



Project	Annual Improvements Exposure Draft August 2010
Topic	IFRS 1 <i>First-time Adoption of International Financial Reporting Standards</i> – fixed date in derecognition exception

Introduction

Objective of this paper

1. A request was received to replace the fixed date of 1 January 2004 in paragraph B2 of IFRS 1 (relating to the derecognition exception) with ‘the date of transition to IFRSs’. The date of 1 January 2004 was originally included as a result of the revision to IAS 39 *Financial Instruments: Recognition and Measurement* in 2003. There are a number of jurisdictions that will be adopting IFRSs in the future. As time passes, the transition date of 1 January 2004 that is ‘hard-wired’ into the exception becomes more remote from the date these jurisdictions will adopt IFRSs.
2. At the March IFRS Interpretations Committee meeting, the Committee debated the following courses of action:
 - (a) changing the fixed date to a relative date (for example the ‘date of transition to IFRSs’),
 - (b) deleting paragraph B2 altogether (and thus removing the exception), or
 - (c) making no change to current requirements.

This paper has been prepared by the technical staff of the IASCF for discussion at a public meeting of the IFRS Interpretations Committee.

The views expressed in this paper are those of the staff preparing the paper. They do not purport to represent the views of any individual members of the IFRS Interpretations Committee or the IASB. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRS Interpretations Committee or the IASB can make such a determination.

Decisions made by the IFRIC are reported in IFRIC *Update*.

Interpretations are published only after the IFRS Interpretations Committee and the Board have each completed their full due process, including appropriate public consultation and formal voting procedures. The approval of an Interpretation by the Board is reported in IASB *Update*.

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3. The Committee noted that they needed more information before they could make a decision, and requested the staff to do the following:
 - (a) perform outreach activities with members of the National Standard Setters group to understand better the consequence of removing or amending the exception, and
 - (b) perform a review of transition to IFRSs in the context of the Derecognition project.

Results of the outreach with the National Standard Setters group

4. The staff asked the National Standard Setters group for feedback on which of the 3 options in paragraph 2 above they considered preferable. Nine responses were received. Appendix A includes the details of these responses.
5. Seven of the nine responses supported changing the fixed date of January 1, 2004 to a relative date, and most supported that the relative date be the 'date of transition to IFRSs'. The reasons given, if any, were broadly to do with the complexity of restating past transactions, especially where previous GAAP derecognition principles vary greatly from those under IFRSs.
6. One of the respondents¹ mentioned the possible abuse of a relative date, where the entity could structure transactions immediately before the date of transition, to achieve a desired result. This point was discussed by the Board in March 2008 (Agenda paper 5), when the issue of the hard-wired date in IFRS 1.B2 was initially discussed. The Board concluded that, although there may be a structuring risk associated with a relative date, principle-based standards should not be written with an anti-abuse focus.
7. Of the remaining two responses:

¹ UK Standard Setter

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- (a) One² supported the third option, ie. to make no change to current requirements. The reasoning given is similar to that discussed in at the March 2010 Committee meeting in paper 7A³; that is, the B2 exception was written into IFRS 1 as a result of the amendment to IAS 39 at the time, and was unrelated to the wave of transition to IFRSs in 2005.
 - (b) The other response⁴ was from a jurisdiction that adopted IFRSs in 2005. This respondent did not elect any of the 3 options discussed by the Committee, since the issue is no longer relevant to them.
8. It is clear from the above that the majority of the respondents support the relative date option. There was no support indicated for deleting paragraph B2.

Additional correspondence received

9. Lending support to the option of changing the fixed date to a relative date, is a letter received from a North American preparer representative body. This letter was received subsequent to the March 2010 Committee meeting, and not as a result of the outreach performed with the National Standard Setters group.
10. The letter supports changing the fixed date in exception B2 of IFRS 1 to ‘the date of transition to IFRS for each individual company’. The writers believe that those jurisdictions due to transition to IFRSs in the future should be in the same position as those jurisdictions that adopted IFRSs in 2005. The letter notes that ‘restating past derecognition transactions would be costly, time consuming and in many cases not possible’, and any information obtained in respect of years past may be ‘biased from the benefit of hindsight’. Further, that it would be ‘extremely difficult for external auditors to gain comfort in this area given the period of time that will have elapsed’.

Discussions with the Derecognition team

² The German Standard Setter

³ [Committee Meeting March 2010](#), paragraphs 2 -3 and 11

⁴ The New Zealand Standard Setter

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11. The staff met with members of the Derecognition team to discuss the transitional provisions to be included in the new Derecognition standard.
12. In March 2009, the Board published an exposure draft ED/2009/3 *Derecognition – Proposed amendments to IAS 39 and IFRS 7*. This exposure draft recommends a consequential amendment to paragraph B2 of IFRS 1 (refer to Appendix B for the relevant extract from ED/2009/3).
13. The proposed consequential amendment proposes deleting the date of 1 January 2004, and replacing it with a '[date]', however the ED does not state whether this date would be a relative one, or another fixed date. The staff discussed the issue with the Derecognition team, who confirmed that they would give the issue further consideration as the process to finalise the new standard continues. The application date of the new Derecognition standard is expected to follow that of IFRS 9 *Financial Instruments*, of January 1, 2013.
14. Given the above, if the new Derecognition standard were to amend the fixed date of January 1, 2004 to a relative date – say 'date of transition to IFRSs' – this relief will not yet be available to any jurisdiction adopting IFRS prior to January 1, 2013 (although early adoption of the new Derecognition standard may be allowed – this has not been finalised yet).

Staff analysis and recommendation

Reconsidering the options

15. The following is a tabular analysis of the pros and cons of the 3 options discussed by the Committee at the March 2010 meeting, in light of the above discussion:

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Option	Pros	Cons
(a) Changing the fixed date to a relative date ('date of transition to IFRSs')	<ul style="list-style-type: none"> • A first-time adopter of IFRSs would be permitted, from the date of transition onwards, to prospectively apply the derecognition principles in force at that time; • This may remove the need for a consequential amendment to be made to IFRS 1.B2 (per Appendix B) when the Derecognition standard is issued. The transitional provisions of the new Derecognition standard may need to be considered in light of this change to IFRS 1, to afford existing users of IFRSs the same relief as first-time adopters • The majority of the feedback the staff has received supports this option. 	<ul style="list-style-type: none"> • The relief may not be made available in time for particular jurisdictions who are currently in the process of adopting IFRSs. Refer discussion below, in paragraphs 16 - 20.
(b) Deleting paragraph B2 altogether (and thus removing the exception)	<ul style="list-style-type: none"> • There seems to be little advantage to following this option. The staff has received no feedback in support of this option, to date. 	<ul style="list-style-type: none"> • In the absence of the exception paragraph B2, a first-time adopter would be required to apply the Derecognition principles

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		<p>retrospectively at the date of transition to IFRSs, in accordance with the principles of IFRS 1. This would not provide any relief for a first-time adopter, and would possibly increase the burden of restatement, to the extent that the entity has continuing involvement at date of transition in transactions that occurred prior to January 1, 2004.</p>
<p>(c) Making no change to current requirements:</p> <ul style="list-style-type: none"> • First-time adopters are currently required to apply the derecognition principles retrospectively between the date of transition to IFRSs and January 1, 2004. 	<ul style="list-style-type: none"> • Assuming the new Derecognition standard proposes the consequential amendment to IFRS 1.B2 as suggested in Appendix B, and the '[date]' is stated as the 'date of transition to IFRSs', an entity adopting IFRS after the amendment is effective would be permitted, from the date of transition onwards, to prospectively apply the derecognition principles in force at that time. In other words, similar relief to that provided by option (a). 	<ul style="list-style-type: none"> • The relief may not be made available in time for particular jurisdictions who are currently in the process of adopting IFRSs. Refer discussion below, in paragraphs 16 - 20.

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16. If the Committee were to decide on option (a), and to amend IFRS 1 through the Annual Improvements process, would this process provide the relief in time for those jurisdictions planning to transition to IFRS currently, and in the near future?
17. The Annual Improvements Standard (following the October 2010 ED) would be published in April/May 2011. The application date of the standard would typically be January 1, 2012, with possible earlier adoption.
18. Realistically therefore, the earliest a first-time adopter would be able to take advantage of this relief would be from when the standard is published, on an early adoption basis; that is, April/May 2011. However, there would be a further delay where the amendment needs to be incorporated into law before use. If this date falls within the period covered by an entity's first IFRS financial statements (up to the date the financial statements are issued), it may be able to take advantage of the relief.
19. If, however, this date falls after an entity issues its first IFRS financial statements, the relief will not be available to that entity. This would be the case for some jurisdictions currently transitioning to IFRSs.
20. Further, some entities, for example those transitioning in 2011, may be able to take advantage of the relief for the purposes of their *annual* financial statements (per paragraph 18 above), but perhaps not for their *first quarter interim* financial statements in that year. This would mean that an entity would still need to perform the work required in respect of any restatement for that interim period.

Staff recommendation

21. Results of the outreach done indicate that there is strong support for changing the date of January 1, 2004 to 'date of transition to IFRSs'. In addition, a consequential amendment is planned to IFRS 1.B2 when the Derecognition standard is issued. The Derecognition team support the change to a relative date.

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22. In light of the above, the staff recommend option (a), to change the date of January 1, 2004 to 'date of transition to IFRSs'. The staff recommend, however, that this amendment to IFRS 1 be made as soon as possible.

Questions for the Committee

Question 1 - Considering the research and analysis provided above, does the Committee agree with the staff's recommendation in paragraph 22?

Question 2 – Does the Committee think this amendment should be made in the Annual Improvement process, or sooner?

Appendix A – Responses from National Standard Setters group

A1 The following was asked of the National Standard Setters group:

‘We are currently researching a potential IFRIC agenda item and we would appreciate your thoughts.

The IFRIC received a request to replace the fixed date of 1 January 2004 in paragraph B2 of IFRS 1 (relating to the derecognition exception) with 'the date of transition to IFRSs'. The date of 1 January 2004 was originally included as a result of the revision to IAS 39 *Financial Instruments: Recognition and Measurement* in 2003.

This issue was discussed at the March 2010 IFRIC meeting. The IFRIC debated the following courses of action:

- changing the fixed date to a relative date (for example the 'date of transition to IFRSs'), or
- deleting paragraph B2 altogether and thus removing the exception, or
- making no change to current requirements.

To this end, the IFRIC requested the staff to perform outreach activities with members of the National Standard Setters group to understand better the consequences of the above possible courses of action. The staff will bring the issue back to the May 2010 IFRIC meeting.

We understand that this issue is particularly relevant for those jurisdictions that are currently transitioning to IFRS, or that are due to do so in the future. We would appreciate your views on the above alternative courses of action, drawing on your experience of this issue in your jurisdiction.’

A2 The following table captures extracts and salient points of the responses we received:

National Standard Setter	Response
1. Canada	Position has not changed since the topic was brought to the Board in March 2008, by Canadian Standard Setter staff - support changing the fixed date to the date of transition to IFRSs. For

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	<p>banks, restating the securitization transactions back to 2004 is one of the biggest issues for the IFRS transition; however work on the restatement is well underway.</p> <p>If an amendment is going to be made to the exception however, they request that this amendment be made known as soon as possible to avoid further restatement work being carried out.</p>
2. New Zealand	<p>Transitioned so long ago; transition issues relating to IFRS 1 are not particularly relevant any more in this jurisdiction.</p> <p>A comment however - it would make sense to keep this paragraph in IFRS 1 aligned with the equivalent transitional provision in IAS 39 (paragraph 106).</p>
3. UK	<p>Support changing the fixed date to the date of transition to IFRSs.</p> <p>However, noted a concern regarding abuse of a relative date – suggest consider an alternative for the relative date being 3 or 4 years before the date of transition.</p>
4. Italy	<p>Support changing the fixed date to the date of transition to IFRSs. However, also believe that the issue should be addressed under the Derecognition project.</p>
5. Sweden	<p>Support changing the fixed date to the date of transition to IFRSs.</p>
6. Taiwan	<p>Support changing the fixed date to the date of transition to IFRSs.</p>
7. Germany	<p>No change should be made to the current requirements: the exception arose as a result of the revision to IAS 39 in 2003; addressing a specific situation at a given point in time. Jurisdictions that are currently transitioning to IFRS or that are due to do so in the future should be familiar with the derecognition requirements of IAS 39, and are in the position to clearly anticipate any consequences when transitioning to IFRS. This situation is completely different to the scenario in 2003/04, when the new derecognition requirements of IAS 39 coincided with jurisdictions transitioning to IFRS at the time.</p>
8. Japan	<p>Support changing the fixed date to the date of transition to IFRSs:</p> <ul style="list-style-type: none"> - current derecognition requirements under IAS 39 are complex to apply - replacement to the transition date may allow an entity to structure transactions before the date of transition; however, we believe that existing consolidation requirements under SIC-12 could mitigate some of those concerns because it normally be difficult to structure the transactions

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	<p>without using another vehicles, which are subject to SIC-12 requirements, and SIC-12 does not have such exception under IFRS 1;</p> <p>- local GAAP derecognition principles similar to those under US GAAP, therefore a need to re-assess whether many transactions executed in the jurisdiction in the past qualify for derecognition under IAS 39, which does not focus on the legal isolation concept.</p>
9. Singapore	<p>Support changing the fixed date to the date of transition to IFRSs:</p> <ul style="list-style-type: none">- less burdensome for IFRS first-time adopters;- but, be mindful of the implications of any proposed amendment to the IFRS 1 on this in view of the proposed derecognition guidance.

Appendix B – Extracts from ED/2009/3 *Derecognition – Proposed amendments to IAS 39 and IFRS 7*

Proposed amendments to IFRS 1 First-time Adoption of International Financial Reporting Standards (as revised in 2008)

Appendix B

Exceptions to retrospective application of other IFRSs

Paragraphs B2 and B3 are amended (new text is underlined and deleted text is struck through).

Derecognition of financial assets and financial liabilities

- B2 Except as permitted by paragraph B3, a first-time adopter shall apply the derecognition requirements in IAS 39 *Financial Instruments: Recognition and Measurement* prospectively ~~for~~ to transactions ~~occurring~~ entered into on or after ~~1 January 2004~~ [date]. ~~In other words, Accordingly:~~
- (a) if a first-time adopter derecognised non-derivative financial assets or non-derivative financial liabilities in accordance with its previous GAAP as a result of a transaction ~~that occurred~~ entered into before 1 January 2004 [date specified above] or, if applicable, the date from which the entity elected to apply the requirements, it shall not recognise those assets and liabilities in accordance with IFRSs (unless they qualify for recognition as a result of a later transaction or event).
 - (b) if, in accordance with its previous GAAP, a first-time adopter did not derecognise financial assets or financial liabilities as a result of a transaction entered into before [date specified above] or, if applicable, the earlier date from which the entity elected to apply the requirements, it shall not derecognise those assets or liabilities in accordance with IFRSs (unless they qualify for derecognition as a result of a later transaction or event).
- B3 Notwithstanding paragraph B2, an entity may apply the derecognition requirements in IAS 39 ~~retrospectively~~ prospectively to transactions ~~entered into from a~~ entered into ~~before the date of the entity's choosing~~ specified in paragraph B2, provided that the entity obtained the information needed to apply IAS 39 to financial assets and financial liabilities derecognised as a result of past transactions ~~was obtained~~ at the time of it initially accounting for those transactions. If an entity elects to apply the derecognition requirements in IAS 39 prospectively to transactions entered into before the date specified in paragraph B2, it shall disclose that fact, and it shall apply the requirements to all transactions from that date.