

INFORMATION TECHNOLOGY ADVISORY SERVICES

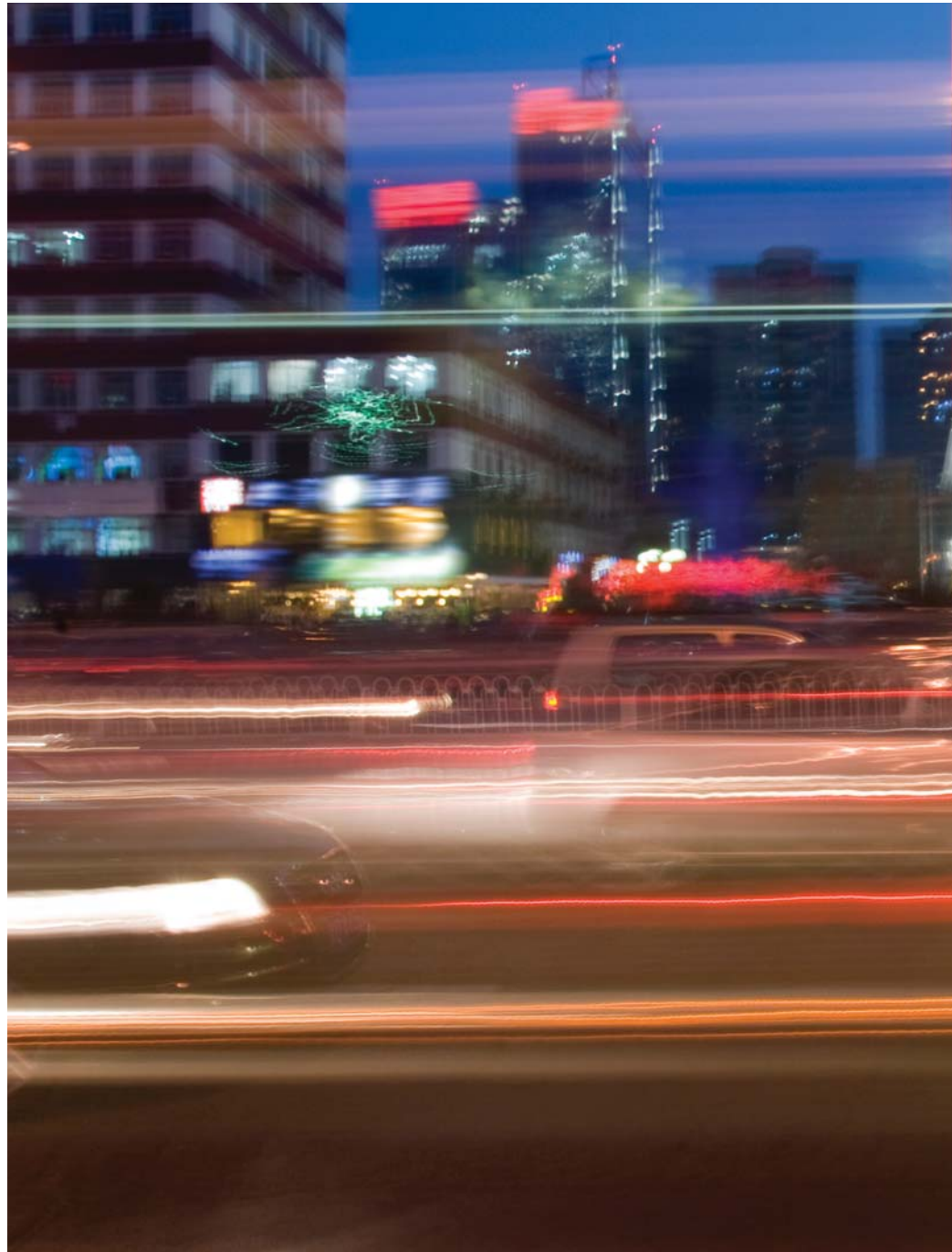
The Effects of IFRS on Information Systems

ADVISORY



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Executive Summary



IFRS—Today's Challenge

Many Canadian companies are considering how extensively they may be affected by the upcoming shift from Canadian GAAP to International Financial Reporting Standards (IFRS).

IFRS conversion has posed a significant challenge to those organizations that have undertaken it in almost 100 countries worldwide. The conversion is a substantial business change project being undertaken by large sectors of the global business community and will make a significant contribution to achieving transparency and increased understanding of global financial reporting. Many companies have found that while their conversion initially appeared to be an accounting challenge, it quickly evolved into a multifaceted business initiative involving systems and processes, people and change management, and other business considerations. To accomplish these initiatives, organizations generally establish a program management office (PMO) with oversight by C-level management and with participants representing finance and accounting, IT, process, controls, change management, and tax.

The complexity of an IFRS conversion results from circumstances both inside and outside the organization, including

- The intricacies of the technical accounting standards
- The overlap with local and international regulatory considerations
- The need to implement the conversion across business units and countries
- The number of separate information systems in use within many organizations
- The limited number of IT professionals with IFRS technical knowledge who have the ability to interpret and translate it into IT changes.

Effects on Information Systems

Worldwide, companies have spent considerable time, money, and other resources to convert to IFRS—and many of them report that a substantial component of their conversion costs were IT related. Nonetheless, many companies also report benefits from the IFRS conversion, including consistency of processes and applications that have helped improve their global IT architecture.

Implementation experience in Europe indicates that the cost of IFRS conversion for Canadian companies is also likely to be significant, depending on how they approach and plan the effort. For example, in the initial phases of conversion many European organizations focused heavily on the technical accounting involved in this change and neglected information systems—a strategy that ultimately resulted in higher conversion costs overall.

The effect of IFRS conversion on IT systems arises from 1) differences in the accounting treatment between current accounting standards and IFRS, 2) increased level of disclosure required under IFRS and 3) the requirements to report financial information under Canadian GAAP and IFRS for 2010 (commonly referred to as the dual reporting requirements). Conversion may create a need for

- New data
- Changed calculations
- Changes in reporting.

Key IT Take-Aways

- IFRS is accounting-driven but it will drive major changes to IT systems, as well as business processes and personnel.
- Experience indicates that IT costs are generally a significant portion of the cost of IFRS conversion.
- Organizations benefit when they identify and integrate the efforts of the IT team early in the IFRS conversion process.
- IT efforts will comprise a mix of short- and long-term projects within the organization's overall IFRS initiative.
- The IFRS conversion effort provides opportunities for achieving synergies with other IT projects and strategic initiatives, such as an ERP implementation.

To facilitate these changes, information systems may need to be implemented, modified, remapped, or reconfigured. Timing and resource constraints may create a need to implement tactical, short-term strategies while transitioning to a long-term approach that integrates with the overall business and information systems strategies. These strategic and tactical decisions should be made early in the project life cycle to prevent duplication of effort, changes in approach, cost extensions, and overruns at a later stage.

Other Considerations

The degree of complexity of any conversion will be compounded by the need for alignment with other regulatory initiatives, such as *Sarbanes-Oxley* (SOX) and its Canadian equivalent (NI 52-109)¹, and Basel II. The increasing number of international regulations facing organizations will likely create interdependencies—between initiatives, resources, processes, and change activities—that organizations will need to manage carefully.

A strategic focus on the information systems underlying these initiatives, including proper planning and consideration of interdependencies, should result in a more efficient process and enhance the benefits derived from conversion. Indeed, to achieve success in an IFRS conversion initiative, leaders should view it in the context of the entire business, the information systems portfolio, and the organization's IT governance program.

What's more, to the extent that the organization is undergoing transformational projects—such as large ERP (enterprise resource planning) conversions, process change, migration to shared-service centres, or other regulatory implementations—it should

plan and execute the IFRS conversion initiative in alignment with those transformation projects. By taking this approach, the organization can help ensure that all initiatives share potential efficiencies, avoid duplication of effort, and benefit from efforts to identify business requirements and standardize systems and processes.

A Call to Action

In a regulatory environment increasingly focused on strengthening financial reporting controls, organizations need to effectively manage their IFRS conversions so that the result is sustainable, accurate, and controlled. Such a comprehensive effort calls for

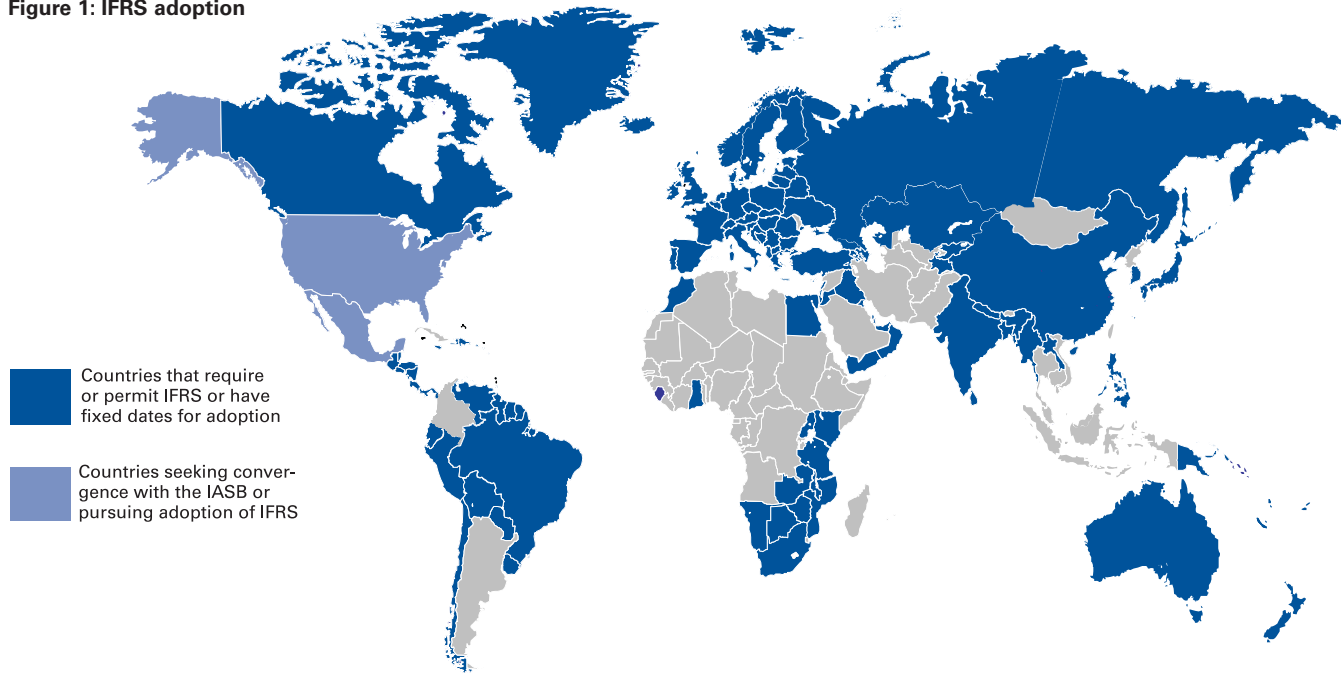
- Scoping all components of the project appropriately, and not just focusing on the technical accounting issues
- Designing business data flows, processes, and systems that are robust and sustainable, rather than short-term solutions that might be cumbersome or more expensive in the long run
- Rolling out effective project strategies to deliver the desired outcomes
- Managing the change in a manner that comprehensively addresses accounting and reporting, data, technology, processes, controls and compliance, tax, and organizational change management and user readiness.

To succeed, the IFRS conversion should reflect its broad influence on the organization—although accounting-driven, it is fundamentally a business initiative. What's more, it is not new; Europe and Australia, for example, have been addressing IFRS conversion issues for a number of years. Canadian companies should seek to learn from their successes and challenges, and benefit from their experiences.

¹ CSA National Instrument 52-109

Background

Figure 1: IFRS adoption



Source: KPMG International, 2008

Most countries with significant economic activity have already adopted IFRS, or have plans to adopt it for domestic listed companies, and are considering using IFRS for statutory reporting.

IFRS Explained

International Financial Reporting Standards (IFRS) comprise “a single set of high-quality, global accounting standards that require transparent and comparable information in general-purpose financial statements.”²

Drivers for Converting to IFRS

Widespread adoption of IFRS will help world markets achieve

- Consistent global financial reporting (this capability would enable organizations’ financial statements to be understood in the global marketplace, facilitate access to global capital markets, and encourage the development of new business)
- Comparable reporting of financial information between organizations operating in multiple countries
- Facilitation of group decision making for multinational organizations through common and consistent accounting standards.

Impacts on Organizations Converting to IFRS

The conversion to IFRS may represent a fundamental change to the financial reporting framework of many organizations. In addition to accounting and reporting changes, organizations can expect far-reaching implications for business processes, personnel, and information systems. For large, multinational organizations with complex group structures, the process to convert to IFRS will consist of a program of multiple projects, each with its own country and organization-specific requirements, as illustrated in Figure 1.

Impacts on Financial Information Systems

The differences that arise in the accounting treatment between current accounting standards and IFRS will create a need for new data, changed calculations, and changes in reporting. Information systems will need to be implemented, modified, remapped, or reconfigured to facilitate these changes. Management will need to make a number of strategic and tactical decisions relating to information systems early in the conversion project to limit unnecessary costs and risks—for example, those arising from duplication of effort or changes in approach at a later stage—as well as to enhance potential benefits.

² International Accounting Standards Board (IASB), iasb.org/news/iasb.asp

Assess IFRS Impact and Develop a Conversion Work Plan

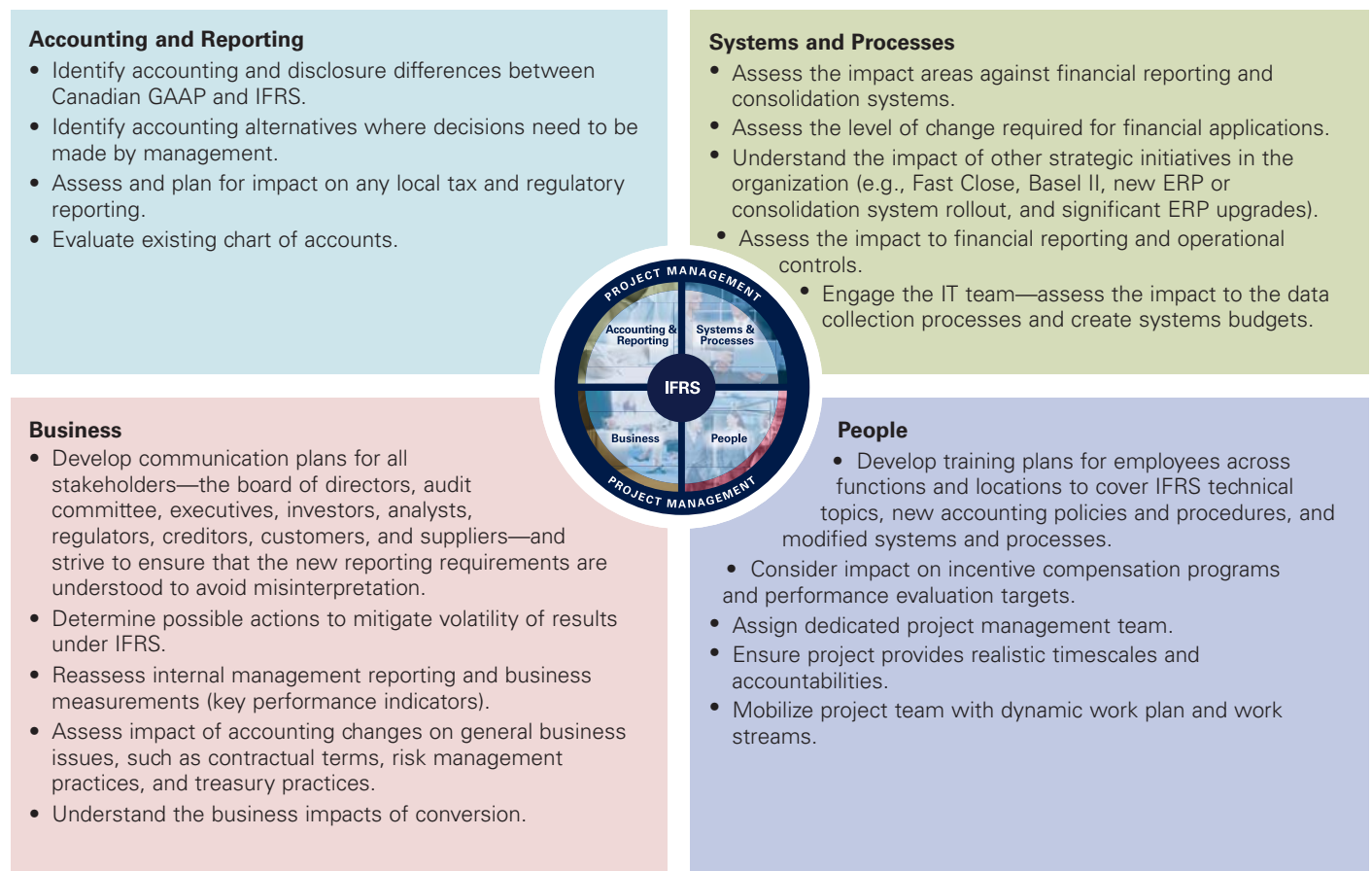
The degree of change resulting from the conversion to IFRS will vary significantly between organizations. Every organization must carefully consider how changing its accounting basis to IFRS will affect its own specific information systems.

The effort required to convert to IFRS will vary within countries and by industry, and it will drive changes throughout organizations. Information systems could be significantly affected by these changes, which will typically result from variations in the accounting policies and differences in accounting disclosure requirements.

Assessment Phase

Figure 2 provides a framework for the assessment phase of an IFRS initiative. Adopting this approach can help organizations assess the effect that conversion to IFRS may have on their accounting and reporting, data, technology, processes, controls and compliance, tax, people and change, and supporting information systems. The framework for the assessment process will assist in determining the scale of the IFRS conversion, as well as the scope of the change management effort.

Figure 2: The assessment framework



Source: KPMG LLP (Canada), 2008

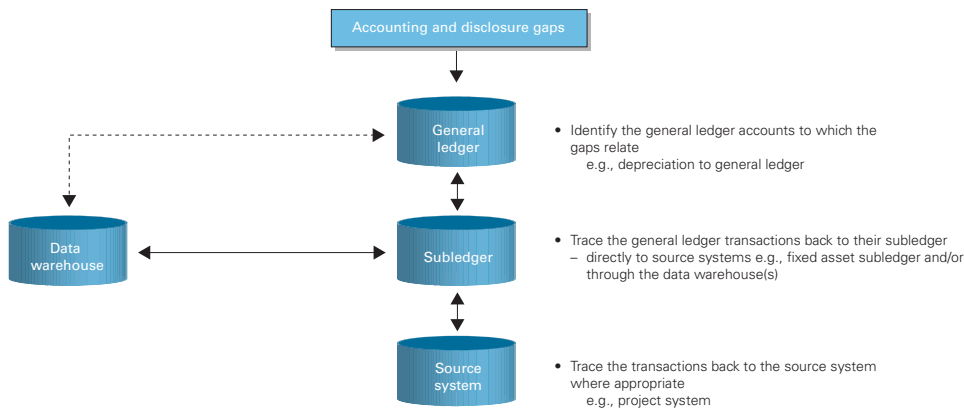
Translating the Numbers

An organization should have a detailed understanding of the differences in accounting policies and procedures under IFRS as compared to local GAAP policies, and the potential impact and risk to information systems and controls, before it can determine the information systems changes required. This effort is time consuming, and it should take place during the assessment phase of the conversion—it is the foundation for determining the potential IT ramifications and for translating the accounting differences to technical system specifications.

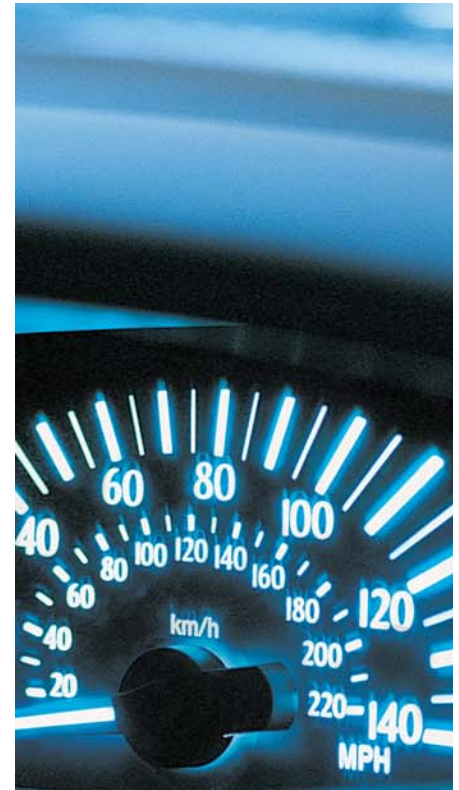
One of the difficulties organizations often face in creating technical specifications is a lack of understanding of the detailed end-to-end flow of data from the source systems (including models or spreadsheets) to the general ledger.

Figure 3 outlines the process that organizations may adopt to identify the information systems impacts. For illustrative purposes, the organization’s complexity has been simplified.

Figure 3: Process of identifying the information systems impacts of IFRS



Source: KPMG LLP (Canada), 2008



“An organization may use the move to IFRS as an opportunity to assess where financial and reporting processes and systems need to be rebuilt, tweaked or completely replaced.”

*“Making the Move,”
Accounting Week*

Effects on Information Systems

IFRS conversion affects information systems in many ways, from the initiation of transactions through to the generation of financial reports, even if merely through the creation of new accounts in the general ledger. The following table details some of the categories of changes that may be required:

Type of Change	Details	Information Systems Impacts
New data requirements	New accounting disclosure and recognition requirements may result in <ul style="list-style-type: none"> • More detailed presentation of information • New data elements or fields to be recorded • Information to be calculated on a different basis. 	Changes to allow for the capture of new or changed data.
Changes to the chart of accounts	There will almost always be a change to the chart of accounts due to reclassifications and additional reporting criteria.	Creation of new accounts and deactivation of accounts that are no longer required.
Reconfiguration of existing systems	Existing systems may already have capabilities built in to deal with the specific IFRS requirements, particularly the larger enterprise resource planning (ERP) systems and high-end general ledger packages.	Reconfiguration of existing software to enable accounting under IFRS.
Modifications to existing systems	New reports and calculations required to accommodate IFRS. Spreadsheets and models used by management as an integral part of the financial reporting process should be included when considering the required systems modifications.	Amendments such as <ul style="list-style-type: none"> • New or changed calculations • New or changed reports • New models.
Selection and implementation of new systems	Where previous financial reporting standards did not require the use of a system, or the existing system is inadequate for IFRS reporting, it may be necessary to implement new software.	Implementation of software in the form of a new software development project, or the selection and implementation of a package solution.
Interface and mapping changes	With the introduction of new source systems and the decommissioning of old systems, interfaces may need to be changed or developed and there may be changes to existing mapping tables to the financial system. Where separate reporting tools are used to generate the financial statements, the mapping to these tools will require updating to reflect changes made to the chart of accounts.	Interfaces may be impacted by <ul style="list-style-type: none"> • Modifications made to existing systems • The need to collect new data • The timing and frequency of data transfer requirements.
Consolidation of entities	Under IFRS, there will potentially be changes to the number and type of entities that need to be included in the group consolidated financial statements. For example, the definition of "control" may be different under IFRS.	Consolidation systems and models will need to be updated to account for changes in consolidated entities.
Financial Reporting tools	Reporting tools may need to be modified to <ul style="list-style-type: none"> • Gather additional disclosure information from branches or subsidiaries operating on a standard general ledger package • Collect information from subsidiaries that use different financial accounting packages. 	Reporting tools used by subsidiaries and branches to provide financial information will need to be modified.

Each individual International Accounting Standard (IAS) and IFRS will require different information system changes. The table on the next page indicates some of the requirements under IFRS, the impact on the financial statements, and the possible information systems impacts arising from these changes.

IFRS Accounting Treatment	Impact on Financial Statements	Possible Information Systems Effects ³	
Consolidation	<p>IFRS requires uniform accounting policies between the parent, subsidiaries, joint ventures, and associates. Accounting policy choices can affect many areas, such as property, plant, and equipment (PP&E); investment property; and employee benefits.</p>	<p>Impact anticipated for various lines in the balance sheet and income statement to harmonize depreciation methods, cost vs. revaluation method for PP&E, fair-value methods for investment property, and the recognition of actuarial gains and losses.</p>	<p>Modification of the existing system, or selection and implementation of a new general ledger and consolidation system to accommodate the following:</p> <ul style="list-style-type: none"> • Harmonized chart of accounts between the parent and all subsidiaries, joint ventures, and associates.
Property, plant, and equipment (PP&E)	<p>Separate accounting for components of PP&E is more rigorously applied and broader under IFRS, and can include physical components, such as major spare parts, or non-physical components, such as a major inspection or overhaul.</p>	<p>Increased volume of depreciation transactions.</p>	<p>Modification of the existing system, or selection and implementation of a new fixed asset sub-ledger system to accommodate the following:</p> <ul style="list-style-type: none"> • Functionality to track different components of fixed assets • More complex depreciation calculation to handle different estimated useful lives for each individual component • Additional processing to summarize and post the cost and accumulated depreciation for different components to the general ledger accounts.
PP&E and investment property	<p>Under IFRS, a company can choose between the amortized cost and revaluation/fair-value methods to measure PP&E and investment property.</p>	<p>Increased volatility in equity and earnings under the revaluation/fair-value method for PP&E and investment property, respectively.</p>	<p>Modification of the existing system, or selection and implementation of a new fixed asset sub-ledger system to accommodate the following:</p> <ul style="list-style-type: none"> • Functionality to track the history of revaluation increases or decreases, which affects the posting/interface to the general ledger • Extensive data storage requirements to track the history of revaluation increases or decreases by individual asset.
Impairments	<p>Under IFRS, reversal of impairment charges, (other than goodwill) is required if the circumstances leading to the impairment have changed. Certain ceilings are placed on the amount of the reversal, thereby creating the need for tracking multiple asset values in the event of a writedown.</p>	<p>Increased volatility in earnings due to more frequent impairment charges, and reversal of impairment charges expected under IFRS since</p> <ul style="list-style-type: none"> • Impairments are tested on an asset or cash generating unit basis, which is typically at a lower level than a reporting unit under Canadian GAAP • The cash flow test for recoverability is based on discounted cash flows rather than undiscounted cash flows under Canadian GAAP. 	<p>Modification of the existing system, or selection and implementation of new sub-ledgers or other systems to accommodate</p> <ul style="list-style-type: none"> • Functionality to track the history of impairment charges for each individual asset to cater for potential reversals, if impairment is tested individually.
Financial instruments	<p>IFRS requires foreign exchange gains and losses on available-for-sale debt securities to be recognized in profit or loss.</p>	<p>Increased volatility in earnings as a result.</p>	<p>Modification of the existing system, or selection and implementation of a new sub-ledger system to accommodate the following:</p> <ul style="list-style-type: none"> • Functionality to handle multi-currency • Functionality to track both the book cost and fair value of individual securities in original and translated currencies • Functionality to track adjustments to fair value in two accounts (income statement for foreign exchange and equity for other changes).

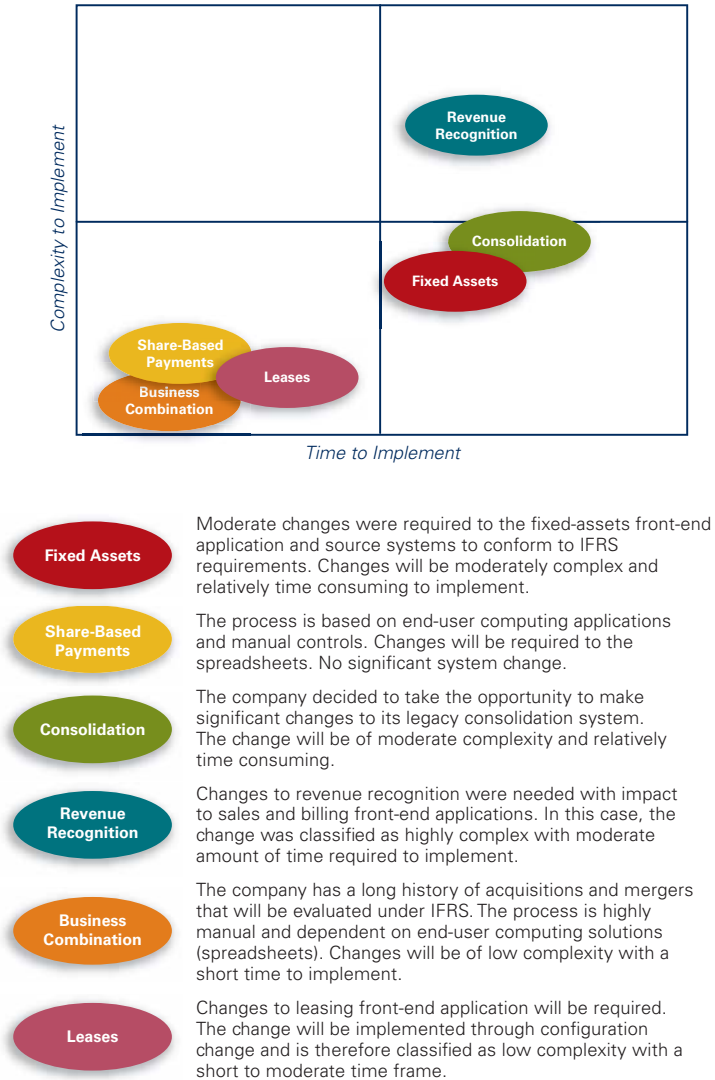
³ The information systems' effects are examples only and will vary according to each organization's specific circumstances.



“The differences that arise in the accounting treatment between local GAAP and IFRS will generate the need for new data, altered or modified calculations, and changes in reporting. Information systems will need to be implemented, modified, remapped, or reconfigured to facilitate these changes.”

Figure 4 provides examples of accounting areas in which IFRS can affect IT systems. (This chart illustrates one company-specific situation and is not intended to be a general representation of the IT impact of IFRS for all companies.)

Figure 4: An Example of the time and complexity of IT Changes



Source: KPMG LLP (US), 2008

A conversion process is complex and can be expensive, so some companies will choose a low-cost, expedient spreadsheet option in the short term, with the understanding that they will need to ultimately invest in a long-term source conversion. Those that choose the short-term option should remember that it is less expensive only in the short term and may actually be more expensive in the long term. Over time, managing the risks of converting to and reporting under IFRS will be critical, and doing so will require an investment of time and resources.

Design the Conversion Changes

A long-term approach integrated with the overall business objectives requires leaders to make strategic and tactical decisions early in the conversion project life cycle. Doing so may limit unnecessary costs resulting from duplication of effort or changes in the approach at a later stage.

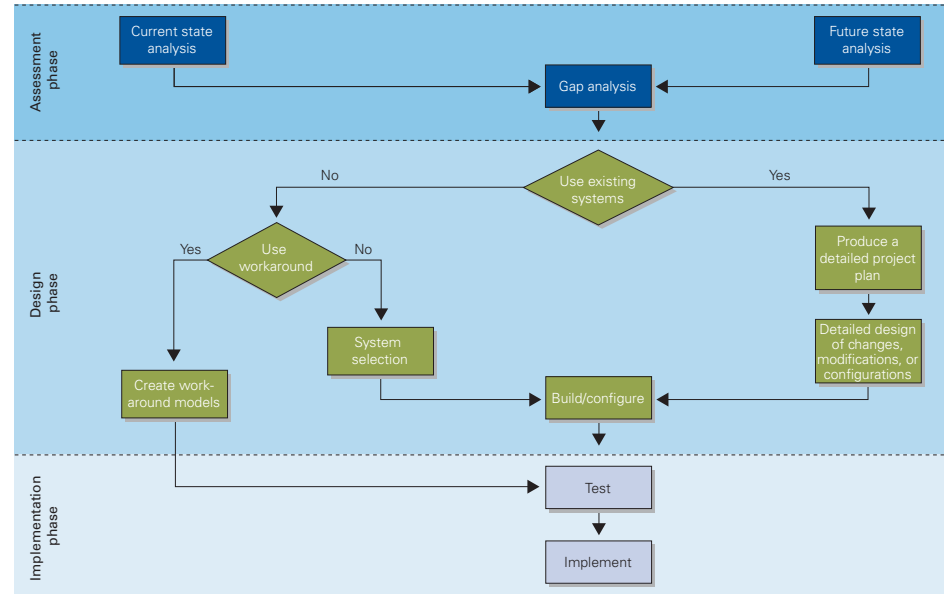
Organizations have differing structures, systems, and industry-specific circumstances, preventing a “one-size fits all” approach to the conversion to IFRS. The assessment phase will reveal whether it is possible to reconfigure or modify the current systems to enable compliance with IFRS. Where this reconfiguration is not possible, organizations may need to purchase new systems; where financial or time constraints exist, they may need to develop workarounds, such as spreadsheets, to produce the required information.

The decisions around the development of the solution should be made during the design phase of an IFRS conversion initiative. Figure 5 demonstrates the decision process typically followed during this phase.

To develop a robust short- and long-term approach to conversion, organizations should consider the following:

- Whether to make changes at the group, company, or source system levels
- How to cope with multiple reporting requirements
- How to decide when to cut over from the local GAAP general ledger to the IFRS general ledger
- What data is available to comply with new accounting policies
- Whether to buy a new system or make modifications to existing systems

Figure 5: Process flow for the assessment, design, and implementation of IFRS



- How IFRS affects internal control over financial reporting
- The most appropriate methods to harmonize internal and external reporting
- How to manage the risks of model-driven remedies used as short-term solutions
- The effects of conversion on the internal and external audit functions
- If there are additional competing regulatory requirements.

Management should address these questions early in the conversion life cycle. Their decisions will guide how they address the ramifications to information systems, and how they limit unnecessary costs resulting from duplication of effort or changes in approach at a later stage.

The financial impact of the information systems changes is likely to be significant and may be a major consideration for management when determining the approach to information systems changes. Costs can vary according to

- Organization size
- Industry
- Level of IFRS adoption within each country
- Existing information systems preparedness for IFRS.

Costs are likely to arise from

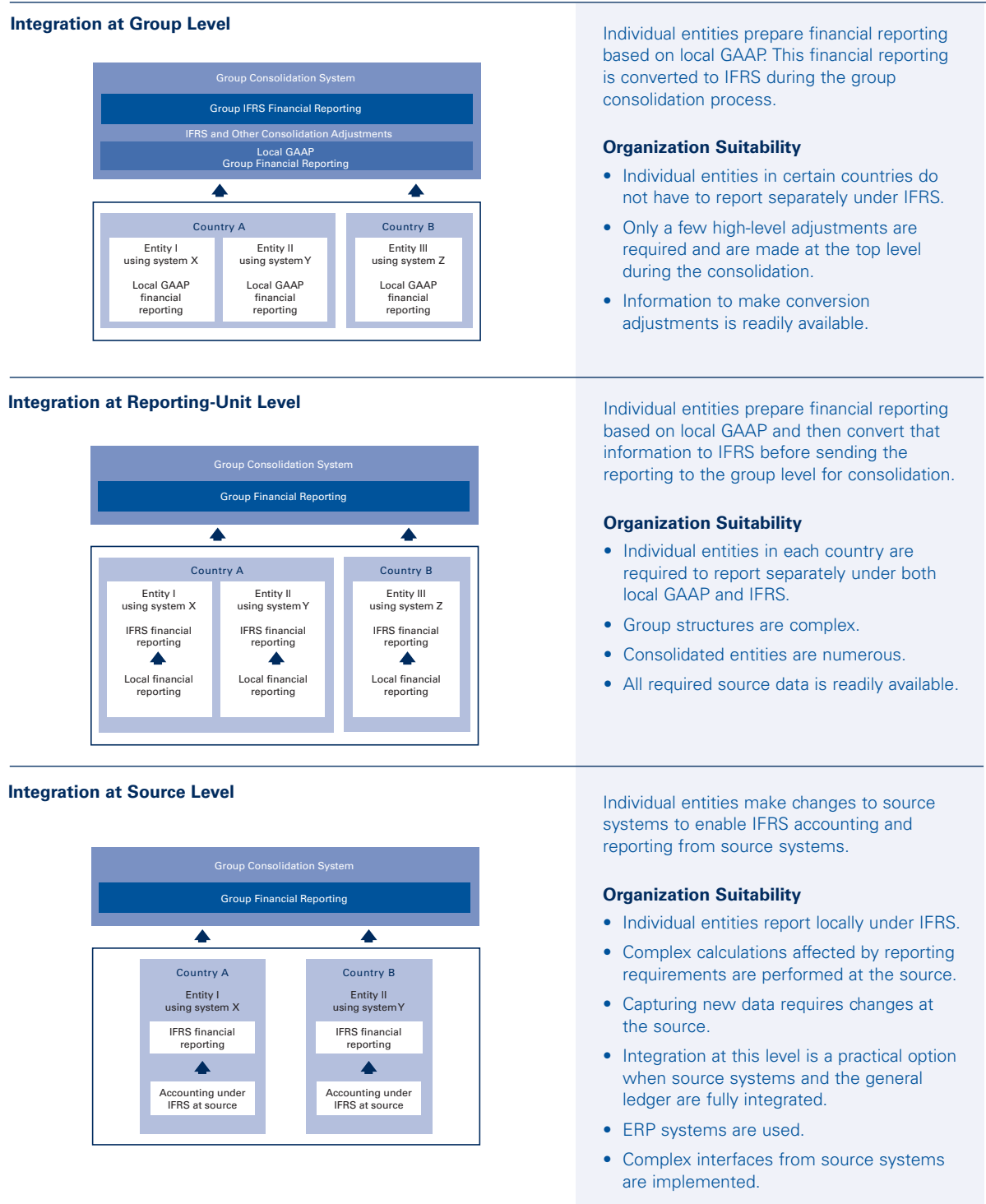
- The modification or reconfiguration of new systems
- Vendor maintenance and ongoing support
- Employment of additional resources
- Project management
- Training needs
- Implementing both a short-term solution to meet tight deadlines, and a more robust long-term solution at a later stage to address the same problem.

The strategic and tactical IFRS conversion decisions should be conducted within the organization’s information systems governance framework, to closely align any significant IT changes with the organization’s strategic business goals.

Identifying the Appropriate Level for Systems Changes

Changes to information systems may be made at different levels in an organization’s financial reporting process; for example, at the group level, at the company level, and at the source level. To determine the appropriate level, management must consider various factors, including those outlined in Figure 6 on the next page.

Figure 6: Levels of system changes



Source: KPMG LLP (Canada), 2008



Achieving Synergies in Transformational Initiatives

To the extent that the organization is engaged in transformational projects, such as large ERP implementations and conversions, process change, migration to shared-service centres, or other implementations, it should plan and execute the IFRS conversion initiative in alignment with those projects. Because an IFRS conversion affects the organization's financial reporting and the underlying systems and processes that ultimately produce that reporting, it will likely have significant interdependencies with other transformational projects.

The table below provides examples of transformation projects and potential IFRS considerations. In each case, management was able to gain efficiencies in both time and effort by coordinating their transformation projects with the IFRS initiatives. Key IFRS efforts including identification of data flows, processes, and systems were made easier by work already done for the transformation initiative. The shift to IFRS can also be a catalyst for undertaking a project such as the migration to a shared-services centre. Indeed, organizations that perceive the IFRS conversion effort as an opportunity for business improvement can leverage the effort in a variety of important ways.

Example Transformation Project

Regional shared services

IFRS Synergies Achieved

A global consumer markets company had subsidiaries worldwide with disparate systems and processes. Although management knew a shared-services business model could help it achieve cost and efficiency benefits, it was initially reticent to begin such a comprehensive effort.

As part of the IFRS conversion project, the company standardized its accounting policies for fixed assets, and consolidations (among others), and modified or replaced its procurement, supply chain, fixed asset, and general ledger applications at many locations. It also modified its business process procedures and controls.

Management realized that the newly standardized business model and the extensive understanding of detailed business processes and systems would greatly aid in the migration to a regional shared-service centre. When it undertook this project, leveraging the IFRS conversion activities enabled it to save considerable time and money.

Global ERP implementation

A large financial institution was undergoing a global SAP implementation when it embarked on an IFRS conversion initiative. Once the company determined its future accounting policies under IFRS, the process of conversion was assisted by the SAP implementation in process. For example, the company had developed a detailed understanding of its business processes and practices as a part of the requirements planning (blueprinting) phase of the implementation project, including the detailed data sources and structures. These activities greatly aided the IFRS IT impact analysis.

The company had to repeat certain aspects of its global template blueprinting phase to accommodate the changes due to IFRS. Additionally, the use of a parallel accounting strategy (recommended by SAP) for IFRS conversion added additional complexities. Nevertheless, the close coordination of the IFRS and SAP implementation activities yielded the most efficient process for each initiative.

Build, Implement, and Roll Out

The build, implement, and roll-out phase of an IFRS conversion project usually requires the involvement of resources from all areas of the business, including finance, the front office, executive management, tax, and information technology. The involvement of IT in this phase is critical to the overall project success, and it can account for a substantial part of the project cost. Changes to information systems will include changes to data, applications, technology, controls, and related business processes. This phase will require a strong focus on change management activities and should be guided by a program management office (PMO). The PMO should take a formal program management approach to managing the conversion, potential effects on other ongoing transformational projects, and the necessary changes representing all aspects of the business.

During the implementation of an IFRS conversion, the IT organization should confirm its understanding of the new data requirements and configure or build application systems to meet those

requirements. An effective system development life cycle (SDLC) is an essential enabler for successfully configuring or building application systems in accordance with the requirements. The IT department can expect to be involved in all phases of the implementation of the IFRS conversion, including configuring or building application systems, thoroughly testing changes, and managing the cutover process. As new processes and changes to application systems are built, leadership should consider how these new processes and controls affect the existing control environment. New controls will likely be needed to maintain integrity in transaction processing.

Prior to rollout, the PMO should design and execute strategies and plans to effectively communicate with and train users on the modifications to business processes and application systems. All users should be appropriately trained on the new accounting policies, as well as the effects those policies have on the supporting IT infrastructure. The company

should also evaluate whether any of the modifications result in the need for additional skill sets or knowledge.

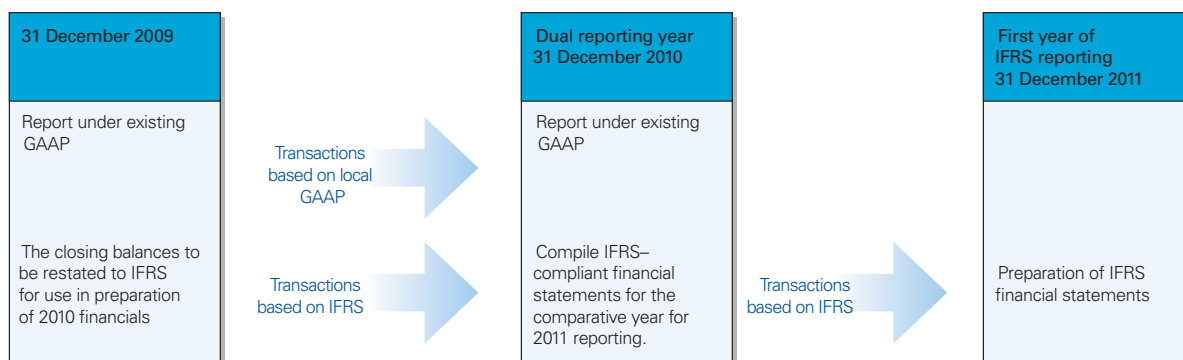
Dealing with the Dual and Ongoing Multi-GAAP Reporting Requirements

First Year of IFRS Reporting

IFRS requires financial statements to be presented with comparative-year figures. There is no exception for the first year of reporting under IFRS. The comparative year would have been reported under Canadian GAAP in the previous year. This is commonly referred to as the dual reporting requirement.

Figure 7 illustrates the stages in the dual reporting process for an organization that is required to produce its first IFRS financial statements as at December 31, 2011.

Figure 7: Dual reporting for the first IFRS financial statement



Source: KPMG LLP (Canada), 2008

To cater to the dual reporting requirements, a number of options are available. These depend on each organization's specific circumstances and the capabilities of its current information systems, as outlined in the table below.

Dual Reporting Options	Considerations ⁴
Some systems and reporting packages have the functionality to produce multiple financial statements based on different reporting standards, enabling parallel accounting.	Systems with this functionality may still require significant configuration and testing prior to the start of the comparative year for the IFRS reporting module.
Parallel accounting can also be achieved by setting up duplicate "companies" in the system to be used for IFRS reporting.	<p>Most appropriate for systems that have the ability to post transactions to both companies, or if there are limited transactions.</p> <p>This approach leads to doubling the number of companies in the system, which may create system capacity issues and increase reconciliation efforts.</p>
<p>Adjustments could be made to the comparative year to restate it from existing GAAP to IFRS by one of the following methods:</p> <ul style="list-style-type: none"> • Specific IFRS adjustment codes are set up in the chart of accounts. IFRS adjustments are then posted to the IFRS adjustment accounts to produce IFRS-compliant financial statements. • Posting IFRS adjustments to a separate period in the system (e.g., period 14). 	<p>Considerations for these methods are as follows:</p> <ul style="list-style-type: none"> • More appropriate for groups with a large number of consolidating entities; the system should have the ability to select accounts for consolidation • More appropriate where the system cannot select individual accounts for consolidation.

Cutover from Existing GAAP to IFRS Reporting

Source systems are usually mapped to the general ledger, which has been set up to produce financial statements under local standards. To enable reporting under IFRS, an additional ledger (IFRS general ledger) may be required, either in parallel or through adjustments.

At some stage, a cutover will be required from the local general ledger to the IFRS general ledger, so that IFRS becomes the primary basis of accounting. This effort will require the organization to map the changes so that they link the source systems to the IFRS general ledger, without the need for IFRS adjustments.

Cutovers may be handled in various ways, however, system cutovers generally happen in stages. Throughout the process, careful planning and execution will be required because the timing will affect the nature and volume of adjustments, as demonstrated in the table on the next page.

The alternative cutover options provide organizations with the flexibility to undertake a phased approach to IFRS adoption. Such an approach allows cutover of the accounts affected by IFRS to be aligned with the organization's business approach.

⁴ The information systems effects are examples only and will vary according to each organization's specific circumstances

Timing of Cutover	Example Effects
First day of the year in which IFRS reporting commences (e.g., January 1, 2011)	No adjustments will be required for current-period financial information. IFRS changes will flow through subsystems to the general ledger.
Cutover made over time, after the first day of the year in which IFRS reporting commences (e.g., after January 1, 2011)	As source systems are modified, IFRS adjustments will be replaced by automatic feeds directly from the source systems.
Cutover prior to first day of the year in which IFRS reporting commences (e.g., prior to January 1, 2011)	<p>This action results in the need for a variety of adjustments:</p> <ul style="list-style-type: none"> • Where cutover changes for IFRS have been made, adjustments for conversion back to local standards are necessary for dual reporting requirements. • Where cutover changes to IFRS are still required, adjustments for conversion to IFRS are necessary to allow full IFRS reporting in the following year and to restate comparative figures in the year of transition.



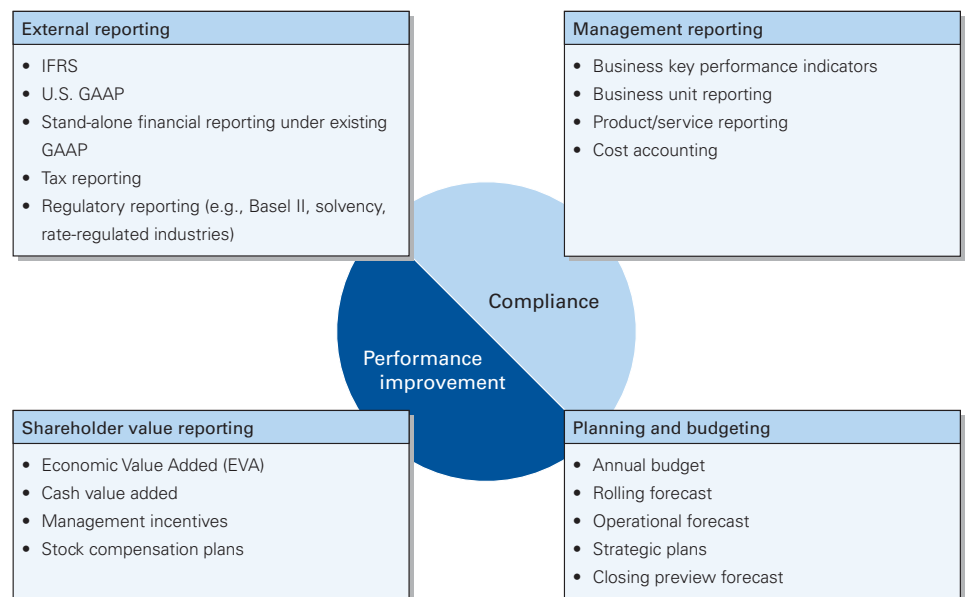
Harmonization of Internal and External Reporting

Figure 8 shows the possible internal reporting areas that may be impacted by changing systems to accommodate the new IFRS reporting requirements.

The process of aligning internal and external reporting will involve the following:

- Where mappings have changed from the source systems to the general ledger, mappings to the management reporting systems and the data warehouses should also be changed.
- Where data has been extracted from the source systems and manipulated by models to create IFRS adjustments that are processed manually through the general ledger, the impact of these adjustments on internal reporting should be carefully considered.
- Alterations to calculations and the addition of new data in source systems, as well as new timing of data feeds, could have an impact on key ratios and percentages in internal reports, which may need to be redeveloped to accommodate them.

Figure 8: Harmonizing internal and external reporting



Other Considerations

Ongoing Multipurpose Reporting

Some countries may require statutory reporting in addition to IFRS on an ongoing basis. For example, the local tax authorities may require tax returns to be prepared using a local standard rather than IFRS. Some companies may also be required to report financial information under a set of rules in addition to IFRS, existing GAAP, and tax reporting (e.g., reporting in a regulated environment).

Organizations that are required to perform multipurpose reporting on a regular basis will need to develop permanent, robust, and well-controlled solutions. One approach is to assign the adjustments required to produce additional reporting to specific accounts in the chart of accounts. These accounts are then selected as appropriate to produce reporting under a particular standard or for the purposes of management.

In a complex systems environment with multipurpose reporting requirements, the chart of accounts redesign involves more than just adding new accounts or regrouping accounts. This can be a complex, time-consuming, and technical exercise.

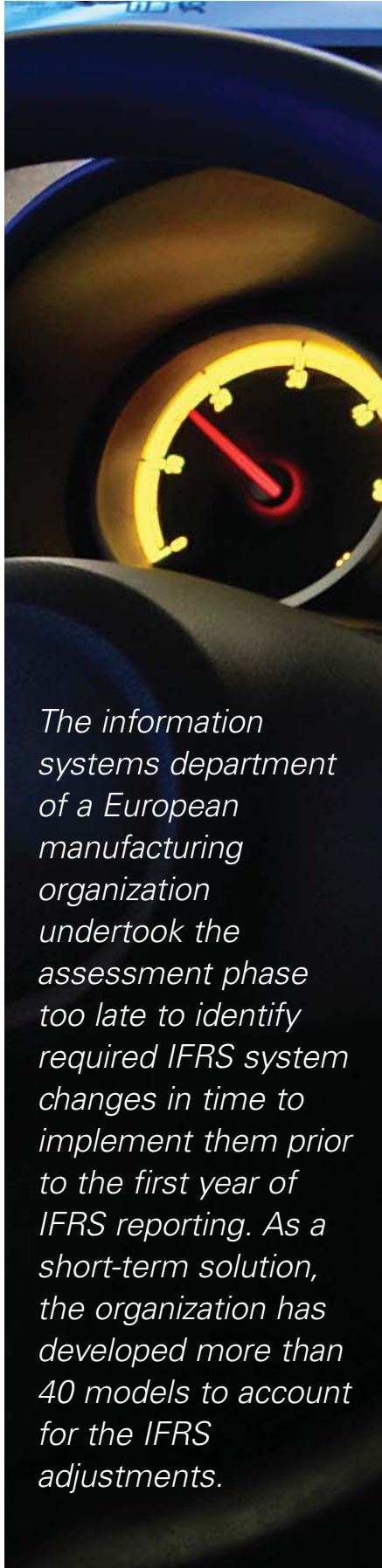
Consolidation systems are structured on the basis of the chart of accounts, which must therefore be revised before the redesign of consolidated systems.

Spreadsheets or models that are used as short-term remedies to provide the necessary adjustments to convert local GAAP to IFRS are generally not subject to the same stringent controls normally built into integrated financial packages. This can significantly increase the risk of errors. Strict controls will need to be implemented to manage, monitor, and reconcile the flow of data between models and other systems.

Tax Considerations

Making a transition from Canadian GAAP will affect tax reporting, tax accounting, and the underlying data processes associated with an organization's tax function. The involvement of tax professionals is important to the IFRS conversion process because, for Canadian companies, tax processes and controls have been designed to deliver information to meet the financial statement reporting requirements of Canadian GAAP. IFRS conversion will require companies to review and possibly modify these processes and controls for collecting tax-sensitive information, computing temporary differences, tracking deferred taxes, and preparing the tax note under IFRS. Companies may also need to consider the ability to handle multiple or changing reporting requirements that may arise during the transition.

A large insurance company incorporating 20 entities with independent general ledgers had 180 accounts affected by IFRS. The organization was unable to convert all accounts prior to the first year of conversion, and it therefore adopted a phased approach. It developed a detailed reconciliation model to track the 3,600 IFRS adjustments that were posted on a monthly basis. As subsequent changes were made to the information systems, the number of adjustments required decrease.



The information systems department of a European manufacturing organization undertook the assessment phase too late to identify required IFRS system changes in time to implement them prior to the first year of IFRS reporting. As a short-term solution, the organization has developed more than 40 models to account for the IFRS adjustments.

Managing the Risks of Short-Term Solutions Based on Spreadsheets

With long lead times required for modifications to legacy systems, limited skilled resources to make the changes, and strict IFRS deadlines, organizations are increasingly considering end-user-developed spreadsheets and model solutions. These models can potentially be used as a short-term remedy to provide the necessary adjustments to convert local financial statements to IFRS.

In most cases, these models are gradually replaced by modifications to core systems. However, they may still be used for certain specialized reporting requirements and, therefore can be managed using some of the methods outlined in the table below.

Risks	Managing the Risks ⁵
Models and spreadsheets are generally not subject to the input, processing, output, and program change management controls traditionally built into typical integrated financial packages, which significantly increases the risk of errors.	<ul style="list-style-type: none"> • Design appropriate built-in controls, version control, security, and change management procedures. • Perform independent model reviews to identify errors before models are used. • Undertake user acceptance testing as part of the development process.
The introduction of numerous intermediary models between subsystems and the general ledger increases the risk of information not passing or passing inaccurately to the general ledger.	<ul style="list-style-type: none"> • Implement strict controls to monitor and reconcile the flow of data between models and other systems.
Input to models and spreadsheets may be obtained from existing data warehouses, where data may not be as reliable as data contained in core systems.	<ul style="list-style-type: none"> • Consider reliability of data in warehouses. • Perform regular reconciliations to source data. • Determine if appropriate security over data warehouses is in place.
Moving substantial financial processes from the generally tightly controlled information systems arena into less controlled user domain may result in increased security, segregation of duties, data integrity, and operational issues. The overall control environment may be weakened through the excessive use of spreadsheets.	<ul style="list-style-type: none"> • Increase management awareness of the risks that models pose to the overall control environment. • Develop long-term plans for replacement of models with core systems.
The introduction of numerous models between subsystems and the general ledger creates additional work steps, and increases the risk of delays to the period-end financial statement closing and reporting process.	<ul style="list-style-type: none"> • Increase management and staff awareness of the risks of delay in the financial statements closing process. • Critically review and minimize dependencies between period-end financial statement closing tasks.

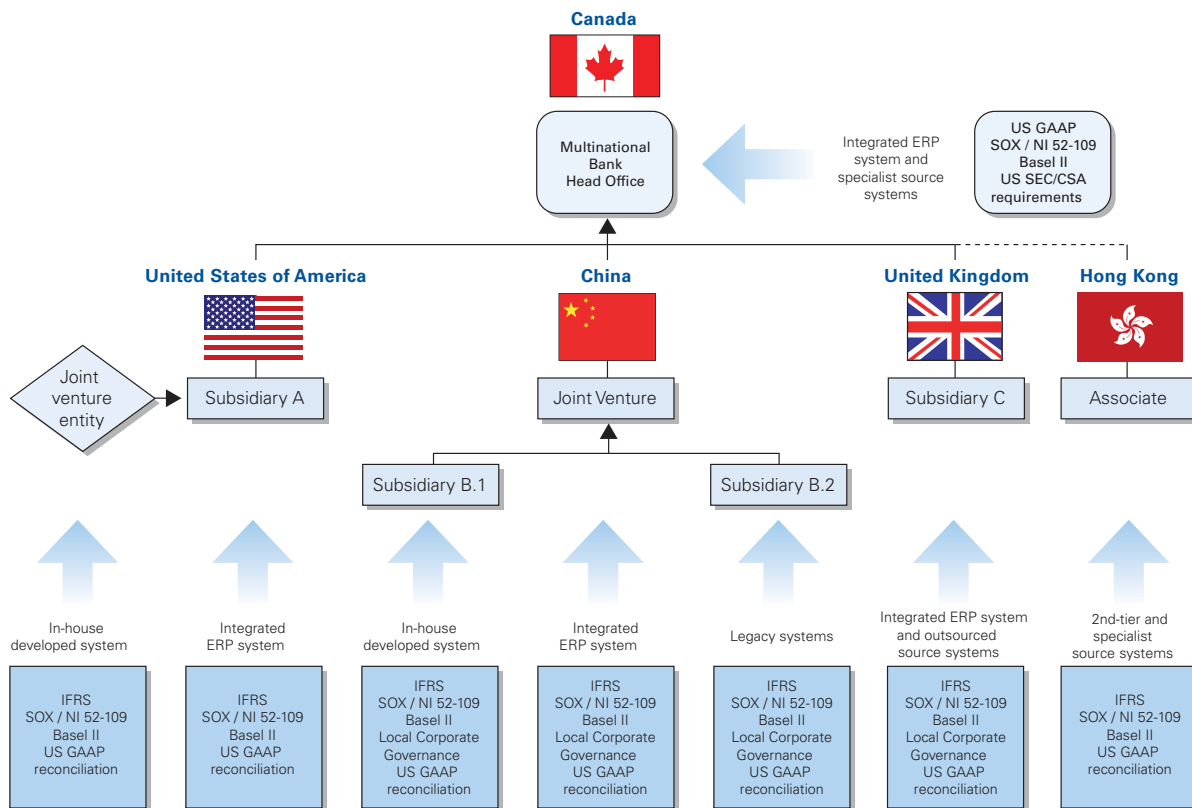
⁵ These methods of managing risks are examples only. Detailed analysis based on the specific circumstances of the organization would be required to determine the appropriate risk management methods. These methods may not be completely effective in all circumstances and some residual risks may remain.

Other Requirements

IFRS conversion projects should not be considered in isolation. Large, complex multinationals should carefully consider the interdependencies between IFRS projects and other regulatory initiatives.

In addition to IFRS, global organizations are facing an increasing number of regulations, including *Sarbanes-Oxley*, country-specific corporate governance legislation, and Basel II. Figure 9 illustrates that the conversion to IFRS represents a significant challenge for large multinationals with complex group structures, differing information systems, and country-specific legislation.

Figure 9: Multinational bank with complex reporting environment



Source: KPMG LLP (Canada), 2008

For multinational organizations (such as the one pictured in Figure 9), the process to convert to IFRS will consist of a program of multiple projects, each with its own country- and organization-specific requirements. The IFRS project should be planned and executed with consideration of, and in conjunction with, the other regulatory initiatives and requirements that apply to the organization. Issues specific to certain of these regulatory initiatives are outlined below.

Internal Control Certification

Section 404 of the *Sarbanes-Oxley Act* of 2002, its Canadian equivalent, and similar standards in other jurisdictions, require management to document and assess internal control over financial reporting, and report on the assessment.

The conversion to IFRS may substantially influence a significant proportion of the internal controls over financial reporting due to

- Excessive use of uncontrolled end-user developed models
- Budgetary constraints
- Lack of available skilled resources
- Time constraints resulting in emphasis on implementation rather than the internal controls.

This impact on internal controls over financial reporting may affect the organization's ability to achieve a "clean" certification. It is therefore important that these projects are closely aligned with control requirements addressed during the IFRS design and implementation phases.

Corporate Governance Legislation

Many countries may be impacted by local corporate governance legislation, such as Canada's CSA National Instrument 52-109. This legislation requires management to develop a sound system of internal controls to support the financial reporting process and certify its operating effectiveness.

The approach taken for IFRS conversion may affect a significant proportion of the internal controls over financial reporting, a situation that in turn may impact the organization's ability to comply with local corporate governance legislation. IFRS and corporate governance requirements should therefore be closely aligned.

Basel II

Basel II is an evolving regulation addressing the capital adequacy of internationally active banks. IFRS and Basel II have different objectives, but they also have a number of similarities. Data requirements are likely to overlap substantially, so, as part of the IFRS initiative, leaders should carefully consider Basel II data and reporting requirements to help enable the organization's systems to cope with the demands of these two standards.

Industry-based Regulations

Companies must often comply with a variety of industry-based regulations that have extensive data requirements. Management should take steps to avoid overlapping or redundant compliance efforts and duplicative internal reporting efforts.

The Effect of IFRS on Internal and External Audit

With the move to IFRS, many accounting processes and information systems responsible for financial reporting and the preparation of financial statements will change, in turn affecting the organization's governance structure and internal control over financial reporting. Management will need to assess and report on the reliability of these new processes, information

systems, and related controls, and provide adequate documentation and data for both internal and external auditors.

Integrating the internal and external auditors into the change management process of the IFRS conversion may help manage their expectations and facilitate the post-conversion audits. An effective governance model should provide for ongoing communication with auditors.

Typical risks and example controls are outlined in the table below.

Risks to the Audit Process	Controls ⁶
Inadequate documentation of changed processes can be problematic.	<ul style="list-style-type: none"> Produce updated internal control documentation as part of the development of the new processes, using a standard format and approach.
Manipulation of data in models or spreadsheets may eliminate the audit trail from the general ledger to the source system.	<ul style="list-style-type: none"> Develop models so that calculations may be reperformed Produce comprehensive documentation of the models Implement a strict change management process over the development of models Build in functionality to allow traceability of transactions Undertake user acceptance testing as part of the development process.
Key controls to provide integrity and accuracy of financial reporting information may not be implemented, or may be bypassed.	<ul style="list-style-type: none"> Design and implement appropriate information systems general controls Implement strong application input, processing, and output controls.
Complexity of the management of numerous transition adjustments may result in transactions not being posted to the general ledger.	<ul style="list-style-type: none"> Design and implement controls over completeness and accuracy when posting adjustment transactions to the general ledger.

⁶ These controls are examples only. Control design would require detailed analysis based on specific information systems characteristics and business needs. Controls cannot be totally effective in all circumstances and some residual risks may remain.


Looking Ahead

Legislated deadlines for IFRS reporting should be seen as only one milestone of the conversion initiative. In most cases, significant effort will still be required after this date to replace the short-term remedies with more robust long-term solutions, to refine internal and external reporting, and to strengthen controls over newly implemented solutions.

Post-Conversion Activities

The magnitude of the required information systems changes, amendments, or alterations will, by necessity, vary significantly between organizations. All required systems changes might not be made prior to the first year of accounting on an IFRS basis. Many organizations make the most essential changes first and then address the others with short-term solutions, such as spreadsheet models. In addition, the International Accounting Standards Board's (IASB's) recently updated work plan indicates continued delays in certain key accounting standards that were initially expected to be finalized before Canada's changeover on January 1, 2011. The plan indicates that a large volume of new standards are to be issued after the changeover to IFRS. Consequently, the systems changes that result might extend past the IFRS conversion date and be implemented over a number of years.

In the planning phase, organizations should assess whether current information systems adequately support the organization's business goals. The need to change, amend, or alter the information



To enable the organization to succeed, the IFRS conversion initiative should reflect the true impact in the entire organization—it is far more than just the numbers.

systems for IFRS may become the driver for modernization or replacement of legacy systems. The information systems function should undertake any such program in conjunction with the broader business to achieve the desired result in line with the overall business strategy.

IT Advisory

KPMG can help organizations strengthen or restore a business-driven focus to technology decisions. IT Advisory professionals offer a range of services designed to assist organizations in the creation of business value through better management of technology investments and related risks. These service offerings are detailed below.

Service Offering	Description
Business Systems Advisory	<p>KPMG's Business Systems Advisory is a suite of services that can assist our clients with existing information technology support, enhance their current systems integrators, and support their IT and Finance project management and leadership team in articulating the role of business systems in the organization. Our systems knowledge covers a broad spectrum of applications, including, but not limited to, ERP, customer relationship management, business intelligence, and corporate performance management. Using effective use of software functionality, Business Systems Advisory combines deep business, finance, and accounting experience with extensive knowledge in application governance, risks and controls, technical configuration and security, system implementation life cycle, regulatory compliance mandates, and GAAP conversion.</p>
IT Project Advisory (ITPA)	<p>IT Project Advisory can assist clients with business initiatives, such as project management organization, process development, risk assessments, and review of architecture for integration requirements, to help increase the likelihood of project success.</p>
IT Sourcing Advisory	<p>IT departments face conflicting demands, such as increasing services, automation, and corporate efficiency, while at the same time stabilizing or even reducing IT costs. One option is to review your IT sourcing arrangements. KPMG can provide support throughout the full sourcing life cycle, from option assessment, readiness planning, and service transition, through management and remediation, to service evolution.</p>
IT Strategy	<p>IT Strategy focuses on the effective management of IT performance, value, and risk, by establishing a vision for the functioning of an IT department. A key objective is to align IT with the organization's overall business goals to enhance business performance. KPMG can assist by defining a set of initiatives to help achieve this objective.</p>
Governance and Performance	<p>Effective IT governance and performance can help organizations enhance their business systems to deliver value to the business and monitor unique technology risks within an appropriate governance framework. Our services can assist clients in establishing a governance structure that is flexible enough to effectively guide technology decisions and technology management, while helping to ensure the appropriate controls are in place to mitigate the risks faced by the organization.</p>



Service Offering	Description
IT Optimization	IT Optimization is a strategic review of the value IT delivers to an organization. Focusing on cost performance, KPMG can identify the cost drivers and the relative financial performance of the IT systems and operations. IT optimization can lead to the development of long-term sustainable performance enhancement consistent with strategic goals.
Security and Privacy Advisory	Security and Privacy Advisory Services can provide clients with an independent review of the alignment of their security architecture with their strategic position and vulnerabilities. Through the understanding of the threats and risks an organization is exposed to, KPMG can assist in determining the performance enhancements that could improve an organization's secure environment.
IT Asset Management and Contract Compliance	IT Asset Management looks at how an organization tracks and administers its technology assets, by assessing the design and operating effectiveness of the asset management system, including people, processes, and technology, to identify process weaknesses. This service may also identify financial exposures from non-compliance with existing contracts.
Infrastructure and Continuity	Business Continuity Management provides services that can help organizations identify and manage disruption risk and reduce their vulnerability to devastating events. This service can help an organization resume critical operations within an acceptable time frame following interruption.
IT Due Diligence	IT Due Diligence reviews a target to assess the risks associated with its IT systems and the feasibility of the projected EBITDA, given the alignment of IT plans with business plans. The service can help assess the target's IT people, processes, systems, and technology to provide indications of anticipated post-deal IT expenditures and opportunities for performance enhancement.
IT Attestation	IT Attestation Services can provide clients with independent assurance regarding the effectiveness of their internal controls and/or other aspects of their IT systems and related processes.

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