



AUDIT COMMITTEE INSTITUTE

Canadian Audit Committee Update

Issue 2009-02

KPMG LLP

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*Increased Sensitivity Needed
During Uncertain Times*

*Sharpening Your Focus:
Overseeing IFRS Conversion
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*Regulatory, Accounting, and
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Preface



We are pleased to provide you with the 2009-02 issue of KPMG's *Canadian Audit Committee Update*.

Effective audit committees have never been more important. Many enterprises continue to deal with the consequences of ongoing economic uncertainty, while concurrently having to press forward to meet the quickly approaching deadlines for financial reporting under IFRS.

In addition, the regulator continues to cast a watchful eye. In 2009, the CSA placed increased scrutiny around the quality of reporting issuers' disclosure in response to the credit crisis and market turmoil. The CSA has indicated that, as part of their 2010 disclosure review, CSA staff will focus on disclosures around valuation of goodwill, intangibles, asset impairments, and going concern issues as well as disclosure of IFRS changeover plans in the MD&A. Through their oversight, audit committees have an opportunity to ensure that financial statement disclosures are sufficiently robust and therefore more useful to financial statement users.

In **Current Issues Dominating the Audit Committee Agenda**, we address some difficult accounting issues that warrant increased attention—impairment, going concern, and debt covenants—and the implications for audit committee oversight.

In **Financial Reporting Updates**, we outline significant regulatory, accounting, and auditing rules, standards, and projects issued since our 2009-01 issue of *Canadian Audit Committee Update*. Because of Canada's upcoming move to IFRS, we are now including in this section recent changes to IFRS accounting standards as well as projects to develop future guidance.

Audit Committee Evolving Issues focuses again on the changeover to IFRS. An enterprise's rate of progress through its changeover project has implications for audit committee and board oversight. As enterprises move well into their conversion projects, the questions posted by boards and audit committees will often be more focused and specific. To help the audit committee to reflect on areas it may want to explore, this section poses questions to consider on several major themes:

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

In **Audit Committee Resources**, we identify additional resources to help audit committee members meet today's challenges.

KPMG is committed to helping audit committee members fulfill their responsibilities by

- communicating regulatory, accounting, and auditing changes
- addressing current and emerging issues
- sharing audit committee leading practices.

We hope this publication provides you with relevant, timely information that supports your decision making.

We encourage those in the financial reporting process—management, internal auditors, external auditors, and audit committee members—to discuss the financial reporting and other matters included in this issue of *Canadian Audit Committee Update*. While the ultimate impact of certain recommendations may depend upon decisions yet to be made at various regulatory and standard-setting bodies, other elements can be evaluated and implemented, as appropriate, by those involved in the financial reporting process.

Current Issues Dominating the Audit Committee Agenda



Increased Sensitivity Needed During Uncertain Times

This section explores current events and issues and their implications for audit committees. In this edition, we discuss the audit committee's oversight of difficult accounting issues arising as a result of the economic crisis of the last 18 months.

As 2009 draws to a close, the elements that have been squeezing liquidity out of global markets for over a year appear to be loosening their grip. The economy seems to be emerging from the stranglehold of the credit crunch and entering a period of recovery, albeit cautiously. This apprehension stems from uncertainty whether market activity, unemployment rates, consumer spending, and bank lending have reached a new equilibrium.

Individual companies will be faced with different challenges. Some companies may be focused on growth, as the recession presents them with attractive acquisition opportunities. Other companies, however, may still be struggling just to maintain adequate cash.

Depending on a company's position, its audit committee and board may need to deal with new accounting issues. For example, layoffs and closure of business segments may lead to accounting for discontinued operations and restructuring provisions that previously were not concerns. Other companies may be considering sale-leaseback transactions or financing of receivables in order to shore up their cash positions. Even those that have weathered the recession may need to revisit some difficult accounting estimates made previously to ensure they are still appropriate.

We highlight some examples of difficult accounting issues that warrant the audit committee's attention and oversight in these uncertain times.

Revisiting Impairment

Which accounting judgments and estimates may be affected by the recession? How do the underlying financial models drive impairment valuations? The audit committee will need to apply healthy scepticism when deliberating the answers to such questions.

If financial asset and goodwill impairment were painful issues in 2008, the extended impact of the recession may make these exercises even more difficult this year. Market capitalization may be below book value for the second year in a row, making any goodwill impairment test particularly

challenging. Even if a company did not take a writedown in 2008 because, for example, cash flow projections showed growth or flat sales in 2009, the audit committee should nonetheless inquire about the accuracy of the prior year's projections and review management's conclusion about the critical assumptions driving this year's valuation models.

Financial assets that were determined to be temporarily impaired at the end of 2008 will have built up another year's worth of information to assist in assessing this decision for 2009. If such assets are still impaired, it is less likely that such a sustained drop in value is still temporary.

Other financial instruments can also be impaired. Management needs to assess carefully whether any financial instruments have had a prolonged drop in value.

Implications for audit committee oversight

Regardless of whether impairment provisions are new, recurring, or not needed, the audit committee needs to understand

- what assets have been identified for possible impairment
- what events triggered a need to identify possible impairment
- who is developing the models and who is making the assumptions
- what is in the models that could go wrong
- what may be missing
- the historical accuracy of the models for all important valuations.

Going Concern

As part of its reporting process, management is required to assess whether any significant uncertainties may affect the company's ability to continue to operate in the foreseeable future. In developing this assessment, referred to as the going concern assessment, management must take into account all available information about the future, including, at a minimum, information during the 12 months following the balance sheet, although this assessment can extend beyond 12 months. The level of detail required for the assessment decreases, depending on how well the company has performed historically.

If management is no longer able to point to a recent history of consistent profit making, significant energy will be required to determine whether the projected cash flows, which may now extend into 2011, are indicative of a company that remains a viable going concern.

Implications for audit committee oversight

Audit committees should understand how management is addressing the going concern requirement. The audit committee should also ensure that the auditors agree with management's assessment, and that the analysis was performed with due care, especially if there are any concerns that the company may not be able to emerge from current troubles.

Debt Covenants

Management may have renegotiated debt agreements in the past year, either to modify the existing covenants or change the terms of the debt. Any change to a debt agreement triggers the need to assess whether such changes have any accounting implications—intended or unintended.

Implications for audit committee oversight

The audit committee should determine whether management has made any controversial interpretations of their debt agreements in order to ensure that the company is in compliance with both quantitative and qualitative covenants. When the terms are vague or uncertain, management should obtain clarification from the lender. If this matter of interpretation is critical, and interpretations of the contract differ, the audit committee should require management to obtain the opinion of an independent third party.

The audit committee should also inquire whether any cross-covenant violations may affect significant financial instruments. Violation of covenants in debt agreements that appear not to be material can inadvertently trigger a cross-covenant violation of more significant financial instruments.

Enhancing MD&A Disclosure

The Canadian Securities Administrators recently published a staff notice detailing the results of their review of disclosure for reporting issuers. CSA staff noted the following common deficiencies in MD&A:

- inadequate disclosure relating to working capital requirements and circumstances that would affect a company's sources of financing
- insufficient discussion about the risks and uncertainties expected to affect the issuer's future performance given the current economic conditions
- insufficient discussion of critical accounting estimates, including a lack of disclosure of assumptions underlying the accounting estimate.

While this summary of the CSA staff's comments is by no means exhaustive, it does indicate that staff expect enhanced disclosure during this time of heightened economic uncertainty. CSA staff clearly state that the focus of their reviews through March 31, 2010, will include valuation of

goodwill, intangibles, asset impairments, and going concern issues, including the new requirements for management to assess whether the company is a going concern.

Implications for audit committee oversight

The audit committee's review of the MD&A and financial statements should focus on all areas noted above to gain comfort that management has provided fulsome disclosure.

Be Vigilant

Healthy scepticism is always an essential element of good corporate governance, but vital in uncertain times. Effective oversight may require the audit committee—and all directors—to question, challenge, and test management in the areas of greatest concern.

Applying an adequate dose of scepticism does not, however, mean distancing oneself from management. Frequently communicating, both formally and informally, with management and the auditors is critical to gaining a sound understanding of the issues and challenges requiring clarity.

Effective corporate governance requires that members of the audit committee roll up their sleeves and address all major issues—head-on and vigilantly.

Financial Reporting Updates



In this section, we identify recent significant regulatory, accounting, and auditing rules, standards, and projects issued since our 2009-01 edition of *Canadian Audit Committee Update*, as well as future projects of broad interest to audit committees. The information in this section provides a general summary and is intended only to increase awareness of financial reporting developments. For detailed guidance on the application of these standards, readers should consult their financial advisers and the original pronouncements.

Canada will adopt International Financial Reporting Standards for publicly accountable enterprises for fiscal years beginning on or after January 1, 2011. These entities are therefore increasingly interested in IFRS developments. Accordingly, this edition of the *Canadian Audit Committee Update* includes recent changes to IFRS accounting standards and projects.

To keep abreast of ongoing changes to IFRS standards and projects, we encourage you to review the IASB's work plan at www.iasb.org/Current+Projects/IASB+Projects/IASB+Work+Plan.htm. The Work Plan is a timetable showing the current best estimate of publication dates of proposed changes to IFRS standards. The current Work Plan indicates that IASB will issue in 2010 and 2011 several new or amended standards, which will have effective dates no earlier than 2012. However, where early adoption is permitted, Canadian companies should be evaluating the merits of early adopting these standards as part of their overall conversion efforts.

Regulatory and Other Developments

CSA increases scrutiny over quality of issuers' disclosure

We highlight here recent significant regulatory and other developments in Canada and the US since our 2009-01 edition of *Canadian Audit Committee Update*.

Canadian Developments

CSA Staff Notice 51-329, *Continuous Disclosure Review Program Activities for the fiscal year ended March 31, 2009*

CSA staff issued this report of findings from their continuous disclosure reviews of reporting issuers other than investment funds.

In fiscal 2009, the CSA completed 1,094 reviews, comprising 465 full reviews and 629 issue-oriented reviews. This total represents an increase of 28 percent in the number of reviews compared to fiscal 2008. Based on the reviews, no action was required for 20 percent of issuers; 48 percent of issuers required prospective changes; 14 percent received recommendations for future filings; 13 percent required refilings; and 5 percent were referred to enforcement, or a cease trade order was issued.

Common deficiencies

The most common deficiencies found in MD&A included

- repeating information from the financial statements without providing sufficient analysis
- inadequate disclosure of liquidity and capital resources
- no or insufficient discussion about the risks and uncertainties expected to affect the issuer's future performance in the current economic environment
- lack of quantitative analysis in the results of operations' discussion
- no or limited disclosure of the adoption of new accounting policies
- inadequate related party disclosures
- insufficient discussion of critical accounting estimates and their underlying assumptions.

Financial statement deficiencies included

- failure to properly measure financial instruments
- failure to disclose the credit, liquidity, and market risks associated with financial instruments, and the methods used to determine fair value
- lack of meaningful disclosure regarding an issuer's capital
- inadequate revenue recognition policy disclosures
- inadequate segment information disclosures.

CSA outlines its focus for ongoing reviews of issuers' disclosures.

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

2010 reviews

CSA staff have indicated that potential review areas for fiscal 2010 include

- valuation of goodwill, intangibles, and asset impairments
- going concern
- executive compensation disclosures
- disclosure of IFRS changeover plans in the MD&A
- disclosures and valuation of restructured ABCP notes.

Proposed Revised National Instrument 52-107, *Acceptable Accounting Principles and Auditing Standards*

These proposals would require that domestic issuers with financial years beginning on or after January 1, 2011,

- prepare annual and interim financial statements in accordance with Canadian GAAP applicable to publicly accountable enterprises
- make a statement of compliance with IFRS in the notes to their annual and interim financial statements
- file auditor reports accompanying their financial statements that refer to IFRS.

The proposals grant a 30-day extension to the deadline for filing the first interim financial report in the year of adopting IFRS, for an interim period beginning on or after January 1, 2011. This extension recognizes 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.

The new rules will apply to issuers with financial years beginning on or after January 1, 2011. Issuers with non-calendar year-ends will continue to comply with the old version of the continuous disclosure rules until their changeover to IFRS.

CSA Staff Notice 52-324, *Issues relating to changeover to International Financial Reporting Standards*

This notice is an update on issues related to the changeover to IFRS in Canada.

CSA staff are prepared to grant exemptive relief, on a case-by-case basis, to domestic issuers that prepare financial statements in accordance with IFRS in advance of the changeover date in 2011. A condition of exemptive relief will be that the issuer file revised interim financial statements prepared in accordance with IFRS, together with revised MD&A and new interim certificates.

The remainder of the issues addressed in this notice are included in the proposed revisions to NI 52-107, *Acceptable Accounting Principles and Auditing Standards*, discussed above.

CSA review highlights numerous deficiencies in disclosure.

CSA Staff Notice 52-325, *Certification Compliance Review*

This notice outlines the results of a review of compliance with the provisions of NI 52-109, *Certification of Disclosure in Issuers' Annual and Interim Filings*.

Based on the reviews, no action was required for 38 percent of issuers; 32 percent of issuers were required to make prospective changes in future filings; 16 percent were required to refile annual MD&A and certificates; and 14 percent were required to refile only the certificates.

MD&A

The following issues were noted:

- failing to fully disclose their conclusions about the effectiveness of disclosure controls and procedures or internal control over financial reporting
- qualifying conclusions about the effectiveness of DC&P and/or ICFR by using language such as DC&P and ICFR are effective subject to certain qualifications or exceptions
- using ambiguous language with respect to “limitations” around ICFR and procedures to remedy the “limitations”
- limiting the scope of design of DC&P and ICFR.

Certificates

For those issuers required to refile their certificates, deficiencies identified included

- significant amendments to the wording of the form
- incorrect inclusion of paragraphs indicating the presence of a material weakness or scope limitation when none existed
- failing to file an updated certificate when refiling financial statements, MD&A, or AIF
- failing to refile a certificate when AIF voluntarily filed subsequently
- failure by venture issuers to include a note to reader.

For those issuers required to make prospective changes in future filings, the changes related to

- amendments to wording and dates on the forms
- filing and dating the certificates on the same date the related financial statements, MD&A, or AIF are filed
- inclusion of recommended cautionary language in voluntary filings where a venture issuer provides disclosure about DC&P and ICFR.

CSA Proposal, Implementation of Point of Sale Disclosure for Mutual Funds

This proposal introduces enhanced disclosure for mutual funds and focuses on three key principles: providing investors with key information about a fund; providing the information in a simple, accessible, and comparable format; and providing the information before investors make their decision to buy.

The proposal introduces the Fund Facts document. This document highlights information that is important to investors, including past performance, risks, and the costs of investing in a mutual fund. The Fund Facts document will be required for each class or series of a mutual fund and is to be filed concurrently with the mutual fund's simplified prospectus and annual information form.

The proposal has a planned two year staged implementation.

US Developments

SEC Proposal, Proxy Disclosure and Solicitation Enhancements

The SEC is proposing changes that would enhance registrants' disclosures about executive compensation and corporate governance, specifically

- overall compensation policies
- stock and option awards to executives and directors
- director and nominee qualifications
- company leadership structure
- the board's role in the risk management process
- potential conflicts of interest of compensation consultants who advise companies.

The proposal would significantly change current reporting requirements for multi-year stock and option awards to executives and directors.

If adopted, the amendments will be effective for the 2010 proxy season.

SEC Interpretive Release—Commission Guidance Regarding FASB's Accounting Standards Codification

This release clarifies the impact of the new FASB codification on certain SEC rules and staff guidance, as follows:

- References in the SEC's rules and staff guidance to specific standards under US GAAP should be understood to mean the corresponding reference in the Codification.

Proposal expands disclosure requirements for executive compensation and corporate governance.

- The Codification does not supersede SEC rules and regulations and is not the authoritative source for those rules and regulations.
- The SEC plans to comprehensively revise existing references to standards under US GAAP in the SEC's rules and staff guidance to reference the Codification.

The interpretation is effective for interim and annual periods ending after September 15, 2009.

The Centre for Audit Quality has issued a related alert that discusses the SEC staff's views about financial statement references. The SEC is encouraging companies to make financial statements more useful to users by drafting financial statement disclosures that avoid specific GAAP references and clearly explain accounting concepts.

SEC Issues *Dear CFO* Letter about Provisions and Allowances for Loan Losses

The SEC recently issued *Dear CFO* letters to certain public companies, expressing staff's views about a number of disclosure issues companies should consider when preparing Management's Discussion and Analysis. These issuers were asked to consider whether the information upon which accounting decisions related to provisions and allowances for loan losses were made remain relevant in light of the current economic environment.

The SEC staff's MD&A disclosure suggestions are related to

- higher-risk loans
- changes in practices followed to determine allowance for loan losses
- declines in collateral value.

SEC Announcement—*Extension for Small Public Companies Requiring Audit of Internal Control Over Financial Reporting*

On October 2, 2009, the SEC announced that small public companies with a public float below \$75 million must begin to comply with the final stage of Section 404, which requires auditor attestation of the effectiveness of internal control over financial reporting, beginning with their annual reports for fiscal years ending on or after June 15, 2010. The SEC decided to grant a six month extension after publishing its internal control study less than three months before the previous deadline of December 15, 2009.

SEC recommends more MD&A disclosures about loan losses.

Accounting Developments

We highlight certain significant new accounting standards issued in Canadian GAAP, IFRS, and US GAAP issued since our 2009-01 edition of *Canadian Audit Committee Update*. We also describe current and future projects underway regarding new accounting standards in Canadian GAAP and IFRS, indicating the direction of future standards.

Recently Issued Guidance—Canada

Amendments to HB 3855, *Financial Instruments—Recognition and Measurement*

In response to changes made to the IFRS financial instruments standard in light of deteriorating financial market conditions, the AcSB decided to make several amendments to this standard to ensure consistency in areas where the standards are converged.

The first amendment provides guidance on the assessment of embedded derivatives upon reclassification of a financial asset out of the held-for-trading category. An assessment is required to determine whether an embedded derivative may be separated from its host contract and accounted for separately upon the reclassification of a financial asset out of the held-for-trading category. The combined contract continues to be classified as held-for-trading if an entity is unable to make the assessment. This amendment is effective for reclassifications made on or after July 1, 2009.

The second amendment was made to the criteria used to determine when a prepayment option in a host debt instrument is closely related to the host instrument. The amendment states that, if the exercise price of a prepayment option compensates the lender for an amount equal to the present value of the lost interest for the remaining term of the host instrument, the feature is considered to be closely related to the host contract. This amendment is effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011, with early adoption permitted.

The final amendment aligns Canadian GAAP and IFRS in the recognition and measurement of impairment of debt instruments. Previously, the standard included two models for impairment of debt financial assets: a full fair value model was applied to debt instruments categorized as held-to-maturity or available-for-sale financial assets, and an incurred-credit-loss model was applied to loans and receivables. The standard prohibited a debt security from being included in the category of loans and receivables. The amendment now permits these assets to be classified as loans and receivables, assuming they meet the definition, unless they are quoted in an active market. As a result, impairment measurement is based on the decline in value due to an expected reduction or delay in future cash flows rather than recognizing the full decline in asset value in net income, as was previously the case. Additionally, the standard requires the reversal of an

IASB and AcSB continue to refine financial instruments accounting standards and guidance.

impairment loss relating to an available-for-sale debt instrument when the fair value of the instrument subsequently increases, and the increase can be objectively related to an event occurring after the loss was recognized. The amendment applies to interim and annual financial statements relating to fiscal years beginning on or after November 1, 2008.

A clarifying paragraph was also added to this standard, providing guidance on calculating the effective interest rate when an impairment loss is recognized. The standard now requires that, subsequent to the impairment write down of a financial asset (other than a loan or receivable), interest income is recognized using the same interest rate used to measure the impairment loss.

Amendments to HB 3862, *Financial Instruments—Disclosures*

This standard has been amended to enhance the disclosure requirements related to fair value measurements and liquidity risks of financial instruments. This amendment is equivalent to recent amendments to financial instrument disclosures under IFRS discussed in more detail on page 18.

This amendment is effective for annual financial statements relating to fiscal years ending after September 30, 2009.

Generally Accepted Accounting Principles for Private Enterprises

The AcSB recently approved final accounting standards for private enterprises. For years beginning on or after January 1, 2011, Canadian private enterprises may choose to adopt the new standards or IFRS. A private enterprise is defined as a profit-oriented enterprise that

- has not issued, and is not in the process of issuing, debt or equity instruments that are, or will be, outstanding and traded in a public market (e.g., a stock exchange or an over-the-counter market), and
- does not hold assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses.

The standards were developed based on the following approach:

- principles-based set of standards that encourages the use of professional judgment
- existing Canadian GAAP used as a starting point, with the majority of recognition and measurement requirements remaining unchanged
- exclusion of standards that are not relevant to private enterprises
- simplification of certain complex accounting areas
- elimination of *Emerging Issues Committee Abstracts*, except for certain limited instances where significant issues addressed are directly incorporated in the standards
- significant reduction in disclosure requirements.

Private enterprises may choose to adopt the new "made in Canada" standards or IFRS.

Significant changes to existing Canadian GAAP were made to the following standards:

- financial instruments
- employee future benefits
- asset retirement obligations
- goodwill and intangible assets
- stock-based compensation
- income taxes
- subsidiaries
- investments
- joint ventures.

The proposed standards include detailed rules on first-time adoption of the new standards.

The new standards will be published by the end of 2009 and can be used for 2009 financial year-end reporting purposes for entities that choose to early adopt the new standards.

Abstracts from the Emerging Issues Committee—Canada

We highlight certain abstracts from the Emerging Issues Committee.

Amendments to EIC—107, Application of 3465 to Mutual Fund Trusts

This abstract was revised to amend the consensus that exempted a trust from recording future income taxes relating to temporary differences in the trust, provided certain criteria are met. Previously, one of the criteria for not recognizing future income taxes required the trust to be contractually committed to distribute all, or virtually all, of its taxable income to its unitholders. The amendment permits a trust to apply the exemption criteria if it expects to distribute all, or virtually all, of its taxable income without any contractual commitment to do so.

The amendment is to be applied retrospectively to financial statements issued after July 8, 2009.

EIC—174, Mining Exploration Costs

This abstract replaces another abstract and provides additional guidance on when exploration costs that have been capitalized should be tested for impairment. An enterprise that has initially capitalized exploration costs has an obligation in the current and subsequent accounting periods to consider certain conditions in determining whether a write-down of capitalized costs is required. For example, a significant drop in mineral prices or a deterioration in

the availability of financing typically indicate a significant adverse change in the business climate for a mining exploration enterprise. The abstract clarifies that the implications of such an adverse change should be considered on a case-by-case basis.

The abstract is effective for financial statements issued after March 27, 2009.

Recently Issued Guidance—IFRS

IFRS 1, *First-time Adoption of International Financial Reporting Standards*

This standard has been amended to add two additional optional exemptions from retrospective application of IFRS for first-time adopters.

The first provides an optional exemption that companies can, upon adoption of IFRS, elect not to reassess certain arrangements that may contain a lease that were entered into (or modified) after January 1, 2005.

The second will be extremely beneficial to first-time adopters in the oil and gas industry using full-cost accounting. The amendment would allow such entities to elect to measure exploration and evaluation assets at amounts determined under Canadian GAAP, and development or production assets at amounts determined based on the related cost centre under Canadian GAAP. However, an impairment test of the assets to which the exemption is applied is required at the date of transition, and certain disclosures are required.

When an entity uses the deemed-cost exemption for oil and gas assets in the development or production phase, the amount of any adjustment required to measure decommissioning, restoration, and similar liabilities at the date of transition is recognized directly in retained earnings, rather than adjusting the carrying amounts of the underlying assets.

The amendments are effective for annual periods beginning on or after January 1, 2010.

IFRS 2, *Share-based Payment*

This standard has been expanded to include within its scope group cash-settled share-based payments, for example, a parent making a payment to employees of its subsidiary based on the share price of the parent. Previously, the standard required that a subsidiary account for these transactions in its own financial statements only if they were settled in equity instruments. Under the expanded guidance, a group entity, such as the subsidiary in our example, receiving goods or services in either a group equity-settled or a cash-settled share-based payment transaction must account for the transaction in its own financial statements. The entity that receives the services is referred to as the receiving entity, and the entity that settles the transaction is referred to as the settling entity.

In the oil and gas industry, first-time adopters using full-cost accounting will benefit from IFRS 1 amendment.

Recent amendments will enhance transparency of financial instruments disclosures.

The standard also includes guidance on the classification of group share-based payment transactions. If the counterparty to the transaction will receive equity instruments of the receiving entity (or a cash payment that is based on the equity instruments of the receiving entity), or if the receiving entity has no obligation to settle the transaction, then the receiving entity accounts for the transaction as an equity-settled share-based payment. If the receiving entity has no obligation to settle the transaction, then it recognizes both an expense and a contribution from its parent as an increase in equity. In all other cases, the receiving entity accounts for the share-based payment as a cash-settled transaction and remeasures the obligation each period.

This amendment is applicable retrospectively to annual periods beginning on or after January 1, 2010, subject to the transitional requirements in IFRS 2.

IFRS 7, *Financial Instruments: Disclosures*

This standard has been amended to enhance disclosures about fair value measurement of financial instruments and to require additional quantitative and qualitative disclosures of liquidity risk.

The amendments require that fair value measurement disclosures use a three-level fair value hierarchy as follows:

- Level 1—fair values measured using quoted prices (unadjusted) in active markets for identical instruments
- Level 2—fair values measured using directly or indirectly observable inputs, other than those included in Level 1
- Level 3—fair values measured using inputs that are not based on observable market data.

For each class of financial instrument, disclosures are required of the level used to measure fair value, and the significant effect on the fair value measurements, if one or more of the inputs used in the fair value measurements are changed to a reasonably possible alternative assumption.

Disclosures are required of any significant transfers between Level 1 and Level 2 from one period to another, as well as changes in valuation techniques, and the reasons therefor.

The effective date is for annual periods beginning on or after January 1, 2009, with earlier application permitted. In the first year of application, comparative disclosures are not required.

Improvements to International Financial Reporting Standards 2009

Once a year, the IASB makes non-urgent, minor but necessary improvements to IFRS. The 2009 improvements contain 15 amendments to 12 standards; all will be effective for Canadian entities adopting IFRS in 2011.

Requires assessment of the classification of long-term land leases.

Of the various amendments, two may be of special interest:

- **Leases**—A land lease with a lease term of several decades or longer may be classified as a finance lease, even if, at the end of the lease term, title will not pass to the lessee. Currently, under both IFRS and Canadian GAAP, leases of land are classified as operating leases unless title transfers to the lessee at the end of the lease term (assuming the terms do not contain a bargain purchase option)
- **Revenue**—This amendment provides guidance on the indicators to consider in assessing whether an entity is acting as a principal or agent.

IAS 39, *Financial Instruments: Recognition and Measurement* and IFRIC 9, *Reassessment of Embedded Derivatives*

This amendment requires entities to assess whether an embedded derivative is required to be separated from a host contract when the entity reclassifies a hybrid financial asset out of the fair value through profit or loss category. Such assessment is to be made on the basis of the circumstances that existed when the entity first became a party to the contract, or, if later, when there was a change in the contract that significantly modified the cash flows. When the fair value of an embedded derivative that would be separated cannot be measured reliably, the reclassification of the hybrid financial asset out of the fair value through profit or loss category is not permitted.

This amendment is applicable for annual periods ending on or after June 30, 2009.

Projects to Develop Future Guidance— Canada and IFRS

The AcSB intends to replace Canadian GAAP with IFRS for publicly accountable enterprises for interim and annual financial statements related to fiscal years beginning on or after January 1, 2011. As part of this plan, the AcSB has exposed certain IASB proposed standards or amendments to standards as part of the IFRS standards to be adopted into Canadian GAAP upon changeover to IFRS.

ED – *Adopting IFRS in Canada*

The AcSB has issued a second omnibus exposure draft on the status of Canada's transition to IFRS.

In addition to exposing for comment additional IFRS standards and interpretations, the exposure draft provides definitions of key terms such as "public market" and "fiduciary capacity" to assist entities in determining whether or not they are publicly accountable entities.

The exposure draft confirms that the planned adoption date for publicly accountable entities is January 1, 2011, and proposes that IFRS be applied to interim financial statements in the year of adoption.

AcSB issues second omnibus exposure draft on adoption of IFRS.

Single standard will provide framework for measuring and disclosing fair value.

Proposals are not limited only to financial instruments, they also affect fair value measurement in other standards.

ED – Derecognition

The AcSB issued an exposure draft to replace Canadian standards on derecognition of financial assets and liabilities with those proposed by the IASB in March, 2009. The proposals in the IASB's ED were not well received; however, the alternative model in the ED received qualified support. This will result in a re-exposure of the revised proposal. Canadian entities for whom derecognition is significant should monitor IASB developments closely, and consider the impact the proposed transitional provisions will have on adoption of IFRS.

ED – Fair Value Measurements

The AcSB has issued a proposed standard on fair value measurement. This standard is identical to that proposed by the IASB.

The objective of the proposal is to establish a single source of guidance for all fair value measurements. The proposals do not introduce new fair value measurements but explain “how” to measure fair value. The proposals are not limited to only financial instruments but also affect fair value measurement in other standards.

Fair value is defined as the “exit price,” i.e., the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In the absence of an actual transaction on the measurement date, fair value would be measured using a hypothetical transaction in the most advantageous market from the perspective of a market participant.

To increase consistency and comparability of fair value measurements, a fair value hierarchy is outlined that prioritizes the inputs to the valuation model:

- Level 1—quoted prices (unadjusted) in active markets for identical assets or liabilities
- Level 2—inputs other than quoted prices included in Level 1 that are observable either directly or indirectly
- Level 3—inputs that are not based on observable market data.

For assets and liabilities measured at fair value, an entity would be required to disclose information that enables users of financial statements to assess the methods and inputs used to develop these measurements.

The proposals also expand the minimum disclosure requirements for non-financial assets and liabilities. Disclosures are also required about the determination of, and changes in, the fair value of liabilities and disclosures about assets, if their highest and best use differs from their current use.

The IASB expects to issue its proposed standard in final form in 2010. If this timeline is met, the AcSB will incorporate the final standard into Canadian GAAP as part of the changeover to IFRS.

Proposed standard represents first phase of a comprehensive project to improve and simplify financial instruments accounting.

ED – Financial Instruments—Classification and Measurement

An exposure draft has been issued to incorporate into Canadian GAAP the IASB's recently issued proposed standard on the classification and measurement of financial instruments. The exposure draft represents the first part of the IASB's comprehensive project to improve and simplify financial instruments accounting requirements.

Under the proposals, existing classification categories would be reduced, and all financial instruments would be measured at amortized cost or fair value. A classification would be made on initial recognition, based on the characteristics of the instrument and the business model under which it is managed. This classification would be irrevocable.

The proposals would retain the option, on initial recognition, to measure at fair value a financial instrument that would otherwise be measured at amortized cost, when doing so would prevent an accounting mismatch.

The proposals are expected to simplify many aspects of financial instrument accounting, including the following

- The tainting rules for held-to-maturity investments would be avoided.
- Financial instruments with embedded derivatives would not be separated into a fair value component and a cost or amortized cost component.
- Income currently reported in other comprehensive income and subsequently recycled to net income would be reported in a single location.

The IASB has not yet determined an effective date, but expects the new standard would not be applicable on a mandatory basis before January 1, 2012. The AcSB intends to incorporate the new standard into Canadian GAAP as part of the IFRS standards to be adopted in 2011. However, the new standard would not be available as part of existing Canadian GAAP, other than through the early adoption of IFRS.

ED – Improvements to IFRSs

As part of its third annual improvement process, the IASB has issued an exposure draft proposing certain changes to specific standards. The exposure draft includes 15 amendments to 11 standards. One significant proposal that could affect Canadian entities is an amendment to the standard on first-time adoption of IFRS. It would require that, during the period covered by the first IFRS financial statements, any changes in accounting policies or the use of IFRS 1 exemptions be addressed in the explanation of the effects of the transition from previous GAAP to IFRS.

The proposed effective dates for the amendments are generally January 1, 2011. The IASB expects to publish the amendments in final form in the second quarter of 2010.

The proposed standards apply to general purpose financial statements of pension plans.

ED – Income Tax

An exposure draft has been issued proposing to incorporate into Canadian GAAP the new income tax standard proposed by the IASB. The proposed final standard was planned to be incorporated into Canadian GAAP as part of the changeover to IFRS. However, the IASB has recently announced that the project will not continue in its current form. In October 2009, the FASB and the IASB indicated that they would consider undertaking a fundamental review of accounting for income taxes at some time in the future. In the meantime, the IASB will consider whether it should address any aspects of its ED on Income Taxes as part of a limited scope improvement project.

ED – Pension Plans

The AcSB has decided that, upon adoption of IFRS by publicly accountable enterprises, pension plans will continue to prepare their financial statements in accordance with existing Canadian GAAP.

The AcSB has also proposed new standards for pension plans that would be applicable to issuers of general purpose financial statements of pension plans.

The proposed standards are based on existing Canadian GAAP, with the following significant modifications:

- Financial statements would be prepared on a basis consistent with IFRS, to the extent that these requirements do not conflict with the specific requirements in the proposed standard.
- The statement of financial position (currently known as the “statement of net assets available for benefits”) would include net assets available for benefits and pension obligations.
- Guidance would be provided on the level of detail to be provided about investment assets and liabilities.
- All investment assets and liabilities would be measured at fair value.
- A pension plan would be permitted to use the plan sponsor’s accrued benefit obligation as its pension obligation in its financial statements.

Disclosure requirements would include those required by various standards. Disclosures of the effective date of the next required actuarial valuation, significant accounting policies, and additional related party information would also be required. Existing “desirable” disclosures would become required.

If the proposals are approved, pension plans may need to make changes to their accounting and reporting practices to meet the requirement to measure investment assets and liabilities at fair value.

The proposed standards would be effective for annual financial statements for fiscal years beginning on or after January 1, 2011.

New framework proposed for the recognition, measurement and disclosure of regulatory assets and regulatory liabilities.

ED – Rate-regulated Activities

The AcSB has proposed to adopt the standard on rate-regulated activities recently proposed by the IASB. Currently, there is no comprehensive standard under Canadian GAAP or IFRS for accounting for rate-regulated activities. In practice, however, many Canadian rate-regulated entities apply the US GAAP standard in this area.

The proposed standard would apply to regulated operating activities when a regulator establishes a binding price that the entity must charge its customers and the entity is subject to a cost-of-service regulation. Under the proposed standard, an entity would recognize regulatory assets and liabilities when it has the right to increase, or the obligation to decrease, rates in future periods as the result of the actual or expected actions of the regulator.

The exposure draft proposes that regulatory assets or regulatory liabilities are to be measured at the present value of expected future cash flows, on initial recognition and subsequent remeasurement. This provision represents a significant change from current practice in Canada.

The exposure draft includes regulator-specific disclosures, including information about the nature and financial impact of rate regulation on an entity's operating activities, and the significant assumptions used to value the regulatory assets and regulatory liabilities.

The standard proposes some relief for first-time adopters of IFRS. A first-time adopter could elect to use the carrying amount of an item at the date of transition as deemed cost when it includes amounts that would have been recognized as a separate regulatory asset or liability under these proposals.

The IASB's proposed standard is expected to become final sometime in 2010. The AcSB intends to incorporate the standard into Canadian GAAP upon changeover to IFRS.

Recently Issued Guidance—United States

SFAS 165, Subsequent Events

The statement establishes accounting and disclosure requirements related to subsequent events. SFAS 165's requirements for subsequent-events accounting and disclosure are not significantly different from those in auditing standards.

Under the statement, the effects of events that occur subsequent to the balance-sheet date should be evaluated through the date the financial statements are issued (or are available to be issued for certain non-public entities). SEC staff consider financial statements issued as of the earlier of the date the financial statements are widely distributed to all shareholders and other financial statement users or are filed with the SEC.

Requirements make management directly responsible for subsequent-events accounting and disclosure.

The statement is effective prospectively for interim and annual financial periods ending after June 15, 2009.

SFAS 166, Accounting for Transfers of Financial Assets—an amendment of FASB Statement No. 140

This statement eliminates the concept of a qualifying special-purpose entity and associated guidance, which had been a significant source of complexity, creates more stringent conditions for reporting a transfer of a portion of a financial asset as a sale, clarifies other sale-accounting criteria, and changes the initial measurement of a transferor's interest in transferred financial assets. Former QSPEs will be evaluated for consolidation, based on the provisions of Interpretation No. 46(R) as amended by SFAS 167.

The statement is effective for fiscal years beginning after November 15, 2009, and for subsequent interim and annual reporting periods. Early adoption is prohibited.

SFAS 167, Amendments to FASB Interpretation No. 46(R), Consolidation of Variable Interest Entities

This amendment eliminates exceptions to consolidating QSPEs. The statement contains new criteria for determining a VIE primary beneficiary and requires entities to more frequently assess whether they must consolidate a VIE.

Additional disclosure requirements are intended to assist financial statement users in understanding the significant judgments and assumptions made in determining whether a company must consolidate and/or disclose information about its involvement with a VIE.

The statement is effective for fiscal years beginning after November 15, 2009, and for subsequent interim and annual reporting periods. Early adoption is prohibited.

SFAS 168, The FASB Accounting Standards Codification and the Hierarchy of GAAP—a replacement of FASB Statement No. 162

This statement replaces SFAS 162 and establishes a single source of authoritative accounting principles recognized by the FASB to be applied by non-governmental entities in preparation of financial statements in conformity with GAAP.

This statement establishes two levels of GAAP: authoritative and non-authoritative. If guidance for a transaction/event is not specified in a source of authoritative GAAP, an entity first considers authoritative GAAP for similar transactions/events, and then considers non-authoritative guidance from other sources. Rules and interpretive releases of the SEC will remain as sources of authoritative guidance for SEC registrants.

More VIEs are expected to be consolidated.

Transition to the Codification provides an opportunity to improve disclosures by using plain-English descriptions of policies.

Auditing Developments

Clarified International Standard on Auditing replaces existing Canadian standard.

Transition to the Codification may provide an opportunity for entities to review their disclosures and to revise them to use plain-English descriptions of their policies. In many cases, it is more helpful to financial statement users to describe the specifics of the accounting policy applied in the financial statements than to refer readers to the relevant text within GAAP.

The statement is effective for financial statements issued for interim and annual periods ending after September 15, 2009.

We highlight recent significant CICA Auditing and Assurance Standards issued since our 2009-01 edition of *Canadian Audit Committee Update*.

Recently Issued Guidance

CAS 210, *Agreeing the Terms of Audit Engagements*

This recently approved standard addresses the auditor's responsibilities for agreeing the terms of the audit engagement with management and those charged with governance. The standard requires that the auditor determine if the preconditions for an audit are present and confirm with management and those charged with governance a common understanding of the terms of the engagement. The standard also describes additional considerations for engagement acceptance and considerations, if there is a change in the terms of the engagement.

The standard is effective for audits of financial statements for periods ending on or after December 14, 2010.

HB 7500, *Auditor's Consent to the Use of the Auditor's Report in Connection with Designated Documents*

Recently, the AASB approved revisions to this standard, which focuses on the auditor's responsibilities after the completion of the audit of an entity's financial statements, when the auditor agrees to consent to the use of the auditor's report in connection with designated documents. Designated documents include

- continuous disclosure documents filed with a securities regulatory authority
- an offering document issued by the entity containing, or incorporating by reference, the entity's financial statements and auditor's report thereon.

The revised standard covers a narrower range of documents in order to distinguish from the requirements of CAS 720, *The Auditor's Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements*.

The revised standard will require the auditor to read the information in an AIF and consider whether there are any material inconsistencies between the information in the AIF and the audited financial statements and, if so, to appropriately address such inconsistencies.

The standard includes additional requirements regarding

- agreeing on the terms of an engagement that includes a request for the auditor to issue consent
- prerequisites for issuing consent.

The standard is effective for periods ending on or after December 14, 2010.

Projects to Develop Future Guidance

EDs of Canadian Auditing Standards—Convergence with International Standards

In early 2006, the AASB obtained significant support from stakeholders to adopt International Standards on Auditing. ISAs are developed and issued by the International Auditing and Assurance Standards Board.

Since then, the AASB has issued many exposure drafts based on ISAs. Simultaneously with the issuance of an exposure draft of an ISA, the AASB issues an equivalent exposure draft of a Canadian Auditing Standard. The CAS is based on the ISA and follows the equivalent numbering pattern.

The earliest effective date for the new CASs will be no earlier than for periods beginning on or after December 14, 2010.

The descriptive and summary statements included in the Financial Reporting Updates section are not intended to substitute for the original rules, standards, and pronouncements. All relevant facts and circumstances should be evaluated to arrive at situation-specific conclusions. Persons who apply these rules, standards, and pronouncements may want to consult their advisers.

Canadian and international auditing standards continue to converge.

Audit Committee Evolving Issues



Sharpening your focus: Overseeing IFRS conversion through 2010

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

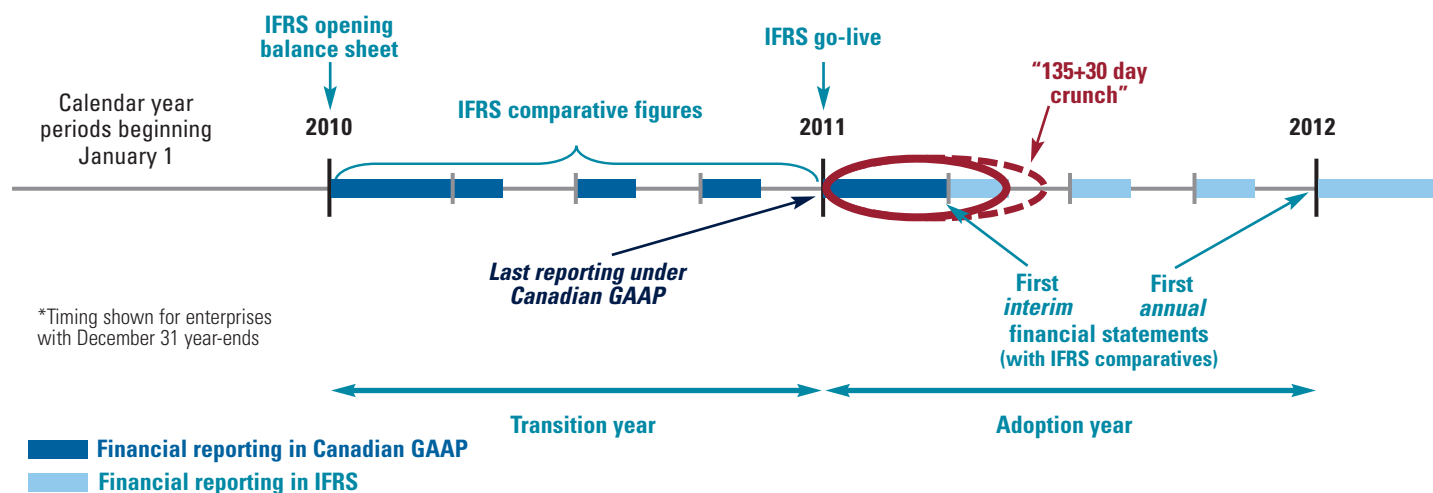
Deadlines are looming in Canada's transition to IFRS. States of readiness vary widely across publicly accountable enterprises. This article explores the questions audit committees should consider to focus the audit committee agenda through 2010 and beyond.

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."¹

Questions to Consider

As enterprises move well into their conversion projects,² 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 to understand how the statements are changing as well as any expected issues? When will our audit committee review this information?

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

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.

Audit Committee Resources



KPMG is committed to helping audit committee members fulfill their responsibilities by communicating accounting, auditing, and regulatory changes and by sharing audit committee leading practices. In each issue of *Canadian Audit Committee Update*, we describe current publications and other valuable resources pertaining to audit committees. The following resources may be of particular interest.

Shaping the Canadian Audit Committee Agenda

This publication is designed to assist audit committees in examining what they are doing and how they are doing it. In it, we discuss leading audit committee practices to help audit committees identify and react to current and future economic events, as well as address accounting, auditing, and regulatory changes.

Shaping the Canadian Audit Committee Agenda covers the full range of audit committee activities involved in creating, sustaining, and running an effective audit committee. The publication identifies and describes the audit committee's responsibilities for oversight of financial reporting and disclosures, financial risks and internal control process, and the external and internal audit processes.

The publication has relevant audit committee toolkit items, including an example audit committee charter, potential audit committee topics, a planning framework for audit committee meeting agendas, evaluations of the audit committee and the external auditor, and recommendations for conducting a private session with the auditor.

For a copy of *Shaping the Canadian Audit Committee Agenda*, visit www.kpmg.ca/auditcommittee/shaping.html or contact a KPMG office near you.

Accountability e-Lert

Audit committee members, directors, officers, and others with an interest in corporate reporting are invited to subscribe to our e-mail-based information service, *Accountability e-Lert*. This free service provides readers with useful information on the most important breaking developments in North American corporate reporting and sends a concise analysis to your personal e-mail address. Previous issues are available on our Web site. Subscribe to *Accountability e-Lert* on-line at www.kpmg.ca/accountability.

Focus on Financial Reporting

Focus on Financial Reporting is published annually by KPMG and provides an overview of recent financial reporting developments in Canada and the US. Our most recent edition (December 2008) reflects accounting pronouncements released prior to that date. For a copy of *Focus on Financial Reporting*, visit www.kpmg.ca/en/services/audit/FFR.html.

Canada's Transition to IFRS

Because Canada's transition to IFRS presents enterprises with a significant new challenge, KPMG has developed, and regularly updates, our special Web site devoted to IFRS at www.kpmg.ca/ifrs. Visit this Web site to obtain Canadian and international information dealing with the accounting standards themselves, the changeover process, and the financial reporting implications of this change.

Some materials on this Web site have been developed specifically for directors and audit committees. Other information will be helpful to both management and directors. For example, directors considering their financial literacy in IFRS may want to obtain copies of our publication, *IFRS compared to Canadian GAAP: An overview*, to help them understand the significant differences between these accounting standards.

Audit Committee Institute—Resource for Audit Committee Members

Developed by KPMG, the Audit Committee Institute was created to help serve and educate audit committee members. Wholly sponsored by KPMG, the Audit Committee Institute provides complimentary guidance and helps increase awareness for corporate audit committee members who need to keep up with their evolving responsibilities. The Audit Committee Institute's Web site at www.kpmg.ca/auditcommittee provides access to Canadian content of interest to audit committees, including archived issues of *Canadian Audit Committee Update* and the joint Audit Committee Institute and Institute of Corporate Directors Canadian surveys of audit committee members. This Web site

also provides access to the Audit Committee Institute's Web sites in other countries around the world. Audit committees with a particular interest in US developments should visit www.kpmg.com/aci.

Audit Committee Roundtables

The Audit Committee Institute facilitates roundtable sessions designed to provide a forum for the exchange of views and insights on topics of interest to members of audit committees. Feedback from audit committee members attending these roundtables has been consistently positive and enthusiastic.

Each spring and fall, roundtable sessions are held in Calgary, Toronto, and Vancouver. These roundtables explore the issues and challenges currently facing audit committee members. For more information on these roundtable sessions, please contact your local KPMG office or register on-line at www.kpmg.ca/aciroundtable.

Audit Committee Insights—International Edition

The International Edition of the Audit Committee Institute's *Audit Committee Insights* is a complimentary bi-weekly e-mail alert covering issues and topics of interest to audit committee members, corporate officers, or anyone concerned with financial reporting oversight in a global context. This electronic publication incorporates relevant articles from hundreds of respected business journals, industry publications, and association Web sites. Subjects include financial reporting, surveys and trends, shareholder issues and news, commentary and perspectives, and more.

Subscribe to *Audit Committee Insights—International Edition* on-line at www.kpmginsights.com.

Many of KPMG's publications are available in electronic and hard copy. If you, a colleague, or an associate would be interested in obtaining copies, please contact a KPMG office near you.

Acronyms Defined



| | | | |
|-----------------|---|-----------------|--|
| AASB | — Auditing and Assurance Standards Board (CICA) | FASB | — Financial Accounting Standards Board (US) |
| ABCP | — Asset-backed commercial paper | GAAP | — Generally Accepted Accounting Principles |
| AcSB | — Accounting Standards Board (CICA) | HB | — Handbook (CICA) |
| AIF | — Annual Information Form | IAS | — International Accounting Standard |
| CAS | — Canadian Auditing Standard | IASB | — International Accounting Standards Board |
| CEO | — Chief Executive Officer | ICFR | — Internal Control over Financial Reporting |
| CFO | — Chief Financial Officer | IFRS | — International Financial Reporting Standards |
| CICA | — Canadian Institute of Chartered Accountants | ISA | — International Standards on Auditing |
| CSA | — Canadian Securities Administrators | MD&A | — Management’s Discussion and Analysis |
| DC&P | — Disclosure Controls and Procedures | NI | — National Instrument |
| ED | — Exposure Draft | QSPE | — Qualifying special-purpose entity |
| EIC | — Emerging Issues Committee (CICA) | SEC | — Securities and Exchange Commission (US) |
| EPS | — Earnings per share | SFAS | — Statement of Financial Accounting Standards (FASB) |
| EBITDA | — earnings before interest, taxes, depreciation, and amortization | US | — United States |
| | | VIE | — Variable interest entity |

About the Audit Committee Institute

Recognizing the importance of audit committees, KPMG created the Audit Committee Institute to serve audit committee members and help them to adapt to their changing role. Wholly sponsored by KPMG, the Audit Committee Institute provides knowledge to audit committee members and is a resource to which they can turn for information or support, or to share knowledge.

Since 1999, KPMG's Audit Committee Institute has been communicating with audit committee members to help enhance their awareness of—and commitment and ability to implement—effective audit committee processes. Today, audit committee members, directors, and senior

management from organizations around the world draw on Audit Committee Institute resources to help strengthen the integrity of their financial reporting process and the quality of their corporate governance practices.

The Audit Committee Institute Web site at www.kpmg.ca/auditcommittee provides access to Canadian content of interest to audit committees. Audit committee members with a particular interest in developments in other countries, including the US and the UK, can also visit www.kpmgauditcommitteeinstitute.com.

If you want to learn more, need assistance, or have any questions, please contact a KPMG office near you.

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