



20 things to do before 2010

A practical checklist to keep IFRS conversion on track for 2011

In an ideal world, every Canadian publicly accountable enterprise ("PAE") would be ready to generate parallel International Financial Reporting Standards ("IFRS") -compliant and Canadian generally accepted accounting principles ("GAAP") -based financial data as of January 1, 2010. In the real world – the one in which virtually every business has spent the past year navigating the financial crisis – many organizations simply aren't there yet.

Based on Deloitte's IFRS conversion experience so far in Canada, and our previous IFRS conversions in numerous jurisdictions worldwide, our IFRS professionals have pinpointed 20 key things – from the tactical to the strategic – that PAEs can focus on now to keep their IFRS conversion on track for 2011. The items fall into three categories:

- Accounting policy;
- Process; and
- Policies and governance

While all 20 items are relatively high priority, some are more urgent than others. To help set priorities appropriately, each item has been classified based on its urgency:

▲ ▲ ▲ ▲ is the highest priority, and should – in almost all circumstances – be addressed in 2009; and

▲ ▲ ▲ is still high-priority, but may not be quite as urgent.

As always, this checklist is intended to provide a guideline only; each PAE is different, and should consult a trusted advisor who understands the organization's unique needs.



Accounting policy issues

1

Check designation of hedges

If hedging relationships are going to apply from the start under IFRS, they must be designated and documented – complete with effectiveness assessment and measurement – by January 1, 2010, and each quarter thereafter. It's a complex process. Changes may be required to incorporate credit valuation adjustments. Short cut or critical terms match assessments will need to be replaced by other methods. Some Canadian GAAP-based hedges will be ineligible for hedge accounting under IFRS. And all forms of hedges need to be assessed. Organizations that don't complete this task by the end of 2009 risk income statement volatility, and may face significant challenges in re-designating hedges later on.

Priority



2

Designate financial instruments into categories

When moving from Canadian GAAP to IFRS, organizations can change the designations of some financial instruments. Such decisions will determine, for example, whether financial instruments will be carried at amortized cost or at fair value, or whether the gains or losses will be recognized in operations. And there's a one-time exception on conversion that allows:

- designating a previously recognized financial asset or financial liability at fair value at that date through profit or loss (subject to certain criteria in IAS 39), or
- designating a previously recognized financial asset as available for sale.

While there's always the option to simply default to existing designations, the decision merits careful analysis. Designations and documentation should be complete by January 1, 2010 – although IASB projects could alter these categories before the end of 2010, and again in 2011.

Priority



3

Check for consistency of estimates between Canadian GAAP and IFRS

Aside from correcting errors or implementing new requirements, estimates generally will not change from Canadian GAAP to IFRS. Now is the time to check that existing estimates are consistent with IFRS, and to develop data sources for new estimates that may be needed in 2010 – for example, various types of provisions, or balance sheet entries that have been broken down from a single item into its multiple components.

Priority



4

Check for anomalies within Canadian GAAP


Experience has shown that conversion to IFRS can expose situations that have been tolerated under Canadian GAAP processes but that don't make sense and can't exist under IFRS. For example, Canadian practice under group depreciation has been to allow fixed asset sub-ledger classifications or groupings to carry credit balances – a situation that's best to fix in the 2009 financial statements, before the issue becomes highlighted on the conversion into IFRS in 2010.

Priority




- 5 Validate the functional currency**


Determining which monetary unit will be used as a functional currency by an entity – or by its segments or reporting units – is a much more detailed procedure under IFRS than under Canadian GAAP. Changing the functional currency can have a domino effect on everything from hedging programs to the magnitude of gains and losses. Considering its widespread impact, it's advisable to address this issue in 2009.

Priority  ☐
- 6 Check for the categorization of debt as current or otherwise**


Under IFRS, compliance with bank covenants will determine the categorization of debt as current or non-current. But unlike Canadian GAAP – which gives debtors a grace period to address compliance with bank covenants – IAS 1 *Presentation of Financial Statements* provides no such leeway. So now is the time to find out if IFRS will change the interpretation of bank covenants, and if loans currently classified as long-term will still be in compliance.

Priority  ☐
- 7 Evaluate business combination protocols**


Although any business combinations completed in 2010 can initially be reported under current Canadian GAAP, those 2010 acquisitions must be restated to IFRS standards in the 2011 IFRS comparative statements. This may substantially change the results of the transaction – and of the 2010 operations when reported under IFRS. For example, some items, such as transaction expenses, are written off under IFRS. To avoid surprises, organizations should be ready to evaluate all proposed transactions, and process any completed transactions, under both Canadian GAAP and IFRS. One solution may be adopting the new Canadian business combination standard – which is identical to the IFRS standard – in 2010.

Priority  ☐
- 8 Review segmentation and allocation of assets to cash generating units**

To test impairment of assets, including goodwill, assets will need to be allocated to cash generating units ("CGUs") – which may not have been done under Canadian GAAP. In many cases, each new CGU will require individual impairment testing on January 1, 2010. Here's the snag: if the organization waits to do this comparative impairment testing, the numbers generated retroactively for January 1, 2010 may be difficult to obtain. That's because the data used to support the 2010 calculation must be based on January 1, 2010 data, including management's expectations and plans at that date. If facts and circumstances have changed, and records of plans and budgets are not kept, the organization may have to rely on potentially hazy memories to justify calculations. What's more, new data and processes may be required to gather this data – not something done overnight.

Priority  ☐
- 9 Check for assets held for disposal**

The criteria for assets held for disposal under IFRS differ from those of Canadian GAAP. There may be major reclassifications of numbers currently shown as discontinued operations on the income statement – and the balance sheet. To avoid being surprised by discrepancies in 2010 numbers when IFRS reporting commences in 2011, it's wise to pinpoint such reclassifications now.

Priority  ☐

Process issues

10

Ensure all related entities (and suppliers) are ready

Subsidiaries, joint ventures, equity investees, and newly consolidated entities all need to be accounted for using IFRS standards. IAS 28 Investments in Associates, for example, requires equity-accounted investees to provide IFRS-compliant financial statements to investors within 90 days of the period end of the investor, and to include certain significant transactions as well. In addition, suppliers such as auditors, actuaries and valuers will need to work within IFRS requirements. But will these parties be ready for IFRS? That's a question you don't want to ask at the eleventh hour.

Priority



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Check for data consistency and availability for IFRS calculations

Certain IFRS calculations may hinge on data not previously required – and not readily available – under Canadian GAAP. This “you don't know what you don't know” factor has sparked last-minute scrambling in many IFRS conversions. Take, for example, impairment testing. Under IFRS, impairment testing is conducted on identified CGUs. Within each CGU, the testing will require the carrying values of all assets in the CGU, future cash flow estimates and budget and actual data – prepared consistently for each CGU to determine if further testing is appropriate. In many cases IT systems are not designed to provide this data. Assembling such data on short notice (particularly as impairment should be assessed quarterly) may prove difficult.

Priority



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Prepare IT for dual data processing in 2010 under Canadian GAAP and IFRS

Underestimating the extent of IT changes has thrown many projects unexpectedly off-course. With IFRS, however, there's no deadline flexibility. The list of potential IT process changes required to capture data differently under IFRS is extensive – affecting everything from revenues and expenses, to currencies, to subsidiaries and assets held for sale. Ideally, IT process changes should be completed in 2009, so that it's all systems go to capture IFRS-compliant data real-time in 2010 – parallel with Canadian GAAP-based 2010 numbers. The risk of using a 2011 “go live” date is that there won't be ample time to re-process 2010 transactions for comparative statements. Potentially double trouble in 2011 – with no Plan B slack.

Priority



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Design processes to capture additional information needed for disclosure

IFRS frequently requires the disclosure of additional data that may not be routinely produced for Canadian GAAP purposes – for example, opening to closing reconciliations for most major asset categories, and approved capital budgets for classes of assets. Unless there's a process in place to capture this additional data, it may prove difficult to find when it is needed at a later date.

Priority



Policy and governance issues

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Prepare for Management's Discussion & Analysis (MD&A) and financial statements

The MD&A should address two key requirements:

- Prior to conversion, management's assessment of progress towards conversion, on a quarterly basis, identifying progress in seven key areas identified by the Canadian Securities Administrators ("CSA"); and
- Upon conversion, management's explanation of how the IFRS changeover has impacted the entity's reported performance, financial condition and expectations – and how this is reflected in, for example, the determination of compensation.

The CICA web site www.cica.ca or your advisor can help you formulate these discussions in the MD&A.

Priority



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Are necessary internal controls being put in place?

The changeover to IFRS will need to be captured within the CEO and CFO certification of internal controls – for instance, for Sarbanes-Oxley purposes. This issue should be addressed with auditors well in advance of 2011. Remember: controls can be put in place in advance, but can't be installed after the fact. So the 2011 certification process must pay particular attention to controls over elections and other choices, estimates and valuations and other IFRS-related records that are not part of the regularly-controlled enterprise systems, such as manually-prepared spreadsheets.

Priority



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Are all contracts referring to financial data being reviewed or amended?

Contracts including purchase and sale agreements, leases, and debt covenants may refer to financial data that will change under IFRS. Now is the time to determine if references to Canadian GAAP are still appropriate. It's also the time to review the internal consistency and relevance of matters such as compensation, earn-outs and income tax, which may blend several years of data across the conversion period – through loss carry-forwards, long-term payouts and compensation awards. If revisions are required, they may need to be renegotiated with other parties – a process that requires some lead time.

Priority



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Ensure functional financial reporting resources are in place

No matter how well prepared systems or processes may be, the people living with IFRS day-to-day can make or break an IFRS conversion. The first step is identifying these individuals; the next step is training them. If they're not adequately trained – or if they doubt their own ability to operate under new IFRS rules – there must be a back-up plan to fulfill their responsibilities. Such planning takes time.

Priority



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Obtain commitment/process to get tasks done on a timely basis

When it comes to IFRS conversion, there are essentially two potential outcomes: the first is to gain the backing of the highest level of authority and get the job done; the second is to fail to deliver on conversion deadlines and requirements, and pay the price. Those headed in the right direction will deal with issues on a timely basis, have a realistic and detailed monitoring process, and IFRS will appear regularly on the audit committee agenda. Those who aren't should prepare to answer to investors and regulators disappointed by delayed results, and to face class-action litigators. Consider this the final boarding call.

Priority



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Have a contingency plan

As the recent financial crisis has illustrated, contingency planning is a business essential. IFRS conversion presents an array of known and potential contingencies: ongoing changes to standards dealing with taxes, joint ventures, financial instruments, fair value and rate regulation; the inability to obtain data to convert key components (for example, no historical values to calculate property, plant and equipment balances); unexpected business combinations; and changes in key personnel. Now is the time to establish a list of fall-back resources.

Priority



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Get ready to be audited, reviewed, challenged and compared

With the principles-based nature of IFRS, organizations will be making significant judgement calls – which will need to be documented, defended (for example, to analysts) and audited. Well-armed organizations will prepare IFRS financial statement mock-ups, practice account closings, complete a data gathering dry-run, check and document controls and conduct industry benchmarking. Although IFRS may allow for more diversity of judgement, choices need to be justified through researching the literature and documenting decisions and the basis for conclusions.

Priority



What's your score

Time is running out to get your IFRS conversion on track. If your organization can put a checkmark beside most of this top 20, congratulations – you're clearly headed in the right direction. If not, what are you waiting for? We can help.



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