

Countdown

Deloitte Canada's IFRS transition newsletter



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The key theme in this issue of Countdown is, not surprisingly, the "credit crisis," which has been impossible to ignore based on the events of the last month. The outcome from an IFRS perspective has been an increased focus on clarity and transparency in financial reporting with the International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB) coordinating efforts in response to current events.

From an IFRS transition perspective, such developments need to be factored into your IFRS transition plan, all aspects of these accelerated changes considered. Our lead article from Karen Higgins, Partner and National Director of Accounting Services in Deloitte Canada, delves deeper into this topic.

Also this month, we are highlighting the release of *iGAAP 2008 - IFRS in Canada*, the first and only desktop reference available which focuses on IFRS transition from a Canadian perspective.

As always, we welcome direct feedback from you, including ideas for articles you would like to see in future issues of Countdown. Please submit your ideas and suggestions to deloitteifrs@deloitte.ca.

Don Newell
IFRS National Services Leader

The Credit Crunch - Economic slowdown driving IFRS-accelerated changes

The credit crunch or credit crisis is the primary business issue currently facing companies around the world. The magnitude of this issue is driving changes in other areas too, including IFRS. **Karen Higgins** is a leading expert in both financial instruments and international financial reporting matters. She has provided a synopsis of recent events and their impact on IFRS and, accordingly, on your IFRS transition.



There has been a tremendous focus on global accounting standards as part of the political and regulatory response to the current credit crisis. One of the most influential factors in the timing and prioritization of the IASB's short and long-term standard-setting agenda is a "call to action" that was issued by the Financial Stability Forum (FSF) in April 2008. The FSF report was the result of a collaboration by the main international bodies and national authorities in key financial centers, including the IASB responding to the credit crisis. It set out 67 recommendations, which were endorsed by the G7 on April 11, 2008, many of which have been embraced by regulators, politicians, standard-setters and financial-statement preparers.

The FSF report, in combination with an ongoing focus on fair value accounting from financial-statement preparers, regulators and politicians, has been very influential in the prioritization of various projects spearheaded by the IASB as well as on the speed at which amendments are made. The following is a high-level summary of how these factors have influenced the IASB's standard-setting agenda and what this will mean to Canadian companies.

a. Amendments to standards made with "expedited" due process

The IASB issued an expedited amendment to IAS 39 *Financial Instruments – Recognition and Measurement* (IAS 39) on October 13, 2008, which will allow certain financial assets previously classified as Fair Value Through Profit & Loss (FVTPL) (except those classified through the Fair Value Option) to be reclassified out of FVTPL in "rare circumstances," such as the current inactive market conditions.

What does this mean for Canadian companies? –The Canadian Accounting Standards Board (AcSB) has also issued a similar expedited proposal to amend CICA 3855 *Financial Instruments – Recognition and Measurement* to permit the same limited-scope reclassifications out of Held for Trading. If additional amendments are proposed by the IASB, the AcSB may continue to adopt "mirror" amendments on a similarly expedited basis.

b. Accelerated timelines for certain amended standards

The IASB has accelerated its project timeline to issue an amended consolidation exposure draft (scheduled for Q4 2008 release), which will also address special purpose entities. The IASB has also accelerated the timeline for completing its project on the derecognition of financial assets, which impacts accounting for asset securitization by the asset originator. The IASB expects to issue an exposure draft by the first half of 2009.

It is also possible that the current credit crisis may also accelerate the timeline for the sweeping amendments to IAS 39 proposed in the 2008 exposure draft issued by the IASB *Reducing Complexity in Reporting Financial Instruments*.

What does this mean for Canadian companies? - Due to the accelerated timelines, it is likely that the amended standards will be on the fast track to completion and they may have effective dates in fiscal 2010 or 2011. If so, the recommendations of the revised standards may be required to be adopted on transition to IFRS and therefore the draft recommendations, and final standards, require careful analysis and consideration during the implementation project.

The Credit Crunch - Economic slowdown driving IFRS-accelerated changes (cont'd)

c. Other key initiatives of the IASB

The IASB has also been active in many other areas including, but not limited to, the establishment of a Joint Advisory Group with the FASB and senior leaders with broad international experience in financial markets. The Joint Advisory Group has been tasked with considering how improvements in financial reporting could help to enhance investor confidence in financial markets. The group is also charged with identifying the accounting issues requiring boards' urgent and immediate attention as well as issues for longer-term consideration.

The IASB has also issued exposure drafts to enhance financial instrument disclosures and financial statement presentation and, as a result, has formed an Expert Advisory Panel. Refer to our International Round Up later in this newsletter for more information.

What does this mean for Canadian companies? – All of these initiatives mean that change in global accounting standards is happening at an unprecedented pace. Canadian companies need to continue to monitor developments at the IASB to ensure that their IFRS conversion plans are adjusted appropriately to incorporate any short- and medium-term changes to IFRSs which will have an impact on the IFRS opening balance sheet adjustments. Conforming changes may be adopted by the AcSB on an accelerated basis, which will require Canadian companies to assess the impact for Canadian GAAP reporting between now and 2011.

In summary, careful monitoring of developments by the IASB, FASB and AcSB is required to ensure that you are aware of proposed changes to IFRSs and Canadian GAAP, especially as the timelines for completing certain "critical" projects are compressed, resulting in significant changes to IFRSs occurring between now and your IFRS transition date.

Acquisition accounting under IFRS – M&A strategy considerations

IFRS 3 (revised) *Business Combinations* (IFRS 3R) was issued in January 2008 by the IASB. Under the new rules, certain items must be accounted for outside of the purchase transaction as an expense of the period and anything that is deemed to be part of the purchase transaction is now generally measured at the acquisition date and at fair value.

| What's out? | What's in? |
|--|--|
| <ul style="list-style-type: none"> ✗ Transaction costs may no longer be capitalized as part of the purchase price ✗ Restructuring costs are generally not considered part of the purchase price allocation ✗ Negative goodwill is written off as income and is no longer eliminated against the non-current assets acquired | <ul style="list-style-type: none"> ✓ Contingent consideration is recognized at fair value at the acquisition date ✓ Shares issued as purchase consideration are measured at the acquisition (vs. announcement) date ✓ Adjustments made during the measurement period must be made retrospectively, requiring restatement of prior periods if applicable |

Acquisition accounting under IFRS – M&A strategy considerations (cont'd)



Mark Wayland, a partner in the Complex Accounting and Transaction Expertise Group in Toronto, emphasizes that this is not just an accounting change. “These changes may trigger reconsideration of the merger and acquisition (M&A) strategies for many Canadian companies adopting IFRS. By being aware of the changes, companies have the ability to assess the impact on the pricing of future acquisitions and the impact on post-acquisition earnings.”

In the table below, Mark and his Financial Advisory Services colleague, Kenneth Johnston, have combined accounting with valuations expertise to provide a summary of M&A strategy considerations triggered by the new accounting guidance.

| New accounting under IFRS 3R | M&A strategy considerations |
|---|---|
| <p>Contingent consideration – Under IFRS 3R, contingent consideration is included in acquisition accounting, at fair value (either as a liability or in equity, depending on its nature). For contingent consideration recorded as a liability, subsequent changes in fair value are recognized in the income statement (until settled). This is in contrast to current Canadian GAAP when such contingencies are generally not recorded until resolved.</p> <p>Pre-acquisition Contingencies – Generally included in acquisition accounting at fair value under IFRS 3R. Any subsequent changes in measurement are included in income.</p> | <p>Consider the need to engage valuation experts</p> <ul style="list-style-type: none"> Valuation of contingent consideration and pre-acquisition contingencies will likely be complex. Contingent consideration recorded as a liability will need to be re-measured on an ongoing basis – valuation expertise may be required over an extended period of time. <p>Consider valuation issues early in the due diligence process</p> <ul style="list-style-type: none"> Liability recognition and associated valuation issues for pre-acquisition contingencies should be understood and evaluated as part of the due diligence process as these recognized liabilities could impact deal value. Consider alternative purchase price structures to minimize the possible post-acquisition income statement volatility that could arise with certain contingent consideration arrangements. |
| <p>Restructuring costs – Post-combination restructuring plans of the acquiring company are generally recognized in the income statement as incurred under IFRS 3R. Under current Canadian GAAP, many of these restructuring costs are recognized as liabilities in the purchase price allocation.</p> | <p>Consider the impact on business acquisition modeling</p> <ul style="list-style-type: none"> Ensure all post-acquisition expenditures and costs are appropriately reflected in the income statement <ul style="list-style-type: none"> Expensing of post-acquisition restructuring costs will reduce earnings of the combined company, possibly contributing to an early dent in the initial results after the acquisition. |
| <p>Measurement date of acquirer’s equity securities issued – IFRS 3R requires that equity securities issued as consideration in a business combination be recorded at fair value as of the acquisition date. Under current Canadian GAAP, these securities are valued over the period of a few days before and after the terms of the business combination are agreed to and announced. Because the value of securities often changes between the announcement date and the acquisition date, IFRS 3R might result in substantially different amounts recorded as consideration.</p> | <p>Consider the timing of the deal closing</p> <p>Closing transactions closer to the announcement date could reduce risk of purchase price impact from subsequent changes in securities prices in share transactions.</p> |

Acquisition accounting under IFRS – M&A strategy considerations (cont'd)

| New accounting under IFRS 3R | M&A Strategy Considerations |
|---|--|
| <p>Measurement period – Consistent with current Canadian GAAP, IFRS 3R retains the concept of an <i>allocation period</i>, in which up to one year is given to complete the business combination accounting. IFRS 3R requires an acquirer to revise comparative information for prior periods presented.</p> | <p>Consider the timing of the deal closing</p> <ul style="list-style-type: none"> Closing transactions at the beginning of a reporting period will maximize the time a company has to finalize acquisition accounting prior to a reporting deadline. This reduces the risk of needing to revise comparative information to reflect changes in acquisition accounting during the measurement period. <p>Consider valuation issues early in the due diligence process</p> <ul style="list-style-type: none"> Addressing valuation issues early will allow companies to close acquisition accounting earlier thus minimizing the risk of needing to revise comparative figures within the measurement period. |

Deloitte IFRS publications and events

A comprehensive summary of Deloitte publications and events is [available here](#). (*Please first login, first time visitors will need to complete a short registration form*). Below we have included new publications and events most relevant to Canadian companies. Other new events not featured below include a webcast by the US firm for the power and utilities industry and an IFRS brochure providing insights on IFRS in the Real Estate sector.

iGAAP – IFRS for Canada – it's here!

Deloitte Canada has just released *iGAAP 2008 – IFRS for Canada*. This publication focuses specifically on IFRS transition from the standpoint of Canadian companies and is the first comprehensive desk reference for IFRS transition in Canada.

The publication, approximately 2,400 pages long, is based on our successful global IFRS reference book, *iGAAP*, which provides a walkthrough of each IFRS standard supplemented by Deloitte's interpretative guidance, examples, and commentary. *iGAAP 2008 – IFRS for Canada* goes one step further by comparing each standard to current Canadian Generally Accepted Accounting Principles (GAAP) and analyzing potential differences and other considerations relevant to a Canadian company undergoing IFRS transition. This is certainly timely and relevant guidance and a worthy companion for IFRS implementation teams in Canada. Contact your local Deloitte partner or IFRS specialist to find out how to obtain your copy of *iGAAP 2008 – IFRS for Canada*.

Fall and Winter IFRS Webcasts – don't forget to register

Canada: Deloitte Updates

Deloitte Updates are informative, interactive webcasts with discussion about financial reporting and regulatory developments. They also qualify towards Continuing Professional Development (CPD) or Continuing Professional Education (CPE) hours. Our upcoming webcasts are as follows – for your convenience, they are recorded and may be viewed at another date up to 90 days after the live presentation.

Deloitte IFRS publications and events (cont'd)

November 6, 2008: The accounting framework in Canada continues to move towards IFRS harmonization. Learn more about recent accounting changes in each framework, including clear harmonization projects towards IFRS. Our discussion will include:

- Canadian GAAP update
- IFRS update
- Regulatory developments
- Private enterprise strategy update

[Click here to register for this webcast](#)

IAS Plus Newsletters

Deloitte has issued three special-edition IAS Plus Newsletters this month summarizing and providing our views on recent standard-setting activity:

- [Reclassification of financial instruments \(IAS 39\)](#)
- [Proposed amendments regarding discontinued operations \(IFRS 5\)](#)
- [Additional exemptions and amendments proposed for first-time adopters \(IFRS 1\)](#).

Reclassification of financial instruments and the ensuing amendments to IAS 39 *Financial Instruments – Recognition and Measurement* are discussed in our International Round-Up. Proposed amendments to IFRS 1 and IFRS 5 were discussed in our [September 2008 newsletter](#). (*Please first login, first time visitors will need to complete a short registration form*).

Insurance

Earlier this month, we released the Canadian publication [On the Road Ahead: IFRS Top Ten Accounting Issues in Insurance Industry](#). For the insurance industry overall, the following are the top ten recurring areas of particular significance:

1. Insurance contracts – measurement principles
2. Product classification
3. Insurance contracts – financial statement presentation and disclosures
4. Insurance contracts – embedded derivatives and unbundling
5. Insurance contracts – changes in accounting policies
6. Impairment
7. Financial instruments
8. Real estate
9. First-time adoption of IFRS
10. Other areas including business combinations, leases, share-based payments/related parties, and employee benefits

The new Deloitte research publication, *The IFRS Journey in Insurance: A Look Beyond the Accounting Changes* examines the implications of the use of IFRSs in the insurance industry across the globe.

Click to download [The IFRS Journey in Insurance](#).

Deloitte IFRS publications and events (cont'd)

IFRS Road Map for Executives

Our firm has published *Buckle Up (On the Road to IFRS)* (Please *first login*, first time visitors will need to complete a short registration form) which provides practical solutions designed to help executives understand the implications of IFRS and their role in addressing the associated changes. The publication focuses on the business aspects of IFRS that are critical to consider and that will be helpful for Canadian executives facing similar issues.

International Round-up: Updates and news from the IASB

Much of the news of this month focuses on the IASB's response to the credit crisis with new events or updates from the IASB almost every day. Selected items of interest are included below. For additional details and events, you can access <http://www.iasplus.com/index.htm> for general IFRS news and <http://www.iasplus.com/crunch/creditchunch.htm> for IFRS news specifically related to the credit crisis. Given the constant news on this particular issue, we encourage you to review www.iasplus.com regularly to receive an ongoing status report of how standard-setters around the world are responding to the credit crisis.

October 17, 2008: Financial Reporting Alert on the credit crisis

Deloitte Canada issued a *Financial Reporting Alert* (Please *first login*, first time visitors will need to complete a short registration form) to enable Canadian companies to obtain a comprehensive understanding of recent issues relating to the credit crisis and applicable considerations for Canadian companies. The alert provides a summary of developments internationally, in Canada and in the United States and the collaborative approach that is being taken by the standard-setters to increase harmonization and provide clarity and promote stability in the current environment. A summary of recent international events follows; however, we encourage you to also read the alert to gain a better appreciation of what is happening with financial reporting standards and how to apply the changes that are being introduced.

October 16, 2008: Discussion Paper on financial statement presentation

The IASB and FASB have jointly published for comment a *Discussion Paper (DP), Preliminary Views on Financial Statement Presentation*. (Please *first login*, first time visitors will need to complete a short registration form) The project is intended to create a standard requiring an entity to organize financial statements in a way that clearly communicates an integrated financial picture of an entity. The main objectives for presentation are proposed as cohesiveness (enabling a reader to follow the flow of information) and disaggregation (separating information that responds differently to economic events). The comment deadline is April 14, 2009 and an Exposure Draft (ED) of proposed revisions to IAS 1 *Presentation of Financial Statements* is planned for 2010.

October 15, 2008: IASB ED on financial instruments disclosures

In response to the credit crisis, the IASB has issued an *ED of proposed amendments to IFRS 7 Financial Instruments Disclosures*. Proposed changes relate to fair value and liquidity risk disclosures including the introduction of a three-level hierarchy when disclosing fair values (comparable to US GAAP) and disclosure of liquidity risk for derivative financial liabilities. These proposed changes build on advice the IASB has received from the Expert Advisory Panel the IASB established to deal with financial reporting matters relating to the credit crisis. At the crux of the changes is the need for entities to provide as much clarity and transparency as possible when explaining to investors how fair values of financial instruments are determined.

The ED, entitled *Improving Disclosures about Financial Instruments*, has a comment deadline of December 15, 2008 and a proposed effective date of July 1, 2009.

International Round-Up: Updates and news from the IASB (cont'd)

October 13, 2008: IASB amendments regarding reclassification of certain held for trading financial assets

The IASB issued amendments to IAS 39 *Financial Instruments – Recognition and Measurement* and IFRS 7, permitting reclassification of financial instruments out of the fair value through profit or loss category (held for trading) and out of the available for sale category. The amendments are effective July 1, 2008 and introduce the same reclassifications that are permitted under US GAAP in specific (and rare) circumstances. In a press release issued the same date, the IASB indicated that the current market conditions are one possible example of when such rare circumstances may exist.

October 14, 2008: IASB press release on applying fair value in inactive markets

The IASB issued a press release with an update on its work on how fair value determination should be applied when markets become inactive. In the press release, IASB chairman, Sir David Tweedie, stated that fair value is not the price that would be achieved in a distress sale and that such transactions should not be included in fair value measurement. He also indicated that the position of the IASB on such determinations of fair value is consistent with the FASB position.

This update builds on the discussions on the same subject which took place on September 18, 2008 on the IASB Expert Advisory Panel. The discussion includes one of the most comprehensive summaries available of factors to be considered when determining fair value when markets are inactive or illiquid.

October 13, 2008: ICAS study on IFRSs in UK, Italy and Ireland.

The Institute of Chartered Accountants of Scotland (ICAS) has published a study examining the costs involved in IFRS implementation, the resulting changes in financial reporting, and the most problematic areas of IFRS financial reporting. This report may be useful for Canadian companies currently undergoing the process of IFRS transition.

October 4, 2008: Four planned credit crisis actions proposed by the IASB

In response to the credit crisis, the IASB has stated that it is monitoring developments in the United States and other jurisdictions to avoid inconsistencies between IFRS and US GAAP. The IASB announced the following next steps it expects to take as follows:

- Ensure consistent fair value guidance between IFRS and US GAAP
- Consider the impact of the US Emergency Economic Stabilization Act of 2008 on asset and liability valuation
- Immediately consider the ability to reclassify financial instruments (see October 14, 2008 amendment above)
- Be willing to participate in any study on the impact of accounting on the credit crisis

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