STAFF PAPER

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IASB® meeting

Project	Annual Improvements to IFRS Standards 2018 – 2020 Cycle		
Paper topic	Due Process Steps and transition for the proposed amendment to IFRS 1		
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This paper has been prepared for discussion at a public meeting of the International Accounting Standards Board (Board) and does not represent the views of the Board or any individual member of the Board. Comments on the application of IFRS® Standards do not purport to set out acceptable or unacceptable application of IFRS Standards. Technical decisions are made in public and reported in IASB® *Update*.

Introduction

1. The International Accounting Standards Board (Board) tentatively decided to include the following proposed amendments in the next cycle of annual improvements (ie *Annual Improvements to IFRS Standards 2018–2020 Cycle)*:

    (a) IFRS 1 *First-time Adoption of International Financial Reporting Standards*—Subsidiary as a first-time adopter;

    (b) IFRS 9 *Financial Instruments*—Fees in the '10 per cent' test for derecognition;

    (c) Illustrative Example 13 accompanying IFRS 16 *Leases*—Lease incentives; and

    (d) IAS 41 *Agriculture*—Taxation in fair value measurements.

2. In June 2018, the Board tentatively decided to propose some amendments to IFRS 17 *Insurance Contracts* as part of its next cycle of annual improvements. However, in November 2018, the Board tentatively decided to propose a deferral of the mandatory effective date of IFRS 17 and in Agenda Paper 2 for this meeting, the staff recommended standard-setting to amend the requirements of IFRS 17 beyond the annual improvements the Board had already tentatively decided to propose. Accordingly, we have not included any discussion about the proposed amendments to IFRS 17 in this paper.

The International Accounting Standards Board is the independent standard-setting body of the IFRS Foundation, a not-for-profit corporation promoting the adoption of IFRS Standards. For more information visit www.ifrs.org.

3. The objective of this paper is:

   (a) to ask the Board whether it agrees with our recommendation regarding transition for the proposed amendments to IFRS 1—Subsidiary as a first-time adopter;

   (b) to set out the due process steps the Board has taken in developing the proposed amendments to be included in the Exposure Draft *Annual Improvements to IFRS Standards 2018–2020 Cycle* (Exposure Draft) (see Appendix A); and

   (c) to ask the Board to confirm it is satisfied that it has complied with the applicable due process requirements.

Structure of the paper

4. The paper is structured as follows:

   (a) summary of the proposed amendments;

   (b) IFRS 1 transition requirements;

   (c) comment period;

   (d) intention to dissent;

   (e) proposed timing for balloting and publication; and

   (f) confirmation of due process steps.

5. This paper includes one appendix—Appendix A: Actions taken to meet the due process requirements.

Summary of the proposed amendments

6. The proposed amendments are summarised below:

   (a) The proposed amendment to IFRS 1 would require a subsidiary that applies paragraph D16(a) of IFRS 1 to measure cumulative translation differences using the amounts reported by its parent, based on the parent's date of transition to IFRS Standards (see paragraphs 9–11 of this paper for more information).

(b) The proposed amendment to IFRS 9 clarifies which fees an entity includes when it applies the '10 per cent' test in paragraph B3.3.6 of IFRS 9[1] in assessing whether to derecognise a financial liability. Applying the proposed amendment, an entity would include only fees paid or received between the entity (the borrower) and the lender, including fees paid or received by either the entity or the lender on the other's behalf.

(c) The proposed amendment to Illustrative Example 13 accompanying IFRS 16 would remove from the example the illustration of the reimbursement of leasehold improvements by the lessor. The proposed amendment would resolve any potential confusion regarding the treatment of lease incentives that might arise because of how lease incentives are illustrated in that example.

(d) The proposed amendment to IAS 41 would remove the requirement in paragraph 22 of IAS 41[2] for entities to exclude taxation cash flows when measuring the fair value of a biological asset using a present value technique. The proposed amendment would ensure consistency with the requirements in IFRS 13 *Fair Value Measurement.*

[1] Paragraph B3.3.6 of IFRS 9 states 'For the purpose of paragraph 3.3.2, the terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10 per cent different from the discounted present value of the remaining cash flows of the original financial liability…'

[2] Paragraph 22 of IAS 41 states: 'An entity does not include any cash flows for financing the assets, taxation, or re-establishing biological assets after harvest (for example, the cost of replanting trees in a plantation forest after harvest).'

7. The Board and the IFRS Interpretations Committee (Committee) discussed the proposed amendments on the following dates:

Standard	Amendment	Committee meeting(s) /Agenda Papers ref	Board meeting(s) /Agenda Papers ref
IFRS 1 ***First-time Adoption of International Financial Reporting Standards***	Subsidiary as a first-time adopter	March 2017 —AP5 September 2017 —AP5C November 2017 —AP6.	December 2017 —AP12C.
IFRS 9 ***Financial Instruments***	Fees in the '10 per cent' test for derecognition	May 2016 —AP11. September 2016 —AP9. November 2016 —AP2.	April 2017 — AP12A.
IFRS 16 ***Leases***	Lease incentives	N/A	May 2018 — AP12
IAS 41 ***Agriculture***	Taxation in fair value measurements	September 2017—AP3.	January 2018— AP12B.

8. Regarding transition:

(a) the Board tentatively decided to propose that an entity would apply:

(i) the proposed amendment to IFRS 9 only to modifications or exchanges of financial liabilities that occur on or after the beginning of the annual reporting period in which the entity first applies the amendment; and

(ii) the proposed amendment to IAS 41 to fair values measured after the effective date of the amendments.

(b) the Board did not consider transition requirements for the proposed amendment to Illustrative Example 13 accompanying IFRS 16 because the amendment proposed is to (non-mandatory) material accompanying IFRS 16 (see Agenda Paper 12 to the May 2018 Board Meeting).

(c) the Board has not yet considered transition requirements for the proposed amendment to IFRS 1. The next section discusses transition for this proposed amendment.

IFRS 1 Transition Requirements

What does the proposed amendment require entities to do?

9. At its December 2017 meeting, the Board tentatively decided to propose an amendment to IFRS 1. The proposed amendment would require a subsidiary that applies paragraph D16(a) of IFRS 1 to measure cumulative translation differences (CTD) using the amounts reported by the parent, based on the parent's date of transition to IFRS Standards (subject to any adjustments made for consolidation procedures and for the effects of the business combination in which the parent acquired the subsidiary).

10. Paragraph D16(a) of IFRS 1 states:

> D16 If a subsidiary becomes a first-time adopter later than its parent, the subsidiary shall, in its financial statements, measure its assets and liabilities at either:
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> (a) the carrying amounts that would be included in the parent's consolidated financial statements, based on the parent's date of transition to IFRSs, if no adjustments were made for consolidation procedures and for the effects of the business combination in which the parent acquired the subsidiary (this election is not available to a subsidiary of an investment entity, as defined in IFRS 10, that is required to be measured at fair value through profit or loss); or…

11. The proposed relief would remove a potential difference in the amounts of CTD reported by a subsidiary and its parent. This proposed amendment is in line with the Board's original rationale for the current exemption in paragraph D16(a), which is explained in paragraph BC60 of IFRS 1. Paragraph BC60 states that the Board provided this exemption so that such a subsidiary would not have to keep two sets of records based on different dates of transition to IFRS Standards.

Overall approach in IFRS 1 to transition

12. IFRS 1 applies to entities that present their first IFRS financial statements (ie first-time adopters) and specifies how an entity transitions from its previous GAAP to IFRS Standards. First-time adopters have not previously applied IFRS Standards. Accordingly, those entities would simply apply the applicable requirements in IFRS 1 when transitioning to IFRS Standards, and any transition requirements for the proposed amendments to IFRS 1 would not be relevant for those entities. Accordingly, transition requirements are not required for first-time adopters.

13. We considered whether the Board should permit or require entities that have applied IFRS 1 in a previous period (previous first-time adopters) to retrospectively apply this proposed amendment to IFRS 1.

14. For all (but one) of the previous amendments to IFRS 1, the Board did not permit or require previous first-time adopters to apply those amendments retrospectively because those entities are not first-time adopters, and accordingly, are outside the scope of IFRS 1. Moreover, if a previous first-time adopter were to make IFRS 1 transition adjustments in any reporting period after applying IFRS 1, this could confuse users of its financial statements. This is because users would generally expect the adoption of IFRS Standards to be a one-off event—ie they would not expect an entity to have IFRS 1 transition adjustments after its date of transition to IFRS Standards.

15. We have identified one instance (paragraph 39E of IFRS 1) in which the Board permitted, but did not require, retrospective application of an amendment to IFRS 1 by previous-first-time adopters. This was an amendment to the deemed cost exemption in paragraph D8 of IFRS 1. The Board amended paragraph D8 to allow an entity to recognise an event-driven fair value measurement as deemed cost when the event occurs, provided this is during the periods covered by its first IFRS financial statements. The relief was provided so that entities do not have to keep two sets of measurements for its assets and liabilities—one to comply with IFRS Standards and one to comply with local law. The Board also decided the same relief should apply to previous first-time adopters.

16. Retrospective application of the proposed amendment to paragraph D16(a) of IFRS 1 by previous first-time adopters would require a subsidiary that previously applied paragraph D16(a) of IFRS 1 to restate its CTD. That restatement would represent the difference between its reported CTD and the amount reported in the parent's consolidated financial statements for the subsidiary's CTD calculated at the subsidiary's date of transition to IFRS Standards. This difference would already have been calculated for consolidation purposes. Furthermore, this difference would remain static from the subsidiary's date of transition until the parent company disposes of part or all of its investment in the subsidiary[3]. Accordingly, we think permitting a previous first-time adopter to apply the proposed amendment retrospectively would not provide additional cost relief because maintaining two sets of records is not unduly onerous in this situation. Permitting retrospective application would also unnecessarily complicate the proposed amendment.

17. In addition, we think the history of amendments to IFRS 1, noted in paragraph 14 above, creates an expectation for users of financial statements that a previous first-time adopter will not have IFRS 1 transition adjustments after its date of transition to IFRS Standards.

Staff conclusion and recommendation

18. For the reasons outlined in paragraphs 12–17 above, we have concluded that transition requirements for the proposed amendment to IFRS 1 are not relevant for first-time adopters. We also recommend that the Board does not permit or require previous first-time adopters to apply the proposed amendment to IFRS 1 retrospectively.

[3] Applying paragraph 48 of IAS 21 *The Effects of Changes in Foreign Exchange Rates*.

Question 1 for the Board

1. In respect of the proposed amendment to IFRS 1, does the Board agree with:

(a) our conclusion that transition requirements are not relevant for first-time adopters; and

(b) our recommendation not to permit or require previous adopters to apply the proposed amendment to IFRS 1 retrospectively.

Comment Period

19. Paragraph 6.15 of the *Due Process Handbook* says that the Board 'normally allows a minimum period of 90 days for comment on Annual Improvements.'

20. We have not identified any reason to deviate from this requirement and, accordingly, recommend a comment period of at least 90 days for the Exposure Draft.

Intention to dissent

21. Applying paragraph 6.9 of the *Due Process Handbook*, we are asking whether any Board member intends to dissent from the proposed amendments.

Proposed timing for balloting and publication

22. We expect the balloting process for the Exposure Draft to begin in January 2019 and expect to publish the Exposure Draft in the second quarter of 2019.

Confirmation of due process steps

23. In Appendix A to this paper, we have set out the due process steps required in developing and publishing an exposure draft of annual improvements together with the current status of, and any planned action for, these steps. We note that the applicable due process steps to date for commencing balloting of the Exposure Draft have been completed.

Questions 2–4 for the Board

2. **Comment period**—does the Board agree with our recommendation to have a comment period of at least 90 days for the Exposure Draft?
3. **Dissent**—does any Board member intend to dissent from the proposed amendments to be included in the Exposure Draft?
4. **Permission to ballot**—is the Board satisfied that it has complied with the applicable due process requirements and that it has undertaken sufficient consultation and analysis to begin the balloting process for the Exposure Draft?

Appendix A—Actions taken to meet the due process requirements

A1. The following table sets out the actions taken by the Board to meet the due process requirements.

Development and publication of annual improvements exposure drafts

Step	Actions
The Board and Committee meetings are held in public, with papers being available for observers. All decisions are made in public session.	The Board discussed and approved the following proposed amendments for inclusion in the *2018–2020 Annual Improvements Cycle*: (a) IFRS 1—December 2017 meeting—AP12C. (b) IFRS 9— April 2017 meeting—AP12A (c) IFRS 16—May 2018 meeting—AP12 (d) IAS 41—January 2018 meeting—AP12B The project webpages have up to date information: o Subsidiary as a first-time adopter (Amendments to IFRS 1) o Fees in the '10 per cent' test for derecognition (Amendments to IFRS 9) o Lease incentives (Amendment to Illustrative Example 13 accompanying IFRS 16) o Taxation in fair value measurements (Amendments to IAS 41) Agenda Papers were posted on the website before every Board or Committee meeting.
Finalisation	
Due process steps are reviewed by the Board.	This step will be met by this Agenda Paper.
A check is performed to ensure that each amendment included in the package meets the Annual Improvements criteria.	We prepared an assessment against the annual improvements criteria for each of the proposed amendments. This assessment was included in the following agenda papers: (a) IFRS 1—Agenda Paper 12C—December 2017 meeting (b) IFRS 9—Agenda Paper 12A—April 2017 meeting (c) IFRS 16—Agenda Paper 12—May 2018 meeting (d) IAS 41—Agenda Paper 12B—January 2018 meeting The Board agreed with our assessment of the annual improvements criteria for each of these proposed amendments.
The Exposure Draft has an appropriate comment period.	Applying the requirements in paragraph 6.15 of the Due Process Handbook, we are recommending a comment period of at least 90 days. Please refer to paragraphs 19 and 20 of this paper.
Drafting	
Drafting quality assurance steps are adequate.	The Translations, Taxonomy and Editorial teams will review the pre-ballot draft. We will perform an editorial review of the pre-ballot draft with some external parties, including Committee members. The pre-ballot draft will be made available to members of the International Forum of Accounting Standard-Setters (IFASS).

Publication	
Press release to announce the publication of the of the Annual Improvements Exposure Draft package.	A press release will be published with the Exposure Draft.
Publication of the Exposure Draft *Annual Improvements to IFRS 2018–2020 Cycle*.	The Exposure Draft will be made available on our website when published.