

IFRS conversion

Who's managing risks
on the road ahead?



The journey from Canadian GAAP to IFRS is dotted with risks

How will you navigate the bumps ahead?

Getting from Canadian Generally Accepted Accounting Principles (GAAP) to International Financial Reporting Standards (IFRS) will take every Canadian publicly accountable enterprise on a journey deep into every corner of their organization. To effectively manage this complex, interconnected process, organizations will need to explore the implications of changing not only financial and tax reporting, but also processes as diverse as human resources and compensation, budgeting and forecasting, CEO and CFO certification, contracts and financing agreements – to name a few. Adopting IFRS is not simply a policy change; it is a business change. And if it's not well planned and well managed, it could be a rough – and unnecessarily costly – ride.



Do you know who's in the driver's seat?
Have you mapped out your risks?
It's time to buckle up and plan a
risk intelligent ride.



Managing risk on the journey from Canadian GAAP to IFRS

A **Risk Intelligent Enterprise™** is one that is positioned to effectively identify, assess and manage risk exposure – making the difference between creating value and jeopardizing success. When it comes to IFRS, this means making risk management a constant companion on your conversion journey.

Organizations that **invest in a risk assessment** of their IFRS conversion plans and activities can avoid project delays, missed deadlines, increased costs, and other negative impacts on processes, personnel or systems.

With change comes risk. Changing from Canadian GAAP to IFRS is going to pose new risks for Canadian publicly accountable enterprises between now and the 2011 adoption deadline. Getting from here to there with minimal disruption will require a risk intelligent approach.

In a Risk Intelligent Enterprise™ – an organization that views risk management not as a task but as part of the culture, the way of doing business – managing the risks of IFRS starts with embedding risk management in the IFRS conversion plan. Considering that IFRS conversion will require management to explore many implications, it promises to be a complex journey. **Who's helping you navigate the risks?**

The risk paradigm: recognizing weaknesses builds strength

According to Deloitte Canada partner and IFRS enterprise risk specialist Steen Skorstengaard – who guided clients through the European Union's 2005 IFRS adoption before moving from Denmark to Canada in 2006 – poor project management is almost always the underlying cause of project failures. And every project management weakness exposes an organization to specific risks. With IFRS, common project management weaknesses include:

- underestimating resource needs
- not understanding impacts on information technology and finance
- ineffective organization structure
- poor communication
- poorly defined roles and expectations

Recognizing such potential pitfalls is the first step in keeping IFRS conversion plans on the straight and narrow.

Because IFRS impacts virtually every corner of the organization – going beyond accounting – it presents an opportunity to create inroads toward a stronger overall risk management culture. The key is to take a step back and review plans before the IFRS rubber hits the conversion road. That means having risk professionals – whether your own internal audit team, or an external provider such as Deloitte – review the IFRS implementation plan. Organizations that invest in this crucial step in the planning process minimize project delays, missed deadlines, increased costs, and other negative impacts on processes, personnel or systems. However, management needs to be prepared to consider challenges to the strategy, and be prepared to make changes to the plan.

“To avoid costly surprises, organizations need to adopt a risk intelligent approach, making risk management an inherent part of managing the conversion project. This approach enables a focused and pragmatic implementation, in which you recognize and deal with what matters. Unless you prioritize your decisions, the work can become overwhelming.”

Steen Skorstengaard, Partner, Deloitte



Surveying the IFRS terrain: the three-phase IFRS conversion approach

First things first. Before you create your IFRS conversion plan, you need to take a step back and envision the steps required to get there. Most organizations take a three-phase approach to IFRS adoption.

Phase 1 Map every impact

Before an organization moves ahead with IFRS adoption, it's vital to map the impacts across the organization. The goal is to understand what processes, people and systems will be affected, who needs to be involved in planning the journey, and what red flags may appear on the road ahead. There are several points of view to consider, including:

Reporting

How will IFRS affect current reporting, both internally and externally? Answering this question requires mapping the source and applications for every piece of financial data that will be released publicly and in internal reports used by management. Not surprisingly, whether you simply create a mock-up of financial statements as they would look under IFRS or undertake a more substantial review, this exercise will inevitably lead down multiple parallel and interconnected paths. By identifying the sources of data, you can pinpoint which policies and financial reports will need to be adapted, and track the chain reactions of each disclosure choice.

Process and systems

Processes and systems at the heart of generating financial data will undoubtedly be impacted. Organizations need to consider how adopting IFRS will affect closing and reporting processes. Timelines and responsibilities may change. Additional reconciliations may need to be performed and reviewed. Accounting processes and systems to maintain current reporting standards need to be carefully reviewed. New IFRS-driven policies must be embedded in your staff's day-to-day reporting processes.

Tax

IFRS presents new tax opportunities; the question is how to take advantage of them. Organizations must be ready to revise methodologies for calculating and disclosing income tax. Because tax data is often housed on a different – and often very manual – technology platform, there may be separate tax-related system and process issues to address. Tax has been the biggest cause for material weaknesses in Sarbanes-Oxley Act (SOX), so changes need to be given high priority.

Legal

The effects of conversion to IFRS will also ripple out to your legal department. Many contracts and financing agreements will need to be re-examined for possible impact. Changes to how income and fixed assets are measured may mean that some contracts need to be updated or even renegotiated and restructured.

Internal controls

What steps will the organization take to ensure the control environment continues to support accurate and timely reporting within an IFRS environment? Entity and process level controls, disclosure controls, as well as information technology controls, will all need to be aligned with IFRS requirements.



Investor relations

Management's discussion and analysis (MD&A) will have to reflect any modification of comparative results of operations on conversion, as well as any material changes that may evolve pre-conversion. With the time-sensitive nature of this task – companies must produce coherent analysis for the first quarter of the IFRS conversion year within days of completing the Canadian GAAP-based annual report for the previous year – companies will need to manage investor expectations. How will you explain the impact or fluctuations of earnings per share and return on capital?

Training

The best-laid adoption plans won't go far unless the people behind the systems and those responsible for putting processes in motion are IFRS-literate. Who are the key internal stakeholders? What do they need to know to perform their jobs under IFRS? Management must recognize that training applied broadly across the organization is ineffective and costly. Instead, organizations need to identify key stakeholders, and determine the information needs of each group – including boards and audit committees.

Project management office

It can't be stressed enough that risk intelligent project management is a cornerstone of successful IFRS adoption. Who will keep track of progress, and track every key risk? The project management office needs to be involved at every step, establishing a comprehensive plan, monitoring and coordinating conversion activities, and setting in place a strong risk assessment process – an issue discussed in more detail later in this document.

Phase 2

Get changes rolling

Phase II is all about unrolling the IFRS map, and getting started on conversion preparations – following a comprehensive plan with clearly defined responsibilities. With IFRS affecting systems, processes and people in every corner of the organization, an effective IFRS plan allows the organization to simultaneously complete several different conversion activities. To ensure that risk management is an integral part of the project during this crucial conversion phase, organizations need to address certain risk-related questions. These include, but are not limited to:

Technology

What are the risks of adapting your current technology system, versus completely replacing the system?
Can your current system even be adapted to IFRS?

Interpretation

Principle-based elections under IFRS provide flexibility, allowing each organization to best align financial reporting with the nature of their business. However, inevitable differences of interpretation introduce a new set of risks – including potential disputes with your auditor and differences within your industry. What are the risks associated with your interpretations?

Disclosures

In adopting IFRS, explanations will be required within the quarterly management's discussion and analysis, press releases, exemptive relief, and revisions to debt arrangements – not to mention the expanded notes to the financial statements under IFRS. Do you know what needs to be disclosed and when? How will you ensure disclosures remain consistent from the parent company through to every subsidiary?

Whether you're currently scoping the impacts of IFRS, or are already well down the road toward IFRS adoption, **there's no time like the present to manage IFRS conversion risks.**

Boards and audit committees

How will the organization ensure that boards and audit committees are appropriately engaged in IFRS decision-making? What steps will be taken to ensure these groups have the level of IFRS literacy required to fulfill their responsibilities? Will the audit committee expect the internal audit team to review the process? Have the CEO/CFO certification implications been considered and worked into the plan?

Tax planning

With changes to both the financial source data and the areas that require deferred tax calculated, companies can anticipate changes in tax planning. What are the tax implications of IFRS – now and in the future? Who is assessing this?

Policies and processes

Have you reviewed all policies and processes to ensure they align with IFRS requirements? Have you considered how to involve your auditor in policy development? Who's leading the implementation of necessary changes?

Post-adoption

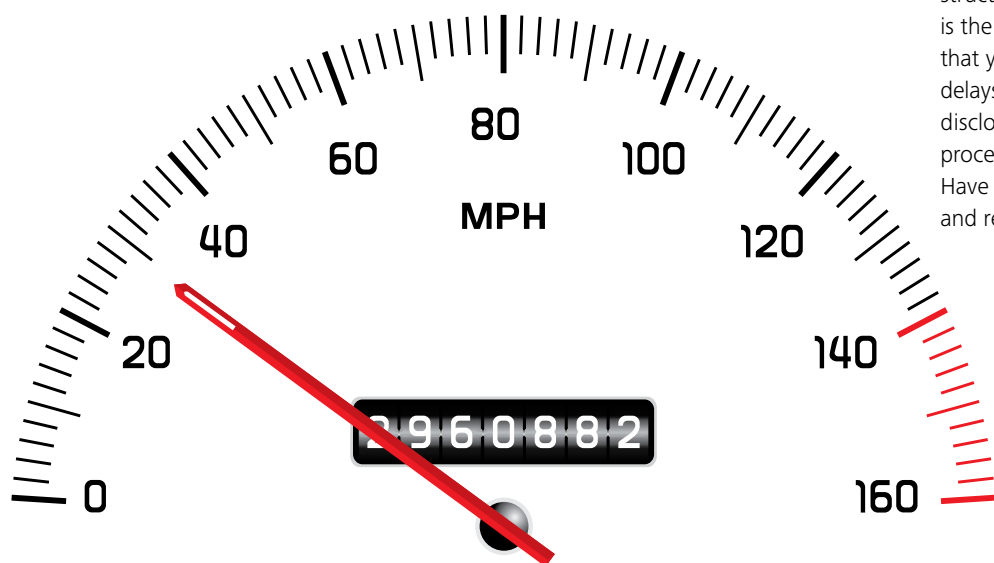
IFRS standards will evolve over time. What processes are in place to ensure you will constantly reassess your interpretation and application of individual standards as they change?

Whether these activities run in parallel or are interconnected, intelligently managing risks will require strong communication and role definition at every step of the way. Keep in mind that although all roads may lead to IFRS, strong risk management throughout the conversion journey can ultimately make the difference between a well-coordinated adoption and a last-minute scramble to issue the initial set of financial statements prepared under IFRS.

Phase 3

All systems (and people and processes) go

Before any organization releases its first set of financial statements prepared under IFRS, there's one last bridge to cross: taking IFRS plans for the ultimate test drive. In this final pre-adoption phase, all paths laid during Phase II converge, and it's time to see how systems, processes and people will respond when the IFRS light turns green. While you can expect this to be an iterative process, which will vary depending on the structure and size of your organization, the end game is the same: you must conduct testing to guarantee that your financial reporting processes will work. No delays. No errors. No questions about interpretations or disclosures. This will inevitably require you to revise the processes that you spent so much effort developing. Have you built these final checks into your timelines and resourcing?



The risk assessment: it's never too late to manage risks

The bottom line is that properly applying risk management principles will help save your organization money.

While it's best to set a strong risk management tone from the beginning, it's never too late to adopt a risk intelligent mindset. No matter when – and to what extent – you embrace the principles of risk management in your IFRS conversion, it's an investment that will be well worth the effort. It will enable you to efficiently allocate resources, and avoid such risks as flawed audits, ineffective certification results, or even restatements.

Building a strong risk infrastructure

It's clear that with IFRS affecting most of the organization, creating a comprehensive project plan will require gathering multiple perspectives. But the more people you have driving change within particular areas of the organization, the more potential there is for risk exposure. Organizations should define ownership for project management activities – whether it's an individual, a team, or an external organization such as Deloitte – to track every milestone.

To ensure your IFRS risk management infrastructure is built for the long haul, it must be designed with an eye for sustainability and continuous improvement. This requires a defined process and frequency for reviewing risk components and making appropriate updates, and for identifying – then sharing – lessons learned along the way. There must also be effective communication among management, complete with a reporting system to escalate any perceived risks or failures, and safeguards to ensure data integrity of management reports.

Establishing a consistent decision-making direction

To establish consistent rules for managing risks along the road, a risk intelligent IFRS infrastructure must include a risk assessment and a mechanism for ongoing risk tracking. Regardless of where you are on the IFRS journey, the risk assessment approach is essentially the same. A risk intelligent approach to managing IFRS risks involves the following key steps:

Step 1 – Identify potential events and risks as opportunities or threats to successful IFRS adoption. As part of this process, pinpoint risk interdependencies and interrelationships, then map where these risks need to be communicated at all levels of the organization.

Step 2 – Assess and measure each risk, drawing insight from internal and external subject matter experts. Anticipating the events that lie ahead, you should examine both the initial inherent risks and any new vulnerabilities that could arise as a result of mitigation activities – creating a sustainable assessment process for evaluating financial and non-financial value impacts.

Step 3 – Develop a response plan that prioritizes risks according to impact and vulnerability. This categorized plan should include specific tasks, resources required, responsibilities and time frames – taking into consideration alternative risk responses based on the enterprise's risk tolerance and risk appetite.

Step 4 – Build a monitoring system with established risk thresholds to act as an early warning. Establish ongoing monitoring and reporting that will allow you to quickly detect significant risk changes. Build in the flexibility to incorporate follow-up on any corrective actions taken in response to management assurance activities.

Step 5 – Assure and escalate risk related issues and risk mitigation analysis to executive management and the board. To do this, you will need to constantly gather, analyze, aggregate, communicate and report on your activities.



Creating a risk register: prioritizing, allocating and communicating each item

With an infrastructure in place and decision-making direction set, it's time to create a categorized inventory of risks – a “risk register” – that will act as a reference point for monitoring risk throughout the conversion process. By doing this, organizations get a snapshot of all of the risks associated with every facet of their IFRS project and, depending on the organization's appetite for risk, can decide how to respond. While Phase I is the ideal time to establish a risk register, there's really no wrong time to take stock of risks.

With each decision having the potential to cause chain reactions within other IFRS adoption activities, organizations can expect the risk register to be a constantly evolving document – one that requires ongoing oversight by a knowledgeable person with the time and authority to take action when required. For each risk, the organization essentially needs to decide:

- Is this something our IFRS adoption plan needs to address?
- Does the issue require further discussion or tracking?
- If a decision is required, who needs to make it and when?

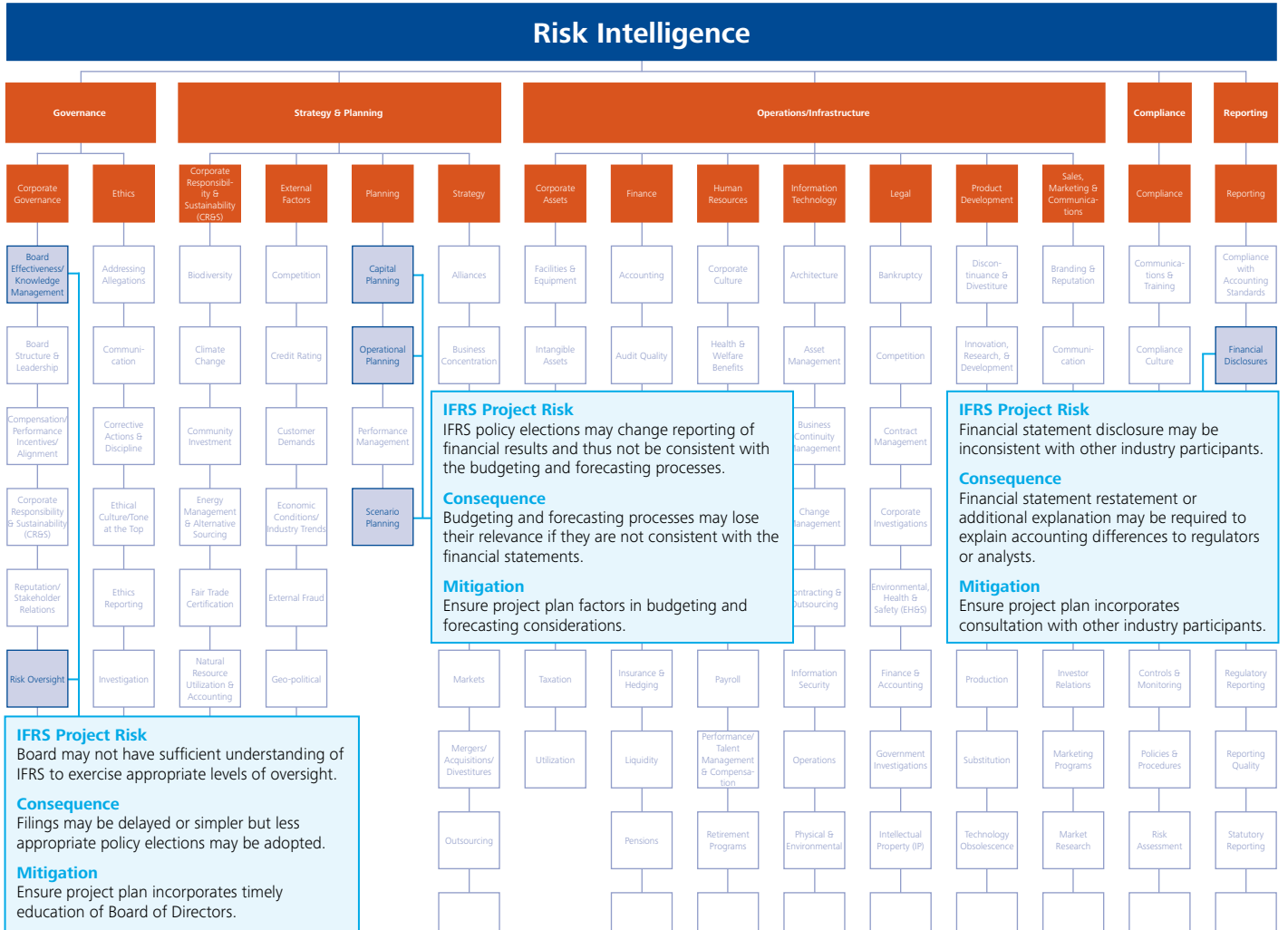
Drawing from the IFRS conversion plan, **the IFRS project team should create a categorized inventory of risks – a “risk register”** – that will act as a reference point for risk throughout the process.

Explore your risk universe: taking it from the big picture to single steps

How do we put this theory into practice when adopting IFRS? To help clients explore and identify where potential risks lie, Deloitte maps out a risk universe that represents potential areas of risk exposure. It will vary in size and significance for each business. This big-picture risk universe is used to map out a risk register. From that risk register, the organization can track the consequences of each risk – outlining the paths you can choose from to navigate each risk. From this perspective, risks can be prioritized and scheduled accordingly. It doesn't have to be complex. To illustrate the process, take a look at a few examples – which zoom in from the big picture to individual items in the risk register.



The Risk Intelligence Map is not a definitive or comprehensive representation of all possible risks that may be encountered by an organization. Consider customizing the Risk Intelligence Map based on risks that impact your organization. Areas to consider could include regulatory, geographic, industry, and company-specific issues.



Widening the risk viewpoint: beyond financial reporting

There's no question that an enterprise's finance team needs to be at the core of IFRS conversion activities. After all, finance will be the driving force behind translating the organization's accounting policies from Canadian GAAP to IFRS, and redesigning financial statements.

And with such a complex journey ahead, someone needs to be at the wheel – typically the controller or another senior finance person. To ensure that every stakeholder is delivering on expectations, this person will need to adopt a broad risk viewpoint. That means consulting a range of stakeholders affected by the cascading impacts of financial decisions, each of whom will bring different risk perspectives from guiding changes in their own particular area.

Looking beyond financial reporting, at least three other specific stakeholder groups can expect significant impacts from IFRS conversion: internal audit, internal control certification, and information technology. This trio needs to be directly involved along the IFRS journey, as they can provide unique insights into particularly challenging aspects of the conversion effort. Keep in mind, of course, that while these three groups should anticipate notable impacts from IFRS conversion, other stakeholders will need to be addressed as well – including tax, treasury, investor relations, legal, boards, and audit committees, to name a few. With that in mind, let's walk through some of the responsibilities internal audit, internal control certification, and information technology may be asked to fulfill.



The role of internal audit

Shouldering responsibility for providing objective assurance and proactive monitoring of enterprise-wide risks, internal audit has a central role to play in keeping IFRS activities on the proper path. Key areas where internal audit should be involved include, but aren't limited to:

Enterprise risk assessment

Do you have a clear picture of how IFRS will affect enterprise risk? Are current risk management procedures adequate to manage evolving risks?

Project management

Are you engaged with the IFRS steering committee as a meeting observer? Is there a process in place to conduct periodic project reviews, to ensure the project remains on track, and that risks are constantly re-assessed?

Data and system conversion

With a 2011 deadline for adoption, 2010 implementation year will be the make-or-break year for IFRS data and system conversion. Have you reviewed the data conversion strategy and plan? For example, are there adequate controls over capital asset data conversion – data cleansing procedures, mapping of converted data, handling of data exceptions or invalid data procedures, timing of conversion, and reconciliations?

Internal control over financial reporting

Do you know what new or revised business processes are being developed to compile additional IFRS-compliant data? Have you performed a walk-through of these processes to identify key controls and test operating effectiveness?

Post-adoption

Have you reviewed the reasonableness of management's judgment and estimates, and ensured this judgment is being consistently applied? Do you know how your organization's interpretations of individual standards compare to industry peers – or what policies and processes are in place to maintain industry consistency?

The role of internal control certification

Internal control certification teams must have their fingers firmly on the pulse of change throughout IFRS conversion – even more than their global counterparts who have already completed IFRS conversion. That's because Canadian public companies face stringent requirements around internal control certification, and disclosure controls and procedures, to cover changes in GAAP as well as normal course activities.

This group must pay particular attention to documentation, ensuring updates reflect new and updated controls, and that the design and operating effectiveness of those controls have been adequately evaluated. Policies, procedures and documentation – along with the underlying associated internal controls – will likely need to be adjusted to accommodate the re-designed accounting, reporting, consolidation, reconciliation and disclosure processes. With this in mind, internal control certification's scope of activities can include, but are certainly not limited to:

Scoping and risk assessment

With each IFRS interpretation creating potential changes to the organization's risk profile, how will risk assessment and internal control over financial reporting (ICFR) processes be adapted? Have you assessed accounting policies and IFRS 1 elections? Does the project plan provide an adequate level of detail around the specific activities and timing to address IFRS transition? Are you confident that risk assessment and scoping will be constantly re-evaluated?

Disclosure controls and procedures

Are there communication protocols in place to ensure policies and procedures remain relevant within the new IFRS environment? Are you confident that the board and audit committee have the appropriate level of IFRS literacy to review disclosures?

Entity level controls

What are the financial reporting risks of IFRS implementation? Have you assessed the control environment? Is the audit committee effectively responding to reporting implications? Does the core accounting or reporting team have adequate knowledge of IFRS to complete conversion activities, and operate within an IFRS environment?

Business process controls

Do you understand the new processes required to comply with IFRS reporting requirements? Have you ensured that process owners have received adequate IFRS training, and have the tools to assess the impact of accounting changes on their controls? Are you confident that process owners are equipped to assess the impact of any deficiencies identified?

Information technology

Have you reviewed technology-related IFRS change management controls? Have existing information technology or general computer controls been assessed to identify processes that need to be updated or established? Are you confident that existing information technology controls are sufficient to address the dual reporting environment?

Beyond 2011

Like Canadian GAAP, IFRS standards will constantly evolve. Processes need to be put in place to ensure the organization is aware of – and equipped to respond to – changes. Are you confident that the ICFR and IFRS teams are well positioned to maintain two-way information flow throughout conversion and after adoption? Have you clearly defined the potential impacts of failure to meet IFRS deadlines?

The role of information technology

Adopting IFRS will require close collaboration between your IT and finance teams. As data flows through technology, getting further from its source, the risk of errors increases. IFRS is expected to have wide-ranging effects at different levels of information technology systems architecture, requiring significant time and resource commitments. Realignment of information systems will pose a real challenge not just for IT, but for the entire organization. Virtually every application and interface in the system architecture can be affected – from the “upstream” source of data to the farthest “downstream” end of reporting tools. As you plan changes to your IT systems, the scope of activities to be considered should include:

Information quality

To make IFRS-based accounting decisions, you’ll need access to historical data. Do you know where historical data will be stored? Will you be able to locate this data during and after IFRS conversion?

Reporting data warehouses/data marts

Do you fully understand the changes to financial reporting requirements – and have you assessed how these changes will impact information management systems? Are you confident that data governance functions and metadata repositories will be able to handle new data definitions?

Upstream systems

Have you thoroughly analyzed upstream systems – including financial sub-ledgers, financial instrument or investment valuation systems, product-specific systems, and interfaces that post financial transactions – to identify and document which internal and external data sources need to be updated? Are you confident that you have flagged all data that will be missing due to differences in account treatment? Have you ensured that required enhancements to legacy systems are included in the IFRS plan?

Downstream systems

Do you know what additional information will be needed to support IFRS reporting and disclosure requirements? Are you confident that the information systems are sufficient to provide information on non-financial data that may be required – directly or indirectly – to support IFRS analyses? Are you confident that the business intelligence environment will be IFRS-ready?

Infrastructure

Do you have a clear picture of how IFRS will impact support applications such as rules engines, allocation engines, middleware and operation data stores that affect or transact financial information? Will IFRS changes affect outsourcing arrangements or systems?

Making it personal: addressing “me” issues across the organization

While there is clearly a significant amount of work to be done to prepare systems, processes and controls, don't forget to take a step back to understand the human impacts of IFRS conversion. Successful organizational change will require robust communication and strong support from the people responsible for living out changes day-to-day. Companies will need to be ready to answer the most basic question arising from any organizational change: “How will this affect me personally?”

In order to develop and deliver targeted communications and training, all enterprises need to identify key internal stakeholder groups – whether they're tied to particular business units, processes, levels within the organization, or other criteria – then pinpoint the impacts on each group. For example, if your compensation is tied directly to earnings per share, how will IFRS affect your people's compensation? If certain policies or processes need to change, are the people responsible for applying these policies and processes aware of the how this will affect their daily decision-making? The bottom line is that different stakeholders will require different types and levels of information, so organizations need to develop a tailored training program that connects all of the IFRS dots.



Where to go from here

Organizations currently working toward IFRS adoption vary widely in terms of size, industry, stakeholders and appetite for risk, so there's no all-inclusive guide that will suit everyone. You now have a snapshot of the road ahead, and are alert to some of the risks inherent throughout the IFRS conversion process. But every organization will need to map its own unique route from Canadian GAAP to IFRS. You know your organization best, but that doesn't mean you need to go it alone.

Deloitte has taken countless organizations on the IFRS adoption journey around the world. Pairing insight from global professionals and industry specialists, with a proven understanding of the Canadian business terrain, Deloitte's IFRS professionals are ready to guide you on your IFRS journey.

The next step is yours.
Make sure that step
points you in a risk
intelligent direction.



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