New accounting rules

Some 12 months after the Financial Reporting Council committed Australia to adopting international accounting standards by January 2005, the Institute discusses the major changes to financial reporting and analyses the numerous implications for Australian companies and for the preparers and users of financial statements.

Over the next year, Australian companies will be called upon to make significant changes to how they report their financial performance by January 1, 2005. While the Institute endorses the new accounting regime as a move in the right direction, we are concerned about key implementation issues, in particular the short preparation lead period and how the adoption process will be managed at the statutory level.

Influence the outcome—members' feedback welcome

The Institute strongly encourages members to consider the IASB-issued Exposure Draft proposals and contribute comments on their practical applicability to the Australian market.

Under the AASB's implementation approach, the content and wording of the IASB-issued standards will be adopted, with changes permitted only "where there is a need to accommodate the Australian legislative environment" (such as including an Australian-specific application referring to the Corporations Act 2001) and provided that the proposed amendment does not affect the core substance of the IFRS requirements.

There is still time to influence the final outcome and ensure that financial statements produced under IFRS are reliable, relevant, transparent, consistent and comparable.

From an industry perspective, the most constructive thing the Institute can do now is to encourage the maximum amount of participation by Australian professionals and technical experts in the process of formulating and vetting the proposed international standards.

Impact and implications

While the conversion to IFRS relates primarily to technical changes, the impact will extend beyond the financial reporting exercise.

For reporting entities, there will be major flow-on implications for business strategy, operational systems, internal control systems, investor relations—perhaps even a change of mindset on some conceptual aspects of compliance, governance, transparency and disclosure. (See articles pages 6–12 and 37–40.)

Preparation for change is the key

The Institute is concerned that many Australian companies and market participants may not fully comprehend or may underestimate what is involved in moving to IFRS in practice.

However, the ramifications of the IFRS adoption exercise are likely to really sink in by 31 March 2004, when the IASB plans to have finalised and issued the whole package of new and revised IFRS standards applicable to accounts for the financial year beginning on or after 1 January 2005.

For their first reporting period beginning after the January 2005 adoption date, Australian reporting entities will have to apply the Australian equivalent of the IFRS standards and provide comparative figures for their previous financial year.

Therefore, compliance plans and internal reporting, resourcing and information management processes must be tested and operational prior to that operative date.

There will be a pressing need to familiarise, train and educate those involved in preparing financial reports and those involved in interpreting, evaluating or reporting on the accounts (such as company directors, CEOs, CFOs, company secretaries, auditors, research analysts, financial journalists, regulators, valuers, insurers and the investment community) about the change of mindset and application methods employed under the IFRS system.

Companies must prepare themselves and the market for some marked volatility in reported earnings that will likely occur on converting to IFRS accounts.

Reporting entities should make preparations to brief their board members, audit committees, senior management, investment bankers, equities analysts and institutional and retail shareholders on the likely significant or different impacts on business operations, key analytical ratios and investment potential.

Consideration will have to given as to how best to present and explain the nature and extent of critical changes expected to appear in the financial statements.

Outstanding issues

A potential complicating factor in Australia aligning itself to the IFRS regime involves the shifting stance and status of convergence between the US Financial Accounting Standards Board (FASB) and the IASB. Although the two accounting standard setters have a memorandum of agreement that sets out a strategy to reduce or eliminate the differences between US and international accounting pronouncements and bring the US capital markets into line with the standards of the IFRS system, progress on full convergence seems to have stalled. J