

# Sharpening your focus: Overseeing IFRS conversion through 2010

Reprinted from *Canadian Audit Committee Update*, Issue 2009-02

With relatively few audit committee and board meetings remaining until the actual IFRS changeover date, where should you be focusing your oversight?

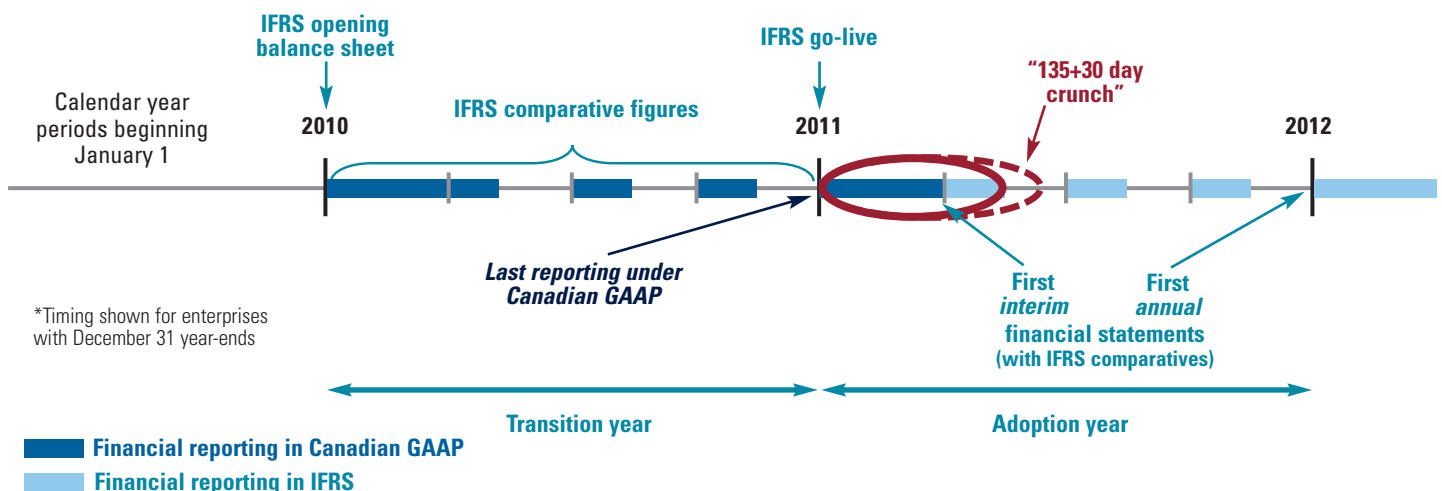
Deadlines are looming in Canada's transition to IFRS. States of readiness vary widely across publicly accountable enterprises. This article explores the questions audit committees should consider to focus the audit committee agenda through 2010 and beyond.

As the timeline below illustrates, very few audit committee and board meetings remain until the January 1, 2011, IFRS changeover date. How can you make the most of your meetings? Will you need to schedule more of them?

## Oversight by Audit Committees and Boards

Based on KPMG's survey in July 2009, many enterprises have completed their detailed assessments of the changes required under IFRS and are well into the design and implementation phases. An enterprise's rate of progress through its changeover project has implications for audit committee and board oversight.

To assess whether management is making appropriate progress, audit committees and boards need to clearly understand the extent of change that IFRS will introduce, the specific deadlines and overall time constraints, and the challenges they can pose.



*Audit committees are likely to need additional time to review and approve the first set of IFRS financial statements in 2011.*

Some IFRS-triggered changes may affect only a few companies. For example, the January 1, 2010, IFRS transition date may have special importance for those with significant financial instruments or hedging arrangements. To achieve the desired result for purposes of reporting 2010 IFRS results, they may need to decide on the designation of financial instruments or modify hedging documentation by the end of 2009. Missing this deadline could create ongoing consequences for such entities.

In 2011, however, *all enterprises* should expect the time crunch to be extreme. Preparing the Q1 interim financial statements and IFRS first-time adoption disclosures will be *more onerous than any interim statements companies have ever prepared*. Moreover, directors need to understand the rationale behind the CSA's current proposal to extend the filing deadlines by 30 days. As outlined in their Request for Comment, the CSA "recognize that boards of directors, audit committees, and in some cases auditors, will require additional time to review and approve the first set of IFRS financial statements."<sup>1</sup>

### Questions to Consider

As enterprises move well into their conversion projects,<sup>2</sup> the questions posed by boards and audit committees will often be more focused and specific.

To stimulate directors to think about the areas that an audit committee or board may need to explore with management, we are providing potential questions and clustering them by major themes

- accounting policies and elective exemptions
- financial reporting
- business impacts on the enterprise and its stakeholders.

Many of these questions highlight the need for the audit committee members and board to be appropriately *financially literate* in IFRS as it applies to your enterprise.

Of course, no list of potential questions can be complete or definitive for every situation. In providing oversight and seeking to gain comfort, audit committees will need to ask many questions and probe when necessary.

1. Canadian Securities Administrators, *IFRS-related Amendments to Continuous Disclosure Rules, the Prospectus Rule and the Certification Rule: Request for Comments*, September 25, 2009.

2. For questions to serve as a stimulus for audit committees still at an early stage in their oversight process, refer to "IFRS Transition—What Audit Committees should be asking," *Canadian Audit Committee Update 2008-01*, May 2008.

### Accounting policies and elective exemptions

1. What accounting standards or IFRS 1 elections, if any, may require actions before January 1, 2010, for our opening balance sheet? What progress is being made?
2. As the audit committee, how comfortable are we that our current knowledge of IFRS is adequate to enable us to consider management's choices of accounting policies, IFRS 1 exemptions, and judgment processes? If necessary, what actions are we taking to reach our desired level of IFRS financial literacy?
3. In which accounting standards will significant differences between IFRS and Canadian GAAP affect our business or our financial results? When and how will the audit committee and the board understand, in an appropriate level of detail, about these differences and their impact on the enterprise?
4. For **each IFRS standard with significant differences for your enterprise:**
  - a. What are the significant differences between IFRS and Canadian GAAP? How will they affect us (e.g. scope of differences, extent of change)?
  - b. How is management assessing the options, if any, for addressing such differences, and how the different choices would affect the enterprise's financial reporting as well as the conversion effort?
  - c. What are the implications of our new accounting policy choices for our opening balance sheet and reported results?
  - d. How and what is management learning about accounting policy selections being made within our industry?
  - e. Are there IFRS 1 elective exemptions applicable in this area?
  - f. Initially on a directional basis, but, ultimately based on quantitative estimates, how will IFRS likely affect our
    - i. transitional balance sheet (assets, liabilities, equity)
      - includes mandatory adjustments on transition as well as adjustments arising from optional IFRS 1 elections
    - ii. go-forward P&L after changeover
    - iii. key performance indicators (EBITDA, EPS, total assets, net debt, net debt to equity, etc.)
    - iv. business arrangements (debt covenants, capital requirements, tax and regulatory reporting, dividend policies, compensation arrangements, etc.)

5. For **optional exemptions in IFRS 1 *First-time adoption of IFRS***,
  - a. How is management analyzing its choices? What are management's recommended selections?
  - b. For each optional exemption, what is the trade-off between conversion effort and financial reporting impact? How will this choice affect our ongoing financial statements?
  - c. What are our auditors' comments on these choices?
6. What new significant management judgments and estimates will be required under IFRS? How does our audit committee plan to provide ongoing oversight?
7. How are our auditors being kept informed about management's detailed analysis of IFRS impacts? What are their comments?
8. How will IFRS affect the enterprise's data collection requirements and systems?
9. What will be the effect on internal control over financial reporting? How is management ensuring that it identifies when new controls are needed, and that they are appropriately designed, implemented, and tested?
10. What is the likelihood that the enterprise's financial results may show more volatility?
11. What further changes in IFRS standards may occur and be effective for purposes of preparing our opening IFRS balance sheet? Which IFRS changes are likely to affect our enterprise? How is management monitoring these changes and addressing their impact? When and how will the audit committee learn about their impact?

#### **Financial reporting**

1. How financially literate in IFRS are directors on the board who are not *currently* on the audit committee? Who requires further education? How and when will it be undertaken?
2. How clearly do our audit committee and board understand how the IFRS changeover will affect our financial statement presentation (what the IFRS financial statements and notes will look like)?
3. When is management planning to prepare mock interim IFRS financial statements (initially without numbers, then with) and disclosures, both as at the IFRS transition date and ongoing? How is management evaluating the completeness of the MD&A and interim financial statement disclosures? How will management help the audit committee and board

*For more information on how these standards compare with Canadian GAAP, refer to KPMG's publication, [IFRS compared to Canadian GAAP: An Overview](#).*

to understand how the statements are changing as well as any expected issues? When will our audit committee review this information?

4. How are our auditors involved in management's activities? What are their comments on what management is designing and implementing?
5. How well do management, the audit committee, and the board understand the *increased level of disclosure* required (in financial statements as well as MD&A) for first-time adoption of IFRS in Q1 2011? For example,
  - a. full disclosure of IFRS accounting policies
  - b. explanations of their impact
  - c. new areas of significant judgment and estimates.

#### **2010 opening IFRS balance sheet**

6. What is management's plan for the restatement process and for preparing the restated opening balance sheet at January 1, 2010?
7. When will the auditors review (or audit) the opening balance sheet and the related reconciliation included in first interim financial statements? When will our audit committee review this information?

#### **2010 interim IFRS financial statements**

8. When does management expect to create the first real set of interim IFRS financial statements for quarters in 2010? When will it conduct a dry run of preparing IFRS figures? Is management contemplating a three-month lag from preparing the Canadian GAAP figures for that period? ... a six-month lag?
9. When will our auditors review the 2010 quarterly IFRS results and the related reconciliations, which will be included in 2011 quarterly filings?
10. How comfortable are the audit committee and board with management's approach? How will these plans alleviate the potential time crunch in Q1 2011?
11. When those initial financial statements are available, what are the broader implications of the IFRS financial results across the business? (for example, new sensitive information being disclosed for the first time, financial covenants, contractual arrangements, capital requirements, regulatory reporting, dividend policies, performance indicators and metrics, incentive compensation arrangements)? How is management addressing any potential business issues?

***2011 interim IFRS financial statements***

12. How realistic, in terms of level of effort and timing, are management's plans to produce the required first interim 2011 financial statements and disclosures?
13. How realistic is the time being allowed to enable the auditors and audit committee to review them? What are our auditors' views?
14. As the audit committee, based on our experience leading up to the 2011 changeover date, what areas do we think may require closer examination and probing as we review the enterprise's first interim IFRS financial statements?

**Business impacts**

***IT systems and internal controls***

1. How comfortable is management that the IT systems will provide the necessary information for the first-time disclosure and ongoing financial statements?
2. If workarounds will be required in the short term, how are potential internal control issues being managed and ICFR being maintained? When will the workarounds be eliminated by systems or process changes?
3. How is management addressing the internal control certification requirements while also making the changeover to IFRS? What changes are being made? How are risks being identified and managed? How is management maintaining its certification process?

***Business operations***

1. What will be the effect on management reporting within the enterprise? How will key performance indicators change? How will these changes affect the planning, budgeting, and forecasting processes? How are issues being addressed by management?
2. How are the implications for financial covenants, contractual arrangements, and capital requirements being handled? For our dividend policies?
3. How will IFRS affect incentive compensation arrangements? As appropriate, how are specific board committees being made aware of these changes and their implications (e.g., compensation committee)?
4. How will IFRS affect our tax reporting and tax filings?
5. How will IFRS affect our other regulatory filings?

**Communications, including required MD&A disclosures**

1. Who are the key internal and external stakeholders who need to receive communications and/or education (affected employees, senior management, board, lenders, regulators, investors, analysts, etc.)?
2. What level of information do these parties expect to receive, and how frequently? What communications have been provided to date?
3. What are the enterprise's communications plans and the timing of key activities for specific stakeholder groups? How are these plans being executed?
4. How does management plan to inform investors or analysts about the impact of IFRS on our enterprise or our industry? Is our audit committee comfortable with these plans?
5. Are the company's current DC&P for financial information adequate for public disclosures in MD&A about its changeover to IFRS?
6. Do our MD&A disclosures to date regarding our changeover to IFRS provide sufficient information for shareholders? How do our MD&A disclosures compare with those of other similar companies? How do our disclosures align with the CSA's expectations? How effectively is management providing incremental information every quarter in 2009 through 2010 regarding the company's changeover?
7. In 2010, when does management plan to include quantified information about the impact of IFRS?
8. What other information should be disclosed now or during 2010 about the broader implications of our changeover to IFRS (e.g., information relevant to shareholders, such as the effect on key performance indicators)?
9. How might our disclosures affect external perceptions of our enterprise?

*For more information about the transition to IFRS in Canada, visit our Web site at [www.kpmg.ca/ifrs](http://www.kpmg.ca/ifrs).*

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

KPMG and the KPMG logo are registered trademarks of KPMG International, a Swiss cooperative.  
© 2009 KPMG LLP, a Canadian limited liability partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International, a Swiss cooperative. All rights reserved.  
Printed in Canada. 2519