

6<sup>th</sup> November 2002

Sir David Tweedie  
Chairman  
International Accounting Standards Board  
30 Cannon Street  
London  
EC4M 6XH

Dear Sir David:

The global organisation of Ernst & Young is pleased to comment on Exposure Draft 1, *First-time Application of International Financial Reporting Standards* (the "FTA Standard").

We fully support the Board's objectives in the First-time Application Project as they are set out in the Invitation to Comment. However, notwithstanding our full support for this project, there are a number of areas in which we have reservations with respect to the approach the Board has taken. Our comments below have been grouped under the following headings:

1. Principles, structure and drafting of the Exposure Draft;
2. Scope of the standard;
3. SIC-8 as an allowed alternative treatment;
4. Business combinations; and
5. Undue cost or effort.

Answers to the Board's questions on the FTA Standard and our detailed comments are included in the Appendix to this letter.

### **Principles, structure and drafting of the Exposure Draft**

In our view, the Exposure Draft as currently drafted falls short of what we understand as being the Board's objective of producing high quality standards. This is because the underlying principles are not well articulated, the structure of the FTA Standard is confusing and the actual drafting itself is unnecessarily complicated.

#### *Principles*

We believe that IFRS should be based on clearly articulated principles that are presented in black-lettered paragraphs and are explained in the grey-lettered paragraphs. The current draft contains only three black-lettered paragraphs (paragraphs 7, 25 and 30), which, in our view, do not clearly articulate the principles underlying the Standard.

The main objectives of the FTA Standard should be:

- To ensure that financial statements prepared under IFRS are high quality, comparable and transparent;
- To provide a suitable and comparable starting point for the preparation of financial statements under IFRS; and
- To offer limited exemptions in those cases where the general requirement to apply standards retrospectively would either be impracticable or reduce the reliability and comparability of IFRS financial statements.

To achieve the objective of high quality, reliable, comparable and transparent financial reporting going forward:

- The scope paragraphs of the FTA Standard should be as permissive as possible to bring a maximum number of entities within its scope. The FTA Standard should require all first-time adopters to restate financial statements prepared under their previous GAAP to IFRS, using the principles set out in the FTA Standard, which are:
  - Entities should apply the same accounting policies throughout all periods presented;
  - Exemptions from the requirements of IFRS should be available only when retrospective application is impracticable, impossible or unreliable as a result of the need to apply hindsight, or where IFRS requirements are based on management intent;
  - Users should be provided with information that enables them to understand the changes to the financial statements as a result of the transition to IFRS; and
- However, entities that fall outside the scope of the FTA Standard but that erroneously asserted IFRS compliance should be required to achieve full IFRS compliance by applying IAS 8, *Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies*.

#### *Structure*

To avoid inconsistent application of the FTA Standard and improve its readability, we believe that additional exemptions (from the general principle set out in paragraph 7 of the FTA Standard) should be set out in the body of the Standard rather than in an Appendix to the Standard or in the Implementation Guidance. In the current drafting of the Standard additional exemptions can, for example, be found in:

- Appendix C, *Hedge Accounting*;
- Example 4 in Appendix B, *Business Combinations*; and
- Paragraphs IG21-22 of the Implementation Guidance, which provides an “undue cost or effort” exemption regarding the application of IAS 23, *Borrowing costs*, in determining cost-based measurements.

#### *Drafting*

We urge the Board to review and improve the drafting of the Standard, as there are numerous instances where the drafting obscures the underlying requirements of the Standard and may give rise to interpretation issues. For example, the tortuous wording of, and circular references among, paragraphs 7, 8 and 13 make the Standard unnecessarily difficult to understand and may give rise to differences in interpretation. The interaction of these three paragraphs also creates confusion as to how the exemptions under paragraphs 14-24 should be applied;

#### **Scope of the standard**

We believe that the aim of the FTA Standard should be to provide a suitable and comparable starting point for the preparation of high quality, comparable and transparent financial statements under IFRS, while at the same time offering limited exemptions in those cases where the general requirement to apply standards retrospectively would be impracticable. We are not convinced that the quality of financial reporting will be improved by denying certain entities the use of the FTA Standard and we believe that it will actually reduce comparability of their financial statements.

Whilst some entities claim that their national GAAP financial statements already comply with IFRS, we believe that the quality of financial reporting could improve significantly if they were allowed to apply the FTA Standard when migrating to IFRS as their primary basis of reporting. The only entities to which the FTA Standard should not apply are those that have previously published audited IFRS financial statements. Therefore, we believe that paragraph 3 should be deleted, as the risk of those entities not properly converting to IFRS outweighs the risk of 'cherry picking' by true IFRS reporting entities. The reason we hold this view is that we believe that to achieve the greatest possible comparability, reliability and transparency in IFRS reporting going forward, the FTA Standard should be as permissive as possible to bring a maximum number of entities within its scope. We believe the benefits of taking this approach far exceed concessions that are afforded to entities that apply the FTA Standard.

However, the aim of the scope paragraphs of the FTA Standard, as drafted, seems to be to deny all entities that have claimed IFRS compliance the option to use the first-time application exemptions. At the same time "true" first-time adopters have to restate their financial statements in accordance with the FTA Standard's requirements. Should this be the Board's objective, the FTA Standard may not achieve this aim in a number of circumstances unless the Board clarifies what "an explicit and unreserved statement of compliance with all IFRSs" means. For example, it is not clear whether:

- An entity that previously stated that its accounting policies were "consistent" with IFRS would be within the scope of the FTA Standard or not; and
- An entity that, for example, made a statement that it complied with all IFRS except for IAS 14, *Segmental Reporting*, should be treated differently from an entity that chose to make an explicit and unreserved statement of compliance with IFRS, but the auditors qualified their report on the basis of non-compliance with IAS 14.

Therefore, we believe that the Board should clarify what is meant by "an explicit and unreserved statement of compliance with all IFRSs", as used in paragraphs 2 and 3. We suggest that it should be made clear that this requirement applies only to financial statements on which the auditors have reported with respect to compliance with IFRS. Similar entities could otherwise be treated in different ways under the FTA Standard, if the requirement for an explicit and unreserved statement of compliance is defined without reference to the audit report.

Furthermore, the Board should clarify whether – in the absence of a reference to IFRS in the auditors' report – paragraph 3(a) would place entities outside the scope of the FTA Standard if they had previously published national GAAP financial statements together with non-statutory, unaudited pro-forma accounts under IFRS.

The Appendix to this letter addresses a number of other areas where the wording of the scope paragraphs is ambiguous.

#### **SIC-8 as an allowed alternative treatment**

Paragraph 13 of the FTA Standard requires that an entity, which does not use the exemptions in the FTA Standard, shall "...apply the IFRSs that were effective in each period and may, therefore, need to consider superseded versions of IFRSs if later versions required prospective application." This accounting treatment would in essence be equivalent to that required by SIC-8, *First-time Application of IASs as the Primary Basis of Accounting*, except that SIC-8's exemption on the grounds of impracticability would not be available. The shortcomings of the SIC-8 method are well documented and prompted the Board's first-time application project. Therefore, it is not appropriate to include an option in the FTA Standard that permits entities to

use this method. Entities that are within the scope of the FTA Standard should apply the principle outlined in paragraph 7 and all exemptions.

#### **Business combinations**

An entity may have entered into business combinations that were neither recognised nor accounted for as business combinations under its previous GAAP. For example, an entity may have acquired a subsidiary, but never determined the carrying amount of individual assets and liabilities of that subsidiary as that subsidiary was not required to be consolidated. This means that the method described in paragraph 20 cannot be applied as the deemed cost of assets and liabilities acquired are unknown. The Board should clarify whether in such cases the entity should apply IAS 22, *Business Combinations*, retrospectively as of the original date of acquisition or whether another accounting treatment is more appropriate – for example, the full grandfathering of the previous accounting. As stated in the Appendix to our letter we believe that retrospective application of IAS 22 should be prohibited.

#### **Undue cost or effort**

In the FTA Standard there are a number of exemptions that are based on the principle of “undue cost or effort”. We are concerned that, in the absence of further guidance as to how this test should be applied in practice, the concept is virtually meaningless, and entities will apply varying interpretations as to the circumstances under which the exemption may be invoked. At the extreme end of possible interpretation, some might take the view that this criterion would allow an entity to regard almost any cost as undue, whereas the test of impracticability is much more stringent. The link between “undue cost or effort” and materiality is important also, but has not been addressed.

We believe that the Board is effectively introducing a hidden option without definition. In our view, the Board should revert to the former “impracticable” approach, but should give more guidance about how the impracticability test should be applied in practice.

Yours sincerely

*Ernst & Young*

## Appendix

### QUESTION 1

*The proposed IFRS would apply when an entity first adopts International Financial Reporting Standards (IFRSs) as its new basis of accounting, by an explicit and unreserved statement of compliance with all IFRSs (paragraphs 1-5 and paragraphs BC4-BC10 of the Basis for Conclusions.*

*Is this an appropriate description of the circumstances when this proposed IFRS should apply? If not, what changes would you suggest and why?*

We agree that the proposed IFRS (“the FTA Standard”) should apply when an entity first adopts IFRS. However, the following amendments are required in paragraphs 2-5 to provide an appropriate description of the circumstances when the FTA Standard should apply.

#### **An entity’s “basis of accounting”**

The reference to “its basis of accounting” in paragraph 2 implies that an entity can only have one set of financial statements prepared under one basis of accounting. However, in our experience this is not always the case. For example, entities from the Peoples Republic of China (PRC) that are listed on the Hong Kong Stock Exchange may publish two sets of financial statements. One set is based upon PRC GAAP (to meet national legal requirements) and another, based upon IAS, is to meet Hong Kong listing requirements.

The reference in paragraph 2 to “its basis of accounting” is unnecessary. Therefore, we suggest that the IASB should scope out of the FTA Standard those entities that have published audited IFRS financial statements, regardless of whether IFRS represented the entity’s “basis of accounting” at the time.

#### **The use of “for example” in paragraphs 2 and 3**

The lists of examples that explain what is meant by “an entity’s first IFRS financial statements” (paragraph 2) and the one that explains when “an entity does not adopt a new basis of accounting” (paragraph 3) seem to be exhaustive. Therefore, the phrase “for example” should be removed from paragraphs 2 and 3, as it introduces unnecessary ambiguity. However, if the Board has identified other possibilities, these should be added.

#### **When an entity does not adopt a new basis of accounting – paragraph 3**

As discussed in the cover letter, we are not convinced that the quality of financial reporting will be improved by denying certain entities the use of the FTA Standard. The only entities to which the FTA Standard should not apply are those that have previously published audited IFRS financial statements. Therefore, we believe that paragraph 3 should be deleted, and the FTA Standard require all existing IFRS reporting entities, which do not fully comply with all IFRS requirements, to apply IAS 8, *Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies*.

Paragraph 2(b) refers to “... the entity’s owners *or* other external users” [emphasis added]. Strictly speaking this means, for example, that the mere act of providing internal IFRS financial statements to one’s bankers could put a first-time adopter into a position where it can no longer apply the FTA Standard. We believe this to be an anomaly and recommend a change to the wording of paragraph 2(b) as follows:

“(b) prepared financial statements under IFRSs for internal use only, without making them available to the entity’s owners and other external users; or”

As drafted, there is a lack of symmetry between paragraph 2(b) and paragraph 3 (if retained). For the sake of completeness, clarity and consistency, the following underlined wording should be added to sub-paragraph 3(a):

“(a) stops presenting separate financial statements under national requirements, having previously presented them as well as another set of financial statements that contained an explicit and unreserved statement of compliance with IFRSs and made them available to the entity’s owners and other external users; or”

#### **Exclusion of certain subsidiaries from the recognition and measurement requirements**

We agree that certain qualifying subsidiary undertakings should only comply with the disclosure requirements of the FTA Standard. However, the reason given should be based on the fact that, having already reported to its parent using IFRS, the subsidiary would not be expected to encounter unnecessary cost or effort in preparing the required information for its own first IFRS financial statements.

With regard to paragraph 5(b), it is unclear to us why the Board wants to require unanimous agreement by all minority shareholders on whether a subsidiary should be considered a first-time adopter. We think this is a legal matter that is outside the remit of the IASB. In addition, the requirement for a unanimous vote could give rise to practical difficulties in entities with a large number of individual minority shareholders. Therefore, we believe that paragraph 5(b) should be removed.

#### **QUESTION 2**

*The proposed IFRS proposes a requirement that an entity shall prepare its opening IFRS balance sheet using accounting policies that comply with each IFRS effective at the reporting date for its first IFRS financial statements. Paragraphs 13-24 propose limited exemptions from this requirement.*

*Are all of these exemptions appropriate? Should the Board amend any of these exemptions or create any further exemptions (paragraphs BC11-BC89)? If so, why?*

We agree with the basic principle that first-time adopters should apply the same accounting policies throughout all periods presented under and complying with IFRS effective at the reporting date for its first IFRS financial statements, as this greatly facilitates the adoption of IFRS.

Paragraph 13 of the FTA Standard requires that an entity, which does not use the exemptions in the FTA Standard, shall “...apply the IFRSs that were effective in each period and may, therefore, need to consider superseded versions of IFRSs if later versions required prospective application.” As discussed in the cover letter, this accounting treatment would in essence be equivalent to that required by SIC-8, *First-time Application of IASs as the Primary Basis of Accounting*. The shortcomings of the SIC-8 method are well documented and prompted the Board’s first-time application project. Therefore, it is not appropriate to include an option in the FTA Standard that permits entities to use this method and paragraphs 8 and 13 should be deleted.

Regarding the second part of Question 2; we consider the proposed exemptions to be appropriate, subject to the following amendments:

**Paragraphs 16, 23 and “undue cost or effort”**

As discussed in the covering letter, we are concerned that, in the absence of further guidance as to how the “undue cost or effort” test should be applied in practice, the concept is virtually meaningless, and entities will apply varying interpretations as to the circumstances under which the exemptions may be used. We do not believe that paragraph BC13 assists in this matter. Instead the Implementation Guidance should include examples that clarify the Board’s view as to what would constitute undue cost or effort, and what would not. The link between undue cost or effort and materiality is also relevant and should be addressed in the Implementation Guidance.

**Using valuations under previous GAAP as deemed cost**

Paragraph 17 allows entities that have used a deemed cost under their previous GAAP to continue to elect to do so without adjustment. Indeed, if such values were determined before the date of transition, the wording of paragraph 16 implies that this treatment would be mandatory (by prescribing the exemption “unless paragraph 17 or 19 applies”).

The Board should replace the phrase “broadly comparable” in paragraph 17 with “not materially different”, as this is more readily understood by preparers of financial statements and their auditors.

The Board should also clarify whether “revalued the items to an amount that *is* broadly comparable to IFRSs” (emphasis added), requires the test of comparability to be applied as at the date of transition or the date of the original revaluation. Otherwise it is not clear under what circumstances the Board expects this exemption to apply. We suggest that the Board changes the wording to “revalued the items to an amount that was broadly comparable to IFRS at the date of revaluation”.

**Event-driven fair value measurement as deemed cost**

The Exposure Draft should explain clearly why the existence of event driven values would always require their use as deemed cost. For example, certain event driven values may have been established for regulatory/political purposes and with no regard to whether the entity maintained records that could produce reliable cost based measurements.

Paragraph BC30 causes confusion by suggesting that the exemption is based on relevance of information to users and then reverting to a seemingly generic justification of undue cost or effort.

In addition, the FTA Standard should address the Board’s required treatment in situations where the value of certain intangible assets have been determined at the time of a privatisation or IPO.

**Reserves relating to previously revalued property, plant and equipment**

The Board should explain how an entity should record the revaluation reserve from its most recent previous financial statements, when it takes the exemption under paragraph 17 to treat a previous GAAP revaluation as deemed cost under IFRS.

In our view, having classified this measurement as a deemed cost rather than a valuation, the related revaluation reserve should be taken to retained earnings as at the date of transition. Failure to require this opens the door to entities potentially charging subsequent asset impairments to the revaluation reserve, rather than to the income statement.



**Retrospective application of IAS 22 *Business Combinations***

1. We agree that entities should not be required to apply IAS 22, *Business Combinations*, retrospectively to business combinations recognised under previous GAAP. For all the reasons that are already well rehearsed regarding the use of hindsight and reliability of information, we believe that the retrospective use of IAS 22 should be prohibited. We note that paragraph BC39 of the Basis for Conclusions confirms this view in stating that the relevance and reliability of the first IFRS financial statements could be reduced if an entity had to recreate data that was not available at the time of the acquisition or to make subjective estimates after the event.
2. The Board should confirm whether the exemptions proposed in paragraphs 20-21 also apply to the notional goodwill on acquiring associates.

**Acquired assets – treating the previous carrying amount as deemed cost under IFRS**

The Board should explain in the body of the Standard the proposed interaction between paragraphs 20-21 and paragraph 11(a), with regard to the treatment of previously unrecognised intangible assets on first-time implementation of IFRS (such as acquired Research and Development). If paragraph 20(a) means that the deemed cost of such intangible assets is nil, the Board should state this explicitly.

For other assets, the carrying amount under previous GAAP might not give rise to a relevant measure of deemed cost under IFRS, because the operation of paragraphs 11 and 20 result in a liability being assigned a value on the transition balance sheet, without giving rise to a related asset. For example, in certain jurisdictions assets leased under a finance lease are not recognised because national GAAP requires legal title to pass to the lessee before such recognition is required. On conversion to IFRS, paragraph 20(a) would require entities to retain a deemed cost of zero for any such assets or liabilities that were acquired as part of an earlier business combination – thereby effectively grandfathering previously unrecognised finance leases, but only if they were acquired as part of a business combination. Under paragraph 11(a), the previously unrecognised leasing liability would be recognised as at the date of transition, with the associated debit being taken directly to equity. The analysis is further confused in considering how these requirements interact with paragraph IG11 in the Implementation Guidance. This would require the lease to be reclassified at the transition date as a finance lease and an asset to be recognised. The Board should clarify whether it requires unrecognised finance leases that were acquired in a business combination:

1. To be accounted for at a deemed cost of zero in accordance with paragraph 21; or
2. To be recognised in accordance with the requirements of paragraph IG11.

Furthermore, we do not believe that the FTA Standard is clear and specific enough about how previously unrecognised deferred tax assets and liabilities should be dealt with.

**Testing goodwill for impairment as at the date of transition**

Paragraph 20(b) should make it clear that the “resulting impairment loss” is taken to equity as at the date of transition. Otherwise, some could interpret, “the entity shall apply IAS 36” to mean that the loss should be taken to the income statement. It would also help if an example in Appendix B demonstrated the recognition of such impairment losses.



**Goodwill taken to equity under previous GAAP**

The prescribed treatment of goodwill that under previous GAAP was written off directly to equity should be set out here and not left to the examples. Currently, the statement that neither the goodwill nor any unrecognised intangible assets are reinstated is only set out in Example 4 of Appendix B. It would be better if Appendix B, being “an integral part of the [draft] IFRS” were actually incorporated within the body of the IFRS.

Paragraph 20(c) should be inserted to prescribe the treatment of such goodwill on the subsequent disposal of the business to which it relates. Whilst in principle we believe that such goodwill should be recycled through the income statement upon disposal, we concede that the practical difficulties surrounding identification preclude this from being made mandatory.

**Unrecognised assets, liabilities and costs under IAS 19 *Employee Benefits***

Paragraph 22 does not prescribe the treatment for other differences, such as unrecognised past service costs. We suggest that the following text should be inserted, based on paragraph 155 of IAS 19.

“If the transitional asset or liability is more than the asset or liability that would have been recognised at the same date under the entity’s previous accounting policy, the entity should recognise any change in the carrying amount against retained earnings.”

**Cumulative translation differences**

Paragraph 23 does not appear to address the situation where an entity is not able to determine which part of the total cumulative translation difference relates to which subsidiary. We believe that the Board should require entities in such cases to reset the cumulative translation difference to zero, which would be in accordance with the transitional provisions of IAS 21.

**Creating further exemptions – prior derecognition transactions under IAS 39 (revised)**

As a general principle we agree that the transitional requirements in IFRS are not relevant to first-time adopters (paragraph 9). Consequently, we agree with the statement in paragraph IG43, “An entity recognises all financial assets and financial liabilities (including derivatives) that qualify for recognition under IAS 39 and have not yet qualified for derecognition under IAS 39”.

However, we have noted that paragraph 171B of the Exposure Draft on the Proposed Amendments to IAS 39 would require entities to reinstate financial assets from earlier transactions that do not meet the new derecognition criteria. If the final version of the revised IAS 39 contains any limited exemptions from this requirement, we believe that a similar exemption should be available to first-time adopters.

**Designation of hedges by entities presenting two years’ comparatives in their first IFRS financial statements**

Paragraph 24 requires an entity to “apply the hedging requirements of IAS 39 *Financial Instruments: Recognition and Measurement* prospectively from the date of transition”. Under paragraph 7, the entity should apply the version of IAS 39 effective at the reporting date for its first IFRS financial statements. Some entities may be required to present two years’ comparative information in their financial statements. If converting to IFRS in December 2005, the date of transition would fall in December 2002.

**Appendix (continued)**

Until the revised version of IAS 39 is published in its final form, the Board should allow entities to use the designation and documentation requirements of IAS 39 as it applies on the date of transition.

**“Hidden” exemptions in the Implementation Guidance**

When the Board proposes additional exemptions from the general principle set out in paragraph 7, these should be set out in the body of the Standard rather than in the Implementation Guidance.

For example, sections of the draft Implementation Guidance refer situations that “may involve undue cost or effort” that are not set out in the body of the FTA Standard. These paragraphs comprise paragraphs IG21-22 on the application of IAS 23 *Borrowing Costs* in determining cost-based measurements and paragraph IG26 on the impact of past hyperinflation on the measurement of items of property, plant and equipment.

**QUESTION 3**

*Paragraphs 28-37 of the proposed IFRS deal with presentation and disclosure requirements (see also paragraphs BC90-BC97). Are all of these disclosures appropriate? Should the Board require any further disclosures or eliminate or amend any of the proposed disclosure requirements? If so, why?*

We agree that entities should provide an explanation of the effect of the transition, including the reconciliation of equity and of profit and loss, and disclosures regarding the reversal of previous impairments. However, the body of the Standard should prescribe the detail required in these reconciliations, where this information should be disclosed and examples should be given in the Implementation Guidance. In our opinion the disclosures are appropriate, subject to the amendments suggested below.

**Reconciling more than one previous version of GAAP to IFRS**

Paragraph 3(a) acknowledges that an entity might present two sets of financial statements under different accounting principles, and in our response to Question 1 we referred to the possibility of neither version complying with IFRS.

The Board should clarify how such entities would satisfy the requirements of paragraphs 30–35. In particular the Board should clarify whether or not such an entity should present a reconciliation to explain the transition to IFRS from each version of GAAP used in previous financial statements.

**The format of the reconciliation of the entity’s equity**

The Board should clearly define the form and content of the reconciliation of equity and provide examples in the Implementation Guidance on what constitutes “sufficient detail” for the narrative disclosures required in paragraph 32. This is particularly important as at the date of transition because the FTA Standard “does not require an entity to present its opening IFRS balance sheet in its first IFRS financial statements” (paragraph 10).

Paragraph 32 should require a tabular format to be presented in the notes to the financial statements. Each material variation between a line appearing on the balance sheet and the

**Appendix (continued)**

amounts determined under previous GAAP should be described and quantified as a separate reconciling item. A possible format for the table could be as follows:

	Changes in accounting policies	Changes in estimates	Correction of errors	Total
Equity as at 31 December 2003, as previously reported under National GAAP				
<b>Balances restated on conversion to IFRS</b>				
<i>Goodwill</i>				
<i>Other intangible assets</i>				
<i>Property, plant and equipment</i>				
Equity as at 1 January 2004, as restated under IFRS				

A narrative description should be required for each variation and reclassification disclosed in the table. The narrative should also highlight items in the IFRS balance sheet that were not recognised in the most recent previous financial statements.

Our concern is that, as the FTA Standard is currently drafted, there exists the risk that companies will publish “boilerplate” narrative under paragraph 30, and merely provide abbreviated equity reconciliations under paragraph 31(a), which might fail to explain and clarify significant restatements.

In addition, the last sentence of paragraph 32 should read, “An entity shall also explain and quantify the material adjustments to the cash flow statement.”

**The date of transition, the latest period presented under previous GAAP and the date of the first IFRS financial statements**

The Board should provide an example that clarifies the requirements of paragraph 31, particularly with regards to the dates as at which each of the required reconciliations would be presented. This would be consistent with the Board’s decision to present an example after paragraph 8.

**Disclosures relating to “undue cost or effort”**

The Board should explain why an entity is required to justify its determination of “undue cost or effort” only in the case of it using fair value as deemed cost, and not in support of the exemption granted under paragraph 23 of the Standard. The requirement should exist for both exemptions or for neither.

**Historical summaries**

In order to avoid confusion, paragraph 36 should be replaced with a statement that historical information should not be presented within the financial statements unless they are IFRS compliant for periods before the transition date. The ability of a user of accounts to identify trends in performance would be impaired if, for example, two years’ information prepared under IFRS were presented alongside a number of prior years’ data under national GAAP. We do not believe that the additional disclosures suggested in paragraph 36 would mitigate this deficiency.

**QUESTION 4**

*Do you have any other comments on the Exposure Draft?*

**Completeness of the draft Implementation Guidance**

The Board should explain why the Implementation Guidance does not cover all extant IFRS and IFRIC interpretations.

For example, the interaction between the FTA Standard and SIC-12, *Consolidation – Special Purpose Entities*, is not considered. It might be appropriate to provide transitional provisions on the measurement of acquired assets and liabilities for entities that are consolidating certain special purposes entities for the first time (because they were excluded from consolidation under national GAAP). Similar considerations might apply in terms of the interaction between the FTA Standard and IAS 27 or IAS 28.

**Paragraph 11 and the requirement to review past transactions**

The Board explains in paragraphs BC18-21 that it does not propose to limit the “look back” period required for a first-time adopter to investigate transactions that occurred before the date of transition to IFRS.

Therefore, the Implementation Guidance should explain how the Board would expect entities to apply retrospectively the revenue recognition criteria in IAS 18. In particular, examples should be given where a transaction before the date of transition did not meet all of the criteria under paragraph 14 of IAS 18, such that an entity would record an asset or liability in its transition date balance sheet under IFRS (when under its national GAAP it had derecognised the asset and recorded income on the transaction).

In paragraph BC21, the Board states that it has rejected other precedents for transitional provisions on the basis that to do so would not be consistent with the June 2002 Exposure Draft of Proposed Amendments to IAS 39. That Exposure Draft would require an entity to review all previous transactions that involved derecognition of a financial asset, to apply the criteria under the amended IAS 39 and to determine whether the financial asset should be reinstated. Therefore, the FTA Standard should require the same treatment in respect of past derecognition of a non-financial asset that did not meet the criteria for revenue recognition under IFRS.

**Measurement of available-for-sale financial assets at the date of transition**

Paragraph BC55 states, “the Board concluded that it should treat first-time adopters in the same way as entities that already apply IFRSs by requiring retrospective application”. However, paragraph IG49 suggests a difference in the treatment of first-time adopters in the way that subsequent gains and losses would be measured in the income statement.

An entity that records an adjustment to the carrying value of available-for-sale financial assets at the date of transition is required to take any difference to a separate component of equity and transfer it to the income statement when the asset is later derecognised or impaired.

A first-time adopter that had previously revalued available-for-sale assets in a manner consistent with IFRS would record no such adjustment. In the absence of guidance on how equity or its components should be reclassified on first-time application, such an entity may record a different gain or loss in its income statement when the asset is eventually derecognised or impaired.

**Appendix** (continued)

The Board should either remove the requirement for first-time adopters only to establish this separate component of equity for any adjustment on date of transition (to later recycle these differences through the income statement), or require all entities to determine the cumulative gain or loss (against cost) as at the date of transition and record this as a separate component of equity.

**Bold text, “main principles” and the application of paragraph 14 of the Preface to IFRS**

It is not clear how the Board has applied paragraph 14 of the Preface to International Financial Reporting Standards in determining which elements of the FTA Standard denote “main principles” and should therefore be shown in bold text.

For example, it is not clear why paragraph 10 is not in bold, given that the preparation of an opening IFRS balance sheet should constitute a “main principle” of a standard on first-time application.

**IFRS vs. IFRSs**

Throughout the document there are references to both “IFRS” and “IFRSs”. However, it is not always clear why one is used and not the other. For example, paragraph 29 uses both versions.

There is no logic to the use of “IFRS” first and “IFRSs” at the end of the same sentence. We note that there seemed to be no need before to talk about “IASs” and so we question the requirement now for “IFRSs”.

We suggest that the definition of the term “IFRS” should be changed in the Glossary, such that it becomes a collective noun that can be used in both the singular and plural.