

IFRS Briefing Sheet

IFRSs and the E.U. endorsement process: a status report

November 2005, **Issue 37**

This *IFRS Briefing Sheet* considers the status of the European Union's (E.U.) endorsement of International Financial Reporting Standards (IFRSs).

Background – The IAS Regulation

The IAS Regulation (EC 2002/1606) requires an E.U. company listed on an E.U. regulated market to comply with **international accounting standards adopted for use in the E.U.**

Accordingly, a standard (or interpretation) issued by the International Accounting Standards Board (IASB) must be *adopted* into E.U. law *before* its use becomes mandatory under the IAS Regulation. The adoption process is sometimes referred to as 'endorsement'.

The European Commission (E.C.) adopts an individual standard or interpretation, provided that it meets the criteria for endorsement set out in the IAS Regulation and subject to a certain level of support from member states of the E.U. A summary of the endorsement process is included in Appendix A.

Which Standards have been Endorsed?

As of 25 November 2005, all documents issued by the IASB have been endorsed except for the following:

- Amendments to IAS 39 *Financial Instruments: Recognition and Measurement* – Cash Flow Hedge accounting for forecast intragroup transactions (April 2005)
- Amendment to IFRS 6 *Exploration for and Evaluation of Mineral Resources* and IFRS 1 *First-time Adoption of IFRSs* (June 2005)
- IFRS 7 *Financial Instruments: Disclosures* (August 2005)
- IAS 1 *Presentation of Financial Statements* – Capital disclosures (August 2005)
- Amendments to IAS 39 *Financial Instruments: Recognition and Measurement* and IFRS 4 *Insurance contracts* – Financial Guarantee Contracts (August 2005)
- IFRIC 6 *Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment* (September 2005)
- IFRIC 7 *Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies* (November 2005).

See Appendix A for details of the endorsement status of each standard and interpretation.

A supplement to KPMG's publication IFRS in Brief

IAS 39 initially was adopted for use in the E.U. with amendments to the original IASB version of the standard that:

- removed the fair value option to designate liabilities as measured at fair value
- amended the interest rate hedge accounting requirements so that certain elements no longer are compulsory.

This amended version often is referred to as the 'carve-out' version of IAS 39.

As part of the E.C.'s adoption on 15 November 2005 of Amendments to IAS 39 *Financial Instruments: Recognition and Measurement* – The Fair Value option (June 2005), the E.C. has reinserted into the E.U. adopted version of IAS 39 the parts of IAS 39 that deal with the fair value option.

However, the E.C. has not announced any plans to reinsert into the E.U. adopted version of IAS 39 the interest rate hedge accounting requirements.

Timetable for Endorsement

At a minimum, endorsement of a new IFRS takes about six months to complete. However, the timetable is subject to great uncertainty, in part because each standard or interpretation must be available in all of the E.U.'s official languages before it can be endorsed. In practice, endorsement can take much longer than six months.

Unfortunately, it is probable that the completion of the endorsement process for the remainder of the standards and interpretations will not occur until 2006. In the case of the most recent standards (e.g., IFRS 7) it is possible that the process may not be completed before April / May 2006.

Consequences of non-endorsement

An E.U. company may prefer to apply one or more of these standards and interpretations in its first IFRS annual financial statements.

Endorsement only after the Balance Sheet Date

In our view, there is no requirement that the completion of the endorsement process must occur prior to the balance sheet (i.e., reporting) date. Instead a standard or interpretation that is not mandatory for a particular annual period may be applied voluntarily if the endorsement process is completed before the annual financial statements are authorised for issue, assuming that the standard or interpretation itself permits early adoption.

Non-endorsed Standards

What if a standard or interpretation remains unendorsed at the date of authorisation for issue of the financial statements? It is clear that the requirements of such a standard are not mandatory, but can an entity apply an unendorsed standard or interpretation voluntarily?

In our view, an entity may comply additionally with the requirements of an unendorsed standard or interpretation to the extent that those requirements are consistent with endorsed IFRSs.

In practice, an unendorsed interpretation generally will be of endorsed standards. This means that an entity will be able to use the guidance in the unendorsed interpretation in determining an accounting policy for the relevant transaction that is consistent with standards that have been endorsed.

The presentation and disclosure requirements of a standard that has

not yet completed the endorsement process generally may be applied as the disclosures can be presented in addition to the requirements of endorsed standards. However, such dual compliance may be burdensome. For example, the disclosures set out in IFRS 7 (if unendorsed) could be presented, but the company will still need to comply with the disclosure requirements of all endorsed standards, including IAS 30 and IAS 32.

The recognition and measurement requirements of a standard that has not yet completed the endorsement process requires careful consideration. They may be applied by a company only if consistent with the recognition and measurement requirements of endorsed standards, with which the company must comply.

One specific issue for the adoption of recognition and measurement guidance in IFRSs that are not yet endorsed is transitional relief. The endorsed version of IFRS 1 contains all transitional requirements and relief for a first-time adopter of endorsed IFRSs. Any transitional relief added to endorsed IFRS 1 by an unendorsed standard or interpretation is unavailable to a first-time adopter. This is because the company must comply with the endorsed version of IFRS 1.

E.U. Accounting Framework

The legal requirement in the E.U. is the application of international accounting standards adopted for use in the E.U., not IFRSs as issued by the IASB.

The Fédération des Experts-Comptables Européens (FEE) has urged the E.C. to issue authoritative guidance on how companies in the E.U. should refer to their legal financial reporting framework.

FEE recommends that the E.U. framework should be described as: **International Financial Reporting Standards (IFRSs) as adopted for use in the E.U.**

The same description of the framework should be used in the accounting policy disclosures in the notes to the financial statements and in the report of the auditor.

In our view, this short reference should be explained in the notes to the financial statements as being IFRSs as adopted for use in the E.U. "... further to the IAS Regulation (EC 1606/2002)."

FEE concludes that an E.U. company always should include a statement of compliance with the legally required framework.

FEE encourages companies to provide an explanation in the notes to the

financial statements as to how their accounting policies depart from IFRS as issued by the IASB. These disclosures are meant to enhance comparability of European companies with companies listed outside of the E.U.

When a company voluntarily complies with IFRSs as issued by the IASB, in addition to the endorsed standards, the description of the accounting framework should state separately compliance with the legal requirement and compliance with IFRSs as issued by the IASB.

Other Practical Issues

For a discussion of some of the practical issues of the application of IFRSs as adopted for use in the E.U., please refer to IFRS Briefing Sheet – issue 18, "IFRSs and the E.U. endorsement process: a status report."

U.S. Securities and Exchange Commission (SEC) Relief for a First-time Adopter

Finally, a reminder that the SEC has granted exemptions to certain non-U.S. companies registered with the SEC. The exemptions are applicable to a first-time adopter of either IFRSs as published by the IASB or IFRSs as adopted for use in the E.U. (see IFRS Briefing Sheet – issue 22, "Publication of U.S. Securities and Exchange Commission's (SEC's) Final Rule for First-time Adopters of IFRSs)."

If you would like further information on any of the matters discussed in this issue of *IFRS Briefing Sheet*, please talk to your usual local KPMG contact or call any of KPMG firms' offices.

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Appendix A

The European Union (E.U.) Endorsement Process

The **IAS Regulation** empowers the European Commission (E.C.) to adopt implementing measures necessary to meet the objectives set out in that legislation. The IAS Regulation defines the nature of the implementing measures and the criteria for their acceptability (see below).

Implementing measures are adopted as E.C. Regulations and contain as appendices the text of the relevant standard or interpretation.

The criteria for the adoption of a standard or interpretation are that it:

- is not contrary to the 'true and fair' principle set out in the E.U. Accounting Directives
- is conducive to the European public good

- meets the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management.

The E.C. decides whether these criteria are met, based in part on technical advice provided to it by the European Financial Reporting Advisory Group (EFRAG).

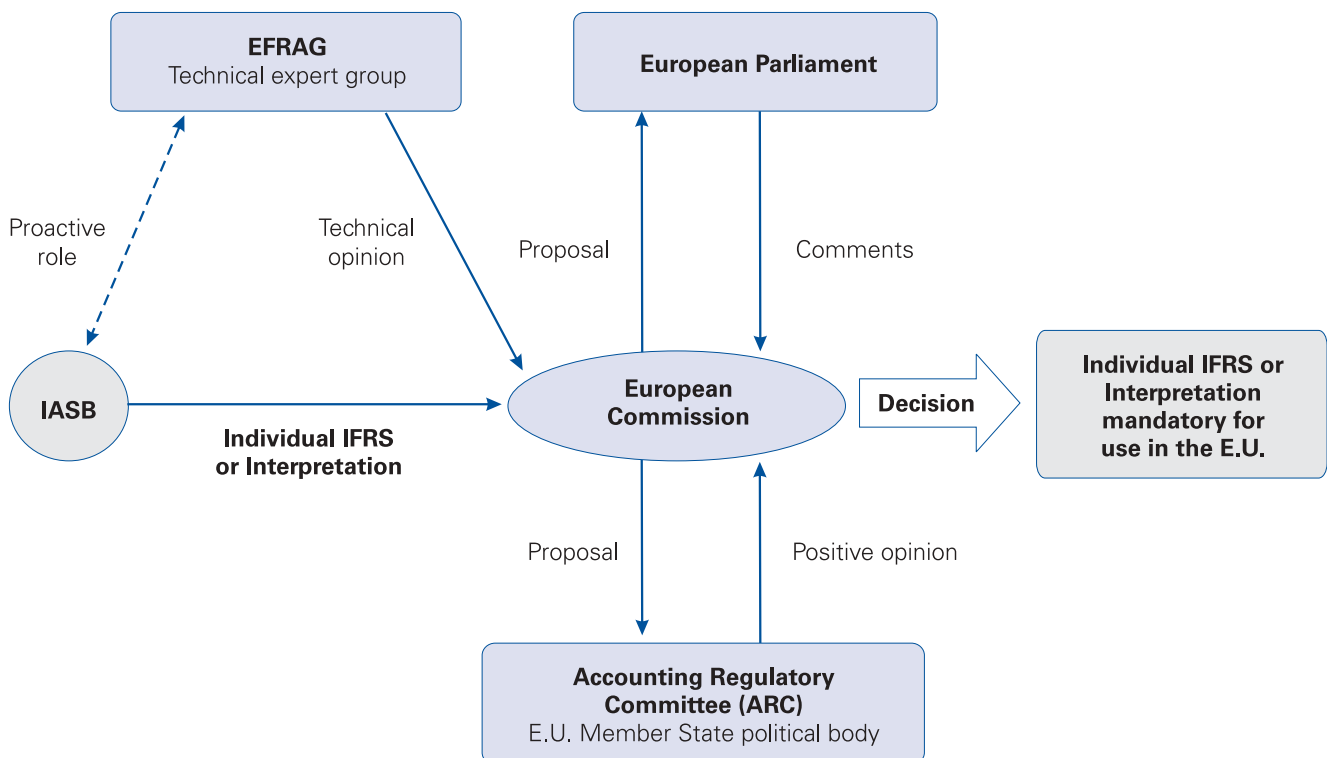
The E.C. can adopt an implementing measure only if it has the support of a regulatory committee, the ARC, set up for the purpose.

The ARC contains representatives of the E.U. member states. Each member state has a different number of votes and voting requires a qualified majority. As a result a small

number of large countries can establish a blocking minority. If the ARC fails to support the E.C.'s decision, then the Commission can ask the full European Council (composed of government ministers from the member states) to do so. Proposals for implementing measures also are delivered to the European Parliament for its comments.

Adopted standards and interpretations become part of European Community law and are published in the *Official Journal of the European Communities* and translated into all of the E.U.'s official languages. E.C. Regulations adopting standards can be accessed via the E.C. Web site at www.europa.eu.int/comm/internal_market/accounting/ias_en.htm#2002_1606.

E.U. Endorsement Process Illustrated



Source: KPMG IFRG Limited

Status of Endorsement of IFRSs by the E.U. at 25 November 2005¹

	Issued / Revised / Amended (Effective Date) ²	Endorsement Status	Date	Commission Regulation
IAS 1 <i>Presentation of Financial Statements</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004
Amendment to IAS 1 Capital Disclosures	August 2005 (Effective 1 January 2007)	Awaiting endorsement decision (Supported by EFRAG) ³		
IAS 2 <i>Inventories</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004
IAS 7 <i>Cash Flow Statements</i>	December 1992	Endorsed	29 September 2003	(EC) 1725/2003
IAS 8 <i>Accounting Policies, Changes in Accounting Estimates and Errors</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004
IAS 10 <i>Events after the Balance Sheet Date</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004
IAS 11 <i>Construction Contracts</i>	December 1993	Endorsed	29 September 2003	(EC) 1725/2003
IAS 12 <i>Income Taxes</i>	November 2000	Endorsed	29 September 2003	(EC) 1725/2003
IAS 14 <i>Segment Reporting</i>	August 1997	Endorsed	29 September 2003	(EC) 1725/2003
IAS 16 <i>Property, Plant and Equipment</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004
IAS 17 <i>Leases</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004
IAS 18 <i>Revenue</i>	December 1993	Endorsed	29 September 2003	(EC) 1725/2003
IAS 19 <i>Employee Benefits</i>	May 2002	Endorsed	29 September 2003	(EC) 1725/2003
Amendments to IAS 19 <i>Employee Benefits</i> – Actuarial Gains and Losses, Group Plans and Disclosures (including consequential amendments to IAS 1, IAS 24 and IFRS 1)	December 2004 (Mandatory requirements effective 1 January 2006)	Endorsed	8 November 2005	(EC) 1910/2005
IAS 20 <i>Accounting for Government Grants and Disclosure of Government Assistance</i>	1994	Endorsed	29 September 2003	(EC) 1725/2003
IAS 21 <i>The Effect of Changes in Foreign Exchange Rates</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004
IAS 23 <i>Borrowing Costs</i>	December 1993	Endorsed	29 September 2003	(EC) 1725/2003
IAS 24 <i>Related Party Disclosures</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004
IAS 26 <i>Accounting and Reporting by Retirement Benefit Plans</i>	1994	Endorsed	29 September 2003	(EC) 1725/2003
IAS 27 <i>Consolidated and Separate Financial Statements</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004
IAS 28 <i>Investments in Associates</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004

1. Does not include previous versions of standards and interpretations if they are superseded by new or revised versions that also have been adopted.

2. The date is not altered in case of subsequent consequential amendments.

3. Unless otherwise noted "Awaiting endorsement decision" means that EFRAG has not yet issued its endorsement advice to the E.C.

	Issued / Revised / Amended (Effective Date)	Endorsement Status	Date	Commission Regulation
IAS 29 <i>Financial Reporting in Hyperinflationary Economies</i>	1994	Endorsed	29 September 2003	(EC) 1725/2003
IAS 30 <i>Disclosures in the Financial Statements of Banks and Similar Financial Institutions</i>	1994	Endorsed	29 September 2003	(EC) 1725/2003
IAS 31 <i>Interests in Joint Ventures</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004
IAS 32 <i>Financial Instruments: Disclosure and Presentation</i>	December 2003	Endorsed	29 December 2004	(EC) 2237/2004
IAS 33 <i>Earnings per Share</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004
IAS 34 <i>Interim Financial Reporting</i>	February 1998	Endorsed	29 September 2003	(EC) 1725/2003
IAS 36 <i>Impairment of Assets</i>	March 2004	Endorsed	29 December 2004	(EC) 2236/2004
IAS 37 <i>Provisions, Contingent Liabilities and Contingent Assets</i>	July 1998	Endorsed	29 September 2003	(EC) 1725/2003
IAS 38 <i>Intangible Assets</i>	March 2004	Endorsed	29 December 2004	(EC) 2236/2004
IAS 39 <i>Financial Instruments: Recognition and Measurement</i>	March 2004 (i.e., including Amendment on Fair Value Accounting for a Portfolio Hedge of Interest Rate Risk, issued in March 2004) ⁴	Endorsed	19 November 2004	(EC) 2086/2004
Amendments to IAS 39 <i>Financial Instruments: Recognition and Measurement</i> – Transition and Initial Recognition of Financial Assets and Financial Liabilities (including consequential amendments to IFRS 1)	December 2004	Endorsed	25 October 2005	(EC) 1751/2005
Amendments to IAS 39 <i>Financial Instruments: Recognition and Measurement</i> – Cash Flow Hedge Accounting of Forecast Intragroup Transactions	April 2005 (Effective 1 January 2006)	Awaiting endorsement decision (Supported by EFRAG)		
Amendments to IAS 39 <i>Financial Instruments: Recognition and Measurement</i> – The Fair Value Option (including consequential amendments to IAS 32 and IFRS 1)	June 2005 (Effective 1 January 2006)	Endorsed ⁵	15 November 2005	(EC) 1864/2005

⁴ The endorsed IAS 39 contains carve outs in the following paragraphs:

Standard: Paragraphs 9b, 35 and 81A

Application Guidance: 31, 99A, 99B, 107A, 114 (c) and (g), 118 (b), 119 (d), (c) and (f), 121, 122, 124 (a) and (d), 126, 127, 129 and 130.

⁵ As part of the endorsement of this amendment to IAS 39, the E.C. amended the endorsed version of IAS 39 to add those paragraphs relating to the fair value option that were “carved-out” of the version endorsed in EC 2086/2004 (see footnote 4 above).

	Issued / Revised / Amended (Effective Date)	Endorsement Status	Date	Commission Regulation
Amendments to IAS 39 and IFRS 4: <i>Financial Guarantee Contracts</i>	August 2005	Awaiting endorsement decision (Supported by EFRAG)		
IAS 40 <i>Investment Property</i>	December 2003	Endorsed	29 December 2004	(EC) 2238/2004
IAS 41 <i>Agriculture</i>	February 2001	Endorsed	29 September 2003	(EC) 1725/2003
IFRS 1 <i>First-time Adoption of International Financial Reporting Standards</i> (Applicability clarified in (EC) 2086/2004)	June 2003	Endorsed	6 April 2004	(EC) 707/2004
IFRS 2 <i>Share-based Payment</i> (including consequential amendments to IAS 12, IAS 16, IAS 19, IAS 32, IAS 33, IAS 38, IAS 39 and IFRS 1)	February 2004	Endorsed	4 February 2005	(EC) 211/2005
IFRS 3 <i>Business Combinations</i>	March 2004	Endorsed	29 December 2004	(EC) 2236/2004
IFRS 4 <i>Insurance Contracts</i>	March 2004	Endorsed	29 December 2004	(EC) 2236/2004
IFRS 5 <i>Non-current Assets Held for Sale and Discontinued Operations</i>	March 2004	Endorsed	29 December 2004	(EC) 2236/2004
IFRS 6 <i>Exploration for and Evaluation of Mineral Resources</i> (including consequential amendments to IFRS 1, IAS 16 and IAS 38)	December 2004 (Effective 1 January 2006)	Endorsed	8 November 2005	(EC) 1910/2005
Amendment to IFRS 6 <i>Exploration for and Evaluation of Mineral Resources</i> and IFRS 1 <i>First-time Adoption of International Financial Reporting Standards</i>	June 2005 (Effective 1 January 2006)	Awaiting endorsement decision		
IFRS 7 <i>Financial Instruments: Disclosures</i>	August 2005 (Effective 1 January 2007)	Awaiting endorsement decision (Supported by EFRAG)		
SIC-7 <i>Introduction of the Euro</i>	October 1997	Endorsed	29 September 2003	(EC) 1725/2003
SIC-10 <i>Government Assistance – No Specific Relation to Operating Activities</i>	January 1998	Endorsed	29 September 2003	(EC) 1725/2003
SIC-12 <i>Consolidation – Special Purpose Entities</i>	June 1998	Endorsed	29 September 2003	(EC) 1725/2003
Amendments to the scope of SIC-12 <i>Consolidation – Special Purpose Entities</i>	November 2004	Endorsed	25 October 2005	(EC) 1751/2005

	Issued / Revised / Amended (Effective Date)	Endorsement Status	Date	Commission Regulation
SIC-13 <i>Jointly Controlled Entities – Non-Monetary Contributions by Venturers</i>	June 1998	Endorsed	29 September 2003	(EC) 1725/2003
SIC-15 <i>Operating Leases – Incentives</i>	June 1998	Endorsed	29 September 2003	(EC) 1725/2003
SIC-21 <i>Income Taxes – Recovery of Revalued Non-Depreciable Assets</i>	July 2000	Endorsed	29 September 2003	(EC) 1725/2003
SIC-25 <i>Income Taxes – Changes in the Tax Status of an Entity or its Shareholders</i>	July 2000	Endorsed	29 September 2003	(EC) 1725/2003
SIC-27 <i>Evaluating the Substance of Transactions Involving the Legal Form of a Lease</i>	December 2001	Endorsed	29 September 2003	(EC) 1725/2003
SIC-29 <i>Disclosure – Service Concession Arrangements</i>	December 2001	Endorsed	29 September 2003	(EC) 1725/2003
SIC-31 <i>Revenue – Barter Transactions Involving Advertising Services</i>	December 2001	Endorsed	29 September 2003	(EC) 1725/2003
SIC-32 <i>Intangible Assets – Web Site Costs</i>	March 2002	Endorsed	29 September 2003	(EC) 1725/2003
IFRIC 1 <i>Changes in Existing Decommissioning, Restoration and Similar Liabilities</i>	May 2004	Endorsed	29 December 2004	(EC) 2237/2004
IFRIC 2 <i>Members' Shares in Co-operative Entities and Similar Instruments</i>	November 2004	Endorsed	7 July 2005	(EC) 1073/2005
IFRIC 3 <i>Emission Rights</i> WITHDRAWN BY IASB (June 2005)	December 2004	NOT APPLICABLE		
IFRIC 4 <i>Determining whether an Arrangement Contains a Lease</i> (including consequential amendments to IFRS 1)	December 2004 (Effective 1 January 2006)	Endorsed	8 November 2005	(EC) 1910/2005
IFRIC 5 <i>Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds</i> (including consequential amendments to IAS 39)	December 2004 (Effective 1 January 2006)	Endorsed	8 November 2005	(EC) 1910/2005
IFRIC 6 <i>Liabilities arising from Participating in a Specific Market-Waste Electrical and Electronic Equipment</i>	September 2005 (Effective 1 December 2005)	Awaiting endorsement decision (Supported by EFRAG)		
IFRIC 7 <i>Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies</i>	November 2005 (Effective 1 March 2006)	Awaiting endorsement decision		