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The Transition from US GAAP to IFRS: Fundamental Differences and Their Implications on Financial Statements That Walmart Should Know

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In the business world, it is known that companies must utilise proper accounting standards, whether they are operating in the United States (US) or outside the US. Following the correct accounting standards will help corporations' managements to avoid failing into legal and financial issues which ultimately have an effect on company performance. Such matters might result in shaking the confidence to deal with such a business. Hence, shifting from the US GAAP to the IFRS must have fundamental adjustments of followed accounting styles and methods. Therefore, the primary aim of this document is to focus on a descriptive (comparative) analysis of two significant systems called US Generally Accepted Accounting Principles (US GAAP) and International Financial Reporting Standards (IFRS). The two approaches have similarities and differences. This document, in result, explains the substantial differences between the US GAAP and the IFRS and their impacts on financial reports that US companies have to take into account in terms of the revenue recognition and measurement; inventory valuation methods; extraordinary items; and the presentation of income and balance sheet statements.

Keywords: *Walmart, US, GAAP, IFRS, Revenue recognition, LIFO, FIFO, Balance sheet.*

Background

Walmart is considered one of the biggest retail companies in the world. In 1962, Sam Walton established the company in Bentonville, Arkansas, in the United States of America (USA). Today, Walmart operates stores in more than 27 countries around the world. Most of its branches are located in the USA, Mexico, and Canada. The company's revenues, net income, assets, employees, and stores are all described in the report below from 2018 (annual report, 2018).

Amounts for revenues, net income, and assets are in USD

Year	Revenues	Net income	Total assets	Share price	Employees	Stores
2018	500,343	9,862	204,522	90.80	2,300,000	11,718

Source: 2018 annual report of Walmart

In addition to Walmart, many American publicly traded corporations have increasingly started operating internationally. Working outside of the USA environment would require firms to comply with the international accounting standards. Therefore, by assuming Walmart is among the companies that wants to use the IFRS entirely, it should make several necessary adjustments to its financial statements during that transition process. Hence, this paper will clarify the significant differences which Walmart should pay attention to.

Hypothesis

1. There are fundamental differences that could have an effect on financial statements during the transition from the US GAAP to the IFRS.
2. There are no fundamental differences that could have an effect on financial statements during the transition from the US GAAP to the IFRS.

Introduction

The international financial and accounting reporting standards that were founded in 2001 by the International Accounting Standards Board (IASB) are considered as being 'principles-based', in which they largely govern the accounting treatments for business within more than 110 countries worldwide (Nguyen, 2018). The accounting standards in the US, on the other hand, are referred to as the Generally Accepted Accounting Principles (GAAP), of which were founded by the Financial Accounting Standards Board (FASB) and are considered as being 'rules-based' (Ross, 2018).

In addition to the accounting rules and various measures, many inevitable issues have to be properly addressed and fully understood by the corporations during the shift to the IFRS from the US GAAP. For instance, cultural factors, law obligations, tax policies, and the handling murmurs formworks.

Despite both approaches aiming to govern, unify, and organise accounting procedures into the presenting of financial statements for business operations, public traded companies such as Walmart should consider that there are some basic differences between those two systems, with respect to the preparation of financial statements. This paper will explain each common key difference between them, in order to obtain a comprehensive overview regarding understandability, comparability, variance, and similarity.

Revenue Recognition

Based on the footnotes of Walmart's annual report, the corporation announced that the actual revenue recognition occurs when the goods or services are performed. Nevertheless, under both the IFRS and the US GAAP, a percentage of completion could be calculated when the outcome reliably is determined and also an immediate recognition of losses or profits when they can be expected, as it is explained in Table 2 below. However, the IFRS states that revenue recognition has to be calculated at the same extent of costs and costs are considered as expenses when they actually incurred. Profits are calculated at its time completion (Bohusova & Nerudova, 2009.) The US GAAP in return states that a completed contract method can be used and therefore, revenues, costs, and profits would be recognised when the contract is completed (Bohusova & Nerudova, 2009).

The best way to fully understand the above information is to provide an example. Such as, assuming that Walmart has signed a contract to sell office furniture to 'XYZU University' for \$10,000, and the reliably total costs of the contract was \$8,000. The costs were projected by Walmart as follows:

Year	**2015**	**2016**	**2017**	**Total**
Cost Incurred	\$4,000	\$1,600	\$2,400	\$8,000

Required: Calculate the achieved revenues and profits under the IFRS and the US GAAP when (1) the outcome can be reliably measured, and (2) when the outcome cannot be reliably measured.
Situation 1: As mentioned before, when the outcome is a reliably measured, both the IFRS and the US GAAP indicate a percentage of completion can be utilised. Therefore, Walmart will recognise the revenues and costs, plus the profits as follows:

Table 2: When the outcome can be reliably measured

Year	2015	2016	2017	Total
% of Competition	50%	20%	30%	100%
Revenues	$5,000	$2,000	$3,000	$10,000
Costs	$4,000	$1,600	$2,400	$8,000
Profits	$1,000	$4,00	$6,00	$2,000

Situation 2: According to the IFRS, when the outcome cannot be reliably measured, Walmart would recognise revenue at the same amount of the achieved cost (see Table 3). While under the US GAAP, net profits will be recognised in the year that the project is expected to be completed (see Table 4). Hence, we observe that the project was completed in 2017, and the recognised profits, in which Walmart will report in the financial statements, is $2,000, as stated below.

Table 3: The outcome cannot be reliably measured — IFRS

Year	2015	2016	2017	Total
Revenues	$4,000	$1,600	$4,400	$10,000
Costs incurred	$4,000	$1,600	$2,400	$8,000
Profits	$0	$0	$2,000	$2,000

Table 4: The outcome cannot be reliably measured — US GAAP

Year	2015	2016	2017	Total
Revenues	$0	$0	$10,000	$10,000
Costs incurred	$0	$0	$8,000	$8,000
Profits	$0	$0	$2,000	$2,000

Presentation of Income Statement

For both sets, the income statement indicates the company's performance in terms of the operating classifications, where we can observe that some companies that follow the IFRS would name some items differently compared to corporations that follow the US GAAP. There is no specific format to prepare income statements under the IFRS, however it must include several items, such as net revenues, total costs, tax expenses, and losses or profits. On the other hand, the US GAAP is considered to be more detailed. Thus, in addition to the items mentioned above, other elements exist under the US GAAP, including income, expenses, gains, losses, and comprehensive income (CI).

Additionally, Waqar has explained in his article that under the US GAAP, either a single-step or multiple-step format could be used to prepare a consolidated statement of income. The US GAAP also allows businesses to announce a statement of Comprehensive Income (CI) separately (Murphy, 2012). Comprehensive income, nevertheless, is equal to attributed consolidated net income that is added to other comprehensive income (OCI) (Sean, 2018). From here, it is clear that Walmart is using a multiple-step format and the comprehensive income is resulted by combining the attributed consolidated net income to other comprehensive net income, as the US GAAP requires (see Exhibit 1).

Walmart Inc.		
EXIHIBT 1 Consolidated Statements of Comprehensive Income based on US GAAP's requirements		
(Amounts in millions)	**2018**	**2017**
Consolidated net income	**$10,523**	**$14,293**
Consolidated net income attributable to non-controlling interest	(661)	(650)
Consolidated net income attributable to Walmart	**$9,862**	**$13,643**
Other comprehensive income (loss) net of income taxes		
Currency translation and other	2,540	(3,027)
net investment hedges	(405)	413
Unrealised gain on available for sale	1,501	145
Cash flow hedges	437	21
Minimum Pension Liability	147	(397)
Other comprehensive income (loss) net of income taxes	4,220	(2,845)
Other comprehensive (income) net attributable to non-controlling interest	(169)	210
Other comprehensive income (loss) attributable to Walmart	**$4,051**	**(2,635)**
Comprehensive income, net of income taxes	14,743	11,448
Other comprehensive (income) net attributable to non-controlling interest	(830)	(440)
Comprehensive income attributable to Wal-Mart	**$13,913**	**$11,008**

Presentation of Balance Sheet

Under both the US GAAP and the IFRS approaches, the current and non-current assets and liabilities are separately reported on the balance sheet. However, the IFRS does not classify (specify) in which current or non-current should come first, regarding the assets section. Companies that use the US GAAP are required to sort the current assets first, and then the non-current assets. Whereas, the IFRS mostly requires and encourages corporations to start preparing the balance sheet with less liquid, and then, most liquid assets. The US GAAP in return, prefers to begin the reporting assets section with the most liquid, and then, less liquid assets (MURPHY, 2012).

For liabilities and shareholders' equity, there are some differences between the two sets regarding the items classifications. For example, common stocks are usually called "share capital" under the IFRS. Also, additional paid in capital (APIC) is a term under the US GAAP, but it is called 'share premium' under the IFRS (MURPHY, 2012). Hence, there are fundamental accounting adjustments that US companies, including Walmart, should consider, as explained in the following example.

Scenario: Assuming that Walmart's balance sheet is according to the US GAAP's requirements as follows:

Walmart Inc:	
Balance Sheet based on US GAAP	
Exhibit 2	
Assets	**Liabilities and Equity**
Current assets	Current Liabilities:
Cash and equivalents $6,756	Short-term borrowings $5,257
Receivables 5,614	Accounts Payable 46,092
Inventories 43,783	Accrued Liabilities 22,122
Prepaid Expenses and other 3,511	Accrued income taxes 645
Total Current assets **59,664**	Long-term debt due within one year 3,738
	Capital lease and financing obligations within one year 667

Property and equipment:	Total Current liabilities 78,521
Property and equipment 185,154	
Less accumulated depreciation 77,479	Long-term debt 30,045
Property and equipment, net 107,675	Long-term capital lease and financing obligations 6,780
	Deferred income taxes and other 8,354
property under capital lease and financing obligations	Tax payable Non-current 0
Property leases and financing obligations 12,703	
Less accumulated amortization 5,560	
Property leases and financing obligations, net 7,143	Equity
	Common Stock 295
	Capital in taxes of par value 2,648
Other Assets and deferred charges	Surplus (Deficit) -
Goodwill 18,242	Retained earnings 85,107
Other assets and deferred charges, net 11,798	Accumulated other comprehensive loss (10,181)
	Total Walmart shareholder's equity 77,869
	Non-controlling interest 2,953
	Total equity 80,822
Total assets $204,522	**Total Liabilities and Equity $204,522**

Additional Information

1. The company is using the LIFO method for inventory calculation. The year began with $15,000 as LIFO reserve and ended up with $20,000.
2. At 01/01/2018, the fair market value of property, plant, and equipment was $85,000, which resulted in a $5,000 increase (more than the recorded book value).
3. At 10/12/2018, the presented assets based on the Fair Market Value (FMV) was $10,000. However, the Goodwill impairment accounted for $3,000 in 2017.
4. The depreciation period of property, plant, and equipment was over a 10-year period. The amortization of intangible assets period was 4 years, no salvage recorded, and the straight-line method is utilised.
5. At 10/12/2018, there is a $11,000 as an investment and the Fair Market Value (FMV) is used. The value at the beginning of the year was $8,000, by which the gain of exchange rate is due of $3,000.
6. There was a lawsuit which cost the company $15,000 and significant damages, due to the store flooding.

Required

Determine whether there are effects between the US GAAP and the IFRS on the prepared balance sheet.

Solution

1- Since the IFRS does not allow using the LIFO method in the calculation of inventory, it would therefore be a difference between the LIFO and FIFO.
The LIFO reserve of $5,000 ($25,000 less $20,000) could result in decreasing COGS, as in 1A below. Further, the $20,000 would be recorded as in 1B, as explained under the journal entries below:

1A Inventory $5,000
GOGS $5,000 (goes to income statement)

1B Inventory $20,000
Deferred income tax $6,000
Retained Earnings $14,000

2- There is $5,000 as an increase of the carrying value of fixed assets, which goes to the shareholders' equity (Book Value less Fair Market Value). This $5,000 will increase the depreciation expenses and accumulated depreciation by $500 ($5,000/10 years — straight line method):

2A Depreciation expenses $500 (goes to income statement)
Accumulated depreciation $500

2B Fixed assets $5,000
   Shareholders' equity $5,000 (goes to comprehensive income)

3- No adjusting of the entry for Goodwill due to both the US GAAP and the IFRS sets having the same accounting treatment method.

4- The increase of the investment gains of $2,000 will be recorded under non-operating income, so the journal entry is:
   Shareholders' equity $2,000 (goes to comprehensive income)
   Exchanging rate gains $2,000

5- The IFRS does not allow companies to report extraordinary items separately. In this case, the resulted loss from flooding has to be under non-operating income of the income statement schedule. For more information, please read the explanation of the extraordinary items. Hence, below is how to prepare a balance sheet according to the IFRS and the US GAAP; a comparison between the two approaches.

Walmart Inc:		
Balance Sheet based on US GAAP- IFRS reconciliation		
		As of December 31, 2018
Exhibit 3 (Amounts in millions)		
Assets		**According to GAAP**
Adjustments **According to IFRS**		
Current assets		
Cash and equivalents		$ 6,756
$6,756		
Receivables		5,614
5,614		
Inventories	43,783	(1)
25,000 68,783		
Prepaid Expenses and other		3,511
3,511		
Total current assets		**59,664**
84,664		
Property and equipment		
Property and equipment	185,154	(2)
5,000 190,154		
Less accumulated depreciation	77,479	(2)
500 76,979		
Property and equipment, net		107,675
113,173		

Property under capital lease and financing obligations	
Property under capital lease and financing obligations 12,703	12,703
Less accumulated amortization 5,560	5,560
Property under capital lease and financing obligations, net 7,143	7,143
Other assets and deferred charges	
Goodwill 18,242	18,242
Other assets and deferred charges, net 11,792	11,798
Total assets **$ 204,522** **30,500** **$ 235,022**	**$**
Liabilities and Equity	
Current Liabilities:	
Short-term borrowings $5,257	$ 5,257
Accounts payable 46,092	46,092
Accrued liabilities 22,122	22,122
Accrued income taxes 645	645
Long-term debt due within one year 3,738	3,738
Capital lease and financing obligations within one year 667	667
Total Current liabilities 78,521	78,521
Long-term debt 30,045	30,045
Long-term capital lease and financing obligations 6,780	6,780
Deferred income taxes and other 8,354	8,354
Tax payable non-current 0 6,000 6,000	(1)

Equity	
Common Stock 250	295
Capital in taxes of par value 2,648	2,648
Surplus (Deficit) (4) 2,000 10,000	- (2) 6,000 (3) 3,000
Retained earnings 14,000 99,107	85,107 (1)
Accumulated other comprehensive loss (10,181)	(10,181)
Total Walmart shareholder's equity 102,369	77,869
Non-controlling interest 2,953	2,953
Total equity 105,322	80,822
Total Liabilities and Equity **30,500 $ 235,022**	**$ 204,522**

Inventory Valuation Methods

According to the US GAAP, first in first out (FIFO), weighted average, and last in first out (LIFO) are allowed to be used in relation to valuing inventory. Thus, by reading page 47 of Walmart's annual report of 2018, it can say its branch that operates in the US uses the LIFO method. On the other hand, Walmart International utilises FIFO for an inventory calculation. The purposes of using the two methods is that the company tries to have an adjustment and compliance with international and domestic legislations. In other words, to ensure compliance with both systems instructions. Although both approaches emphasise the inclusion of all direct inventory expenses, including 'overhead', the US GAAP states that companies have to record the inventory at the lower of cost or market value, while the lower of cost or net realisable value (replacement cost) has to be used to measure the inventory under the IFRS.

On the other hand, the IFRS prohibits using LIFO because in addition to its being unrealistic, LIFO might not always reflect the accurate flow of income levels for taxation purposes (Murphy & DBA, 2012). Therefore, there are significant adjustments in the inventory accounting methods if public companies, including Walmart, want to shift entirely to the IFRS.

In addition to the variation between the US GAAP and the IFRS regarding the used inventory methods, there is also another difference related to the inventory reserve concepts. Wherein, the US GAAP requires US businesses — Walmart as an example — to disclose the inventory reserve, which is the difference between LIFO and FIFO in the footnotes of their prepared annual report (Nguyen, 2018). So, US Walmart uses LIFO and Walmart International utilises FIFO in the inventory valuation. In other words, they did not announce the LIFO reserve (Annual report, page 47).

In order to understand that point, the example below compiled by the authors explains the LIFO reserve for 2016, 2017, and 2018, for Walmart respectively. (Note: The numbers are to provide an idea about the difference between LIFO and FIFO).

Table 5: Years 2015, 2016 and 2017

Amounts in thousands of USD			
ITEMS /2015	**LIFO**	**FIFO**	**LIFO Reserve**
Inventory Purchase	$1,750	$1,750	
COGS	800	500	300
Closing Inventory	$950	$1,250	$300
ITEMS /2016	**LIFO**	**FIFO**	**LIFO Reserve**
Inventory Purchase	$950	$1,250	$300
COGS	500	300	200
Closing Inventory	$450	$950	$500
ITEMS /2017	**LIFO**	**FIFO**	**LIFO Reserve**
Inventory Purchase	$450	$950	$500
COGS	300	150	150
Closing Inventory	$150	$850	$650

Logically, the important point we can notice from the last example is that the difference between LIFO and FIFO equals a LIFO reserve that Walmart should yearly (year-to-year) calculate to provide an accurate presentation of its financial reports and taxes purposes. So, based on the shown table, the LIFO reserve increased to $500,000 in 2016, and became $650,000 in 2017. Hence, according to the US GAAP, that increase of the LIFO reserve has to be recorded as a contra inventory of footnotes by the company in its annual report.

Research & Development Costs Valuation

Basically, the research costs according to the IFRS are considered expenses under the income statement. When they are incurred and development costs, they can be considered as capitalisation costs under the balance sheet statement. The US GAAP in return, does not allow either research or development costs to be capitalised. Hence, both of those costs will be shown under the operating expenses section of the income statement, according to the US GAAP (Forgeas, 2008). Therefore, for Walmart, for instance, research and development costs were shown to include the total operating expenses which were $483,042 in 2018 (Walmart's annual report, 2018).

Extraordinary Items

Usually extraordinary items are considered as a natural disaster incurred in certain circumstances out of a company's control, such as losses of flooding and gains or losses of sale of assets, lawsuits, acquisition, etc. Therefore, these events may unexpectedly and directly affect business performance. The US GAAP allows companies to report those irregularly losses or gains separately under so-called 'extraordinary items' in the consolidated statement of comprehensive income.

Meanwhile, extraordinary items, according to Walmart's annual report of 2018, have been reported separately under the consolidated income statement. So, the net income before tax has increased by $200,000, as extraordinary items (gains) became $9,862,000 (Annual report, 2018) (Forgeas, 2008). Oppositely, the IFRS prohibits such items to be separately reported in the comprehensive income statement. Therefore, this amount should be reclassified from extraordinary to non-operating expenses of the income statement (Harris & Washington, 2013).

Conclusion

Overall, this paper has illustrated that more than 110 countries globally use the IFRS. So, due to its flexibility and common accounting language, the number of companies, including Walmart, that want to shift to the IFRS are increasing continuously. Whereas, the US GAAP focusses on the USA area that structures, guidelines, and organises the applied accounting methods for companies during the financial disclosure.

In addition to Walmart, these companies should consider some similarities and key differences related to the financial statements of the two approaches during the movement from the US GAAP to the IFRS, which can be summed up in the following points: (1) The IFRS is considered to be "principles-based" and the US GAAP is considered to be "rule–based", so it is more detailed than the IFRS because it reflects all the performance elements such as revenues, expenses, profits, losses, gains, assets, liabilities and comprehensive income; (2) Revenues recognition according to the IFRS should be at the same extent of costs. On the other hand, the US GAAP states that a completed contract method can be used and therefore, revenues would be recognised when the contract is completed or the goods or services are completely performed; (3) Regarding inventory valuation, the IFRS prohibits utilising the LIFO method, while it is allowed to be used under the US GAAP; (4) Inventory reserve is prohibited under the US GAAP and it is permitted under the IFRS, but in certain aspects; (5) Development and research costs are expenses under the US GAAP and are capitalised under the IFRS; and (6) The IFRS prohibits reporting extraordinary items separately in the presenting of the income statement, and they have to be reclassified under non-operating expenses of the income statement. The US GAAP, nevertheless, allows business to disclose them separately.

It is clear that we cannot accept hypothesis two, which states that there are no fundamental differences that could affect the reported financial statements during the movement from the US GAAP to the IFRS. Therefore, we accept hypothesis one, which states that there are fundamental variations.

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