

Disclosing the Impact of Adopting IFRS – When and How?

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Reporting under IFRS will change financial reporting. It will likely affect not only an enterprise's reported results and financial position, but also the format of its financial statements

Canadian audit committees are very focused on this upcoming move to IFRS and the impact on their company's financial reporting. However, external stakeholders also need to understand, before the actual changeover, what is likely to occur and why.

How well do external stakeholders understand the IFRS-related changes that are coming? Analysts are often considered to be a reasonable proxy for the wider investment community. To gauge their understanding of IFRS and its impact, KPMG commissioned a survey of Canadian financial analysts, both buy-side and sell-side. The results of this survey suggest that external stakeholders still have a lot to learn about IFRS and how it will affect the financial reporting of specific enterprises.¹

Canadian regulators expect companies to prepare stakeholders for these changes. In 2008, the CSA initially provided guidance on IFRS-related disclosures.² This guidance recognized that appropriate entity-specific disclosure would assist investors in assessing the readiness of an issuer for transition to IFRS as well as the impact the adoption of IFRS is expected to have on the issuer.

In their targeted review of 2008 annual and 2009 interim MD&A, OSC staff found, however, that "issuers are not adequately disclosing information related to their IFRS transition efforts."³ The OSC therefore advises issuers to be prepared because, going forward, regulators will be giving close scrutiny to IFRS-related disclosures in MD&A, and, as required, will request re-filings or take other regulatory actions.

The audit committee is responsible for reviewing the company's MD&A before its public release. The OSC's cautions therefore serve as a timely reminder. How does an audit committee become satisfied that the company's MD&A and other communications are providing investors and other stakeholders with meaningful and timely information about the company's move to IFRS?

1. *Preparing your stakeholders for IFRS*, KPMG in Canada, February, 2010, www.kpmg.ca/en/ms/ifrs/preparing_stakeholders.html.

2. CSA Staff Notice 52-320 *Disclosure of Expected Changes in Accounting Policies Relating to Changeover to International Financial Reporting Standards*, May 9, 2008.

3. OSC Staff Notice 52-718 *IFRS Transition Disclosure Review*, February 5, 2010.

Think about external stakeholders' needs and expectations

Who are the company's key stakeholders, and what should they know and understand? Remember that the term 'stakeholders' can encompass many different external parties, including shareholders, institutional investors, buy-side and sell-side analysts, lenders, debt investors, credit rating agencies, unions, regulators, and the financial media.

Periodically, audit committee members may find it useful to step back and reflect on their own learning curve for the company's move to IFRS. Their recollections should help them relate to investors and other stakeholders who also need to understand what financial reporting under IFRS will mean for them, but who do not enjoy the same level of direct support from management that the audit committee receives.

What kinds of information do these stakeholders generally require? How do they expect it to be communicated to them, for example, through financial statements, MD&A, earnings releases, investor/analyst calls or webcasts, supplementary materials, or other sources?

What about regulators – what information do they expect issuers to include in MD&A disclosures? OSC staff remind issuers that, moving through 2010, their disclosures should include more detailed information about the effects of IFRS—providing significant details of their conversion plan, and describing their policy choices under IFRS 1 *First-time Adoption of International Financial Reporting Standards*. In addition, CSA Staff Notice 52-320 recommends that:

“If an issuer has quantified information about the impact of IFRS on the key line items in the issuer's financial statements available when it prepares its interim and annual MD&A for the financial year beginning one year before an issuer's changeover date, an issuer should include this information in its MD&A.”

In other words, a company with a calendar year-end should include this information in its 2010 interim and annual MD&A.

The OSC also points out that, through 2010, staff will conduct further targeted reviews of issuers' IFRS transition disclosures. If an issuer has not met its disclosure obligations, regulators have said they are likely to request re-filings of MD&A or take other action.

How detailed and informative are the “leading edge” MD&A disclosures?

Naturally, each company’s disclosures should be specific to its circumstances. From the outset, however, some companies’ disclosures have been more fulsome than others. In their 2009 annual MD&A, for example, some 2011 adopters provided quantitative estimates of the expected impact of specific accounting policy decisions they are considering under IFRS. Through 2010, more companies will provide meaningful IFRS-related MD&A disclosures, including quantifying the potential impact on key financial statement line items. These disclosures will effectively ‘raise the bar’ in terms of the market’s expectations of all issuers. As a result, companies will likely feel increasing pressure from investors, analysts, regulators, and other stakeholders to explain the likely impact of IFRS in quantitative terms.

Determine when to quantify the impact of IFRS

To understand the impact of IFRS on financial results, most people know that being able to work through the numbers is generally more effective than having to rely on words alone.

When should a company provide quantified information about the impact that IFRS is likely to have, both on transition and ongoing? This question triggers considerable discussion, but the answers appear to fall into two clusters.

- Some financial executives take a conservative stance. They strongly believe that companies should disclose quantitative information only when management is absolutely confident that the information it can provide is complete and accurate.
- In contrast, other financial executives are willing to provide quantitative insights at an earlier point. They are prepared to provide information, when they have it, on the potential quantitative impact of specific accounting policies being considered. They will, however, require that their disclosures be subject to certain conditions. For example, they may indicate that management has confidence in the process used to reach these decisions and reasonable confidence in the numbers being provided, and also include in the disclosure appropriate cautionary language about key assumptions and that amounts are unaudited.

For each company, determining the right time to provide quantitative disclosure will require a fine balance—management’s comfort with the level of accuracy and completeness of the information versus stakeholders’ need for information to understand the likely impact of IFRS. As noted earlier,

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management's initial plans about when to provide quantitative information may be further complicated by peer companies or competitors making information available earlier than anticipated. Also, regulators clearly expect this information to be provided as soon as possible.

Effective disclosure controls and procedures as well as the company's disclosure committee should certainly demonstrate their value this year. For example, any messages being delivered by investor relations to the market definitely need to be aligned with any quantitative IFRS-related disclosures provided in MD&A.

Audit committees should be prepared for interesting and challenging discussions through 2010. To help directors in considering how effectively their company is communicating with stakeholders about its move to IFRS, we provide the following questions to stimulate some ideas.

IFRS-related communications – Potential questions for audit committees

1. Who are the key internal and external stakeholders who need to receive communications and/or education (e.g., affected employees, senior management, board, lenders, regulators, investors, analysts)?
2. What level of information do these parties expect to receive, and how frequently? What communications have been provided to date? How should these communications change in the future (e.g., different level of detail or frequency)?
3. What are the company's communications plans and the timing of key activities for specific stakeholder groups? How will these communications help these stakeholders to 'connect the dots'? How are these plans being executed? How does management feel its communications plans, particularly the timing, compare with similar plans for the company's peers and competitors?
4. How does management plan to inform investors, analysts, and other stakeholders about the financial reporting impact of IFRS on the company and/or its industry? How comfortable is the audit committee with these plans and the disclosures to date?
5. Are the company's current disclosure controls and procedures for financial information adequate for public disclosures in MD&A about its changeover to IFRS? What about disclosures outside MD&A?
6. Do the company's MD&A disclosures to date regarding its changeover to IFRS provide sufficient information for shareholders? How do these MD&A disclosures compare with those of other similar companies? How

do the company's disclosures align with the CSA's expectations? How is management planning to provide incremental information every quarter through 2010 regarding the company's changeover?

7. When does management plan to include quantified information about the impact of IFRS? When does management expect the company's peers or competitors to provide similar information? How do the company's disclosures compare with what others have recently disclosed?
8. What other information should be disclosed during 2010 about the broader implications of the company's changeover to IFRS, e.g., information relevant to shareholders, such as the effect on key performance indicators (KPIs)?
9. How effectively is the company updating and augmenting the information it has provided in the past?
10. How might IFRS-related disclosures affect external perceptions of the company?

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