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OFFICIAL SUPPLIER

March 2010

Countdown

Deloitte Canada's IFRS transition newsletter

Welcome to the March 2010 issue of Countdown!

Spring is once again upon us, as we put winter, and a very successful Olympics, behind us! The predictions made by Karen Higgins in January weren't far off from our actual results: she predicted Canada would get a total of 30 medals of which 10 would be gold, we ended up with 26 medals, but 14 of these were gold… and as she predicted both the men and women's Canadian hockey teams came out on top. Well done, Canada, and well done, Karen!

As we are getting closer to January 1, 2011, the much anticipated IFRS changeover date, with only nine months left for calendar year-end entities, our lead article this month focuses on Financial Literacy. This will be a year of significant change for boards of directors, audit committees and senior management, as they work through a conversion year of IFRS choices, decisions and anticipated outcomes.

Lightyear this month focuses on Provisions, which is (and should be) a topic of significant interest for many Canadian entities. In addition, the much awaited International Accounting Standards Board (IASB) project on the same subject is getting closer to the finish line and, therefore, adds some additional interest, and perhaps complexity, to the implementation of this guidance.

As always, we want to continue to understand and meet your needs, so please submit ideas regarding matters that you would like to see us address in Countdown to deloitteifrs@deloitte.ca.

See you again in April!

Don Newell
National Leader - IFRS services

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Assessing and building IFRS financial literacy across the organization

by Karen Higgins

As the countdown towards the IFRS go-live date winds down, there are now only three quarterly reports and one annual report remaining before calendar year-end companies will start publicly reporting under IFRS. As you will see later in "The Real Deal", one of the challenges for Lightyear in implementing the provisions standard is learning the new terms and definitions that are part of the guidance. This applies to numerous other IFRS standards as well. On a broader scale; however, this consideration needs to be addressed across the organization as a whole, from those who prepare the financial statements, and those in senior management who review and approve them, to the audit committees and boards responsible for the oversight process. Indeed, audit committee members in particular are required to meet specific financial literacy criteria when serving on the audit committee of a publicly listed company in Canada. At the heart of financial literacy for any member of the organization or governing body is the ability to read and understand IFRS-compliant information. This would include, for instance, familiarity with the terms and definitions, the ability to understand how an entity's financial position has been impacted by first-time adoption and sufficient knowledge of the rules of IFRSs to be able to interpret the results and financial position of an entity.

Accordingly, if not undertaken already, the first half of 2010 is an appropriate time for organizations to conduct an assessment of their collective IFRS financial literacy. The dual objectives of this assessment would be to (a) communicate to individuals the level of IFRS knowledge they are expected to have attained and (b) identify where supplemental training or other actions to enhance financial literacy may be required.

The following is an overview of some of the major considerations relevant to a financial literacy program to assess and build skills across an organization. The considerations do not contemplate entity specific facts and accordingly should be considered a starting point for your financial literacy assessment that can then be tailored for your organization.

1. Group individuals into literacy categories based on their roles in the organization and their financial reporting responsibilities

The IFRS literacy needs for individuals will vary based on whether or not they are directly responsible for financial reporting and heavily involved in financial statement process, or whether their role is one of oversight and review. The following are examples of the types of major literacy categories that an organization could consider.

Category 1: Detailed knowledge of all IFRSs

Individuals directly involved in the financial reporting process require a detailed knowledge of all IFRSs which impact the organization. Individuals in this group should also ensure they understand the applicable IFRS standards in their entirety and have deepened their knowledge beyond just understanding differences between IFRS and Canadian generally accepted accounting principles (GAAP).

IFRS will soon be the primary accounting basis for the organization, and individuals with responsibility for the financial reporting process should be comfortable analyzing transactions and financial results under the primary IFRS guidance, rather than performing the analysis under Canadian GAAP and then determining if there is an IFRS-Canadian GAAP difference.

One of the primary resources utilized by individuals in this literacy category to develop their personal knowledge should be the official IFRS standards, the basis for conclusions and the interpretive guidance issued by the IASB and the International Financial Reporting Interpretations Committee (IFRIC).

Category 2: Detailed knowledge of certain IFRSs; awareness knowledge of other IFRSs

Certain individuals only require detailed knowledge of a specific or limited number of IFRSs based on the specific nature of their financial reporting responsibilities. For example, an individual specifically responsible for fixed asset reporting may require detailed knowledge of IAS 16 *Property, Plant & Equipment* and IAS 36 *Impairment of Assets* but may only require an awareness level of knowledge for the other standards. These individuals with narrow and specific financial reporting responsibilities should obtain at least an awareness level of understanding of IFRS standards which do not directly impact their current financial reporting obligations to provide them, for instance, with enhanced mobility to other roles within the organization.

Category 3: Awareness knowledge of IFRSs sufficient to perform financial management or financial reporting governance responsibilities

Individuals in this category may include senior management and members of the audit committee. These individuals require sufficient knowledge of the IFRS standards to be able to:

- understand the IFRS policy choices and judgments made,
- understand and interpret the reported financial results,
- challenge the appropriateness of the results, and
- identify potential anomalies in the reported financial information.

In addition, individuals in this category may also be required by the Canadian Securities Administrators (CSA) to obtain a certain level of financial literacy due to their responsibilities for chief executive officer (CEO) and chief financial officer (CFO) certification, or because they are a member of an audit committee. The CSA has explicit requirements regarding the financial literacy of audit committee members. Under CSA Multilateral Instrument 52-110 *Audit Committees*, financial literacy is explained in the following manner:

Meaning of Financial Literacy - For the purposes of this Instrument, an individual is financially literate if he or she has the ability to read and understand a set of financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of the issues that can reasonably be expected to be raised by the issuer's financial statements.

Category 4: Overview knowledge

This final category often includes non-finance members of management or individuals outside the finance function who may have some responsibility for, or involvement in, the financial reporting process. For example, individuals in the investor relations function will require a base level of understanding of IFRSs in order to be able to draft press releases and similar communications. Members of the in-house legal team may need similar knowledge levels to address contracts and agreements. These individuals will need a basic level of awareness and understanding but will likely not require detailed knowledge by standard.

2. Develop and communicate general IFRS literacy targets and objectives for each group

It is important that the organization provide clear expectations regarding the level of IFRS knowledge individuals are required to achieve. In many organizations, training programs have been developed which are customized for the different categories of required IFRS literacy and individuals have been told which training they are required to attend. It is important that attendance is monitored and that the training program clearly lays out the level of IFRS knowledge the individual is expected to have achieved once the training is complete.

It may be unlikely that individuals in each of these categories, especially those in Category 1, would be able to achieve the required level of IFRS knowledge solely through attendance at training sessions. As a result, the training program should identify what other resources, for instance, self-learning and reference materials, are available to assist those individuals in supplementing the knowledge gained during the formal training sessions. For example, individuals could supplement the formal training by completing online e-learning courses for specific IFRS standards such as those available free of charge on Deloitte's global IFRS website www.iasplus.com and clicking on the following symbol: Deloitte IFRS e-Learning

3. Determine a method to assess the IFRS knowledge and literacy

A critical component of any training program is assessing the effectiveness of the training in providing the attendees with a predetermined, required level of knowledge. It may not be sufficient for an individual to demonstrate that they have attended that training but rather they need to demonstrate that they have achieved the level of IFRS literacy that is appropriate for their role.

Organizations should consider how they measure and assess the IFRS knowledge of their employees, management and audit committees. It is most critical that the IFRS literacy of employees with direct responsibility for financial reporting be assessed by the organization, either formally or informally.

While there is no easy answer on how to perform that assessment, organizations could consider providing refresher training on critical IFRS standards before the go-live date. Perhaps the key finance individuals could participate in the development and/or delivery of the refresher training. Another option may be to have regular roundtable discussions on the impact of critical IFRS standards on the organization and encourage active participation by all attendees in the discussion. Other options include requiring individuals to perfom self-assessments using an internally or externally generated quiz, questionnaire or e-learning course.

In conclusion, the achievement of an appropriate level of IFRS knowledge by all individuals involved in the changeover process will be essential to a smooth, error-free transition during this year of change.

The Real Deal

Provisions

One of the core standards that Lightyear had previously not tackled in depth is IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* (IAS 37). This was one of the standards that Lightyear, and other Canadian companies, considered a potential moving target during IFRS transition. Since Lightyear started its IFRS implementation, the standards could have fallen into any one of the following categories:

- Stable – Standards which are not subject to change under the current IASB project plan
- Shaking – Standards which are subject to change but still at a preliminary stage
- Moving – Standards which are at an advanced status of change with a reasonable possibility that a new standard may be effective for IFRS transition in Canada

IAS 37 falls into the "Moving" category ……and has been there throughout the course of the IFRS implementation plan. Lightyear had initially deferred tackling in any depth those "moving" standards to avoid duplication of work at a time when there was no shortage of other standards to be dealt with. However, it's almost the end of March 2010 now and, in consultation with their Deloitte advisor, Hugh Guardian, the team decided it will get to work on completing the preliminary analysis that was started last year.

What's the Deal?

IAS 37 is somewhat of an "umbrella" standard, in that it covers a multitude of areas that are dealt with by specific dedicated sections under current Canadian GAAP. One way of analyzing liabilities is through considering those which are financial in nature, and therefore generally dealt with under IAS 39 *Financial Instruments: Recognition and Measurement* (IAS 39), and those which are non-financial in nature. The latter category, which encompasses a wide range of scenarios, is essentially the subject of IAS 37 (and indeed the proposed successor guidance to IAS 37 is entitled "non-financial liabilities"). This includes items such as matters pertaining to litigation and lawsuits, restructuring provisions, warranty provisions and asset retirement obligations. Temporarily putting to one side the point regarding movement in the standard, the implementation of IAS 37 raises a few other specific challenges:

1. Terminology and key definitions: There are some differences in the new terms and definitions in IAS 37 relative to current Canadian GAAP. The most commonly cited example is that of a contingent liability (IFRS language) vs. a contingent loss (Canadian GAAP). While the terms are almost identical, the definition of each is distinctly different as we will see shortly.

2. Use of Estimates: Remember that IFRS 1 *First-time Adoption of IFRS* (IFRS 1) requires that the same policies be applied throughout all periods presented in the first IFRS financial statements? And then there is of course the "estimates" exception which precludes the use of hindsight in the estimation setting process. IAS 37 is a standard which is framed around liability recognition when there is uncertainty involved and the use of estimates is required. Accordingly, the recognition and measurement requirements of the standard need to be applied with careful consideration of both the IFRS 1 and IAS 37 requirements for all periods presented!
3. Broad Scope: As noted above, IAS 37 sets out specific principles and requirements that are to be applied to a large cross section of non-financial liabilities. Over time, this may perhaps simplify and streamline process designed to capture and measure liabilities but it does represent a significant change from a current Canadian GAAP framework where we have specific standards and interpretations linked to a specific type of liability.

Below we have attempted to clarify some of the potential muddiness that dilemmas such as the above could result in, to summarize how to address these matters in the practical application of the guidance.

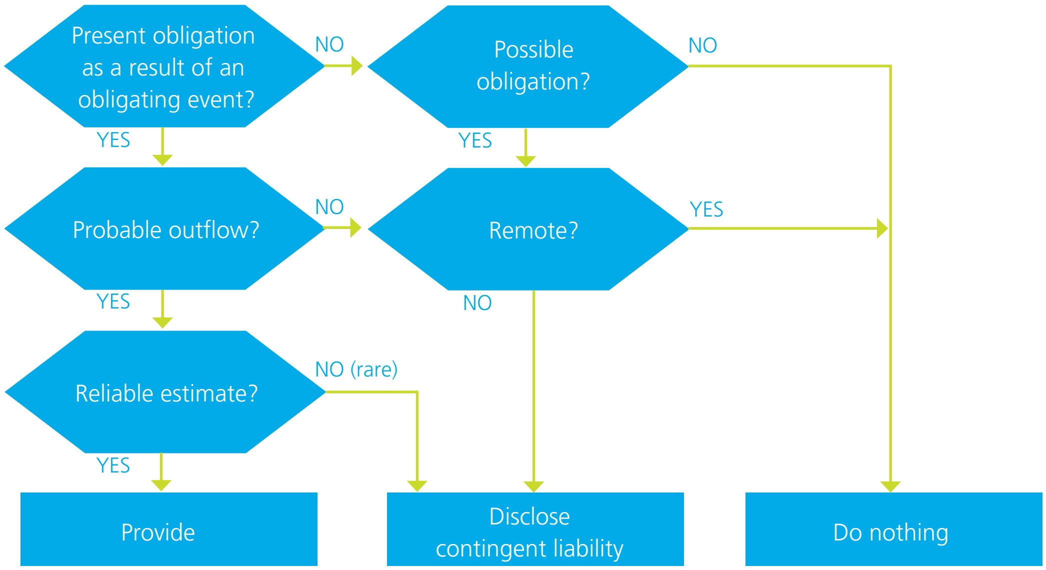
Keeping it Real

Learning the Lingo: What are the key terms and definitions I need to add to my accounting vocabulary and how does this govern the treatment?

Some of the key terms that Lightyear will need to consider (given differences from definitions under Canadian GAAP) are as follows:

<table>
<tr><th>Term</th><th>Definition</th><th>Treatment</th></tr>
<tr><td>A Provision</td><td>A liability of uncertain timing or amount</td><td>• Recognize as a liability</td></tr>
<tr><td>A Contingent Liability</td><td>A possible obligation that will be confirmed by one or more future events
or
A present obligation that is not probable or cannot be measured reliably</td><td>• Not recognized as a liability
• Certain disclosures required (unless remote possibility of an outflow of resources)</td></tr>
<tr><td>A Legal Obligation</td><td>An obligation that derives from:
• A contract;
• Legislation; or
• Other operation of law</td><td rowspan="2">• Both legal and constructive obligations will be assessed under the IAS 37 criteria to determine whether they meet the definition of a provision or contingent liability
• The same assessment applies independent of whether the obligation is contractual/legal vs. constructive in nature</td></tr>
<tr><td>A Constructive Obligation</td><td>An obligation that derives from an entity's actions:
• An established pattern of past practice, published policies or a sufficiently specific current statement, indicates to other parties that the entity will accept certain responsibilities; AND
• As a result the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities</td></tr>
</table>

A decision tree, extracted from the appendix to IAS 37, provides a visual summary of the treatment of obligations in the table above.



From a terminology standpoint, Hugh points out to the Lightyear team that many of the items that are recognized as "contingent losses" under Canadian GAAP would also meet the recognition criteria under IFRSs, but would fall under the category of provisions. Any reference to a liability as being 'contingent' is reserved for those situations where, for the time being, only disclosure is required. One final point to remember is that liability recognition under IAS 37 refers to probable outflows of resources arising from present obligations, probable under IAS 37 meaning it is more likely than not (i.e. 50%). Under Canadian GAAP, loss recognition attached to similar events is based on consideration of whether "it is likely" that a liability has been exercised. In this case, on transition, some attention to the fine print is required to ensure this change in approach is appropriately implemented, despite the similarities on the surface of parts of the guidance.

I need to better understand how to address my estimation process under IAS 37 combined with the estimates I made under Canadian GAAP combined with the IFRS 1 exception. I'm also a bit concerned as it's now the end of March 2010……….have I left this all too late?

IAS 37 is a standard which focuses on uncertainty, future events and outcomes which are beyond the control of the entity. Measurement of the provision should be based on the "best estimate of the expenditure required to settle the present obligation at the end of the reporting period". New events that occur, or conditions which are after the end of the reporting period are not subsequently incorporated into the estimate.

When it comes to first-time adoption of IFRS, Lightyear should ensure that its provisions under IAS 37 at the date of transition are indeed based on those conditions which exist at the date of transition. The fact that, for Lightyear, the date of transition has passed does not mean this task cannot be done; however, the longer the passage of time between the end of the reporting period and the estimation process, then the more difficult it will be to ensure that the benefit of hindsight has not been incorporated in this process.

What are some examples of the items within the scope of IAS 37 and how should I deal with this?

Below are some simplified examples related to Lightyear which are likely to be situations common to other entities.

Type of risk	Considerations
Lightyear has a class action law suit filed against them relating to damages incurred from a fire six years ago. The matter is currently in the midst of legal proceedings. An out-of-court settlement is not something that is contemplated at this time. Lightyear's internal legal counsel advises that it is not probable that the entity will be found liable. External counsel indicates that the outcome of the matter is not presently determinable.	• A past event has occurred and Lightyear will need to determine whether or not there is a present obligation based on analysis of all pertinent facts at this date • A provision will be recognized under IFRS if an outflow of resources (e.g. the entity is required to pay damages) is probable and can be reliably measured • IAS 37 generally requires fairly substantive disclosures related to provisions and contingent liabilities – including those attached to lawsuits. In "extremely rare" cases an alternative and less specific level of disclosure is permitted where such disclosure could seriously prejudice the position of the entity. The use of this more general disclosure allowance should be limited only to the situations where an entity can fully support the reasons behind the non-disclosure • Considerations will include: – Internal and external legal counsels' views – Current status of legal proceedings – Events in the post-transition reporting period to the extent that they provide further evidence of conditions which existed at the date of transition • The analysis would be similar under Canadian GAAP. In this instance, a contingent loss would be accrued only if it was likely – a higher recognition hurdle than IFRSs
Lightyear is considering closing down one of its divisions that is unrelated to their core business. A detailed plan for closing the division (including severance calculations) has been agreed to by the board and management, but has not yet been communicated to customers or employees that will be affected. No portion of the plan has been implemented at the date of transition.	• The plan has been approved but <u>not communicated</u> to those affected by it at the date of transition • Specific guidance exists on this in IAS 37 relating to restructuring provisions approved by the Board but not yet communicated • Under IAS 37, this would not meet the definition of a present obligation from a past event at the date of transition • Under Canadian GAAP, this is addressed in interpretative guidance in EIC-134 *Accounting for Severance and Termination Benefits* and EIC-135 *Accounting for Costs Associated with Exit and Disposal Activities* • The treatment under Canadian GAAP would need to be analysed with the timing of liability recognition varying with the nature of the various closing costs
Lightyear offers warranties on products for two years from the date of purchase on all manufacturing defects. Past experience shows that there will be some claims.	• A past event has occurred • Lightyear believes there is a present obligation based on past history. Although there is some uncertainty as to the amount of future claims, there is enough past history and data on the products impacted to reliably measure the required provision • Lightyear believes that it should recognize a provision for warranty claims under both IFRSs and Canadian GAAP at the date of transition. As IAS 37 contains specific measurement examples on provisions such as warranties, Lightyear will need to review these and assess whether they are, or would be expected to be, aligned with the Canadian GAAP measurement basis

Disclosure

Consistent with the general IFRS trend, disclosures relating to IAS 37 are more extensive than under Canadian GAAP. In general, the objective of the disclosures required under the guidance is to ensure that sufficient information is disclosed in the notes to the financial statements to enable users to understand the nature, timing and amount of provisions, contingent liabilities and contingent assets.

Some of the items that will now required to be disclosed in the notes to the financial statements, such as uncertainties about the amount or timing of expected outflows and major assumptions made concerning future events, were previously disclosed in Lightyear's management's discussion and analysis (MD&A) and not in the entity's financial statements. This additional financial statement footnote disclosure, plus the requirement to provide a continuity or rollforward of the carrying amount of each class of provision, will require Lightyear to consider whether additional internal controls are required with respect to the collection and reporting of this information. In addition, sufficient information must be obtained from the financial reporting systems to ensure this information can be audited by their internal and/or external auditors.

Movement in the Standard

IAS 37 is expected to be changing, the exposure draft (ED) has already been issued, with a final standard expected during the second quarter of 2010. Lightyear has concluded that the revised liabilities ED is a significant change from the current standard and may be subject to amendment after the comment process so they have determined that they will adopt the current version of IAS 37 and monitor the project.

Next Steps

The key steps that Lightyear has to complete in their preparation for transition to IFRSs are: identify constructive obligations which may not have been recognized under Canadian GAAP, consider if any onerous contracts need to be recognized and prepare for the increased disclosure requirements. Lightyear must also communicate with their lawyers on IAS 37 to ensure that legal letters and confirmations continue to provide the desired information and evidence within the terminology of the standard.

Deloitte IFRS publications and events

A comprehensive summary of Deloitte IFRS 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.

Webcasts

IFRS technical update – Keeping current in a year of change! - It's official – the IFRS standards have now been incorporated into the Canadian Institute of Chartered Accountants (CICA) Handbook. Stay up to date with recent activities at the CICA and the International Accounting Standards Board (IASB) on key projects under development and how they may impact your organization. Keep current on matters being discussed by the Canadian Accounting Standards Board (AcSB), the Canadian Securities Administrators (CSA) and other regulators. Receive some tips and suggestions to consider during your 2010 conversion activities.

- **March 23, 2010** - English session
  View archive here
- **April 7, 2010** - French session
  Click here to register

Beneath the numbers - A systems perspective on IFRS - Information systems are an integral part of the IFRS conversion process as data, reporting, and disclosure requirements change under IFRS. To accommodate these new standards, modifications may be required to source data, interfaces and the chart of accounts. Age and flexibility of current systems, as well as potential impacts to other systems and processes will drive decisions to replace or upgrade systems. Starting early and mapping out how your information systems will be impacted by IFRS are important first steps. This webinar will provide you with tools to address information system challenges on your journey to IFRS conversion.

- **April 27, 2010**
  Click here to register

Toronto

IFRS workshop series: The journey together.

- **April 14, 21, 27:** An IFRS workshop series specific to investment dealer firms. For more information please click here.
- **April 21, 22, 28:** An IFRS workshop series specific to mutual fund dealer firms. For more information please click here.
- **April 14, 22, 27:** An IFRS workshop series specific to dealer and adviser firms focusing on portfolio managers, investment fund managers, exempt market dealers and restricted dealers. For more information please click here.

Calgary

IASeminars – IFRS Hot Topics for Oil and Gas Entities

- **May 26, 2010**
  Click here for more information

International Round-up

Updates and news from the IASB

March 3, 2010 IASB updates its work plan

The IASB's work plan, which details its best estimate of document publication dates of IFRSs, has been updated as of March 3, 2010. Click here for further details.

March 15, 2010: Conceptual Framework ED on reporting entity

The IASB and the US Financial Accounting Standards Board (FASB) have published an exposure draft (ED) on the reporting entity concept. The proposals form part of a joint project to develop a common and improved conceptual framework that provides the basis for developing future accounting standards. The ED proposes what a reporting entity is and when an entity controls another entity. Comments on the ED are due by July 16, 2010. Click here for further details.

March 21, 2010: Comment deadline extended on proposal to replace IAS 37

The IASB extended the deadline to comment on a revised exposure draft (ED/2010/1) of one section of a replacement for IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. That section deals with measurement of liabilities that are within the scope of IAS 37. The original deadline for comments on this exposure draft was April 12, 2010 but this has been extended to May 19, 2010. The IASB intends to replace IAS 37 in the third quarter of 2010. Click here for further details.

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