TWISTS IN THE TALES OF THE SIC'S DELIBERATIONS

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One of the many important changes which Sir Bryan Carsberg has made at the IASC is the establishment of the standing interpretations committee (SIC). This is a long overdue improvement in the IASC's procedures. However, Sir Bryan must have been as surprised as I was when, with its first decisions, the SIC overturned an earlier board decision on LIFO and adopted different answers to the same question on IAS 2 and IAS 23. I am sure that this was not what Sir Bryan had in mind when he talked of rigorous interpretations of IASs.

The crux of the problem is the IASC's efforts to ban or reduce the use of LIFO. The original IAS 2 allowed an enterprise to use a variety of formulas, including LIFO, to account for inventories for which specific costs could not be identified. This free choice was one of most significant to be considered during the IASC's comparability project. But it has also proved to the most troublesome.

Following its review of the comments on E32 *Comparability of Financial Statements*, the IASC decided that it should ban the use of LIFO. However, when it came to the final vote, the IASC was forced to reinstate LIFO as an allowed alternative treatment because Germany, Italy, Japan and Korea refused to back the ban. A significant factor in the decision of at least one of the four countries was IOSCO's last minute message that this was one choice which the IASC should not eliminate (claims that IOSCO had advised the IASC of this view two years earlier are incorrect).

Paul Cherry of Canada was the chairman of the IASC's improvements steering committee and was, therefore, responsible for the review of IAS 2. After the reinstatement of LIFO, he expressed concern that the revised draft did not permit an enterprise to use LIFO for some inventories and FIFO or weighted average cost for other inventories. He argued that the revised standard should allow such flexibility. But in a written ballot, the majority of the IASC board disagreed with him. The board confirmed that an enterprise which wanted to use LIFO for some inventories had to use LIFO for all its inventories; in other words, like transactions should be accounted for in a like way. While the board had not gone as far as many wanted, it had achieved some progress towards the use of the same accounting for the same inventories.

Given the controversy associated with the issue, it was no surprise that some sought to interpret IAS 2 more flexibly than the board intended. Coopers & Lybrand were among the first to break ranks. In *Understanding IASs*, the firm argued that IAS 2 was silent on the issue and that an enterprise 'may use weighted average, FIFO and LIFO formulas for assigning costs to different classes on inventories'. The team responsible for this view included Paul Cherry, the IASC's chairman Michael Sharpe and two other partners who had participated in the board's discussions on LIFO and the subsequent ballot.

In the circumstances it was also not surprising that this issue was placed on the agenda of the SIC particularly as Paul Cherry had been appointed as the committee's first chairman. The obvious solution for the SIC was to support the board's earlier decision. Furthermore, the SIC had also been asked to look at the same principle - the mixing of benchmark and allowed alternative treatments - in the context of IAS 23 *Borrowing Costs*. Again the solution was obvious - adopt the same approach agreed by the board for inventories and so adopt a consistent precedent for all IASs which include benchmark and allowed alternative treatments.

Instead of doing the obvious thing, the SIC overturned the board's decision on inventories. One member of the SIC told me: 'We felt that IAS 2 needed changing.' So change it, they did in spite of the fact that only the board, and not the SIC, can change IASs. On borrowing costs, the SIC decided that an enterprise had to use either the benchmark treatment or the allowed alternative - the right answer but a different one from that on inventories.

There is one further twist to this story. Members of the SIC have confirmed to me that when they considered their draft interpretation they were not told that the board had decided earlier that an enterprise which wants to use LIFO for some inventories had to use LIFO for all its inventories. Members of the committee did not learn about this decision until they read the comments (including mine) on the published draft. This is a quite extraordinary state of affairs which undermines the credibility of the whole interpretations process.

It would be easy to dismiss the SIC's decision on LIFO as an exception which reflects the controversy which has surrounded this topic. However the SIC will be asked to consider other controversial issues where its members might disagree with existing IASs. Examples include the definition of extraordinary items, the criteria for the use of the pooling of interests method, the entity approach to consolidations and the application of the proposed IAS on provisions.

The IASC board should remind the SIC that its work is an important part of Sir Bryan Carsberg's efforts to improve further both the quality and the acceptability of IASs and to win IOSCO's endorsement of IASs. His efforts will fail if the SIC overturns board decisions, if relevant information is withheld from the SIC, and the SIC adopts conflicting solutions to the same problem. The SIC and the IASC board should ensure that Sir Bryan's efforts succeed.

Sir Bryan Carsberg's objective of one uniform system of accounting throughout the world also requires further efforts to remove the choice between LIFO and FIFO/weighted average cost. The IASC's deliberations should focus on what is good accounting and should be free of the tricks which have hampered the debate so far. And who knows, perhaps LIFO will emerge, on merit, as the only acceptable formula for the valuation of inventories.