



# Getting Ready for IFRS: *Top 10 Actions to Take Now*

KPMG in Canada

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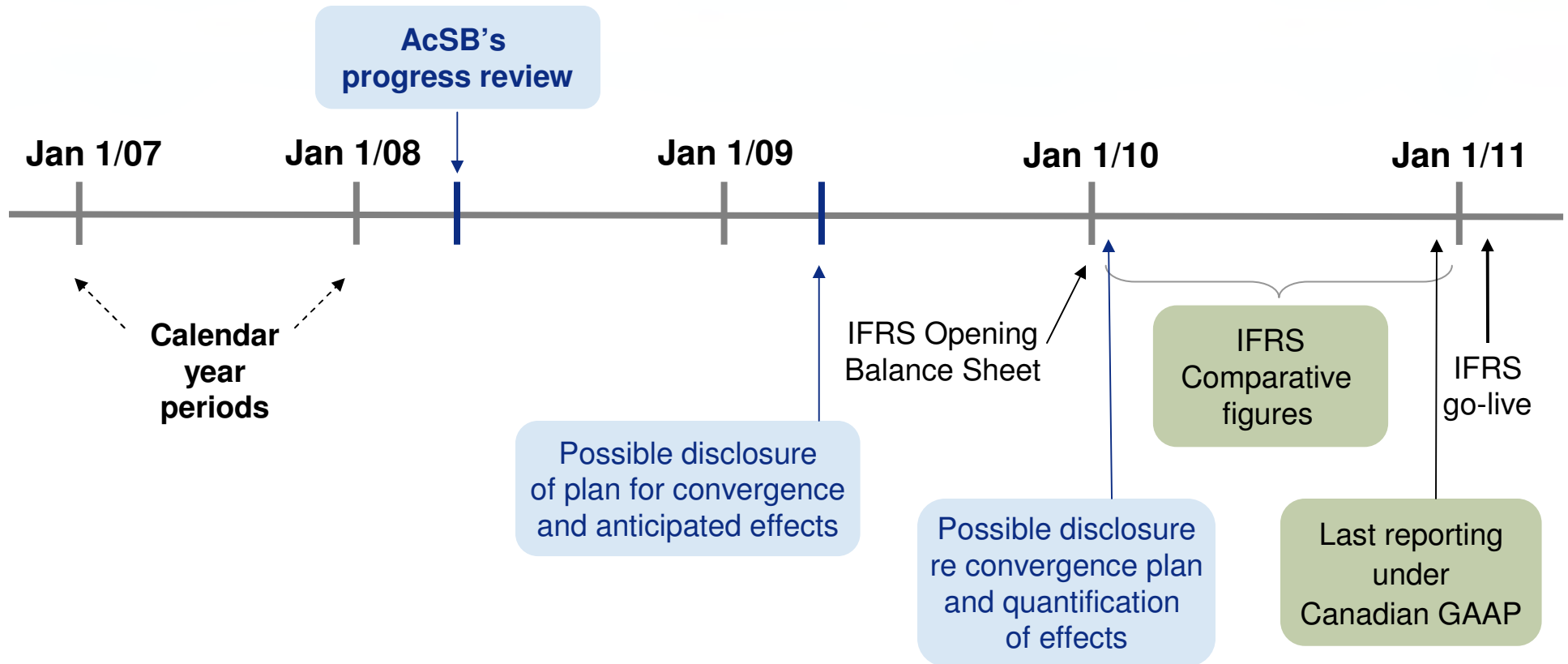
# Today's agenda

- **How will Canada's transition to IFRS affect your enterprise?**
- **Top 10 actions to take now**
- **Questions**

# Canada's transition to IFRS

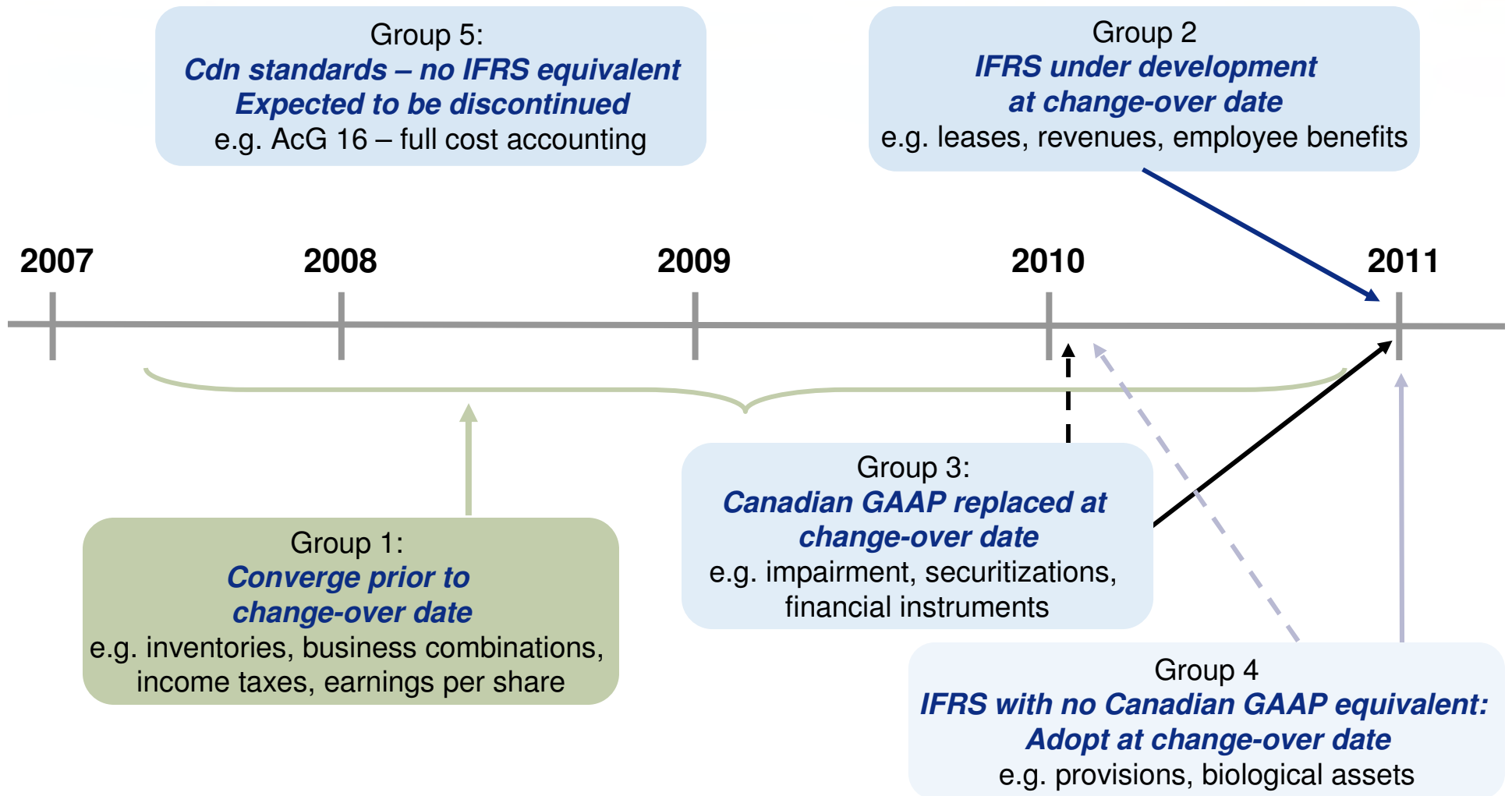
- **Who is affected – “publicly accountable enterprises”**
- **To be adopted by**
  - All “profit-oriented” enterprises, unless
    - Securities not publicly listed
    - Do not hold assets in fiduciary capacity for broad group of outsiders
  - Government business enterprises (recent PSAB exposure draft)
- **Currently an SEC registrant could choose US GAAP**

# Timeline for Canada's adoption of IFRS



**No "quiet period" until 2011 –  
"accounting standards fatigue" will continue through 2009**

# Phased convergence with IFRS – AcSB's five categories



# What does this mean to you?

- **The clock is ticking...**
- **Will likely have to disclose transition plans in your 2008 annual filings & anticipated impact in 2009 filings**
- **Your real deadline is 2009**
  - to make decisions with accounting implications
  - to be ready to create January 1, 2010 opening balance sheet and restate 2010 results for comparative purposes
- **Learn from others' experiences in making the change**

# Action 1:

## Understand key differences in IFRS vs. Canadian GAAP *for your enterprise*

# IFRS versus Canadian GAAP:

## *Our focus today*

- **Explain the basis of IFRS**
- **Review general similarities and differences in the two sets of standards**
- **Make you aware of areas of major difference**
- **Use specific standards to illustrate the extent to which they can differ from Canadian GAAP**
- **Emphasize that ... *'similar' doesn't mean 'the same'***

# International Financial Reporting Standards

- Based on International Accounting Standards
- Established by the IASB



# IFRS versus Canadian GAAP – *Similarities*

- **Comprehensive set of principles-based standards**
- **Similar to Canadian GAAP in structure and form**
- **Similar basic concepts and recognition / measurement principles**
- **Similar structure and content of financial statements**
- **Many standards in IFRS provide approach similar to Canadian GAAP**

# IFRS versus Canadian GAAP – *Differences*

- **Fewer bright lines and rules**
- **Some standards in IFRS differ considerably from Canadian GAAP – e.g. impairment and provisions**
- **More accounting policy choices**

*Applying IFRS requires more professional judgement and results in greater volume of disclosures*

- ***Many differences in application/interpretation***

**BE CAREFUL – The devil is in the detail!**

# IFRS accounting policies

- **IFRS has a “hierarchy” for selecting accounting policies**
  1. Apply the specific IFRS standard / interpretation; consider any relevant implementation guidance
  2. Refer to other IFRS standards / interpretations dealing with similar issues
  3. IFRS Framework
  4. Consider pronouncements of other standard-setting bodies (with similar conceptual framework)
    - US GAAP *may* be appropriate when IFRS is silent, provided it is not inconsistent with either IFRS Framework or guidance in IFRS standards for similar issues
      - *Use caution!*

# IFRS versus Canadian GAAP:

## *Standards with more significant differences*

- **Inventories**
- **Impairment of assets \***
- **Provisions (incl. asset retirement obligations)**
- **Financial instruments & hedging**
- **Leases**
- **Property, plant and equipment**
- **Employee benefits**
- **Securizations \***
- **Stock-based compensation**
- **Revenue recognition**
- **Accounting for income taxes & tax uncertainties**
- **Consolidations, SPEs, investments, JVs**
- **Rate-regulated operations \***
- **Industry-specific issues – insurance, extractive industries**

*\* Fundamentally different from Canadian GAAP*

# Inventories – *Significant changes*

- **Extensive guidance on determination of cost**
  - may be consistent with past practice; may be different
- **Cost includes fixed and variable overhead that**
  - includes depreciation and maintenance of factory and equipment
  - must be allocated based on normal capacity
- **Cost excludes abnormal waste, storage, admin overhead and financing component of deferred settlement terms**

# Inventories – *Significant changes*

- **Measure at lower of cost and net realizable value**
  - Replacement cost *not* an acceptable proxy for NRV
  - NRV less normal profit margin *not* acceptable
- **Prohibits use of the LIFO cost formula**
- **Permits use of retail inventory costing method if the results approximate cost**
- **Requires reversal of write-downs in future periods**
- **Requires certain major spare parts to be treated as PP&E, not inventory**

# Impairment – *Summary of approach*

## IFRS has one general impairment standard

### *IFRS – “1-step process”*

- **Recoverable amount is higher of**
  - fair value less cost to sell
  - value in use (discounted CF)
- **Discounting required in**
  - evaluation stage

### *Canadian GAAP – “2-step process”*

For an asset in use, undiscounted future cash flows from use establish recoverability and fair value used for the impairment calculation

Discounting occurs only in the valuation stage

***Impairments are more likely under IFRS!!***

# Impairment – *Long-lived assets and finite-life intangible assets*

- **Timing of impairment tests same as Canadian GAAP**
- **Estimate recoverable amount for**
  - individual asset or, if not possible
  - the asset's cash-generating unit
- **Apply CGU concept when asset does not generate cash flows independent from other assets**
  - similar to “asset group” but could have differences
- **Presume future cash flows beyond initial 5 years not reliable – no projected increases after year 5**
- **Reverse impairment charges if circumstances change**

# Impairment – *Testing goodwill for impairment under IFRS*

- **Allocate goodwill post-acquisition to CGUs or groups of CGUs**
  - expected to benefit from combination
  - at lowest level at which goodwill is monitored  
*(level could be lower than under Canadian GAAP)*
  - cannot be larger than a segment
- **One-step impairment test – factor in discounting at impairment evaluation stage**
- **Use “value in use” measurements – base on entity specific assessments not marketplace assumptions**

# Property Plant & Equipment – *Recognition and measurement*

- **Major spare parts – *must be treated as PP&E***
- **Components approach – *more rigorously applied and broader than under Canadian GAAP***
  - On initial recognition, allocate cost to significant parts of the asset (including non-physical components such as major overhaul / inspection)

# PP&E – *Recognition and measurement (cont'd)*

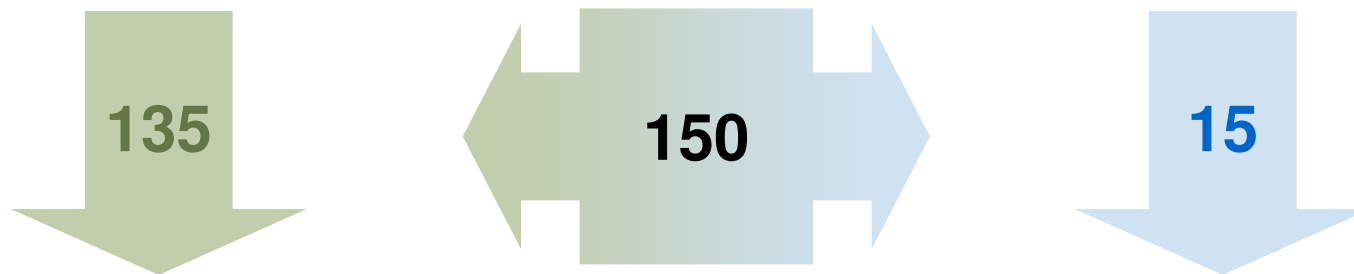
- **Borrowing costs directly attributable to construction or production of “qualifying” assets – *must be capitalized / extensive guidance provided***
- **Subsequent measurement options**
  - Cost model or revaluation model  
(record a fair value through equity)
  - Apply to all items in a category of PP&E

# PP&E – *Components approach: an illustration*

## Boiler costs \$150

Useful life – 10 years

Major overhaul / inspection after three years – estimated overhaul cost \$15



Depreciate over 10 years

- a) Depreciate over three years
- b) Capitalize subsequent overhaul costs when incurred

# IFRS versus Canadian GAAP: *Standards with more significant differences*

- *Inventories*
- *Impairment of assets* \*
- Provisions (incl. asset retirement obligations)
- Financial instruments & hedging
- Leases
- Property, plant and equipment
- Employee benefits
- Securitizations \*
- Stock-based compensation
- Revenue recognition
- Accounting for income taxes & tax uncertainties
- Consolidations, SPEs, investments, JVs
- Rate-regulated operations \*
- Industry-specific issues – insurance, extractive industries

***And don't forget all the other standards!***

*\* Fundamentally different from Canadian GAAP*

## **Action 2:**

### **Carefully consider your options**

- **IFRS 1**
- **Choices for SEC registrants**

## **Action 2: Carefully consider your options**

### ***IFRS 1 – First-time adoption of IFRS***

- **General principle is retrospective application**  
**– *restate as though always applied IFRS***
- **Provides some relief the first time an entity fully adopts IFRS**
- **Requires certain disclosures and reconciliations on adoption**
- **Contains mandatory exemptions and certain elective exemptions on applying the new basis of accounting**

***Evaluate available exemptions –  
both the impact on conversion effort and  
impact on post-changeover reported earnings***

# First-time adoption

## – *General requirements*

- **Select IFRS accounting policies**
  - Best approach vs. easiest
  - Consider industry counterparts in IFRS countries
- **Recognize / derecognize where necessary**
  - Liabilities (e.g. future losses, asset retirement obligations, onerous contracts)
  - Special purpose entities
  - Assets (pre-operating costs, securitizations)

# First-time adoption

## – *General requirements (cont'd)*

- **Re-measure**
  - Where basis has changed (e.g. from cost to fair value)
  - Where discounting is required/prohibited (e.g. provisions, impairments)
  - Revise estimates for errors only, not new information
  - Reversal of past impairment charges, other than goodwill
- **Reclassify**
  - Between captions or classification (e.g. future income taxes, debt refinanced post balance sheet date)

# IFRS 1 – *Types of exemptions*

Two types of exemptions from  
“general rule” of retrospective application

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graph TD; A["Two types of exemptions from 'general rule' of retrospective application"] --> B["Retrospective application prohibited"]; A --> C["Elective exemptions include"]; B --- B1["Hedge accounting"]; B --- B2["Estimates"]; C --- C1["Deemed cost"]; C --- C2["Actuarial gains and losses"]; C --- C3["Cumulative translation differences"]; C --- C4["Share-based payment transactions"];
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## Retrospective application prohibited

Hedge accounting

Estimates

## Elective exemptions include

Deemed cost

Actuarial gains and losses

Cumulative translation differences

Share-based payment transactions

***Can pick and choose elective exemptions!***

# IFRS 1 – *Deemed cost exemption*

- **Used for PP&E – can elect for individual items**
- **Allows cost basis to be adjusted to fair value (with corresponding adjustment to equity)**
- **Can use fair value at transition date, or possibly roll forward of revaluations made under Canadian GAAP**
- **Why would you elect to use?**
  - Trade off higher future depreciation charges with additional effort of addressing componentization of PP&E, adjustment of capitalized of interest

# IFRS 1 –

## *Actuarial gains / losses exemption*

- **Allows for unamortized actuarial gains / losses to be reset to zero (with corresponding adjustment to equity), even though will use corridor approach going forward**
- **Why would you decide to use the election?**
  - Avoid the reconstruction of unamortized pools of actuarial gains and losses from inception of plan
  - If in a position of cumulative unamortized losses, can avoid their subsequent recognition through the P&L

# IFRS 1 –


## *Cumulative translation adjustment exemption*

- **Can be used to reset CTA to zero on adoption of IFRS (with corresponding adjustment to retained earnings)**
- **Why would you elect to use the exemption?**
  - If cumulative FX losses, avoids their subsequent realization through the P&L
  - Avoids assessing if CTA was relieved in circumstances where no drawdown permitted under IFRS

## Action 2: Carefully consider your options

### – *What options do SEC registrants have?*

- **First decision – *Adopt IFRS or US GAAP?***
- **Second decision – When to do so?**
- **SEC proposal – Allow foreign private issuers to file F/S using IFRS without reconciliation to US GAAP**
- **SEC concept release – Provide same option for domestic US issuers**
- **Still unresolved**
  - How many years of comparative information for SEC?
  - CSA response
- ***Assess the pros and cons for your company***



# **Action 3:**

## **Raise awareness throughout your organization**

## Action 3 – *Raise awareness throughout your organization*



### Mobilize organization for the conversion

- Alert senior management to the potential effect on reported financial results and business operations
- Engage all relevant functions in the business – HR, Legal, Tax, Treasury, Sales, Operations
- Identify and involve the right people – core team, extended resources, project manager, steering group – and ensure they will be available
- Secure senior management's support – *essential early*

# Experiences from overseas

- **Companies found that they**
- **Underestimated the effort needed to convert**
  - it was more than just an accounting exercise!
- **Waited too long to get started**
  - spent too little time upfront in planning phase
- **Suffered from poor project management**
  - didn't create a formal process for identifying issues
- **Required significant systems upgrades / adjustments (IT and management reporting systems)**
  - Needed to renegotiate contracts (e.g. bank and compensation agreements)



## Action 4:

# Establish a formal project plan

# Action 4 – *Establish a formal project plan*



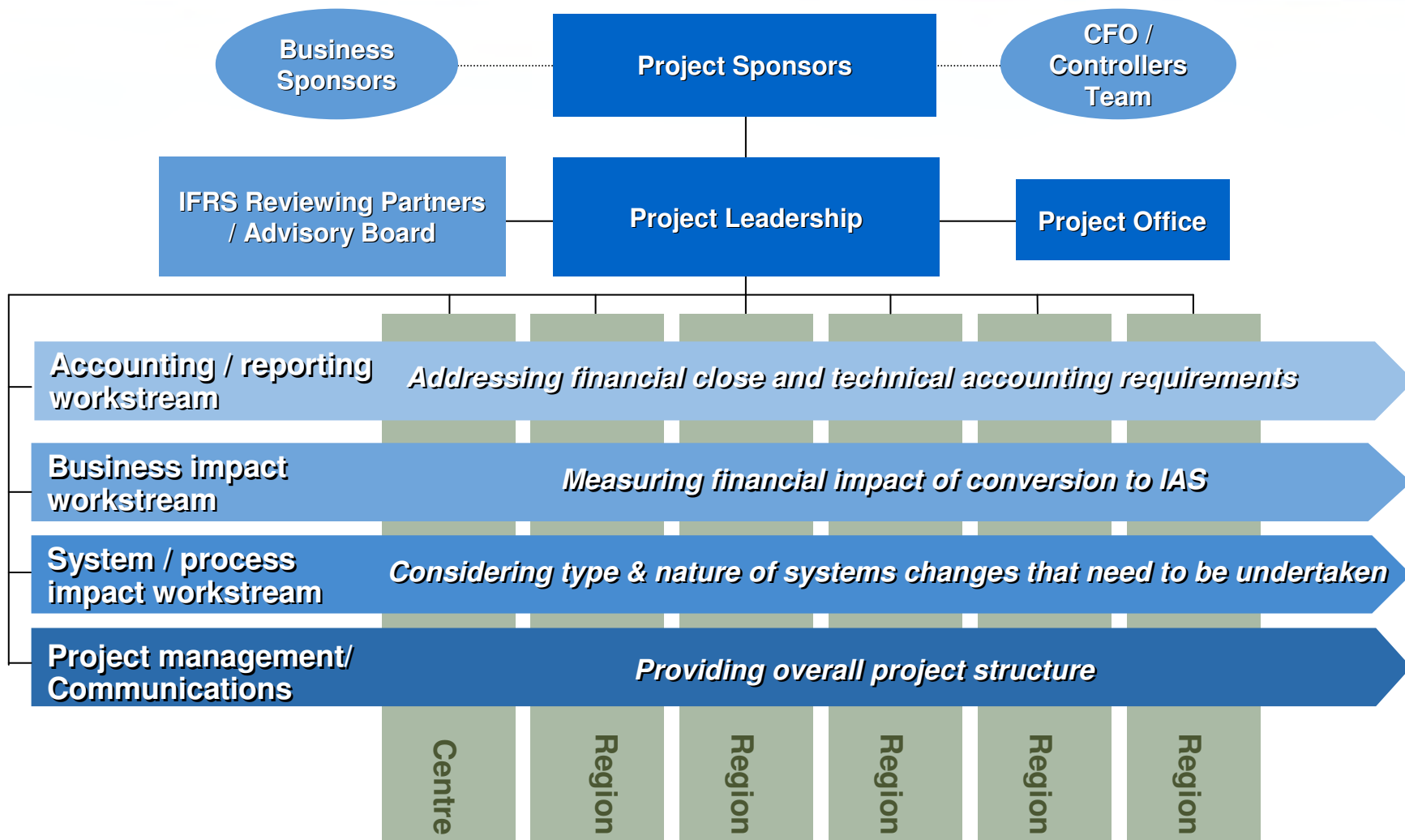
## Assess impact and plan conversion

- Identify major affected areas in the organization
- Do a “gap analysis”– acctg standards, policies, procedures
- Agree on timelines and determine priorities
- Evaluate reporting alternatives
- Evaluate information requirements & demand on IT system
- Develop master conversion plan and resource requirements
- Conduct training needs assessment

# Project planning and governance

- **Dedicated project management is a critical success factor for your transition project**
- **Ensure the plan is realistic in terms of timescales and specific accountabilities for all tasks – allow for slippage**
- **Revisit the plan regularly ...or else it will quickly become redundant**
- **Most significant challenge will be managing a virtual team over an extended time-period and maintaining the momentum of the project**
- **If you start doing work on accounting differences without a clearly defined plan and approach – you run the risk of missing key aspects of what project should cover**

# Project planning and governance



# Training and training strategy

- **Don't underestimate time to train finance/operations staff**
- **Generic training only useful early on – then tailor to company**
- **Timing of training – critical for its effectiveness**
- **Consider most effective training method for target audience**
- **To embed IFRS knowledge, people need opportunity to actually restate real numbers**
  - Try to build a dry run into the restatement plan – test finance staff's understanding

## **Action 5:**

**Consider the impact on  
your systems and processes**

# IT and systems issues

- **Assess current ERP and GL systems**
  - *adequately capture all required information?*
- **Engage the IT team early – appropriately modify data collection processes and create systems budgets**
- **Seek to embed and automate data collection**
- **Elect to embed IFRS in local ledgers where appropriate**
- **Need a contingency plan**
  - *what if strategy for collecting data isn't feasible?*
- **Dry-run your data collection process**
  - *check integrity of your numbers*



## **Action 6:**

# **Link IFRS with your internal control certification project**

# Link to internal control certification process

- **Assess the implications of IFRS on**
  - Accounting policy development and rollout
  - Development and approval of management estimates
  - Technical financial reporting capabilities in complex areas
- **Mitigate the risk of new control deficiencies**
  - Properly plan for new and enhanced internal controls as part of your IFRS conversion
  - Assess internal control design for accounting policy management as well as financial close processes
  - Be cognizant of the impact of manual work-arounds
  - Budget for necessary technical recruiting and training

## **Action 7:**

**Focus on the big picture –  
*enterprise-wide impacts***

# Enterprise-wide implications of change to IFRS

- **Changing your “accounting language” – implications for**
  - Planning and budgeting
  - Performance indicators, including compensation plans
  - Financing, contracts, agreements, covenants
- **Identify who will need education or communication**
  - Internal staff, Investor Relations, stakeholders – Board, audit committee, auditors
  - Establish an issues-management process
  - Manage expectations

## **Action 8:**

**Develop a strategy  
for external stakeholders**

# External stakeholders and disclosure

- **Lesson learned**
  - External communications left until forced to look at them
  - Sometimes caught unaware
- **Investors, analysts, brokers**
  - Need to understand likely IFRS impact on company and industry
  - Plan external disclosures early in the process
  - Manage expectations
- **Industry collaboration and communication**
  - Likely common industry issues on adoption

# Auditor involvement

- **Explicit acknowledgement on the part of the reporting entity for frequent auditor involvement**
- **Audit involvement should be an integral part of the project governance process**
- **Clear specification is made of what is to be expected and when for all key deliverables, including timely IFRS technical partner involvement**

# Action 9:

## Actively monitor your progress

# Monitor your progress

- **Ensure project plan is realistic**
  - Timescales
  - Accountabilities for all tasks
- **Two levels of plan**
  - High level milestones
  - Detail level for day-to-day operations
- **Revisit plan at least bi-weekly or it will quickly become redundant**
- **REMEMBER ... *your real deadline is Fall 2009!***

## **Action 10:**

**If you haven't already begun...  
*get going!!***

## In summary... Top 10 actions to take now

1. Understand key differences: IFRS vs. Canadian GAAP
2. Carefully consider your options
3. Raise awareness throughout your organization
4. Establish a formal project plan
5. Consider the impact on your systems and processes
6. Link to your internal control certification program
7. Focus on the big picture – enterprise-wide impacts
8. Develop a strategy for external stakeholders
9. Actively monitor your progress
10. If you haven't already begun... *get going!!*

# Information to assist you

- **Copies available as you leave today**
  - *Managing the Transition to IFRS: The journey to 2011*
  - *Managing the Transition to IFRS: Special considerations for SEC registrants*
  - *Financial Reporting by Private Companies: Evaluating the options*
- **Visit our Web site for many other resources**  
[www.kpmg.ca/ifrs](http://www.kpmg.ca/ifrs)

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