

Financials2011

MARCH 8–11 • LAS VEGAS

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Governance, Risk & Compliance

MARCH 8–11 • LAS VEGAS

Tips and Techniques to Manage Asset Accounting Activities to Stay in Compliance with IFRS

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In This Session ...

Asset Accounting (FI-AA) is one of the areas most impacted by IFRS

The SAP solution of many US-based companies is ill prepared to accommodate IFRS

Let's go beyond the theory of IFRS and discuss tangible solutions in SAP

How does configuration need to change to accommodate IFRS?

How do business processes need to change to accommodate IFRS?

Does SAP provide new solutions for IFRS?

What We'll Cover ...

General Ledger design impacts on IFRS solution in Asset Accounting

Changes to Asset Accounting configuration for IFRS

IFRS requirements impacts

Asset Accounting process impacts

Wrap-up

General Ledger Design Impacts on IFRS Solution in FI-AA

Parallel Accounting is the biggest challenge to a successful implementation of IFRS for most US-based customers

SAP solutions designed exclusively for US GAAP and US Tax are not configured to accommodate the multiple standards required by IFRS



Heads-Up

The Asset Accounting (FI-AA) solution is dictated by the General Ledger design

General Ledger Design Impacts on IFRS Solution in FI-AA (cont.)

There are many ways in SAP to manage the multiple scenarios (US GAAP, Local GAAP, IFRS) that are required by adoption of IFRS



Tip

There is a parallel accounting solution for every customer but the best solution will vary depending on time, budget, requirements, and existing SAP Solution

The GL design is the first and most important step to successful implementation of IFRS as it establishes how parallel accounting will be managed

Pre SAP ERP (SAP R/3 4.7 and earlier)

- With no upgrade to SAP ERP 6.0
 - ◆ Account Solution
 - ◆ Parallel Company Codes
 - ◆ Special Purpose Ledger
- Upgrade to SAP ERP 6.0
 - ◆ Migrate to SAP General Ledger
 - Account Solution
 - Special Purpose Ledger
 - Parallel Ledger

SAP ERP with SAP General Ledger

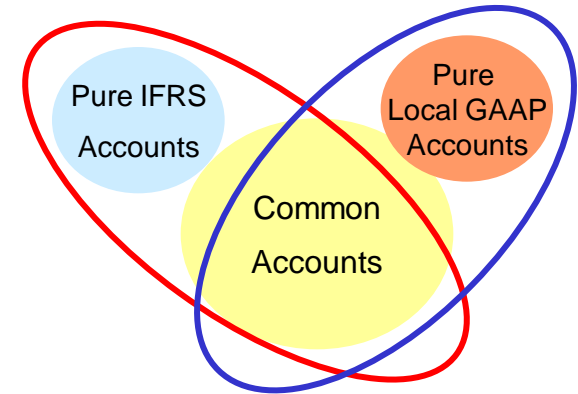
- Account Solution
- Special Purpose Ledger
- Parallel Ledger

SAP ERP with classic General Ledger

- Account Solution
- Special Purpose Ledger
- Migrate to SAP General Ledger
 - ◆ Account Solution
 - ◆ Special Purpose Ledger
 - ◆ Parallel Ledger

What is an Account solution?

- Uses single ledger for all postings
 - ◆ Could be the Leading Ledger for SAP General Ledger
- Accounts are “grouped” according to legal reporting requirements
 - ◆ Example
 - 300000 to 400000 Operational Chart
 - 500000 to 550000 IFRS
 - 600000 to 650000 Local GAAP
- Each group of accounts must be in balance
 - ◆ Requires extra care to ensure correct account determination
 - ◆ And the establishment of a coding handbook
- IFRS Financial Statements report using common accounts and “pure” IFRS accounts together
 - ◆ Red oval in diagram



Account solution is recommended where:

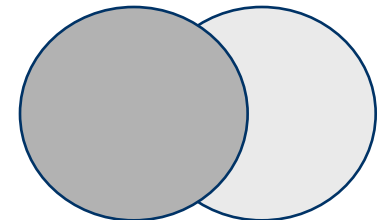
- Relatively few valuation differences exist between IFRS and local GAAP
- No issue with an increased number of GL accounts
- Standard reporting is used
- Different fiscal years not required



Don't
Forget

What is a Parallel Company Code solution?

- FI-AA can post from additional valuation areas into additional company codes (supports depreciation posting and gain/loss from sale of assets)
- FI-AA is not activated in additional company codes
- Valuation adjustments via valuation area 01 posts online and is always carried in the GL of the main company code
- This approach is supported only for FI-AA, FI, and manual postings
- Involves high volume of manual postings
- SAP not planning any enhancements in this area



Parallel Company Codes is recommended where:



**Don't
Forget**

- Increased number of GL accounts is an issue
- Valuation differences only result from FI-AA, FI, or manual postings
- Standard reporting is used
- Larger number of company codes is not problematic
- Various company codes do not need different GL account names

What is a Parallel Ledger solution?

- Provides IFRS and local accounting standard reporting from multi-ledgers
 - ◆ Can be configured to meet both reporting requirements from the first go-live date
- Utilizes the best features of the SAP General Ledger
 - ◆ Document splitting
 - ◆ Segment reporting
 - ◆ Etc.
- Recommended option for complex installations
 - ◆ Large differences between IFRS reporting standards and the current legal reporting standard



What is a Parallel Ledger solution?

- Feeds properly formatted IFRS data directly into the reporting and analytics layer
 - ◆ Simplifies reporting and requires little manual adjustment after consolidations
- Implementation from the beginning of fiscal year
 - ◆ Matches IFRS timeline

Parallel Ledger configuration is recommended where:

- Segment reporting is required
- Increasing the number of SAP General Ledger accounts is not desirable
- Complete set of separate legal reporting books is preferred
- Different fiscal year is needed for different legal sets of books



**Don't
Forget**

What is a Special Purpose Ledger solution?

- Additional Special Ledgers (SL) are set up to maintain a parallel set of ledgers for each accounting principle
- Automatic valuation methods can create entries into either ledger as appropriate
- Accounting principle controls posting destination ledgers
- Data transfer from Main Ledger to Special Ledgers through Integration Manager and data selection rules
- Postings to Special Ledgers from FI, FI-AA, CFM, MM, SD, and CO







Special Purpose Ledger is recommended where:

- Large number of GL accounts not desirable
- Complete set of separate books for each accounting principle is preferred
- Different fiscal year is needed
- Access to FI data from SL reports is not needed
- Large number of valuation differences exist



**Don't
Forget**

General Ledger Design Impacts on IFRS Solution in FI-AA (cont.)

Approach	Comments	SAP R/3	SAP ERP	Recommended?
Account-Based 	<ul style="list-style-type: none"> Easiest to implement Can lead to unmanageable COA in SAP General Ledger 	X	X	Yes
Parallel Company Codes 	<ul style="list-style-type: none"> No additional functionality planned by SAP Not a recommended solution for most companies 	X	X	No
Parallel Ledger 	<ul style="list-style-type: none"> Most transparent approach Independent set of books Future IFRS requirements more easily accommodated 		X	Yes
Special Ledger 	<ul style="list-style-type: none"> No additional functionality planned by SAP Not a recommended solution for most companies 	X	X	No

What We'll Cover ...

**General Ledger design impacts on IFRS solution in
Asset Accounting**

Changes to Asset Accounting configuration for IFRS

IFRS requirements impacts

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Wrap-up

Changes to Asset Accounting Configuration for IFRS

Asset Accounting requires parallel valuations to be tracked for each asset in order to produce financial statements in US GAAP and IFRS

Each valuation (depreciation area) must:

- **Track cost and depreciation separate from the other valuations**
- **Be capable of using different useful lives and depreciation terms**
- **Be posted to the GL in order to produce financial statements by valuation**

Changes to Asset Accounting Configuration for IFRS (cont.)

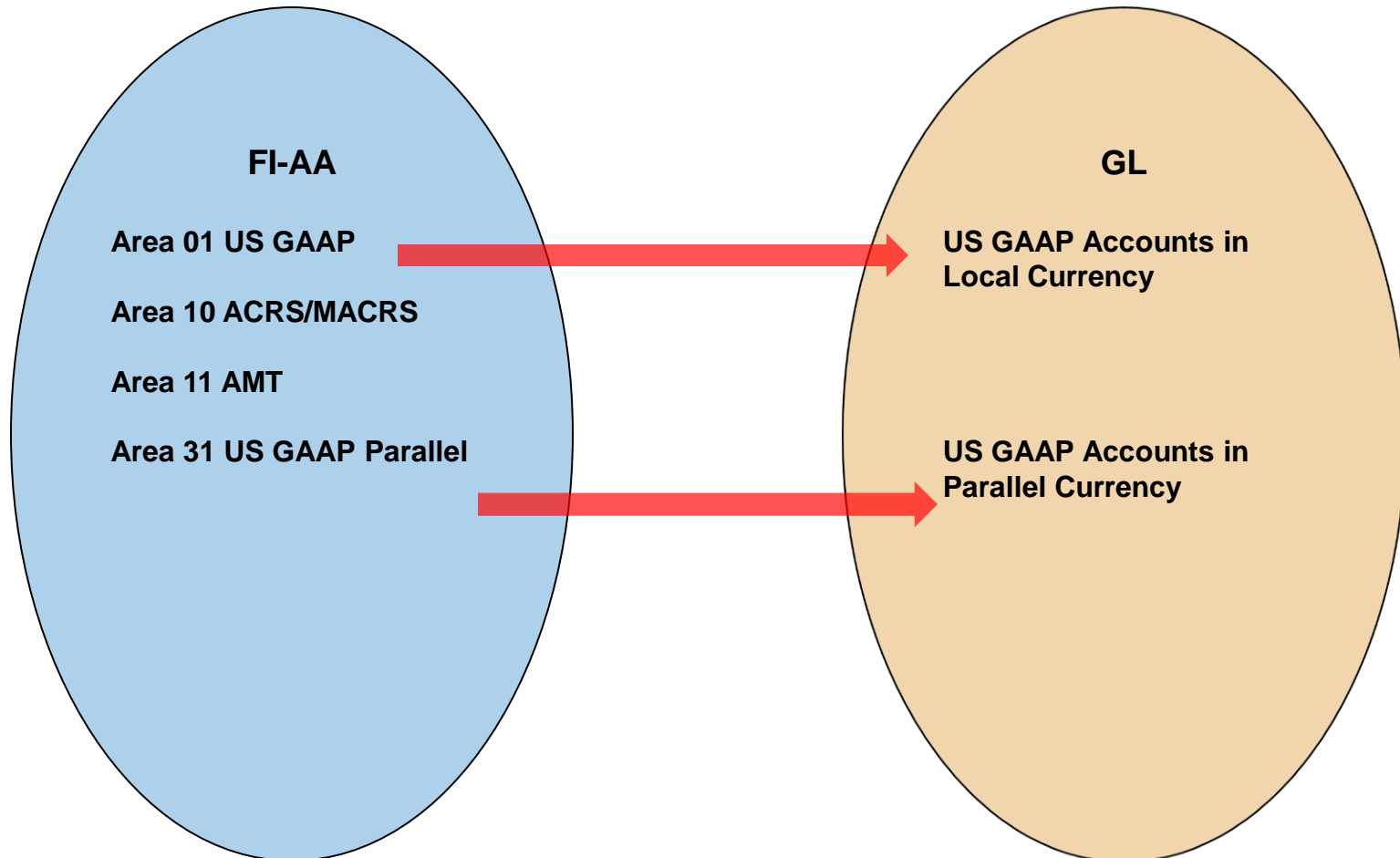
Most US-based FI-AA solutions manage a single valuation (US GAAP)

Managing and integrating multiple valuations from Asset Accounting into the GL is the first challenge to implementing IFRS in Asset Accounting!

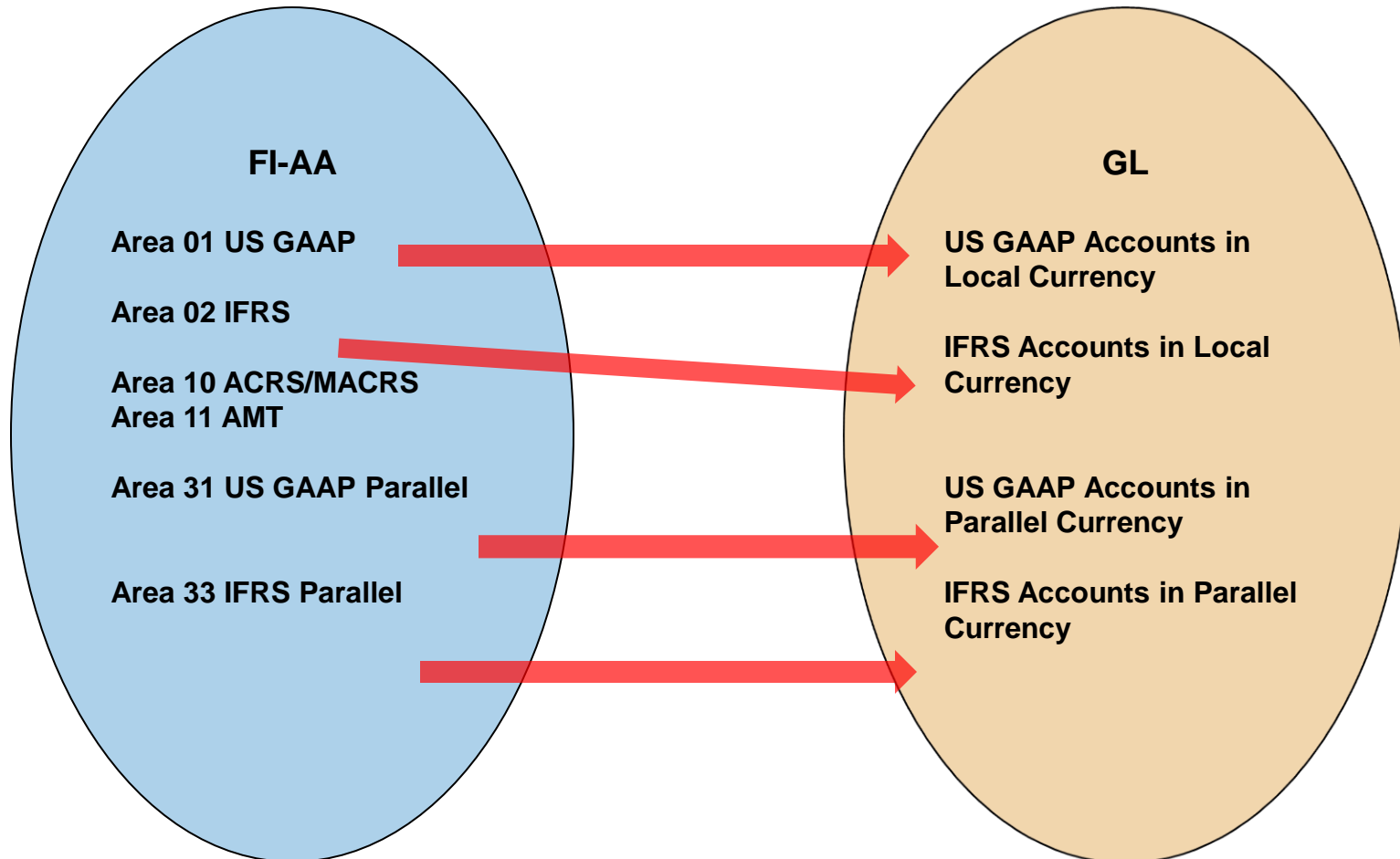


Heads-Up

Current Solution



Example: Account Solution



IFRS Solution for FI-AA Using an Account Solution

Add new Depreciation Area(s) for IFRS

Configure new area(s) to update the Alternative Accounts

Add new accounts to the COA to receive the parallel valuation postings

Adjust month-end processes to incorporate periodic processing from Asset Accounting

Adjust GL and Asset Accounting reporting processes to incorporate new accounts and depreciation areas

Adjust RICEFs to accommodate new areas and processes

Build preventative measures to avoid mixing main and alternative accounts in an unbalanced posting



Tip

IFRS Solution for FI-AA Using a Parallel Company Solution

Add new Depreciation Area(s) for IFRS

Configure new area(s) to update the Parallel Company Codes

Adjust month-end processes to incorporate periodic processing from Asset Accounting to additional Company Codes

Adjust month-end processes to additional Company Codes

Adjust General Ledger and Asset Accounting reporting processes to incorporate new Company Codes

Adjust RICEFs to accommodate new Company Codes

IFRS Solution for FI-AA Using a Special Ledger Solution

Add new Depreciation Area(s) for IFRS

Add Special Purpose Ledgers (SPL) and configure them accordingly

Configure new area(s) to update SPL(s)

Adjust month-end processes to incorporate periodic processing from FI-AA to SPL(s)

Adjust General Ledger, SPL, and FI-AA reporting processes to incorporate new SPL(s) and depreciation areas

Adjust RICEFs to accommodate new areas and processes

IFRS Solution for FI-AA Using a Parallel Ledger Solution

Add new Depreciation Area(s) for IFRS

Configure new ledgers in SAP General Ledger

Configure relevant area(s) to update appropriate Ledger Groups

Adjust month-end processes to incorporate periodic processing from Asset Accounting

Adjust General Ledger and Asset Accounting reporting processes to incorporate new ledgers and depreciation areas

Adjust RICEFs to accommodate new ledgers and processes

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IAS16/IAS36 – Fixed Assets/ASC 360 Plant, Property & Equipment

- **Componentization – Subjective but significant parts need to be separated**
- **Depreciation – Components depreciated separately**
- **Valuation – Impairments reversible; Revaluations optional**

IAS17 Leases/ASC840 Leases

- **Land and Building assets considered separately**
- **Not limited to PP&E**

IAS38 Intangible Assets/ASC350 Intangibles (ASC730 – R&D)

- **Revaluation permitted**
- **Development costs capitalized**

IFRS Componentization Requirement

- Definition of an asset is subjective
- Grouping of minor assets allowed
- Components of an asset may be grouped if useful life and depreciable method are identical
- Assets are separated into components if significant cost components differ in their useful life

US (ASC360-30) Componentization

- Asset are allowed to be grouped
- Asset componentization allowed but rarely used
- Asset componentization is prescribed for some regulated industries

Impacts of Componentization on SAP

- **Master data**
 - ◆ **Asset Classes**
 - ◆ **Conversion**
 - ◆ **Changing from current assets to componentized assets**
- **Transactions**
 - ◆ **Asset creation and capitalization processes must be reviewed**
 - ◆ **Identify impact on follow-on assets processes**



**Building
Blocks**

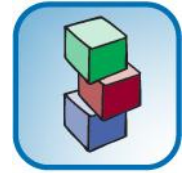
IFRS Depreciation Requirement

- Asset retirement requires Income Statement gain or loss
- Idle assets must continue to depreciate
- Asset components are depreciated separately
- Estimation of useful life is subjective based on similar assets

US (ASC360-35) Depreciation

- Ordinary gain or loss on retirement is deferred to balance sheet accumulated depreciation for grouped assets
- Income Statement gain or loss only on extraordinary asset retirement
- Grouping of assets for depreciation is allowed

Impacts of Depreciation Differences on SAP



**Building
Blocks**

■ Design

- ◆ Is reallocation of depreciation reserves required to support componentization?

■ Master data

- ◆ Do current depreciation keys support componentization?
- ◆ Do current default depreciation keys and lives support componentization?

■ Transactions

- ◆ Impacts on depreciation forecast or retirement process?

IFRS (IAS36) Impairment

- The objective is to ensure assets are carried at no more than their recoverable amount
- Assets of Revenue Generating Units must test that all assets do not have a carrying value which exceeds the recoverable value
 - ◆ If so, assets are adjusted to the higher of fair value less selling costs or the value in use

US (ASC360-35) Impairments

- Done by asset group
- Two-step test
 1. Carrying value exceeds recoverable value, and ...
 2. Carrying value exceeds fair value
- Review based on changes in circumstance
- Loss reversal prohibited

IFRS (IAS16) Revaluation

- **Optional**
- **For entire class of assets**
- **Fair value less impairment and accumulated depreciation**

US (ASC360-40) Revaluation

- **Revaluation is not permitted**
- **PP&E valued at historical cost**

IFRS (IAS17) Leases

- Scope not limited to PP&E
- Land and building are considered separately unless land is immaterial
- Finance (capital) lease if:
 - ◆ Lease term comprises substantial portion of asset life
 - ◆ Present value of lease payment covers substantially all of asset's fair value
- Sale leaseback gain/loss
 - ◆ Amortized over lease term if finance
 - ◆ Recognized immediately if operating

US (ASC840) Leases

- Land is considered separately if 25% or greater of lease fair value
- Capital lease if:
 - ◆ Lease term is greater than 75% of asset life
 - ◆ Present value of lease payment is greater than 90% of asset fair value
 - ◆ Two tests for lessor sale-type lease
 - Collection is reasonably expected
 - Un-reimbursable costs are certain
 - Then, replace asset with receivable if capital
- Sale leaseback gain/loss
 - ◆ Recognize now if seller relinquishes
 - ◆ Amortize over term if seller controls

Master Data

- Check asset classes to ensure all required lease asset types are covered
- Amend screen layouts to include leasing data fields if needed

Transactions

- Review capitalization processes to ensure proper compliance of leasing requirements
- Review depreciation postings for leased assets to ensure proper accounting treatment



**Building
Blocks**

IAS38 – Applies to Intangible Assets that have three critical attributes:

- **Identifiable**
- **Control (power to obtain benefits from the asset)**
- **Future economic benefits (such as revenues or reduced future costs)**

IAS38 – Does not apply to:

- Financial assets
- Exploration and evaluation assets (extractive industries)
- Expenditure on the development and extraction of minerals, oil, natural gas, and similar resources
- Intangible assets arising from insurance contracts issued by insurance companies
- Intangible assets covered by another IFRS, such as intangibles held for sale, deferred tax assets, lease assets, assets arising from employee benefits, and goodwill

IAS38 – Intangible Assets

- **Development costs are capitalized if asset is ...**
 - ◆ **Technically feasible**
 - ◆ **Intended for completion, or**
 - ◆ **Saleable in the future**
- **Revaluation allowed**
- **Impairment adjustments**
 - ◆ **Loss reversal is allowed**
 - ◆ **Include indefinite life assets**
 - ◆ **At least annually**
 - ◆ **Use fixed asset methods**

US (ASC350, ASC730) – Intangible Assets

- Development costs expensed as incurred except capitalize ...
 - ◆ Software for external use, after technical feasibility
 - ◆ Software for internal use, only during development stage
- Revaluation not allowed
- Impairment adjustments
 - ◆ Reversal of loss prohibited
 - ◆ Include indefinite life assets
 - ◆ When conditions change
 - ◆ Use PP&E methods

Master Data

- Check asset classes to ensure all intangible asset types have an appropriate class

Transactions

- Review capitalization processes to ensure intangible costs are captured and capitalized correctly
- Review depreciation postings for intangible assets to ensure proper accounting treatment



**Building
Blocks**

What We'll Cover ...

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Wrap-up

Daily Processes

- Procurement and Capitalization processes must be reviewed in order to ensure compliance with IFRS
- Accounting methods across standards must be reviewed so that the proper downstream accounting solution (account-based, SPL, additional ledger) is considered



Caution

Monthly Processes

- **Periodic Posting of AA balances to the General Ledger must be included in the month end (not previously needed when one standard was used)**
- **Incorporate new monthly postings related to impairments, revaluations, leases, etc.**
- **Add month-end close steps for additional ledgers or company codes**
- **Update month-end reporting solution to include additional ledgers, company codes, or accounts**

Year-End Processes

- Update year-end processes to include additional ledgers, company codes or accounts. Examples are:
 - ◆ Roll Fiscal Year Balances
 - ◆ Close Fiscal Year
- Include the same in year-end reports

What We'll Cover ...

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Resources

www.ifrs.org/NR/rdonlyres/FBE30248-225B-48AF-AAE5-96494D83A978/0/LeasesSnapShot0810.pdf

- Paper describing IAS17 and its impact on Leases

www.ifrs.org/NR/rdonlyres/2D5D6C15-65CE-4430-AB1D-1E4E4E74D7FE/0/IAS16.pdf

- Paper describing IAS16 and its impact on PP&E

www.ifrs.org/NR/rdonlyres/715CDD70-96A4-4D37-B53A-A0E4E61FB828/0/IAS36.pdf

- Paper describing IAS36 and its impact on Impairments

www.ifrs.org/NR/rdonlyres/8A3C6720-AABE-4BE2-B776-0BBE51961AA0/0/IAS38.pdf

- Paper describing IAS38 and its impact on Intangible Assets

7 Key Points to Take Home

IFRS rule changes are well documented but little time has been spent focused on the “How To’s” of implementing IFRS in SAP

SAP solutions designed for US GAAP and US Tax must change to accommodate multiple standards (e.g., US GAAP, US Tax, and IFRS)

General Ledger design is the first critical design choice to a successful implementation of IFRS

The General Ledger design is very flexible but can be constrained by the SAP release in use

Asset Accounting solution must change to follow the General Ledger solution

7 Key Points to Take Home (cont.)

Asset Accounting design and processes must change to accommodate IFRS

IFRS impacts in Asset Accounting are primarily:

- **Componentization**
- **Leases**
- **Impairments**
- **Depreciation**
- **Intangibles**

Thank you for your attention



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Any further questions?