

Putting IFRS in motion*

The Impact of International Financial Reporting Standards
on the Canadian Pharmaceutical and Life Sciences Sector



Introduction



More than 100 countries have adopted the use of International Financial Reporting Standards (IFRS) by public companies. Canadian publicly accountable companies will be required to adopt IFRS for interim and annual financial statements for financial years beginning on or after January 1, 2011, with early adoption permitted by securities regulators on a case-by-case basis. Even private companies will need to consider whether a transition to IFRS is aligned with their long term strategic objectives.

The move to IFRS will fundamentally change the way Canadian companies in the Pharmaceutical and Life Sciences sector report their business results to analysts, investors and other stakeholders.

For some organizations, implementing IFRS may not be very complicated, but for others it will be a highly complex process that goes well beyond the finance and accounting functions. Other business operations, such as human resources, investor relations, business development and information technology (IT) departments, need to be involved in the IFRS conversion plan.

Our experience in assisting listed and private companies that have already adopted IFRS shows that for some, full conversion and adoption can take anywhere from two to five years, depending on the complexity of the organization. Are you on track?

Certain industries have a long and complex conversion process because significant accounting policy changes are required. It is often extremely difficult to extract the historical information necessary to make these changes, and the accounting processes and systems have to be modified on a go-forward basis.

One of the most significant challenges in converting from Canadian Generally Accepted Accounting Principles (GAAP) to IFRS is determining which Canadian GAAP differences will impact the organization. This publication outlines some of the accounting differences that arise between Canadian GAAP and IFRS in the Pharmaceutical and Life Sciences sector. The background and context behind the decision to adopt IFRS and the key strategic issues you will face in converting to IFRS are outlined in our publication, *Putting IFRS in motion – Keeping on track*. To obtain a copy, contact a PwC professional or visit www.pwcifrs.ca. As well, please visit www.pwc.com/ca/lifesciences to learn more about the Pharmaceuticals and Life Sciences sector.

Companies in the Pharmaceutical and Life Sciences sector that have already implemented IFRS understand that the new standards may place a sizeable responsibility on management to be able to communicate effectively to the market in the new IFRS language.

Accounting under IFRS

Canadian publicly accountable companies will be required to adopt IFRS for interim and annual financial statements for financial years beginning on or after January 1, 2011, with early adoption permitted by securities regulators on a case-by-case basis. The move to IFRS will fundamentally change the way Canadian companies report their business results to analysts, investors and other stakeholders. The implementation of IFRS for Canadian Pharmaceutical and Life Sciences companies may at first look like a complicated, expensive and difficult process. However, the size and complexity can be managed if companies plan ahead before the new accounting and reporting standards become effective.

Many Pharmaceutical and Life Sciences companies throughout Europe and Australasia have completed their transition and have been applying IFRS since January 1, 2005. The transition to IFRS for Pharmaceutical and Life Sciences companies in these countries has shown there are some interpretation and application challenges unique to the sector.

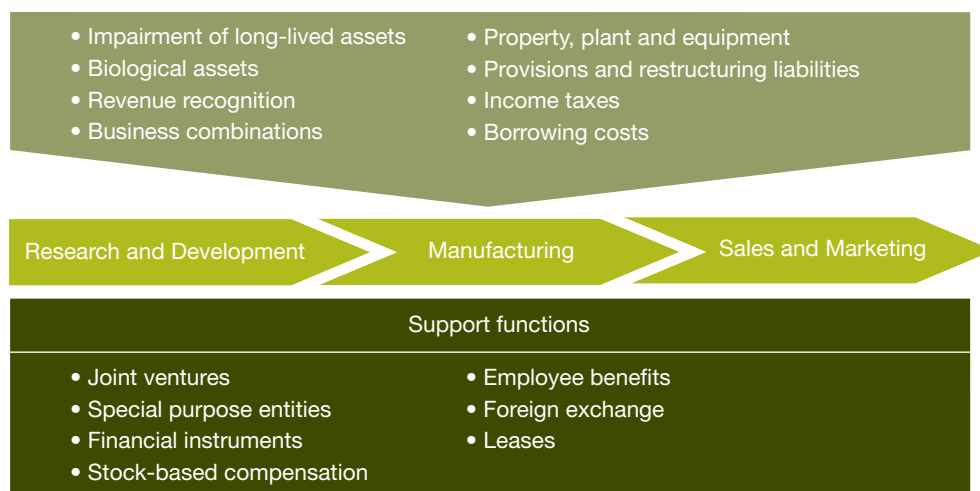
IFRS generally has more extensive disclosure requirements compared to Canadian GAAP. Entities will need to identify and consider these disclosure requirements in addition to

the measurement differences included in this publication. In particular, IAS 24, *Related Party Disclosures* and IFRS 3, *Business Combinations Revised (IFRS 3R)* have more detailed disclosure requirements than Canadian GAAP. The first time interim and annual IFRS financial statements will also need to comply with the disclosure requirements of IFRS 1, *First-time Adoption of International Financial Reporting Standards* which includes disclosure of the opening IFRS balance sheet as well as reconciliations of equity and other comprehensive income between IFRS and Canadian GAAP.

A PwC survey of Pharmaceutical implementations in Europe, noted the average page length of core financial statements increased from 130 to 185 pages. Additional disclosures include income statement disclosures, balance sheet account roll-forwards and sensitivity analyses. Some information already included in the MD&A will move into the financial statements.

The following sections of this publication highlight some of the significant differences between Canadian GAAP and IFRS that will specifically impact the value chain of Pharmaceutical and Life Sciences companies.

Value chain and significant accounting issues



Significant Accounting Issues

First Time Adoption of IFRS

Under IFRS 1, *First-time Adoption of IFRS*, the underlying principle is retrospective application of all standards at the entity's first reporting period. The International Accounting Standards Board (IASB) acknowledged that in some cases it may be too difficult, too costly or even impossible to accumulate historical information on an IFRS basis. The IASB, therefore, decided to allow preparers of financial statements to select alternatives to retrospective application in certain areas such as property, plant and equipment, business combinations, leases and pension liabilities. The IASB also considered that retrospective application is subjective in certain areas and, therefore, decided to prohibit retrospective application in certain areas such as de-recognition of financial assets and financial liabilities and accounting for estimates.

Where differences exist and there is no exemption or exception available, companies may have to dedicate significant effort to remeasure various historical transactions under IFRS. Early identification of Canadian GAAP differences and consideration of the exemptions are critical for a successful conversion and we can advise on the selection of appropriate IFRS 1 elections.

Impairment of Long-lived Assets

IAS 36, *Impairment of Assets* (IAS 36), differs significantly from current Canadian GAAP standards for the impairment of long-lived tangible and intangible assets. Under IFRS, there is no initial assessment of an asset's recoverability based on undiscounted cash flows as there is under Canadian GAAP. Rather, the carrying value of the asset is compared to the higher of the asset's "value in use" and its "fair value less costs to sell" in determining whether an impairment charge is required and, if so, the amount. This accounting difference may result in companies requiring write downs of assets under IFRS that were previously considered recoverable using the initial undiscounted cash flow test under Canadian GAAP.

Another significant difference from the current Canadian standards is that IFRS requires the reversal of previous impairment losses where there is an indication that the loss

may no longer exist or may have decreased. This requirement may lead to higher volatility in the income statements of Pharmaceutical and Life Sciences companies with impairments recorded and reversed in response to changes in economic conditions. Reversal of impairment losses are not permitted when related to goodwill.

Under IAS 36, at each reporting date (including the opening balance sheet date), companies are explicitly required to assess whether impairment indicators exist for long lived assets. At the opening balance sheet date, goodwill and indefinite lived intangible assets are required to be tested for impairment. Both Canadian GAAP and IFRS require assets to be tested for recoverability whenever events or circumstances indicate that the carrying amount may not be recoverable.

Biological Assets

If a Pharmaceutical or Life Sciences company undertakes biological activity (for example, grows plants from which particular drugs are developed), then this activity will fall within the scope of IAS 41, *Agriculture* (IAS 41). There is no specific guidance under Canadian GAAP in connection with accounting for biological assets.

Under IAS 41, biological assets should be measured, both at initial recognition and at each subsequent reporting date, at their fair value less costs to sell, except when fair value cannot be reliably measured.

The quoted price in an active market, if available, is the appropriate basis for determining the fair value of the asset in its present location and condition.

Gains and losses that arise on remeasuring biological assets at fair value less costs to sell are recognized directly in the income statement in the period in which the gain or loss arises.

Fair valuing of biological assets is an area of significant judgment and will likely require special expertise. We have experience in helping companies through this transition to IAS 41.

Revenue Recognition

IFRS is more principles based than current Canadian GAAP with respect to revenue recognition. The application of these principles may allow for changes in accounting policies relating to revenue recognition that companies will need to consider. Practically, the key areas will be in the evidence required to split multi-element contracts and in evidencing arrangements with customers.

Certain Pharmaceutical and Life Sciences companies generate revenue by entering into collaboration or licensing agreements. These arrangements often involve Pharmaceutical companies providing the financial support, marketing and development expertise and Life Sciences companies providing the new drug candidates, targets and cutting-edge science. In recent years this has led to the creation of a significant number of strategic alliances, collaboration agreements and other types of arrangements which may include upfront milestone payments, royalties and participation in joint steering committees.

Each agreement is unique and may contain complex clauses and, therefore, it is difficult to provide a “one-size-fits-all” accounting solution. Each agreement should be evaluated on its own merits, and the accounting should reflect the substance and commercial reality of the arrangement. As of yet there is no specific industry guidance or literature as to how these types of arrangements should be accounted for under IFRS.



The IASB and the United States Financial Accounting Standards Board (FASB) have undertaken a joint project to develop a new, comprehensive standard for revenue recognition. The new standard will replace the existing IAS 18, *Revenue*. The IASB and FASB issued a discussion paper in December 2008 setting out their preliminary views, to be followed by an exposure draft in 2010 and a final standard in 2011.

The discussion paper is based on the principle that revenue is recognized on the basis of increases in a company's net position in a contract with a customer. The percentage-of-completion method for revenue recognition may no longer exist as a separate and distinct model.

Careful analysis will be required to understand the implications of the proposed changes and assess the impact on current revenue recognition policies of Pharmaceutical and Life Sciences companies.

Business Combinations

There are significant updates in IFRS 3R, compared to the previous version of the standard (IFRS 3), that will impact future business acquisitions. These differences include, but are not limited to:

- What constitutes a business under IFRS 3R can differ from that under IFRS 3 and EIC 124, *Definition of a Business*. Under IFRS a development stage company is likely to be considered a business and, therefore, its acquisition would be accounted for as a business combination rather than an asset acquisition;
- All elements of consideration are fair valued e.g. contingent consideration or contingent liabilities;
- Transaction costs associated with the acquisition are expensed rather than capitalized; and
- Pre-existing interests are fair valued through income.

In January 2009, the Canadian Institute of Chartered Accountants (CICA) issued the new Handbook Section 1582, *Business Combinations*. This section provides the Canadian equivalent for IFRS 3R. If a calendar year company is considering completing a business combination on or after January 1, 2010, it should consider early adopting Section 1582 to minimize differences on the transition to IFRS.



Property, Plant and Equipment

Property, plant and equipment would initially be recorded at cost. However, IAS 16, *Property, Plant and Equipment* (IAS 16), provides entities with the option to revalue property, plant and equipment. The revaluation adjustment is recorded directly to equity if the revaluation results in an increase in the carrying value of the property, plant and equipment. If the revaluation adjustment results in a decrease in the carrying value of the property, plant and equipment, the difference is first recorded in equity to the extent of previous valuation adjustment increases, with any additional decrease recorded in the income statement. The use of the revaluation model requires regular valuations of entire classes of assets.

IAS 16 requires that the cost of property, plant and equipment be broken down into its major component parts, which are separately measured and amortized over their respective useful lives. As a result, there may be significantly more tracking required for the individual major component parts under IFRS. Although Canadian GAAP requirements are similar, application of IAS 16 will likely result in more rigorous application of this requirement than traditionally applied under Canadian GAAP.

Provisions and Restructuring Liabilities

Under IAS 37, *Provisions, Contingent Liabilities and Contingent Assets* (IAS 37), restructuring liabilities are not recognized until management is demonstrably committed, i.e. a formal plan exists and details of the restructuring have been communicated to those affected by the plan.

Canadian companies generally apply a threshold of 75% when determining whether an event is “likely” to occur. The “probable” threshold used under IFRS is lower, and generally accepted to be more than 50%. Therefore, Canadian companies may have to record provisions earlier under IFRS because of the lower threshold. Under IFRS a long-term provision should be discounted to reflect its fair value. This is different from Canadian GAAP where discounting is only necessary when specifically required by the accounting literature.

The IASB and the FASB issued an exposure draft in June 2005 that should be followed by a revised standard for the accounting for provisions and contingencies before the end of 2009. This new standard will likely no longer include the probability recognition criteria to record a provision. Pharmaceutical and Life Sciences companies will need to monitor the implications of the proposed changes and assess the impact on current accounting policies.

Income Taxes

Although accounting for income taxes under IFRS and existing Canadian GAAP are fundamentally similar the differences between IAS 12, *Income Taxes* (IAS 12) and Handbook Section 3465, *Income Taxes* are in the details.

For example, although there is no specific guidance on the treatment of R&D tax credits under IFRS, there appear to be opportunities to account for such credits as a reduction of tax expense or as a reduction of research and development (R&D) expenditures under existing IFRS, depending on the specific facts and circumstances. Canadian GAAP, however, specifically requires that such credits be reported as a reduction of R&D expenditures.

In terms of some of the more basic principles of recognition of deferred tax assets, Canadian GAAP requires that a deferred tax asset be recognized and a valuation allowance recorded to the extent that it is not “more likely than not” that the asset will be realized. Under IFRS, however, the standard used to recognize deferred tax assets is “probable”, which is not a defined term. Although the IASB has agreed that “probable” should be defined as meaning “more likely than not”, enterprises will still have to carefully consider how they interpret the term “probable” under IFRS and ensure that it is consistent with the interpretation of that term under other accounting standards.

There are several other differences in relation to business combinations, such as the recognition of deferred tax assets identified subsequent to a business combination. In these instances Canadian GAAP provides that the benefit subsequently recognized be applied to reduce goodwill and intangible assets recognized on acquisition before a recovery is recognized in tax expense. IFRS, however, does not permit such backward tracing, but rather requires that the income tax recovery be recognized in the income statement. There are also other differences in respect of deferred tax assets recognized at the time of a business combination that must be considered.

Note that in March 2009 the IASB issued an exposure draft outlining some significant changes to IAS 12. The final standard is expected in 2010. The progress of this exposure draft should be monitored carefully to ensure that changes to the standard are interpreted and applied appropriately.

One example of significant change under the IAS 12 exposure draft is the introduction of a weighted average approach to assessing uncertain tax positions, which is not required under existing Canadian GAAP or existing IAS 12.

Borrowing Costs

Under the revised IAS 23, *Borrowing Costs*, borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset shall be capitalized as part of the cost of that asset. Under Canadian GAAP, the capitalization of interest is an accounting policy option.

Intangible Assets and R&D Costs

The new CICA Handbook Section 3064, *Goodwill and Intangible Assets*, converges with IAS 38, *Intangible Assets* (IAS 38). Therefore, no major GAAP differences are expected with regard to recognition principles for intangible assets and R&D costs.

Accounting treatment for acquired intangible assets is generally consistent between the two frameworks. Capitalization of in-process R&D, technology and patents is permitted as long as these items meet the definition of an asset under IAS 38. At the opening balance sheet date, companies will need to assess whether assets acquired as part of past asset acquisitions or business combinations can be recognized under IFRS; if not, the asset will have to be derecognized against goodwill.

Special Purpose Entities (SPE)

IFRS does not contain a standard equivalent to AcG-15, *Variable Interest Entities*, under Canadian GAAP. Instead, IFRS applies a consolidation model requiring consolidation based on control or where the substance of the relationship indicates control. Standing Interpretations Committee SIC-12, *Consolidation – Special Purpose Entities* (SIC-12), states control of a special purpose entity may be indicated by an entity's exposure to risks and benefits related to the special purpose entity.

In December 2008, the IASB issued an exposure draft, ED 10, *Consolidated Financial Statements*. The final standard is expected to be issued at the end of 2009 with the objective to replace both IAS 27, *Consolidated and Separate Financial Statements – Revised*, and SIC-12. The exposure draft addresses the following aspects:

- A revision of the control definition in order to apply the same control criteria to all entities. The work on the revised control definition will focus on, but is not limited to, the consolidation of structured entities, the new term introduced for SPE; and
- Enhanced disclosures regarding consolidated and non-consolidated entities.



Financial Instruments

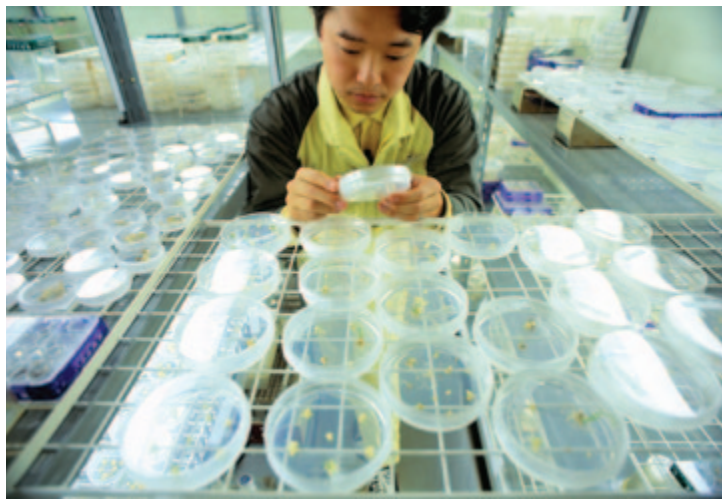
Financial instrument accounting is relatively similar between IFRS and Canadian GAAP since the adoption of CICA Handbook Section 3855, *Financial Instruments – Recognition and Measurement*. There are subtle differences between the frameworks applicable to impairment, derivatives and hedging that will need to be analyzed and addressed. For example:

- IFRS does not allow the use of the “shortcut method” for interest rate swaps or the “critical terms match method” for retrospectively assessing effectiveness for cash flow hedges; and
- Under Canadian GAAP, impairment of available for sale financial assets is recognized if the decrease in value is considered to be “other than temporary”. IFRS expands on this concept by introducing terms such as a “significant” or “prolonged” decline in the fair value of a financial asset. In practice, “significant” is considered to mean a decline greater than 20% below cost on a security by security basis. A period of 12 months or greater (below its cost) is generally used to assess whether a “prolonged” decline exists.

IFRS 7, *Financial Instruments: Disclosures*, has extensive disclosure requirements for financial instruments; however, CICA Handbook Section 3862, *Financial Instruments – Disclosures* and Section 3863, *Financial Instruments – Presentation*, eliminate the majority of these differences.

A current IASB project is proposing to broaden the definition of a derivative, which may have implications on derivatives and embedded derivatives. Careful analysis will be required to understand the implications of the proposed changes and assess the impact on current financial instruments and hedging policies of Pharmaceutical and Life Sciences companies.

Other General Accounting Issues



Joint Ventures

Under current IFRS standards, joint ventures are accounted for using either the proportionate consolidation method or the equity method. However, the IASB is expected to finalize a new accounting standard in 2009, following issuance of an exposure draft, ED 9, *Joint Arrangements*, which would limit the use of the proportionate consolidation method. The new standard also introduces the “dual approach”, which considers that a single joint arrangement may contain more than one type of arrangement; a joint operation and a joint venture, for example, each type of arrangement having a specific accounting treatment.

Joint venture arrangements will, therefore, need to be carefully analyzed to determine the appropriate accounting under the revised IFRS standard.

Stock-based Compensation

IFRS is similar in many respects to existing Canadian GAAP regarding the accounting for stock-based compensation, however, there are certain measurement and other differences. For example:

- IFRS does not allow the use of the straight-line method for graded-vesting awards with service conditions; whereas Canadian GAAP may permit either the straight-line method or the graded-vesting attribution method in certain circumstances;
- Under IFRS 2, *Share-based Payments*, an estimate for forfeitures must be made when determining the number of equity instruments expected to vest.

Foreign Exchange

Under IAS 21, *The Effects of Changes in Foreign Exchange Rates*, each individual entity has to determine its own functional currency, based on various primary and secondary indicators, and measure its results and financial position in that currency.

Once the functional currency of all foreign subsidiaries has been determined, IFRS requires the operations to be translated from the functional currency into the group's reporting currency.

Employee Benefits

The accounting for employee benefits is a complex area that is governed by IAS 19, *Employee Benefits* (IAS 19), which applies to both short-term and long-term employee benefits. Although many aspects of Canadian GAAP are aligned with IFRS on this topic, there are several areas where differences may arise. The following are some of the key areas where differences exist between the IFRS standard and Canadian GAAP as it relates to defined benefit plans:

- Under the current version of IAS 19, actuarial gains and losses are either recognized directly in equity or in the income statement using the “corridor” approach or through the application of an accelerated recognition approach; whereas, Canadian GAAP does not permit the recognition of actuarial gains and losses directly in equity;
- Under the “corridor” approach, the minimum amortization of actuarial gains and losses is over the average remaining service period of employees participating in the plan regardless of whether the majority of participants are active or inactive. Canadian GAAP requires the amortization of actuarial gains and losses over the average remaining life expectancy of the former employees when all, or almost all, of the employees in the plan are no longer active;
- Past service costs are recognized on a straight-line basis over the average period until the benefits become vested; whereas, under Canadian GAAP, past service costs are typically recognized over the average remaining service period of active employees expected to receive benefits under the plan;
- Gains or losses on the curtailment or settlement of a defined benefit plan are recognized when the curtailment or settlement occurs, whereas Canadian GAAP requires a curtailment loss to be recognized when it is probable that a curtailment will occur; and
- The plan assets and obligations must be measured with sufficient regularity that the amounts recognized in the financial statements do not differ materially from the amounts that would be determined at the balance sheet date. Canadian GAAP permits the use of a date not more than three months prior to the date of the financial statements.

In 2008 the IASB issued a discussion paper on employee benefits. The discussion paper proposes eliminating the deferred recognition (the “corridor approach”) and smoothing features of IAS 19, which would essentially eliminate the ability to defer recognition of actuarial gains and losses and past service costs. The IASB has in fact issued an exposure draft recently and intend to issue another exposure draft on recognition and presentation of employee benefits in late 2009.

The accounting for defined contribution plans under IAS 19 is substantially converged with Canadian GAAP.

Leases

Lease classification concepts under IAS 17, *Leases*, are similar to those under Canadian GAAP. A substance rather than legal form approach is applied under both Canadian GAAP and IFRS, however, under Canadian GAAP, there are certain quantitative thresholds or bright-line tests used to assess the classifications between operating and finance (i.e. capital) leases. Under IFRS, there are no similar bright-line tests, rather, the classification is determined using qualitative guidelines and professional judgement. Upon review of the specific fact pattern for each lease agreement, a different conclusion on the lease classification could result under IFRS.

The IASB and FASB have commenced a joint project to review the overall accounting for leases as it relates to lessees, and the estimated publication date of the final standard is 2011. The IASB published a discussion paper in March 2009, which considers a right-of-use approach, which would require the lessee to recognize an asset for its right to use the leased item (“the right-of-use asset”) for the lease term and a corresponding liability for its obligation to pay rentals. This approach applies the same accounting to all lease contracts, therefore, under IFRS, companies would account for all leases in a manner similar to that used for finance (i.e. capital) leases today. The current operating lease classification would be eliminated.

Conversion is not just a Technical Accounting Exercise

IFRS will present unique challenges for senior management, the financial reporting function, the treasury function and many other areas across the organization. IFRS may impact existing management reporting including budgets, forecasts, performance measures, reward schemes and bonus structures, key performance measures and covenants. Furthermore, new procedures should be considered to ensure IFRS implications are considered as part of the approval process for all new strategic investments. Depending on the size and complexity of the organization, most Pharmaceutical and Life Sciences companies will likely find that their human resources, IT, investor relations and business development departments will need to be involved in planning the transition to IFRS.

IFRS across your Organization

Implementation Resources

- Need for resources over 12-18 months
- Competing projects
- Not just a finance issue

Training and Education

- All finance staff will need training
- Broader awareness of the issues
- Other business professionals within organization
- Executives need to be able to understand and explain the “new” numbers

Business Acquisitions

- Need for IFRS figures for due diligence
- Models required for annual goodwill impairment tests

Financing/Refinancing

- Impact of IFRS on earnings or asset based debt covenants

Remuneration

- Impact of earnings volatility on profit-based bonus plans

Systems and Processes

- Need for different/new data
- New systems

Sarbanes Oxley / ICFR Certification

- Process/control documentation updates

Investor Relations

- Preparing analysis for the impact of IFRS

Management Reporting

- Budgets, forecasts, management accounts and KPIs need to be on an IFRS basis
- Examples of key metrics that could be impacted are EBIT, EPS, ROI and cash flows from operations

Communication

The financial statements of a Canadian Pharmaceutical or Life Sciences company will look different under IFRS than they currently do under Canadian GAAP. Senior executives need to be prepared to discuss the reasons for, and the nature of, the differences to board members, shareholders, the investment community and financial analysts. A detailed communication plan is necessary to educate stakeholders and actively manage perceptions.

There are a number of areas within IFRS that are subject to interpretation. While a primary aim of the IASB is to have a global set of standards applied consistently, the reality is that there are differences in the specific application of a particular accounting rule from one company to another.

Communication of key policy choices, interpretations and accounting decisions in some detail may also be necessary to differentiate and explain a Pharmaceutical or Life Sciences company's financial results compared to its peers.

Our experience with companies globally has shown that early communication, including the sharing of pro forma financial statements with preliminary figures and/or opening balance sheets under IFRS – in advance of transition date – has allowed investors and analysts to understand and become comfortable with financial results and their presentation. In contrast, late or absent dialogue with key stakeholders concerning the financial implications of the adoption of IFRS could result in a direct impact on share price.

Impact on Systems and Processes

IFRS compliance may require the realignment of reporting systems for new and additional data.

Our experience has shown that many companies implementing IFRS underestimate the time and resources needed to meet this challenge. This is especially true with existing management systems or legacy systems from past acquisitions that have never been updated and are not geared to provide sufficient or appropriate data for preparing new and increased disclosures. To make the best decisions about IT investment and achieve user engagement, it is important that company IT executives have sufficient time to perform systems realignment and are not forced to complete this work in a “fire-drill” environment.

Other process changes under the move to IFRS can be equally as important and may include the following:

- Revising existing reporting templates and other checklists to incorporate data required for disclosures under IFRS;
- Rationalizing or expanding the chart of accounts to post additional measurement changes and/or collect additional disclosures under IFRS;
- Reviewing period-end close procedures to achieve efficient close times;
- Reviewing outsourced operations' controls and capability in producing IFRS compliant information; and
- Obtaining IFRS information from significantly influenced and/or variable interest entities.

Education, Awareness and Culture

The migration to IFRS may also require a training program that combines knowledge transfer with the ability to address skills, attitudes and motivation. The entire organization will need to be trained in this area. Training should focus on what information individual business units and/or departments will need to provide in order to comply with IFRS and how IFRS will affect their decision-making and value creating strategies.

Early awareness training on the important impact areas and changes under IFRS will enable key stakeholders, including executives and board members, to be fully briefed on the new requirements and help drive a positive spirit of change management throughout the organization.

You should consider the development of an IFRS accounting manual. It will act as a reference manual to ensure consistency in implementation of accounting matters.

Regulatory requirements

The adoption of IFRS will require Canadian entities to consider various regulatory requirements.

Use of IFRS by Canadian SEC Registrants

A significant benefit to a Canadian SEC registrant adopting IFRS is that the entity will no longer have to reconcile its primary financial statements to US GAAP in SEC filings. The SEC also has extended an accommodation to first-time IFRS reporters, enabling them to present only a single year of comparative financial statements, rather than the two years it usually requires.

The SEC's IFRS accommodations are effective now but are not available to Canadian SEC registrants before 2011 unless approval of an early adoption of IFRS is obtained from the Canadian securities regulators for Canadian filing purposes.

The Canadian Securities Administrators are also proposing to retain the existing option in National Instrument 52-107 for Canadian SEC registrants to continue reporting under US GAAP.

Internal Controls over Financial Reporting

Public companies will also need to consider Multilateral Instrument 52-109 (certification of disclosures in issuers' annual and interim filings) and Sarbanes Oxley requirements (management's assessment of internal controls) as they transition to IFRS. Specifically, entities will need to update their documentation on the internal controls over financial reporting and related evaluation procedures for processes and changes impacted by the IFRS migration. Furthermore, entities will need to consider controls over the conversion process itself.

Merger and Acquisition Implications

The move to IFRS may add increased complexity to merger and acquisition (M&A) transactions in countries that have not yet adopted IFRS.

The main challenges will be the need to translate the target's historical and projected performance into IFRS to assess the accounting implications of the transaction and to understand the impact on the acquirer's earnings per share.

Complexities in IFRS accounting will lead to tougher due diligence requirements when evaluating targets in the Pharmaceutical and Life Sciences sector, even if the target is already reporting under IFRS.



Given that a number of areas of IFRS, specifically affecting Pharmaceutical and Life Sciences companies, require judgment and interpretation, comparability and consistency in the application of IFRS across countries and companies could vary markedly. Acquirers may need to devote more time and resources to scrutinizing how the target's numbers have been produced.

The potential cost of bringing the target's reporting systems up for the acquirer's standards, and the time required to do this, could significantly affect a company's ability to realize integration synergies, especially as we get closer to the transition date.

To the extent that a Canadian entity completes any acquisition of a target company not currently reporting under IFRS before 2011, it will need to include the target company in its IFRS conversion and readiness plan.

Our experience assisting companies with M&A transactions has shown that they have struggled to obtain additional data and disclosures required for target companies under IFRS.

Planning an Effective Conversion

It is easy to underestimate the volume and complexity of the work involved with the implementation of IFRS.

Our experience internationally has shown that some companies transitioning or applying IFRS for the first time will try to make manual adjustments from local GAAP to IFRS using spreadsheets or similar tools. These quick fix conversions are often not the most cost-effective choice in the long run – especially as these fixes can be prone to error, confusion and typically lack the appropriate internal controls surrounding their preparation.

To ensure sustainable and uniform application of IFRS throughout your organization, you will need to document your accounting policy selections and make sure they are consistently followed.

Each individual company will have unique circumstances that require sound judgment and expert advice. Advanced planning and an in-depth diagnostic of how IFRS will affect your company's financial reporting will reduce the risk associated with compliance and lower the overall cost of transition.

The Future of Canadian GAAP

In early May 2009, the AcSB released its exposure draft on the proposed GAAP for Private Enterprises in Canada. Canadian private enterprises will now have an option to adopt one of the two following sets of standards:

- IFRS; or
- Canadian GAAP for Private Enterprises.

Both frameworks will be effective for annual financial statements relating to fiscal years beginning on or after January 1, 2011. As a result of this, Canadian private enterprises will need to start considering which set of standards to adopt. The decision will not be easy or clear as there are many variables that a private enterprise will need to consider before making its final decision such as long-term strategic plans or comparability with competitors. Whichever choice you make, or if you need help making the right choice for your company, we can guide you through developing an appropriate conversion strategy and related time frame.

The background and context behind the decision for private enterprises to adopt IFRS and the key strategic issues you will face in converting to IFRS are outlined in our publication, Private Enterprise GAAP or IFRS? Canadian private enterprises will soon need to make the choice? To obtain a copy, contact a PwC professional or visit www.pwcifrs.ca.

IFRS – Still a Moving Target

The IASB is currently undertaking a significant reform program. As a result, a number of international standards are subject to new issuance, update and revision. Current and proposed projects could result in changes to existing standards, including but not limited to revenue recognition, and income taxes. Between now and 2011 the AcSB has numerous projects on its agenda, which will see Canadian GAAP largely converged with IFRS prior to full adoption.

Changes could materially affect how Canadian companies account for transactions. As such, IFRS conversion projects will require close monitoring of related reporting requirements which impact the companies' financial statements.

The Canadian IFRS Conversion Timeline

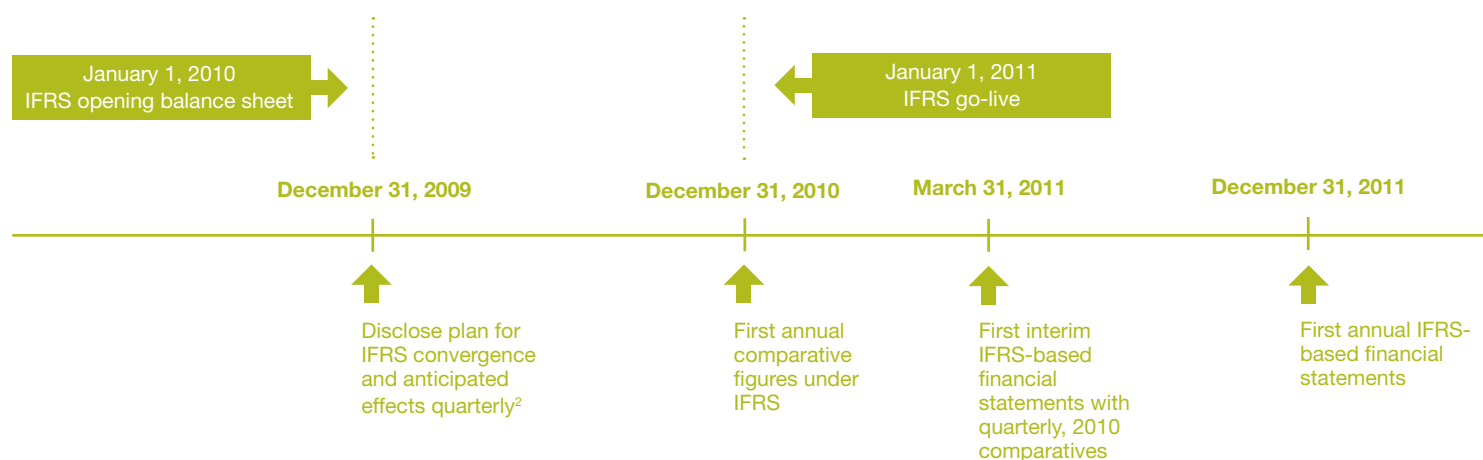
A key challenge for all entities adopting IFRS will be ensuring that all aspects of the organization are aware and educated on the impact of the change to IFRS, including the impact on systems, processes and controls.

Even though the Canadian changeover to IFRS is scheduled for 2011, the scale of the transition means that there are decisions to be made today. Accounting information will need to be converted to IFRS starting January 1, 2010 for comparative financial statements that will be reported for the first quarter of 2011. In addition, once a company commences a changeover plan, it is expected to provide quarterly disclosures in its Management Discussion and Analysis related to expected changes in accounting policies as a result of the changeover to IFRS.

In March 2009, the Accounting Standards Board issued its exposure draft “Adopting IFRS in Canada, II” which reconfirmed that publicly accountable enterprises are required to adopt IFRS for financial years beginning on or after January 1, 2011, including interim periods in 2011. Comparative interim and annual information will be required for the year ending December 31, 2010. Entities should consider preparing quarterly information on an IFRS basis starting for the first quarter ending March 31, 2010 to allow for a seamless transition.

An overview of the proposed IFRS conversion timetable is presented below:

The Canadian IFRS conversion timeline: Key dates and milestones¹



¹ The table assumes a calendar year in which a company first reports under IFRS in 2011 and presents a single year of comparatives as well as an opening IFRS statement of financial position as at the date of transition to IFRS.

² Canadian Securities Administrators Staff Notice 52-320 requires quarterly disclosures in Management’s Discussion and Analysis starting in 2008 on the plan for IFRS convergence and, starting in 2009, the expected impact of the adoption of IFRS. Quantification of the impact of adoption of IFRS will be required in 2010 in the annual Management’s Discussion and Analysis at the latest.

How we can help you

PwC has unparalleled experience in helping many of the world's largest companies adopt IFRS. Our dedicated resources and experience in working with many of the more than 12,000 companies that have already made the transition to IFRS have taught us valuable lessons that will help Canadian Pharmaceutical and Life Sciences companies with their own conversion process. We have assisted, and are assisting, a large number of Pharmaceutical and Life Sciences companies with IFRS conversion projects globally and in Canada.

To combine our collective experiences and promote consistency across our clients, we have established a Pharmaceutical and Life Sciences group within PricewaterhouseCoopers. The group has access to a multidisciplinary team of over 1,100 dedicated Pharmaceutical and Life Sciences specialists from some of the key territories in which IFRS is currently being adopted or already applies, including Europe and Australasia. The group has knowledge and experience in providing solutions for the accounting issues faced by the Canadian Pharmaceutical and Life Sciences sector and plays a key role in resolving new issues that emerge.

Our experience has shown that a critical success factor for IFRS conversion is a well-planned implementation, which is started several years in advance of the required convergence date.

Our industry-focused teams specialize in IFRS/GAAP conversions for a wide range of organizations – from large, complex institutions, requiring detailed analysis, to organizations with more straightforward requirements. These teams are supported by our Capital Markets Group, a global team of over 500 IFRS conversion experts, who specialize in multi-GAAP environments and the related conversion implications.

PwC's Transition/IFRS Methodology

While compliance with the new rules is the driver for IFRS projects, our experience indicates that a methodical approach to the conversion process can yield wider benefits. Our Transition/IFRS methodology is a robust, tried and tested framework that has an inherent flexibility, enabling us to adapt it to work most effectively within your organization and one that we would tailor to your needs and phases, as outlined below. This methodology has consistently delivered successful results.

Typically, each IFRS transition project consists of three phases. In Phase 1, the diagnostic stage, we carry out an initial impact analysis and plan the later phases. Phase 2 consists of the detailed steps necessary to prepare the first complete IFRS financial statements. In Phase 3, we assist you with taking the information, issues and solutions gathered and integrating them into your underlying financial systems and processes.

Transition/IFRS acts as a springboard from which you can launch and control your conversion project, accessing the support and guidance you need as the implementation progresses.

PwC professionals can help you plan and complete your transition to IFRS by providing:

- **An initial diagnostic of Canadian GAAP/IFRS accounting differences**
- **Advice on selection of appropriate accounting policies**
- **Advice on development of an IFRS implementation plan**
- **Training for all levels of your staff, including your board of directors**
- **IFRS trained and experienced people to supplement your IFRS team**
- **Project management support to your IFRS team**
- **Communication strategies and change management support**
- **Assessment of your requirements for data, processes, systems and controls**
- **Advice on process and system solutions to embed IFRS**
- **Competitor benchmarking**
- **M&A target accounting conversion assistance**
- **Valuation advice under IFRS fair value and impairment models**
- **Tax planning considerations on conversion to IFRS**

We can also play a consulting role during your IFRS conversion process which includes:

- Providing project management advice and assistance to your IFRS project manager;
- Reading component evaluations and related technical papers completed and approved by management as well as providing our observations and recommendations; and
- Providing advice throughout the process of evaluating and adopting IFRS accounting policies.

We are ready to help you manage the conversion process with fewer headaches. To learn more about how we can help, visit our website at www.pwcifrs.ca or contact one of the IFRS professionals listed on the next page.



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