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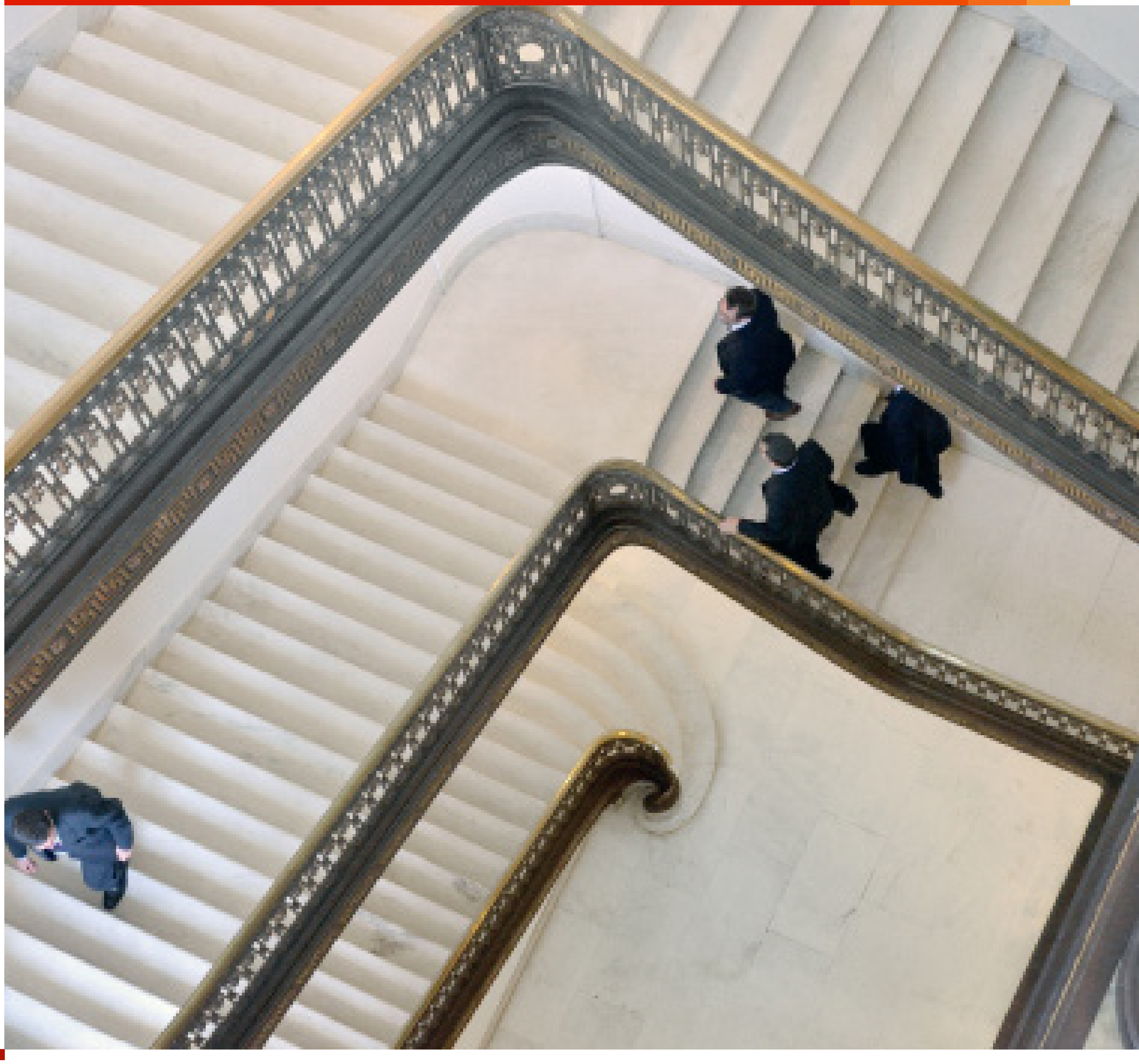
Keeping your head above water

Recent issues in financial reporting



Financial Reporting Release

September 2018

In this issue

The last decade or more may have been dominated by Canada's conversion to IFRS, efforts to improve accounting standards in the wake of financial scandals, and an ill-fated attempt at global GAAP harmonization, but these are rapidly becoming fading memories of a distant era. The main themes controlling the conversation now are about improving the quality of financial reporting more generally, including the 80% of it that lies outside the financial statements, whether the information needs of investors are being properly balanced against the cost to public companies, and the emergence of non-financial reporting issues, such as climate change. In this edition of the *Financial Reporting Release*, you'll see these themes popping up again and again, in topics such as the latest efforts to improve the quality of non-GAAP reporting, the possibility of the US, and thus Canada, giving up quarterly reporting in favour of semi-annual reporting, climate change-related risks and opportunities reporting, and the Canadian Securities Administrators' plans for reducing the regulatory reporting burden.

Of course, GAAP issues, as usual, are demanding their share of the conversation. In this *Release*, we discuss why implementing the new revenue and financial instruments standards isn't really over yet, even though your transition is, counter-intuitive as that might sound, and how companies are faring in their implementation of the new leasing standard. You'll also find out about how IFRS is coping with more recent developments – cryptocurrency and the cannabis reporting issues. Not well, say some. We've also got a few words about the IASB's newly revised Conceptual Framework – strange as it may seem, you may have some work to do as a result of its release. Then there's the IASB's latest initiative to scale heights never before scaled to establish a set of principles for distinguishing liabilities from equities untarnished by arbitrary overrides and exceptions. Those of you having issued cumulative preferred shares might want to pay particular attention. Be warned. You may not like what you read.

As financial reporting is evolving, so too is auditor reporting. Canadian auditing authorities have been trying for some years to import the new international audit opinion for Canadian use, which would require auditors to disclose the key matters arising during the audit. Now Canadian SEC registrants are facing a different alternative altogether. We explain why.

And there you have it. Could you ask for anything more? Wait. Don't answer that question.

Non-GAAP Reporting

"I have an existential map. It has 'You are here' written all over it."
– Steven Wright

Non-GAAP reporting, widely viewed as being both the curse and the blessing of corporate reporting, has been hitting the headlines in the financial press again. Consider:

- The IASB is deliberating whether to require companies to include their key non-GAAP earnings measures (e.g., EBITDA, or, everyone's favourite, "adjusted EBITDA", etc.) in IFRS financial statements, as well present four or five standard earnings subtotals on the income statement, including those that come close to operating profit and EBIT. The purpose, says Hans Hoogervorst, the IASB's Chair, is to promote greater comparability among companies, and more discipline in the use of non-GAAP measures by providing more anchors for companies to reconcile to. You should know that Hoogervorst hates non-GAAP earnings reporting and would quite happily see it dead. This is the next best thing. (Keep your friends close and your enemies closer!)

- The Canadian Accounting Standards Board (AcSB) have proposed and the Financial Reporting Lab of the UK's Financial Reporting Council have issued separate non-authoritative frameworks for developing, overseeing and reporting non-GAAP measures. These frameworks apply not only to earnings measures but also to any performance-related information that companies disclose that's not part of the financial statements, such sales per square foot, same store sales, etc. Among other things, the frameworks emphasize that measures should meet investor needs, link to business strategies and internal management reporting, and be subject to audit committee oversight and capable of independent verification.

- The Center for Audit Quality in the US has issued a paper outlining key considerations for audit committees overseeing non-GAAP reporting, including best practices.

- The Canadian Auditing and Assurance Standards Board has begun holding roundtables seeking input on the auditability of the proposed Canadian framework.

Securities regulators have been busy too:

- Canadian Securities Administrators (CSA) are updating their existing staff guidance on non-GAAP measures and converting it into a mandatory rule. Why a rule? It gives them greater power to enforce the requirements. Canada isn't seeing nearly the improvement in non-GAAP reporting that the US did after the SEC launched its campaign to clean it up a few years ago.

- The Chief Accountant of the SEC has been emphasizing in speeches the need for companies to have appropriate disclosure controls, including governance practices, to prevent mischief with numbers, not only inside the financial statements, but outside as well.

Get the feeling that somebody's trying to tell you something?

PwC observation. These initiatives stem mainly from increasing concern over the proliferation of customized metrics that too often seem to be designed to put companies' best foot forward rather than highlighting the ups and downs of actual performance. Of the initiatives, Canadian public companies will be most directly impacted by the CSA rule, but it will be a while yet before it's finalized (look for the CSA to issue a proposed rule for comment soon). The Canadian and UK frameworks for non-GAAP reporting are another matter altogether. Their recommendations aren't new by any means, but they provide a useful basis that companies and audit committees may wish to consider in assessing the quality of their reporting. The Chair of the AcSB also hopes that the framework will act as a catalyst for starting a broader conversation about improving non-GAAP reporting and developing more standardized practices within industries. The IASB's project raises a broader issue. By considering the possibility of importing non-GAAP measures into GAAP financial statements (as counter-intuitive as that might sound), the Board is raising a fundamental, almost existential, question about what the purpose of GAAP financial statements is, and what the criteria should be for deciding what information appears in them and what doesn't. The line's already very blurry. This might rub it out altogether.

Semi-Annual Reporting

Marty McFly: "I dreamt that I went…back in time."
Lorraine Baines: "Well, you're safe and sound now, back in good old 1955."
Marty McFly: "1955?"
– Back to the Future

Donald Trump casually dropped a bombshell on a fine August morning, as he is wont to do, by tweeting that he had asked the Chair of the SEC to consider permitting semi-annual instead of quarterly reporting. A day or so later, the Chair issued a statement (no tweets for him!) explaining that the Commission was already considering the frequency of reporting as part of a broader initiative to encourage long-term capital formation by public companies. Semi-annual reporting is now permitted in Europe, the UK (after a brief fling with quarterly reporting), Japan, and Australia, so North America is very much the outlier.

The CSA raised the possibility of permitting semi-annual reporting last year, as part of a proposed initiative on reducing the burden of regulatory reporting. The CSA decided not to pursue it further earlier this year for a number of reasons, including that a majority of constituents responding to the CSA's proposals either opposed the idea altogether, or were in favour of permitting it in only narrow circumstances.

PwC observation. The SEC required semi-annual reporting starting in 1955 (before then it was only annual reporting), but shifted to quarterly reporting in 1977. Recognizing that markets and regulatory regimes are entirely different today, it nevertheless might be instructive to go back in time to understand what originally convinced the Commission to shift. We supported the retention of quarterly reporting in Canada in our response to the CSA's initiative, but recognize that it would likely be impossible to continue requiring it here if the US were to give it up.

Revenue and Financial Instruments Disclosures

"I can whistle with my fingers, especially if I have a whistle."
– Mitch Hedberg

You didn't think implementing the revenue and financial instruments standards was over, did you? Not by a long shot.

Sure you've done transition, but remember, the extensive new annual disclosures these standards require are almost upon you. Companies generally have delayed thinking about these, on the basis that they had more than enough on their plate dealing with transition, thank you very much. Now the chickens are coming home to roost. As they always do.

How significant might these disclosures be? Significant. Consider what's happening in the US with revenue, for example. Public companies there have to include the annual disclosures of new standards in interim financial statements in the year they adopt the standards. Surveys of larger US companies' disclosures this year reveal that on average they tripled because of the new standard.

PwC observation. The disclosures shed more light on a company's financial performance and financial condition and thus will be a key area of focus for investors and regulators. Certainly, they'll be a key feature of CSA continuous disclosure reviews. In developing their disclosures, companies should be paying particular attention to estimates that materially depend upon assumptions about the future (e.g., expected credit losses for loans). Providing both qualitative and quantitative information may be necessary to meet the requirements. The CSA has already blown the whistle, rather loudly, warning that disclosures about uncertain estimates often have been rotten in the past (too much boilerplate and not enough specifics) so assuming that what you've done in the past will be good enough now may not be a winning strategy.

The New Disclosures

Revenue

- Disaggregating revenues according to how they're affected by economic factors, including their relationship to segment revenues (also required for interims)
- Changes in contract balances
- Performance obligations, including practical expedients and the effects of variable consideration
- Allocation of transaction prices to unsatisfied obligations, including judgments and estimates on variable consideration

Financial instruments

- **Classification, reclassifications and measurements**
  – Equity investments classified as FVOCI
  – Financial liabilities classified as FVTPL
  – Reclassifications
- **Impairment**
  – Qualitative and quantitative information about credit risk management practices, including internal credit rating information
  – Expected credit loss inputs, assumptions and estimation techniques
  – Reconciliation of expected credit loss balances
  – Modifications
  – Collateral
  – Written off assets
  – Credit risk exposures
- **Hedging**
  – Risk management strategies
  – Amount, timing and uncertainty of hedging cash flows
  – Effect of hedges and hedged items on performance
  – Hedging ineffectiveness and gains and losses
  – OCI reconciliations
  – Credit risk exposures designated as FVTPL

Leases

***"Never travel faster than the speed of a camel."* – Ibn Battuta**

The new leasing standard was the IASB and FASB's parting gift before they decided to break up and go their own separate ways again. And what a gift it was, considering estimates are that $3 trillion US of operating leases are expected to come onto lessee's balance sheets on January 1, 2019 as depreciable assets and interest bearing liabilities. Some companies will be adding billions. And billions.

Issues arising from implementation echo those experienced this time last year when companies were preparing for revenue and financial instruments, with companies often underestimating the time, resources and system requirements necessary for compliance. Particular issues giving rise to transition challenges include having to review leases to identify key terms and service contracts to see if they include embedded leases and developing and integrating new systems, processes and internal controls.

Surveys suggest that almost everyone will be transitioning to the standard using the so-called modified retrospective method (MRM) (over 94% of participants in one recent US survey indicated that they would be using this method). Under the simplest version of it, you recognize leases on the balance sheet only at the beginning of 2019, and measure the asset and liability for a lease by discounting its remaining minimum payments by a current interest rate, in effect stating the asset and the liability at a current value. Beware. While this approach is less onerous than restating comparative financial statements as if the standard had always applied, there's a price to pay. This includes:

- Losing comparability in lease accounting between 2018 and 2019.
- Having to report lease liabilities as bearing interest at current rather than historical rates. This often will exacerbate the frontend loading of leasing expenses in the future if the current interest rate assigned to a lease is higher than its historical rate.
- Having to absorb higher depreciation expenses in the future because the value of lease assets at transition almost always will be higher. Under IFRS you can eliminate the higher asset value for any or all leases by calculating what the asset value at transition would be had you restated using a simplifying assumption about interest rates, but this will be a lot more work.
- Transition disclosures will, of course, increase.

Among the differences between IFRS and US GAAP on leases is that under the former you have to charge depreciation and interest expense on operating leases to the income statement. Under US GAAP you continue to present rent expense as if operating leases were still off balance sheet (why they allow this is a long story). The Boards have tended to dismiss this difference on the basis that it usually won't significantly impact net earnings. On the other hand, it will materially affect cash flow from operating activities and EBITDA. Some IFRS companies are now considering whether to adjust their EBITDA and cash flow KPI reporting as a result (e.g., deducting rent expense in calculating adjusted EBITDA to align with the US).

PwC observation. Despite textbooks on change management and integration that say that slow and deliberate is always the best, implementation of the leases standard appears to be following the same trajectory we saw for revenue and financial instruments – delayed take off followed by a scramble at the end. Companies and audit committees should now be charting their progress to completion, and if interim solutions are necessary, taking care that appropriate internal controls are in place to avoid material restatements. Also, it's time to consider how best to address the financial reporting consequences of the new standard, including the impact of applying the MRM.

Accounting for Cryptocurrencies

"A nickel ain't worth a dime anymore."
– Yogi Berra

A few years ago, the Chair of the IASB dismissed out of hand the possibility of the IASB providing specific guidance on bitcoin and other cryptocurrencies. Besides, he said, surely holdings of cryptocurrencies should be measured at fair value with changes in fair value recognized in earnings as they arise (FVTPL). Would that this were so. What basis of accounting to use for cryptocurrencies under IFRS has become the subject of significant debate as their number and popularity grows.

The debate is whether cryptocurrencies are intangible assets or inventory and thus generally should be measured on a cost basis. While in some cases, these standards permit fair value measurement, you never quite get to FVTPL. For example, under the intangible asset model you could elect to measure a cryptocurrency at fair value if it's actively traded, but cumulative gains are reported in other comprehensive income rather than earnings. The closest you can come to FVTPL is that broker traders can value cryptocurrency inventory at fair value less cost to sell. Note that even if measuring a cryptocurrency at fair value is appropriate, there can be significant challenges to estimating it.

Recently, the IASB decided not to address the accounting for cryptocurrencies. However, some members were concerned about a diversity in practice developing that's not based on the words in IFRS. The Board therefore asked the IFRS Interpretations Committee, Robin to the IASB's Batman, to provide further information about how an entity might walk through IFRS in deciding the appropriate accounting for holdings of cryptocurrencies. The exact parameters of this project haven't been decided yet, but whatever they might be, it will take time.

PwC observation. Our view is that the intangible asset/inventory model generally would apply in accounting for cryptocurrencies under IFRS. Implicit in this view is a rejection of the proposition that cryptocurrencies necessarily represent cash or another financial asset for which FVTPL would be appropriate. Indeed, as of the time of writing we haven't seen a single cryptocurrency that could be considered to cash or a currency under IFRS or that otherwise meets the definition of a financial asset. Nevertheless, the facts and circumstances of every case need to be carefully considered. The range of possible results for classifications as well as their associated measurement indicate the importance of understanding the nature and characteristics of the cryptocurrency as well as the entity's business model/purpose for holding the asset. This underlines the need for implementing specific accounting policies and ensuring their consistent application to similar transactions. As a company might hold different portfolios for different purposes, different treatments might apply within an entity.

Cannabis Accounting

"In the book of Life, the answers aren't in the back."
– Charlie Brown, Peanuts

If measuring cryptocurrencies on a cost basis instead of fair value is perplexing to some (see the previous page), even more perplexing to others is the thought companies measuring cannabis at fair value (less cost to sell) as it's growing, rather than cost. Some have gone so far to describe this accounting as "hallucinatory". Unlike cryptocurrencies, there's no arguing the propriety of this accounting. It's just that nobody likes it – even most producers think its wacky and obscures rather than illuminates results. A particular concern is that producers are reporting profits as they build up their inventory instead of when they sell it, and in some cases, reporting gross margins that are higher than their sales, which is quite a feat indeed.

More technical issues relating to the use of fair value include:

- How best to measure fair value, especially if cannabis is being grown for different markets, or to be converted into different products? (Valuation experts may be necessary in some circumstances to answer this question properly.)
- Whether to capitalize expenditures incurred to grow plants, and present changes in fair value net of these expenditures, or expense growing expenditures as incurred, with the change in fair value being presented gross, excluding expenditures?
- If capitalizing expenditures is appropriate, exactly what costs are eligible for capitalization?
- How to present changes in the fair value of plants in the income statements (e.g., whether they should be treated as an adjustment of cost of sales and thus affect gross profit)?

Canada's IFRS Discussion Group has discussed these issues and generally concluded that because views can reasonably vary on these issues, companies should develop accounting policies and estimates most appropriate to their circumstances and provide transparent disclosure about their effects, assumptions, and sensitivities. The Group has referred these issues to the AcSB, which is considering whether to direct them on to the IASB or the IFRS Interpretations Committee.

It's also possible that the CSA will weigh in with their views too – you can be sure that they are closely monitoring practice.

PwC observation. The pressure's on audit committees to make sure that the accounting and disclosures for their companies is appropriate and useful to investors.

The Conceptual Framework

"You can't teach an old dogma new tricks."
– Dorothy Parker

The IASB issued a revised Conceptual Framework a few months ago. What changes does it introduce? Can it affect your accounting? The answer to the first question is, nothing major. The answer to the second is, well…

In the revised Framework, the basic concepts of assets and liabilities, equity, revenue, expenses, profit and loss, other comprehensive income, and using a mixed measurement model all survive intact. What has changed is some stuff around the edges, mainly to incorporate new perspectives the Board applied when overhauling its standards over the last decade or so. Most importantly, the revised Framework updates, clarifies and broadens the definitions of assets and liabilities, affirms that uncertainty affects the way you measure assets and liability rather than their recognition, confirms that profit and loss is the primary measure of financial performance, and acknowledges that putting revenues and expenses and gains and losses in OCI is a last resort that applies only when common sense trumps conceptual purity. There are other, even narrower, changes but these won't interest anyone that actually has a life.

Could the revisions to the Framework affect your financial statements? In theory at least, yes. In rare circumstances, a company might have relied on the Framework to develop an accounting policy because no standard provided relevant guidance. If so, the company has to consider whether any revisions to the Framework affect that policy and change it as necessary. The revised Framework is effective immediately upon its publication, so if you're in this situation, get hopping. There's another way your statements could be affected. Certain IFRS standards include references to the Conceptual Framework, which means that companies may have had to consider the Framework in applying those standards. The IASB updated most of these references so that they now refer to the revised Framework and so you've now got to consider whether any of the revisions could affect your application of these standards. The updates are effective for years beginning on or after January 1, 2020, with earlier application permitted.

PwC observation. We expect the revised Framework and updates will have a very limited impact on financial statements. Nevertheless, you've got to look!

Distinguishing Liabilities from Equity

"You know, what Mr. Einstein said is not so stupid."
– Wolfgang Pauli

Depend on it. Every generation of standard setters will take on the challenge of establishing a comprehensive, principle-based model for distinguishing financial instruments as equity or liabilities. It's the Mount Everest of standard setting. That the trail is littered with the frozen bodies of standard setters that died in the attempt is never a deterrent. "This time," they say, "things will be different".

The IASB's latest quest began in earnest this summer, with the issue of a Discussion Memorandum on a proposed new classification model. It's a hybrid of sorts, carrying forward existing principles in IFRS intact, but adding another. What types of instruments would change their classification if the proposal goes through? Most significantly:

- Non-redeemable cumulative preferred shares, which would be liabilities, not equity.
- Some types of equity-linked derivatives, which would be equity, not liabilities. This might affect the bifurcation of certain types of convertible debt and other compound instruments into components.

Here's the model:

- If a financial instrument isn't a liability, it's equity.
- An instrument is a liability if it establishes an obligation to deliver cash or another financial asset before liquidation, or, and this is the new bit,
- The issuer promises the holder an amount that's independent of a common share's entitlement. (This is a very rough translation from the original geek, but valid enough to give you the drift.)

The Board intends to preserve existing exemptions that permit treating certain puttable instruments and members' shares in co-operatives as equity.

Other proposals in the Paper:

- Recognizing the changes in the value of a liability in OCI rather than profit and loss when the holder's return is entirely equity driven (e.g., a fixed number of common shares mandatorily redeemable for cash for their market price).
- Requiring companies to allocate comprehensive income earned to the various classes of equity instruments, even if the effect is anti-dilutive.
- Expanding disclosures and presentation requirements for liabilities and equities.

PwC observation. One of the Board's objectives in the project was to change existing IFRS as little as possible. The reason for this is that the existing requirements are working well overall; it's only the stuff at the fringes that needs attention, though some might argue that the classification of cumulative preferred shares isn't a fringe issue. It'll take some time to come to grips with the proposals and their implications, but the Discussion Memorandum does raise interesting ideas and propose solutions that deserve careful attention and consideration.

CSA Continuous Disclosure Review Program

"Reality continues to ruin my life."
– Calvin and Hobbes

The CSA has issued its biennial report on the results of its reviews of public companies' financial reporting. Common deficiencies are listed in the table. The report also provides examples of both poor disclosure and good disclosure in specified areas, and so provides helpful guidance for companies looking to improve their reporting.

How did companies fare in the reviews? About 26% of issuers (2017 – 19%) were obliged to refile reports, or, worse, were referred to enforcement, cease traded or placed on the default list. Another 25% (2017 – 24%) had to make corrections prospectively.

PwC observation. The CSA review program is valuable, but the fact that the same deficiencies appear year after year and that more than 25% of review outcomes resulted in restatements or worse is discouraging.

Common Reporting Deficiencies

Financial statements

- Statement of cash flows
- Fair value measurements
- Accounting policy disclosures
- Business combinations
- Revenue recognition
- Related party transactions
- Significant judgments and estimates

MD&A

- Non-GAAP measures (see earlier discussion)
- Discussion of operations
- Disaggregation of investment operations
- Concentrated investments reporting
- Related party transactions
- Forward looking information

Other

- Mining technical reports
- Gender diversity disclosure
- Executive compensation – missing filing deadlines
- Climate change reporting (see discussion later)
- Inappropriate social media posts
- Filing of material contracts
- News releases or material change notices with unbalanced or insufficient disclosures

CSA Project to Reduce the Regulatory Reporting Burden

"The first rule about low hanging fruit is to always watch out for low hanging branches."
– Stephen Richards

Last year the CSA invited constituents' views on what can be done to reduce the regulatory reporting burden by Canadian public companies while still protecting investors' interests. Earlier this year the CSA announced how they are going to proceed. Their plans are to:

- Remove or modify the requirements for filing business acquisition reports.
- Facilitate at-the-market offerings.
- Revisit the primary business requirements to provide greater clarity to issuers preparing an IPO prospectus.
- Consider a more concise and focused short form prospectus model.
- Reduce or streamline certain continuous disclosure requirements, such as eliminating duplicative disclosures in the financial statements, MD&A, and other forms, consolidating reporting into a single document, and reducing the volume of information in interim and annual reports.
- Enhance electronic document distribution for investors.

PwC observation. The CSA invitation to comment identified a great many more options, including permitting semi-annual reporting, which we discussed earlier. Only six were selected to go forward because the CSA were looking for projects that had the broad support of constituents, could be expected to be completed within a reasonable time frame, and that could be achieved within the existing regulatory framework. While some might regret the CSA giving up the opportunity for slashing regulatory requirements more deeply, we think this is an appropriate course of action. Start with the low hanging fruit, if you will, and see what comes next. Of course, there can be significant obstacles to gathering even low hanging fruit.

Climate Change Reporting

"Today was ninety degrees in the sun. I was clever. I stayed in the shade."
– Tommy Cooper

In 2017, when climate change reporting by public companies was becoming a major issue at shareholders' meetings, the CSA announced that it was initiating a comprehensive project to consider whether new Canadian securities requirements in this area were necessary. The project included consulting with companies and investors, reviewing the quality of existing Canadian reporting and surveying other countries' practices and disclosures requirements.

Earlier this year the CSA announced its decision that specific new requirements aren't warranted at this time. Instead, their plan is to:

- Focus on educating Canadian reporting issuers on the disclosure of climate change-related risks, opportunities and financial impacts. We expect this education will often take the form of comment letters arising from continuous disclosure reviews. A major goal, we suspect, will be getting companies to replace boilerplate with more entity specific information;
- Consider developing new disclosure requirements in respect of governance processes relating to material risks and opportunities, and how companies oversee the identification, assessment and management of risks;
- Monitor the ongoing development of climate change-related disclosure practices, and evaluate whether disclosure will continue to evolve and improve; and
- Assess developments in voluntary reporting frameworks, evolving disclosure practices and users' need for additional types of climate change-related disclosures, including whether disclosure of certain categories of greenhouse gas emissions are warranted in the future.

PwC observation. The CSA decided that existing general requirements for disclosing material risks already provides a sufficient basis for climate change reporting, even though they acknowledged that there's fundamental disagreement between companies and investors as to when climate change risks are material and thus should be disclosed. They also dismissed a proposal to require companies to explicitly disclose that climate related risks and opportunities aren't material if they don't provide any disclosures on the subject. We encourage companies that have significant climate change-related issues to consider adopting one of the voluntary climate change reporting frameworks if they haven't already done so.

Auditor Opinions

"We plan. The Gods laugh."
– Ancient proverb

Changes are coming to the normally staid world of auditor reporting. Not without controversy and unexpected twists and turns, mind you.

Recall that starting with audit opinions on financial statements for years ending on or after December 15, 2018, the standard Canadian audit opinion will include much more detail about the auditor's responsibilities and independence, going concern matters, etc., and identify the name of the partner in charge of the audit. You'll still see the usual "presents fairly in accordance with…" opinion, except that it'll come first, not last, in the opinion followed by the expanded discussion. The report will also make explicit the auditor's responsibility for reviewing and reporting on "other information", such as the company's MD&A and the company's glossy annual report.

These changes are just preliminaries to the main event, of course. What everyone's really waiting for is when the auditor has to include in its opinion a discussion of key audit matters (KAMs) that arose during the engagement and discuss their resolution. We had expected that the Canadian Auditing Standards Board (AASB) would have approved a final standard requiring KAM reporting for the 2020 audits of all TSX-listed companies by now, but the Board has announced that it's still considering issues relating to what the scope of KAM reporting should be, with a specific focus on TSX-listed investment funds.

Introducing these changes will align Canadian auditor reporting with international auditing standards, but not with those in the US, which differ in certain major respects. For example, the US doesn't have KAMs, it has "critical audit matters" (CAMs). CAMs are somewhat narrower in scope, primarily to avoid duplicating US auditor reporting requirements for reporting deficiencies in internal controls. (CAM reporting is effective in the US for large accelerated filers for years ending on or after June 30, 2019 and years ending on or after December 15, 2020 for other SEC registrants.) Other differences include that in the US the name of the partner responsible for the audit is published separately rather than in the opinion itself, and there are no reporting requirements relating to "other information". Cumulatively, the differences are so significant that most Canadian auditors are giving up the common practice of providing a combined audit opinion for Canadian SEC registrants that meets both countries' requirements. Instead, auditors now will plan on issuing a US-style audit opinion. (In situations where regulators require a Canadian opinion, which may be the case for banks and insurance companies, it may be necessary to issue two separate opinions.)

PwC observation. While some will be sorry indeed that the unexpected consequence of introducing new Canadian auditor opinion requirements is to cause auditors of most Canadian SEC registrants to drop their Canadian reporting altogether, the alternative of presenting a combined Canadian/US opinion isn't feasible absent accommodations that permit combined reporting. Turning to the question of which Canadian public companies should subject to KAM reporting, we've never agreed with the AASB's initial tentative decision to apply the standard to all listed companies. In our view, the Board also should be considering factors such as the size of a company, the nature of its activities and the expected benefits to be derived from this reporting. We are happy to see the Board focusing on the application of KAMs to investment funds, but the Board needs to go further.

For more information

This newsletter has been prepared for the clients and friends of PwC 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/financialreportingrelease.

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Complex Mergers and Acquisitions

- Carve-out financial statements
- Pro-forma financial information
- Accounting function integration

IPOs and Capital Market Transactions

- Readiness assessments for public reporting
- Advice on regulatory and exchange requirements
- Assistance with financial statements, prospectus and other documents
- Assistance with due diligence process
- Advice on alternatives

Regulatory Issues and Restatements

- Assistance with offering documents
- Support in responding to regulatory comments and requests
- Advice on alternatives

GAAP / IFRS Interpretation and Conversions

- Diagnostic summary of key impacts on transition
- Evaluation and development of accounting policies
- Training development
- Support in analyzing and documenting technical accounting issues

Accounting Standard Adoption

- Adoption of new standards under IFRS, U.S. GAAP and Canadian GAAP for Private Enterprises
- Diagnostic summary of key impacts on adoption
- Evaluation and development of accounting policies
- Training development and implementation
- Support in analyzing and documenting technical accounting issues

Other Services and Products

- On-site assistance / expert secondment
- Quantitative analysis and model development
- Tax Accounting Services
- Comperio
- Automated Disclosure Checklists
- PwC IFRS Manual of Accounting

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