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Toronto Public Library Board

Audit plan for the year ending December 31, 2012

November 15, 2012

Members of the Board
Toronto Public Library Board

Dear Board Members:

We are pleased to present our audit plan for the 2012 audit of the financial statements of Toronto Public Library Board (the Library) prepared in accordance with Canadian generally accepted accounting principles (hereafter referred to as the financial statements).

This document summarizes our audit plan including our view on audit risks, the nature, extent and timing of our audit work as well as our proposed fees and the terms of our engagement.

We value your feedback and we hope that this document will facilitate two-way communication with you on the risks identified and our audit approach. We welcome any suggestions and observations you may have.

Yours very truly,

PricewaterhouseCoopers LLP

Terri McKinnon
Partner
Audit and Assurance Group

cc: Mr. Larry Hughsam, Director of Finance and Treasurer

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Appendices

1. Executive summary

We have prepared the attached document to provide you with the opportunity to review and comment on our audit plan for the 2012 audit of the financial statements.

This audit plan includes the required communications between an auditor and the Board as required by Canadian generally accepted auditing standards (Canadian GAAS).

Below, we highlight key areas for discussion, including new matters or changes from the prior year's audit plan to facilitate your review.

Discussion item	**Summary**	**For further reference**
Client service team	• Terri McKinnon is your engagement leader and Sarah Valimohamed is your engagement manager. • Our team is consistent with the prior years, except for the addition of Hisham Baig, the senior associate.	Page 3
Audit approach	• Our audit approach will consist of a mixture of key controls reliance and substantive detail testing. • Consistent with Canadian GAAS, we will also implement a level of unpredictability into our procedures each year.	Page 6
Risk analysis	• The areas of significant audit focus are consistent with the prior year: o Revenue recognition o Management override of controls o Overstatement of accruals and expenses o Valuation of employee future benefits • In addition, for the current year, we have identified the relocation of the Front Street operations as an area of focus as well	Page 6

2. *Your team*

Your client service team comprises the following individuals:

Name	Role	Number of years on engagement	Phone number	Email address
Cathy Russell	Engagement partner for the City of Toronto	3	416 815 5291	*cathy.russell@ca.pwc.com*
Terri McKinnon	Engagement partner	3	416 228 1922	*terri.mckinnon@ca.pwc.com*
Sarah Valimohamed	Engagement manager	2	416 218 1533	*sarah.valimohamed@ca.pwc.com*

3. *Scope of our services*

a. Our audit objectives

As the Library's auditor, our primary responsibility is to form and express an opinion on the Library's financial statements as at December 31, 2012 and for the year then ended in accordance with Canadian generally accepted principles. The financial statements are prepared by management with the oversight of those charged with governance (the Board).

An audit of the financial statements does not relieve management or the Board of its responsibilities. We will conduct our audit in accordance with Canadian GAAS. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

In addition, we are committed to being a trusted advisor to management and to the Board. Where appropriate, we will discuss industry standards, provide management our views and insights and also advise management of other services we feel could be helpful–at all times staying within the realms of our independence rules.

b. Engagement terms

Our engagement letter, which has been signed by the City of Toronto, sets out the terms and conditions for our engagement as the independent auditor of the Library for the above-mentioned year. In addition, our engagement letter outlines our responsibilities as the auditor and the responsibilities of management.

c. Our service deliverables

Our audit and audit related service deliverables with respect to 2012 are:

	Audit and audit related services	**Timing/status**	**The Board approval**
Audit opinion	• Audit of financial statements for the Library	• May 2013	• To be approved at your meeting in May 2013.
Audit report findings	• Key findings (particularly regarding significant estimates, transactions, accounting policies and disclosures) • Any significant deficiencies identified in internal controls • Provide a confirmation of our independence	• May 2013	• N/A

4. When will we do the audit?

Working with management, we have developed the following project timeline, which is consistent with the Library's reporting requirements.

Audit planning	
Presentation of audit plan to the Board by management	November 29, 2012
Audit	
Interim audit visit	November 12 - 16, 2012
Year-end audit	April 8 - 19, 2013
Clearance meeting with management and PwC	April, 2013
Year-end Board meeting [1] and approval of financial statements by Board of Directors	May, 2013

[1] At the year-end Board meeting we will provide our draft audit opinion, key findings (particularly, regarding significant estimates, transactions, accounting policies and disclosures), any significant deficiencies identified in internal controls and also provide a confirmation of our independence.

5. *How will we do the audit?*

a. Our audit approach

Our audit approach is designed to allow us to execute a quality and efficient audit. We do this by:

i. Gaining an understanding of the business by focusing on new developments and key business issues affecting the Library as well as management's monitoring of controls and business processes;
ii. Identifying significant audit risks, sharing our perspectives, obtaining your feedback and ensuring our audit is tailored to these risks;
iii. Using well-reasoned professional judgment, especially, in areas that are subjective or require estimates; and
iv. Leveraging reliance where possible on the Library's internal controls and information technology and data systems.

In the current year, our planned work will include testing of key controls in the following areas:

- Purchases, payables and disbursements
- Payroll

All other areas will be subject to tests of detail and substantive analytical testing.

Our approach will, therefore, include a mixture of key controls reliance, substantive analytics and detailed testing. Our understanding of the Library also drives our assessment of materiality and the identification of audit risks.

Throughout the audit, we scale our work based on the size of an account balance, its complexity and its impact on the financial statements. As a result, you will always hear us talking to you about the key issues.

b. Risk analysis

Significant risks are those risks of material misstatement that, in our judgment, require special audit consideration. We have identified the following significant audit risks and other risks, including business risks with a potential audit impact, as part of our planning process.

These risks were identified based on discussions with management, our knowledge of the business and current developments in your industry and the economy.

They are the most important risks from our perspective. We request your input on the following significant risks and whether there are any other areas of concern that the Board has identified.

Risk area (including key judgments and estimates)	Management's response	Our audit approach
Risk of management override of controls	All non-routine journal entries are reviewed and approved by the appropriate level of management.	• We will review manual journal entries focusing on large and unusual entries. • We will review accounting estimates for biases that could result in material misstatement due to fraud. • We will incorporate unpredictable procedures in the audit approach.
Revenue recognition	Government grants are supported by approved documents, which specify the period to which the revenue relates. User charges relate to fines and late fees levied by library branches. Transaction tapes for these charges are reconciled to cash deposited on a daily basis. Donations are primarily from the Library Foundation and agree to the Foundation's financial statements. Other income consisting primarily of rental revenue over properties rented out, are reconciled monthly and agreed to the lease agreements and period earned.	• Assess the design and validate the operating effectiveness of certain key revenue cycle controls. • Perform substantive analytical and tests of detail procedures, including grant revenue confirmations.
Overstatement of accruals and expenses	Accruals are reviewed closely during period end to ensure proper cut off. Management prepares quarterly reports of actual-to-budget, with significant or unusual variances investigated and presented to the Board.	• We will review the nature of expenses/accruals to ensure they are accurate and properly exist, and included in the correct period.
Valuation of employee future benefits	The Library relies on a third party valuation expert, Buck Consultants, to value the employee future benefits.	• We will obtain confirmation of valuation from Buck Consultants. • We will consult with our internal Actuarial group to ensure that the discount

Risk area (including key judgments and estimates)	**Management's response**	**Our audit approach**
		rates and assumptions used in the valuation are appropriate.
Relocation of Front Street operations In the current year, the City negotiated a land exchange with a third party to facilitate the City's goal of bringing certain pieces of land under public ownership	With the change of ownership at 281 Front Street, the Library will reflect a tangible capital asset disposition for the building.	• PwC will review the details of the transaction, including the resolutions detailed in the Board minutes to ensure the transaction was accounted for correctly

- Our professional standards require us to communicate the qualitative aspects of new accounting policies selected and our views on alternative policies.

c. Materiality

Misstatements, including omissions, are considered to be material if they (individually or in aggregate with other misstatements) could reasonably be expected to influence the economic decisions of users, taken on the basis of the financial statements.

Judgments about materiality are made in light of surrounding circumstances and are affected by the size or nature of a misstatement, or a combination of both. A common measure for setting materiality for a not-for-profit Library is to use ½% to 2% of revenue or expenditures.

We have set our preliminary materiality for the audit as follows:

	Basis	**Amount**	**Prior year's amount**
Overall materiality[1]:	1 ½% of expenses (2011 – 1 ¼%)	$ 3,100,000	$2,600,000
Unadjusted and adjusted items in excess of this amount will be reported to the Board	5% of overall materiality	$155,000	$130,000

d. Discussion on fraud risk

Canadian GAAS require us to discuss fraud risk annually with the Board. We understand that part of your governance role is also to consider the fraud risks facing the Library and the responses to those risks.

Question 1:

Required discussion	• Through our planning process (and prior years' audits), we have developed an understanding of your oversight processes including: o Code of conduct o Discussion at Board meetings and our attendance at those meetings o Presentations by management, including business performance reviews o Signing authorities • Are there any new processes or changes to the above that we should be aware of?
Notes:	

1 Our materiality calculation is based on current forecasted results; should there be a significant change, we will communicate changes to the Board at year-end.

Question 2:

Required discussion	We are not aware of any fraud at the current time. We would like to ask whether you are aware of instances of actual, suspected or alleged fraud affecting the entity.
Notes:	

6. Our commitment to audit quality

We are proud of PwC's long history of delivering high quality and recognize that quality in everything we do is paramount. We know that you expect our people to be competent, objective and embody the right level of professional skepticism - while at all times maintaining an open dialogue with your management team. We believe our core values described below ensure that we achieve audit quality and quality service at the same time.

Core Value	***How it helps us execute a high quality audit***
Investing in relationships	• We believe that the professional relationships we foster with management and the Board allow us to have open and candid dialogue over issues including, when necessary, asking those difficult questions. • Relationships also allow us to provide timely advice and enable us to better understand the company's business.
Sharing and collaborating	• Tackling today's complex business issues requires the collaboration of different team members from various areas of our firm such as tax or valuation experts. • Our experts will work with members of your team to help solve complex issues and bring forward best practices
Putting ourselves in others' shoes	• Listening to and understanding others' perspectives allows for enhanced dialogue and allows us to think about issues from various points of view. • We consider issues from multiple perspectives, starting with the standards, and including the views of management and the Board as well as our assessment of what financial statement users expect. While we will express our views or preferences, we do not impose them on you unless we believe that there are no other alternatives within the standards.
Enhancing Value	• Our understanding of the business and execution of a quality audit allows us to identify issues that are important to the Board and management. • Within the realms of our independence rules, it also offers opportunities to provide recommendations and insight on improvements in controls, operations and other areas of business that can enhance shareholder value.

These core values govern how we operate - the audit work and documentation of procedures in our files are also always of the same high standard. Our people are subject to continuous training to ensure that they are equipped with the right tools and best practices to achieve quality and a focus on continuous improvement.

Although our audits are planned to focus on the key risks, our professional audit standards and regulators require us to ensure that we have sufficient evidence in all areas of our files. While we strive to achieve high quality in a cost effective manner, the reality is that we are being required to do more to comply with existing standards and to meet our regulator’s interpretations of what audit quality is. This means that you will see us performing procedures in areas that you might consider lower risk.

As always we welcome your feedback on our performance and your views on how we achieve quality. You have our commitment that audit quality is paramount and you can have the confidence that the audit work performed by PwC will stand up to the scrutiny of contributors and other stakeholders.

7. Our fees

Our estimated fees are based on the expected time required to complete the audit. Our fees exclude taxes and include out-of-pocket costs, as outlined in our engagement letter dated November 1, 2010.

We estimate our fees for 2012 will be as follows:

Service description	Estimated fees 2012 $	Actual fees 2011 $
Audit of the financial statements	28,690	26,730

Should we incur additional costs due to changes in the level of effort or scope changes, we will advise management.

Conditions that could result in additional costs include, but are not limited to, the following:

1. Changes to the timing of the engagement at your request may result in the services being performed by staff at a higher rate than initially planned, or difficulty in reassigning individuals to other engagements, either of which may result in our incurring significant unanticipated costs.

2. All schedules are not (a) provided by you on the date requested, (b) completed in a format acceptable to us, (c) mathematically correct or (d) in agreement with your accounting records (e.g. general ledger accounts).

3. Your personnel are not readily available or there is a significant delay in providing adequate responses to our requests for information, such as reconciling variances or providing requested supporting documentation (e.g. invoices, contracts and other documents).

4. Significant number of adjustments posted by you after we start our work that result in us having to update previously completed work.

5. The financial statements are received late or there are a significant number of drafts or a significant number of changes identified as a result of our review.

8. New accounting standards

a. Financial instruments and financial statement presentation

In March 2011 PSAB approved section PS 3450, Financial Instruments, and will be effective for periods beginning on or after April 1, 2012 for government organizations and April 15, 2015 for governments. The new section provides guidance on the recognition, measurement, presentation and disclosure of financial instruments. Financial assets and/or financial liabilities are to be recognized when the entity becomes a party to a financial instrument contract. Derivatives and portfolio investments that are equity instruments quoted in an active market are to be measured at fair value. The entity may report non-derivative financial assets and/or financial liabilities on a fair value basis if it manages and reports performance of these items on a fair value basis. The change in fair value of the items is recognized in the statement of remeasurement gains and losses until settlement.

In March 2011 PSAB approved section PS 1201 which replaces section PS 1200, Financial Statement Presentation, and will be effective for periods beginning on or after April 1, 2012 for government organizations and April 15, 2015 for governments. The new Section includes a statement of remeasurement gains and losses which will report; unrealized gains and losses with the change in fair value of financial instruments; exchange gains and losses associated with monetary assets and monetary liabilities denominated in foreign currency that have not been settled; amounts reclassified to the statement of operations upon derecognition or settlement; and other comprehensive income reported when an entity includes the results of its government business enterprises and government business partnerships in the summary financial statements.

We have assessed the impact of these changes on the financial statements of the Library. The impact is not expected to be significant.

b. Other projects

Other previously communicated projects are in progress for PSAB:

- Amalgamation and government restructuring - A project was approved in March 2009 to issue an accounting standard that addresses the definition and classification of amalgamation and restructuring activities; the recognition criteria and accounting treatment of various elements of the amalgamation and restructuring transaction; the measurement basis of assets and liabilities involved; and the disclosure requirements unique to amalgamation and restructuring. A statement of principles is expected to be approved in December 2011.
- Assets - Section PS 3200 addresses the basic concepts and key terms in the definition of liabilities with further guidance, examples and indicators. It also establishes the recognition and disclosure standards for liabilities. Similar standards on assets would be useful not only for financial statement preparers and auditors in application and interpretation of the definition of assets, but also for the development of future standards on specific assets. The objective of this project is to provide guidance relating to the key terms in the definition and essential characteristics of assets, define contingent assets and contractual rights, provide recognition and derecognition criteria for assets and contingent assets, provide guidance on the measurement of assets and contingent assets (including impairments) and provide guidance on the disclosure of assets, contingent assets and contractual rights. PSAB approved the project proposal in June 2009 and a statement of principles is expected to be approved in December 2011.
- Related Party Transactions and Appropriations - PSAB approved a project proposal in September 2010 to issue a new accounting standard covering related party transactions. The objectives of the project are to define related parties in the context of government and government organizations; describe the disclosures required; and address recognition and disclosure appropriations. Our audit national public sector leader is the chair of this PSAB task force.

The Library will need to monitor these projects for future impact on their own financial reporting.

Appendix A: Financial Reporting Release

Financial Reporting Release – September 2012

Keeping your head above water …

Recent issues in financial reporting

In this issue

"The present tense made him nervous." – William Gibson

Gather round. It's time, once again, for taking stock of what's happening in the Canadian financial reporting world. What? Is that a groan we hear? Stop it.

Indeed, if you're a fan of the status quo, we have good news to report – no major accounting standards or Canadian regulatory requirements were issued in the last six months or so, not even an exposure draft of one. The only sign of activity has been the release of a few technical amendments, clarifications and interpretations. These might excite the techies of the world, but not anyone who actually has a life.

Don't get too happy though – there are still plenty of things to worry about. Perhaps the most pressing is the prospect of having to adopt changes to International Financial Reporting Standards in the last few years that you were able to set aside when transitioning from old Canadian GAAP because of their delayed effective dates. Implementing these changes isn't mandatory until 2013, true, but that's now very near. Which of the new requirements are proving particularly troublesome to interpret and apply in practice? Which have potentially major income statement consequences? Are there other implications? We have some quick observations.

The other worry is that there are a lot of changes still in the hopper, major ones – like revenue recognition, leases, financial instruments, impairment, insurance and hedging. They're taking a little longer to finish than originally anticipated. Well, okay, a lot longer. Hence the lull in action. Confused about the reasons for the delays? Wondering where things are going and when the changes will be effective? Need something to talk about at the dinner table? We've got a status update that'll put you in the know.

The Canadian Securities Administrators ("the CSA") have always carried our detailed reviews of the quality of companies' financial reporting and, IFRS transition notwithstanding, last year was no exception. We've summed up their findings on what you should be doing to improve your own reporting as well their priorities for their 2013 year's reviews.

Fans of the soap rate regulated accounting opera, never fear, we've got the latest. This time it's a good news show – a long-term solution may be at hand. We've also got a few new messages for Canadian SEC registrants. First, "Big Brother is watching!" Second, "Get ready" – auditors are about to engage you in a dialogue more than they ever have before. Way more.

And, finally, there are the developments affecting the International Accounting Standards Board and its quest to develop IFRS into a single set of high quality global accounting standards. Learn the latest about how well the IASB is faring in convincing the SEC to move the US over to IFRS, and its new strategic and agenda priorities. The game is about to change. Big time.

And there you have it. Everything you need to know in the next eight pages. Can it get any better?

Upcoming IFRS Changes

*"I'm going to live through this even if it kills me."– Klinger, M*A*S*H*

One of the downsides for Canadian companies that moved to IFRS in 2011 is that it came in the middle of the IASB's and FASB's joint program to improve and converge IFRS and US GAAP. The consequence is that they'll be forced to change the IFRS they just adopted to give effect to any GAAP changes arising from the program that weren't already in place at transition. The old double switcheroo! Ain't life grand.

Here are the main changes, all effective for 2013:

- Consolidation – redefines when one entity controls another and so must take up the controlled entity's assets, liabilities, revenues and expenses into its financial statements. This one affects not only special purpose entities ("SPEs") and other structured arrangements, but operating companies too. A key feature of the new requirements is the concept of "de facto" control, under which holding of a large block of voting shares might be sufficient to trigger consolidation even if you don't have a majority of the votes. Everything depends on how widely dispersed the other votes are.

- Joint arrangements – eliminates proportionate consolidation for "joint ventures" but permits it for "joint operations". Which is which? Aye, there's the rub.

- Disclosures of interests in other entities – requires more discussion of nature and risks. Please.

- Employer accounting for defined benefit pension and other employee plans – mandates immediate recognition of changes in the value of plan assets and liabilities in other comprehensive income, limits the rate of return on plan assets used in calculating pension expense to a high quality bond rate, even if the company expects to (and actually does) earn a higher one. Oh, there's more disclosure too.

- Fair value measurement – reconciles diverse and sometimes conflicting guidance previously in IFRS about what fair value is and how to measure it. Some measurements may change as a consequence; e.g. some derivatives, liabilities, etc. Did we mention that there are more disclosures?

- Mining stripping costs – introduces rules for accounting for overburden by mining companies. These may not be a big issue given previous practice in Canada, but you never know till you look, do you? Dig deep.

Other 2013 changes include presentation of OCI, disclosures about offsetting assets and liabilities, a few amendments to IFRS transition rules (relax, they apply only to new transitions), and some modifications to existing standards.

pwc observation. *In practice, the rules relating to SPE consolidation and joint arrangements are proving to be the most difficult to understand and apply. Significant judgment and consultation often will be necessary. Also, some companies are using the rules on mining stripping costs as an opportunity to reconsider and refine aspects of their existing accounting.*

IFRS in the Pipeline

"Dese are da conditions dat prevail." – Jimmy Durante

Alas, the 2013 IFRS changes on the preceding page are just the beginning – there's much more in the pipeline. We provide a brief overview of the nature and objectives of these projects below. All of them, save one, are joint ones with the US, so when we say "the Boards" we mean the IASB and FASB working together. Well, sort of...

- Revenue – establishing a one-size-fits-all model for recognition and measurement. After ten years of study and debate (scary that), the (evil?) forces of fair value have been beaten back, and existing revenue recognition principles are largely being carried forward in triumph. Nevertheless, the new model will affect some companies, especially those relying on industry-specific guidance.
- Leases – putting all leases on the balance sheet as assets and liabilities (the project is also known as "death to all operating leases"). Some on both Boards now are threatening to vote against a compromise proposal designed to make it more palatable for the masses. Is this project in trouble? Maybe.
- Classifying financial assets – revisiting when you have to measure financial assets at fair value and whether changes in fair value go to the income statement or OCI, or both. The IASB got rid of OCI for financial assets when it bashed out a revised financial instruments standard in 2008 (still your beating hearts, it's not mandatory until 2015) but the FASB still wants it and it looks like the IASB is going to agree, for convergence's sake, of course.
- Impairment – recognizing and measuring loan losses using the so-called "three bucket approach" under which the losses get bigger as you move from bucket to bucket. Or maybe not. After consultation with constituents, the FASB has very recently decided the model just isn't workable. It's now going to develop a different solution all on its own, which it'll then share with the IASB. And what's the IASB going to do? We don't know, but it's not happy. Convergence in this area is critical to financial institutions. The Chair of the IASB has gone so far as to describe the prospect of the project's collapse as an embarrassment to both Boards.
- Hedging – simplifying and expanding hedge accounting using a business model approach. This isn't really a joint project – the only link to US GAAP is that the FASB has agreed to ask constituents what they think of the IASB solution at the same time it proposes something completely different. The IASB also has a "macro hedging" project on the go, something we suspect the US wouldn't touch with a ten foot pole.
- Insurance contracts – figuring out a common model for all insurers, well, not quite, as the Boards have fallen out over one technical aspect (you don't want to know). Still, they're way closer than they are on impairment or hedging. So far anyway.
- Investment entities – providing an exception for these entities that would allow them to measure investments in subsidiaries at fair value instead of consolidating them. The Boards don't see eye to eye on some major aspects but getting the IASB to provide an exception of any kind has been quite the achievement. Until recently, the IASB viewed any idea that you might not consolidate a subsidiary as blasphemy.

pwc observation. *The IASB has promised the G20 and the Financial Stability Board that it would get all of these projects out the door by the middle of next year, but that seems almost impossible now. Regardless of the timing of finalization, we expect that the more significant projects, such as revenue, impairment and leases, will have extended transition periods (e.g., three full years) to give companies ample opportunity to properly consider them. So, you don't have to start sweating just yet. Unless you want to, of course. For instance, some companies are eager to adopt the new hedging rules as soon as possible. The IASB is targeting issuing these particular rules by the end of this year (don't forget the Canadian Accounting Standards Board will have to ratify them too).*

CSA Views on the Current State of Canada's Financial Reporting

"I feel like a fugitive from the law of averages." – William H. Mauldin

In June, the Canadian Securities Administrators issued their annual report on the results of their continuous disclosure review program for their year ended March 31, 2012. Not only does it provide the CSA's views on Canada's cross-over to IFRS last year, it also assesses the quality of the country's ongoing IFRS accounting, Mangement Discussion and Analysis and other reporting such as executive compensation details. The report thus isn't merely a memorial to a transition exercise that no one cares about anymore, but rather one that is actually relevant to your future reporting.

Here are the principal findings:

- Canada's transition to IFRS. "Generally positive" (though about five percent of issuers were required to restate financial statements).
- Financial statement presentation. Debt too often is being shown as long-term when it's current, at least under IFRS.
- Accounting policies. Too much boilerplate and vague disclosure. Also, a failure to disclose all policies that are relevant to understanding the financial statements (e.g., companies that issue flow through shares not disclosing their accounting for these arrangements).
- Business combinations. Frequent failure to make all IFRS-required disclosures.
- MDA. Often insufficient and less than incisive analysis (e.g., for revenue, not quantifying volume and price changes and their reasons, including the impact of competition; for liquidity not being sufficiently forthcoming about commitments, events or uncertainties – remember, the MDA is supposed to complement the financial statements, not just duplicate them). Companies in specialized industries, the high-tech sector for example, beware! The CSA has fingered reporting in these industries as being especially problematic.
- Other areas. Spotty compliance with statutory disclosure requirements for mining projects and oil and gas activities, the statement of executive compensation, and corporate governance practices.

The report's overarching observation is that companies should be focusing on providing "entity specific" disclosures, in both their financial statements and the MDA. For this year's reviews, impairment, business combinations and judgments and estimation uncertainty disclosures are particular priorities.

pwc observation. *You might want to consider how well your own financial reporting stacks up against the CSA's findings and take appropriate remedial action if necessary. Remember, it's not a question of whether your reporting gets reviewed, it's when. The alternative of hoping the CSA won't notice significant deficiencies usually isn't a very good bet. As to CSA's priorities for this year, impairment and business combinations are predictable choices, but some might be surprised to see judgments and estimation uncertainty disclosures on the list. The CICA's IFRS Discussion Group raised companies' practices in this area as an issue earlier this year. The objective of the disclosure is to discuss only those key uncertainties and estimates that are most significant and provide meaningful disclosure about their effects. Not, repeat not, throw everything in but the kitchen sink with little or no discussion of impacts.*

Rate Regulated Enterprises

"Record-Setter for Longest Time to Live with Bullet in Head Dies at 103." – Recent obituary headline

For Canadian rate regulated enterprises, the path to IFRS has been a rocky one, full of near death experiences.

Recall that the Canadian Accounting Standards Board gave RREs until 2012 to transition to IFRS, rather than forcing them to move over in 2011 like almost everyone else. The RRE deferral came about because of the IASB's last minute decision in 2010 not to provide clarity on whether IFRS allows an RRE to set up assets and liabilities as the result of a regulator's rate order, as old Canadian GAAP does. Many hold the view that IFRS doesn't permit setting up assets or liabilities at all. We don't agree, but even under our view, you won't always get the same answers as old Canadian GAAP.

In 2011, Canadian provincial securities commissions responded to RREs concerns about the impact of IFRS by giving those listed on exchanges the option of following US GAAP instead. This generally requires the same accounting as old Canadian GAAP. There's a catch, though. The CSA's relief is only good through to the end of 2014. Then companies will have to either switch to IFRS or register with the SEC to maintain the right to follow US GAAP that exists under current Canadian securities legislation. The CSA hasn't said why it imposed this limit but the best guess is that they were trying to avoid setting a game changing precedent by allowing an entire industry to use US GAAP and at the same time allow for an IFRS-based solution to develop.

If so, it might just work! In May, the IASB announced a decision to consider whether to put RRE accounting back on its agenda. While a final standard wouldn't be in place in time for 2015 reporting, some members of the IASB also have raised the possibility of introducing interim measures that would allow Canadian RREs to continue their existing basis of accounting. Seizing on this possibility, the Canadian Board promptly extended the date of mandatory transition to IFRS for RREs until 2013. This decision mostly benefits non-public ones (such as entities in the public sector) unable to take advantage of the US GAAP reporting option available to public ones.

pwc observation. *For the longest time now, accounting for rate regulation, Canadian style, has been among the walking wounded. Whether the IASB's actions are a prelude to a full recovery and a long and healthy life remains to be seen. We understand that the IASB's tentative agenda decision is the result of special pleading from Canada, Brazil and India. We say, Good on you!*

Developments affecting Canadian SEC Filers

"Most conversations are simply monologues delivered in the presence of a witness." – Margaret Miller

Two things have happened recently that you need to be aware of if you're a Canadian SEC registrant.

The first is that the SEC has begun to review and comment on first time IFRS financial statements included in Canadian SEC filings. If you haven't got one already, you can expect a friendly letter soon. Remember, too, that communications with the SEC are a matter of public record.

The second relates to communications between auditors and audit committees. In August, the US Public Company Accounting Oversight Board approved new requirements for the auditor to discuss:

- Its evaluation of the quality of the company's financial reporting.
- Certain matters about the company's accounting policies and practices on estimates including a description of the processes and assumptions management used in critical estimates.
- Significant unusual transactions including the underlying business rationale.
- Its views on significant accounting or auditing matters when they are aware that management has consulted with other accountants about these matters and the auditor has a concern.

The new rules also formalize PCAOB required communications that many auditors already are making to audit committees as a matter of practice or as the result of other regulations (e.g. audit strategy and risks, specialized skill needs (such as actuaries, valuators and others), principal auditor determinations, concerns about management's proposed adoption of new standards, outside consultations, contentious matters, going concern issues, qualifications in audit reports, etc.)

The requirements, if approved by the SEC, would apply for years beginning on or after December 15, 2012 however, there may be some scope exceptions.

pwc observation. *With respect to SEC reviews of Canadian IFRS filings, so far the SEC seems to be asking interesting questions about IFRS matters but generally isn't raising an extensive number of comments. With respect to auditor communications, the PCAOB has emphasized that the objective of the requirements is to establish meaningful dialogues between auditors and audit committees, not to create yet another compliance checklist.*

IFRS in the US

Georgia: "Jonathon, will you marry me?"
Jonathon: "Not even a little bit."
The Bad and the Beautiful, 1942

That whooshing noise you're hearing? It's the sound that comes from rapidly deflating expectations.

Devout readers of Financial Reporting Release will know that the IASB has been pressuring the SEC for years to incorporate IFRS into US financial reporting. Getting a firm commitment out of the US to do this has been a very big deal for the IASB, not only because the US is the world's biggest economy but also because a US move to IFRS would go a long way to convincing China, Japan and India to embrace it as well. In short, the US is the biggest thing standing in the way of the IASB realizing its goal of becoming the world's sole purveyor of global accounting standards.

Hopes among IFRS supporters were high that the SEC staff would recommend the US make a positive commitment of some kind or another in its long-awaited final report to the Commission about its IFRS investigations. Alas, the report, issued in July, is limited strictly to a pros and cons assessment of IFRS and the IASB. All the report says about transition is that there's substantial backing in the US for the idea of exploring methods for incorporating IFRS on a basis that both reflects US support for a single set of high quality global accounting standards and considers US concerns. So the door hasn't been closed completely, but it hasn't been opened either. Not even a crack.

What's been the response from the IASB and its supporters? Frustration, disappointment, and, in some quarters, more than a little bitterness. In their view, the time for exploring options has long since past. Whoosh!

pwc observation. *There appears to be a number of factors that weighed against the SEC taking a stand on IFRS right now. Perhaps the most significant are (1) support for IFRS in the US business community is very much on the wane, and the small business sector, which sees substantial costs but no benefits, actively opposes it, (2) the SEC report raises significant issues about the completeness of IFRS relative to US GAAP, the consistency of IFRS application and enforcement around the world, and the adequacy of the IASB's interpretative processes and funding, (3) this is a presidential election year and the SEC is leery about doing anything that might be politically controversial, and (4) the possibility of having to involve Congress in any decision. Of course, among the risks to the US of continuing to sit on its hands is that it gets booted off the IASB and its oversight bodies, losing some of its influence over global standard setting. Might that happen? We'll see.*

The Future of the IASB

"... I'm designing T-shirts now. They're gonna be huge. Also medium and small." – Dylan, Modern Family

Some months before the SEC released its report on IFRS that we discussed on the preceding page, the oversight bodies of the IASB, the IFRS Trustees and the Monitoring Board, unveiled a new strategic plan for the IASB – a new vision, if you will, establishing the IASB's direction, operations, governance and funding for the next ten years.

The plan affirms that the IASB's foremost objective is developing IFRS as a single set of high quality, understandable and enforceable global accounting standards. Major new strategic initiatives flowing from this objective include:

- Given the widespread and growing use of IFRS, focusing activities on serving the needs of the countries that have adopted or plan to adopt IFRS.
- Maintaining a network of national and regional bodies involved with standard setting as an integral part of the standard setting process. The idea here is that the network would undertake research, provide guidance on priorities, encourage stakeholder input from their own jurisdiction into the IASB's due process, identify emerging issues, etc. The goal is to reduce the risk of non-endorsement of new IFRS.
- Improving the clarity of its standards and the responsiveness of the IFRS Interpretations Committee.
- Developing a mechanism for securities and audit regulators, the accounting profession and the IASB to discuss ways to enforce the application of IFRS and identify and address areas of divergence.
- Establishing funding on a basis that relies more on long-term fixed commitments from participating countries and less on short-term voluntary contributions.

pwc observation. *The Chair of the IASB describes its new strategic initiatives as establishing global financial reporting supply chain, and the final piece in the jigsaw that is international reporting standards. While the concept and its design have been greeted with enthusiasm, let's face it – plans come cheap. The real challenge will be their implementation. For IFRS to be an effective set of high-quality global accounting standards, it's not enough that the standards be "enforceable"; they must be consistently enforced. And that will require extensive co-operation, co-ordination and commitment from local regulators and other bodies that participate in this process. This is a huge challenge if the difficulties the IASB and FASB have had in co-operating over the development of converged standards are any guide.*

The IASB's New Agenda Priorities

"I was a peripheral visionary. I could see the future, but only way off to the side." – Steven Wright

pwc observation. *We have two general observations about the Board's agenda priorities. The first is that we are very glad to see disclosure and basic financial statement concepts becoming priorities. Both are root causes of complexity in financial statements. While the disclosure initiative perhaps may seem a bit tentative, we expect it's only a first step. As for the financial statement concepts project, a key priority will be re-examining measurement and financial statement presentation, areas which constituents have been complaining about for years but nobody has done much about. Certainly the time is ripe for action. Did you know, for instance, that collectively IFRS has over 20 different bases of measurement now in play? Our second observation relates to the role that convergence with US GAAP now plays in the Board's agenda decisions – none whatsoever. Once its existing projects are done, that's it; the IASB has no further interest in convergence as a long-term strategy. Such an approach can't help but to raise the risk of divergence, but, as we've already seen earlier on these pages, working together provides no guarantee that converged answers will result anyway. In the IASB's view, a single global GAAP can emerge only if everybody uses the same standards. And in the IASB's view, those are IFRS. If the US doesn't want to play ball, so be it.*

Coincident with its new strategic priorities, the IASB has been doing some forward thinking about what its agenda priorities should be after it completes its existing projects (see "IFRS in the Pipeline"). This has been preceded by an unprecedented level of consultation with constituents, something that is itself a new feature of the IASB's standard setting processes.

Reacting to concerns constituents expressed about standards overload, the Board adopted a new attitude in developing its agenda priorities, one best summed up by its Chair in a recent speech as "Fix what needs fixing and no more". (As a motto, not quite as catchy as "No wine before its time", perhaps, but not bad.) The result is that the Board has decided to consider adding only three standards-level projects to its agenda – rate regulated enterprises (see our earlier discussion); applying the equity method in separate financial statement of the investor; and improving existing IFRS on agriculture. That's it, at least for new standards... but there are a few other initiatives as well:

- Hosting a public forum to assess strategies for improving the quality of financial reporting disclosures within the framework of existing requirements.
- Reactivating its project to re-examine basic financial statement concepts.
- Initiating a staff research program focusing initially on discount rates, the equity method of accounting, extractive industries/intangible assets/R&D, financial instruments with characteristics of equity, foreign currency translation, non-financial liabilities, and financial reporting in high-inflation and hyper-inflationary economies. Also, recommencing research on emissions trading schemes and business combinations under common control.
- Establishing a consultative group to assist the IASB with matters relating to Shariah law.

The idea behind separating the research function from the standard setting one is to limit to the scope and sharpen the focus of the standards-level projects.

For more information ...

This newsletter has been prepared for the clients and friends of PricewaterhouseCoopers by National Accounting Consulting Services. For further information on any of the matters discussed, please feel free to contact any member of ACS, or your PwC engagement leader. This newsletter is available from the PwC Canada web site, which is located at www.pwc.com/ca.

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