

# ***Major Changes in IFRS and Comparison with US GAAP***

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**Abstract:** The evolution of International Financial Reporting Standards (IFRS) reflects the needs of the global business environment and the pursuit of higher quality financial reporting. This paper discusses and explores major changes implemented in IFRS, specifically in the areas of revenue recognition, lease accounting, and the treatment of intangible assets. The shortcomings of the past application of IFRS standards in these aspects are presented in this paper, as well as changes and benefits after IFRS made corresponding modifications. By reviewing materials and literature, the study conducts a comparison between IFRS and the United States Generally Accepted Accounting Principles (US GAAP). These two major accounting frameworks have adopted unique methods and standards. Still, both the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) work hard together to realize international harmonization. The outcomes of this research make it clear that ongoing refinements to IFRS have significantly improved the clarity, consistency, and comparability in how financial activities are reported. Such changes have been pivotal in diminishing uncertainties and bolstering the trustworthiness of financial disclosures. Being influenced by the continuous developments in IFRS, greater transparency and accountability in financial reporting will be achieved. This has made a great contribution to helping investors in sound economic decision-making and enhancing investor confidence.

**Keywords:** Accounting Principles, Revenue Recognition, Lease, Intangibles

## **1. Introduction**

Consistency and transparency are essential in the intricate web of global finance and commerce. The International Financial Reporting Standards emerged as a beacon of standardization, propelling international business dealings into an era of clearer communication, reduced ambiguities, and enhanced accountability. Over the decades, cross-border trade and investment have grown exponentially. At this time, the preparation of financial statements is more important than ever at this time. Multinational corporations often have to prepare different sets of financial statements for different jurisdictions, which is a laborious and complex task. These variances in financial reporting hindered investors and other stakeholders from making informed decisions due to the inconsistencies and disparities in data presentation. Therefore, IFRS is important to act as standards and framework under which these financial statements are prepared. Governed by the International Accounting Standards Board, IFRS has emerged as a globally recognized framework. By applying IFRS, cross-country comparability increases, enabling smoother monitoring and benchmarking across organizations [1]. IFRS also improves the transparency of corporate financial reporting. Companies

are mandated to prepare financial statements in accordance with IFRS standards and requirements. This set of requirements allows stakeholders to understand more disclosure of the company's details. The need for IFRS in financial reporting was driven by the need to bridge gaps, create standardized systems, and foster an environment where transparency, clarity, and trust flourish. It paves the way for a more interconnected and efficient global financial landscape.

Amidst the global financial landscape, two predominant frameworks govern financial reporting—the International Financial Reporting Standards and the United States Generally Accepted Accounting Principles. For a comprehensive understanding of international financial reporting subtleties, examining both IFRS and US GAAP is indispensable. The Financial Accounting Standards Board manages US GAAP, which has anchored U.S. financial statements for years using a 'rules-based' system. Meanwhile, IFRS, directed by the International Accounting Standards Board, employs a 'principles-based' method. The enduring application of US GAAP reveals the profound impact of regional economic, cultural, and regulatory elements in the financial narrative. While some contend that US GAAP's explicit framework brings about transparency, diminishing vagueness in fiscal reports, there are voices that champion the adaptability inherent in IFRS, deeming it more aligned with the fluidity of the global trade arena. Acknowledging the strengths of both paradigms and the value of synergy, the FASB and IASB have, over periods, engaged in tandem to lessen the chasm between the two, aiming to minimize differences and make financial statements more comparable across the globe [2].

After delving into the origins and import of IFRS and juxtaposing it with US GAAP, it's imperative to understand the evolution of these standards. With the ever-shifting global business terrain, IFRS has continually adapted with modifications and updates to address burgeoning financial intricacies. Concurrently, the indelible imprint of US GAAP on international financial reporting warrants attention. Although they originate from diverse antecedents and adopt disparate methodologies, their symbiosis in the contemporary global economic fabric remains a salient discourse. The ensuing sections of this paper will shed light on the transformations in IFRS policies over time, especially in areas such as revenue recognition, leases, and intangibles. A subsequent juxtaposition with US GAAP will highlight disparities, similarities, and potential points of convergence, revealing the expansive implications for international financial reporting, along with its associated challenges and prospects.

## **2. Major Changes in IAS & IFRS**

### **2.1. Revenue Recognition**

Within the domain of financial documentation, understanding revenue recognition remains fundamental. Because it significantly reflects an organization's economic stability and performance. Historically, under the umbrella of International Accounting Standards, the principles guiding revenue recognition were dispersed across several standards and interpretations. Predominantly, IAS 18 "Revenue" and IAS 11 "Construction Contracts" acted as the guiding lights in this domain. Although these indicators were widely used, these standards posed several complexities.

A major concern was the inherent ambiguity in IAS 18, especially in its treatment of multiple-element arrangements. Due to the need for more clarity, different companies have different interpretations of the standard in IAS 18. It causes firms, even within analogous industries, to adopt disparate revenue recognition practices. Such discrepancies posed challenges in ensuring uniformity and hindered the comparability of financial statements across firms [3]. Considering this fragmented guidance, which encompassed a plethora of standards and diverse interpretations focused on revenue, the inherent intricacy of the domain was further intensified, invariably leading to a wide range of variations in both revenue recognition and the subsequent measurement methodologies [4].

The challenges posed by previous standards, combined with the necessities of a globalized business environment, made reforming these standards necessary. The outcome was the introduction of IFRS 15 "Revenue from Contracts with Customers" in 2014, a joint endeavor by the IASB and the US's FASB. This standard was a departure from the past since a comprehensive framework for revenue recognition was created. A flagship feature of IFRS 15 was its structured five-step model to determine the timing and amount of revenue to be recognized. This model provided entities with a systematic procedure, bringing in much-needed consistency across the board. Moreover, the standard delved deeper into the concept of performance obligations in contracts, elucidating the criteria for revenue recognition tied to each obligation, thus addressing previously grey areas. IFRS 15 also made another major advancement, introducing stricter disclosure obligations. Companies were now obliged to unveil comprehensive information regarding the nature, amount, timing, and uncertainties tied to revenue and the subsequent cash flows. Such transparency facilitated better stakeholder understanding and instilled greater confidence in financial statements. In addition, IFRS 15 provides a clear indication of the costs directly attributable to the contract. This standard for goods. This will ensure that the revenue recognition under this standard reflects the true nature of the transaction [5]. The transformative nature of IFRS 15 had a profound impact on businesses worldwide. This standard brings about a fundamental shift. Enterprises had moved from a risk and rewards model to a control-based model. The essence of this transition was to ensure that revenue is recognized when control of goods or services is transferred to the customer. As a result, this standard can more accurately reflect the underlying economic substance of transactions. However, there are still some challenges in the process of implementation of IFRS 15. Many companies need to conduct a complete review of existing systems, processes and internal controls to meet the new requirements. At the same time, they need to collect and analyze a lot of internal information.

The changing dynamics of business transactions and global financial reporting need a more comprehensive framework. IFRS 15 uses intricate guidelines and a forward-looking approach to bridge the gaps of the past and ensure a more transparent, consistent, and comparable revenue recognition landscape.

## 2.2. Lease

The legacy lease accounting standard, IAS 17, delineated leases into two categories: finance leases and operating leases. Finance leases, where the lessee effectively owned the asset, were recorded on the balance sheet, reflecting the asset's value and associated liability. In contrast, operating leases were not capitalized; lease payments were treated as an operating expense and the lease obligations were typically disclosed in the footnotes of financial statements. This dichotomy presented a significant loophole, allowing companies to structure leases in a manner that kept substantial liabilities off the balance sheet, thereby obscuring the true financial standing of the entity [6].

One weakness of IAS 17 is that it made a company's financial statements less transparent. This poses an obstacle for stakeholders trying to understand a company's financial health since financial reports present a one-sided perspective. Operating leases obscured a company's leverage. It potentially leads to underestimation of financial risks and overvaluation of the company. As a result, the financial risks of the company may be underestimated and there would be an overvaluation of the company. Analysts and investors often found themselves making adjustments to financial statements to estimate the impact of these hidden liabilities, causing inconsistencies and inefficiencies in financial analysis. As leasing occupies an increasingly important position in the company, the problems of leasing in different industries are becoming more and more prominent. Companies increasingly opted to lease, rather than purchase, assets for various strategic and financial reasons. This trend was especially prevalent in sectors like aviation, retail, and logistics, where the benefits of leasing—such as flexibility, access to newer assets, and off-balance-sheet financing—were

particularly compelling. As a result, the shortcomings of IAS 17 became more pronounced, and the call for change more urgent.

Recognizing these issues and challenges, the IASB undertook a fundamental reform of lease accounting, and IFRS 16 was introduced in 2016. By removing the operating lease classification for those holding leases, IFRS 16 mandates the recording of substantial lease obligations directly within the balance sheet, offering a more transparent view of a company's financial obligations [7]. As a result, lessees must now recognize both a right-of-use asset and a corresponding lease liability, ensuring that the financial statements more precisely mirror the true nature of leasing transactions.

Implementing IFRS 16 has indeed made a noticeable positive impact on how financial information is reported. Now, greater transparency in financial reporting provides stakeholders with a solid ground to stand on when evaluating a company's financial health, leading to smarter and more informed investment choices. Moreover, the standard has managed to even the playing field, minimizing the room for financial engineering regarding lease arrangements. By pulling lease obligations into the balance sheet, IFRS 16 ensures that a company's financial leverage is portrayed more accurately. This change is crucial as it improves the reliability of financial ratios and other metrics used by investors and analysts. Beyond just lifting the veil for clearer transparency and aligning standards for better comparability, IFRS 16 has brought a welcome breath of simplicity into the world of lease accounting. Its one-size-fits-all lessee accounting framework cuts through the tangle of complexity, ensuring a uniform application across diverse industries and jurisdictions. This change is an opportunity, especially for entities with extensive leasing activities, smoothing out their accounting journey and significantly dialing down the odds of mistakes creeping in.

Moving from IAS 17 to IFRS 16 signifies a crucial turning point in financial reporting, tackling the age-old complexities tied to lease accounting. IFRS 16 ensures every major lease obligation makes its way onto the balance sheet, offering a framework for lease accounting that's not just more transparent but also reliable and uniform across the board.

### 2.3. Intangibles

The value and contribution of intangible assets to contemporary businesses have been steadily increasing, and the domain of intangible assets under financial accounting has long been a subject of extensive debate. Historically, the accounting for intangible assets has been fraught with challenges. Because of the intangible nature of these assets and the difficulty in reliably measuring their fair value.

Before the substantial advancements in International Financial Reporting Standards, the methodologies applied in accounting intangible assets were frequently criticized due to their apparent lack of clarity and uniformity. Businesses were regularly seen capitalizing on intangible assets that lacked active markets, resulting in evaluations that could be deemed subjective or sometimes overly optimistic. These valuation challenges were starkly evident in sectors heavily reliant on intangible assets such as brand strength, patent portfolios, and intellectual property rights. The economic tumult of 2008 brought these practices into sharp relief, underscoring the hazardous nature of inflated asset valuations and marking them as a notable contributor to the financial instability.

In tackling these issues, the International Accounting Standards Board has put in considerable work to improve and sharpen the accounting rules associated with intangible assets. The substantial shift in intangible assets recognition has largely been driven by IFRS 3(Business Combinations) and IAS 38 (Intangible Assets), which offer more concrete directions for recognizing, measuring, and disclosing intangible assets. IFRS 3, for instance, introduced the concept of fair value measurement for acquired intangible assets, ensuring that such assets are recorded at a more objective and reliable value at the time of acquisition. IAS 38, on the other hand, delineates the criteria for recognizing internally generated intangible assets, aiming to ensure that only intangibles with probable future economic benefits and reliable measurement are capitalized [8].

These updated guidelines have profoundly influenced how intangible assets are reported, bringing about a noticeable enhancement in clarity and consistency. By establishing more dependable and objective ways to quantify the worth of intangibles, these standards have made it easier for investors to make sound financial decisions. Besides, the ramped-up requirements for sharing information mean that stakeholders now have a much clearer insight into the nature and value of a company's intangible assets, building a stronger foundation of trust and accountability in the financial data presented [9].

In conclusion, how intangible assets are accounted for under IFRS remains a topic that sparks extensive discussion and is still evolving. Adjustments and progress in IFRS pertaining to intangible assets have markedly tackled the long-existing complexities and hurdles related to these particular assets. The improved consistency, reliability, and transparency in financial reporting ensure stakeholders make more informed decisions and promote accountability and stewardship. As intangible assets continue to play an increasingly vital role in the value creation of companies, IASB needs to continue to refine the accounting standards to ensure that financial reporting evolves to meet the demands of the dynamic business environment.

### **3. Comparison with US GAAP**

#### **3.1. Overall Differences in the Framework**

IFRS and US GAAP are two of the most widely used accounting frameworks in the world. While both aiming to present transparent and dependable financial data to stakeholders, the methodologies, fundamental principles, and procedures they employ diverge substantially.

Taking a broad view, IFRS generally follows a more principles-based methodology, laying out wide-ranging principles aimed to cover a variety of transactions and industry scenarios. The focus is on the economic substance of the transactions rather than the legal form. This approach encourages adaptability, yet it might introduce a level of subjectivity, requiring more judgment and interpretation from the accountants and auditors at play. This could bring about a lack of uniformity and a certain degree of fluctuation in financial reports. In contrast, US GAAP tends to lean towards a rules-oriented methodology, offering precise and comprehensive criteria for numerous particular circumstances. This meticulousness supports uniformity and aids in aligning financial reports across various organizations and fields. Nonetheless, it could also usher in a degree of intricacy and propel a shift in emphasis from grasping the genuine economic substance of transactions to a stringent adherence to compliance [10].

The foundational distinctions between these two accounting standards stem primarily from their underlying conceptual frameworks. IFRS's framework is based on a single set of global accounting principles. It is intended to improve consistency and transparency in financial reporting across different countries and regions. However, US GAAP has evolved through a mixture of standards set by different standard-setting bodies over time, making it a more complex and sometimes inconsistent framework. Furthermore, IFRS provides less guidance on certain topics, such as segment reporting and earnings per share, when compared to the exhaustive and detailed guidance under US GAAP. Such variances can noticeably impact the presentation of these elements within financial documents. In terms of presentation, there are also distinct differences. For example, IFRS does not apply a particular format for the income statement or the balance sheet, allowing for more flexibility, while US GAAP provides more specific presentation requirements.

#### **3.2. Specific Differences in Application**

IFRS and US GAAP have significant differences that persist in their application across various accounting aspects. This is also the reason for the different results of their financial reports.

Although both standards have moved towards a performance obligation approach with IFRS 15 and ASC 606 regarding revenue recognition, nuances remain in how contract modifications and variable considerations are treated, creating potential disparities in reported revenue. Taking intellectual property licensing as an example, IFRS allows for a certain level of flexibility in terms of when revenue can be recognized. In contrast, US GAAP lays out precise instructions, which could result in different timings for recognizing revenue. When it comes to expense recognition, especially in the realm of research and development (R&D), IFRS provides an option to capitalize development costs under certain conditions, a flexibility not afforded by US GAAP, which requires all R&D costs to be expensed as incurred. Such a pivotal discrepancy may result in entities that report under IFRS showcasing elevated asset figures and diminished expenses on their income statements, which could, in turn, sway investment choices. Besides, when it comes to leases, a crucial component of numerous businesses' operations, substantial transformations have occurred following the implementation of IFRS 16 and ASC 842. These new standards mandate the inclusion of the majority of lease obligations on the balance sheet. Even with this alignment, there are noticeable distinctions in their approaches. IFRS 16 opts for a streamlined method, categorizing all lease agreements as finance leases from the perspective of the lessee. On the other hand, US GAAP retains the dual classification, leading to differing effects on key financial indicators such as leverage ratios and the asset turnover rate. Furthermore, Pension accounting further illustrates the disparities between IFRS and US GAAP. IFRS requires immediate recognition of actuarial gains and losses in other comprehensive income and calculates net pension cost based on the net defined benefit liability or asset. In contrast, US GAAP allows for deferral of certain gains and losses and segregates the components of pension cost, leading to different presentations in the income statement and comprehensive income [11].

### 3.3. International Harmonization

Striving for global consistency and the ability to easily compare financial statements, the move towards international uniformity in financial reporting has stood at the forefront of the ongoing convergence between IFRS and US GAAP. To successfully attain convergence, it's imperative to establish a unified, clear, and workable set of global accounting standards. These standards should facilitate the production of high-caliber, transparent, and consistent information within financial reports, which is a crucial step to guarantee the alignment of IFRS and GAAP [12]. Spanning several decades, the IASB and FASB have dedicatedly worked together, making strides in bringing their respective accounting standards closer.

The Norwalk Agreement in 2002 was an important step in this convergence process. IASB and FASB committed to developing high-quality, compatible accounting standards in this agreement. After this, various joint projects were undertaken by the organizations, addressing key areas of divergence such as revenue recognition, leases, and financial instruments. The joint endeavors of both standard-setting bodies eventually led to the unveiling of IFRS 15 'Revenue from Contracts with Customers' and ASC Topic 606. As a result, a unified framework for revenue recognition was established. Lease accounting also witnessed significant alignment with the introduction of IFRS 16 and ASC 842, both of which brought leases onto the balance sheet, enhancing transparency and comparability across entities irrespective of the accounting standards adopted.

Although considerable strides have been taken toward alignment, full global uniformity in financial reporting standards still appears to be a distant target. The divergences between IFRS and US GAAP are deep-seated, stemming from their unique historical evolutions, foundational principles, and the distinct legal and regulatory contexts they inhabit. IFRS adopts a principle-based strategy, offering a wider and more flexible accounting framework. At the same time, US GAAP is characterized by its rule-based guidance, a trait shaped by the litigious tendencies prevalent in the American corporate landscape [13]. The complexity of reconciling different economic, legal, and

cultural backgrounds presents ongoing challenges. Relevant organizations need to work together to create a more integrated and transparent global financial reporting landscape.

#### 4. Conclusion

The evolution of the IFRS reflects a pivotal change in the financial reporting. Financial reporting is more transparent, comparable, and uniform than ever before. This paper has meticulously examined the substantial effects stemming from key revisions in revenue recognition, lease accounting, and the management of intangible assets. It emphasizes the shortcomings in handling these aspects under IFRS before the modifications and how addressing these deficiencies has enhanced the quality of financial reporting. The comparison with US GAAP has underscored the distinct philosophies underpinning these two predominant accounting frameworks while highlighting the commendable strides made towards convergence. International harmonization efforts have significantly improved cross-border investments and financial statement quality. As the business environment evolves, it is important to continuously refine IFRS. The capability of accounting standards to swiftly adapt to new developments and intricate scenarios is vital for maintaining the integrity and functionality of financial reporting. The path forward calls for sustained collaboration among standard setters, regulators, and stakeholders across the globe. In the broader context of global financial reporting, the evolution of IFRS reflects the needs of the global business environment and the pursuit of higher quality financial reporting. As FASB and IASB continue to improve the financial reporting standards, financial reporting will become increasingly reliable. This ultimately lays a robust foundation for informed decision-making, bolsters investor confidence, and fosters sustainable growth in the global economy. And that ultimately creates a solid foundation for informed decision-making, enhances investor confidence, and supports sustainable global economic growth.

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