,**
- **contracts,**
- **capital investments,**
- **management reporting,**
- **external communication?**

Who is affected by the IFRS conversion and what are their training needs?

What would a high level conversion plan look like, which resources are needed, how can subprojects be coordinated?

Source: www.kpmg.com

Implementing IFRS is not just an accounting exercise

IFRS will change how your business is managed ✓

IFRS will change how you communicate with the marketplace ✓

IFRS will provide greater transparency with your peer group ✓

- **Senior sponsorship is required as IFRS will impact constituencies beyond the finance function**

General Principles of IFRS 1

- Objectives and Scope
  - Transparency for users and comparability over all periods presented;
  - Provides a suitable starting point for accounting under IFRS; and
  - Can be generated at a cost that does not exceed the benefits to users.
- Entities are required to apply IFRS 1 in their first IFRS financial statements and in each interim financial report, if any, prepared in accordance with IAS 34 Interim Financial Reporting for part of the period covered by those first IFRS financial statements.
- An entity’s first IFRS financial statements are the first annual financial statements in which it adopts IFRSs by including an explicit and unreserved statement of compliance with IFRSs.

Content of First IFRS Financials

- An entity's first IFRS financial statements include at the least:
  - Three statement of financial position including one at the date of the transition
  - two statements of comprehensive income,
  - two income statements (if presented),
  - two statements of cash flows, and
  - two statements of changes in equity.
  - Four mandatory exception and 19 optional exemption
  - Explanation of the transition to IFRS by providing reconciliations as at the date of transition and for the periods covered by the financial statements
  - equity reconciliations and comprehensive income (Profit) reconciliations.

Implementation of IFRS 1

- Opening IFRS balance sheet at the **date of transition.**
- **Opening balance sheet prepared in accordance with IFRSs effective at the end of reporting period.**
- The entity recognizes all assets and liabilities in accordance with the requirements of the IFRSs and derecognizes assets and liabilities that do not qualify for recognition under IFRS.
- All adjustments above are adjusted to opening retained earning (date of transition).
- Estimates on the date of transition under IFRS should be consistent with estimates made for the same date under previous GAAP.
- Comparative financial statements

Implications of IFRS Conversion

- Complete compliance with IAS 1 *Presentation of Financial Statements requirements*
- Explanation of the transition to IFRS by providing reconciliations as at the date of transition and for the periods covered by the financial statements-equity reconciliations and comprehensive income (Profit) reconciliations.
- Significant GAAP Differences
- Software reassessment is required
  - May either need replacement or Upgrading
- Top level management buy-in
  - A project team may have to be dedicated to the conversion
  - IFRS awareness at the board level
- Knowledge gap – Training required
- Conversion cost - e.g. A consultant may be needed
- Regulatory Framework must be up to date.

Implications of Adoption – Cont'd

- Revenue recognition
  - (No local standard dedicated to revenue recognition)
- Fair value measurement (heavily used in IFRS)
  - Hierarchy of Fair values
  - Need for management judgement and estimate is increased
- Business combinations
  - Full Goodwill approach may be used
  - Impairment of CGUs with allocated goodwill
- Share based compensation
  - (No Local Standard)
- Depreciation
  - (Available for Use vs. Put into use)
- Property, plant and equipment
  - Componentisation approach is required
  - Annual review of useful life and residual values of PPE.
  - Identifying impairment indicators and testing for impairment.

Implications of Adoption – Cont’d

- Financial instruments
  - Impairment testing methodology will change
  - Embedded derivatives may now have to be identified
  - Use of Effective interest method for revenue recognition
  - Increased volatility of earnings is likely to be witnessed
  - Hedge accounting
  - Individual and Collective assessment for receivables impairment testing rather than mere age analysis of debts
  - “Higher of IAS 39 and Revised Prudential Guidelines” for Banks
  - Extensive disclosures of IFRS 7
  - Treatment of Convertible debts in accordance with IAS 32.

Implications of Adoption – Cont'd

- Employee Benefits
  - Corridor approach
  - Asset Ceiling
- Presentation of Financial Statements
  - New statements will have to be prepared e.g. Statement of Changes in Equity
- Deferred Taxes
  - Timing difference approach vs. Temporary difference approach
- Statement of Cash Flows
  - More flexibility for classification of Interest income and Interest expense.
- Provision and Contingences
  - The requirement that there must be a present obligation as a result of past events must now be applied strictly

Practical Considerations for the Nigerian Insurance Companies

In general, transition from N-GAAP to IFRS is more than just an accounting exercise. It will have an effect outside the finance function in areas such as:

- information technology;
- human resources; and
- investor relations.

It involves modification or outright replacement of:

- systems and data
- financial reporting processes and outputs
- financial compliance controls and certification activities,
- business metrics and performance management systems,
- extent and depth of financial disclosures.

PRACTICAL IMPLICATIONS – OPERATIONAL

Systems impact	Forecasting future cash flows based on probability-weighted scenarios will require significant upgrade of modeling capabilities
Organisational impact	Use of risk margins and cash flow analyses in accounting will require closer integration among finance, regulatory, actuarial and risk management functions.
Resource impact	Need for more qualified actuarial as well as finance and IT personnel

PRACTICAL IMPLICATIONS – FINANCIAL REPORTING

Earnings volatility	Revaluing insurance liabilities will create potential earnings volatility
Potential day one profit or loss	Using current exit values could lead to reported profit or loss at contract inception
Impact on revenue	The question of whether certain premiums should be treated as income or deposits is left open and could affect “top line” revenue
Impact on equity	Discretionary policy dividends qualify as liabilities only if there is a ‘constructive obligation’ to pay them

The Case Study

Thank you for your attention !