



AUDIT COMMITTEE INSTITUTE

Overseeing IFRS Transition—Implications for CEO/CFO control certifications

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Audit committees generally recognize the significant challenge that the IFRS changeover is posing to management. Do they also understand the possible ramifications for the CEO and CFO certifications throughout this changeover?

For management of non-venture issuers, two complex processes need to be carefully linked over the next 18 months and beyond—maintaining effective disclosure controls and procedures, and internal control over financial reporting, while successfully managing the changeover to IFRS.

In this article, we review the key areas affected and the potential implications. We also include some questions that are intended to help an audit committee not only to think about the areas that it may need to explore and probe with management, but also to reflect on the committee's own activities in overseeing these processes.

Most companies have begun working on their changeover to IFRS, which will replace Canadian generally accepted accounting principles for publicly accountable enterprises on January 1, 2011.

Certain Canadian listed domestic issuers will be required to report their first set of IFRS financial statements in the first quarter of 2011. At the same time, certifying officers of non-venture issuers will also need to certify on the design and implementation of disclosure controls and procedures (DC&P), and internal control over financial reporting (ICFR).

Management's challenge: Linking two complex processes

Successfully managing this transition, while maintaining effective DC&P and ICFR, will be a challenge for management. Making this major adjustment in a company's financial reporting framework may cause significant changes in underlying processes and controls. In turn, these changes may also increase the risk of error or fraud.

Certifying officers will now need to consider whether adequate controls are in place to address IFRS conversion challenges. They may also need to modify their prior testing strategy to reflect changed risk assessments.

KPMG's recent publication, *IFRS Conversion: Implications for CEO and CFO Certifications*, focuses on issues that certifying officers of non-venture issuers should be considering, and how the issues might change through the various phases of a company's changeover to IFRS. Broadly, these issues can be clustered into three areas:

- regulatory considerations regarding the company's changeover to IFRS
- activities to support initial reporting under IFRS
- implications for ongoing certifications.

How could the IFRS changeover process affect ICFR or DC&P? We have included some examples to help audit committee members in understanding what management is dealing with in the company.

Making accounting policy choices may affect ICFR design

The conversion to IFRS requires many accounting policy choices; some choices are required in applying IFRS for the first time under IFRS 1, while others relate to on-going accounting policies. In many areas, a company's choices can have significant and wide-ranging implications for the design of its controls.

To illustrate how an account policy choice has implications for the design of controls, we highlight a choice that will affect all companies, the IFRS requirement for financial statement presentation:

IFRS accounting treatment: IFRS requires, as an accounting policy choice, that expenses be presented either by nature or by function on the face of the statement of operations. This choice can result in significant changes to captions in the statement of operations.

Implications for controls: Having made its choice, a company may need to put in place controls over the creation of general ledger accounts and the mapping of these accounts to the appropriate captions in the financial statements. In addition, the company may need to consider any program change controls required for consolidation software and the related IT application controls.

Implementing the IFRS changeover plan – more control challenges

Changing a company's financial reporting framework may, directly or indirectly, affect underlying controls and processes that require certification. In considering many activities related to the IFRS changeover, management will have to determine what could affect the company's controls. The following examples illustrate the kinds of activities with potential control or disclosure implications:

- designing and documenting new controls and processes to address changes in accounting policies and increased disclosure required under IFRS
- reevaluating risk of fraud or error, then modifying prior testing strategies to reflect changed risk assessments
- testing IT program change controls
- amending budgeting processes to reflect accounting policy changes under IFRS to enable appropriate monitoring of results in 2011
- developing controls for forward-looking guidance in MD&A to ensure that IFRS is applied appropriately to financial measures
- providing IFRS training for accounting and financial personnel throughout the company
- reviewing existing contracts to determine if they require amendment because IFRS is a different financial reporting framework
- capturing changes in ICFR to evaluate if they have or may have a material effect on financial statements and require disclosure in MD&A.

Audit committee's challenge: Focused and ongoing oversight

Through its oversight, the audit committee can contribute to a smooth IFRS transition and help to reduce the likelihood of any material weaknesses. Throughout the changeover planning and implementation, the audit committee should regularly be asking how management is addressing the internal control certification requirements while also making the changeover to IFRS. The audit committee's active oversight of the changeover process can also help to facilitate its review of the required MD&A disclosures, not only regarding management's IFRS conversion plans, but also about any changes in ICFR.

In addition, the audit committee itself may be part of ICFR through its review of accounting policy selections contained within financial statements. Because of their involvement, audit committee members should assess whether they need to enhance their knowledge of IFRS.

Questions for audit committees to ask

No list of potential questions can be complete or definitive for every company. In providing oversight and seeking to gain comfort, audit committees will need to ask many questions. The following questions are intended to help an audit committee not only to think about the areas that it may need to explore and probe with management, but also to reflect on the committee's own activities:

- Have changes in ICFR that have a potential material effect on financial reporting been appropriately disclosed in MD&A?
- How is management ensuring that people in accounting and finance roles acquire adequate IFRS knowledge?
- How will the implementation of IFRS affect the audit committee's oversight activities?
 - How adequate is the audit committee's knowledge of IFRS?
 - What is the timeline for the audit committee's involvement? How is the timeline for the committee's involvement changing over time?
 - What additional meetings are required, if any?
- How are DC&P and ICFR considerations included in the company's IFRS conversion plan?
 - How is management ensuring that the company is identifying when new controls are needed, and that they are appropriately designed and implemented?
 - What information technology system changes may be or are required to implement IFRS? What program change controls are in place?
 - How is management ensuring that the required controls are designed and implemented on a timely basis to allow the creation of the first set of IFRS financial statements, with restated comparatives, by the first quarter in 2011?
 - In what areas will the documentation of controls require significant revisions to meet regulatory requirements?
 - How is management ensuring the documentation will be in place for the first quarter in 2011?

- What analysis will be completed to support the recommended selection of IFRS accounting policies and elective exemptions under IFRS 1 *First Time Adoption of IFRS*?
 - When will this analysis be available for the audit committee’s review?
 - How are third parties involved in this analysis?
 - Will management prepare a set of mock-up IFRS financial statements for the audit committee to review?
 - How is management gaining knowledge with respect to accounting policy selections being made within our industry?
- What risk assessments does management expect to alter as a result of IFRS changes? How will these adjustments affect the testing to certify operating effectiveness for the first annual financial statements in 2011?
 - How is the nature of tests being changed?
 - How is the extent of testing being changed to address revised risk assessments or encompass different controls?
 - How is the timing of testing being altered?
- Does management believe it has adequate resources to deal with IFRS conversion and control testing for certification?
 - How are the internal auditors involved in the process?
 - How are the external auditors and/or other third parties involved in the process?

For more ideas on focusing your audit committee’s oversight of your company’s IFRS changeover, refer to our article, IFRS Transition — What Audit Committees Should Be Asking, at www.kpmg.ca/en/ms/auditcommittee/publications_ifrs_transition.html

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