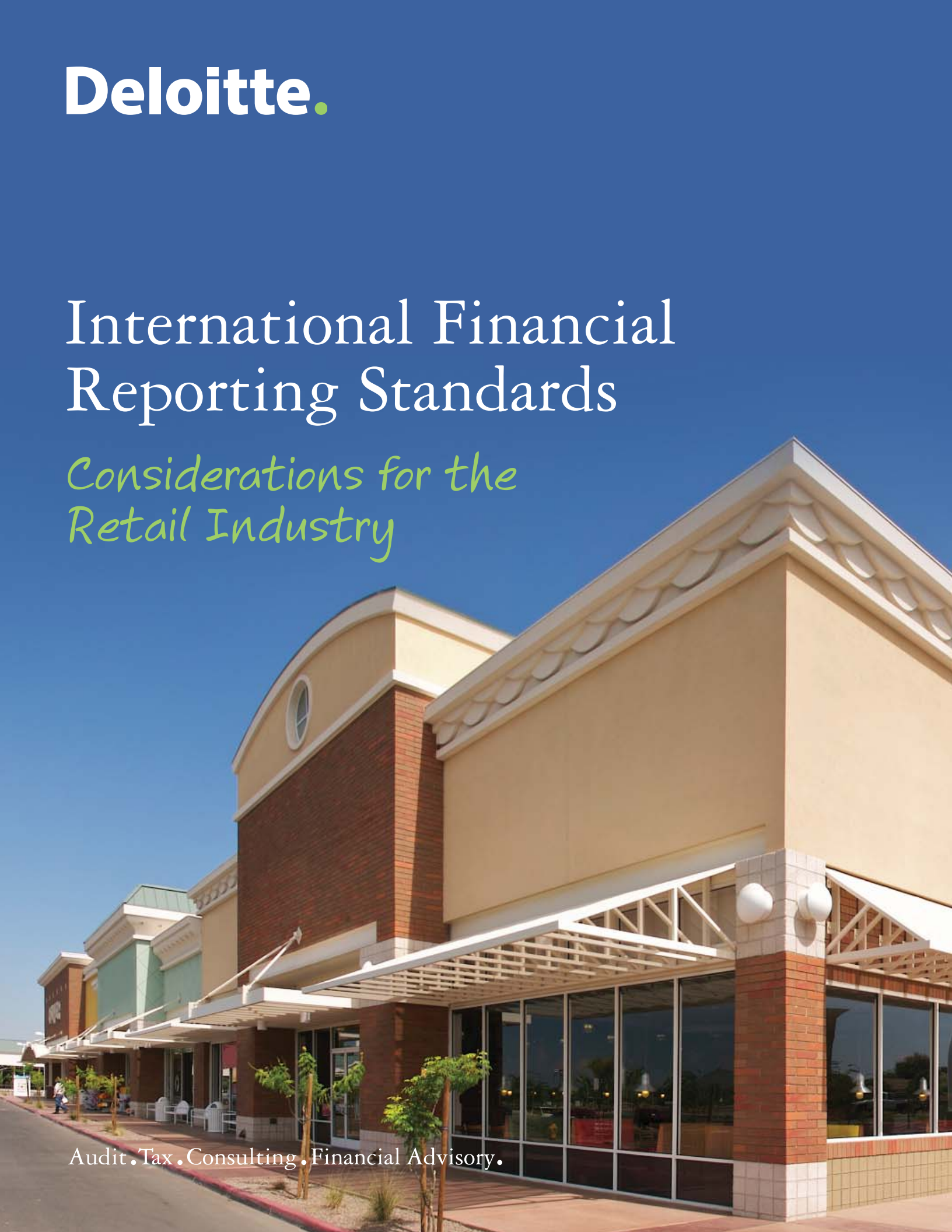


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# International Financial Reporting Standards

*Considerations for the  
Retail Industry*

Audit . Tax . Consulting . Financial Advisory .



# Table of Contents

- Key Differences between U.S. GAAP and IFRS for Retail Companies ..... 3**
  - Inventories..... 3
  - Leases..... 4
  - Impairment of Long-Lived and Indefinite-Lived Assets..... 4
  - Property, Plant and Equipment..... 6
  - Additional Technical Accounting Differences..... 7
- What Now?..... 8**

# International Financial Reporting Standards

## Considerations for the Retail 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.

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:

### Retail Competitive Landscape

Company	U.S. GAAP	IFRS	International Operations	Revenue* (Billions)
Ahold		x	x	\$42
Best Buy	x		x	\$40
Carrefour		x	x	\$125
Casino		x	x	\$38
Costco	x		x	\$66
CVS Caremark	x			\$76
Home Depot	x		x	\$77
J.C. Penney	x			\$20
Kingfisher		x	x	\$19
Kroger	x			\$70
Liberty Media		x	x	\$9
Lowe's	x		x	\$48
Macy's	x			\$26
Office Depot	x		x	\$15
PPR		x	x	\$30
Sears Holdings	x		x	\$51
Supervalu	x			\$34
Target	x			\$63
Tesco		x	x	\$95
Walgreen	x			\$55
Wal-Mart	x		x	\$379

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

- 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](http://www.deloitte.com/us/ifrs).

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 retailers 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 income tax planning.

In our *2008 Global Powers of Retailing* report, we noted that slow growth in many mature markets and not-to-be-missed-opportunities in emerging markets, particularly China, India and Russia, are powerful driving forces of globalization in the retail world today. While U.S. retailers are among the least likely right now to have foreign operations compared to retailers based in other countries, globalization is slowly accelerating. The U.S. retailers included in the top 250 retailers in the world (based on revenues) operate in an average of 3.7 countries, up from an average of only two countries 10 years ago. This increasing global diversification in retail creates yet another reason for U.S. companies to understand the benefits of a level financial reporting playing field.

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.

### Key Impacts of IFRS Implementation

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

One significant challenge is a shift in how accounting policies are developed, written and applied. Since IFRS focuses much 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 publication is to provide insight on the potential impact to retailers 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. Note 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 retail 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 Retail 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 retailers are discussed below, along with their associated impact on tax, processes and systems.

## Inventories: International Accounting Standard (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. Therefore, retailers may not be able to use the retail method of accounting to compute cost in one operating segment and the weighted average method in another.

## 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, retailers 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 retailers, 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 retailer'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 so that the new carrying amount is the lower of the cost or the revised net realizable value (i.e. the reversal is limited to the amount of the original write-down). 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"> <li>• LIFO prohibited</li> <li>• Consistency of accounting method</li> <li>• Measure at cost or NRV</li> <li>• Use slightly different valuation method</li> <li>• Reversal of impairment</li> </ul>	<ul style="list-style-type: none"> <li>• Valuation of inventory</li> <li>• Impairment charges</li> </ul>	<ul style="list-style-type: none"> <li>• Inventory system changes</li> <li>• Processes around reversal of inventory impairment</li> </ul>	<ul style="list-style-type: none"> <li>• Potential significant cost if LIFO is eliminated</li> <li>• Impact from change in valuation</li> </ul>

## Leases: IAS 17 & International Financial Reporting Interpretation Committee (IFRIC) 4

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). Intangible assets are within the scope of IAS 17 if rights are established 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 — 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 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 if certain criteria are met. 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, is allocated between the land and building elements in proportion to their relative fair values at the inception of the lease.

### 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 U.S. GAAP, a gain or loss on a sale-leaseback transaction is deferred and amortized over the lease term with limited exceptions regardless of the leaseback classification (seller retains less than substantially all of the use of the leased asset). 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. A gain or loss on a finance lease is deferred and amortized over the lease term. A gain or loss on an operating lease is recorded immediately if the sales price is established at fair value. Otherwise, it should be deferred and amortized over the lease term.

### Summary of Impact on Leases

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

## Impairment of Long-Lived and Indefinite-Lived Assets: IAS 36

The indicators, timing and levels for long-lived and indefinite-lived asset impairment testing are similar under IFRS and U.S. GAAP.

Goodwill and other indefinite-lived intangibles are tested for impairment at least annually, or more frequently 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 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.

## Method

Long-lived asset impairment is a one-step approach under IFRS and is assessed on the basis of recoverable amount, which is calculated as either fair value less costs to sell or value in use (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 calculating if the total carrying value of the reporting unit exceeds fair value. If no impairment exists, skip step 2.	Compare undiscounted cash flows to carrying amount of the asset group to determine if impairment exists.	Calculate impairment charge by comparing the carrying value to the recoverable amount (as defined above). Any excess in carrying value results in impairment charge in the amount of excess.
Step 2	Calculate and assign fair value of all other recognized and unrecognized assets and liabilities of reporting unit, remaining amount equals implied goodwill. Impairment loss is measured as the difference between the carrying amount and implied fair value of goodwill.	The carrying amount of the asset is reduced to its estimated fair value based on quoted market prices or other valuation techniques.	Not applicable.

Under IFRS, impairment charges will likely occur sooner than under U.S. GAAP. For example, assume a store's undiscounted cash flow exceeds the asset carrying amount but value in use (i.e., based on discounted cash flows) is less than the asset carrying amount. 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.

## Reversal of Impairment Charge

Except for goodwill, IFRS allows the reversal of impairment losses if the recoverable amount of an asset has increased since the impairment loss 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. However, the reversal should not exceed the carrying amount of the asset that would have existed if no impairment loss had been recognized (i.e., the otherwise net carrying amount after regular depreciation and amortization expense is deducted). Impaired assets must be tracked at original value in order to calculate the amount of impairment reversal.

After the reversal of an impairment loss, the amortization amount for the asset should be determined on the basis of the new recorded value of the asset, its estimated residual value, and its remaining useful life.

Summary of Impact on Impairment of Long-lived and Indefinite-Lived Assets			
Key Accounting Differences	Potential Implications		
	Financial Statements	Process/Systems	Taxes/Other
<ul style="list-style-type: none"> <li>• Goodwill impairment performed at CGU level, could result in lower level</li> <li>• One-step impairment test</li> <li>• Differences in fair value calculation</li> <li>• Reversal of impairment loss is allowed, except goodwill</li> </ul>	<ul style="list-style-type: none"> <li>• Impairments may occur more frequently</li> <li>• Fluctuations between periods due to reversal of impairments</li> </ul>	<ul style="list-style-type: none"> <li>• Increased judgments around asset valuation and depreciation</li> <li>• Process around reversal of asset impairment and tracking impaired assets</li> <li>• Allocation of goodwill to CGU</li> </ul>	<ul style="list-style-type: none"> <li>• Tax considerations with fluctuation and reversal of impairment</li> <li>• Increased effort/resources</li> </ul>

## Property, Plant and Equipment: IAS 16

Under IFRS, and unlike U.S. GAAP, an entity may elect to value property, plant and equipment (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. Revaluation increases are credited to equity. Revaluation losses are charged first against any revaluation surplus in equity related to the specific asset, and any excess charged to income.

### Component Approach

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 retail store with different depreciation methods or rates might include the building, roof, flooring, furnishings and parking lot.

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.

### Summary of Impact on Property, Plant and Equipment

Key Accounting Differences	Potential Implications		
	Financial Statements	Process/Systems	Taxes/Other
<ul style="list-style-type: none"><li>• Revaluation method</li><li>• Component approach</li></ul>	<ul style="list-style-type: none"><li>• Asset measurement</li><li>• Depreciable amount and calculation of depreciation expense</li></ul>	<ul style="list-style-type: none"><li>• Data capture for first-time adoption of ongoing tracking and reporting requirements</li><li>• General ledger and sub-ledger enhancements</li><li>• Asset fair value and residual value evaluation</li></ul>	<ul style="list-style-type: none"><li>• Book/tax considerations related to depreciation</li><li>• Increased effort/resources</li></ul>



## Additional Technical Accounting Differences

Additional technical accounting differences of specific interest to retailers 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.
Customer Loyalty Programs	Under U.S. GAAP, there is no specific accounting guidance surrounding the accounting for customer loyalty programs. In fact, EITF 00-14, "Accounting for certain sales incentives" and EITF 00-22, "Revenue arrangements with multiple deliverables," specifically exclude this type of arrangement. As a result of the lack of specific guidance, practice may vary where some entities have elected to apply the multiple element approach while others have applied the accrual or incremental cost approach.  IFRIC 13, "Customer Loyalty Programs," provides guidance for when customers can redeem goods or services for free or at a discount. IFRIC 13 specifies that such awards are "multiple element revenue transactions" and the fair value of any consideration received or receivable should be allocated between the award credits granted and the other components of the transactions. This treatment applies irrespective of whether the entity supplies the awards or whether a third party supplies them.
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"> <li>• represents a separate major line of business or geographical area of operations, or</li> <li>• is part of a single coordinated plan to dispose of a separate major line of business or geographical area of operations, or</li> <li>• is a subsidiary acquired exclusively with a view to resale.</li> </ul> <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: 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.
Store Closings / Restructurings	Under U.S. GAAP, the present value of costs associated with location closings (primarily future lease obligations) are charged to earnings when a location is vacated.  Under IFRS, costs related to a lease contract for which the entity will remain obligated over the remaining term, without economic benefit may be recognized earlier than when the location is vacated.

## Additional Tax Considerations

In addition to the potential impact from changes in technical accounting, key tax considerations for adoption of IFRS include: 1) financial accounting for income taxes - converting from FAS 109 to IAS 12; 2) tax compliance processes; 3) tax accounting methods; and 4) 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 no significant areas that specifically impact the retail industry.

Whether it is income, sales, property, business, value added or other taxes, retail companies are familiar with the tax compliance obligations of operating in numerous jurisdictions. With respect to income taxes, because taxable income in most jurisdictions is based on financial statement earnings, the underlying methodology to determine taxable income will change. 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 a retailer's franchisee operations be included within the financial statements. 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 enterprise resource planning (ERP) and reporting systems to provide data tailored to tax reporting requirements. Current systems may need to be recalibrated under IFRS as a result.

- 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. 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.

### Regulatory Impact

The transition of accounting standards raises questions about how U.S. regulators will operate under an IFRS framework.

The SEC's Division of Corporation Finance is responsible for reviewing all company filings, including those of foreign private issuers. Over the past two years, the SEC staff has reviewed more than 100 filings containing IFRS financial statements of foreign private issuers. Like domestic issuers, foreign private issuers have received various comments requesting additional information about the accounting treatment underlying items in the financial statements and the related disclosures made. In certain cases, the SEC staff has suggested that issuers enhance the disclosures made in filings on a future-filing basis (i.e., make changes in subsequent filings). In a few cases, the staff has requested that issuers revise current filings (i.e., a restatement).

To help financial statement preparers understand the items that the SEC staff has focused on during the review process over the past two years, please refer to the Deloitte publication "SEC Comment Letters on Foreign Private Issuers Using IFRS" found at [www.deloitte.com/us/IFRS/Library](http://www.deloitte.com/us/IFRS/Library). The document provides an overall analysis of the comments made, including the nature and types of comments issued. Also included are extracts from actual comment letters accompanied by an analysis of the topic involved and forward-looking considerations.

Overall, the SEC staff reviewed more than 100 filings of foreign private issuers and had an average of 19 comments per filing. In the comment letters Deloitte reviewed, we noted several themes:

- Presentation and disclosure were significant areas of focus across industries.
- Recognition and measurement comments varied by industry.
- There was a particular interest in "converged" standards.
- Comments were geared toward understanding the judgments made and assumptions used in applying IFRS.

### What Now?

#### Two Approaches

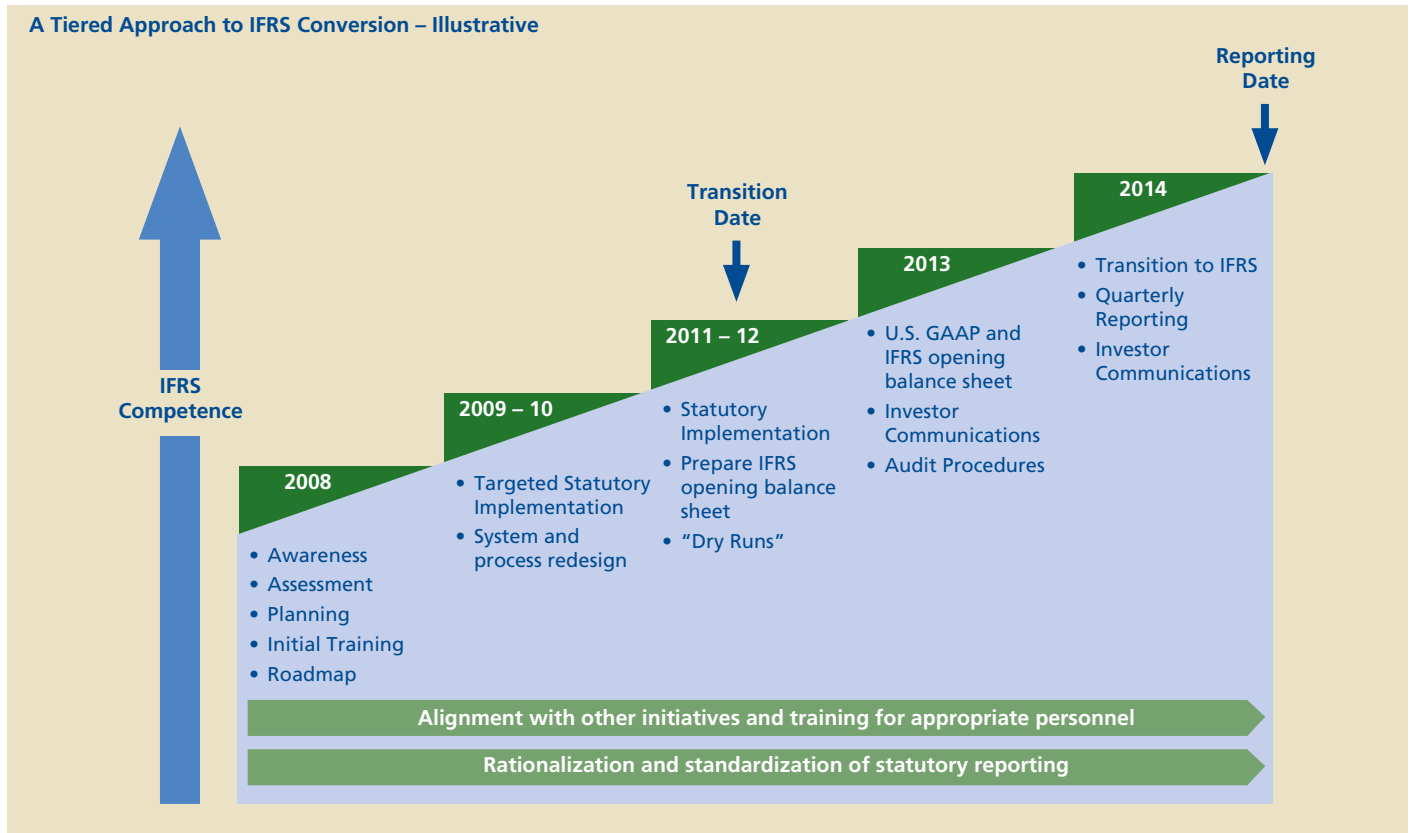
Generally speaking, two approaches to IFRS conversion predominate: all-in and tiered. The former is characterized by a relatively short timeframe, simultaneous conversion of all reporting entities, dedicated project teams, and devotion of significant resources. The latter is conducted over a more extended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

To draw historical parallels, compliance with the Sarbanes-Oxley Act may be considered, at least for accelerated filers, as an all-in approach. In contrast, a major project such as transition to a shared services model is often handled in a tiered fashion.

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 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.

Deloitte strongly recommends a tiered approach – staged, rational, and measured – to IFRS conversion. This advice 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 almost immediately.

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 entitled, "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.



### The Roadmap

Whether you plan to charge full-steam ahead or take small, measured steps, Deloitte recommends that you develop an IFRS implementation roadmap without delay. Through this effort, you’ll be able to chart the optimal course, determine the pace of your journey, and skirt any detours and potholes.

To start, collect answers to a few preliminary questions:

- 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?
- Do we have a major ERP or finance transformation project in the works?
- Are we involved in or considering a major acquisition?

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 should 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 the rushed approach (and unnecessary expense) that characterized such initiatives as the Sarbanes-Oxley Act and the Year 2000 problem. A carefully designed roadmap will empower your company to convert on its own terms. By taking a measured and informed approach, you will be able to identify 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

### International Accounting Resources

The International Accounting Standards Board (IASB) develops international financial reporting standards for general purpose financial statements. Visit the IFRS section of [www.iasb.org](http://www.iasb.org) for additional details and copies of the standards.

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