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### **The SEC Proposes Roadmap for the Potential Use of Financial Statements Prepared in Accordance with IFRS by U.S. Issuers**

Yesterday the Securities and Exchange Commission (SEC) unanimously voted to publish for public comment a Roadmap that could potentially phase out the application of United States Generally Accepted Accounting Principles (GAAP) by U.S. issuers, beginning in the year 2014, and instead mandate the application of International Financial Reporting Standards (IFRS) for financial reporting. The text of the release proposing the Roadmap is not yet available, so the descriptions provided in this special alert are based on statements made by the SEC Commissioners and Staff at the Open Meeting, and in the SEC's press release.<sup>1</sup>

The Roadmap sets out certain key milestones that, if met, would lead to a determination by the SEC in 2011 as to whether to adopt the mandatory use of IFRS by U.S. issuers, beginning in the year 2014. Some of the proposed milestones relate to improvements in accounting standards, improvements in the ability to use interactive data in connection with IFRS reporting, educational training related to the use of IFRS in the United States, the limited early use of IFRS by a small class of eligible U.S. issuers and greater accountability by the International Accounting Standards Board, which created and will have ultimate authority with respect to IFRS. With the inclusion of the milestones, the SEC is acknowledging that transitioning from the U.S. GAAP system to IFRS will not occur without overcoming many obstacles and challenges, including those relating to regulatory and contractual issues.

Although the Roadmap contemplates the mandatory use of IFRS for some companies beginning in 2014, the release will include a question for comment regarding whether or not the 2014 transition date to IFRS should be sequenced in some way, with large accelerated filers being the first to be required to file IFRS financial statements in 2014, followed by accelerated filers in 2015 and non-accelerated filers in 2016.

Another important part of the proposal would permit a small number of U.S. issuers to adopt IFRS early as the standard of accounting in a company's financial statements. The SEC has identified at least 110 U.S. companies, based on market capitalization, that may be eligible to use IFRS as early

<sup>1</sup> See SEC Press Release 2008-184, available at <http://www.sec.gov/news/press/2008/2008-184.htm> (Aug. 27, 2008).

as 2010, for the fiscal year ending after December 15, 2009. John White, Director of the Division of Corporation Finance, stated that “only an issuer of a certain size within its industry and whose industry, when considered on a global basis, uses IFRS as the basis of financial reporting more than any other set of accounting standards would be eligible to elect IFRS in its Commission filings.” As a result, the early adoption of IFRS would be limited to the 20 largest issuers within an industry group as measured by market capitalization. In order for a U.S. issuer to determine its eligibility to use IFRS before the year 2014, the issuer would have to both look to the parameters set forth in the Roadmap and obtain a letter of no objection from the Division of Corporation Finance.

The Roadmap requests comments on two alternatives that address what U.S. GAAP information must be provided by U.S. issuers who qualify for the early use of IFRS. Under proposal A, which mirrors IFRS 1, a U.S. issuer would have to reconcile its company’s financial statements from U.S. GAAP to IFRS for only the first year of reporting under IFRS. The second alternative, proposal B, would require a U.S. issuer to “provide on an ongoing basis in its Form 10-K annual report an unaudited reconciliation from IFRS to U.S. GAAP covering the three years of IFRS financial statements included in the Form 10-K.” It was highlighted during the Open Meeting that proposal B may provide the safest option for U.S. issuers eligible to use IFRS before the year 2014, in the event that the SEC decides not to adopt IFRS in 2011 or chooses to delay the timeline for its adoption. If some issuers adopt IFRS early, the SEC will be able to collect important market information with respect to costs related to converting from U.S. GAAP to IFRS, and market responses related to changes in prices, volume and liquidity.

With the SEC’s pronouncement, IFRS undoubtedly gained another foothold in the United States’ investment community with Division Director White’s acknowledgement that “IFRS has the potential to become the global set of high-quality accounting standards.” Presently, IFRS is required or permitted in nearly 100 countries around the world, and approximately 85 of these countries require that domestic companies apply IFRS as the principal standard of accounting. In light of the increasing use of IFRS within the international community, the SEC recognizes that the adoption of a single set of high-quality, internationally accepted accounting principles within the United States would further help U.S. companies to remain in the forefront of capital formation by promoting investor confidence, transparency and greater cross-border investment opportunities. In his opening remarks, SEC Chairman Cox noted that “[a]n international language of disclosure and transparency is a goal worth pursuing on behalf of investors who seek comparable financial information to make well-informed investment decisions.” Commissioner Elisse B. Walter, however, cautioned that, while it is important that the SEC consider the potential use of IFRS by U.S. issuers in the future, there are a number of significant hurdles that must be overcome before adoption, and she would support the transition to IFRS if and only if it is in the best interest of investors.

Comments on the proposed rule will be due 60 days after it is published in the Federal Register.

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