Further notes on Canada's gradual adoption of International Financial Reporting Standards

Appendices to the article "IFRS in Canada: evolution or revolution?", which appeared in the May 2007 issue of *CMA Management*

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The figure and chart appended with this note provide illustrations of the impact on financial statements that the adoption of International Financial Reporting Standards (IFRS) will have in Canada (see the figure) and a brief summary of individual differences between the two sets of rules (see the chart).

The figure compares the presentation of financial statements prepared (A) under Canadian GAAP prior to the adoption of the IFRS approach regarding financial instruments and comprehensive income in October 2006 for public companies (October 2007 for non public), and (B) under IFRS. It shows the following:

- **In the balance sheet:** Sub-titles are the same but the ranking may be reversed. One difference appears in the presentation of minority interest, which is included in shareholders' equity under IFRS.
- **In the income statement**: There is no separate presentation of extraordinary items under IFRS and minority interest is not considered an expense. However, the profit under IFRS is broken down into two shares: one attributable to the equity holders of the parent and one attributable to minority interest.
- **In the equity-related statements:** The full equity is reconciled under IFRS while just the retained earnings are under Canadian GAAP. Also, an additional disclosure named *statement of recognised income and expenses* is required under IFRS.

The chart gives a summary of the differences discussed in the paper mentioned above. It also includes recent changes on consolidation (non-amortization of goodwill) and business combinations (abolishment of pooling-of-interest method), as well as the current Canadian project on business combinations that proposes to extend the measurement of assets, liabilities and minority interest of acquired subsidiaries to the full fair value on the date of acquisition. The chart contains the following:

- Canadian practices prior to convergence
- Actual IFRS
- Actual or anticipated date of convergence
- Some brief comments about the impact on financial statements of the convergence to IFRS in Canada

Footnotes relating to the figure:

1. The figure compares presentation only, it does not consider measurement
2. The Canadian GAAP are prior to October 2006 for public companies, and prior to October 2007 for non-public
3. Other equity items include contributed surplus and foreign exchange gains/losses under the current rate method
4. One common practice under IFRS is to rank balance sheet items in increasing-liquidity order (such as in the figure). The ranking in decreasing-liquidity order (such as under Canadian GAAP) is also permitted by IFRS
5. The statement of recognised income and expenses is an additional disclosure named comprehensive income in the new approach of Canadian GAAP

FIGURE - COMPARISON OF FINANCIAL STATEMENT PRESENTATION[1] : CANADIAN GAAP PRIOR TO OCTOBER 2006[2] VS IFRS

A) Financial statements under Canadian GAAP prior to October 2006[2]

B) Financial statements under IFRS

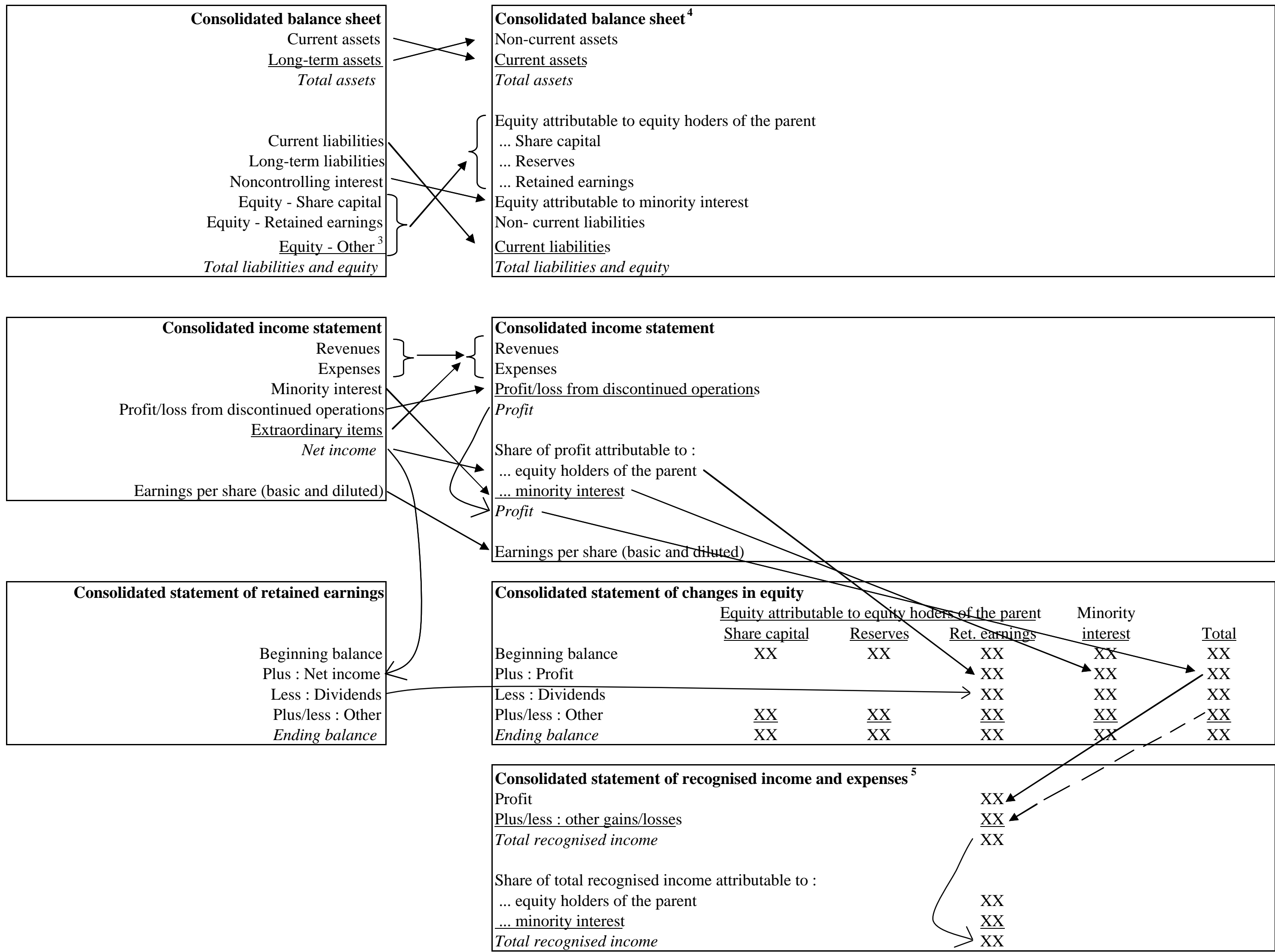

CHART - SELECTED DIFFERENCES BETWEEN CANADIAN GAAP AND IFRS
Prepared by Michel Blanchette, CMA, FCMA

Canadian practice prior to convergence	International financial reporting standards (IFRS)	Date of convergence*	Impact on financial statements of the convergence to IFRS in Canada
Ranking of balance sheet items By decreasing order of liquidity.	By decreasing or increasing order of liquidity.	2011*	This is about presentation only in the balance sheet. Content is similar but ranking of items may be reversed.
Inventory valuation Several methods accepted including last-in-first-out (LIFO).	LIFO is prohibited.	2008*	Inventory will generally increase and cost-of-goods-sold decrease for companies that used LIFO.
No reversal of impairment losses possible.	Reversal of impairment losses is possible.	2008*	Gains on reversal of impairment will increase profit.
Long-lived assets Tangible and intangible assets are measured at cost or amortized cost, with possible impairment. No revaluation at fair value is possible except in the context of push-down accounting.	Tangible and intangible assets are measured at cost or amortized cost, with possible impairment, and revaluation at fair value is possible.	2011*	Long-lived assets are going to be revalued upward as market values increase.
No reversal of impairment losses possible.	Reversal of impairment losses is possible.	2011*	Gains on reversal of impairment will increase profit.
Financial instruments Until 2006, most financial instruments were measured at cost, except for trading, speculative or non-hedging derivative financial instruments that were at fair value since 2003.	Derivatives and held-for-trading instruments are measured at fair value and gains/losses immediately recognised in the income statement. Available-for-sale instruments are also measured at fair value but gains/losses allocated directly to equity (in a reserve account) until realised.	2006	Volatility of financial assets/liabilities and underlying gains/losses will increase, but some of the latter will be allocated directly to equity (reserves or other comprehensive income - OCI), bypassing the income statement until their realisation.
Transaction costs on financial instruments other than held-for-trading can be expensed or capitalized.	Transaction costs on financial instruments other than held-for-trading must be capitalized.	2011*	Carrying value of some financial assets/liabilities will increase slightly.

* When the date is asterisked, it is anticipated. Otherwise it is actual.

Canadian practice prior to convergence	International financial reporting standards (IFRS)	Date of convergence*	Impact on financial statements of the convergence to IFRS in Canada
Interests in joint ventures Joint ventures must be consolidated using the proportionate consolidation method.	Both proportionate consolidation and equity method are possible. But proportionate consolidation should be prohibited by 2008.	before 2011*	The accounting treatment for joint ventures will consist of netting the share held of all assets/liabilities on one line in the balance sheet and also of all revenues/expenses on one line in the income statement. One effect will be that individual debts of joint ventures will become off balance sheet.
Hyperinflation No special treatment when there is hyperinflation in the economy, except that the temporal method must be used for foreign currency translation in that context (current rate method is not permitted when there is hyperinflation).	Non-monetary items are restated to current value using a general price index to reflect changes in the general purchasing power when there is hyperinflation in the economy of the reporting currency.	2011*	Non-monetary items of the balance sheet will increase dramatically in value when there is hyperinflation. Also the volatility of profit will increase due to the gains/losses resulting from the change in the purchasing power of the net monetary position.
Deferred income tax Terminology used in Canada is *future income tax*. It is possible to present *future income tax* in current and long-term assets/liabilities.	Deferred income tax cannot be presented in current assets/liabilities. It must be presented as non-current.	2009*	Some current assets/liabilities will transfer to long-term.
Minority interest Minority interest is called *noncontrolling interest* in Canada. It is measured at carrying value and presented outside of equity in the balance sheet.	Minority interest is measured at fair value (of identifiable net assets) on the date the subsidiary is acquired and presented within the shareholders' equity.	2009*	Minority interest will shift from outside to inside shareholders' equity and will be measured initially at fair value instead of carrying value. This will reduce the leverage or debt ratio.
The share of profit attributable to minority shareholders is an expense named *non-controlling interest* in the income statement.	The share of profit attributable to minority shareholders does not reduce profit as an expense in the income statement.	2009*	Profit in the income statement will increase as the share of profit attributable to minority shareholders will not be expensed any more (assuming the subsidiaries are profitable).

Canadian practice prior to convergence	International financial reporting standards (IFRS)	Date of convergence*	Impact on financial statements of the convergence to IFRS in Canada
Equity-related items Until 2006, the equity section included share capital, retained earnings, and some other items. Other items included contributed surplus and foreign exchange gains/losses. The *statement of retained earnings* was presented. Since October 2006, equity is converged with IFRS, except for minority interest and for the terminology associated to OCI.	Four categories compose equity: share capital, retained earnings, reserves and minority interest. The individual components of equity must be reconciled in a *statement of changes in equity*.	2006	The well-known *statement of retained earnings* will be replaced by a global reconciliation of all equity items.
Comprehensive income Didn't exist in Canada before 2006.	A *statement of recognised income and expenses* (or statement of comprehensive income) must be presented. This statement includes net income and other unrealised gains/losses.	2006	A new measure of profitability is going to be presented, more centred on fair values and including net income and other unrealised gains/losses.
Long-term contracts Long-term contracts can be accounted for using the percentage-of-completion method or the completed-contract method.	Long-term contracts must be accounted for using the percentage-of-completion method. Completed-contract method is prohibited.	2011*	There will be less volatiliy in profit for companies that used the completed-contract method.
Changes in depreciation/amortization methods Until 2006, changes in depreciation/amortization methods were considered changes in accounting policies and treated retroactively.	Changes in depreciation/amortization methods are considered changes in estimates and treated prospectively.	2007	Adjustments due to changes in depreciation/amortization methods will have to be applied to the current and/or future income statements as they will be treated prospectively.
Foreign exchange gains and losses under the temporal method Foreign exchange gains/losses were amortized until 2001. This treatment was abolished in 2002.	All foreign exchange gains/losses are included in the income statement immediately.	2002	The stop on amortizing foreign exchange gains/losses increases volatility of profits.
Foreign exchange gains/losses on financial assets available-for-sale are allocated to OCI.	Foreign exchange gains/losses on financial assets available-for-sale are immediately included in the income statement.	2011*	Variations in profit will increase as unrealised foreign exchange gains/losses on financial assets available-for-sale will be forced to the income statement (instead of OCI).

Canadian practice prior to convergence	International financial reporting standards (IFRS)	Date of convergence*	Impact on financial statements of the convergence to IFRS in Canada
Extraordinary items Separate presentation as extraordinary items is possible when gains/losses meet certain criteria.	Separate presentation as extraordinary item is prohibited.	2011*	The breakdown of items will change as extraordinary qualification will not be permitted. But it won't change the bottom line.
Business combinations and consolidation Goodwill is not amortized since 2001. Before that date, it was amortized over a maximum of 40 years.	Goodwill is not amortized since 2004. Before that date, it was amortized over a maximum of 20 years.	2004	The stop on the amortization of goodwill increases profits, except for the years when impairment losses are recognised.
All business combinations are accounted for using the purchase method since 2001. Before that date, the pooling-of-interests method could be used in some circumstances.	All business combinations are accounted for using the purchase method since 2004. Before that date, the pooling-of-interests method could be used.	2004	Subsequent profits after business combinations that could have been treated as pooling-of-interests are reduced because of the increased amortization.
On the date of acquisition, the measurement of items acquired is based on their fair value to the extent of the ownership acquired.	On the date of acquisition, the measurement of items acquired is based on their full fair value.	2009*	Assets/liabilities are going to increase when subsidiaries are acquired at less than 100% ownership. Subsequent profits will be affected downwards because of the increased amortization expense (but they will also be affected upward because of the share of profit attributable to minority shareholders which is not going to be expensed any more in the income statement - as described above).
Interest and dividends in the cash flow statement Interest and dividends are generally presented in operating activities.	Interest and dividends can be presented in operating, financing or investing activities.	2011*	The net cash variation will be the same in the cash flow statement, but the breakdown of interests and dividends in individual categories will change, improving their classification (financing or investing instead of operating).