

Deloitte.

International Financial Reporting Standards

*Considerations for the
Consumer Products Industry*



Audit • Tax • Consulting • Financial Advisory.

Table of Contents

- Key Differences between U.S. GAAP and IFRS for Consumer Products Companies4**
 - Inventories.....4
 - Leases.....5
 - Impairment of Long-Lived and Indefinite-Lived Assets.....6
 - Property, Plant and Equipment.....6
 - Additional Differences.....7
- More Than Accounting8**
- What Now?.....10**
 - Two Approaches10
 - The Roadmap11
- Resources and Contacts.....12**

International Financial Reporting Standards

Considerations for the Consumer Products Industry

By now you've likely heard the increasing warning signals about the inevitable movement toward International Financial Reporting Standards (IFRS) as a single set of globally accepted accounting standards. While this was intended to provide consistency in financial reporting standards and increased globalization of companies, it also has resulted in significant efforts outside of financial reporting, in areas such as information technology and human resources, and therefore, requires the attention of corporate executives and leaders throughout the organization. Additionally, it may also provide a strategic opportunity for positive organizational change for those who understand the benefits of a reasoned and deliberate conversion process. Of course, like any significant business decision, determining the timing and pace of conversion to IFRS requires an understanding of the potential costs and benefits. It is important to make an informed choice based on a thorough analysis.

Recent events suggest that reporting under IFRS will be allowed or required for most public companies in the U.S. and around the globe within the next few years. On November 14, 2008, the SEC issued its long-awaited proposed IFRS "roadmap" outlining milestones that, if achieved, could lead to mandatory transition to IFRS starting in fiscal years ending on or after December 15, 2014. The roadmap also contains proposed rule changes that would give certain U.S. issuers the early option to use IFRS in financial statements for fiscal years ending on or after December 15, 2009. The SEC believes that "the use of a single, widely accepted set of high-quality accounting standards would benefit both the global capital markets and U.S. investors by providing a common basis for investors, issuers and others to evaluate investment opportunities and prospects in different jurisdictions." The roadmap also notes that IFRS has the potential "to best provide the common platform on which companies can report and investors can compare financial information." The SEC is seeking comments on numerous questions raised in the proposed roadmap. The comment period is expected to run until mid-to-late February 2009.

The proposed roadmap outlines seven milestones. Milestones 1–4 discuss issues that need to be addressed before mandatory adoption of IFRS:

1. Improvements in accounting standards.
2. Accountability and funding of the International Accounting Standards Committee Foundation.
3. Improvement in the ability to use interactive data for IFRS reporting.
4. Education and training on IFRS in the United States.

Milestones 5–7 discuss the transition plan for the mandatory use of IFRS:

5. Limited early use by eligible entities: This milestone would give certain U.S. issuers the option of using IFRS for fiscal years ending on or after December 15, 2009.
6. Anticipated timing of future rule making by the SEC: On the basis of the progress made on milestones 1–4 and experience gained from milestone 5, the SEC will determine in 2011 whether to require mandatory adoption of IFRS for all U.S. issuers. Potentially, the option to use IFRS could also be expanded to other issuers before 2014.
7. Implementation of mandatory use: The roadmap raises many questions, including whether the transition to IFRS should be phased in. According to the roadmap, large accelerated filers would be required to file IFRS financial statements for fiscal years ending on or after December 15, 2014, then accelerated filers in 2015, and nonaccelerated filers in 2016.

Under the proposed roadmap, U.S. issuers that meet both of the following criteria would be eligible to use IFRS earlier in financial statements for fiscal years ending on or after December 15, 2009:

- The U.S. issuer is globally among the 20 largest listed companies worldwide in its industry, as measured by market capitalization.
- IFRS, as issued by the International Accounting Standards Board (IASB), is used as the basis for financial reporting more often than any other basis of accounting by the 20 largest listed companies worldwide in the U.S. issuer's industry, as measured by market capitalization.

An issuer that meets these criteria and chooses to use IFRS (an "IFRS issuer") must prepare its financial statements in accordance with IFRS as issued by the IASB. Issuers electing to file IFRS financial statements with the SEC would be required first to do so in an annual report and would not be able to file IFRS financial statements with the SEC for the first time in a quarterly report, registration statement, or proxy or information statement.

Investment companies; employee stock purchase, savings, and similar plans; and smaller reporting companies, as defined by the SEC, are excluded from the definition of an "IFRS issuer" in the proposed roadmap and therefore would not be eligible to early adopt IFRS. For more information on the SEC's action, visit www.deloitte.com/us/ifrs.

As is becoming increasingly apparent, an IFRS conversion is not primarily an exercise in reshuffling the chart of accounts, nor is it principally a technical accounting and financial reporting matter. Rather, your company is likely to spend a significant amount of time and effort addressing concerns about taxes, valuation, treasury, legal, personnel, technology and communications. Clearly, a great deal of work lies ahead. Yet, despite these challenges, you may find that the benefits of reporting under IFRS outweigh the costs.

Consider these factors:

Conversion provides a fresh look at stale practices. If your close process includes reconciling multiple generally accepted accounting principles (GAAPs), and dealing with a variety of sub-ledgers, manual adjustments, data hand-offs, and accounting overrides, you may want to consider a fresh look at your accounting policies and procedures. IFRS provides the opportunity.

Conversion can be a catalyst for streamlining and consolidation. As your company expands through growth and acquisitions, your information technology systems may become increasingly convoluted. Many companies operate a patchwork of legacy accounting and Enterprise Resource Planning (ERP) systems — systems that can't talk directly, leading to error-prone adjustments and reconciliations. Moving to IFRS provides a chance to streamline and consolidate these disparate systems.

IFRS offers an opportunity to use principles-based accounting. Many finance professionals have become increasingly frustrated with U.S. GAAP and its voluminous rules for dealing with virtually every accounting issue. For a decade or more, CFOs and other finance executives have openly pined for principles-based accounting to help standardize and improve the reliability of financial reporting. IFRS answers that wish.

IFRS helps open the doors of the global marketplace. Adopting IFRS may improve access to foreign capital markets by giving foreign investors greater insight into a company's financial performance. Such investors may be more comfortable with or have more confidence in a globally accepted set of accounting standards. Companies themselves can also benefit from improved ability to benchmark with peers and competitors. Many Consumer Product companies operate on a worldwide scale: Growing markets. Expanding customer bases. Escalating merger and acquisition activity. The fact is, your company already does business globally. Shouldn't you be reporting under a global standard?

Consumer Products Competitive Landscape*

Company	U.S. GAAP	IFRS	Other	International Operations	Revenue** (Billions)
Altria Group, Inc.	X			X	\$101
Hewlett-Packard Company	X			X	\$92
Samsung Electronics Co., Ltd.			X	X	\$92
Nestle SA		X		X	\$79
Matsushita Electric Industrial Co., Ltd.	X			X	\$77
The Procter & Gamble Company	X			X	\$76
Sony Corporation	X			X	\$64
Toshiba Corporation	X			X	\$60
Dell Inc.	X			X	\$57
Nokia Corporation		X		X	\$52
Unilever Group		X		X	\$50
LG Electronics Inc.			X	X	\$48
Motorola, Inc.	X			X	\$43
Japan Tobacco Inc.			X	X	\$40
Canon Inc.	X			X	\$35
PepsiCo, Inc.	X			X	\$35
Koninklijke Philips Electronics N.V.	X			X	\$33
Sharp Corporation			X	X	\$27
Bridgestone Corporation			X	X	\$26
Tyson Foods, Inc.	X			X	\$26
The Coca-Cola Company	X			X	\$24
Fujifilm Holdings Corporation			X	X	\$24
Imperial Tobacco Group PLC		X		X	\$21
Michelin Group		X		X	\$21
The Goodyear Tire & Rubber Company	X			X	\$20

* Top 25 Global Consumer Products companies, based on revenues, as of the most recent annual publicly filed report.

** Obtained from the most recent annual publicly filed report.

Accounting Considerations

While IFRS is similar to U.S. GAAP in many respects, there are still some significant differences. For example, IFRS specifically prohibits the use of the last-in, first-out (LIFO) costing method, and it provides the ability to reverse inventory write-downs, revalue fixed assets, and reverse long-lived and indefinite-lived impairment charges (with the exception of goodwill).

Many international companies have already adopted IFRS. Some of the benefits that have been derived from this shift include increased transparency and consistency of financial information, more efficient use and availability of global resources, streamlined internal controls, additional access to capital, simplified cross-border M&A transactions, and opportunities for improved cash management and local income tax cash liability reductions and income tax planning.

Key Impacts of IFRS Implementation

Technical Accounting	Process and Statutory Reporting	Technology Infrastructure	Organizational Issues
<ul style="list-style-type: none"> Overall approach to IFRS implementation First time adoption policy considerations, including reporting dates and use of exemptions Ongoing policy considerations, including alternatives and approach to “principles” 	<ul style="list-style-type: none"> Internal controls and processes, including documentation and testing Management and internal reporting packages Global reporting packages Statutory reporting, including “opportunities” around IFRS adoption 	<ul style="list-style-type: none"> General ledger and chart of account structure, including performance metrics Global consolidation Sub-system issues related to configuration and data capture Capabilities to manage multiple GAAP accounting during transition 	<ul style="list-style-type: none"> Tax structures Treasury and cash management Legal and debt covenants People issues, including education and training, and compensation structures Internal communications External and shareholder communications

The potential benefits of transitioning a multinational organization to a single set of accounting standards do not come without a cost, however.

Conversion to IFRS will require a significant commitment of specialized resources in order to properly analyze and plan implementation. Companies must assess and create policies with a global understanding of the processes and goals of the entire organization, train the appropriate people in the organization (often across cultural and language barriers) and implement appropriate information systems and operational processes.

One significant challenge is a shift in how accounting policies are developed, written and applied. Since IFRS focuses more on principles rather than the rules-based approach under U.S. GAAP, the implementation of IFRS will involve a new way of thinking about accounting and financial reporting. This new way of thinking places greater emphasis on interpretation and application of principles — with a particular focus on the substance and underlying economics of a transaction, and on transparency of financial information rather than uniformity of practices. This requires a renewed focus on professional judgment in arriving at accounting conclusions. A cultural shift to IFRS may prove very challenging because most accounting and finance professionals in the U.S. are accustomed to detailed guidance and strict conformity of application. Companies will need to look at accounting and financial reporting in a new way.

While IFRS allows for a more principles-based approach, there are also published standards and rules that contain significant differences from U.S. GAAP. The purpose of this communication is to provide insight on the potential impact to consumer product companies that may result in a conversion from U.S. GAAP to IFRS, including technical accounting differences and the potential impact on income taxes and information systems. Keep in mind that no summary publication can do justice to the many differences in the details that exist between IFRS and U.S. GAAP and this document only focuses on the areas with a broad impact to the consumer products industry. In addition, even if the overall approach taken in the guidance is similar, there can be differences in the detailed application, which could have a material impact on the financial statements.



Key Differences between U.S. GAAP and IFRS for Consumer Products Companies

IFRS guidance is currently comprised of 38 standards and 26 interpretations. Some of the more significant differences between U.S. GAAP and IFRS of particular interest to consumer product companies are discussed below, along with their associated impact on tax, processes and systems.

Inventories: International Accounting Standard 2 (IAS 2)

Accounting Methods

The cost of inventory under both U.S. GAAP and IFRS generally includes direct expenditures of getting inventories ready for sale, including overhead and other costs attributable to the purchase or production of inventory. IAS 2 specifically requires use of either the first-in, first-out (FIFO) or the weighted-average cost method, but allows the standard cost method or the retail method for convenience if the results approximate cost. Further, IFRS requires that the same costing formula be used for all inventories with a similar nature and use to the entity.

The Tax Dilemma

Under U.S. GAAP, during periods of rising prices, the LIFO costing method leads to higher recognized costs of sales, and thus reduces taxable income. Under Internal Revenue Service (IRS) rules, consumer product companies using the LIFO method must conform their financial reporting method to LIFO. But under IFRS, use of the LIFO costing method is explicitly not permitted. The adoption of IFRS for financial reporting purposes could result in significant tax consequences, as its stated preclusion of LIFO for financial reporting would violate current IRS conformity requirements for those using LIFO for tax purposes.

Some business observers speculate that the U.S. Congress and the IRS will be compelled to address this issue should IFRS be mandated, perhaps by offering a one-time conversion opportunity that limits the tax liability. Companies should closely monitor developments in this area and may want to begin the analysis to estimate the dollar cost of converting from LIFO under the current IRS conversion rules.

Carrying Value

Under U.S. GAAP, inventories are required to be stated at the lower of cost or market ("LCM"), with market defined as current replacement cost. Market should not exceed net realizable value (defined as the estimated selling price in the ordinary course of business less reasonably predictable costs of completion and disposal) or be less than NRV reduced by an allowance for a normal profit margin. For U.S. GAAP purposes, application of the LCM approach leads to an acceptable range of practice among consumer product companies, given the floor and ceiling concept in the definition of market.

Under IFRS, inventories are stated at the lower of cost or net realizable value (defined as the estimated selling price in the ordinary course of business less the estimated cost of completion and the estimated cost necessary to make the sale). Under IFRS, there is no concept of reducing NRV to allow for a normal profit margin. While the definitions of carrying value under U.S. GAAP and IFRS appear to be only slightly different, the outcome may be significantly different depending on a company's current practice for determining LCM.

Reversal of Write-Downs

A new assessment is made of net realizable value in each subsequent period. Under IFRS, unlike U.S. GAAP, when the circumstances that previously caused inventories to be written down below cost no longer exist or when there is clear evidence of an increase in net realizable value because of changed economic circumstances, the amount of the write-down is reversed (i.e., the reversal is limited to the amount of the original write-down) so that the new carrying amount is the lower of the cost or the revised net realizable value. This occurs, for example, when an item of inventory that is carried at net realizable value because its selling price had declined, is still on hand in a subsequent period and its selling price has increased. Any impairment or reversal is recorded to cost of sales in the period in which it occurs.

Summary of Impact on Inventories

Key Accounting Differences	Potential Implications		
	Financial Statements	Process/Systems	Taxes/Other
<ul style="list-style-type: none"> • LIFO prohibited • Measure at cost or NRV • Use same valuation method • Reversal of impairment 	<ul style="list-style-type: none"> • Valuation of inventory • Impairment charges 	<ul style="list-style-type: none"> • Inventory system changes • Processes around reversal of inventory impairment 	<ul style="list-style-type: none"> • Potential significant cost if LIFO change • Impact from change in valuation

Leases: IAS 17

The scope of IFRS lease guidance includes the right to use other types of assets in addition to property, plant, and equipment (e.g., certain intangible assets). Certain intangible assets are within the scope of IAS 17 if they establish rights for the exclusive use of the intangible asset. For example, brands and trademarks often are licensed exclusively and therefore are included in the scope of IAS 17.

Lease Classification

Under IFRS, lease classification (e.g., operating or finance – which is the IFRS term for capital lease) depends on similar criteria as U.S. GAAP, but without the bright-line guidance. For example, IAS 17 states that a lease would normally be a finance lease if the lease term is for the “major part” of the economic life (not a strict 75 percent), or the present value of the minimum lease payments at lease inception is for “substantially all” of the fair value (not 90 percent). The basic IFRS principle is: if the lease does not transfer substantially all risks and rewards incidental to ownership to the lessee, then the lease is classified as an operating lease.

Leases of Land and Buildings

U.S. GAAP generally requires the lease of land and building elements to be accounted for as a single unit in all but limited circumstances. IAS 17 requires the lease of land and building elements to be accounted for separately for a lease classification unless the land element is not material. The present value of the minimum lease payments, including any lump-sum upfront payments, are allocated between the land and building elements based on the relative fair values of the lessee’s leasehold interest in the land and the building. This can significantly impact Consumer Product companies that lease both the land and the building. Consumer Product companies will need to reassess their lease classifications and may need to break out the land and the building into separate leases.

Lease Expense

Similar to U.S. GAAP, lease expense should be recognized on a straight-line basis over the lease term, unless another systematic basis is more representative of the pattern of benefit. Lease incentives (such as free rent periods) are recognized as a reduction of expense over the lease term.

Sale-Leaseback Transactions

Under U.S. GAAP, separate requirements exist for sale and leaseback transactions involving real estate. Under IFRS, there is no difference in accounting between sale and leaseback transactions involving real estate and non-real estate assets. Under IFRS, the timing of recognition of a gain or loss on a sale and leaseback transaction differs depending on the classification of the leaseback.

Comparison of Impairment Approaches

	IFRS	U.S. GAAP
Capital/Finance Lease	Deferred and amortized over lease term	Deferred and amortized over lease term with limited exceptions (seller retains less than substantially all of the use of the leased asset)
Operating Lease	Record immediately if sales price is established at fair value. Otherwise, defer and amortize over lease term.	

Summary of Impact on Leases

Key Accounting Differences	Potential Implications		
	Financial Statements	Process/Systems	Taxes/Other
<ul style="list-style-type: none"> • Determining lease classification • Break out land and building into separate lease • If known, use implicit rate for discount rate even if higher than incremental borrowing rate • Recognize gain on sale-leaseback for operating lease immediately • No specific guidance for specialized leases (leveraged-leases, etc.) 	<ul style="list-style-type: none"> • Potentially more capital leases • Income recognition from operating sale-leasebacks 	<ul style="list-style-type: none"> • Lease classification system changes • Increased diligence to determine separate value of land and building, identify implicit rate, and apply guidance 	<ul style="list-style-type: none"> • Impact from change in lease classification and sale-leaseback gains • Covenants

Impairment of Long-lived and Indefinite-lived Assets (IAS 36 (Revised))

Management agreements, franchise agreements, license agreements, customer lists, trademarks, and goodwill represent some of the long-lived and indefinite-lived assets held by Consumer Product companies.

IFRS requires that goodwill and other indefinite-lived intangibles be tested for impairment at least annually, or more frequent if an indicator is present. Other long-lived assets are reviewed at the end of each reporting period for any indication of impairment, and tested for impairment if necessary. IFRS requires impairment testing at the “cash-generating unit” (CGU) level, which is generally similar to the U.S. GAAP “asset group” level, but may result in a lower level of testing.

However, IFRS differs from U.S. GAAP in the method and valuation for calculating impairment, and allows for reversal of impairment with the exception of goodwill. Long-lived asset impairment is a one-step approach under IFRS and is assessed on the basis of recoverable amount, which is calculated as the higher of fair value less costs to sell or value in use (e.g. discounted cash flows). If impairment is indicated, assets are written down to the higher recoverable amount.

Comparison of Impairment Approaches			
	U.S. GAAP		IFRS
	Goodwill	Fixed Assets	All Finite & Indefinite-Lived Assets
Step 1	Determine if impairment exists by comparing the total carrying value of the reporting unit to its fair value. If the carrying value exceeds the fair value, go to step 2.	Determine whether impairment exists by comparing the carrying value of the asset group to the undiscounted cash flows. If the carrying value exceeds the undiscounted cash flows, go to step 2.	Determine if impairment exists by comparing the carrying value of the CGU or asset to its recoverable amount as defined above. If the carrying value exceeds the recoverable amount, impairment is recognized for the difference.
Step 2	Calculate and assign fair value of all other assets and liabilities of reporting unit, remainder equals implied goodwill. Impairment charge is measured as the difference between the carrying value and implied fair value of goodwill.	An impairment charge is recognized by reducing the carrying value of the asset group to its estimated fair value.	Not applicable.

The ultimate effect of IFRS is that impairment will likely occur sooner than under U.S. GAAP, but may not be as high. For example, assume a manufacturing facility’s undiscounted cash flow exceeds the asset carrying value but value in use is less than the asset carrying value. No impairment charge would be recorded under U.S. GAAP as the step 2 test would not be performed. An impairment charge would be recorded under IFRS.

After the recognition of an impairment charge, the depreciation or amortization charge for the asset shall be adjusted in future periods to allocate the asset’s revised carrying amount, less its residual value, on a systematic basis over its remaining useful life. An impairment charge shall be recognized immediately in profit or charge, unless the asset is carried at revalued amount. Any impairment charge of a revalued asset shall be treated as a revaluation decrease.

Reversal of Impairment Charge

Except for goodwill, IFRS allows the reversal of impairment charges if the recoverable amount of an asset has increased since the impairment charge was recognized. An entity should increase the value of the asset to its current recoverable amount and the prior impairment charge recorded is therefore reversed, not above the carrying amount of the asset that would have existed if no impairment charge had been recognized (i.e., the otherwise net carrying amount after regular depreciation expense is deducted). A reversal of an impairment charge for an asset other than goodwill shall be recognized immediately in profit or loss, unless the asset is carried at revalued amount. Any reversal of an impairment charge of a revalued asset shall be treated as a revaluation increase.

Impaired assets must be tracked at original value in order to calculate the amount of impairment reversal. The reversal of the impairment is only allowed to the extent of the impairment previously recognized. After the reversal of an impairment charge, the amortization amount for the asset should be adjusted on the basis of the new value of the asset, its residual value, and its remaining useful life.

Property, Plant, and Equipment (IAS 16 (Revised))

Property, plant, and equipment (PP&E), one of the most significant line items on a Consumer Product company’s balance sheet, represents a key area of difference between IFRS and U.S. GAAP.

Measurement after Recognition

Under IFRS, an entity may elect to value PP&E using either the cost or revaluation model. Under the revaluation model, an entire class of PP&E is revalued at fair value regularly, if fair value can be measured reliably. The revalued amount is the fair value of the asset at the revaluation date less any accumulated depreciation and accumulated impairment charges. Revaluation increases are credited to equity and labeled revaluation surplus. However, if a revaluation decrease has been previously charged to income, then the revaluation increase would be charged to income to the extent of the previous revaluation loss and any additional amount would be credited to equity and labeled revaluation surplus. Revaluation losses are charged first against any revaluation surplus in equity related to the specific asset, and any excess charged to income.

This is significant to THL companies, since companies may choose to revalue certain asset groups (e.g. land and buildings), but not revalue other groups (e.g. machinery and furniture and fixtures). In turn, Consumer Product companies will also need to determine the impact this will have on their accounting systems. Systems will need to be established to track these changes and recompute the related depreciation. Similarly, the decrease in fair value of the asset will trigger a decrease in the annual depreciation.

Depreciation

IFRS requires a component approach for depreciation where assets must be separated into individual components and depreciated over their useful lives. For example, components of a Consumer Product company's building may include, building, roof, flooring, furnishings and parking lot, etc. Each of these assets could represent a separate component and may have a different depreciation method or rate. Subsidiary ledgers will need to be set up to ensure that asset components are properly recorded as individual components.

Estimates of useful life and residual value, and the method of depreciation are reviewed at least annually. The residual value may be adjusted up or down, and any changes that result in differences in expectations from previous estimates, shall be accounted for as a change in an accounting estimate under IFRS. These changes also have a direct effect on the depreciation taken on the asset, as the higher values would result in higher depreciation and vice versa. Additionally, IFRS requires that the depreciation method applied to an asset be reviewed at each financial year-end. If there is a significant change in the expected pattern of consumption of the future economic benefits of the assets, the method shall be changed to reflect the changed pattern.

Additional Differences

Additional technical accounting differences of specific interest to consumer product companies include:

Revenue Recognition	Generally, for U.S. GAAP under SAB Topic 13A, "Revenue Recognition," delivery is required to have occurred to provide sufficient evidence that risks and rewards of ownership have passed. IAS 18, "Revenue," accepts that delivery is not always necessary for revenue to be recognized, because the risks and rewards of ownership may be transferred to the buyer even though the goods have not yet been delivered. For example, it is possible to recognize revenue on bill-and-hold sales and lay-away sales under IAS 18, when those sales would not be recognized under U.S. GAAP.
Discontinued Operations	IFRS 5 requires that a discontinued operation is a component of an entity that either has been disposed of or is classified as held for sale and: <ul style="list-style-type: none"> • represents a separate major line of business or geographical area of operations, or • is part of a single coordinated plan to dispose of a separate major line of business or geographical area of operations, or • is a subsidiary acquired exclusively with a view to resale. <p>U.S. GAAP allows discontinued operations treatment for a component of an entity rather than a separate major line of business or geographical area of operations. Therefore, many routine dispositions of components do not meet the criteria for discontinued operations treatment under IFRS.</p>
Asset Retirement Obligations	Under U.S. GAAP, FASB Statement No. 143, "Accounting for Asset Retirement Obligations," states, in part: upon initial recognition of a liability for an asset retirement obligation, an entity shall capitalize an asset retirement cost by increasing the carrying amount of the related long-lived asset by the same amount as the liability.
	Conversely, IAS 16, "Property, Plant and Equipment," states that an entity applies IAS 2, inventories to the costs of obligations for dismantling, removing and restoring the site on which an item is located that are incurred during a particular period as a consequence of having used the item to produce inventories during that period. The obligations for costs accounted for in accordance with IAS 2 or IAS 16 are recognized and measured in accordance with IAS 37, "Provisions, Contingent Liabilities and Contingent Assets." In other words, IFRS allows asset retirement obligation costs to be added to the carrying amount of the inventory in the period in which they are incurred.
Advertising Costs	Under U.S. GAAP, advertising costs are expensed as incurred or capitalized and then expensed the first time the advertisement runs. The timing of expense recognition could be different under IFRS based on facts and circumstances.
Vendor Allowances	Under IFRS, accounting for vendor allowances, which commonly include volume rebates, advertising contributions, promotional discounts, and slotting fees, is not as clearly defined as under U.S. GAAP. Three criteria should be considered in identifying the accounting treatment of vendor allowances under IAS 18: 1) benefit to the vendor; 2) whether services provided are separable from the purchases; 3) whether the service is billed at fair value. If these three criteria are met, expensing these costs would appear appropriate. If not, these costs should be recorded as a reduction of revenue.

Income Tax Considerations

The key areas for companies to consider are: 1) financial accounting for income taxes - converting from FAS 109 to IAS 12, 2) what will come first, conversion or convergence, 3) IAS 12 provides no guidance for income tax uncertainty (IFRS generally follows IAS 37), 4) tax compliance processes, 5) tax accounting methods, and 6) global tax planning.

The change from FAS 109 under U.S. GAAP to IAS 12 will involve various computational and disclosure changes. While these changes will require a thorough understanding by all companies, there are some areas that specifically impact the consumer products industry (i.e. intercompany transfer of assets remaining within the group).

Whether it is income, sales, property, business, value-added or other taxes, consumer products companies are familiar with the tax compliance obligations of operating in numerous jurisdictions. With respect to income taxes, because taxable income in many non-US jurisdictions is based on financial statement earnings, the underlying methodology to determine taxable income can change and provide the consumer product company with a better cash tax result. In addition, non-income taxes are frequently based on amounts derived from the financial statements.

The accounting standards under IFRS may impact tax compliance processes. A few examples:

- The consolidation regime of IFRS may require that additional operations be included within the financial statements that are not currently included. Thus the starting point to compute taxable income may include entities or operations that would not be included for income tax purposes. Many companies have customized electronic record processing (ERP) and reporting systems to provide data tailored to tax reporting requirements. Current systems may need to be recalibrated under IFRS as a result.
- Under IFRS fixed asset accounting will become more complex due to component depreciation and the revaluation method as discussed earlier in this document. Tax departments will need to work with accounting and IT to assess their current systems and how to track fixed assets, including the calculation of depreciation for tax purposes on an asset by asset basis.
- State income tax apportionment is generally computed by a combination of property, payroll, and sales information that will likely change under IFRS. Tax departments will need to revisit the processes used to extract this information and determine the cash tax impact.

Property taxes for real estate and business personal property are often based on U.S. GAAP amounts. Several open questions include (i) whether IAS 16 will be adopted by local tax jurisdictions as a measure for computing property tax, and (ii) whether existing accounting systems will maintain this information or whether tax departments will need to maintain separate records.

It is important to address the tax consequences of the pre-tax differences between IFRS and GAAP because a conversion to IFRS requires changes to several financial accounting methods. Consequently, companies may need to re-evaluate their existing tax accounting methods. As mentioned above, the starting point for calculating U.S. taxable income is book income as reported in accordance with GAAP (IRC §446). Companies should consider these changes as they would any other financial accounting method changes.

Tax considerations are an essential part of an IFRS strategy. Exploring opportunities to increase after-tax cash flow and managing the organization's overall corporate effective tax rate are important aspects of developing a comprehensive IFRS strategy. There are transactions prior to adoption that may create value to the organization such as intercompany transactions. Companies that make the most of a conversion to IFRS will approach the undertaking as more than a mere "IAS 12 vs. FAS 109" exercise. If the tax accounting and reporting components are overlooked or not properly brought into the fold, unintended adverse tax consequences may occur. Exploring and analyzing the tax consequences early – including the impact on systems and processes – can help inform and determine the optimal path toward a successful IFRS conversion.

More Than Accounting

Without question, IFRS will impact the general ledger and the financials. But in a relative sense, the accounting and financial reporting may be the easy part. How you handle the nonfinancial aspects of the conversion may be a far more accurate indicator of your success. Among the areas warranting your attention are human resources, legal, regulatory, treasury, contract management, and technology.

Human Resources: As noted, IFRS involves much more than reorganizing the chart of accounts. It represents a change that cascades well beyond the finance department. Consequently, human resources issues may be a major concern. A conversion project will place increased demands on your personnel, which may come at a time when you are least able to handle it. Finance organizations have streamlined in recent years, downsizing accounting functions through reduced hiring, layoffs, and attrition, as well as outsourcing or offshoring key functions. Unfortunately, these personnel reductions may mean that the people who could best help with your IFRS efforts are no longer available.

Recruiting may pose another challenge, particularly in the United States. College accounting programs across the country represent an important pipeline for keeping finance functions staffed and operating. Yet, most U.S. university accounting programs are only now beginning to develop comprehensive instruction on IFRS.

This issue can be addressed through training programs in the U.S. and internationally, to help key personnel become proficient in both IFRS and U.S. GAAP.

Legal: The ripple effects of conversion to IFRS will surely be felt by your legal department. Many contracts will need to be examined for possible impact, and some agreements, including debt compliance covenants, may need to be renegotiated and restructured.

Education and retraining will also come into play for the legal team. IFRS principles and associated guidance from the SEC will need to be analyzed and understood from a legal perspective.

Regulatory: The opportunity to reduce local GAAP reporting and coalesce around a single standard will be appealing to many companies. The change may be dramatic. For example, until recently, companies doing business in Western Europe had to track financial information using up to 21 different GAAPs. The EU's 2005 conversion to a single standard harmonized and simplified compliance, and today there is more cross-border consistency in the application of rules and standards.

A fringe benefit of conversion may be the promise of collaboration among various regulatory bodies. The model for this was provided by the Committee of European Securities Regulators (CESR), an independent body that works to improve coordination among EU securities regulators. This group, formed in 2001, played an important role in the IFRS conversion effort by bringing together regulators from across the EU to discuss issues, smooth over differences, and reconcile complex points of view.

As other countries across the globe adopt IFRS, the prospect of additional regulatory bodies (such as the SEC) interacting with their counterparts increases. Thus, the movement toward IFRS is changing the regulatory dynamic, forcing regulators to think globally, instead of nationally, in how they treat these issues.

Treasury: Moving to a global financial reporting model may open up access to new sources of capital. Many global lenders, global private equity firms, and international exchanges require or prefer IFRS reporting due, in part, to its increased transparency into fair values and comparability to other investments or companies. Thus, these sources potentially become new avenues for capital funding.

Note, however, that greater use of fair value may create more volatility in your company's access to capital. That is, not only can reporting under IFRS potentially open up access to additional capital in a favorable fair value environment, but it can also serve to limit additional capital in an unfavorable fair value environment.

Furthermore, with reporting or disclosure under fair value, management will certainly need to understand, evaluate, and manage the expected market reactions to reported volatility of values. This will represent new territory for most U.S.-headquartered Consumer Product companies.

Additional impacts of IFRS on the treasury function may include the following:

- Companies that choose to present fair value may consider the need to lower their leverage models to ensure that market fluctuations can be adequately absorbed by equity.
- Companies may need to consider and revise debt terms for covenants based on U.S. GAAP metrics or financial results which don't make sense or are no longer attainable under IFRS.
- The clearer view that lenders get of the fair value of collateral (whether presented on the balance sheet or disclosed in the footnotes) may alter their evaluation of creditworthiness and may impact the terms of new debt instruments related to collateral values and covenants.

Contract Management: An IFRS conversion will potentially impact your existing contracts. Consider involving your legal team as part of the remedy. Issues may include the following:

Many contracts may need to be reviewed to make sure the proper accounting treatment is followed under IFRS. To improve the efficiency of this process, a contract database could be created (if not already in place) to better monitor the IFRS conversion and tracking of effects.

The IFRS conversion may trigger the need to amend contracts with financial institutions and joint venture partners in regards to financial accounting information to be supplied by your company. You may have to reword certain sections to address regulatory or third-party requirements to replace U.S. GAAP with IFRS information.

Technology: IFRS is expected to have wide-ranging impacts at different levels of the IT systems architecture. The realignment of the company information systems will pose a real challenge for IT (along with the rest of the organization). Virtually all applications and interfaces in the system architecture can be affected, from the upstream or source of data to the farthest end of the reporting tools. As such, time and resource needs may be significant.

As you plan changes to your IT systems, you will need to take into account external factors such as local and international regulations, financial consolidation of subsidiaries, stock markets, and external auditors. This business transformation should not be considered a one-step project. It may be necessary to implement short-term initiatives strategically designed to institute an effective long-term solution for the organization.

Potential Technology Impacts

Upstream Source Systems and Transformation Layer	General Ledger and Financial Applications	Reporting Data Warehouse Planning and Calculation Engines	Downstream Reporting Capabilities
Differences in the accounting treatment between current accounting standards and IFRS will create a need for new input data.	Differences in the accounting treatment between current accounting standards and IFRS will likely drive changes to General Ledger design, Chart of Accounts, as well as sub-ledgers and feeds.	IFRS has much more extensive disclosure requirements, requiring regular reporting and usage of financial data that may not be standardized in current data models.	The differences that arise in the accounting treatment between current accounting standards and IFRS will create a need for changes in reporting.
Data and transactions that are captured, stored and ultimately sent to the financial systems may not have all the needed attributes or qualities.	Multinational companies may ultimately realize a need to re-develop General Ledger platforms or additional sets of books to ensure compliance with multiple financial reporting requirements.	Increased need for documented assumptions, sensitivity analyses, potential factors that could affect future development may expand the scope of information managed by financial systems.	Assumption changes from period to period can introduce significant volatility and require detailed support for derivation and rationale for changes, requiring design of additional reports.
Sub ledgers within the ERP may have additional functionality to support IFRS which is currently not being utilized, but which could be implemented.	Multi-ledger accounting functionality within newer releases of ERP's may be considered for long-term solutions.	Reporting warehouse feeds to calculation engines may need to be adjusted in a standardized way to support reporting processes.	External reporting templates will likely require revisions to reflect IFRS requirements.
Transformation Layer not likely to have been designed with IFRS in mind; data sender/receiver structures may need to be adjusted.	Changes to IFRS will likely necessitate redesigned accounting, reporting, consolidation, and reconciliation processes, which may impact configurations of the financial applications.	Data governance functions and Meta Data Repositories (potentially including Data Dictionary, ETL & Business Intelligence Tools) may need to be adjusted to reflect revised data model.	Increased disclosures such as sensitivity tests and roll-forwards may require additional ad hoc query capabilities.
Over time the potential for acquisitions of companies using IFRS will increase; altering source systems and Extract, Transform and Load (ETL) tools to provide all needed data elements will make integrations significantly more efficient.	Differences that arise in accounting treatment between current accounting standards.	Current valuation systems may not have functionality to handle IFRS requirements.	

What Now?

Two Approaches

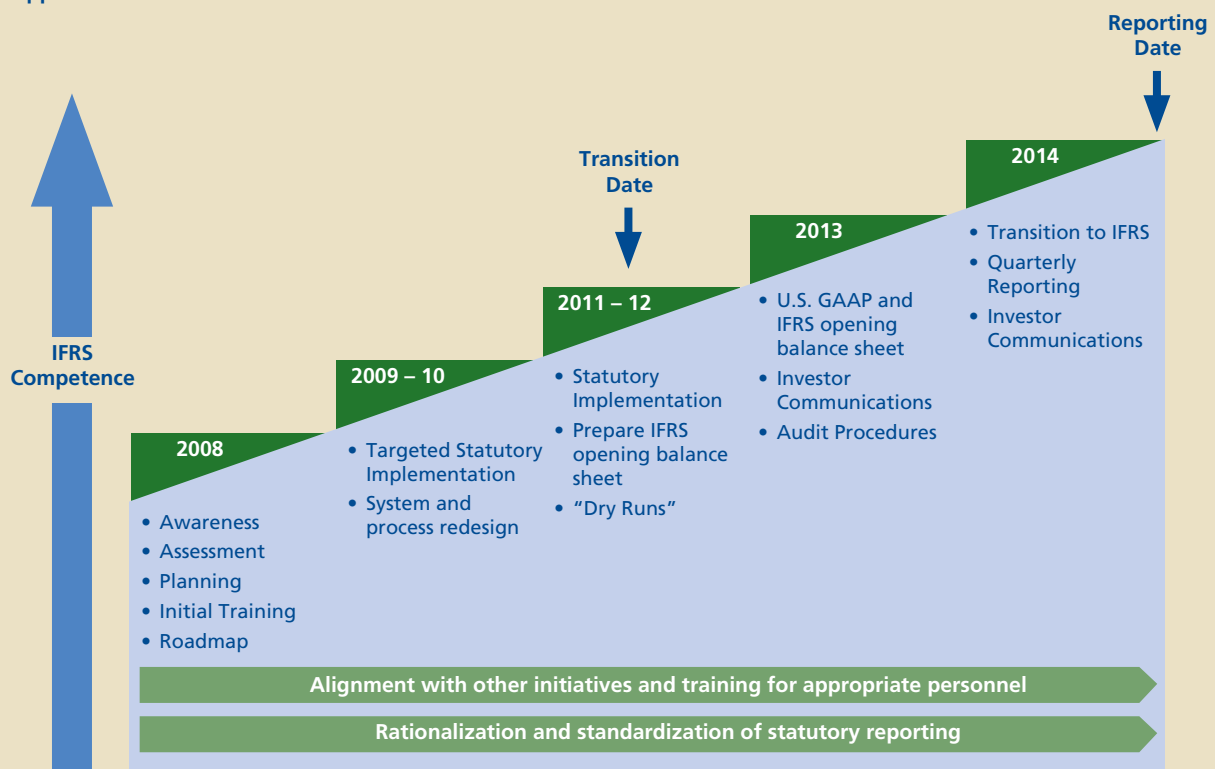
Generally speaking, two approaches to IFRS conversion predominate: all-in and tiered. The former is characterized by a relatively short timeframe; simultaneous conversion of all reporting entities; dedicated project teams; and devotion of significant resources. The latter is conducted over a more extended period with phased conversion of reporting entities, at least some personnel retaining of their “day job” duties, and a spreading out of project costs.

When the European Union converted to IFRS in 2005, it was, for most companies, an all-in effort driven by the tight timelines imposed by the European regulators. Without the luxury of time to convert on a staggered basis, most companies were forced to rush through the process, leading to inevitable inefficiencies and ineffectiveness.

A tiered approach – staged, rational, and measured – to IFRS conversion may be the best approach for consumer products companies. This comes with a seemingly self-contradictory caveat: You’ll have to act fast if you want to go slow. That is, if you want to reap the benefits of phasing in your conversion, you’ll need to start planning soon.

Companies that choose a tiered strategy can stagger their conversions on a country-by-country or region-by-region basis. As each group moves through the stages (see graphic, “A Tiered Approach to IFRS Conversion”), the processes developed and lessons learned are applied to the next group. Many companies will choose Canada for the first conversion, given its 2011 mandate for conversion.

A Tiered Approach to IFRS Conversion – Illustrative*



* The chart reflects the IFRS requirement of three years of income statement reporting (two historical years and the current year) and two years of balance sheet reporting (one historical year and the current year).

The Roadmap

Whether you plan to charge ahead full steam or take small, measured steps, performing an initial assessment and developing an IFRS implementation roadmap will be a good starting point. Through this effort, you'll likely be able to chart the optimal course, determine the pace of your journey, and improve your chances of skirting any detours and potholes.

If you take only one action after reading this document, we suggest it be this: Develop an IFRS implementation roadmap. To kick off this effort, ask yourself and your team a few preliminary questions to gauge the potential impact of IFRS on your company.

- Have we inventoried our current IFRS reporting requirements, if any?
- How many local GAAPs do we currently report under?
- How many of our business units already prepare IFRS financial statements?
- How might our access to capital be impacted by an IFRS conversion?
- How many of our competitors have converted to IFRS? Is there an expectation that they would switch to IFRS, if given the choice in the U.S.?
- Do we have a major ERP or finance transformation project in the works?
- Are we involved in or considering a major acquisition?
- What is the level of IFRS knowledge within the company, both domestically and globally?
- What would be the impacts on our company of a possible IFRS requirement in the U.S.?
- Have we assessed the cost and benefits of adopting IFRS?

The answers to these questions will influence the timing and pace of your IFRS implementation.

Of course, your final roadmap will contain significantly more detail than shown above. Given the far-reaching scope of IFRS, your map-making process may assess the potential impact on each department in your organization, including finance, human resources, tax, legal, information technology, and investor relations. Other stakeholders should also be involved, including the board, audit committee, shareholders, and your external auditor.

By determining your costs, benefits, and timing up front, you can avoid a rushed approach and incurring unnecessary expense. A carefully designed roadmap may empower your company to convert on its own terms. By taking a measured and informed approach, you increase the likelihood of identifying value in an exercise that otherwise may be reactive and solely compliance driven. The value may show itself in the form of reduced costs of implementation, standardization of statutory reporting activities and related controls, greater standardization of accounting policy application, and possibly core finance transformation.

Resources

Deloitte has extensive experience in International Financial Reporting Standards (IFRS). With thousands of IFRS-experienced professionals in our global network, we provide a comprehensive array of services related to IFRS. As a multidisciplinary organization, we can help companies address a wide range of IFRS issues. We offer companies assistance with:

- Evaluating the potential impacts of IFRS
- Assessing readiness for IFRS conversions
- Implementing IFRS conversions, providing support with technical research, project management, and training
- Addressing the implications of IFRS in such areas as tax, finance operations, technology, and valuation

Contacts

For more information, please contact:

Richard G. Kabobjian
U.S. AERS Leader, Consumer Products
Partner, Deloitte & Touche LLP
+1 973 602 6940
rkabobjian@deloitte.com

Pat Conroy
Vice Chairman
U.S. Consumer Products Leader
Deloitte LLP
+1 317 656 2400
pconroy@deloitte.com

D.J. Gannon
National Leadership Partner, IFRS Solutions Center
Partner, Deloitte & Touche LLP
+1 202 220 2110
dgannon@deloitte.com

Joel Osnoss
Leader, Global IFRS Service Line
Partner, Deloitte & Touche LLP
+1 212 436 3352
josnoss@deloitte.com

Alfred Popken
Principal, Deloitte & Touche LLP
+1 212 436 3693
apopken@deloitte.com

Visit Deloitte.com

To learn more about our practice, visit us online at www.deloitte.com/us/consumerproducts. Here you can access our complimentary Dbriefs webcast series, Deloitte Insights podcast program, innovative and practical industry research, and a lot more about the issues facing retailers from some of the industry's most experienced minds.

Contacts

Gilberto Mercado

Phone: +52 (55) 5080 6770

gmercado@deloittemx.com

Miguel Millán

Phone: +52 (55) 5080 6190

migmillan@deloittemx.com

Octavio Aguirre

Phone: +52 (55) 5080 6790

oaguirre@deloittemx.com

Benjamin Gallegos

Phone: +52 (55) 5080 6796

bgallegos@deloittemx.com

Aguascalientes

Universidad 1001, piso 12-1, Bosques del Prado
20127 Aguascalientes, Ags.
Phone: +52 (449) 910 8600, Fax: +52 (449) 910 8601

Cancún

Avenida Tulúm 269, PH-3, SM 15-A, M 3, lote 2-03
77500 Cancún, Q. Roo
Phone: +52 (998) 892 3675, Fax: +52 (998) 892 3679

Celaya

Edificio Deloitte, pisos 1 y 2, Blvd. A. López Mateos 1206 Ote.,
Colonia Las Insurgentes, 38080 Celaya, Gto.
Phone: +52 (461) 159 5300, Fax: +52 (461) 159 5333

Chihuahua

Centro Ejecutivo Punto Alto II, Av. Valle Escondido 5500,
Fracc. Des. El Saucito E-2, piso 1, 31125 Chihuahua, Chih.
Phone: +52 (614) 180 1100, Fax: +52 (614) 180 1110

Ciudad Juárez

Paseo de la Victoria 3751, piso 2, Colonia Partido Senecú
32540 Ciudad Juárez, Chih.
Phone: +52 (656) 688 6500, Fax: +52 (656) 688 6536

Culiacán

Calz. Insurgentes 847 Sur, Local 3, Colonia Centro Sinaloa
80128 Culiacán, Sin.
Phone: +52 (667) 761 4339, Fax: +52 (667) 761 4338

Guadalajara

Avenida Américas 1685, piso 10, Colonia Jardines Providencia
44638 Guadalajara, Jal.
Phone: +52 (33) 3669 0404, Fax: +52 (33) 3669 0469

Hermosillo

Francisco Eusebio Kino 309-9, Colonia Country Club
83010 Hermosillo, Son.
Phone: +52 (662) 109 1400, Fax: +52 (662) 109 1414

León

Paseo de los Insurgentes 303, piso 1, Colonia Los Paraísos
37320 León, Gto.
Phone: +52 (477) 214 1400, Fax: +52 (477) 214 1405

Mazatlán

Avenida Camarón Sábalo 133, Fraccionamiento Lomas de Mazatlán
82110 Mazatlán, Sin.
Phone: +52 (669) 989 2100, Fax: +52 (669) 989 2120

Mexicali

Calzada Justo Sierra 1101-A, Fraccionamiento Los Pinos
21230 Mexicali, B.C.
Phone: +52 (686) 905 5200, Fax: +52 (686) 905 5231

México, D.F.

Paseo de la Reforma 505, piso 28, Colonia Cuauhtémoc
06500 México, D.F.
Phone: +52 (55) 5080 6000, Fax: +52 (55) 5080 6001

Monclova

San Buenaventura 505, Colonia Los Pinos
25720 Monclova, Coah.
Phone: +52 (866) 635 0075, Fax: +52 (866) 635 1761

Monterrey

Lázaro Cárdenas 2321 Poniente, PB, Residencial San Agustín
66260 Garza García, N.L.
Phone: +52 (81) 8133 7300, Fax: +52 (81) 8133 7383

Nogales

Apartado Postal 384-2, Sucursal de Correos "A"
84081 Nogales, Son.
Phone: +52 (631) 320 1673, Fax: +52 (631) 320 1673

Puebla

Edificio Deloitte, vía Atlíxcayotl 5506, piso 5, Zona Angelópolis
72190 Puebla, Pue.
Phone: +52 (222) 303 1000, Fax: +52 (222) 303 1001

Querétaro

Avenida Tecnológico 100-901, Colonia San Ángel
76030 Querétaro, Qro.
Phone: +52 (442) 238 2900, Fax: +52 (442) 238 2975, 238 2968

Reynosa

Carr. Monterrey-Reynosa 210-B, PA, Fracc. Portal San Miguel
88730 Reynosa, Tamps.
Phone: +52 (899) 921 2460, Fax: +52 (899) 921 2462

San Luis Potosí

Carranza 2076-22, piso 2, Colonia Polanco
78220 San Luis Potosí, S.L.P.
Phone: +52 (444) 811 8889, Fax: +52 (444) 811 8922

Tijuana

Agua Caliente 4558, piso 1, Colonia Aviación
22420 Tijuana, B.C.
Phone: +52 (664) 622 7878, Fax: +52 (664) 681 7813

Torreón

Independencia 1819-B Oriente, Colonia San Isidro
27100 Torreón, Coah.
Phone: +52 (871) 747 4400, Fax: +52 (871) 747 4409

www.deloitte.com/mx

This publication contains general information only and Deloitte is not, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional advisor. Deloitte shall not be responsible for any loss sustained by any person who relies on this publication.

About Deloitte

Deloitte refers to one or more of Deloitte Touche Tohmatsu, a Swiss Verein, and its network of member firms, each of which is a legally separate and independent entity. Please see www.deloitte.com/about for a detailed description of the legal structure of Deloitte Touche Tohmatsu and its member firms. Please see www.deloitte.com/us/about for a detailed description of the legal structure of Deloitte LLP and its subsidiaries.