



International Financial Reporting Standards

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Effective January 1, 2011, International Financial Reporting Standards (IFRS) will replace Canadian generally accepted accounting principles (Canadian GAAP) for all Canadian publicly traded companies and non-listed financial institutions, securities dealers and cooperative enterprises that qualify as publicly accountable enterprises (PAEs). As a result, Canadian GAAP will cease to exist for PAEs. For Canadian private enterprises, adoption of IFRS will be permitted but not required. The Canadian Securities Administrators (CSA) *Staff Notice 52-320 - Disclosure of Expected Changes in Accounting Policies Relating to Changeover to IFRS* (Staff Notice 52-320) provides guidance to PAEs on the disclosure of expected accounting policies relating to a PAE's changeover to IFRS as the basis for preparing its financial statements. This guidance applies to disclosure relating to each financial reporting period in the three years before the first year for which a PAE prepares its financial statements in accordance with IFRS.

What is IFRS?

IFRS is a collection of accounting standards issued by the International Accounting Standards Board. IFRS applies to general purpose financial statements of profit oriented enterprises. Currently, over 100 countries require,

permit or have a policy of convergence with IFRS.

Requirement to Change to IFRS

Canadian adoption of IFRS is directed to PAEs which are listed companies and other organizations that are responsible to large or diverse groups of shareholders. The Canadian Accounting Standards Board's definition of PAE excludes profit-oriented entities that:

- Have not issued (and are not in the process of issuing) debt or equity instruments in a public market; and
- Do not hold assets in a fiduciary capacity for a broad group of outsiders.

Early Adoption of IFRS

Understanding that PAEs may want to prepare their financial statements in accordance with IFRS for periods beginning prior to January 1, 2011, CSA Staff have indicated their willingness to recommend exemptive relief on a case by case basis to permit the early adoption of IFRS. PAEs likely to consider early adoption include:

- Domestic PAEs that are subsidiaries of entities based in a foreign jurisdiction that requires compliance with IFRS;
- Domestic PAEs with significant foreign operations in jurisdictions where the operating subsidiaries

must prepare financial statements in accordance with IFRS;

- Domestic issuers that are also Securities and Exchange Commission (SEC) registrants and wish to take advantage of the opportunity to file IFRS financial statements with the SEC without a reconciliation to United States generally accepted accounting principles (US GAAP); and
- Canadian entities considering doing an initial public offering in both Canada and the United States prior to the mandatory changeover date in Canada.

In *CSA Staff Notice 52-321- Early Adoption of IFRS, Use of US GAAP and Reference to IFRS-IASB*, CSA Staff recommends that a PAE considering early adoption should first evaluate the readiness of its staff, board of directors, audit committee, auditors, investors and other market participants to deal with early adoption. In this regard, CSA Staff have recommended that PAEs consider the implications of adopting IFRS before 2011 on their obligations under securities legislation, including those relating to CEO and CFO certifications, business acquisition reports, offering documents and previously released material forward-looking information.

Implications of the Changeover to IFRS

1. Management's Discussion and Analysis

Form 51-102F1 - *Management's Discussion & Analysis* (MD&A) requires a PAE to discuss and analyze any changes in the PAE's accounting policies that the PAE has adopted or expects to adopt subsequent to

the end of its most recently completed financial year. CSA Staff have suggested that PAEs should begin providing general disclosure about the changeover to IFRS in their MD&A three years before the first day of a PAE's financial year for which financial statements are prepared in accordance with IFRS (for a January 1, 2011 changeover date, general disclosure should begin to be provided in the PAE's MD&A for the year ended December 31, 2008). Notwithstanding this guidance, CSA Staff have acknowledged that PAEs will be able to provide more detailed information about the expected effects of IFRS on a PAE's specific circumstances in its MD&A the closer it gets to their changeover date. As a PAE moves closer to their changeover date, CSA Staff recommends that the PAE consider how it might make available meaningful quantified information to allow investors to understand the impact of IFRS on the PAE's financial statements.

A PAE's MD&A should discuss the status, key elements and timing of its changeover plans and, over time, address the impact of a changeover to IFRS on:

- Accounting policies, including general policy and implementation decisions the PAE has implemented or will have to implement as a result of the changeover to IFRS;
- Information technology and data systems;
- Internal control over financial reporting;
- Disclosure controls and procedures, including investor relations and external communication plans;
- Financial reporting expertise, including training requirements;

- Business activities, such as foreign currency and hedging activities, as well as matters that may be affected by a changeover to IFRS, such as debt covenants, capital requirements and compensation arrangements; and
- Key line items presented in the PAE's financial statements.

2. Comparative Financial Statements

Changing from Canadian GAAP to IFRS will be a significant undertaking that may materially affect a PAE's reported financial position and results of operations. PAEs will need to provide comparative information for their first reporting period under IFRS. For most issuers, the first annual financial statements impacted will be financial statements for the year ended December 31, 2011. The first quarterly financial statements to be impacted for these issuers will be the financial statements for the three months ended March 31, 2011. The financial statements to be issued by these issuers for the year ended December 31, 2011 will be required to include comparative information for the period ended December 31, 2010 prepared in accordance with IFRS. PAEs will need to maintain appropriate records to prepare this comparative information. In addition, changing from current Canadian GAAP to IFRS may affect certain business and technology functions of the PAE. The CSA suggests that significant planning for the changeover, if not already started, should start as soon as practicable.

3. Use of U.S. GAAP

The SEC now permits "foreign private issuers" to file financial statements prepared in accordance with IFRS without

reconciliation to U.S. GAAP. This decision now alleviates the need for foreign private issuers to prepare two sets of financial statements based upon two sets of differing accounting principles. While the SEC has yet to adopt IFRS domestically, the SEC is currently considering the issue.

4. Non-Reporting Implications of IFRS

Non-reporting implications resulting from the changeover from Canadian GAAP to IFRS include:

- **Impact on Human Resources** – Changeover to IFRS may have a burdening effect on a PAE's human resources. The requirement to allocate a number of staff specifically to master IFRS changeover may be a difficult proposition for smaller PAEs lacking sufficient human resources.
- **Contractual Financial Covenants** – Changeover to IFRS will affect financial covenants of PAEs. A difference in reported results of operations and financial position between Canadian GAAP and IFRS could affect the PAE's financial ratios and other covenants and trigger defaults under contractual agreements with lenders.
- **Compensation Arrangements** – Adoption of IFRS is likely to result in changes in revenue and expense recognition. To the extent that this occurs, compensation arrangements of PAEs may be affected.
- **Corporate Governance** – Audit committee members (and directors generally) of a PAE must be alert to changes under IFRS and accounting policy choices. Directors will have to

be financially literate and able to read financial statements prepared in accordance with IFRS. Concerns and questions relating to educational requirements of board members and effects of IFRS on directors' and officers' liability should be asked of the PAEs management and of directors themselves.

- **Information Systems** – Increased disclosure under IFRS will create a demand for information relating to the PAE not previously required under Canadian GAAP. New systems may need to be implemented in order to disclose required information. New internal controls may be required to ensure information is reliable.
- **Reporting Obligations** – A PAE should assess its financial reporting obligations under contractual arrangements. Changeover to IFRS could result in inconsistent financial reporting with those reporting obligations agreed to between parties.
- **Shareholder's Analysis** – Changeover to IFRS will impact upon the ability of shareholders to analyze financial statements of PAEs by affecting various accounting measures such as earnings per share, EBITDA and dividend and distribution policies.

All areas of a PAE will be impacted by IFRS. The magnitude of the changeover from Canadian GAAP will present many challenges of which PAEs, their directors and officers must become accustomed. PAEs should assess the impact of the adoption of IFRS on all aspects of their

organization in order to ensure a timely and manageable transition.

This update is intended as a summary only and should not be regarded or relied upon as advice to any specific client or regarding any specific situation.

If you would like further information regarding the issues discussed in this update or if you wish to discuss any aspect of this commentary, please feel free to contact us.

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