Project	**Annual Improvements - 2009-2011 cycle**
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 by the IFRS Interpretations Committee (Interpretations Committee) to clarify whether an entity can apply IFRS 1 *First-time Adoption of International Financial Reporting Standards* more than once.

2. In the September 2010 meeting, the Interpretations Committee recommended that the Board should make an amendment to IFRS 1 to address this issue as part of 2009 – 2011 *Annual Improvements* cycle.

3. The Interpretations Committee proposes that this amendment should clarify that an entity is required to apply IFRS 1 each time that it prepares and presents financial statements that meet the definition of its first IFRS financial statements.

4. In response, this paper:

   (a) provides background information on this issue;

   (b) gives an overview of the analysis performed by the Interpretations Committee;

   (c) assesses the amendment for inclusion as part of the *Annual Improvements Project*;

   (d) makes a staff recommendation on the draft wording for the proposed amendment to IFRS 1; and

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

Background information

5. The request identifies an entity that had previously reported in accordance with IFRSs to meet foreign listing requirements and applied IFRS 1.

6. The entity then delisted and no longer presents its financial statements in accordance with IFRSs, instead reporting in accordance with its national GAAP.

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

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

9. At the meetings in May[1] , July[2] and September[3] 2010, the Interpretations Committee noted that the scope of IFRS 1 requires an entity to apply the standard in its first IFRS financial statements for a second time in the circumstances described.

[1] See Agenda Paper 8 of the May 2010 IFRS Interpretations Committee Meeting : IFRIC Committee Meeting 6 May 2010

[2] See Agenda Paper 9 of the July 2010 IFRS Interpretations Committee Meeting : IFRIC Committee Meeting 6 July 2010

[3] See Agenda Paper 5 of the September 2010 IFRS Interpretations Committee Meeting : IFRIC Committee Meeting 2 September 2010

Staff analysis

Determination that IFRS 1 may be required to be applied more than once

10. The determination by the Interpretations Committee that, in some circumstances, an entity may be required apply IFRS 1 more than once, reflects the application of the following guidance:

    (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.

    (d) The objective of IFRS 1 is to ensure that an entity's first IFRS financial statements contain high-quality information that:

        (i) is transparent for users and comparable over all periods presented;

        (ii) provides a suitable starting point for accounting in accordance with International Financial Reporting Standards (IFRSs); and

        (iii) can be generated at a cost that does not exceed the benefits.

Rejection of the arguments that IFRS 1 may not be applied more than once

11. In determining that, in some circumstances, an entity may be required apply IFRS 1 more than once, the Interpretations Committee rejected the following arguments.

First IFRS financial statements

12. IFRS 1 applies to an entity's **<u>first</u>** IFRS financial statements, as defined below:

> **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**.

13. Some argue that an entity cannot present its **<u>first</u>** financial statements more than once.

14. The Interpretations Committee identified that use of the term 'first' in the standard could be misleading. However the Interpretations Committee determined that an amendment to change use of the word 'first', which would include changing the title of IFRS 1, although it would not be expected to change how entities apply IFRS 1, might, because of its nature, be outside the scope of the Interpretations Committee and the scope of *Annual Improvements*.

15. The staff also believe that use of the term 'first' does appropriately describe the situation for the majority of entities that apply the standard.

IFRS for SMEs

16. Some argue that applying IFRS 1 more than once is inconsistent with the guidance in the IFRS for SMEs relating to first-time adoption of the IFRS for SMEs. This is because paragraph 35.2 of the 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 stops 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)

17. The Interpretations Committee noted that issues relating to the IFRS for SMEs are outside the scope of the Interpretations Committee due process.

18. The Interpretations Committee did note that some constituents questioned whether specific guidance should be provided for transition from the IFRS for SMEs to IFRSs. These constituents proposed identifying the IFRS for SMEs separately from other forms of national GAAP in applying IFRS 1, because the IFRS for SMEs is a specific set of accounting standards issued by the IASB.

19. The Interpretations Committee concluded that they should not recommend that the Board should address this issue, but that the Interpretations Committee would notify the Board that this question might need to be addressed as part of the post implementation review of the IFRS for SMEs.

Abuse concerns

20. The Interpretations Committee also discussed whether the ability of an entity to apply IFRS 1 more than once may lead to potential abuse; for example application of the exemptions allowed, and exceptions required, by IFRS 1 relating to deemed cost, employee benefits and currency translation differences.

21. However, the Interpretations Committee determined that 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).

Staff recommendation

22. The Interpretations Committee determined that, in certain circumstances IFRS 1 is required be applied more than once because:

(a) IFRS 1 is clear that, if the scope criteria are met, an entity is **required** to apply the standard;

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

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

(d) application of guidance in IFRSs other than IFRS 1 to address these situations would decrease transparency and comparability between financial statements;

(e) 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 for a second time.

Assessment against Annual Improvements criteria

23. The Interpretations Committee observed that the current wording of IFRS 1 requires an entity to apply IFRS 1 when certain scope criteria are met. The scope of IFRS 1 does not consider whether an entity has, or has not, previously applied the standard.

24. Consequently the Interpretations Committee determined, in conformity with their understanding of current practice, that an entity is required to apply IFRS 1 when it meets the scope criteria, even if it has applied the standard in a previous reporting period.

25. The Interpretations Committee noted that the scope criteria are based on application of IFRS 1 to an entity's first IFRS financial statements. Paragraph 3 of IFRS 1 provides examples of when an entity's financial statements are considered to be 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.

26. However, the Interpretations Committee recommended that the Board should amend IFRS 1 to clarify this matter.

Assessment against currently-used criteria

27. The existing criteria for inclusion in the 2009-2011 *Annual Improvements* cycle are that the change is **non-urgent** and **necessary**.

28. The Interpretations Committee think that the change is non-urgent, because there are not currently significant divergent interpretations relating to this issue in practice.

29. The Interpretations Committee also think that the change is necessary because some constituents believe that IFRS 1 does not provide clear guidance relating to this issue, and that the amendment should be made to avoid the emergence of future divergent interpretations of the scope of IFRS 1.

30. Consequently, the Interpretations Committee believe that the proposed improvement meets the existing criteria for inclusion in the 2009-2011 *Annual Improvements*.

Proposed new criteria

31. In August 2010, the IFRS Foundation published for public comment proposed enhancements to the criteria for the IASB's annual improvements process.[4] The comment period ends 30 November 2010.

32. Although the proposed criteria are not yet finalised, the staff believe it is also appropriate to assess in the context of these proposed criteria:

> *(a) The proposed amendment has one or both of the following characteristics:*
>
> *(i) clarifying—the proposed amendment would improve IFRSs by:*
>
> *• clarifying unclear wording in existing IFRSs, or*
>
> *• providing guidance where an absence of guidance is causing concern.*
>
> *A clarifying amendment maintains consistency with the existing principles within the applicable IFRSs. It does not propose a new principle, or a change to an existing principle.*
>
> *(ii) correcting—the proposed amendment would improve IFRSs by:*
>
> *• resolving a conflict between existing requirements of IFRSs and providing a straightforward rationale for which existing requirement should be applied, or*
>
> *• addressing an oversight or relatively minor unintended consequence of the existing requirements of IFRSs.*
>
> *A correcting amendment does not propose a new principle or a change to an existing principle, but may create an exception from an existing principle.*

The staff believe that this amendment is clarifying unclear wording in existing IFRSs, specifically the wording in IFRS 1.The proposed amendment does not change an existing principle, or introduce a new principle into IFRSs.

[4] Trustees seek views on criteria for annual improvements process

> *(b) The proposed amendment has a narrow and well-defined purpose, ie the consequences of the proposed change have been considered sufficiently and identified.*

The staff believe this amendment is narrow and has a well-defined purpose.

> *(c) It is probable that the IASB will reach conclusion on the issue on a timely basis. Inability to reach a conclusion on a timely basis may indicate that the cause of the issue is more fundamental than can be resolved within annual improvements.*

The staff believe the IASB will reach conclusion on the issue on a timely basis. This was indicated by the decisions made by the Interpretations Committee.

> *(d) If the proposed amendment would amend IFRSs that are the subject of a current or planned IASB project, there must be a pressing need to make the amendment sooner than the project would.*

The staff believe that the proposed amendment would not amend IFRSs that are the subject of a current or planned IASB project.

Staff conclusion

33. Based on their assessment under the existing annual improvements criteria, the Interpretations Committee recommend that the change proposed in Appendix A should be included in the 2009-2011 *Annual Improvements* cycle.

34. In addition, the staff believe that this recommendation is consistent with an assessment under the proposed enhancements to the Annual Improvements criteria that were published for public comment after the Interpretations Committee made their recommendation.

Effective date and transition

35. The staff believe that the amendment does not change practice, but provides greater clarification. Consequently, the staff believe that early application should be permitted. If an entity applies the amendment, it should comply with the current IFRS 1 disclosure requirements.

36. The Interpretations Committee propose that an entity shall apply the amendment for annual periods beginning on or after 1 January 2012. Earlier application should be permitted.

Consequential amendment

37. The Interpretations Committee do not believe that any consequential amendment is needed to any other IFRSs.

Proposed draft wording

38. The proposed wording for the amendment to IFRS 1 and for the Basis for Conclusions are in Appendix A.

Question 1 for the Board
1. Does the Board agree with the Interpretation Committee's recommendation that the Board should make an amendment to IFRS 1 to address this issue as part of the 2009-2011 annual improvement projects? 2. Does the Board have any comments on the proposed wording for the amendment to IFRS 1 in Appendix A?

Appendix A – Proposed amendment to IFRS 1 *First-time Adoption of International Financial Reporting Standards*

Paragraphs 2A and 39F are added.

Scope

2 An entity shall apply this IFRS in:

(a) its first IFRS financial statements; and

(b) each interim financial report, if any, that it presents in accordance with IAS 34 *Interim Financial Reporting* for part of the period covered by its first IFRS financial statements.

2A An entity is required to apply this IFRS each time it prepares and presents financial statements that meet the definition of its first IFRS financial statements. This requirement exists when the entity's most recent previous financial statements do not contain an explicit and unreserved statement of compliance with IFRSs, even if the entity has applied this IFRS in a previous reporting period.

Effective date

39F. *Improvement to IFRSs* issued in [date] added paragraph 2A. An entity shall apply this amendment for annual periods beginning on or after 1 January 2012. Earlier application is permitted.

Basis for Conclusions on proposed amendment to IFRS 1 *First-time Adoption of International Financial Reporting Standards*

This Basis for Conclusions accompanies, but is not part of, the proposed amendment.

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

BC1 The Board identified the need to clarify whether an entity is required to apply IFRS 1 in its IFRS financial statements if the entity has applied IFRS 1 in a previous reporting period. For example, an entity may have applied IFRS 1 in a previous reporting period to meet listing requirements in a foreign jurisdiction. The entity then delists and no longer presents financial statements in accordance with IFRSs. In a subsequent reporting period, the reporting requirements in the entity's local jurisdiction may change from national GAAP to IFRSs. Consequently, the entity is again required to present its financial statements in accordance with IFRSs.

BC2 The Board noted that the scope of IFRS 1 focuses on whether an entity's financial statements are its first IFRS financial statements. If an entity's financial statements are its first IFRS financial statements, the entity is required to apply the standard in accordance with paragraph 2(a).

BC3 In determining whether an entity's financial statements are an entity's first IFRS financial statements, the entity assesses whether its most recent previous financial statements include an explicit and unreserved statement of compliance with IFRSs. The entity does not take into consideration any earlier instance (or instances) when it presented its financial statements in accordance with IFRSs.

BC3 However, use of the term 'first' raises the question of whether IFRS 1 can be applied more than once when, after previously applying IFRS 1, an entity's most recent previous financial statements do not include an explicit and unreserved statement of compliance with IFRSs.

BC4 As a consequence, the Board proposes to clarify that an entity is required to apply this IFRS when the entity's most recent previous financial statements do not contain an explicit and unreserved statement of compliance with IFRSs, even if the entity has applied this IFRS in a previous reporting period.