Project **Tentative Agenda Decision**

Topic **IFRS 1 *First-time Adoption* - Repeat Application of IFRS 1**

Purpose of this paper

1. The purpose of this paper is to document the staff analysis and recommendations relating to a request received in March 2010 to clarify whether an entity can apply IFRS 1 more than once.

2. The request identifies an entity that previously applied IFRS 1 *First-time Adoption of International Financial Reporting Standards* and reported in accordance with IFRSs to comply with foreign listing requirements.

3. However, the entity then delists and no longer presents its financial statements in accordance with IFRSs, instead reporting only in accordance with its national GAAP.

4. In a subsequent reporting period, the reporting requirements in the entity's local jurisdiction change from national GAAP to IFRS and the entity is again required to presents its financial statements in accordance with IFRSs.

5. The request asks the Committee to clarify how the entity should transition back to reporting in accordance with IFRSs, and specifically whether it can apply IFRS 1 for a second time.

6. As such, this paper:

   (a) provides background information on this issue;

   (b) analyses the issue within the context of IFRSs;

   (c) provides preliminary agenda criteria assessment;

(d) makes a staff recommendation on the tentative agenda decision; and

(e) asks the Committee whether they agree with the staff recommendation.

Background information

7. The objectives of IFRS 1 include ensuring that an entity's first IFRS financial statements contain high quality information that is transparent, comparable and can be generated at a cost that does not exceed the benefits.

8. In order to achieve these objectives, IFRS 1 requires application of specific exceptions, and allows some exemptions, to other guidance in IFRSs. It also requires disclosures that explain how the transition from previous GAAP to IFRSs affects the financial statements of an entity.

9. The scope of IFRS 1 requires that the standard is applied in an entity's first IFRS financial statements. In considering an entity's first IFRS financial statements, IFRS1.3(a) states:

> An entity's first IFRS financial statements are the first annual financial statements in which the entity adopts IFRSs, by an explicit and unreserved statement in those financial statements of compliance with IFRSs. Financial statements in accordance with IFRSs are an entity's first IFRS financial statements if, for example, the entity:
>
> a) presented its *most recent* previous financial statements:
>
> (i) in accordance with national requirements that are not consistent with IFRSs in all respects … (emphasis added)

10. However, IFRS 1 does not provide guidance on whether;

(a) presentation of IFRS compliant financial statements **<u>before</u>** the entity's most recent previous financial statements should be considered in applying IFRS1.3 (a).

(b) an entity can apply IFRS 1 more than once.

Staff analysis

Other situations where the issue can arise

11. The staff think that the issue of whether an entity can apply IFRS 1 more than once may arise in a number of situations in addition to the specific fact pattern identified in the request.
12. These include the situations summarised below.

List, delist and relist

13. An entity previously adopts IFRSs to comply with national listing requirements.
14. In a subsequent reporting period, the entity delists and presents financial statements in accordance with national GAAP.
15. However, the entity then relists, and for a second time, is required to present financial statements in accordance with IFRSs.

Transition between IFRS for SMEs to IFRSs

16. An entity previously prepares financial statements that are in full compliance with IFRSs.
17. In a subsequent reporting period, an entity ceases to prepare financial statements in accordance with IFRSs, and instead, presents financial statements in accordance with *International Financial Reporting Standard for Small and Medium-sized Entities* (IFRS for SMEs).
18. However, at a later date, the entity once more presents financial statements in accordance with full IFRSs, rather than IFRS for SMEs.

Possible views

19. The staff have identified two possible views (View A and View B) on whether an entity can apply IFRS 1 more than once.

20. In assessing these two views, the staff considered:

    (a) technical guidance in IFRS (specifically IFRS 1) relating to the issue; and

    (b) an assessment of the benefits to financial reporting of an entity being required to apply IFRS 1 more than once (eg adoption of the disclosure requirements in IFRS 1) against the potential costs (eg concerns relating to the potential abuse of exemptions and exceptions in IFRS 1).

View A (Support for applying IFRS 1 more than once)

21. Proponents of View A believe that an entity **is required** to apply IFRS 1 more than once.

Technical guidance supporting View A

22. Proponents of this view believe it is supported by the following arguments:

    (a) The scope of IFRS 1 **requires** an entity to apply the standard in its first IFRS financial statements.

    Financial statements in accordance with IFRSs are an entity's first IFRS financial statements when its **most recent** previous financial statements are not prepared in full compliance with IFRSs.

    (b) IFRS 1 does not prohibit an entity from applying the guidance for first-time adoption more than once.

    (c) The rationale in paragraphs BC4 and BC5 of IFRS 1 is that an entity has adopted IFRSs if, and only if, its **most recent** previous financial statements contain an explicit and unreserved statement of compliance with IFRSs.

Benefits to financial reporting of adoption of View A

23. Proponents of View A also believe that allowing an entity to apply IFRS 1 more than once improves the quality of financial reporting.

24. They note that applying IFRS 1 in these situations provides guidance on:

    (a) how comparative information should be prepared and presented.

    This avoids creating concerns that hindsight is being inappropriately used.

    (b) disclosure requirements explaining how the transition of the entity from previous GAAP to IFRSs affected its financial statements.

    This provides transparency and comparability to users over all periods presented.

    For example, when the issue arises because of a jurisdiction requiring entities to present financial statements in accordance with IFRSs, applying IFRS 1 ensures comparability of financial reporting within the jurisdiction and with other jurisdictions that are first-time adopters of IFRSs.

    (c) generating IFRS information at a cost that does not exceed the benefits.

    This may encourage more entities to resume presenting financial statements in accordance with IFRSs, increasing the number of entities complying with IFRSs.

25. Supporters of this view identify that if IFRS 1 is not applied, guidance relating to an entity resuming the presentation of financial statements in accordance with IFRSs may be limited to:

    (a) the general requirements in *IAS 1 Presentation of financial statements,* specifically IAS 1.112, which requires the entity to provide information that is relevant to understanding the financial statements:.

    112 The notes shall:

    a) present information about the basis of preparation of the financial statements and the specific accounting policies used in accordance with paragraphs 117–124;

> b) disclose the information required by IFRSs that is not presented elsewhere in the financial statements; and
>
> c) ***provide information that is not presented elsewhere in the financial statements, but is relevant to an understanding of any of them.*** (emphasis added)

(b) the requirements in paragraph 24 and 29(e) of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* relating to when retrospective application of changes in accounting policies is impracticable.

26. They believe that application of these alternatives will:

(a) reduce comparability between entities because of the judgements involved in determining what information should be disclosed in accordance with other IFRSs.

(b) not identify an entity in this situation as being significantly different from an entity that did prepare its most recent previous financial statements in accordance with IFRSs.

(c) be more costly for an entity to apply than IFRS 1.

View B (Support for only applying IFRS 1 once)

27. Proponents of View B believe that an entity should **not** be allowed to apply IFRS 1 more than once.

Technical guidance supporting View B

28. Proponents of this view believe it is supported by the following guidance in IFRSs:

    (a) IFRS 1 applies to an entity's **first** IFRS financial statements, as defined below. An entity cannot present its **first** financial statements more than once.

    > **first IFRS financial statements**: The first annual financial statements in which an entity adopts **International Financial Reporting Standards (IFRSs)**, by an explicit and unreserved statement of compliance with IFRSs.
    >
    > **first-time adopter:** An entity that presents its **first IFRS financial statements**.

    (b) consistency with the guidance in IFRS for SMEs relating to first-time adoption of SMEs. Paragraph 35.2 of IFRS for SMEs states:

    > An entity can be a first-time adopter of the IFRS for SMEs ***only once***. If an entity using the IFRS for SMEs stop using it for one or more reporting periods and then is required, or chooses, to adopt it again later, the special exemptions, simplifications and other requirements in this section do not apply to the re-adoption.(emphasis added)

Benefits to financial reporting of adoption of View B

29. Proponents of View B are concerned that the ability of an entity to apply IFRS 1 more than once may lead to potential abuse.

30. Specifically, they note concerns relating to potential application of the exemptions allowed, and exceptions required, by IFRS 1.

31. This includes the following:

Deemed cost

32. IFRS 1.D5 and IFRS 1.D7 allow an entity to use fair value at the date of transition to IFRSs as deemed cost for the measurement of property, plant, equipment.

33. Proponents of View B are concerned that multiple use of this exemption by a reporting entity may lead to:

    (a) reduced financial statements comparability with other entities.

    (b) inappropriate increases in the carrying amount of the entities assets through the entity electing fair value as deemed cost for items with a carrying amount below fair value.

    (c) abuse of the exemption to avoid recognition of impairment charges in profit and loss.

Employee benefits

34. Paragraph D10 of IFRS1 allows an entity to recognise all cumulative actuarial gains and losses at the date of transition to IFRSs.

35. Proponents of View B are concerned that multiple use of this exemption by a reporting entity may lead to abuse, specifically if the reporting entity has significant unrecognised actuarial losses.

36. However, the staff note that concerns relating to repeated use of this exemption are limited as a result of the Board's proposal to eliminate the corridor approach for recognizing actuarial gains and losses in its Exposure Draft *Defined Benefit Plans*, issued in April 2010.

Currency translation differences

37. Paragraph D13 of IFRS 1 states an entity can deem cumulative translation differences to be zero at the date of transition to IFRSs.

38. Use of this exemption may allow an entity to avoid recognising losses (and gains) from translation differences that arose before the date an entity re-applies IFRS 1 when disposing of foreign operations.

39. The staff understand some practitioners in certain jurisdictions have expressed concerns relating to potential abuse of this exemption if an entity may apply IFRS 1 more than once.

Conclusion (Staff recommendation)

40. The staff support View A that IFRS 1 may be applied more than once because it believes:

    (a) it is consistent with the current intent and wording of the objectives and scope of IFRS 1.

    (b) the risk of an entity's potential abuse of exemptions or exceptions if IFRS 1 is applied more than once is limited.

    This is because in the majority of situations, repeat application of IFRS 1 is required because of a decision taken by:

    (i) the entity's jurisdiction, rather than the entity's management (eg a change from national GAAP to IFRS); or

    (ii) by management, but because of reasons other than financial reporting (eg most delisting situations).

    (c) application of guidance in IFRSs other than IFRS 1 to address these situations would increase transparency and comparability between financial statements.

    (d) it may be difficult to resume presenting financial statements in accordance with IFRSs after a long period of time if IFRS 1 is not applied.

41. The staff believe this view is currently reflected in the wording of the scope of IFRS 1.

42. If the Committee believe the scope in IFRS 1 should be clarified further to reflect this view, the staff think an amendment could meet the criteria for inclusion in the Annual Improvements Project (AIP). However, the Committee would need to consider whether an amendment should:

    (a) simply state that IFRS 1 may be applied more than once; or

    (b) provide further principles or rules on situations when an entity may, or may not be required to apply IFRS 1 more than once.

Transition between IFRS for SMEs to IFRS

43. The staff does have concerns as to whether the conclusion reached above should be applied to one specific situation that, although not identified in the agenda request, has been raised by some constituents.

44. This situation relates to an entity that over a period of time may change between presenting its financial statements in accordance with IFRS for SMEs and presenting its financial statement in accordance with IFRSs.

45. This is because the staff believe IFRS for SMEs is a specific set of accounting standards issued by the IASB that should be identified separately from more generic ‘previous GAAP’ that an entity may apply.

46. The Board’s involvement in developing IFRS for SMEs has led to a degree of similarity and consistency between IFRS for SMEs and IFRSs. Consequently, applying IFRS 1 when an entity transitions from IFRS for SMEs to IFRS may;

    (a) be considered unnecessary; and

    (b) lead to application of certain exemptions and exceptions in IFRS 1 that are potentially inappropriate.

47. The staff observe that paragraph 35.1 of IFRS for SMEs states that an entity can be a first-time adopter of the IFRS for SMEs if its previous financial statements complied with full IFRSs:

> This section applies to a first-time adopter of the IFRS for SMEs, ***regardless of whether its previous accounting framework was full IFRSs*** or another set of generally accepted accounting principles (GAAP) such as its national accounting standards, or another framework such as the local income tax basis. (emphasis added)

48. However the staff notes that:

    (a) an entity can be a first-time adopter of IFRS for SMEs only once.

    (b) IFRS 1 was issued before IFRS for SMEs and has not been subsequently amended to address the transition of an entity between IFRS for SMEs and full IFRSs.

    (c) issues relating to the interaction between IFRSs and IFRS for SMEs may be outside of the scope of the IFRS Interpretations Committee due process.

49. In principle the staff think that much of the rationale and reasoning above could be applied to the situation of an entity that changes between reporting in accordance with IFRS for SMEs and reporting in accordance with full IFRSs.

50. However, the staff believe that the Committee should recommend the Board address the specific issue of entities transitioning from reporting in accordance with IFRS for SMEs to reporting in accordance with full IFRSs.

51. This is because the staff believe IFRS for SMEs is a specific form of previous GAAP that an entity may apply before transitioning to IFRSs.

Agenda criteria assessment for the Committee

52. The staff's preliminary assessment of the agenda criteria is as follows:

    (a) *The issue is widespread and has practical relevance.*

    Yes.

    The staff are aware of the issue of whether an entity can apply IFRS 1 more than once being raised by current and future adopters of IFRSs in a range of different situations. Consequently, the staff believe this issue is potentially widespread across different jurisdictions and has practical relevance.

    (b) *The issue indicates that there are significantly divergent interpretations (either emerging or already existing in practice). The Committee will not add an item to its agenda if IFRSs are clear, with the result that divergent interpretations are not expected in practice.*

    No.

    The staff believes that current IFRSs provide clear guidance that an entity shall apply IFRS 1 in its first IFRS financial statements.

    In addition, the staff thinks that IFRS 1.3 provides clear examples of when an entity's financial statements are an entity's first IFRS financial statements, based upon the presentation of the entity's most recent previous financial statements.

    Consequently we understand that entities are applying IFRS 1 more than once in situations when the scope criteria of IFRS 1 are met.

    However, the staff think that some entities are concerned whether application of IFRS 1 more than once is appropriate and consistent with the intention of the standard.

    (c) *Financial reporting would be improved through elimination of the diverse reporting methods.*

    No.

    The staff understands that in practice, entities have been applying the scope guidance in IFRS 1 to determine whether an entity should apply the guidance on first-time adoption of IFRSs and present its first IFRS financial statements.

When the scope criteria of IFRS 1 are met, entities are applying IFRS 1 even if they have previously been a first-time adopter of IFRSs.

(d) *The issue can be resolved efficiently within the confines of existing IFRSs and the Framework, and the demands of the interpretation process.*

Yes.

The staff believe these issues relating to the scope of IFRS 1 are narrow enough that they could be resolved efficiently within the confines of existing IFRSs.

(e) *It is probable that the Committee will be able to reach a consensus on the issue on a timely basis.*

Yes.

It is probable the Committee would be able to reach a consensus on these issues on a timely basis.

(f) *If the issue relates to a current or planned IASB project, there is a pressing need to provide guidance sooner than would be expected from the IASB's activities. The Committee will not add an item to its agenda if an IASB project is expected to resolve the issue in a shorter period than the Committee requires to complete its due process.*

Not applicable.

The IASB does not have any current or planned projects on its agenda that are expected to address these issues.

53. Based on the assessment of the agenda criteria above, the staff recommend that the Committee should not add the issue to its agenda. However, the staff propose that the Committee do recommend the Board provide additional guidance for entities transitioning between reporting in accordance with IFRS for SMEs and reporting in accordance with IFRSs.

54. The proposed wording for the tentative agenda decision is set out in Appendix A.

Question 1 for the Committee
1. Does the Committee agree with the staff's recommendation not to add this issue to its agenda? If not, how does the Committee recommend the staff to proceed? 2. Does the Committee have any comments on the proposed wording for the tentative agenda decision in Appendix A? 3. Does the Committee agree to recommend the Board provide additional guidance for entities transitioning from IFRS for SMEs to IFRSs?

Appendix A – Proposed wording for agenda decision

IFRS 1 *First-time Adoption of International Financial Reporting Standards* ─ Repeat Application of IFRS 1

The Committee received a request identifying an entity that had previously reported in accordance with IFRSs due to foreign listing requirements, and applied IFRS 1. However, the entity then delisted and no longer presents its financial statements in accordance with IFRSs, instead reporting only in accordance with its national GAAP.

In a subsequent reporting period, the reporting requirements in the entity's local jurisdiction change from national GAAP to IFRS and the entity is again required to present its financial statements in accordance with IFRSs. The request asks the Committee to clarify how the entity should transition back to reporting in accordance with IFRSs, and specifically whether it can apply IFRS 1 for a second time.

The Committee noted the scope of IFRS 1 requires an entity to apply the standard in its first IFRS financial statements. Paragraph 3 of IFRS 1 provides examples of when an entity's financial statements are considered its first IFRS financial statements. These examples are based upon assessing whether the entity's most recent previous financial statements were presented in accordance with IFRSs.

The Committee concluded that the scope of IFRS 1 is clear that an entity shall apply the standard when presenting financial statements that meet the definition of an entity's first IFRS financial statements. The Committee noted that this scope requirement does not prevent an entity from repeat application of IFRS 1.

The Committee also noted that IFRS 1 does not provide guidance for an entity transitioning between reporting in accordance with IFRS for SMEs and reporting in accordance with IFRSs.

Consequently, the Committee [decided] not to add this issue to its agenda but to recommend the Board provide additional guidance for entities transitioning from reporting in accordance with IFRS for SMEs to reporting in accordance with IFRSs.

Appendix B – Agenda requests

B1. The staff received the following Committee agenda request. All information has been copied without modification by the staff.

IFRIC Potential Agenda Item Request

<u>The Issue:</u> Issue on IFRS 1:

Can an entity adopt IFRS twice in its history and once in each jurisdiction in which the entity's shares are listed?

An entity X has its shares listed in India, Singapore and US. Entity X is domiciled in India and is reporting as per Indian GAAP. For investors in Singapore, it adopted IFRS in 2005 for the first time and applied IFRS 1 and published its first IFRS financial statements making an explicit and unreserved statement of compliance with IFRS. The IFRS financial statements are now published in India. The IFRS financial statements are published only in Singapore. In US, the entity reports as per US GAAP.

In 2007, the entity delists its shares from Singapore Stock Exchange or takes a special permission from the Singapore Stock Exchange for not presenting IFRS financial statements and that publishing Indian GAAP financial statements with reconciliation to IFRS should be accepted. Now, entity X has to report as per IFRS in India from 1 April 2011.

Would IFRS 1 be applicable to the entity in India? If one sees the immediately preceding financial year, the entity had not published any financial statements making an explicit and unreserved statement of compliance with IFRS.

If entity X cannot apply IFRS 1 as it has published financial statements previously in its history making an explicit and unreserved statement of compliance with IFRS, which standard would provide the required information to the Indian investors on transition from Indian GAAP to IFRS?

If entity X has changed its systems after getting the special permission from Singapore Stock Exchange or after delisting its shares and is not able to call the previous IFRS numbers, how should it account for the adjustments from Indian GAAP to IFRS?

<u>Current Practice:</u>

There is a wide divergence in current practice.

1. ***Application of IAS 8:***

Some are giving weight to Para 3 of IFRS 1 and applying IAS 8 for the adjustments. In this case, where the systems are not available the entities are using the local GAAP figures on the premise that retrospective restatement is impracticable. The investors are not provided with reconciliations as required by IFRS 1 as according to the entity, IFRS 1 is not applicable.

2. *Application of IAS 8 with reconciliations as per IFRS 1:*

   Some professionals who give weight to Para 3 of IFRS 1 and applying IAS 8 for the adjustments give reconciliations as required by IFRS 1 though IFRS 1 is not applicable. This is done as per the requirement of Para 112(c) of IAS 1.

3. *Application of IFRS 1:*

   Some professional give weight to Para 3(a)(1) of IFRS 1 and apply IFRS 1 as the immediately preceding financial statements were published under national GAAP without making any explicit and unreserved statement of compliance with IFRS. Thus, such entities would be enjoying the exemptions given in IFRS 1 for fair value adjustments, business combinations etc twice in its history.

<u>Reasons for the IFRIC to address the issue urgently:</u>

1. Looking to the current practice and views of professionals, it is noticed that there is a wide divergence in practice which needs to addressed immediately

2. IFRS is being adopted in different jurisdictions from different years. IFRS 1 and IAS 8 do not consider such an issue where IFRS is made applicable to an entity in different jurisdiction in different years. Thus, the issue is widespread and significantly diverging interpretations are emerging based on Para 3 and Para 3(a)(1) of IFRS 1.

3. The financial reporting would be significantly improved through elimination of the diversity emerging by making the financial statements more relevant, reliable and comparable to the users of those statements.

4. The issue, if one considers, is a narrow one on whether Para 3 should be applied or Para 3(a)(1) of IFRS 1. However, the issue is not that narrow to be inefficient to apply the interpretation process. Also, the disclosures for transition where IFRS 1 is not applicable by IAS 8 is made applicable also requires to be interpreted which is not addressed by any of the International Financial Reporting Standards.

5. The issue does not relate to a current or planned IASB project and there is a pressing need for guidance as soon as possible as many jurisdictions are adopting IFRS in phased manner.