

International Financial Reporting Standards

Defining and Identifying a Cash Generating Unit

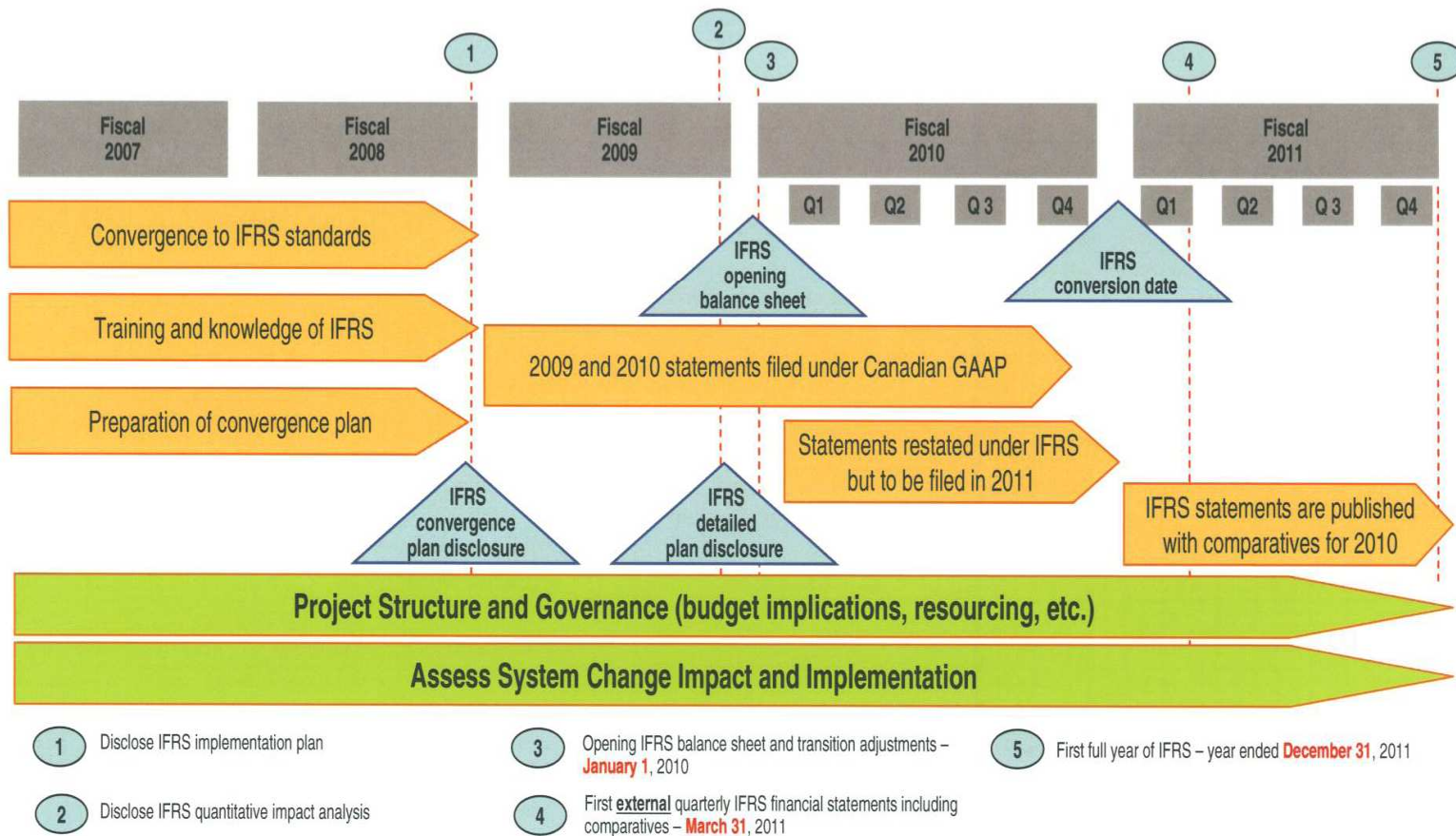
Agenda

- Discussion of the definition of a CGU
- How to identify a CGU
- Examination of the various IFRS requirements for CGU's

Proposed Conversion Timeline

First-time adoption of IFRS

According to the AcSB's provisional timetable, IFRS adoption will be mandatory for all companies that are Canadian reporting issuers for fiscal periods starting on or after January 1, 2011. For each Canadian reporting issuer ("registrant") with a December 31 year end, the requirement to produce comparative financial statements means the balance sheet as at January 1, 2010 will be the first date of transition to IFRS (see timetable below).



Definition of a Cash Generating Unit

Definition of a Cash Generating Unit

- The smallest identifiable group of assets which can generate cash inflows independently from other assets or groups of assets. (IASB)
- **Also note:**
- A portfolio of similar assets that are subject to the same economic and commercial influences. (SAICA)
- Cash-generating units are assets held with the primary objective of generating a commercial return. (AASB)

Considerations

- **Smallest identifiable GROUP of assets:**
- Suppose the assets that comprise the cash generating unit have unequal lives.

- **Generate cash INFLOWS**
- Cash generating unit incurring losses

Considerations

- **Independently from other assets or groups of assets**
- Largely Independent Cash Flows - consider whether a well or battery would have cash inflows independent of other assets
- The ability to sell an asset on a stand-alone basis may be indicative of an independent cash flow
- Consider the degree of shared infrastructure required to obtain inflows
- Independent versus interdependent cash flows – requires judgment
- An asset with independent cash flows inflows but that shares cash outflows with another asset would still be considered a CGU

Practical Considerations when identifying a Cash Generating Unit

Where do we start?



*"Rumor has it that some of you
have a life! I'm determined to
change that!!!"*

Considerations

- Should be consistent with how you **organize** your business
 - For example, consider whether CGU's will be based on type of product versus quality of oil versus type of area
- Should be **meaningful** to how investors assess financial results
- Discuss with individuals in **operations**, integration of business unit leaders
- Assessment of specific assets such as **shared facilities**
- CGUs need to be **consistently** defined period to period
- Allocate Corporate Assets to CGU's on the basis of **relative weighted** carrying amounts

Examples

- A mining entity owns a private railway to support its mining activities. The railway is used to transport the ore mined and does not generate revenue the way passenger trains do. The private railway could be sold only for scrap value and it does not generate cash inflows that are largely independent of the cash inflows from the other assets of the mine.
- A bus company provides services under contract with a municipality that requires minimum service on each of five separate routes. Assets devoted to each route and the cash flows from each route can be identified separately. One of the routes operates at a significant loss.
- An oil and gas company has a SAGD operation, with a Bitumen Processing plant (which can process 3rd party product). Additionally it generates significant quantities of electricity it sells back to the Grid.

IFRS requirements for Cash Generating Units

Reporting Considerations

Reporting consideration for Cash Generating Units:

- IFRS prescribes very few disclosure requirements regarding CGU identification
- If changes are made to an entity's identification or aggregation of CGUs, disclosure of the current and former methodologies and the reason for the change is required
- There are additional disclosure requirements regarding impairment losses and impairment reversals

Reporting Considerations-Examples

http://shareholders.maersk.com/uk/FinancialReports/2008/AnnualReport/uk_05_07.html

<http://www.petrotrin.com/Petrotrin2007/AnnualRep2007/FinancialStatement2007/CriticalAccountingEst.pdf>

www.nesteoil.com/binary.asp?GUID=CED2338D-1012-4A04-AF44

Reporting Considerations

Differing levels of IFRS compliance noted amongst JSE-listed companies

Despite stringent requirements placed on auditors of JSE-listed companies, financial statements still reveal different levels of IFRS disclosures.

Following the global accounting transition to International Financial Reporting Standards (IFRS), all JSE listed companies are required to report under IFRS, a set of international accounting standards issued by the International Accounting Standards Board stating how particular types of transactions and other events should be reported in financial statements. The primary goal of IFRS is to make international comparisons between companies as easy as possible, as well as for regulators, investors and other users of financial statements to be able to compare like with like and to ensure that firms make the same levels of disclosures and employ the same methodologies in reflecting their financial results.

In order to achieve consistent levels of IFRS compliance, the JSE has imposed stringent compliance regulations on audit firms wishing to be placed on the JSE services register. Theoretically speaking, the JSE's regulations mean that all listed companies are now assured of a minimum level of expertise from their auditors. **However, the IFRS framework is so vast that interpretations often differ amongst audit firms and discrepancies in levels of IFRS compliance can, and do, occur**, says Andrew Naudé, director of Moore Stephens Corporate Finance in South Africa. Aug 2009

Our Experiences

- Conversion efforts that begin early and involve continuing personnel, reduce the expenses of involving others and produce benefits which may persist after the conversion date;
- Impairments issues are likely to be accelerated under IFRS, determining their consequences early is more prudent; hence CGU identification is critical
- The more decentralized the reporting function, the greater the degree of difficulty ensuring compliance;
- Gathering data and preparing new spreadsheets or changing G/L programs can be time consuming;
- Drafting financial statement disclosures may be time intensive
- Increased lead times for resources outside of the control of the financial reporting function
- Consider such matters as the MD&A, non GAAP measures, debt agreements, compensation and stock option plans

Lessons Learned – International Clients

- Consideration must be given early to information technology, and data accessibility, availability and integrity.
- Impact of IFRS is pervasive across the organization – ‘push down and across’ to both other and lower levels to assist with planning, integration and support (need executive support)
- Implementation is a multi-disciplinary process (e.g. project management, fit gap analysis, application changes, business impact analysis, change management, etc.). Structure your team appropriately.
- Fully embed IFRS into organization processes (e.g. performance management reporting, budgeting/forecasting, executive compensation) – creating manual work-arounds and ‘spreadsheet accounting’ serves to limit the potential of an adequately planned IFRS convergence initiative and creates inefficiencies (Topside Approach)
- Invest in a project management infrastructure – identify and communicate project leads and sponsors, be specific in defining team roles, prepare detailed project and training plans, communicate strategies frequently and to relevant others (staff, management, BOD, investors)

Lessons Learned – International Clients

- Challenges to communication of financial reporting requirements needs to be anticipated (i.e. media relations, investor relations, performance reporting, etc.)
- Communication of the changes throughout the organization needs to be organized and consistent with executive level commitment
- Tailor training to the specific requirements of your company
- The devil is in the details (remember issues may be industry-specific). You need to allocate potentially significant time to determining and documenting your IFRS policy decisions.
- Don't underestimate the time required (Remember Sox)
- IFRS is new for all stakeholders (senior executives, directors, investors, lenders, regulators and others). Interact with them and help them understand and support the changes.

You can start by looking at the changes made in financial reporting of comparable companies in other countries

Next Steps

- If you haven't done so already, get your diagnostic completed now...this will dictate the extent and nature of work required for your specific situation.
- Based on the results of the diagnostic, evaluate your project team for appropriateness based on the nature, complexity and extent of work required to be completed.
- You need to be able to start collecting IFRS data in 2010 to build the 2010 comparable financial statements (including an opening IFRS balance sheet for Jan 01, 2010)...work backwards to determine timing of project steps and resources required.
- Allocate sufficient time/resources to making your policy decisions and developing the corresponding documentation to support them...this will be a time consuming exercise.
- If internal resource(s) can not be dedicated to the project, considering co-sourcing or outsourcing as a viable alternative (remember the skill sets required to execute this project effectively).

Questions

For more information, please feel free to contact:

Shawn Hendry CISA CIA
Director
shendry@sunera.com
403 455-5050

Matt Kinver ACCA CertIFR
Manager
mkinver@sunera.com
403 605-4077