Project **Amendments to IFRS 1**

Topic **Analysis of comment letters received on exposure draft *Removal of Fixed Dates for First-time Adopters***

Introduction

1. This agenda paper summarises the staff's analysis of the comment letters received on the exposure draft *Removal of Fixed Dates for First-time Adopters,* published in August 2010. This paper includes:
   (a) **background of the issue**;
   (b) a **summary background of the respondents**;
   (c) **analysis of specific comments** including staff recommendations; and
   (d) **discussion of the effective date.**

Background of the issue

2. During 2009 and 2010, the IFRS Interpretations Committee received requests to replace the fixed date of 1 January 2004 with 'the date of transition to IFRSs' in the following paragraphs of IFRS 1 *First-time Adoption of International Reporting Standards*:
   (a) in paragraph B2 (relating to the derecognition exception), and
   (b) in paragraph D20 (relating to the fair value measurement of financial assets or financial liabilities at initial recognition / "day 1 differences").
3. The date of 1 January 2004 was originally included in both paragraphs B2 and D20 as a result of the revision to IAS 39 *Financial Instruments: Recognition*

and Measurement in 2003, in order to place entities then adopting IFRS for the first time in the same position as existing IFRS preparers at that time. However, as time passes, the transition date of 1 January 2004 that is 'hard-wired' into the standard becomes more remote from the date that a number of jurisdictions will adopt IFRSs.

4. In response to this issue, the Board decided to publish an exposure draft *Removal of Fixed Dates for First-time Adopters* in August 2010, with a 60-day comment period so that the relief may be available in time for those jurisdictions that are planning to adopt IFRSs in the near future.

5. The comment letter period of the exposure draft ended on 27 October 2010. The comment letter analysis is presented below.

Summary background of the respondents

6. A total of 34 comment letters were received on the exposure draft *Removal of Fixed Dates for First-time Adopters*. A breakdown of the demographic information on the respondents is provided in Appendix A.

Analysis of specific comments

7. All the comment letters received supported the proposed amendment to IFRS 1. There were ancillary comments made in some of the letters. All comments received were considered by the staff, and the comments most relevant to the issue are included below, as follows:

   (a) Removal of other fixed dates in IFRS 1 (paragraphs 8 – 9),

   (b) Increased relevance of paragraph B3 of IFRS 1 (paragraphs 10 – 16), and

   (c) Querying the meaning of 'in other words' in the second sentence of paragraph B2 of IFRS 1 (paragraphs 17 – 19).

Removal of other fixed dates in IFRS 1

8. Two comment letters[1] noted other fixed dates in IFRS 1, in paragraphs D2 and D3, concerning share-based payment transactions. The letters state that since these dates become less relevant as time passes, they should also be removed.

9. The staff notes that paragraphs D2 and D3 are outside the scope of this exposure draft. In addition, the staff is not aware that these fixed dates are causing difficulties in practice, and recommends that no action is taken in respect of these comments.

Increased relevance of paragraph B3 of IFRS 1

10. Paragraph B3 permits an entity to retrospectively apply the derecognition principles in IAS 39. One respondent[2] states that:

> 'due to the proposed amendment to paragraph B2, paragraph B3 will be more relevant for first-time adopters wishing to apply [IAS 39] retrospectively.'

11. Currently, paragraph B2 requires retrospective application of the derecognition principles, back to 1 January 2004. However, if paragraph B2 is amended as proposed, this will no longer be the case, and an entity will have to apply paragraph B3 if it chooses to retrospectively apply derecognition principles prior to its date of transition to IFRSs.

12. In order for an entity to be able to apply paragraph B3, the information it needs to apply the principles of IAS 39 to financial assets and liabilities derecognised as a result of past transactions must have been 'obtained at the time of initially accounting for those transactions.' The concern raised in the letter is that the entity may not have gathered the necessary information required at the time, and is therefore prevented from applying paragraph B3.

13. The respondent therefore suggests amending paragraph B3 to state that it can be applied 'provided the information required…can be reliably determined',

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[1] Grant Thornton and Accounting Standards Committee of Germany (DRSC)
[2] Ernst & Young

thereby removing the need for the information to have been gathered at the time the transactions were initially accounted for.

14. When entities have applied paragraph B2 up to now, they might have used hindsight in order to obtain the information required to restate any derecognition transactions that occurred between 1 January 2004 and the entity's date of transition to IFRSs. This was an unavoidable by-product of the fixed date issue.

15. However, use of hindsight was the Board's main concern when paragraph B3 was originally worded, as BC 22B of IFRS 1 states:

> 'The Board also noted that financial statements that include financial assets and financial liabilities that would otherwise be omitted under the provisions of the IFRS would be more complete and therefore more useful to users of financial statements. The Board therefore decided to permit retrospective application of the derecognition requirements. It also decided that retrospective application should be limited to cases when the information needed to apply the IFRS to past transactions was obtained at the time of initially accounting for those transactions. This limitation prevents the unacceptable use of hindsight.'

16. The staff think that changing the wording of paragraph B3 to that the respondent suggests will not sufficiently mitigate the risk of using hindsight. If the fixed date in paragraph B2 is replaced with 'date of transition to IFRSs' as proposed, the staff thinks that the wording of B3 should remain as it is. The staff therefore recommend no action in respect of this comment.

Querying the meaning of 'in other words' in the second sentence of paragraph B2

17. A respondent[3] is querying some of the existing wording in paragraph B2. The second sentence of paragraph B2 states:

> 'In other words, 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 before [the date of transition to IFRSs], it shall not recognise those assets and liabilities in accordance with

[3] KPMG

> IFRSs (unless they qualify for recognition as a result of a later transaction or event).'

The respondent states that it is not clear what 'in other words' means. It states that:

> 'It is not clear from the current wording whether the exemption [B2] also is meant to deal with the converse situation, i.e. that the exemption equally is applicable to derecognition transactions in which the entity previously concluded that relevant assets and/or liabilities should not be derecognised, but IAS 39 would require derecognition. Dealing with one type of transaction only seems the sentence should rather be starting with a "For example,…". We suggest that the paragraph either deals with both types of transactions or that the current sentence be rewritten as an example.'

18. The staff thinks that the wording in the first sentence of paragraph B2 is clear, in that a first-time adopter is not permitted to apply the IAS 39 derecognition guidance to earlier transactions (unless paragraph B3 is applied). The staff thinks that paragraph B2 is therefore clear that it applies to both:

    (i) Financial assets or liabilities recognised under previous GAAP, but which would have been derecognised under IAS 39, and

    (ii) Financial assets or liabilities derecognised under previous GAAP, but which would not have been derecognised under IAS 39.

19. The staff therefore thinks that the second sentence of paragraph B2 is providing an example. However, the staff thinks that because the first sentence of paragraph B2 is clear, no amendment is needed to the second sentence.

Question 1 – comment analysis
Does the Board agree with the staff that no action should be taken in respect of the comments discussed above?

Effective Date

20. A respondent[4] requests that:

> 'since entities in Brazil are in the process of conversion to IFRS in 2010, we would strongly recommend to the Board that the approval of the amendments comes to light before the end of December 2010 and effective date of this ED to annual periods beginning on or after 1 January 2010.'

21. The staff does not recommend that the effective date be a date in the past. This is because jurisdictions that incorporate IFRSs into law advise us that they can only do so on a prospective basis, so the effective date is required to be a future date.

22. However, the staff thinks that situations similar to that described will be assisted if the Board retains the proposal in the exposure draft to permit early adoption of this amendment.

23. The staff therefore recommends that the final amendment be effective for annual periods beginning on or after 1 July 2011, so that the relief may be available in time for those jurisdictions that are planning to adopt IFRSs in the near future. The staff also recommend that earlier adoption is permitted.

Authorisation to proceed

24. The staff propose the draft wording of the final amendment in Appendix B.

Question 2 – Authorisation to proceed with drafting and to ballot
Does the Board approve the staff to proceed with this proposed amendment including finalisation of drafting and a ballot to be provided to the Board for finalisation of this project?

[4] Brazilian Standard Setter (CPC)

Appendix A – Demographic information of respondents

A1. This Appendix provides demographic information on the respondents to the exposure draft *Removal of Fixed Dates for First-time Adopters* published in August 2010. The table below contains a full list of respondents to the exposure drafts, categorised the respondents by type and geography.

LIST OF RESPONDENTS

CL#	Respondent	Respondent type	Geography
1	Chris Barnard	Other/Individual	Unknown
2	Linus Low	Other/Individual	Unknown
3	Accounting Standards Board UK	Standard Setter	UK
4	PricewaterhouseCoopers	Accounting firm	International
5	Dutch Accounting Standards Board (DASB)	Standard Setter	The Netherlands
6	CitiBank	Preparer	US/UK
7	International Organisation of Securities Commissions (IOSCO)	Regulator	International
8	Accounting Standards Council (ASC)	Standard Setter	Singapore
9	The Institute of Certified Public Accountants in Ireland (CPA)	Standard Setter	Ireland
10	Grant Thornton International	Accounting firm	International
11	Deloitte	Accounting firm	International
12	BDO	Accounting firm	International
13	Hong Kong Institute of Certified Public Accountants	Standard Setter	Hong Kong
14	Institute for the Accountancy Profession in Sweden (FAR)	Standard Setter	Sweden
15	Mazars	Accounting firm	International
16	Credit Suisse	Preparer	Switzerland
17	Malaysian Accounting Standards Board (MASB)	Standard Setter	Malaysia
18	Ernst & Young	Accounting firm	International
19	Chartered Accountants Ireland	Standard Setter	Ireland
20	Accounting Standards Committee of Germany (DRSC)	Standard Setter	Germany
21	The South African Institute of Chartered Accountants (SAICA)	Standard Setter	South Africa
22	Norwegian Accounting Standards Board	Standard Setter	Norway

CL#	Respondent	Respondent type	Geography
23	Canadian Bankers' Association (CBA)	Preparer representative organisation	Canada
24	Financial Executives International (FEI) Canada	Preparer representative organisation	Canada
25	Financial Executives International (FEI)	Preparer representative organisation	United States
26	Institute of Chartered Accountants in England and Wales (ICAEW)	Standard Setter	UK
27	International Association of Consultants, Valuators and Analysts (IACVA)	Preparer representative organisation	International
28	Accounting Standards Board of Canada (AcSB)	Standard Setter	Canada
29	Bradley Roy and Donald Clarke	Other/Individual	Unknown
30	Brazilian Standard Setter (CPC)	Standard Setter	Brazil
31	Italian Standard Setter (OIC)	Standard Setter	Italy
32	KPMG	Accounting firm	International
33	Zambian Institute of Chartered Accountants	Standard Setter	Zambia
34	European Financial Reporting Advisory Group (EFRAG)	Standard Setter	Europe

Appendix B – Draft wording of the final amendment

B1 The staff proposes draft wording for the final amendment. This appendix shows the proposed draft wording as compared to the current version of IFRS 1. Proposed changes from the current standard are shown as follows: new text is underlined and deleted text is struck through. The final amendment will not include any underlining or strike throughs.

B2 All Board edits/comments are appreciated in preparation for the final amendment balloting.

Amendments to IFRS 1 *First-time Adoption of International Financial Reporting Standards*

Appendix B

Exceptions to the retrospective application of other IFRSs

Paragraph B2 is 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*[5] prospectively for transactions occurring on or after ~~1 January 2004~~ the date of transition to IFRSs. In other words, 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 before ~~1 January 2004~~ the date of transition to IFRSs, 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).

Appendix D

Exemptions from other IFRSs

Paragraph D20 is amended (new text is underlined and deleted text is struck through).

Fair value measurement of financial assets or financial liabilities at initial recognition

[5] References to IAS 39 should be replaced by references to IFRS 9 *Financial Instruments* if IFRS 9 has been early adopted.

D20 Notwithstanding the requirements of paragraphs 7 and 9, an entity may apply the requirements in the last sentence of IAS 39[6] paragraph AG76[6] and in paragraph AG76A[6], ~~in either of the following ways:~~ prospectively to transactions entered into on or after the date of transition to IFRSs.

~~(a) prospectively to transactions entered into after 25 October 2002; or~~
~~(b) prospectively to transactions entered into after 1 January 2004.~~

Effective date

Paragraph 39F is added.

39F *Removal of Fixed Dates for First-time Adopters* (Amendments to IFRS 1), issued in December 2010, amended paragraphs B2 and D20. An entity shall apply those amendments for annual periods beginning on or after 1 July 2011. Earlier application is permitted.

[6] References to IAS 39 should be replaced by references to IFRS 9 *Financial Instruments* if IFRS 9 has been early adopted.

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

Paragraph BC22A and BC83A are amended (new text is underlined)

BC22A The Board reconsidered this issue in completing the revision of IAS 39 in 2003. The Board decided to retain the transition requirements as set out in IFRS 1, for the reasons given in paragraph BC20. However, the Board amended the date from which prospective application was required to transactions that occur on or after 1 January 2004 in order to overcome the practical difficulties of restating transactions that had been derecognised before that date. <u>In 2010 the Board was asked to reconsider whether 1 January 2004 is the appropriate date from which a first-time adopter should be required to restate past derecognition transactions. Constituents were concerned that, as time passes, the fixed transition date of 1 January 2004 becomes more remote and increasingly less relevant to the financial reports as additional jurisdictions adopt IFRSs. The Board accepted that the cost of reconstructing transactions back in time to 1 January 2004 was likely to outweigh the benefit to be achieved in doing so. It therefore decided to amend the fixed date of 1 January 2004 in paragraph B2 to 'the date of transition to IFRSs'.</u>

BC83A IFRS 1 originally required retrospective application of the 'day 1' gain or loss recognition requirements in IAS 39 paragraph AG76. After the revised IAS 39 was issued, constituents raised concerns that retrospective application would diverge from the requirements of US GAAP, would be difficult and expensive to implement, and might require subjective assumptions about what was observable and what was not. In response to these concerns, the Board decided to permit entities to apply the requirements in the last sentence of IAS 39 paragraph AG76 and in paragraph AG76A, in any one of the following ways:

(a) retrospectively;

(b) prospectively to transactions entered into after 25 October 2002; or

(c) prospectively to transactions entered into after 1 January 2004.

<u>In 2010, the Board decided to amend the fixed dates included in paragraph D20 of IFRS 1 to permit a first-time adopter to apply the 'day 1' gain or loss recognition requirement in IAS 39 paragraphs AG76 and AG76A prospectively from the date of transition to IFRSs, Consequently, the Board proposed that in paragraph D20(b), the date of 1 January 2004 should be amended to 'the date of transition to IFRSs', and paragraph D20(a) deleted.</u>