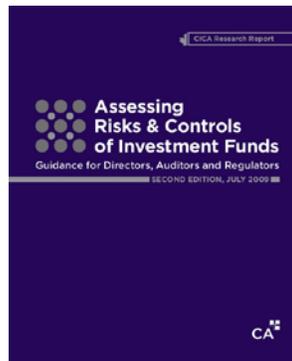




Canadian Institute of Chartered Accountants
INVESTMENT FUNDS UPDATE

Bulletin 2

March 2010



Prepared by the CICA Investment Funds Standing Committee, this Bulletin updates the guidance in the July 2009 CICA research reports, *Financial Reporting by Investment Funds – Second Edition* and *Assessing Risks & Controls of Investment Funds – Second Edition* which are available on the [CICA website](#).

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INVESTMENT FUNDS STANDING COMMITTEE (IFSC)

In April 2009, the Canadian Institute of Chartered Accountants (CICA) established an [Investment Funds Standing Committee](#) (IFSC). The IFSC's objective is to consider and provide timely guidance on risk management, governance and financial reporting matters that are pertinent to investment funds in Canada.

At its first meeting on October 30, 2009, the IFSC decided that updating the guidance on risk management and governance matters was not required at this time. It also decided to provide the investment funds industry with an update on the following matters: proposed amendments to NI 81-106 *Investment Fund Continuous Disclosure*; investor equity; consolidation; financial instruments; and income taxes. The [Investment Funds Update – Bulletin 1](#) was published in December 2009 and is available on the CICA website.

At its second meeting on February 25, 2010, the IFSC decided to provide the investment funds industry with an update on the following matters: proposed amendments to NI 81-106 *Investment Fund Continuous Disclosure*; OSC Staff Notice 33-733 *Report on Focused Reviews of Investment Funds, September 2008 – September 2009*; OSC Staff Notice 52-718 *IFRS Transition Disclosure Review*; transitional balance sheet in first-time IFRS financial statements; consolidation exemption for investment companies; counter party credit risk and the fair value of financial assets and financial liabilities; and, SEC approves statement on global accounting standards.

**PROPOSED AMENDMENTS TO NATIONAL INSTRUMENT 81-106
*INVESTMENT FUND CONTINUOUS DISCLOSURE***

Chapter 6 of the CICA research report *Financial Reporting by Investment Funds – Second Edition* deals with National Instrument 81-106, *Investment Fund Continuous Disclosure* (NI 81-106) and, in particular, the management report of fund performance (MRFP) described in Form 81-106F1, *Contents of Annual and Interim Management Report of Fund Performance*.

[Proposed amendments to National Instrument 81-106 *Investment Fund Continuous Disclosure*](#) and related materials were published for comment on October 16, 2009 for a 90 day comment period. The purpose of the proposed amendments is to accommodate the transition to IFRS. The comment period closed on January 14, 2010. The Canadian Securities Administrators (CSA) received 11 comment letters relating to NI 81-106 and they are publicly available and posted on the [Ontario Securities Commission's website](#) and on the websites of certain other securities regulatory authorities.

OSC STAFF NOTICE 33-733
*REPORT ON FOCUSED REVIEWS OF INVESTMENT FUNDS,
SEPTEMBER 2008 – SEPTEMBER 2009*

In January 2010, the Ontario Securities Commission (OSC) published [Staff Notice 33-733 *Report on Focused Reviews of Investment Funds, September 2008-September 2009*](#). The report summarizes the compliance reviews conducted by staff of the OSC's Compliance and Registrant Regulation Branch and Investment Funds Branch in response to concerns emerging from the market turmoil experienced by the global financial services industry.

The OSC completed a three-phase review of investment funds. The report describes the observations from the last phase, a review of Ontario-based hedge funds, and provides further reporting from the money market funds and non-conventional investment funds reviews previously reported on in OSC [Staff Notice 33-732 *Compliance Team Annual Report*](#). The primary focus of all three phases was to assess fund managers' compliance with Ontario securities laws and was not to evaluate the merits of the investment products covered by these reviews.

The report includes some suggested practices and encourages fund managers to use this report as a self-assessment tool to strengthen their compliance with Ontario securities laws and to improve their systems of internal controls and supervision. The suggested practices include: fund valuations, portfolio holdings, use of service providers, and offering document disclosure. Despite the overall market downturn and its impact on the returns of many of these products during the review period, the OSC did not observe any industry-wide compliance issues.

OSC STAFF NOTICE 52-718
IFRS TRANSITION DISCLOSURE REVIEW

[OSC Staff Notice 52-718 IFRS Transition Disclosure Review](#) was published on February 5, 2010. The report was based on a review of reporting issuers other than investment funds, performed by staff of the OSC's Corporate Finance Branch. Staff's review assessed the extent and quality of IFRS transition disclosure made by corporate issuers in light of the disclosure guidance provided in [CSA Staff Notice 52-320 Disclosure of Expected Changes in Accounting Policies Relating to Changeover to International Financial Reporting Standards](#) (SN 52-320).

SN 52-320 provides separate guidance specifically for investment funds. It states that an investment fund should discuss the changeover to IFRS for each fund or fund family in either the management report of fund performance or the notes to the financial statements. Most investment funds are now two or one year(s) before the first day of an entity's financial year for which financial statements are prepared in accordance with IFRS (the changeover date) and, in annual and interim filings, an investment fund should disclose relevant information about its changeover to IFRS, as applicable, including:

- the key elements and timing of its changeover plan;
- impact on business arrangements;
- impact, if any, on net asset value per unit;
- accounting policy and implementation decisions the fund will have to make;
- major differences the fund has identified between its current accounting policies and those it expects to apply under IFRS; and
- progress made on the fund's changeover plan.

In the year before changeover, investment funds should quantify the impact of the changeover to IFRS. Staff of the OSC Investment Funds Branch continue to review IFRS transition disclosure made by investment funds. Until their findings are communicated, investment funds may find the report useful as it provides for examples of IFRS transition disclosure made by corporate issuers.

**TRANSITIONAL BALANCE SHEET
IN FIRST-TIME IFRS FINANCIAL STATEMENTS**

IFRS 1, [*First-time Adoption of International Financial Reporting Standards*](#), requires an entity to present an opening statement of financial position at its transition date (that is, the beginning of the earliest period presented in its first IFRS financial statements). This balance sheet, generally referred to as the “transitional balance sheet,” is not explicitly required by IFRS 1 to be included in an entity’s first IFRS interim financial statements. However, in October 2009, the CSA published its proposed amendments to National Instrument 81-106, *Investment Fund Continuous Disclosure*, which included a requirement to incorporate the transitional balance sheet in first IFRS interim financial statements for investment funds. Similar requirements for non-investment fund reporting issuers have also been proposed by the CSA in its amendments to National Instrument 51-102, *Continuous Disclosure Obligations*.

The transitional balance sheet is expected to be presented as a primary financial statement in both first interim and first annual financial statements under IFRS. For example, this means that an entity’s first IFRS balance sheet will include a third column at the date of transition. If an entity’s interim financial statements are reviewed by its auditor, the auditor will be required to review the transitional balance sheet, together with the first IFRS interim financial statements. However, many entities do not have auditor reviews of interim financial statements. In these cases, the auditor will not be required to review the transitional balance sheet for the first IFRS interim financial statements, but will be required to audit the transitional balance sheet in the first IFRS annual financial statements.

CONSOLIDATION EXEMPTION FOR INVESTMENT COMPANIES

The CICA research report *Financial Reporting by Investment Funds – Second Edition* addresses consolidation matters in Chapter 3 and Appendix E. As outlined in the March 2010 edition of [*FYI – Accounting Standards*](#) issued by Canada’s Accounting Standards Board, the International Accounting Standards Board (IASB) tentatively agreed to exempt investment companies from the requirement to consolidate controlled investments.

At its February 17, 2010 meeting with the US Financial Accounting Standards Board (FASB), the IASB tentatively agreed to require these entities to measure those investments at fair value. This is a reversal of its previous position (as indicated in the December 2008 Exposure Draft ED10, “Consolidated Financial Statements” which was summarized in Appendix E of the CICA research report *Financial Reporting by Investment Funds – Second Edition*) and was made in response to concerns raised by stakeholders in Canada and several other jurisdictions, and users’ unanimous agreement that investment companies should measure all investments at fair value.

To converge with US GAAP, the IASB decided to develop the exemption based on existing US guidance in Codification Topic 946 (formerly the *AICPA Investment Company Guide*). The IASB staff has been asked to revise that guidance to exclude US-specific references, include venture capital-type organizations based on investors’ needs and provide accounting guidance for investments held by a parent in an investment company. The FASB also agreed to make corresponding amendments to Topic 946. The IASB and FASB plan to discuss the requirements for the exemption in April 2010 and subsequently re-expose a proposal for comment before a final standard is issued near the end of 2010.

COUNTER PARTY CREDIT RISK AND THE FAIR VALUE OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

The CICA research report *Financial Reporting by Investment Funds – Second Edition* addresses credit risk matters in Chapter 4. As documented in EIC-173 *Counter Party Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*, the Emerging Issues Committee reached a consensus that, effective January 2009, an entity’s own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities, including derivative instruments. In December 2009, The Investment Funds Institute of Canada’s (IFIC) Accounting Advisory Working Group provided some additional implementation guidance for investment funds. The working group considered EIC-173 in connection with *CICA Handbook – Accounting* Section 3855 and the amendments to Section 3862 when drafting its guidance. Although the adoption of EIC 173 was not expected to have a material impact on the financial statements of most investment funds, a documented review process was recommended by the IFIC guidance.

**SEC APPROVES STATEMENT ON
GLOBAL ACCOUNTING STANDARDS**

On February 24, 2010, the [US Securities and Exchange Commission](#) (SEC) issued a press release outlining its position regarding global accounting standards and confirming its belief that a single set of high-quality globally accepted accounting standards would benefit US investors.

This was a long-anticipated announcement following the issuance of the proposed “IFRS Roadmap” in November 2008 in which the SEC received over 200 comment letters from a wide variety of market participants, including those representing investors, regulators, issuers, accounting, legal and other professions, academia, standard setters and international organizations. Commenters expressed widespread support for the goal of having a single set of high-quality globally accepted accounting standards, but differed in their views about the approach in the proposed IFRS Roadmap.

Although there were no definitive conclusions regarding the possible acceptance of IFRS as a replacement of US GAAP, the following highlights were noted in the release:

- encouragement of the continued convergence of US Generally Accepted Accounting Principles and IFRS in order to narrow the differences between the two accounting frameworks;
- development of a work plan, the results of which will aid the Commission in its evaluation of the impact that the use of IFRS by US companies would have on the US securities market and will include an evaluation of the status and progress of the convergence projects between the IASB and FASB;
- by 2011, assuming completion of these convergence projects and the staff’s work plan, the Commission will decide whether to incorporate IFRS into the US financial reporting system, and if so, when and how.

The release also noted that:

- the SEC staff is expected to provide public progress reports on the work plan, as well as the status of the FASB and IASB convergence projects, beginning no later than October 2010 and frequently thereafter until the work is complete; and
- if the SEC determines in 2011 to incorporate IFRS into the US financial reporting system, the first time that US companies would report would be no earlier than 2015.

The original [IFRS Roadmap](#) proposed to scope-out the adoption of IFRS for Investment Companies (which would include most mutual funds) and broker-dealers. There was mixed reaction to this proposal from the respondents, with some commenters indicating that no issuers should be exempt from the scope of the proposed IFRS Roadmap, with others supporting the exclusion of investment companies from adopting IFRS due primarily to the fact of a lack of industry specific accounting guidance under IFRS that addresses the unique financial reporting requirements for these entities.

In light of the different views, the SEC staff is expected to analyze possible approaches for financial reporting requirements for broker-dealers and investment companies, should the SEC decide to incorporate IFRS into the financial reporting system for US issuers. Specifically, the SEC staff will:

- assess the effects of such incorporation on broker-dealers, investment companies and investors, including whether IFRS includes sufficient standards (and the extent of logistics for, and estimated time necessary to undertake any changes) should broker-dealers and investment companies be included in the scope of any potential SEC decision.
- evaluate the effect on investors of excluding broker-dealers and investment companies from the scope of any potential SEC decision.

QUICK LINKS**Access the Unaccompanied IFRS**

The IASC Foundation provides free-of-charge access to the current year's consolidated unaccompanied [International Financial Reporting Standards \(IFRS\)](#) in English as issued by the International Accounting Standards Board (IASB) and published in the Bound Volume.

IASB Foundation Constitution effective March 1, 2010

The IASC Foundation approved changes to the [Foundation's Constitution](#) in January 2010. Effective March 1, 2010, the IASC Foundation becomes the **IFRS Foundation**, the International Financial Reporting Interpretations Committee becomes the **IFRS Interpretations Committee**, and the Standards Advisory Council becomes the **IFRS Advisory Council**.

IASB - Work Plan Projected Timetable

The [International Accounting Standards Board \(IASB\) projected timetable](#) shows the current best estimate of document publication dates. The effective date of amendments and new standards is usually 6-18 months after publication date. In setting an effective date, the IASB considers all relevant factors. In appropriate circumstances, early adoption of new standards will be allowed. The work plan anticipates the completion of several projects in 2010 and 2011.

IASB - Podcast Summaries of Board Meetings

The International Accounting Standards Board (IASB) is currently testing Board meeting audio summaries (podcasts). These podcasts are recorded shortly after each Board meeting and provide a short (approximately 30 minutes) summary of the main topics and projects discussed. The [IASB meeting podcasts for December 2009 to March 2010](#) are available on the IASB website.

Handbook Restructuring

The [CICA Handbook – Accounting](#) now comprises five Parts. This restructuring implements the strategy of the Accounting Standards Board (AcSB) of adopting different sets of standards for different categories of entities. Part I applies to publicly accountable enterprises (except for pension plans) and others permitted to apply International Financial Reporting Standards (IFRS).