Consultation on treatment of financial results under IFRS

I. INTRODUCTION

Pursuant to regulations adopted by the Council of the European Union, all companies listed on exchanges in EU member states are required to prepare their consolidated financial statements for financial years beginning on or after January 1, 2005, in accordance with International Financial Reporting Standards ("IFRS"). However, companies that were reporting using the U.S. Generally Accepted Accounting Principles ('US GAAP') as of January 1, 2005 are permitted to continue doing so until 2007. In addition, several companies in other regions including Norway, Switzerland, Australia, Singapore, Hong Kong and China have also adopted IFRS starting in 2005.

A transition from local GAAP to IFRS may impact the computation of historical long-term earnings and sales trends since IFRS earnings and sales numbers may not be comparable with the numbers reported using local GAAP. Historical earnings and sales numbers over a five year period are important components of MSCI index construction methodology.

On September 29, 2005, MSCI issued a clarification on the treatment of financial results under IFRS and indicated that it would solicit client feedback on a proposal to address the question of how to make adjustments to historical earnings and sales results that were calculated according to local GAAP to make a meaningful comparison with the latest IFRS financial results. This consultation paper proposes that in order to make five-year earnings comparable, MSCI would adjust historical earnings by adding back "amortization of goodwill". This proposal is detailed in Section V, below. MSCI has also examined two other alternatives, which are also detailed in Section V. In order to make sales comparable, MSCI proposes to make case-by-case adjustments wherever possible.

The proposals set forth in this Consultation may or may not be adopted in whole or in part by MSCI. If MSCI determines to make any change to MSCI's index methodology following this consultation, the change will be announced in advance.

II. SUMMARY OF RESEARCH

A majority of the companies subject to the EU regulation that before 2005 were reporting according to local GAAP reported their interim financial statements for the year 2005 under IFRS. Companies adopting IFRS for the purpose of interim reporting generally also provide restated numbers for the corresponding interim period of the previous year as well as for the latest annual financial statements.

Based on data available as of September 30, 2005, in aggregate for the MSCI Europe Standard Index, 62% of the securities transitioned to IFRS for their interim statements in 2005. 21% of the securities had not transitioned because they were already following IFRS or because they continue to follow US GAAP, while 16% of the securities had not published their first IFRS statements by September 2005.

MSCI has analyzed the extent and impact of the transition to IFRS by comparing the pre-IFRS and IFRS results of a sample of Standard index constituents for the latest fiscal year where those companies provided restated numbers for the corresponding interim period of the previous year. The impact on the index level ratios for the MSCI standard indices is small, although some individual securities do see a much greater impact. Key conclusions from this analysis are given below.

- **Earnings:** The impact on earnings is far greater than on sales or book value. In 47% of the cases analyzed, the impact is more than 10%. Aggregate earnings for all European Standard index constituents which transitioned to IFRS in 2005 increased by 3.37%. Aggregate earnings for all index constituents increased by 2.06%.

- **Impact of "amortization of goodwill":** A look at the securities with the largest percentage and aggregate impact on account of transition to IFRS suggests that discontinuation of "amortization of goodwill" explains the change in a majority of the cases. (refer **Appendix 1**)
- On adding back "amortization of goodwill" to pre-IFRS earnings, IFRS earnings show a fall of 2.44% as compared to a rise of 3.37% before adjustment for goodwill. This indicates that apart from goodwill amortization, all other accounting changes in aggregate have a negative impact on earnings
- MSCI's analysis also shows that as a practical matter given the information uniformly available the only item that historical pre-IFRS earnings data can be consistently adjusted for, to make it comparable to IFRS data is "amortization of goodwill". It is not possible to make adjustments to historical data for any other item impacted by the adoption of IFRS, unless restatements are provided by the companies.
- **Sales:** the impact on sales is marginal. In 81% of the cases analyzed, it is less than 5% and in almost 90% of the cases it is less than 10%. Aggregate sales for all European index constituents which have transitioned to IFRS fell by 2.09% whereas sales for all European companies in aggregate only dropped by 1.19%.

Book Value: in 64% of the cases analyzed, the impact is less than 10% and in 83% of the cases analyzed, the impact is less than 20%.

III. PRINCIPAL ACCOUNTING CHANGES

Some of the important accounting standards which have caused significant changes under IFRS are:

IFRS 2 – Share-based payments

- applies to grants of shares, share options or other equity instruments made after November 7, 2002
- fair value of the share based payments on the grant date should be expensed over the vesting period

IFRS 3 – Business combinations

- goodwill will no longer be allowed to be amortised but will be tested for impairment in accordance with IAS 36
- the discontinuation of goodwill amortisation will have a positive impact on the net profit of companies

IAS 12 – Income taxes

- deferred tax liability to be recognized in full rather than at a discounted value

IAS 19 – Employee benefits

- contributions payable to a defined contribution plan recognised as an expense
- companies to recognise a net defined benefit asset or liability comprising the present value of the defined benefit obligations at the balance sheet date, based on actuarial assumptions, net of the fair value of any plan assets at the balance sheet date

IAS 38 – Intangible Assets

- internally generated goodwill, brands, mastheads, publishing titles, customer lists and similar items not recognised as assets
- intangible assets arising from development recognised if specified criteria are met

- depreciable amount of an intangible asset with a finite life is amortised on a systematic basis over its useful life
- intangible assets with indefinite useful life are not amortised, but are tested for impairment at least annually

IAS 39 – Financial instruments - recognition

- financial assets and liabilities recognised at fair value as against the current practice of valuing them at cost

IAS 40 – Valuation of investment properties

- investment property initially recognised at cost and carried either at cost or fair value subsequent to initial recognition
- movements in fair value immediately recognised in profit or loss.

IV. EXTENT OF TRANSITION TO IFRS

Exhibit 1: Transition to IFRS for MSCI Standard Index constituents

Country (# of securities in Standard Index)	Companies following US GAAP and / or already following IFRS		Adopted IFRS by Sep 2005		first IFRS statements not released since mandatory date not reached	
	% weight in the Std index	% of number of companies in the Std index	% weight in the Std index	% of number of companies in the Std index	% weight in the Std index	% of number of companies in the Std index
European countries - DM						
United Kingdom (156)	0.4	0.6	71.8	56.4	27.8	42.9
France (62)	1.6	3.2	97.8	93.5	0.6	3.2
Germany (51)	75.4	90.2	15.1	5.9	9.5	3.9
Switzerland (37)	82.2	97.3	17.8	2.7	0.0	0.0
Spain (33)	0.0	0.0	100.0	100.0	0.0	0.0
Italy (41)	2.0	2.4	88.0	78.0	10.0	19.5
Netherland (26)	2.5	3.8	97.1	92.3	0.4	3.8
Sweden (46)	0.0	0.0	92.2	95.7	7.8	4.3
Finland (21)	15.5	14.3	84.5	85.7	0.0	0.0
Belgium (21)	32.5	52.4	65.6	38.1	1.9	9.5
Norway (18)	46.3	22.2	48.3	66.7	5.4	11.1
Denmark (20)	27.4	25.0	71.4	70.0	1.2	5.0
Ireland (17)	4.5	5.9	38.4	41.2	57.1	52.9
Greece (21)	26.9	19.0	69.0	66.7	4.0	14.3
Portugal (10)	0.0	0.0	100.0	100.0	0.0	0.0
Austria (14)	78.1	85.7	21.9	14.3	0.0	0.0
Europe (594)	**18.9**	**21.4**	**68.1**	**62.0**	**13.0**	**16.7**
Europe ex UK (438)	**29.8**	**28.8**	**65.9**	**63.9**	**4.2**	**7.3**
European countries - EM						
Poland (22)	45.3	22.7	54.7	77.3	0.0	0.0
Hungary (6)	58.0	83.3	42.0	16.7	0.0	0.0
Czech Republic (5)	95.2	80.0	4.8	20.0	0.0	0.0
Non-European countries						
Australia (82)	84.4	79.3	15.6	20.7	0.0	0.0
Hong Kong (40)	4.1	1.4	92.3	85.1	3.6	13.5
China (74)	1.0	2.5	95.8	87.5	3.1	10.0
Singapore (41)	14.9	9.8	76.0	75.6	9.1	14.6

1. Based on data available as on September 30, 2005.
2. Since companies are required to adopt IFRS only for financial years commencing on or after Jan 1, 2005, some companies had not reached the date of their first earnings release under IFRS by September 30, 2005.

In Europe, a major proportion of the companies by number and market capitalization in the United Kingdom, Ireland, Spain, France, Netherlands, Portugal and Italy have either reported or are expected to report in accordance with IFRS for periods within 2005.

In Austria, Switzerland, Germany, the Czech Republic and Hungary, a large proportion of companies by number and market capitalization have already been following IFRS. Accordingly, the overall impact for 2005 – at the country-level – of the transition to IFRS is relatively low.

Among the non-European companies, Hong Kong-listed companies, including China securities followed by MSCI, have shown a major transition. In Australia, most companies followed US GAAP and so far very few companies have adopted IFRS in 2005.

V. IMPACT OF TRANSITION TO IFRS ON THE FINANCIAL RESULTS OF COMPANIES

The analysis of the impact of transition to IFRS on companies' sales, earnings and book value has been made by comparing the pre-IFRS local GAAP numbers of MSCI Standard Index constituents for the fiscal year ended December 31, 2004 with the restated IFRS numbers provided by the companies for the same period. This is based on results reported by companies and updated by MSCI till the end of September 2005.

While the impact of transition to IFRS on the financial results of non-European companies has been marginal, it has been greater in the case of European companies. A summary of the analysis is outlined below.

IMPACT ON BOOK VALUE

Exhibit 2:Percentage impact on book value at the security-level

	Less than 5%	5% - 10%	10% - 20%	20% - 50%	more than 50%	Total
Number of securities	117	53	51	33	13	267
% of securities	44	20	19	12	5	100

An analysis of a sample of 267 MSCI standard constituents, distributed over 17 countries, shows that in almost two-thirds of the cases, the impact on book value was less than 10%. In 83% of the cases, the impact on book value was less than 20%. There are, however, some cases in which the impact of adoption of IFRS on book value was quite large.

Exhibits 3 and 4 highlight respectively some of the largest increases and decreases in book value due to the transition to IFRS.

Exhibit 3: Large book value increases due to adoption of IFRS

		Book value X FIF		Difference		
Security Name	**Country**	**Pre-IFRS**	**IFRS**	**Abs diff**	**% diff**	**Reason for increase in Book value**
Deutsche Telekom	DE	30,049	37,101	7,051	23	Discontinuation of amortisation of mobile licenses
Sanofi-Aventis	FR	36,365	41,974	5,609	15	Capitalisation of in-process R&D acquired with Aventis
Royal Bank of Scotland	GB	52,537	57,680	5,143	10	1) Timing of recognition of proposed dividends 2) Reversal of "amortisation of goodwill"
BNP Paribas	FR	37,039	39,655	2,617	7	Creation of "valuation reserves" of financial instruments
AXA	FR	26,740	29,134	2,394	9	Recording of financial assets at fair value

Note: The security-level book values are in USD millions and are adjusted for the security's foreign inclusion factor ('FIF'). "Book value X FIF" represents the numbers taken into account for the purpose of index-level calculations.

Exhibit 4: Large book value decreases due to adoption of IFRS

		Book value X FIF		Difference		
Security Name	**Country**	**Pre-IFRS**	**IFRS**	**Abs diff**	**% diff**	**Reason for decrease in book value**
BT Group	GB	7,399	86	-7,312	-99	Recognition of deficit in defined benefit pension schemes
Telefonica	ES	19,940	12,805	-7,135	-36	1) Goodwill and fair value adjustments 2) Reclassification of treasury shares
BAE Systems	GB	8,565	5,101	-3,464	-40	Recognition of deficit in defined benefit pension schemes as liability
Barclays	GB	33,463	30,490	-2,972	-9	1) Recognition of deficit in defined benefit pension schemes as liability 2) Accounting for life assurance contracts
Novartis	CH	28,716	26,609	-2,106	-7	1) Recognition of deficit in defined benefit pension schemes 2) Consolidation of employee share participation plan

Note: The security-level book values are in USD millions and are adjusted for the security's foreign inclusion factor ('FIF'). "Book value X FIF" represents the numbers taken into account for the purpose of index-level calculations.

IMPACT ON SALES

Exhibit 5: Analysis of index level sales

	for all Standard Index constituents	for Standard Index constituents, which have shifted to IFRS by Sep 2005
Country	% difference between aggregate IFRS sales and pre-IFRS sales	% difference between aggregate IFRS sales and pre-IFRS sales
United Kingdom	-2.91	-4.37
France	-1.16	-1.27
Germany	-0.04	-0.39
Switzerland	0.07	0.87
Spain	-1.16	-1.59
Italy	-1.79	-2.64
Netherland	0.71	0.93
Sweden	-0.20	-0.22
Finland	-0.56	-0.90
Belgium	-0.28	-0.94
Norway	0.00	-0.01
Denmark	-1.02	-2.05
Ireland	-0.75	-2.78
Greece	-0.73	-2.17
Austria	0.00	0.00
Portugal	-0.79	-0.89
Poland	-0.01	-0.20
Hungary	0.00	0.00
Czech Republic	0.00	0.00
Total	**-1.19**	**-2.09**

At the index level, the impact of the transition to IFRS on sales was marginal for the sampled companies. Aggregate sales for all European companies which had adopted IFRS by September2005 fell by 2.09%. due to the switch to IFRS. Since all companies had not reported according to IFRS for periods in 2005, the index-level impact was diluted. Consequently aggregated sales for all European companies at the index level aggregate dropped only by 1.19%.

Exhibit 6: % impact on sales at the security-level

	Less than 2%	2% - 5%	5% - 10%	10% - 20%	more than 20%	Total
Number of securities	195	31	23	21	8	278
% of securities	70	11	8	8	3	100

For 81% of the securities analyzed, the impact on sales is less than 5%. For almost 90% of the securities, it is less than 10%.

Exhibit 7 highlights some of the largest variations in sales due to transition to IFRS. The key reasons for variations in sales are exclusion of excise duty from sales, recognition of trading sales on net-basis and change in revenue recognition for contracts

Exhibit 7: Large variations in sales due to adoption of IFRS

			Sales X FIF		Difference		
Name of the security	**GICS Industry**	**Country**	**Pre-IFRS**	**IFRS**	**Abs diff**	**% diff**	**Reason for change in sales**
British American Tobacco	Tobacco	GB	45,927	14,544	-31,383	-68	Excise duty excluded from revenues.
Total	Oil, Gas & Consumable Fuels	FR	133,630	106,099	-27,531	-21	Certain transactions within the Trading sector now need to be presented on a net basis in revenues.
Scottish & Newcastle	Beverages	GB	6,667	4,852	-1,815	-27	Excise duty excluded from revenues.
Union Fenosa	Electric Utilities	ES	4,898	3,918	-980	-20	Distribution sales now need to be presented on a net basis in revenues.
SBM Offshore	Energy Equipment & Services	NL	1,375	1,612	237	17	Revenues from contract work in progress recognised under percentage of completion method, replacing the completed contract method.

Note: The security-level sales are in USD millions and are adjusted for the security's foreign inclusion factor ('FIF'). "Sales X FIF" represents the numbers taken into account for the purpose of index-level calculations.

IMPACT ON EARNINGS

Exhibit 8: Analysis of index level earnings

	for all Standard Index constituents	for Standard Index constituents, which have shifted to IFRS by Sep 2005	
Country	% difference between aggregate IFRS earnings and pre-IFRS earnings	% difference between aggregate IFRS earnings and pre-IFRS earnings	% difference between aggregate IFRS earnings and adjusted pre-IFRS earnings *
United Kingdom	-1.04	-1.66	-1.66
France	8.16	8.66	-1.36
Germany	3.52	24.39	-11.61
Switzerland	-0.30	-2.03	-2.03
Spain	2.93	3.57	-2.65
Italy	6.26	9.80	-7.86
Netherland	2.38	2.44	-2.29
Sweden	9.51	10.14	-8.84
Finland	10.00	12.99	8.85
Belgium	1.33	5.41	0.92
Norway	1.60	3.64	2.03
Denmark	5.07	10.15	-5.36
Ireland	-0.07	-0.17	-0.17
Greece	-5.70	-9.20	-9.20
Austria	1.57	6.96	6.96
Portugal	8.94	10.60	2.58
Poland	-0.06	-0.20	-0.37
Hungary	0.00	0.00	0.00
Czech Republic	0.00	0.00	0.00
Total	**2.06**	**3.37**	**-2.44**

Adjusted pre-IFRS earnings refer to pre-IFRS earnings, adjusted by adding back "amortization of goodwill". "Amortization of goodwill" has been added back to pre-IFRS earnings only for those securities where the impact of the transition to IFRS on earnings is more than 10% and has been adjusted for tax-effect using the country corporate tax rate when no other information was available.

In contrast to sales, the impact on earnings was much greater. Aggregate earnings for all European companies which had adopted IFRS by September 2005 increased by 3.37% as a result of the use of IFRS rather than local GAAP. As in the case of sales, since all companies had not adopted IFRS by September 2005, the index-level impact was diluted. Consequently, earnings for all European companies in aggregate increased by 2.06%.

The absolute impact in index-level earnings for various countries range from 0% to 10%. In most cases, the impact is positive.

For companies with the largest percentage and absolute change in earnings, in many cases discontinuation of goodwill explains a bulk of the earnings change due to adoption of IFRS. The only item for which historical pre-IFRS earnings data can be consistently adjusted to make it comparable to IFRS data is ‘amortization of goodwill’. It is not possible to make adjustments for any other item, unless restatements are provided by the companies.

Upon adjusting the pre-IFRS earnings results by adding back “amortization of goodwill”, the aggregate level of earnings for all European securities in the Standard Indices which have used IFRS results shows a decrease of 2.44% as compared to an increase of 3.37% before adjustment. This implies that apart from discontinuation of “amortization of goodwill”, all other accounting changes have, in aggregate, had a negative impact on earnings. Please note that in case of the United Kingdom and Ireland, since MSCI follows earnings before “amortization of goodwill”, there is no difference between pre-IFRS earnings and adjusted pre-IFRS earnings.

Exhibit 9: % impact on earnings at the security-level

	Less than 5%	5% - 10%	10% - 20%	20% - 50%	more than 50%	Total
% difference between IFRS earnings and pre-IFRS earninngs						
Number of securities	104	62	59	50	39	314
% of securities	33	20	19	16	12	100
% difference between IFRS earnings and adjusted pre-IFRS earninngs						
Number of securities	134	84	43	35	18	314
% of securities	43	27	14	11	6	100

Adjusted pre-IFRS earnings refer to pre-IFRS earnings, adjusted by adding back “amortization of goodwill”. “Amortization of goodwill” has been added back to pre-IFRS earnings only for those securities where the impact of the transition to IFRS on earnings is more than 10%.

In 47% of the securities analyzed, the impact on earnings is more than 10%. After adjusting the pre-IFRS earnings by adding back “amortization of goodwill”, the difference between such adjusted earnings and the IFRS earnings was reduced significantly. The percentage of cases with a difference of more than 10% dropped to 31%.

Exhibits 10 and 11 highlight some of the largest increases and decreases in earnings due to the transition to IFRS, based on the comparison between the pre-IFRS numbers for the fiscal year ended December 31, 2004 with the restated IFRS numbers provided by the companies. For the purpose of capturing reasons other than ‘amortization of goodwill’, large variations due to the discontinuation of amortization of goodwill have been excluded from Exhibit 10.

Exhibit 10: Large earnings increases due to adoption of IFRS and not goodwill related

		Earnings X FIF		Difference		
Security Name	**Country**	**Pre-IFRS**	**IFRS**	**Abs diff**	**% diff**	**Reason for increase in earnings**
Unibail Holding	FR	205	942	737	360	Valuation of investment property
Hammerson	GB	147	766	619	421	Valuation of investment property
Aegon	NL	1,988	2,301	313	16	Valuation of financial instruments
Michelin	FR	770	951	181	24	Fall in employee benefit costs
Gecina	FR	36	129	93	255	Valuation of investment property

Note: The security-level earnings are in USD millions and are adjusted for the security's foreign inclusion factor ('FIF'). "Earnings X FIF" represents the numbers taken into account for the purpose of index-level calculations.

Exhibit 11: Large earnings decreases due to adoption of IFRS

		Earnings X FIF		Difference		
Security Name	**Country**	**Pre-IFRS**	**IFRS**	**Abs diff**	**% diff**	**Reason for decrease in earnings**
ABN Amro Holding	NL	4,686	4,003	-683	-15	1) Valuation of financial instruments 2) Treatment of realized lossses from the sale of portfolio investments
Glaxosmithkline	GB	7,588	7,050	-538	-7	Fair value of share options now expensed over vesting period
Cap Gemini SA	FR	-411	-611	-200	-49	Cancellation of deferred tax discounting
Royal & Sun Alliance Ins	GB	434	246	-188	-43	Valuation of financial instruments
Zeltia	ES	-3	-19	-16	-652	Research & development expenses no longer capitalised

Note: The security-level earnings are in USD millions and are adjusted for the security's foreign inclusion factor ('FIF'). "Earnings X FIF" represents the numbers taken into account for the purpose of index-level calculations.

VI. IMPACT ON LONG-TERM HISTORICAL GROWTH TRENDS

MSCI computes Long-term historical Earnings per share Growth Trend ('LT his EPS G') and Long-term historical Sales per share Growth Trend ('LT his SPS G') by applying a regression to the previous four or five yearly EPS and SPS data, respectively. In order to compute a meaningful long-term historical growth trend for the EPS and SPS data, at least four years of comparable data are required.

As a result of the transition to IFRS, EPS and SPS numbers may become non-comparable with the past non-IFRS numbers on a security-level. This may result in distortion of Long-term EPS and SPS trends. The impact of the change will be felt primarily from the year 2006, when most companies that are transitioning will begin reporting their fiscal year under IFRS.

Outlined below are several alternative methodologies to ensure, to the extent possible, that only reasonably comparable sets of data are used in the computation of the Long-term EPS and SPS trends at a security-level. For earnings MSCI proposes to follow Alternative I. However, MSCI welcomes feedback on all the three alternatives. For sales, MSCI proposes to make case-by-case adjustments wherever possible.

The following terminology is used:

- Year 0 is defined as the last year for which annual financial statements are reported under non-IFRS accounting (in most cases, this is the fiscal year ending December 31, 2004)
- Year 1 is defined as the first year for which annual financial statements are reported under IFRS accounting (in most cases, fiscal year ending December 31, 2005)
- Years 2, 3 and so on are the years following Year 1
- Years -1, -2 and so on are the years prior to Year 0

In this context, please note that, for Year 0, MSCI will update both IFRS and non-IFRS numbers since companies will be providing a reconciliation/restatement of the profit or loss for this period to its profit or loss under IFRS for the same period as and when they shift to IFRS.

Until companies release financial statements for the Year 1 fiscal year and the results are updated, MSCI will use five years of non-IFRS data from Year -4 to Year 0.

A. SALES

Adjust historical sales on a case by case basis.

- Where the impact of adoption of IFRS on sales is less than 10%, MSCI would continue to use the existing pre-IFRS historical numbers with the current IFRS numbers.

- Where the adoption of IFRS has resulted in a more than 10% impact on sales, MSCI would conduct further analysis to identify those items for which adjustments can be made to historical sales, e.g., Years -1 to -3 to minimize the difference between the pre-IFRS and IFRS Sales.

- If such an adjustment does not bring down the difference between IFRS numbers and pre-IFRS numbers below 50%, Long-term Historical SPS growth trend will be treated as missing.

- Similarly, if the impact of adoption of IFRS on sales is more than 50% and MSCI finds that it is not possible to adjust historical sales because of lack of sufficient information, LT His SPS G will be treated as missing until MSCI has four years of comparable IFRS data.

B. EARNINGS

ALTERNATIVE I: Adjust historical earnings for goodwill amortization.

Along with IFRS results for Year 1, MSCI will also update Year 0 under IFRS using the reconciliation / restatements provided by the companies. Accordingly, MSCI will have two years of data based on IFRS standards.

- Where the impact of the use of IFRS on earnings is less than 10%, MSCI will continue to use the existing pre-IFRS historical numbers with the current IFRS numbers.

Where the use of IFRS changes earnings by more than 10%, MSCI will add back “amortization of goodwill” to the pre-IFRS earnings of the past years.

- If the difference between IFRS numbers and adjusted pre-IFRS (adjusted by adding back “amortization of goodwill”) continues to be above a threshold of 50%, it would imply that there are factors other than “amortization of goodwill” which have a substantial impact on earnings. In such case, Long-term Historical EPS growth trend will be treated as missing.

Illustration:

	Local GAAP (Reported Data)	IFRS (restated data from the company)	% Difference between IFRS and pre-IFRS data for Year 2004
Year	2004	2004	
EPS	27	45	66.67

In this case, the difference between pre-IFRS 2004 and IFRS 2004 is **66.67%.** Since the difference between the pre-IFRS and IFRS numbers is greater than 10%, MSCI would try to determine whether the impact on earnings is a result of discontinuance of “amortization of goodwill”.

Examination of possible scenarios based on the amount of “amortization of goodwill”:

	Scenario I	Scenario II	Scenario III
Pre-IFRS EPS for the year 2004	27	27	27
“amortization of goodwill” per share	15	2	Not available
Adjusted EPS for the year 2004	42	29	27
% difference as compared to IFRS EPS for 2004 (i.e. 45)	7%	55%	66.67%

Action:

Scenario I: Adjustment for “amortization of goodwill” reduces the difference between pre-IFRS earnings and IFRS earnings to 7%. This implies that “amortization of goodwill” accounts for the major part of the IFRS impact. In this case, MSCI would adjust the past three years for “amortization of goodwill” and use such adjusted numbers for the computation of the Long-term growth trend.

Scenario II: Even after adjustment for "amortization of goodwill", the difference between pre-IFRS earnings and IFRS earnings remains above 50%. This implies that "amortization of goodwill" does not account for the major part of the IFRS impact. In this case, LT His EPS G will be treated as missing until MSCI has four years of comparable IFRS data

Scenario III: If adjustment to pre-IFRS data is not possible due to non-availability of data in relation to "amortization of goodwill", LT His EPS G will be treated as missing until MSCI has four years of comparable IFRS data since the difference between pre-IFRS 2004 and IFRS 2004 is greater than 50%.

ALTERNATIVE II: Using pro forma numbers computed using a "percentage change" method

Until MSCI has five years of IFRS data, LT His EPS G and LT His SPS G will be calculated by using the following methodology:

Stage No.	Availability of IFRS data	Methodology for calculating long-term historical growth trends
1	After MSCI updates Year 1 using the IFRS financial statements released by the companies. (MSCI would have also updated Year 0 under IFRS using the reconciliation provided by the companies)	Use four years of non-IFRS data from Year -3 to Year 0 and pro forma non-IFRS numbers for Year 1. This will give five years of comparable non-IFRS numbers. MSCI will calculate the percentage change between the IFRS numbers for Year 0 and Year 1 and apply this percentage change to the non-IFRS of Year 0 to arrive at pro forma non-IFRS numbers for year 1.
2	After MSCI updates two years, i.e. Year 1 and Year 2 under IFRS. (MSCI would have also updated Year 0 under IFRS using the reconciliation provided by the companies)	Use three years of IFRS data from Year 0 to Year 2 and pro forma IFRS numbers for Year -1. This will give four years of comparable IFRS numbers. MSCI will calculate the percentage change between the pre-IFRS numbers for Year 0 and Year -1 and apply this percentage change to the IFRS of Year 0 to arrive at pro forma IFRS numbers for year -1.
3	After MSCI updates three years, i.e. Year 1, Year 2 and Year 3 under IFRS. (MSCI would have also updated Year 0 under IFRS using the reconciliation provided by the companies)	Use four years of IFRS data spanning from Year 0 to Year 3.

Illustration:

	Local Gaap						IFRS	
	Reported data					Pro forma pre-IFRS EPS for 2005*	Reported Data	
Year	2000	2001	2002	2003	2004		2004	2005
EPS	15	16.5	19	17.25	22		27	30
Numbers used for computing 5-year growth trend		16.5	19	17.25	22	24.4		

* Percentage change between IFRS 2004 and 2005 EPSs, 27 and 30 respectively, (i.e. 11.11%) when applied to 22 (the local GAAP 2004 EPS) results in a pro forma 2005 EPS of 24.44. This number is used with the set of four years of pre-IFRS data to compute the Long-term growth trend.

ALTERNATIVE III: Using pro forma numbers computed using an “absolute change” method

This method for arriving at a set of four or five years of comparable numbers is the same as Alternative II, except that under this method, the pro-forma numbers would be computed by applying the arithmetic difference instead of the percentage growth rate.

Under Stage No. 2, the pro forma non-IFRS numbers for Year 1 will be calculated by adjusting the non-IFRS numbers of Year 0 by the difference between IFRS data of Year 0 and Year 1. Under Stage No. 3, the pro forma IFRS numbers for Year -1 will be calculated by adjusting the IFRS based numbers of Year 0 by the difference between non-IFRS data of Year -1 and Year 0.

Illustration:

	Local Gaap						IFRS	
	Reported data					Pro forma pre-IFRS EPS for 2005*	Reported Data	
Year	2000	2001	2002	2003	2004		2004	2005
EPS	15	16.5	19	17.25	22		27	30
Numbers used for computing 5-year growth trend		16.5	19	17.25	22	25		

* Arithmetic difference between IFRS 2004 and 2005 EPSs, 27 and 30 respectively, (i.e. 3%) when added to 22 (the local GAAP 2004 EPS) results in a pro forma 2005 EPS of 25. This number is used with the set of four years of pre-IFRS data to compute the Long-term growth trend.

APPENDIX 1 - Cases of a large impact on earnings on a percentage basis by Country

FRANCE

Largest percentage increases in earnings on account of transition to IFRS

Name	GICS Industry	Currency	EPS Pre-IFRS	EPS IFRS	Difference Abs diff	Difference % diff	Goodwill as a % of total IFRS impact	Primary reason for shift in earnings
TECHNIP	Energy Equipment & Services	EUR	0.20	4.64	4.45	2278.72	109.52	Discontinuation of goodwill amortisation
UNIBAIL HOLDING	Real Estate	EUR	3.74	17.20	13.46	360.18	0.55	Gains on valuation of property
GECINA	Real Estate	EUR	3.24	11.53	8.29	255.99	0.00	Gains on valuation of property
THALES	Aerospace & Defense	EUR	1.15	1.97	0.82	71.21	120.21	Discontinuation of goodwill amortisation
VIVENDI UNIVERSAL	Media	EUR	0.82	1.33	0.52	63.18	120.74	Discontinuation of goodwill amortisation
VALEO	Auto Components	EUR	1.83	2.93	1.11	60.67	98.90	Discontinuation of goodwill amortisation
AXA	Insurance	EUR	1.19	1.84	0.64	54.13	84.58	Discontinuation of goodwill amortisation
PUBLICIS GROUPE	Media	EUR	1.41	2.15	0.73	52.06	130.99	Discontinuation of goodwill amortisation
SCHNEIDER ELECTRIC	Electrical Equipment	EUR	2.42	3.53	1.11	45.93	83.73	Discontinuation of goodwill amortisation

Largest percentage decreases in earnings on account of transition to IFRS

Name	GICS Industry	Currency	EPS Pre-IFRS	EPS IFRS	Difference Abs diff	Difference % diff	Goodwill as a % of total IFRS impact	Primary reason for shift in earnings
CAP GEMINI SA	IT Services	EUR	-2.73	-4.06	-1.33	-48.75	-29.14	Cancellation of deferred tax discounting

Note: In each of the countries, we have captured the largest percentage changes in earnings, for which information explaining the difference between pre-IFRS and IFRS earnings was available.

Country-level summary

A	Aggregate pre-IFRS earnings of companies who have shifted to IFRS (USD)	48,617,019,906
B	Aggregate IFRS earnings of companies who have shifted to IFRS (USD)	52,825,035,447
C	Aggregate change between pre-IFRS and IFRS earnings (B-A) (USD)	4,208,015,541
D	Aggregate differences as a % of aggregate pre-IFRS earnings (C/A)	8.66%
E	Aggregate absolute differences between pre-IFRS and IFRS earnings (USD)	7,240,991,829
F	Aggregate absolute differences as a % of aggregate pre-IFRS earnings (E/A)	14.89%
G	Aggregate pre-IFRS earnings post-adjustment for goodwill amortisation (USD)	53,553,626,642
H	Aggregate differences between goodwill adjusted pre-IFRS and IFRS earnings (B-G) (USD)	-728,591,195
I	Aggregate of differences post goodwill adjustment as a % of aggregate adjusted pre-IFRS earnings (H/G)	-1.36%

Key Observations:

- In France, a bulk of the increase can be attributed to goodwill amortization.
- Aggregate earnings for all standard constituents in France, which have adopted IFRS by September 30 2005, have increased by 8.66
- However, if pre-IFRS earnings are adjusted by adding back goodwill amortization and then comparing the result to IFRS earnings, the impact is negative (-1.36%).

SWEDEN

Largest percentage increases in earnings on account of transition to IFRS

			EPS		Difference			
Name	**GICS Industry**	**Currency**	**Pre-IFRS**	**IFRS**	**Abs diff**	**% diff**	**Goodwill as a % of total IFRS impact**	**Primary reason for shift in earnings**
SKANDIA FORSAKRING	Insurance	SEK	0.09	0.19	0.10	107.63	12.03	Valuation of financial instruments
TELE2 B	Diversified Telecommunication Services	SEK	4.30	7.74	3.45	80.23	373.92	Discontinuation of goodwill amortisation
SECURITAS B	Commercial Services & Supplies	SEK	4.02	6.98	2.96	73.62	106.46	Discontinuation of goodwill amortisation
ENIRO	Media	SEK	2.79	4.56	1.77	63.38	125.29	Discontinuation of goodwill amortisation
ASSA ABLOY B	Building Products	SEK	4.09	6.42	2.33	57.12	114.52	Discontinuation of goodwill amortisation
CASTELLUM	Real Estate	SEK	14.29	22.34	8.05	56.31	0.00	Valuation of investment property
ALFA LAVAL	Machinery	SEK	5.16	7.52	2.36	45.65	72.72	Discontinuation of goodwill amortisation
SCA SV CELLULOSA B	Paper & Forest Products	SEK	15.48	21.92	6.44	41.60	80.12	Discontinuation of goodwill amortisation

Country-level summary

A	Aggregate pre-IFRS earnings of companies who have shifted to IFRS (USD)	11,482,485,063
B	Aggregate IFRS earnings of companies who have shifted to IFRS (USD)	12,646,960,092
C	Aggregate change between pre-IFRS and IFRS earnings (B-A) (USD)	1,164,475,029
D	Aggregate differences as a % of aggregate pre-IFRS earnings (C/A)	10.14%
E	Aggregate absolute differences between pre-IFRS and IFRS earnings (USD)	2,021,650,185
F	Aggregate absolute differences as a % of aggregate pre-IFRS earnings (E/A)	17.61%
G	Aggregate pre-IFRS earnings post-adjustment for goodwill amortisation (USD)	13,873,758,799
H	Aggregate differences between goodwill adjusted pre-IFRS and IFRS earnings (B-G) (USD)	-1,226,798,707
I	Aggregate of differences post goodwill adjustment as a % of aggregate adjusted pre-IFRS earnings (H/G)	-8.84%

Key Observations:

- No large negative impact cases
- In Sweden, a majority of the increases can be attributed to goodwill amortization.
- Aggregate earnings for all standard constituents in Sweden, which have adopted IFRS by September 30 2005, have increased by 10.14%.However, if pre-IFRS earnings are adjusted by adding back goodwill amortization and then comparing the result to IFRS earnings, the impact is negative (-8.84%).

SPAIN

Largest percentage increases in earnings on account of transition to IFRS

			EPS		Difference			
Name	GICS Industry	Currency	Pre-IFRS	IFRS	Abs diff	% diff	Goodwill as a % of total IFRS impact	Primary reason for shift in earnings
ALTADIS	Tobacco	EUR	1.46	1.90	0.45	30.51	124.45	Discontinuation of goodwill amortisation
MAPFRE (CORPORACION)	Insurance	EUR	0.77	0.92	0.15	19.66	89.33	Discontinuation of goodwill amortisation
REPSOL YPF	Oil, Gas & Consumable Fuels	EUR	1.96	2.28	0.32	16.38	44.90	Discontinuation of goodwill amortisation
BSCH BCO SANTANDER CENTR	Commercial Banks	EUR	0.50	0.58	0.08	15.00	131.60	Discontinuation of goodwill amortisation

Largest percentage decreases in earnings on account of transition to IFRS

			EPS		Difference			
Name	GICS Industry	Currency	Pre-IFRS	IFRS	Abs diff	% diff	Goodwill as a % of total IFRS impact	Primary reason for shift in earnings
ZELTIA	Biotechnology	EUR	-0.01	-0.10	-0.09	-635.93	-6.10	R & D Expenses.
SACYR VALLEHERMOSO	Construction & Engineering	EUR	1.41	1.04	-0.37	-26.29	-11.85	Revision in depreciation rates
BANCO POPULAR ESPANOL	Commercial Banks	EUR	3.52	2.89	-0.64	-18.06	-13.44	Credit loss allowances

Country-level summary

A	Aggregate pre-IFRS earnings of companies who have shifted to IFRS (USD)	16,821,576,925
B	Aggregate IFRS earnings of companies who have shifted to IFRS (USD)	17,422,110,054
C	Aggregate change between pre-IFRS and IFRS earnings (B-A) (USD)	600,533,129
D	Aggregate differences as a % of aggregate pre-IFRS earnings (C/A)	3.57%
E	Aggregate absolute differences between pre-IFRS and IFRS earnings (USD)	1,904,914,818
F	Aggregate absolute differences as a % of aggregate pre-IFRS earnings (E/A)	11.32%
G	Aggregate pre-IFRS earnings post-adjustment for goodwill amortisation (USD)	17,896,248,907
H	Aggregate differences between goodwill adjusted pre-IFRS and IFRS earnings (B-G) (USD)	-474,138,853
I	Aggregate of differences post goodwill adjustment as a % of aggregate adjusted pre-IFRS earnings (H/G)	-2.65%

Key Observations:

- In Spain, all of the largest cases of positive impact of transition to IFRS can be attributed to Goodwill amortization.
- Aggregate earnings for all standard constituents in Spain, which have adopted IFRS by September 30 2005, have increased by 3.57%.However, if pre-IFRS earnings are adjusted by adding back goodwill amortization and then compared to IFRS earnings, the impact is negative (-2.65%).

ITALY

Largest percentage increases in earnings on account of transition to IFRS

Name	GICS Industry	Currency	EPS Pre-IFRS	EPS IFRS	Difference Abs diff	Difference % diff	Goodwill as a % of total IFRS impact	Primary reason for shift in earnings
SEAT P. GIALLE ORD (NEW)	Media	EUR	-0.01	0.01	0.02	179.76	116.77	Discontinuation of goodwill amortisation
EDISON ORD	Independent Power Producers & Energy Traders	EUR	0.04	0.08	0.05	128.39	104.02	Discontinuation of goodwill amortisation
TELECOM ITALIA ORD	Diversified Telecommunication Services	EUR	0.07	0.14	0.06	86.66	167.53	Discontinuation of goodwill amortisation
TELECOM ITALIA RNC	Diversified Telecommunication Services	EUR	0.07	0.14	0.06	86.66	167.53	Discontinuation of goodwill amortisation
AUTOGRILL	Hotels, Restaurants & Leisure	EUR	0.21	0.37	0.16	76.93	144.33	Discontinuation of goodwill amortisation
TELECOM ITALIA MEDIA ORD	Internet Software & Services	EUR	-0.02	-0.01	0.01	52.45	99.30	Discontinuation of goodwill amortisation
LOTTOMATICA (NEW)	Hotels, Restaurants & Leisure	EUR	0.82	1.10	0.27	33.31	221.66	Discontinuation of goodwill amortisation

Largest percentage decreases in earnings on account of transition to IFRS

Name	GICS Industry	Currency	EPS Pre-IFRS	EPS IFRS	Difference Abs diff	Difference % diff	Goodwill as a % of total IFRS impact	Primary reason for shift in earnings
CAPITALIA	Commercial Banks	EUR	0.01	-0.02	-0.03	-386.49	-164.34	Valuation of financial instruments

Country-level summary

A	Aggregate pre-IFRS earnings of companies who have shifted to IFRS (USD)	12,213,941,171
B	Aggregate IFRS earnings of companies who have shifted to IFRS (USD)	13,411,171,414
C	Aggregate change between pre-IFRS and IFRS earnings (B-A) (USD)	1,197,230,243
D	Aggregate differences as a % of aggregate pre-IFRS earnings (C/A)	9.80%
E	Aggregate absolute differences between pre-IFRS and IFRS earnings (USD)	2,056,731,024
F	Aggregate absolute differences as a % of aggregate pre-IFRS earnings (E/A)	16.84%
G	Aggregate pre-IFRS earnings post-adjustment for goodwill amortisation (USD)	14,554,943,371
H	Aggregate differences between goodwill adjusted pre-IFRS and IFRS earnings (B-G) (USD)	-1,143,771,956
I	Aggregate of differences post goodwill adjustment as a % of aggregate adjusted pre-IFRS earnings (H/G)	-7.86%

Key Observations:

- In Italy, all of the largest cases of positive impact of transition to IFRS can be attributed to Goodwill amortization.
- Aggregate earnings for all standard constituents in Italy, which have adopted IFRS by September 30, 2005, have increased by 9.8%.
- However, if pre-IFRS earnings are adjusted by adding back goodwill amortization and then compared to IFRS earnings, the impact is negative (-7.86%). This implies that in case of Italy, apart from "discontinuation of goodwill", other accounting changes have had a negative impact on earnings.

UNITED KINGDOM

Largest percentage increases in earnings on account of transition to IFRS

Name	GICS Industry	Currency	EPS Pre-IFRS	EPS IFRS	Difference Abs diff	Difference % diff	Goodwill as a % of total IFRS impact	Primary reason for shift in earnings
HAMMERSON	Real Estate	GBP	0.30	1.56	1.26	420.67	0.00	Gains on valuation of property
IMPERIAL CHEMICAL ICI	Chemicals	GBP	0.22	0.26	0.04	17.35	0.00	Reversal of employee benefit costs
SCHRODERS	Capital Markets	GBP	0.46	0.54	0.08	16.61	0.00	Reversal of share-based payment costs and employee benefit costs

Largest percentage decreases in earnings on account of transition to IFRS

Name	GICS Industry	Currency	EPS Pre-IFRS	EPS IFRS	Difference Abs diff	Difference % diff	Goodwill as a % of total IFRS impact	Primary reason for shift in earnings
ROYAL & SUN ALLIANCE INS	Insurance	GBP	0.08	0.05	-0.04	-43.21	0.00	Valuation of financial instruments
CATTLES	Consumer Finance	GBP	0.30	0.22	-0.08	-27.72	0.00	Provision for financial instruments
SERCO GROUP	Commercial Services & Supplies	GBP	0.12	0.10	-0.02	-17.13	0.00	Valuation of intangible assets

Country-level summary

A	Aggregate pre-IFRS earnings of companies who have shifted to IFRS (USD)	104,327,898,016
B	Aggregate IFRS earnings of companies who have shifted to IFRS (USD)	102,591,212,944
C	Aggregate change between pre-IFRS and IFRS earnings (B-A) (USD)	-1,736,685,072
D	Aggregate differences as a % of aggregate pre-IFRS earnings (C/A)	-1.66%
E	Aggregate absolute differences between pre-IFRS and IFRS earnings (USD)	9,035,491,815
F	Aggregate absolute differences as a % of aggregate pre-IFRS earnings (E/A)	8.66%

Key Observations:

- In case of the United Kingdom, MSCI follows earnings before “amortization of goodwill”. Therefore, discontinuation of goodwill amortization does not impact earnings. However, we still see some large changes at the company level for reasons other than the treatment of goodwill.

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