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Approval by the Board of IFRS 1 issued in November 2008

International Financial Reporting Standard 1 *First-time Adoption of International Financial Reporting Standards* (as revised in 2008) was approved for issue by the thirteen members of the International Accounting Standards Board.¹

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¹ Professor Barth and Mr Danjou dissented from *Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate* (Amendments to IFRS 1 and IAS 27) issued in May 2008. Their dissenting opinions are set out after the Basis for Conclusions on IAS 27.

Approval by the Board of *Additional Exemptions for First-time Adopters* (Amendments to IFRS 1) issued in July 2009

Additional Exemptions for First-time Adopters (Amendments to IFRS 1) was approved for issue by the fourteen members of the International Accounting Standards Board.

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Approval by the Board of *Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters* (Amendments to IFRS 1) issued in January 2010

Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters (Amendments to IFRS 1) was approved for issue by the fifteen members of the International Accounting Standards Board.

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Approval by the Board of *Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters* (Amendments to IFRS 1) issued in December 2010

Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters (Amendments to IFRS 1) was approved for issue by the fifteen members of the International Accounting Standards Board.

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Approval by the Board of *Government Loans* (Amendments to IFRS 1) issued in March 2012

Government Loans (Amendments to IFRS 1) was approved for issue by the fourteen members of the International Accounting Standards Board.

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

This Basis for Conclusions accompanies, but is not part of, IFRS 1.

In this Basis for Conclusions the terminology has not been amended to reflect the changes made by IAS 1 Presentation of Financial Statements (as revised in 2007).

This Basis for Conclusions has not been revised to reflect the restructuring of IFRS 1 in November 2008, but cross-references have been updated.

Introduction

- BC1 This Basis for Conclusions summarises the International Accounting Standards Board's considerations in reaching the conclusions in IFRS 1 *First-time Adoption of International Financial Reporting Standards*. Individual Board members gave greater weight to some factors than to others.
- BC2 SIC-8 *First-time Application of IASs as the Primary Basis of Accounting*, issued in 1998, dealt with matters that arose when an entity first adopted IASs. In 2001, the Board began a project to review SIC-8. In July 2002, the Board published ED 1 *First-time Application of International Financial Reporting Standards*, with a comment deadline of 31 October 2002. The Board received 83 comment letters on ED 1. IFRS 1 was issued by the Board in June 2003.
- BC2A IFRS 1 replaced SIC-8. The Board developed the IFRS to address concerns that:
- some aspects of SIC-8's requirement for full retrospective application caused costs that exceeded the likely benefits for users of financial statements. Moreover, although SIC-8 did not require retrospective application when this would be impracticable, it did not explain whether a first-time adopter should interpret impracticability as a high hurdle or a low hurdle and it did not specify any particular treatment in cases of impracticability.
 - SIC-8 could require a first-time adopter to apply two different versions of a standard if a new version were introduced during the periods covered by its first financial statements prepared under IASs and the new version prohibited retrospective application.
 - SIC-8 did not state clearly whether a first-time adopter should use hindsight in applying recognition and measurement decisions retrospectively.
 - there was some doubt about how SIC-8 interacted with specific transitional provisions in individual standards.
- BC2B Like SIC-8, IFRS 1 requires retrospective application in most areas. Unlike SIC-8, it:
- includes targeted exemptions to avoid costs that would be likely to exceed the benefits to users of financial statements, and a small number of other exceptions for practical reasons.
 - clarifies that an entity applies the latest version of IFRSs.
 - clarifies how a first-time adopter's estimates in accordance with IFRSs relate to the estimates it made for the same date in accordance with previous GAAP.
 - specifies that the transitional provisions in other IFRSs do not apply to a first-time adopter.
 - requires enhanced disclosure about the transition to IFRSs.
- BC3 The project took on added significance because of the requirement for listed European Union companies to adopt IFRSs in their consolidated financial statements from 2005. Several other countries announced that they would permit or require entities to adopt IFRSs in the next few years. Nevertheless, the Board's aim in developing the IFRS was to find solutions that would be appropriate for any entity, in any part of the world, regardless of whether adoption occurs in 2005 or at a different time.

Restructuring of the IFRS

- BC3A Since it was issued in 2003, IFRS 1 has been amended many times to accommodate first-time adoption requirements resulting from new or amended IFRSs. Because of the way IFRS 1 was structured, those

amendments made the IFRS more complex and less clear. As more amendments become necessary, this problem will become worse.

- BC3B As part of its improvements project in 2007, therefore, the Board proposed to change the structure of IFRS 1 without amending its substance. Respondents to the exposure draft published in October 2007 supported the restructuring. The revised structure of the IFRS issued in November 2008 is easier for the reader to understand and is better designed to accommodate future changes. The focus of the restructuring was to move to appendices all specific exemptions and exceptions from the requirements of IFRSs. Exemptions are categorised into business combinations, exemptions and short-term exemptions. Exemptions are applicable to all first-time adopters regardless of their date of transition to IFRSs. Short-term exemptions are those exemptions applicable to users for a short time. Once those exemptions have become out of date, they will be deleted.

Scope

- BC4 The IFRS applies to an entity that presents its first IFRS financial statements (a first-time adopter). Some suggested that an entity should not be regarded as a first-time adopter if its previous financial statements contained an explicit statement of compliance with IFRSs, except for specified (and explicit) departures. They argued that an explicit statement of compliance establishes that an entity regards IFRSs as its basis of accounting, even if the entity does not comply with every requirement of every IFRS. Some regarded this argument as especially strong if an entity previously complied with all recognition and measurement requirements of IFRSs, but did not give some required disclosures—for example, segmental disclosures that IAS 14 *Segment Reporting*² requires or the explicit statement of compliance with IFRSs that IAS 1 *Presentation of Financial Statements* requires.
- BC5 To implement that approach, it would be necessary to establish how many departures are needed—and how serious they must be—before an entity would conclude that it has not adopted IFRSs. In the Board’s view, this would lead to complexity and uncertainty. Also, an entity should not be regarded as having adopted IFRSs if it does not give all disclosures required by IFRSs, because that approach would diminish the importance of disclosures and undermine efforts to promote full compliance with IFRSs. Therefore, the IFRS contains a simple test that gives an unambiguous answer: an entity has adopted IFRSs if, and only if, its financial statements contain an explicit and unreserved statement of compliance with IFRSs (paragraph 3 of the IFRS).
- BC6 If an entity’s financial statements in previous years contained that statement, any material disclosed or undisclosed departures from IFRSs are errors. The entity applies IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* in correcting them.

Repeated application of IFRS 1

- BC6A In *Annual Improvements 2009–2011 Cycle* (issued in May 2012) the Board addressed a request to clarify whether an entity may apply IFRS 1:
- (a) if the entity meets the criteria for applying IFRS 1 and has applied IFRS 1 in a previous reporting period; or
 - (b) if the entity meets the criteria for applying IFRS 1 and has applied IFRSs in a previous reporting period when IFRS 1 did not exist.

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.

- BC6B The Board noted that the scope of IFRS 1 focuses on whether an entity’s financial statements are its first IFRS financial statements (a term defined in Appendix A). If an entity’s financial statements meet the definition of ‘first IFRS financial statements’, the entity is required to apply IFRS 1 in accordance with paragraph 2(a). However, use of the term ‘first’ raises the question whether IFRS 1 can be applied more than once.
- BC6C In the June 2011 exposure draft the Board proposed to clarify that an entity is required to apply IFRS 1 when the entity’s most recent previous annual financial statements do not contain an explicit and unreserved statement of compliance with IFRSs, even if the entity has applied IFRS 1 in a reporting period before the period reported in the most recent previous annual financial statements. However, in the light of respondents’ comments on the June 2011 exposure draft, the Board decided that an entity that meets the criteria for applying IFRS 1 and that has applied IFRSs in a previous reporting period (regardless of whether it used IFRS 1 or

² In 2006 IAS 14 was replaced by IFRS 8 *Operating Segments*.

SIC--8 *First-Time Application of IASs*, if either, when previously adopting) may choose to apply IFRS 1 when it re-adopts IFRSs. The Board decided that the entity should be allowed, rather than required, to apply IFRS 1 because, as explained in paragraph IN5 of IFRS 1, IFRS 1 grants limited exemptions from some requirements of IFRSs on the assumption that the cost of complying with some IFRSs would be likely to exceed the benefits to users of financial statements. However, the costs of applying IFRSs in full might not exceed the benefits of doing so for an entity that had previously applied IFRSs. Consequently, the Board concluded that an entity returning to IFRSs might determine that the benefits of applying IFRSs as if it had continued to do so without interruption would exceed the costs of preparing such information, and that an entity should not be prohibited from following that approach. In applying such an approach, an entity should apply IFRSs retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* as if the entity had never stopped applying IFRSs. The Board noted that hindsight is not applied by an entity in preparing IFRS financial statements, whether that entity is applying IFRS 1, or whether that entity applies IFRSs retrospectively as if the entity had never stopped applying them in accordance with IAS 8. The Board noted that paragraphs 14–17 of IFRS 1 and paragraph 53 of IAS 8 provide guidance in this regard.

- BC6D The Board also noted that, in accordance with paragraph 2 of IFRS 1, an entity that has never applied IFRSs in the past would continue to be required to apply IFRS 1 in its first IFRS financial statements.
- BC6E The Board also decided that the entity shall disclose the reason why it stopped applying IFRSs and the reason why it is resuming reporting in accordance with IFRSs. The Board thinks that this disclosure requirement provides users with useful information and would discourage the intentional omission of the statement of compliance with IFRSs solely to allow an entity to take advantage of the exemptions in IFRS 1. The Board also decided that an entity that does not elect to apply IFRS 1 shall explain the reasons why it has elected to apply IFRSs as if it had never stopped applying them. The Board believes that this disclosure ensures that useful information will be provided to users.

Basic concepts

Useful information for users

- BC7 In developing recognition and measurement requirements for an entity's opening IFRS balance sheet, the Board referred to the objective of financial statements, as set out in the *Framework for the Preparation and Presentation of Financial Statements*. The *Framework*³ states that the objective of financial statements is to provide information about the financial position, performance and changes in financial position of an entity that is useful to a wide range of users in making economic decisions.
- BC8 The *Framework* identifies four qualitative characteristics that make information in financial statements useful to users. In summary, the information should be:
- (a) readily understandable by users.
 - (b) relevant to the decision-making needs of users.
 - (c) reliable, in other words financial statements should:
 - (i) represent faithfully the transactions and other events they either purport to represent or could reasonably be expected to represent;
 - (ii) represent transactions and other events in accordance with their substance and economic reality and not merely their legal form;
 - (iii) be neutral, that is to say, free from bias;
 - (iv) contend with the uncertainties that inevitably surround many events and circumstances by the exercise of prudence; and
 - (v) be complete within the bounds of materiality and cost.
 - (d) comparable with information provided by the entity in its financial statements through time and with information provided in the financial statements of other entities.

³ References to the *Framework* in this Basis for Conclusions are to the IASC's *Framework for the Preparation and Presentation of Financial Statements*, adopted by the Board in 2001 and in effect when the Standard was developed.

Comparability

- BC9 The previous paragraph notes the need for comparability. Ideally, a regime for first-time adoption of IFRSs would achieve comparability:
- (a) within an entity over time;
 - (b) between different first-time adopters; and
 - (c) between first-time adopters and entities that already apply IFRSs.
- BC10 SIC-8 gave priority to ensuring comparability between a first-time adopter and entities that already applied IASs. It was based on the principle that a first-time adopter should comply with the same standards as an entity that already applied IASs. However, the Board decided that it is more important to achieve comparability over time within a first-time adopter's first IFRS financial statements and between different entities adopting IFRSs for the first time at a given date; achieving comparability between first-time adopters and entities that already apply IFRSs is a secondary objective.

Current version of IFRSs

- BC11 Paragraphs 7–9 of the IFRS require a first-time adopter to apply the current version of IFRSs, without considering superseded or amended versions.⁴ This:
- (a) enhances comparability, because the information in a first-time adopter's first IFRS financial statements is prepared on a consistent basis over time;
 - (b) gives users comparative information prepared using later versions of IFRSs that the Board regards as superior to superseded versions; and
 - (c) avoids unnecessary costs.
- BC11A Paragraph 7 requires an entity to use the IFRSs that are effective at the end of its first IFRS reporting period. Paragraph 8 allows a first-time adopter to apply a new IFRS that is not yet mandatory if that IFRS permits early application. Notwithstanding the advantages, set out in paragraph BC11, of applying a more recent version of an IFRS, paragraphs 7–8 permit an entity to use either the IFRS that is currently mandatory or the new IFRS that is not yet mandatory, if that new IFRS permits early application. Paragraph 7 requires an entity to apply the same version of the IFRS throughout the periods covered by the entity's first IFRS financial statements. Consequently, if a first-time adopter chooses to early apply a new IFRS, that new IFRS will be applied throughout all the periods presented in its first IFRS financial statements on a retrospective basis, unless IFRS 1 provides an exemption or an exception that permits or requires otherwise.
- BC12 In general, the transitional provisions in other IFRSs do not apply to a first-time adopter (paragraph 9 of the IFRS). Some of these transitional provisions require or permit an entity already reporting in accordance with IFRSs to apply a new requirement prospectively. These provisions generally reflect a conclusion that one or both of the following factors are present in a particular case:
- (a) Retrospective application may be difficult or involve costs exceeding the likely benefits. The IFRS permits prospective application in specific cases where this could occur (paragraphs BC30–BC73).
 - (b) There is a danger of abuse if retrospective application would require judgements by management about past conditions after the outcome of a particular transaction is already known. The IFRS prohibits retrospective application in some areas where this could occur (paragraphs BC74–BC84).
- BC13 Some have suggested three further reasons for permitting or requiring prospective application in some cases:
- (a) to alleviate unforeseen consequences of a new IFRS if another party uses financial statements to monitor compliance with a contract or agreement. However, in the Board's view, it is up to the parties to an agreement to determine whether to insulate the agreement from the effects of a future IFRS and, if not, how they might renegotiate it so that it reflects changes in the underlying financial condition rather than changes in reporting (paragraph 21⁵ of the *Preface to International Financial Reporting Standards*).
 - (b) to give a first-time adopter the same accounting options as an entity that already applies IFRSs. However, permitting prospective application by a first-time adopter would conflict with the Board's primary objective of comparability within an entity's first IFRS financial statements (paragraph BC10). Therefore, the Board did not adopt a general policy of giving first-time adopters the same accounting

⁴ *Annual Improvements Cycle 2011–2013* clarified that this paragraph does not require an entity to use a more recent version of an IFRS. It only explains the advantages of applying a more recent version of an IFRS. See paragraph BC11A for further details.

⁵ Amended to paragraph 13 when the *Preface to IFRS Standards* was revised and renamed in December 2018.

options of prospective application that existing IFRSs give to entities that already apply IFRSs. Paragraphs BC20–BC23 discuss one specific case, namely derecognition of financial assets and financial liabilities.

- (c) to avoid difficult distinctions between changes in estimates and changes in the basis for making estimates. However, a first-time adopter need not make this distinction in preparing its opening IFRS balance sheet, so the IFRS does not include exemptions on these grounds. If an entity becomes aware of errors made under previous GAAP, the IFRS requires it to disclose the correction of the errors (paragraph 26 of the IFRS).
- BC14 The Board will consider case by case when it issues a new IFRS whether a first-time adopter should apply that IFRS retrospectively or prospectively. The Board expects that retrospective application will be appropriate in most cases, given its primary objective of comparability over time within a first-time adopter's first IFRS financial statements. However, if the Board concludes in a particular case that prospective application by a first-time adopter is justified, it will amend the IFRS on first-time adoption of IFRSs. As a result, IFRS 1 will contain all material on first-time adoption of IFRSs and other IFRSs will not refer to first-time adopters (except, when needed, in the Basis for Conclusions and consequential amendments).
- BC15 Under the proposals in ED 1, a first-time adopter could have elected to apply IFRSs as if it had always applied IFRSs. This alternative approach was intended mainly to help an entity that did not wish to use any of the exemptions proposed in ED 1 because it had already been accumulating information in accordance with IFRSs without presenting IFRS financial statements. To enable an entity using this approach to use the information it had already accumulated, ED 1 would have required it to consider superseded versions of IFRSs if more recent versions required prospective application. However, as explained in paragraphs BC28 and BC29, the Board abandoned ED 1's all-or-nothing approach to exemptions. Because this eliminated the reason for the alternative approach, the Board deleted it in finalising the IFRS.

Opening IFRS balance sheet

- BC16 An entity's opening IFRS balance sheet is the starting point for its accounting in accordance with IFRSs. The following paragraphs explain how the Board used the *Framework* in developing recognition and measurement requirements for the opening IFRS balance sheet.

Recognition

- BC17 The Board considered a suggestion that the IFRS should not require a first-time adopter to investigate transactions that occurred before the beginning of a 'look back' period of, say, three to five years before the date of transition to IFRSs. Some argued that this would be a practical way for a first-time adopter to give a high level of transparency and comparability, without incurring the cost of investigating very old transactions. They noted two particular precedents for transitional provisions that have permitted an entity to omit some assets and liabilities from its balance sheet:
- (a) A previous version of IAS 39 *Financial Instruments: Recognition and Measurement*⁶ prohibited restatement of securitisation, transfer or other derecognition transactions entered into before the beginning of the financial year in which it was initially applied.
- (b) Some national accounting standards and IAS 17 *Accounting for Leases* (superseded in 1997 by IAS 17 *Leases*) permitted prospective application of a requirement for lessees to capitalise finance leases. Under this approach, a lessee would not be required to recognise finance lease obligations and the related leased assets for leases that began before a specified date.
- BC18 However, limiting the look back period could lead to the omission of material assets or liabilities from an entity's opening IFRS balance sheet. Material omissions would undermine the understandability, relevance, reliability and comparability of an entity's first IFRS financial statements. Therefore, the Board concluded that an entity's opening IFRS balance sheet should:
- (a) include all assets and liabilities whose recognition is required by IFRSs, except:
- (i) some financial assets or financial liabilities derecognised in accordance with previous GAAP before the date of transition to IFRSs (paragraphs BC20–BC23); and
- (ii) goodwill and other assets acquired, and liabilities assumed, in a past business combination that were not recognised in the acquirer's consolidated balance sheet in accordance with previous

⁶ IFRS 9 *Financial Instruments* replaced IAS 39. IFRS 9 applies to all items that were previously within the scope of IAS 39.

GAAP and also would not qualify for recognition in accordance with IFRSs in the balance sheet of the acquiree (paragraphs BC31–BC40).

(b) not report items as assets or liabilities if they do not qualify for recognition in accordance with IFRSs.

BC19 Some financial instruments may be classified as equity in accordance with previous GAAP but as financial liabilities in accordance with IAS 32 *Financial Instruments: Presentation*. Some respondents to ED 1 requested an extended transitional period to enable the issuer of such instruments to renegotiate contracts that refer to debt-equity ratios. However, although a new IFRS may have unforeseen consequences if another party uses financial statements to monitor compliance with a contract or agreement, that possibility does not, in the Board's view, justify prospective application (paragraph BC13(a)).

Derecognition in accordance with previous GAAP

BC20 An entity may have derecognised financial assets or financial liabilities in accordance with its previous GAAP that do not qualify for derecognition in accordance with IAS 39.⁷ ED 1 proposed that a first-time adopter should recognise those assets and liabilities in its opening IFRS balance sheet. Some respondents to ED 1 requested the Board to permit or require a first-time adopter not to restate past derecognition transactions, on the following grounds:

- (a) Restating past derecognition transactions would be costly, especially if restatement involves determining the fair value of retained servicing assets and liabilities and other components retained in a complex securitisation. Furthermore, it may be difficult to obtain information on financial assets held by transferees that are not under the transferor's control.
- (b) Restatement undermines the legal certainty expected by parties who entered into transactions on the basis of the accounting rules in effect at the time.
- (c) IAS 39 did not, before the improvements proposed in June 2002, require (or even permit) entities to restate past derecognition transactions. Without a similar exemption, first-time adopters would be unfairly disadvantaged.
- (d) Retrospective application would not result in consistent measurement, as entities would need to recreate information about past transactions with the benefit of hindsight.

BC21 The Board had considered these arguments in developing ED 1. The Board's reasons for the proposal in ED 1 were as follows:

- (a) The omission of material assets or liabilities would undermine the understandability, relevance, reliability and comparability of an entity's financial statements. Many of the transactions under discussion are large and will have effects for many years.
- (b) Such an exemption would be inconsistent with the June 2002 exposure draft of improvements to IAS 39.
- (c) The Board's primary objective is to achieve comparability over time within an entity's first IFRS financial statements. Prospective application by a first-time adopter would conflict with that primary objective, even if prospective application were available to entities already applying IFRSs.
- (d) Although a new IFRS may have unforeseen consequences if another party uses financial statements to monitor compliance with a contract or agreement, that possibility does not justify prospective application (paragraph BC13(a)).

BC22 Nevertheless, in finalising the IFRS, the Board concluded that it would be premature to require a treatment different from the current version of IAS 39 before completing the proposed improvements to IAS 39. Accordingly, the IFRS originally required the same treatment as the then current version of IAS 39 for derecognition transactions before the effective date of the then current version of IAS 39, namely that any financial assets or financial liabilities derecognised in accordance with previous GAAP before financial years beginning on 1 January 2001 remain derecognised. The Board agreed that when it completed the improvements to IAS 39, it might amend or delete this exemption.

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. 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

⁷ IFRS 9 *Financial Instruments* replaced IAS 39. IFRS 9 applies to all items that were previously within the scope of IAS 39.

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 amended the fixed date of 1 January 2004 in paragraph B2 to 'the date of transition to IFRSs'. The Board also amended the wording of the illustration in paragraph B2, in order to clarify that it is providing an example.

- BC22B 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.
- BC23 The Board removed from IAS 39 the following consequential amendments to IAS 39 made when IFRS 1 was issued, because, for first-time adopters, these clarifications are clear in paragraphs IG26–IG31 and IG53 of the guidance on implementing IFRS 1. These were:
- (a) the clarification that an entity is required to apply IAS 39 to all derivatives or other interests retained after a derecognition transaction, even if the transaction occurred before the effective date of IAS 39; and
 - (b) the confirmation that there are no exemptions for special purpose entities⁸ that existed before the date of transition to IFRSs.

Measurement

- BC24 The Board considered whether it should require a first-time adopter to measure all assets and liabilities at fair value in the opening IFRS balance sheet. Some argued that this would result in more relevant information than an aggregation of costs incurred at different dates, or of costs and fair values. However, the Board concluded that a requirement to measure all assets and liabilities at fair value at the date of transition to IFRSs would be unreasonable, given that an entity may use an IFRS-compliant cost-based measurement before and after that date for some items.
- BC25 The Board decided as a general principle that a first-time adopter should measure all assets and liabilities recognised in its opening IFRS balance sheet on the basis required by the relevant IFRSs. This is needed for an entity's first IFRS financial statements to present understandable, relevant, reliable and comparable information.

Benefits and costs

- BC26 The *Framework* acknowledges that the need for a balance between the benefits of information and the cost of providing it may constrain the provision of relevant and reliable information. The Board considered these cost-benefit constraints and developed targeted exemptions from the general principle described in paragraph BC25. SIC-8 did not include specific exemptions of this kind, although it provided general exemptions from:
- (a) retrospective adjustments to the opening balance of retained earnings 'when the amount of the adjustment relating to prior periods cannot be reasonably determined'.
 - (b) provision of comparative information when it is 'impracticable' to provide such information.
- BC27 The Board expects that most first-time adopters will begin planning on a timely basis for the transition to IFRSs. Accordingly, in balancing benefits and costs, the Board took as its benchmark an entity that plans the transition well in advance and can collect most information needed for its opening IFRS balance sheet at, or very soon after, the date of transition to IFRSs.
- BC28 ED 1 proposed that a first-time adopter should use either all the exemptions in ED 1 or none. However, some respondents disagreed with this all or nothing approach for the following reasons:
- (a) Many of the exemptions are not interdependent, so there is no conceptual reason to condition use of one exemption on use of other exemptions.
 - (b) Although it is necessary to permit some exemptions on pragmatic grounds, entities should be encouraged to use as few exemptions as possible.

⁸ SIC-12 *Consolidation—Special Purpose Entities* was withdrawn and superseded by IFRS 10 *Consolidated Financial Statements* issued in May 2011. There is no longer specific accounting guidance for special purpose entities because IFRS 10 applies to all types of entities.

- (c) Some of the exemptions proposed in ED 1 were implicit options because they relied on the entity's own judgement of undue cost or effort and some others were explicit options. Only a few exemptions were really mandatory.
 - (d) Unlike the other exceptions to retrospective application, the requirement to apply hedge accounting prospectively was not intended as a pragmatic concession on cost benefit grounds. Retrospective application in an area that relies on designation by management would not be acceptable, even if an entity applied all other aspects of IFRSs retrospectively.
- BC29 The Board found these comments persuasive. In finalising the IFRS, the Board grouped the exceptions to retrospective application into two categories:
- (a) Some exceptions consist of optional exemptions (paragraphs BC30–BC63E).
 - (b) The other exceptions prohibit full retrospective application of IFRSs to some aspects of derecognition (paragraphs BC20–BC23), hedge accounting (paragraphs BC75–BC80), and estimates (paragraph BC84).

Exemptions from other IFRSs

- BC30 An entity may elect to use one or more of the following exemptions:
- (a) business combinations (paragraphs BC31–BC40);
 - (b) deemed cost (paragraphs BC41–BC47E);
 - (c) employee benefits (paragraphs BC48–BC52);
 - (d) cumulative translation differences (paragraphs BC53–BC55C);
 - (e) compound financial instruments (paragraphs BC56–BC58);
 - (f) investments in subsidiaries, jointly controlled entities⁹ and associates (paragraphs BC58A–BC58M);
 - (g) assets and liabilities of subsidiaries, associates and joint ventures (paragraphs BC59–BC63);
 - (h) designation of previously recognised financial instruments (paragraph BC63A);
 - (i) share-based payment transactions (paragraph BC63B);
 - (j) changes in existing decommissioning, restoration and similar liabilities included in the cost of property, plant and equipment (paragraphs BC63C–BC63CA);
 - (k) leases (paragraphs BC63D–BC63DB);
 - (l) borrowing costs (paragraph BC63E);
 - (m) severe hyperinflation (paragraphs BC63F–BC63J); and
 - (n) joint arrangements (paragraphs BC63K and BC63L).

Business combinations¹⁰

- BC31 The following paragraphs discuss various aspects of accounting for business combinations that an entity recognised in accordance with previous GAAP before the date of transition to IFRSs:
- (a) whether retrospective restatement of past business combinations should be prohibited, permitted or required (paragraphs BC32–BC34).
 - (b) whether an entity should recognise assets acquired and liabilities assumed in a past business combination if it did not recognise them in accordance with previous GAAP (paragraph BC35).
 - (c) whether an entity should restate amounts assigned to the assets and liabilities of the combining entities if previous GAAP brought forward unchanged their pre-combination carrying amounts (paragraph BC36).

⁹ 'Jointly controlled entities' were defined in IAS 31 *Interests in Joint Ventures*. IFRS 11 *Joint Arrangements*, issued in May 2011, replaced IAS 31 and changed the terminology.

¹⁰ In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which stated that Appendix C of IFRS 1 should only apply to business combinations within the scope of IFRS 3 *Business Combinations*.

- (d) whether an entity should restate goodwill for adjustments made in its opening IFRS balance sheet to the carrying amounts of assets acquired and liabilities assumed in past business combinations (paragraphs BC37–BC40).
- BC32 Retrospective application of IFRS 3 *Business Combinations* could require an entity to recreate data that it did not capture at the date of a past business combination and make subjective estimates about conditions that existed at that date. These factors could reduce the relevance and reliability of the entity's first IFRS financial statements. Therefore, ED 1 would have prohibited restatement of past business combinations (unless an entity used the proposed alternative approach, discussed in paragraph BC15, of applying IFRSs as if it had always applied IFRSs). Some respondents agreed, arguing that restatement of past business combinations would involve subjective, and potentially selective, use of hindsight that would diminish the relevance and reliability of financial statements.
- BC33 Other respondents disagreed. They argued that:
- (a) effects of business combination accounting can last for many years. Previous GAAP may differ significantly from IFRSs, and in some countries there are no accounting requirements at all for business combinations. Previous GAAP balances might not result in decision-useful information in these countries.
- (b) restatement is preferable and may not involve as much cost or effort for more recent business combinations.
- BC34 In the light of these comments, the Board concluded that restatement of past business combinations is conceptually preferable, although for cost-benefit reasons this should be permitted but not required. The Board decided to place some limits on this election and noted that information is more likely to be available for more recent business combinations. Therefore, if a first-time adopter restates any business combination, the IFRS requires it to restate all later business combinations (paragraph C1 of the IFRS).
- BC35 If an entity did not recognise a particular asset or liability in accordance with previous GAAP at the date of the business combination, ED 1 proposed that its deemed cost in accordance with IFRSs would be zero. As a result, the entity's opening IFRS balance sheet would not have included that asset or liability if IFRSs permit or require a cost-based measurement. Some respondents to ED 1 argued that this would be an unjustifiable departure from the principle that the opening IFRS balance sheet should include all assets and liabilities. The Board agreed with that conclusion. Therefore, paragraph C4(f) of the IFRS requires that the acquirer should recognise those assets and liabilities and measure them on the basis that IFRSs would require in the separate balance sheet of the acquiree.
- BC36 In accordance with previous GAAP, an entity might have brought forward unchanged the pre-combination carrying amounts of the combining entities' assets and liabilities. Some argued that it would be inconsistent to use these carrying amounts as deemed cost in accordance with IFRSs, given that the IFRS does not permit the use of similar carrying amounts as deemed cost for assets and liabilities that were not acquired in a business combination. However, the Board identified no specific form of past business combination, and no specific form of accounting for past business combinations, for which it would not be acceptable to bring forward cost-based measurements made in accordance with previous GAAP.
- BC37 Although the IFRS treats amounts assigned in accordance with previous GAAP to goodwill and other assets acquired and liabilities assumed in a past business combination as their deemed cost in accordance with IFRSs at the date of the business combination, an entity needs to adjust their carrying amounts in its opening IFRS balance sheet, as follows.
- (a) Assets and liabilities measured in accordance with IFRSs at fair value¹¹ or other forms of current value: remeasure to fair value or that other current value.
- (b) Assets (other than goodwill) and liabilities for which IFRSs apply a cost-based measurement: adjust the accumulated depreciation or amortisation since the date of the business combination if it does not comply with IFRSs. Depreciation is based on deemed cost, which is the carrying amount in accordance with previous GAAP immediately following the business combination.
- (c) Assets (other than goodwill) and liabilities not recognised in accordance with previous GAAP: measure on the basis that IFRSs would require in the separate balance sheet of the acquiree.
- (d) Items that do not qualify for recognition as assets and liabilities in accordance with IFRSs: eliminate from the opening IFRS balance sheet.

¹¹ IFRS 13 *Fair Value Measurement*, issued in May 2011, defines fair value and contains the requirements for measuring fair value.

- BC38 The Board considered whether a first-time adopter should recognise the resulting adjustments by restating goodwill. Because intangible assets and goodwill are closely related, the Board decided that a first-time adopter should restate goodwill when it:
- (a) eliminates an item that was recognised in accordance with previous GAAP as an intangible asset but does not qualify for separate recognition in accordance with IFRSs; or
 - (b) recognises an intangible asset that was subsumed within goodwill in accordance with previous GAAP.
- However, to avoid costs that would exceed the likely benefits to users, the IFRS prohibits restatement of goodwill for most other adjustments reflected in the opening IFRS balance sheet, unless a first-time adopter elects to apply IFRS 3 retrospectively (paragraph C4(g) of the IFRS).
- BC39 To minimise the possibility of double-counting an item that was included in goodwill in accordance with previous GAAP, and is included in accordance with IFRSs either within the measurement of another asset or as a deduction from a liability, the IFRS requires an entity to test goodwill recognised in its opening IFRS balance sheet for impairment (paragraph C4(g)(ii) of the IFRS). This does not prevent the implicit recognition of internally generated goodwill that arose after the date of the business combination. However, the Board concluded that an attempt to exclude such internally generated goodwill would be costly and lead to arbitrary results.
- BC40 Some respondents to ED 1 suggested that a formal impairment test should be required only if there is a possibility of double-counting—ie when additional, previously unrecognised, assets relating to a past business combination are recognised in the opening IFRS balance sheet (or an indicator of impairment is present). However, the Board decided that a first-time adopter should carry out a formal impairment test of all goodwill recognised in its opening IFRS balance sheet, as previous GAAP might not have required a test of comparable rigour.

Deemed cost

- BC41 Some measurements in accordance with IFRSs are based on an accumulation of past costs or other transaction data. If an entity has not previously collected the necessary information, collecting or estimating it retrospectively may be costly. To avoid excessive cost, ED 1 proposed that an entity could use the fair value of an item of property, plant and equipment at the date of transition to IFRSs as its deemed cost at that date if determining a cost-based measurement in accordance with IFRSs would involve undue cost or effort.
- BC42 In finalising the IFRS, the Board noted that reconstructed cost data might be less relevant to users, and less reliable, than current fair value data. Furthermore, the Board concluded that balancing costs and benefits was a task for the Board when it sets accounting requirements rather than for entities when they apply those requirements. Therefore, the IFRS permits an entity to use fair value as deemed cost in some cases without any need to demonstrate undue cost or effort.
- BC43 Some expressed concerns that the use of fair value would lead to lack of comparability. However, cost is generally equivalent to fair value at the date of acquisition. Therefore, the use of fair value as the deemed cost of an asset means that an entity will report the same cost data as if it had acquired an asset with the same remaining service potential at the date of transition to IFRSs. If there is any lack of comparability, it arises from the aggregation of costs incurred at different dates, rather than from the targeted use of fair value as deemed cost for some assets. The Board regarded this approach as justified to solve the unique problem of introducing IFRSs in a cost-effective way without damaging transparency.
- BC44 The IFRS restricts the use of fair value as deemed cost to those assets for which reconstructing costs is likely to be of limited benefit to users and particularly onerous: property, plant and equipment, investment property (if an entity elects to use the cost method in IAS 40 *Investment Property*) and intangible assets that meet restrictive criteria (paragraphs D5 and D7 of the IFRS).
- BC45 Under the revaluation model in IAS 16 *Property, Plant and Equipment*, if an entity revalues an asset, it must revalue all assets in that class. This restriction prevents selective revaluation of only those assets whose revaluation would lead to a particular result. Some suggested a similar restriction on the use of fair value as deemed cost. However, IAS 36 *Impairment of Assets* requires an impairment test if there is any indication that an asset is impaired. Thus, if an entity uses fair value as deemed cost for assets whose fair value is above cost, it cannot ignore indications that the recoverable amount of other assets may have fallen below their carrying amount. Therefore, the IFRS does not restrict the use of fair value as deemed cost to entire classes of asset.
- BC46 Some revaluations in accordance with previous GAAP might be more relevant to users than original cost. If so, it would not be reasonable to require time-consuming and expensive reconstruction of a cost that complies

with IFRSs. In consequence, the IFRS permits an entity to use amounts determined using previous GAAP as deemed cost for IFRSs in the following cases:

- (a) if an entity revalued one of the assets described in paragraph BC44 using its previous GAAP and the revaluation met specified criteria (paragraphs D6 and D7 of the IFRS).
- (b) if an entity established a deemed cost in accordance with previous GAAP for some or all assets and liabilities by measuring them at their fair value at one particular date because of an event such as a privatisation or initial public offering (paragraph D8 of the IFRS).

BC46A In *Improvements to IFRSs* issued in May 2010, the Board extended the scope of paragraph D8 for the use of the deemed cost exemption for an event-driven fair value. In some jurisdictions, local law requires an entity to revalue its assets and liabilities to fair value for a privatisation or initial public offering (IPO) and to treat the revalued amounts as deemed cost for the entity's previous GAAP. Before the amendment made in May 2010, if that revaluation occurred after the entity's date of transition to IFRSs, the entity could not have used that revaluation as deemed cost for IFRSs. Therefore, the entity would have had to prepare two sets of measurements for its assets and liabilities—one to comply with IFRSs, and one to comply with local law. The Board considered this unduly onerous. Therefore, the Board amended paragraph D8 to allow an entity to recognise an event-driven fair value measurement as deemed cost when the event occurs, provided that this is during the periods covered by its first IFRS financial statements. In addition, the Board concluded that the same relief should apply to an entity that adopted IFRSs in periods before the effective date of IFRS 1 or applied IFRS 1 in a previous period, provided the measurement date is within the period covered by its first IFRS financial statements.

BC46B The Board also decided to require the entity to present historical costs or other amounts already permitted by IFRS 1 for the periods before that date. In this regard, the Board considered an approach where an entity could 'work back' to the deemed cost on the date of transition, using the revaluation amounts obtained on the measurement date, adjusted to exclude any depreciation, amortisation or impairment between the two dates. Although some believed that this presentation would have provided greater comparability throughout the first IFRS reporting period, the Board rejected it because making such adjustments would require hindsight and the computed carrying amounts on the date of transition to IFRSs would be neither the historical costs of the revalued assets nor their fair values on that date.

BC47 Paragraph D6 of the IFRS refers to revaluations that are broadly comparable to fair value or reflect an index applied to a cost that is broadly comparable to cost determined in accordance with IFRSs. It may not always be clear whether a previous revaluation was intended as a measure of fair value or differs materially from fair value. The flexibility in this area permits a cost-effective solution for the unique problem of transition to IFRSs. It allows a first-time adopter to establish a deemed cost using a measurement that is already available and is a reasonable starting point for a cost-based measurement.

BC47A Under their previous GAAP many oil and gas entities accounted for exploration and development costs for properties in development or production in cost centres that include all properties in a large geographical area. (In some jurisdictions, this is referred to as full cost accounting.) Those entities will in most cases have to determine the carrying amounts for oil and gas assets at the date of transition to IFRSs. Information about oil and gas assets recorded in an accounting system using this method of accounting will almost always be at a larger unit of account than the unit of account that is acceptable under IFRSs. Amortisation at the IFRS unit of account level would also have to be calculated (on a unit of production basis) for each year, using a reserves base that has changed over time because of changes in factors such as geological understanding and prices for oil and gas. In many cases, particularly for older assets, this information may not be available. The Board was advised that even if such information is available the effort and associated cost to determine the opening balances at the date of transition would usually be very high.

BC47B IFRS 1 permits an entity to measure an item of property, plant and equipment at its fair value at the date of transition to IFRSs and to use that fair value as the item's deemed cost at that date. Determining the fair value of oil and gas assets is a complex process that begins with the difficult task of estimating the volume of reserves and resources. When the fair value amounts must be audited, determining significant inputs to the estimates generally requires the use of qualified external experts. For entities with many oil and gas assets, the use of this fair value as deemed cost alternative would not meet the Board's stated intention of avoiding excessive cost (see paragraph BC41).

BC47C The Board decided that for oil and gas assets in the development or production phases, it would permit entities that used the method of accounting described in paragraph BC47A under their previous GAAP to determine the deemed cost at the date of transition to IFRSs using an allocation of the amount determined for a cost centre under the entity's previous GAAP on the basis of the reserves associated with the oil and gas assets in that cost centre.

BC47D The deemed cost of oil and gas assets determined in this way may include amounts that would not have been capitalised in accordance with IFRSs, such as some overhead costs, costs that were incurred before the entity

obtained legal rights to explore a specific area (and cannot be capitalised in accordance with IAS 38 *Intangible Assets*) and, most significantly, unsuccessful exploration costs. This is a consequence of having included these costs in the single carrying amount under the method of accounting described in paragraph BC47A. To avoid the use of deemed costs resulting in an oil and gas asset being measured at more than its recoverable amount, the Board decided that oil and gas assets should be tested for impairment at the date of transition to IFRSs.

- BC47E Not all oil and gas entities used the method of accounting described in paragraph BC47A under their previous GAAP. Some used a method of accounting that requires a unit of account that is generally consistent with IFRSs and does not cause similar transition issues. Therefore, the Board decided that the exemption would apply only to entities that used the method of accounting described in paragraph BC47A under their previous GAAP.
- BC47F In *Improvements to IFRSs* issued in May 2010, the Board extended the use of the deemed cost exemption to entities with operations subject to rate regulation. An entity might have items of property, plant and equipment or intangible assets that it holds for use in operations subject to rate regulation, or that it once used for this purpose and now holds for other purposes. Under previous GAAP, an entity might have capitalised, as part of the carrying amount of items of property, plant and equipment or intangible assets held for use in operations subject to rate regulation, amounts that do not qualify for capitalisation under IFRSs. For example, when setting rates regulators often permit entities to capitalise, as part of the cost of property, plant and equipment or intangible assets acquired, constructed or produced over time, an allowance for the cost of financing the asset's acquisition, construction or production. This allowance typically includes an imputed cost of equity. IFRSs do not permit an entity to capitalise an imputed cost of equity.
- BC47G Before this amendment, an entity with such items whose carrying amounts include amounts that do not qualify for capitalisation under IFRSs would have had either to restate those items retrospectively to remove the non-qualifying amounts, or to use the exemption in paragraph D5 (fair value as deemed cost). Both of those alternatives pose significant practical challenges, the cost of which can often outweigh the benefit.
- BC47H Typically, once amounts are included in the total cost of an item of property, plant and equipment, they are no longer tracked separately. The restatement of property, plant and equipment to remove amounts not in compliance with IFRSs would require historical information that, given the typical age of some of the assets involved, is probably no longer available and would be difficult to estimate. Obtaining the fair value information necessary to use the exemption in paragraph D5 may not be a practical alternative, given the lack of readily available fair value information for those assets.
- BC47I The Board decided it would permit entities with operations subject to rate regulation to use as deemed cost at the date of transition to IFRSs the carrying amount of the items of property, plant and equipment or intangible assets determined under the entity's previous GAAP. The Board views this exemption as consistent with the exemptions already included in IFRS 1 in that it avoids excessive costs while meeting the objectives of the IFRS.
- BC47J The Board understands that most first-time adopters with operations subject to rate regulation have previously accounted for property, plant and equipment largely in accordance with a historical cost model consistent with IAS 16. The Board concluded that the cost and effort required to achieve total compliance in this area for the purposes of preparing an entity's first IFRS financial statements is not warranted to meet the objective of providing a suitable starting point for accounting under IFRSs. IFRS 1 requires that each item for which the exemption is used is tested for impairment, either individually or at the cash-generating unit to which the item belongs in accordance with IAS 36, at the date of transition. This requirement provides further assurance that this objective is met.
- BC47K Consistent with the Board's rationale for the use of fair value as deemed cost in paragraphs BC43 and BC44, this exemption means that an entity will report the same cost data as if it had acquired an asset with the same remaining service potential for that amount at the date of transition to IFRSs. An entity's use of this exemption results in a new cost basis for the item and previous GAAP depreciation methods and capitalisation policies are not relevant. Thus, if an entity uses this exemption for items of property, plant and equipment or intangible assets, it does not also apply the exemption for borrowing costs provided in paragraph D23.

Employee benefits

- BC48 [Deleted]
- BC49 The revision of IAS 19 in 1998 increased the reported employee benefit liabilities of some entities. IAS 19 permitted entities to amortise that increase over up to five years. Some suggested a similar transitional treatment for first-time adopters. However, the Board has no general policy of exempting transactions occurring before

a specific date from the requirements of new IFRSs (paragraph 21¹² of the *Preface to International Financial Reporting Standards*). Therefore, the Board did not include a similar transitional provision for first-time adopters.

- BC50 An entity's first IFRS financial statements may reflect measurements of pension liabilities at three dates: the reporting date, the end of the comparative year and the date of transition to IFRSs. Some suggested that obtaining three separate actuarial valuations for a single set of financial statements would be costly. Therefore, they proposed that the Board should permit an entity to use a single actuarial valuation, based, for example, on assumptions valid at the reporting date, with service costs and interest costs based on those assumptions for each of the periods presented.
- BC51 However, the Board concluded that a general exemption from the principle of measurement at each date would conflict with the objective of providing understandable, relevant, reliable and comparable information for users. If an entity obtains a full actuarial valuation at one or two of these dates and rolls that (those) valuation(s) forward or back to the other date(s), any such roll forward or roll back needs to reflect material transactions and other material events (including changes in market prices and interest rates) between those dates (IAS 19 paragraph 57).
- BC52 [Deleted]

Cumulative translation differences

- BC53 IAS 21 *The Effects of Changes in Foreign Exchange Rates* requires an entity to classify some cumulative translation differences (CTDs) relating to a net investment in a foreign operation as a separate component of equity. The entity transfers the CTDs to the income statement on subsequent disposal of the foreign operation. The proposals in ED 1 would have permitted a first-time adopter to use the CTDs in accordance with previous GAAP as the deemed CTDs in accordance with IFRSs if reconstructing CTDs would have involved undue cost or effort.
- BC54 Some respondents to ED 1 argued that it would be more transparent and comparable to exempt an entity from the requirement to identify CTDs at the date of transition to IFRSs, for the following reasons:
- (a) An entity might know the aggregate CTDs, but might not know the amount for each subsidiary. If so, it could not transfer that amount to the income statement on disposal of that subsidiary. This would defeat the objective of identifying CTDs as a separate component of equity.
 - (b) The amount of CTDs in accordance with previous GAAP might be inappropriate as it might be affected by adjustments made on transition to IFRSs to assets and liabilities of foreign entities.
- BC55 The Board found these arguments persuasive. Therefore, a first-time adopter need not identify the CTDs at the date of transition to IFRSs (paragraphs D12 and D13 of the IFRS). The first-time adopter need not show that identifying the CTDs would involve undue cost or effort.

Subsidiary as a First-time Adopter (Annual Improvements to IFRS Standards 2018–2020)

- BC55A Paragraph D16(a) provides a subsidiary that becomes a first-time adopter later than its parent with an exemption relating to the measurement of its assets and liabilities. Paragraphs BC59–BC60 explain that the Board provided this exemption so that a subsidiary would not have to keep two parallel sets of accounting records based on different dates of transition to IFRSs.
- BC55B The exemption in paragraph D16(a) does not apply to components of equity. Accordingly, before the amendment that added paragraph D13A, a subsidiary that became a first-time adopter later than its parent might have been required to keep two parallel sets of accounting records for cumulative translation differences based on different dates of transition to IFRSs. Following the rationale in paragraphs BC59–BC60, the Board decided to extend the exemption in paragraph D16(a) to cumulative translation differences to reduce costs for first-time adopters. The Board noted that IFRS 1 already provides an exemption relating to cumulative translation differences. Extending the exemption in paragraph D16(a) would therefore not diminish the relevance of information reported by a subsidiary that becomes a first-time adopter later than its parent.
- BC55C Entities that apply paragraph D16(a) could in some situations find it burdensome to measure cumulative translation differences using the amount reported by the parent. The Board therefore decided to permit, but not require, a subsidiary applying paragraph D16(a) to use that exemption for cumulative translation

¹² Amended to paragraph 13 when the *Preface to IFRS Standards* was revised and renamed in December 2018.

differences. The amendment also applies to an associate or joint venture that uses the exemption in paragraph D16(a).

Compound financial instruments

- BC56 IAS 32 requires an entity to split a compound financial instrument at inception into separate liability and equity components. Even if the liability component is no longer outstanding, retrospective application of IAS 32 would involve separating two portions of equity. The first portion is in retained earnings and represents the cumulative interest accreted on the liability component. The other portion represents the original equity component of the instrument.
- BC57 Some respondents to ED 1 argued that separating these two portions would be costly if the liability component of the compound instrument is no longer outstanding at the date of transition to IFRSs. The Board agreed with those comments. Therefore, if the liability component is no longer outstanding at the date of transition to IFRSs, a first-time adopter need not separate the cumulative interest on the liability component from the equity component (paragraph D18 of the IFRS).
- BC58 Some respondents requested an exemption for compound instruments even if still outstanding at the date of transition to IFRSs. One possible approach would be to use the fair value of the components at the date of transition to IFRSs as deemed cost. However, as the IFRS does not include any exemptions for financial liabilities, the Board concluded that it would be inconsistent to create such an exemption for the liability component of a compound instrument.

Investments in subsidiaries, jointly controlled entities¹³ and associates

- BC58A IAS 27 *Consolidated and Separate Financial Statements* requires an entity, in its separate financial statements, to account for investments in subsidiaries, jointly controlled entities and associates either at cost or in accordance with IAS 39.^{14,15} For those investments that are measured at cost, the previous version of IAS 27 (before *Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate* was issued in May 2008) required an entity to recognise income from the investment only to the extent the entity received distributions from post-acquisition retained earnings (the ‘cost method’). Distributions received in excess of such profits were regarded as a recovery of investment and were recognised as a reduction in the cost of the investment.
- BC58B For some jurisdictions, these aspects of IAS 27 led to practical difficulties on transition to IFRSs. In order to apply IAS 27 retrospectively, it would be necessary:
- (a) to measure the fair value of the consideration given at the date of acquisition; and
 - (b) to determine whether any dividends received from a subsidiary after its acquisition were paid out of pre-acquisition retained earnings, which would reduce the carrying amount of the investment in the subsidiary in the parent’s separate financial statements.
- BC58C If a parent held an investment in a subsidiary for many years, such an exercise might be difficult, or even impossible, and perhaps costly. For example, in some jurisdictions, entities accounted for some previous acquisitions that were share-for-share exchanges using so-called ‘merger relief’ or ‘group reconstruction relief’. In this situation, the carrying amount of the investment in the parent’s separate financial statements was based on the nominal value of the shares given rather than the value of the purchase consideration. This might make it difficult or impossible to measure the fair value of the shares given.
- BC58D The Board published *Cost of an Investment in a Subsidiary*, an exposure draft of proposed amendments to IFRS 1, in January 2007. In response to the issues outlined in paragraphs BC58A–BC58C, the Board proposed two exemptions from applying the requirements of IAS 27 retrospectively upon first-time adoption of IFRSs:
- (a) an alternative approach for determining the cost of an investment in a subsidiary in the separate financial statements of a parent; and
 - (b) simplification of the process for determining the pre-acquisition retained earnings of that subsidiary.

¹³ ‘Jointly controlled entities’ were defined in IAS 31 *Interests in Joint Ventures*. IFRS 11 *Joint Arrangements*, issued in May 2011, replaced IAS 31 and changed the terminology.

¹⁴ The consolidation guidance was removed from IAS 27 and the Standard was renamed *Separate Financial Statements* by IFRS 10 *Consolidated Financial Statements* issued in May 2011. The accounting requirements for separate financial statements were not changed.

¹⁵ IFRS 9 *Financial Instruments* replaced IAS 39. IFRS 9 applies to all items that were previously within the scope of IAS 39.

- BC58E In developing that exposure draft, the Board considered three ways of determining a deemed cost of an investment in a subsidiary at the parent's date of transition to IFRSs in its separate financial statements. These were:
- the previous GAAP cost of the investment (previous GAAP deemed cost).
 - the parent's interest in the subsidiary's assets less liabilities, using the carrying amounts that IFRSs would require in the subsidiary's statement of financial position (net asset deemed cost).
 - the fair value of the investment (fair value deemed cost).
- BC58F The Board decided that the net asset deemed cost option would provide relevant information to users about the subsidiary's financial position at the date of transition to IFRSs and would be relatively easy to determine. The fair value deemed cost option would provide relevant information at the date of transition to IFRSs, but might be more costly and difficult to determine.
- BC58G In some situations, the cost of an investment in a subsidiary determined using the previous GAAP carrying amount might bear little resemblance to cost determined in accordance with IAS 27. Therefore, the Board rejected the use of a deemed cost based on the previous GAAP carrying amount. The Board proposed to allow entities a choice between the net asset deemed cost and the fair value deemed cost.
- BC58H Respondents to the exposure draft stated that the previous GAAP carrying amount is a more appropriate deemed cost. They argued that:
- a net asset deemed cost would not include goodwill or other intangible assets that might be present in a carrying amount determined in accordance with previous GAAP. When this is the case, the net asset deemed cost option would understate the assets of the entities for which it is used. The resulting reduction in the carrying amount of the investment could reduce the distributable profits of the parent.
 - it was difficult to see why, in the light of the exemption in IFRS 1 from applying IFRS 3 retrospectively, the Board did not propose to permit the cost of the investment in a subsidiary in accordance with previous GAAP to be used as a deemed cost. When an entity had chosen not to apply IFRS 3 retrospectively to a past business combination, it would be logical not to require it to restate the cost of the related investment in the separate financial statements of the parent.
- BC58I In the light of respondents' comments, the Board observed that, in many instances, neither the previous GAAP carrying amount nor the net asset deemed cost represents 'cost'—both numbers could be viewed as being equally arbitrary.
- BC58J In order to reduce the cost of adopting IFRSs in the parent entity's separate financial statements without significantly reducing the benefits of those statements, the Board decided to allow entities a choice between the previous GAAP carrying amount and the fair value as deemed cost.
- BC58K The Board also agreed with respondents that similar issues arise for investments in associates and jointly controlled entities.¹⁶ As a result, paragraph D15 of the IFRS applies to such investments.
- BC58L The Board published its revised proposals in *Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate*, an exposure draft of proposed amendments to IFRS 1 and IAS 27, in December 2007. Respondents generally supported the proposed amendments to IFRS 1. The Board included the amendments in *Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate* issued in May 2008.
- BC58M In developing the December 2007 exposure draft, the Board decided to address the simplification of the process for determining the pre-acquisition retained earnings of a subsidiary more generally through an amendment to IAS 27 (see paragraph 38A of IAS 27 and paragraphs BC66D–BC66J¹⁷ of the Basis for Conclusions on IAS 27).

Assets and liabilities of subsidiaries, associates and joint ventures

- BC59 A subsidiary may have reported to its parent in the previous period using IFRSs without presenting a full set of financial statements in accordance with IFRSs. If the subsidiary subsequently begins to present financial statements that contain an explicit and unreserved statement of compliance with IFRSs, it becomes a first-time adopter at that time. This might compel the subsidiary to keep two parallel sets of accounting records based on different dates of transition to IFRSs, because some measurements in accordance with the IFRS depend on the date of transition to IFRSs.

¹⁶ 'Jointly controlled entities' were defined in IAS 31 *Interests in Joint Ventures*. IFRS 11 *Joint Arrangements*, issued in May 2011, replaced IAS 31 and changed the terminology.

¹⁷ renumbered to paragraphs 12 and BC16–BC22 when IAS 27 was amended in May 2011.

- BC60 In developing ED 1, the Board concluded that a requirement to keep two parallel sets of records would be burdensome and not be beneficial to users. Therefore, ED 1 proposed that a subsidiary would not be treated as a first-time adopter for recognition and measurement purposes if the subsidiary was consolidated in IFRS financial statements for the previous period and all owners of the minority interests consented.¹⁸
- BC61 Some respondents to ED 1 opposed the exemption, on the following grounds:
- (a) The exemption would not eliminate all differences between the group reporting package and the subsidiary's own financial statements. The reporting package does not constitute a full set of financial statements, the parent may have made adjustments to the reported numbers (for example, if pension cost adjustments were made centrally), and the group materiality threshold may be higher than for the subsidiary.
 - (b) The Board's objective of comparability between different entities adopting IFRSs for the first time at the same date (paragraph BC10) should apply equally to any entity, including subsidiaries, particularly if the subsidiary's debt or equity securities are publicly traded.
- BC62 However, the Board retained the exemption because it will ease some practical problems. Although the exemption does not eliminate all differences between the subsidiary's financial statements and a group reporting package, it does reduce them. Furthermore, the exemption does not diminish the relevance and reliability of the subsidiary's financial statements because it permits a measurement that is already acceptable in accordance with IFRSs in the consolidated financial statements of the parent. Therefore, the Board also eliminated the proposal in ED 1 that the exemption should be conditional on the consent of minorities.
- BC63 In finalising the IFRS, the Board simplified the description of the exemption for a subsidiary that adopts IFRSs after its parent. In accordance with the IFRS, the subsidiary may measure its assets and liabilities at the carrying amounts that would be included in the parent's consolidated financial statements, based on the parent's date of transition to IFRSs, if no adjustments were made for consolidation procedures and for the effects of the business combination in which the parent acquired the subsidiary.¹⁹ Alternatively, it may elect to measure them at the carrying amounts required by the rest of the IFRS, based on the subsidiary's date of transition to IFRSs. The Board also extended the exemption to an associate or joint venture that becomes a first-time adopter later than an entity that has significant influence or joint control over it (paragraph D16 of the IFRS). However, if a parent adopts IFRSs later than a subsidiary, the parent cannot, in its consolidated financial statements, elect to change IFRS measurements that the subsidiary has already used in its financial statements, except to adjust for consolidation procedures and for the effects of the business combination in which the parent acquired the subsidiary²⁰ (paragraph D17 of the IFRS).

Designation of previously recognised financial instruments

- BC63A IAS 39²¹ permits an entity to designate, on initial recognition only, a financial instrument as (a) available for sale²² (for a financial asset) or (b) a financial asset or financial liability at fair value through profit or loss (provided the asset or liability qualifies for such designation in accordance with paragraph 9(b)(i), 9(b)(ii)). Despite this requirement, an entity that had already applied IFRSs before the effective date of IAS 39 (as revised in March 2004) may (a) designate a previously recognised financial asset as available for sale on initial application of IAS 39 (as revised in March 2004), or (b) designate a previously recognised financial instrument as at fair value through profit or loss in the circumstances specified in paragraph 105B of IAS 39. The Board decided that the same considerations apply to first-time adopters as to entities that already apply IFRSs. Accordingly, a first-time adopter of IFRSs may similarly designate a previously recognised financial instrument in accordance with paragraph D19 of the IFRS. Such an entity shall disclose the fair value of the financial assets or financial liabilities designated into each category at the date of designation and their classification and carrying amount in the previous financial statements.

¹⁸ In January 2008 the IASB issued an amended IAS 27 *Consolidated and Separate Financial Statements*, which amended 'minority interests' to 'non-controlling interests'. The consolidation requirements in IAS 27 were superseded by IFRS 10 *Consolidated Financial Statements* issued in May 2011. The term 'non-controlling interests' and the requirements for non-controlling interests were not changed.

¹⁹ In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which removed option D16(a) for investments in subsidiaries of investment entities, as defined in IFRS 10 *Consolidated Financial Statements*, required to be measured at fair value through profit or loss.

²⁰ In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which amended paragraph D17 to clarify its application to investment entities, as defined in IFRS 10.

²¹ IFRS 9 *Financial Instruments* replaced IAS 39. IFRS 9 applies to all items that were previously within the scope of IAS 39.

²² IFRS 9 *Financial Instruments* eliminated the category of available-for-sale financial assets.

Share-based payment transactions

BC63B IFRS 2 *Share-based Payment* contains various transitional provisions. For example, for equity settled share-based payment arrangements, IFRS 2 requires an entity to apply IFRS 2 to shares, share options or other equity instruments that were granted after 7 November 2002 and had not vested at the effective date of IFRS 2. IFRS 2 is effective for annual periods beginning on or after 1 January 2005. There are also transitional arrangements for liabilities arising from cash-settled share-based payment transactions, and for modifications of the terms or conditions of a grant of equity instruments to which IFRS 2 has not been applied, if the modification occurs after the effective date of IFRS 2. The Board decided that, in general, first-time adopters should be treated in the same way as entities that already apply IFRSs. For example, a first-time adopter should not be required to apply IFRS 2 to equity instruments that were granted on or before 7 November 2002. Similarly, a first-time adopter should not be required to apply IFRS 2 to equity instruments that were granted after 7 November 2002 if those equity instruments vested before 1 January 2005. In addition, the Board decided that a first-time adopter should not be required to apply IFRS 2 to equity instruments that were granted after 7 November 2002 if those equity instruments vested before the date of transition to IFRSs. Similarly, the Board decided that a first-time adopter should not be required to apply IFRS 2 to liabilities arising from cash-settled share-based payment transactions if those liabilities were settled before the date of transition to IFRSs.

Changes in existing decommissioning, restoration and similar liabilities included in the cost of property, plant and equipment

BC63C IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities* requires specified changes in decommissioning, restoration and similar liabilities to be added to, or deducted from, the cost of the assets to which they relate, and the adjusted depreciable amount to be depreciated prospectively over the remaining useful life of those assets. Retrospective application of this requirement at the date of transition would require an entity to construct a historical record of all such adjustments that would have been made in the past. In many cases this will not be practicable. The Board agreed that, as an alternative to complying with this requirement, an entity should be permitted to include in the depreciated cost of the asset, at the date of transition to IFRSs, an amount calculated by discounting the liability at that date back to, and depreciating it from, when the liability was first incurred.

BC63CA Paragraph D21 of the IFRS exempts from the requirements of IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities* changes in decommissioning costs incurred before the date of transition to IFRSs. Use of this exemption would require detailed calculations that would not be practicable for entities that used the method of accounting described in paragraph BC47A under their previous GAAP. The Board noted that adjustments to liabilities as a result of initial adoption of IFRSs arise from events and transactions before the date of transition to IFRSs and are generally recognised in retained earnings. Therefore, the Board decided that, for entities that used the method of accounting described in paragraph BC47A, any adjustment for a difference between decommissioning, restoration and similar liabilities measured in accordance with IAS 37 and the liability determined under the entity's previous GAAP should be accounted for in the same manner.

Leases

BC63D IFRIC 4 *Determining whether an Arrangement contains a Lease* contains transitional provisions because the IFRIC acknowledged the practical difficulties raised by full retrospective application of the Interpretation, in particular the difficulty of going back potentially many years and making a meaningful assessment of whether the arrangement satisfied the criteria at that time. The Board decided to treat first-time adopters in the same way as entities that already apply IFRSs.

BC63DA IFRIC 4 permits an entity to apply its requirements to arrangements existing at the start of the earliest period for which comparative information is presented on the basis of facts and circumstances existing at the start of that period. Before adopting IFRSs, a jurisdiction might adopt a national standard having the same effect as the requirements of IFRIC 4, including the same transitional provisions. An entity in that jurisdiction might then apply requirements having the same effect as the requirements of IFRIC 4 to some or all arrangements (even if the wording of those requirements is not identical). However, the entity might apply the requirements at a date different from the date in the transitional provisions of IFRIC 4. IFRS 1 would require such an entity to reassess that accounting retrospectively on first-time adoption. This might result in additional costs, with no obvious benefits. Accordingly, the Board decided that if a first-time adopter made the same determination under previous GAAP as that required by IFRIC 4 but at a date other than that required by IFRIC 4, the first-time adopter need not reassess that determination when it adopts IFRSs.

BC63DB The Board considered a more general modification to IFRS 1. It considered whether to modify IFRS 1 so that entities need not reassess, at the date of transition to IFRSs, prior accounting if that prior accounting permitted the same prospective application as IFRSs with the only difference from IFRSs being the effective date from when that

accounting was applied. In this regard, the Board noted that any such proposal must apply to assessments resulting in the *same* determination, rather than *similar* determinations, because it would be too difficult to determine and enforce what constitutes a sufficient degree of similarity. The Board noted that many of the circumstances in which this situation might arise have been dealt with in IFRS 1 or other IFRSs. Accordingly, the Board decided to focus on IFRIC 4 only.

Borrowing costs

BC63E IAS 23 *Borrowing Costs* (as revised in 2007) contains transitional provisions because the Board acknowledged that if an entity has been following the accounting policy of immediately recognising borrowing costs as an expense and has not previously gathered the necessary information for capitalisation of borrowing costs, getting the information retrospectively may be costly. First-time adopters of IFRSs face problems similar to those facing entities that already apply IFRSs. Moreover, although first-time adopters have the option of using fair value as the deemed cost of an asset at the date of transition to IFRSs, this option is not applicable to all qualifying assets, such as inventories. Furthermore, the Board concluded that the existence of the deemed cost option is not sufficient to justify a more stringent requirement for the application of IAS 23 for first-time adopters than for entities that already apply IFRSs. A more stringent requirement for the adoption of the capitalisation treatment could be justified when IFRS 1 was originally issued because capitalisation was then an option. The requirements for the application of mandatory capitalisation, on the other hand, should be the same for entities that already apply IFRSs and for first-time adopters. Therefore, the Board decided to amend IFRS 1, allowing first-time adopters transitional provisions equivalent to those available to entities that already apply IFRSs in paragraphs 27 and 28 of IAS 23, as revised in 2007.

BC63EA In *Annual Improvements 2009–2011 Cycle* (issued in May 2012) the Board addressed some concerns that were raised by first-time adopters about the transitional provisions for borrowing costs relating to qualifying assets for which the commencement date for capitalisation was before the date of transition to IFRSs. Interested parties found it unclear whether borrowing costs capitalised in accordance with previous GAAP should be retained, restated or eliminated in the opening statement of financial position. Interested parties also questioned the accounting, after the date of transition, for borrowing costs that relate to such qualifying assets when these qualifying assets are under construction at the date of transition. They wanted clarification as to whether the first time adopter should apply the requirements of IAS 23 *Borrowing Costs* or whether it should continue applying its previous GAAP even if that previous GAAP is not consistent with IAS 23.

BC63EB The Board clarified that when the entity chooses to apply the exemption in paragraph D23 of IFRS 1, the borrowing costs that were capitalised in accordance with previous GAAP should be carried forward in the opening statement of financial position. This is because gathering the information for capitalisation of borrowing costs under IAS 23 and identifying and eliminating the amounts (if any) capitalised in past years under previous GAAP may be costly. In addition, the Board clarified that an entity should account for borrowing costs that are incurred after the date of transition and that relate to qualifying assets under construction at the date of transition in accordance with IAS 23, regardless of whether the entity capitalised or recognised in profit and loss borrowing costs under previous GAAP. The Board determined that this requirement would ensure useful information to users of financial statements. A first-time adopter could also choose to apply the requirements of IAS 23 from a date earlier than the date of transition, in which case it should account for borrowing costs in accordance with IAS 23 on or after the earlier date selected.

Severe hyperinflation

BC63F In 2010 the Board was asked to clarify how an entity should resume presenting financial statements in accordance with IFRSs after a period of severe hyperinflation, during which the entity had been unable to comply with IAS 29 *Financial Reporting in Hyperinflationary Economies*. An entity would be unable to comply with IAS 29 if a reliable general price index is not available to all entities with that same functional currency, and exchangeability between the currency and a relatively stable foreign currency does not exist. However, once the functional currency changes to a non-hyperinflationary currency, or the currency ceases to be severely hyperinflationary, an entity would be able to start applying IFRSs to subsequent transactions.

BC63G The Board noted that IFRSs did not provide sufficient guidance in these circumstances. The Board therefore decided to amend IFRS 1 to provide guidance on how an entity can present IFRS financial statements after its currency ceases to be severely hyperinflationary, by presenting an opening IFRS statement of financial position on or after the functional currency normalisation date. The Board believed that allowing an entity to apply the exemption when presenting an opening IFRS statement of financial position after, and not just on, the functional currency normalisation date, would address practical concerns that may arise if the functional currency normalisation date and the entity's date of transition to IFRSs are different. The Board decided that this amendment would also be available to entities that were emerging from a period of severe hyperinflation but had not applied IFRSs in the past.

- BC63H The Board decided to permit an entity emerging from a period of severe hyperinflation to elect to measure its assets and liabilities at fair value. That fair value could then be used as the deemed cost in its opening IFRS statement of financial position. The Board believed that this approach would expand the scope of the deemed cost exemptions in IFRS 1 to enable them to be applied in these specific circumstances. However, because severe hyperinflation is a specific set of circumstances, the Board wanted to ensure that the fair value measurement option was applied only to those assets and liabilities that were held before the functional currency normalisation date, and not to other assets and liabilities held by the entity at the time it made the transition to IFRSs. Furthermore, where a parent entity's functional currency has been subject to severe hyperinflation, but its subsidiary company's functional currency has not been subject to severe hyperinflation, the Board decided it was inappropriate for such a subsidiary company to be able to apply this exemption.
- BC63I The Board decided that any adjustments arising on electing to measure assets and liabilities at fair value in the opening IFRS statement of financial position arise from events and transactions before the date of transition to IFRSs. Consequently, those adjustments should be accounted for in accordance with paragraph 11 of IFRS 1, and an entity should recognise those adjustments directly in retained earnings (or, if appropriate, in another category of equity) at the date of transition to IFRSs.
- BC63J The Board observed that entities are required to apply paragraph 21 of IFRS 1 and prepare and present comparative information in accordance with IFRSs. The Board noted that preparation of information in accordance with IFRSs for periods before the functional currency normalisation date may not be possible; hence the exemption refers to a date of transition on or after the functional currency normalisation date. This may lead to a comparative period of less than 12 months. The Board identified that entities should consider whether disclosure of non-IFRS comparative information and historical summaries, in accordance with paragraph 22 of IFRS 1, would provide useful information to users of financial statements. The Board also noted that an entity should clearly explain the transition to IFRSs in accordance with paragraphs 23–28.

Joint arrangements

- BC63K During its redeliberation of the exposure draft ED 9 *Joint Arrangements* the Board decided not to require entities changing from proportionate consolidation to the equity method to adjust any differences between the two accounting methods retrospectively. Instead an entity should determine the opening balance of the investment relating to its interest in a joint venture as the aggregate of the carrying amounts of the assets and liabilities that the entity had been previously proportionately consolidated, including any goodwill arising from acquisition as at the beginning of the earliest period presented. The Board decided to treat first-time adopters in the same way as entities that already apply IFRSs with the following exception.
- BC63L A first-time adopter is required to test for impairment the opening investment in accordance with IAS 36 at the earliest period presented, regardless of whether there is any indication that the investment may be impaired. The Board noted that this is a more stringent requirement for the application of IFRS 11 *Joint Arrangements* by first-time adopters, but is aligned with the requirement for first-time adopters to apply IAS 36 in testing goodwill for impairment at the date of transition to IFRSs regardless of whether there is any indication that the goodwill may be impaired.
- BC63M *Consolidated Financial Statements, Joint Arrangements and Disclosure of Interests in Other Entities: Transition Guidance* (Amendments to IFRS 10, IFRS 11 and IFRS 12), issued in June 2012, amended IFRS 11 to require the transition adjustments of that IFRS to be recognised at the beginning of the annual period immediately preceding the first annual period for which IFRS 11 is applied (the 'immediately preceding period') instead of the beginning of the earliest period presented. The Board agreed that IFRS 1 should not be amended to reflect those amendments because the adjustments required on transition to IFRS should be reflected at the date of transition, which may be earlier than the beginning of the immediately preceding period. Consequently, paragraph D31 was amended to clarify that, when a first-time adopter is applying the transition guidance of IFRS 11, they shall apply the requirements at the date of transition, which is the same as the beginning of the earliest IFRS period presented.

Other possible exemptions rejected

- BC64 The Board considered and rejected suggestions for other exemptions. Each such exemption would have moved the IFRS away from a principle-based approach, diminished transparency for users, decreased comparability over time within an entity's first IFRS financial statements and created additional complexity. In the Board's view, any cost savings generated would not have outweighed these disadvantages. Paragraphs BC65–BC73 discuss some of the specific suggestions the Board considered for embedded derivatives, hyperinflation, intangible assets and transaction costs on financial instruments.

Embedded derivatives

- BC65 IAS 39²³ requires an entity to account separately for some embedded derivatives at fair value. Some respondents to ED 1 argued that retrospective application of this requirement would be costly. Some suggested either an exemption from retrospective application of this requirement, or a requirement or option to use the fair value of the host instrument at the date of transition to IFRSs as its deemed cost at that date.
- BC66 The Board noted that US GAAP provides an option in this area. Under the transitional provisions of SFAS 133 *Accounting for Derivative Instruments and Hedging Activities*, an entity need not account separately for some pre-existing embedded derivatives. Nevertheless, the Board concluded that the failure to measure embedded derivatives at fair value would diminish the relevance and reliability of an entity's first IFRS financial statements. The Board also observed that IAS 39 addresses an inability to measure an embedded derivative and the host contract separately. In such cases, IAS 39 requires an entity to measure the entire combined contract at fair value.

Hyperinflation

- BC67 Some argued that the cost of restating financial statements for the effects of hyperinflation in periods before the date of transition to IFRSs would exceed the benefits, particularly if the currency is no longer hyperinflationary. However, the Board concluded that such restatement should be required, because hyperinflation can make unadjusted financial statements meaningless or misleading.

Intangible assets

- BC68 For the following reasons, some proposed that a first-time adopter's opening IFRS balance sheet should exclude intangible assets that it did not recognise in accordance with previous GAAP:
- (a) Using hindsight to assess retrospectively when the recognition criteria for intangible assets were met could be subjective, open up possibilities for manipulation and involve costs that might exceed the benefits to users.
 - (b) The benefits expected from intangible assets are often not related directly to the costs incurred. Therefore, capitalising the costs incurred is of limited benefit to users, particularly if the costs were incurred in the distant past.
 - (c) Such an exclusion would be consistent with the transitional provisions in IAS 38 *Intangible Assets*. These encourage (but do not require) the recognition of intangible assets acquired in a previous business combination that was an acquisition and prohibit the recognition of all other previously unrecognised intangible assets.
- BC69 In many cases, internally generated intangible assets do not qualify for recognition in accordance with IAS 38 at the date of transition to IFRSs because an entity did not, in accordance with previous GAAP, accumulate cost information or did not carry out contemporaneous assessments of future economic benefits. In these cases, there is no need for a specific requirement to exclude those assets. Furthermore, when these assets do not qualify for recognition, first-time adopters will not generally, in the Board's view, need to perform extensive work to reach this conclusion.
- BC70 In other cases, an entity may have accumulated and retained sufficient information about costs and future economic benefits to determine which intangible assets (whether internally generated or acquired in a business combination or separately) qualify in accordance with IAS 38 for recognition in its opening IFRS balance sheet. If that information is available, no exclusion is justified.
- BC71 Some argued that fair value should be used as deemed cost for intangible assets in the opening IFRS balance sheet (by analogy with a business combination). ED 1 would not have permitted this. However, in finalising the IFRS, the Board concluded that this approach should be available for those intangible assets for which IFRSs already permit fair value measurements. Therefore, in accordance with the IFRS, a first-time adopter may elect to use fair value or some previous GAAP revaluations of intangible assets as deemed cost for IFRSs, but only if the intangible assets meet:
- (a) the recognition criteria in IAS 38 (including reliable measurement of original cost); and

²³ The Board amended the requirements in IAS 39 to identify and separately account for embedded derivatives and relocated them to IFRS 9 *Financial Instruments*. This Basis for Conclusions has not been updated for changes in requirements since IFRIC 9 *Reassessment of Embedded Derivatives* was issued in March 2006.

- (b) the criteria in IAS 38 for revaluation (including the existence of an active market) (paragraph D7 of the IFRS).

Transaction costs: financial instruments

- BC72 To determine the amortised cost of a financial asset or financial liability using the effective interest method, it is necessary to determine the transaction costs incurred when the asset or liability was originated. Some respondents to ED 1 argued that determining these transaction costs could involve undue cost or effort for financial assets or financial liabilities originated long before the date of transition to IFRSs. They suggested that the Board should permit a first-time adopter:
- (a) to use the fair value of the financial asset or financial liability at the date of transition to IFRSs as its deemed cost at that date; or
- (b) to determine amortised cost without considering transaction costs.
- BC73 In the Board's view, the unamortised portion of transaction costs at the date of transition to IFRSs is unlikely to be material for most financial assets and financial liabilities. Even when the unamortised portion is material, reasonable estimates should be possible. Therefore, the Board created no exemption in this area.

Retrospective designation

- BC74 The Board considered practical implementation difficulties that could arise from the retrospective application of aspects of IAS 39.²⁴
- (a) hedge accounting (paragraphs BC75–BC80);
- (b) government loans (paragraphs BC80A–BC80E);
- (c) the treatment of cumulative fair value changes on available-for-sale financial assets²⁵ at the date of transition to IFRSs (paragraphs BC81–BC83); and
- (d) 'day 1' gain or loss recognition (paragraph BC83A).

Hedge accounting²⁶

- BC75 Before beginning their preparations for adopting IAS 39 (or a local standard based on IAS 39), it is unlikely that most entities would have adopted IAS 39's criteria for (a) documenting hedges at their inception and (b) testing the hedges for effectiveness, even if they intended to continue the same hedging strategies after adopting IAS 39. Furthermore, retrospective designation of hedges (or retrospective reversal of their designation) could lead to selective designation of some hedges to report a particular result.
- BC76 To overcome these problems, the transitional requirements in IAS 39 require an entity already applying IFRSs to apply the hedging requirements prospectively when it adopts IAS 39. As the same problems arise for a first-time adopter, the IFRS requires prospective application by a first-time adopter.
- BC77 ED 1 included a redrafted version of the transitional provisions in IAS 39 and related *Questions and Answers* (Q&As) developed by the IAS 39 Implementation Guidance Committee. The Board confirmed in the Basis for Conclusions published with ED 1 that it did not intend the redrafting to create substantive changes. However, in the light of responses to ED 1, the Board decided in finalising IFRS 1 that the redrafting would not make it easier for first-time adopters and others to understand and apply the transitional provisions and Q&As. However, the project to improve IAS 32 and IAS 39 resulted in certain amendments to the transition requirements. In addition, this project incorporated selected other Q&As (ie not on transition) into IAS 39. The Board therefore took this opportunity to consolidate all the guidance for first-time adopters in one place, by incorporating the Q&As on transition into IFRS 1.
- BC78 Some respondents to ED 1 asked the Board to clarify what would happen if hedge accounting in accordance with previous GAAP involved hedging relationships of a type that does not qualify for hedge accounting in accordance with IAS 39. The problem can be seen most clearly for a hedge of a net position (macro hedge). If a first-time adopter were to use hedge accounting in its opening IFRS balance sheet for a hedge of a net position, this would involve either:

²⁴ IFRS 9 *Financial Instruments* replaced IAS 39. IFRS 9 applies to all items that were previously within the scope of IAS 39.

²⁵ IFRS 9 *Financial Instruments* eliminated the category of available-for-sale financial assets.

²⁶ IFRS 9 *Financial Instruments* replaced the hedge accounting requirements in IAS 39.

- (a) recognising deferred debits and credits that are not assets and liabilities (for a fair value hedge); or
- (b) deferring gains or losses in equity when there is, at best, a weak link to an underlying item that defines when they should be transferred to the income statement (for a cash flow hedge).

BC79 As either of these treatments would diminish the relevance and reliability of an entity's first IFRS financial statements, the Board decided that an entity should not apply hedge accounting in its opening IFRS balance sheet to a hedge of a net position that does not qualify as a hedged item in accordance with IAS 39. However, the Board concluded that it would be reasonable (and consistent with IAS 39 paragraph 133²⁷) to permit a first-time adopter to designate an individual item as a hedged item within the net position, provided that it does so no later than the date of transition to IFRSs, to prevent selective designation. For similar reasons, the Board prohibited hedge accounting in the opening IFRS balance sheet for any hedging relationship of a type that does not qualify for hedge accounting in accordance with IAS 39 (see paragraph B5 of the IFRS).

BC80 Some respondents to ED 1 suggested that an entity adopting IFRSs for the first time in 2005 could not meet IAS 39's documentation and effectiveness criteria by the date of transition to IFRSs (1 January 2004 for many entities). Some requested an exemption from these criteria until the beginning of the latest period covered by the first IFRS financial statements (1 January 2005 for many entities). However, for the following reasons, the Board did not create an exemption in this area:

- (a) The Board's primary objective is comparability within a first-time adopter's first IFRS financial statements and between different first-time adopters switching to IFRSs at the same time (paragraph BC10).
- (b) The continuation of previous GAAP hedge accounting practices could permit the non-recognition of derivatives or the recognition of deferred debits and credits that are not assets and liabilities.
- (c) The Board's benchmark for cost-benefit assessments was an entity that has planned the transition to IFRSs and is able to collect the necessary information at, or very soon after, the date of transition to IFRSs (paragraph BC27). Entities should not be 'rewarded' by concessions if they failed to plan for transition, nor should that failure be allowed to undermine the integrity of their opening IFRS balance sheet. Entities switching to IFRSs in 2005 need to have their hedge accounting systems in place by the beginning of 2004. In the Board's view, that is a challenging but achievable timetable. Entities preparing to switch to IFRSs in 2004 should have been aware of the implications of IAS 39 already and the exposure draft of improvements to IAS 39, published in June 2002, proposed very few changes in this area, so delayed transition is not justified for these entities either.

Government loans

BC80A IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* (as revised in May 2008) introduced a requirement that government loans with a below-market rate of interest shall be measured at fair value on initial recognition. At the time this requirement was added, the Board recognised that applying it retrospectively may require entities to measure the fair value of loans at an earlier date. Accordingly, the Board decided that entities should apply this requirement in IAS 20 prospectively, with earlier application permitted.

BC80B In 2011 the application of this requirement by first-time adopters was brought to the Board's attention. The Board noted that the general requirement in IFRS 1 for first-time adopters to apply IFRSs retrospectively at the date of transition to IFRSs could require some entities to measure such government loans at fair value at a date before the date of transition to IFRSs. This may lead to an entity applying hindsight if it must derive a fair value that needs significant unobservable inputs. Accordingly, the Board decided to add an exception to the retrospective application of IFRSs to require that first-time adopters shall apply the requirements of IAS 20 prospectively to government loans existing at the date of transition to IFRSs, unless the necessary information was obtained at the time of initially accounting for that loan. As a result of not applying IAS 20 and IFRS 9 retrospectively to government loans at the date of transition, the corresponding benefit of the government loan at a below-market rate of interest is not recognised as a government grant.

BC80C The Board proposed the exception in October 2011 in the exposure draft *Government Loans* (proposed amendments to IFRS 1). In recognition of comments on the exposure draft, the Board revised paragraph B10 to specify that an entity applies IAS 32 *Financial Instruments: Presentation* to classify the government loans as a financial liability or an equity instrument, and to limit the scope of the exemption to matters of recognition and measurement. This will give first-time adopters the same relief as existing preparers and will mean that if a first-time adopter had classified government loans in equity under its previous GAAP, it will reclassify those loans as liabilities, if those loans meet the definition of a financial liability in IAS 32. The Board also clarified that an entity should use its previous GAAP carrying amount of such loans at the date of transition to IFRSs as

²⁷ In IAS 39, as revised in 2003, paragraph 133 was replaced by paragraphs 84 and AG101.

the carrying amount in the opening IFRS statement of financial position. IFRS 9 should be applied to such loans subsequently.

- BC80D Some respondents to the exposure draft asked why the retrospective application of IAS 20 should be optional, rather than mandatory, if the information needed to apply IFRS 9 had been obtained. The Board thought that mandatory restatement could require an onerous search to determine whether this information had been obtained when initially accounting for loans that were received many years ago.
- BC80E The Board noted that prohibiting the application of this option on a loan-by-loan basis might introduce further complexity into IFRS 1. This is because it may raise further questions, such as whether the retrospective application would be permitted for all the loans for which the information needed was obtained at the time, even if there are other similar loans for which the fair value information was not obtained at that time; and whether the retrospective application should be restricted to all loans received after a certain date and for which all necessary information was obtained to enable retrospective application. The Board concluded that the exception proposed in paragraph B11 should be available on a loan-by-loan basis.
- BC80F In November 2013 the Board amended the examples in the guidance on hedge accounting so that they conformed to IFRS 9, as amended in November 2013, which replaced the hedge accounting requirements in IAS 39.

Available-for-sale financial assets²⁸

- BC81 Retrospective application of IAS 39²⁹ to available-for-sale financial assets requires a first-time adopter to recognise the cumulative fair value changes in a separate component of equity in the opening IFRS balance sheet, and transfer those fair value changes to the income statement on subsequent disposal or impairment of the asset. This could allow, for example, selective classification of assets with cumulative gains as available for sale (with subsequent transfers to the income statement on disposal) and assets with cumulative losses as held for trading (with no transfers on disposal).
- BC82 IAS 39 confirmed the proposal in the exposure draft of June 2002 to give an entity that already applies IFRSs an option to designate any financial asset as at fair value through profit or loss when it first applies the proposed improvements. Although this requirement could increase the risk of selective classification by first-time adopters of the kind discussed in the previous paragraph, the Board noted that an entity could achieve a similar result by selective disposal of some assets before the date of transition to IFRSs. Therefore, the Board concluded that it should treat first-time adopters in the same way as entities that already apply IFRSs by requiring retrospective application.
- BC83 Some respondents to ED 1 commented that the cost of determining the amount to be included in a separate component of equity would exceed the benefits. However, the Board noted that these costs would be minimal if a first-time adopter carried the available-for-sale financial assets in accordance with previous GAAP at cost or the lower of cost and market value. These costs might be more significant if it carried them at fair value, but in that case it might well classify the assets as held for trading. Therefore, the Board made no changes to ED 1's proposal that a first-time adopter should apply IAS 39 retrospectively to available-for-sale financial assets.
- 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.

In 2010 the Board was asked to reconsider whether the fixed dates of 25 October 2002 and 1 January 2004 continued to be appropriate for first-time adopters. Constituents were concerned that, as time passes, these fixed dates become 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 25 October 2002 or 1 January 2004 was likely to outweigh the benefit to be achieved in doing so. It therefore amended the fixed dates included in paragraph D20 of IFRS 1 to permit a first-time adopter to

²⁸ IFRS 9 *Financial Instruments* eliminated the category of available-for-sale financial assets.

²⁹ IFRS 9 *Financial Instruments* replaced IAS 39. IFRS 9 applies to all items that were previously within the scope of IAS 39.

apply the ‘day 1’ gain or loss recognition requirement in IAS 39 paragraphs AG76 and AG76A prospectively from ‘the date of transition to IFRSs’.³⁰

Estimates

- BC84 An entity will have made estimates in accordance with previous GAAP at the date of transition to IFRSs. Events between that date and the reporting date for the entity’s first IFRS financial statements might suggest a need to change those estimates. Some of those events might qualify as adjusting events in accordance with IAS 10 *Events after the Balance Sheet Date*.³¹ However, if the entity made those estimates on a basis consistent with IFRSs, the Board concluded that it would be more helpful to users—and more consistent with IAS 8—to recognise the revision of those estimates as income or expense in the period when the entity made the revision, rather than in preparing the opening IFRS balance sheet (paragraphs 14–17 of the IFRS).

Presentation and disclosure

Comparative information

- BC85 IAS 1 requires an entity to disclose comparative information (in accordance with IFRSs) for the previous period. Some suggested that a first-time adopter should disclose comparative information for more than one previous period. For entities that already apply IFRSs, users normally have access to financial statements prepared on a comparable basis for several years. However, this is not the case for a first-time adopter.
- BC86 Nevertheless, the Board did not require a first-time adopter to present more comparative information than IAS 1 requires, because such a requirement would impose costs out of proportion to the benefits to users, and increase the risk that preparers might need to make arbitrary assumptions in applying hindsight.
- BC87 ED 1 proposed that if the first IFRS financial statements include more than one year of comparative information, the additional comparative information should comply with IFRSs. Some respondents to ED 1 noted that some regulators require entities to prepare more than two years of comparatives. They argued the following:
- (a) A requirement to restate two years of comparatives would impose excessive costs and lead to arbitrary restatements that might be biased by hindsight.
 - (b) Consider an entity adopting IFRSs in 2005 and required by its regulator to give two years of comparatives. Its date of transition to IFRSs would be 1 January 2003—several months before the publication of the IFRS and of the standards resulting from the improvements project. This could contradict the Board’s assertion in paragraph BC27 above that most preparers could gather most information they need for their opening IFRS balance sheet at, or soon after, the date of transition to IFRSs.
- BC88 In response to these comments, the Board deleted this proposal. Instead, if a first-time adopter elects to give more than one year of comparative information, the additional comparative information need not comply with IFRSs, but the IFRS requires the entity:
- (a) to label previous GAAP information prominently as not being prepared in accordance with IFRSs.
 - (b) to disclose the nature of the main adjustments that would make it comply with IFRSs (paragraph 22 of the IFRS).
- BC89 Some respondents to ED 1 suggested that it would be onerous to prepare comparative information in accordance with IAS 32 and IAS 39³² about financial instruments. They suggested that an entity should be able to apply IAS 39 prospectively from the beginning of the year of its first IFRS financial statements (eg 1 January 2005 for many first-time adopters). They noted that US companies were not required to restate comparatives on the introduction of SFAS 133 *Accounting for Derivative Instruments and Hedging Activities*. However, given the

³⁰ IFRS 9 *Financial Instruments* replaced IAS 39. Paragraphs AG76 and AG76A of IAS 39 were relocated to IFRS 9 as paragraphs B5.4.8 and B5.4.9. However, in May 2011 IFRS 13 deleted paragraphs B5.4.8 and B5.4.9 of IFRS 9. In 2014 the requirements for amortised cost measurement and impairment were added to IFRS 9 as Sections 5.4 and 5.5. Paragraphs B5.4.8 and B5.4.9 of IFRS 9 now contain requirements related to amortised cost measurement.

³¹ In September 2007 the IASB amended the title of IAS 10 *Events after the Balance Sheet Date* to *Events after the Reporting Period* as a consequence of the revision of IAS 1 *Presentation of Financial Statements* in 2007.

³² IFRS 9 *Financial Instruments* replaced IAS 39. IFRS 9 applies to all items that were previously within the scope of IAS 39.

Board's emphasis on comparability within the first IFRS financial statements (paragraph BC10) and the assumption of timely planning (paragraph BC27), the Board introduced no general exemption in this area.

- BC89A Nevertheless, the Board noted that the revised IAS 32 and IAS 39³³ were not issued until December 2003. Additionally, the Board's decision to re-expose its proposals for portfolio hedges of interest rate risk had the effect that some of the requirements will not be finalised until early 2004. The Board was sympathetic to concerns that entities that will be required to comply with IFRSs for the first time in 2005 could not make a timely transition to IFRSs because IAS 39 will not be issued in final form until after the start of 2004. Therefore, the Board decided to exempt entities adopting IFRSs for the first time before 1 January 2006 from producing comparative information that complies with IAS 32 and IAS 39, as revised in 2003, in their first IFRS financial statements.
- BC89B In the light of respondents' comments on the June 2011 exposure draft *Improvements to IFRSs*, the Board amended paragraph 21 as part of *Annual Improvements 2009–2011 Cycle* (issued in May 2012) because it considered that the requirements for comparative information for a first-time adopter should be different from the requirements for comparative information for an existing preparer. The Board noted that a first-time adopter should not be exempted from presenting three statements of financial position and related notes because it might not have presented this information previously on a basis consistent with IFRSs.
- BC89C In addition, the Board considered that a first-time adopter may provide additional comparative information that is presented in accordance with previous GAAP to help the user understand the effects of the transition to IFRSs in accordance with paragraph 22 of IFRS 1. For example, a law or a regulator requires an entity to present the first comparative financial statements in accordance with both IFRSs and previous GAAP and the second comparative in accordance with previous GAAP only. The presentation of this information is an exception from the requirement in paragraph 38C of IAS 1 (to allow an entity to present comparative information in addition to the minimum comparative information required by IFRSs).

Historical summaries

- BC90 Some entities choose, or are required, to present in their financial statements historical summaries of selected data covering periods before the first period for which they present full comparative information. Some argued that an entity should present this information in accordance with IFRSs, to ensure comparability over time. However, the Board concluded that such a requirement would cause costs out of proportion to the benefit to users. The IFRS requires disclosure of the nature of the main adjustments needed to make historical summaries included in financial statements or interim financial reports comply with IFRSs (paragraph 22 of the IFRS). Historical summaries published outside financial statements or interim financial reports are beyond the scope of the IFRS.

Explanation of transition to IFRSs

- BC91 The IFRS requires disclosures about the effect of the transition from previous GAAP to IFRSs. The Board concluded that such disclosures are essential, in the first (annual) IFRS financial statements as well as in interim financial reports (if any), because they help users understand the effect and implications of the transition to IFRSs and how they need to change their analytical models to make the best use of information presented using IFRSs. The required disclosures relate to both:
- (a) the most recent information published in accordance with previous GAAP, so that users have the most up-to-date information; and
 - (b) the date of transition to IFRSs. This is an important focus of attention for users, preparers and auditors because the opening IFRS balance sheet is the starting point for accounting in accordance with IFRSs.
- BC92 Paragraph 24(a) and (b) of the IFRS requires reconciliations of equity and total comprehensive income. The Board concluded that users would also find it helpful to have information about the other adjustments that affect the opening IFRS balance sheet but do not appear in these reconciliations. Because a reconciliation could be voluminous, the IFRS requires disclosure of narrative information about these adjustments, as well as about adjustments to the cash flow statement (paragraph 25 of the IFRS).
- BC92A The Board decided to require a first-time adopter to include in its first IFRS financial statements a reconciliation of total comprehensive income (or, if an entity did not report such a total, profit or loss) in accordance with previous GAAP to total comprehensive income in accordance with IFRSs for the latest period reported in accordance with previous GAAP.

³³ IFRS 9 *Financial Instruments* replaced IAS 39. IFRS 9 applies to all items that were previously within the scope of IAS 39.

- BC92B The Board observed that the amendments to IAS 1 in 2007 regarding the presentation of income and expense might result in users having to change their analytical models to include both income and expense that are recognised in profit or loss and those recognised outside profit or loss. Accordingly, the Board concluded that it would be helpful to those users to provide information on the effect and implication of the transition to IFRSs on all items of income and expense, not only those recognised in profit or loss.
- BC92C The Board acknowledged that GAAP in other jurisdictions might not have a notion of total comprehensive income. Accordingly, it decided that an entity should reconcile to total comprehensive income in accordance with IFRSs from the previous GAAP equivalent of total comprehensive income. The previous GAAP equivalent might be profit or loss.
- BC93 Paragraph 26 of the IFRS states that the reconciliations should distinguish changes in accounting policies from the correction of errors. Some respondents to ED 1 argued that complying with this requirement could be difficult or costly. However, the Board concluded that both components are important and their disclosure should be required because:
- (a) information about changes in accounting policies helps explain the transition to IFRSs.
 - (b) information about errors helps users assess the reliability of financial information. Furthermore, a failure to disclose the effect of material errors would obscure the ‘results of the stewardship of management, or the accountability of management for the resources entrusted to it’ (*Framework*, paragraph 14).
- BC94 For impairment losses (and reversals) recognised in preparing the opening IFRS balance sheet, paragraph 24(c) of the IFRS requires the disclosures that IAS 36 would require if those impairment losses (and reversals) were recognised during the period beginning with the date of transition to IFRSs. The rationale for this requirement is that there is inevitably subjectivity about impairment losses. This disclosure provides transparency about impairment losses recognised on transition to IFRSs. These losses might otherwise receive less attention than impairment losses recognised in earlier or later periods.
- BC95 Paragraph 30 of the IFRS requires disclosures about the use of fair value as deemed cost. Although the adjustment arising from the use of this exemption appears in the reconciliations discussed above, this more specific disclosure highlights it. Furthermore, this exemption differs from the other exemptions that might apply for property, plant and equipment (previous GAAP revaluation or event-driven fair value measurement). The latter two exemptions do not lead to a restatement on transition to IFRSs because they apply only if the measurement was already used in previous GAAP financial statements.
- BC95A In August 2023 the IASB amended IAS 21 to define when a currency is exchangeable into another currency. The IASB made conforming amendments to paragraphs 31C and D27 of IFRS 1 which previously referred to, but did not define, exchangeability.

Interim financial reports

- BC96 IAS 34 *Interim Financial Reporting* states that the interim financial report is ‘intended to provide an update on the latest complete set of annual financial statements’ (paragraph 6). Thus, IAS 34 requires less disclosure in interim financial statements than IFRSs require in annual financial statements. However, an entity’s interim financial report in accordance with IAS 34 is less helpful to users if the entity’s latest annual financial statements were prepared using previous GAAP than if they were prepared in accordance with IFRSs. Therefore, the Board concluded that a first-time adopter’s first interim financial report in accordance with IAS 34 should include sufficient information to enable users to understand how the transition to IFRSs affected previously reported annual, as well as interim, figures (paragraphs 32 and 33 of the IFRS).

Accounting policy changes in the year of adoption

- BC97 In *Improvements to IFRSs* issued in May 2010, the Board clarified unclear wording concerning how changes in accounting policies should be addressed by a first-time adopter when those changes occur after the publication of the entity’s first interim financial report. The Board decided that a first-time adopter is exempt from all the requirements of IAS 8 for the interim financial report it presents in accordance with IAS 34 for part of the period covered by its first IFRS financial statements and for its first IFRS financial statements. The Board concluded that to comply with IFRS 1’s requirement to explain its transition to IFRSs, an entity should be required to explain any changes in its accounting policies or the IFRS 1 exemptions it applied between its first IFRS interim financial report and its first IFRS financial statements. The Board decided that the most useful information it could require was updated reconciliations between previous GAAP and IFRSs.

Short-term exemptions from IFRSs

BC98 [Deleted by IASB]³⁴

Deletion of short-term exemptions (amendments issued in December 2016)

BC99 In *Annual Improvements to IFRS Standards 2014–2016 Cycle*, the Board deleted the short-term exemptions in paragraphs E3–E7 and the related effective date paragraphs. The Board noted that the reliefs provided in those paragraphs were no longer applicable. The reliefs provided had been available to entities only for reporting periods that had passed.

³⁴ *Annual Improvements to IFRS Standards 2014–2016 Cycle*, issued in December 2016, deleted some short-term exemptions for first-time adopters (see paragraph BC99), and as a consequence deleted paragraph BC98.

Appendix

Amendments to Basis for Conclusions on other IFRSs

This appendix contains amendments to the Basis for Conclusions on other IFRSs that are necessary to ensure consistency with IFRS 1 (as revised in 2008).

The amendments contained in this appendix when the revised IFRS1 was issued in 2008 have been incorporated into the text of the Basis for Conclusions on IFRS 6 and IASs 27 and 39 as issued at 27 November 2008.

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IFRS 1 *FIRST-TIME ADOPTION OF INTERNATIONAL FINANCIAL
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Guidance on implementing IFRS 1 *First-time Adoption of International Financial Reporting Standards*

This guidance accompanies, but is not part of, IFRS 1.

Introduction

IG1 This implementation guidance:

- (a) explains how the requirements of the IFRS interact with the requirements of some other IFRSs (paragraphs IG2–IG62, IG64 and IG65). This explanation addresses those IFRSs that are most likely to involve questions that are specific to first-time adopters.
- (b) includes an illustrative example to show how a first-time adopter might disclose how the transition to IFRSs affected its reported financial position, financial performance and cash flows, as required by paragraphs 24(a) and (b), 25 and 26 of the IFRS (paragraph IG63).

IAS 10 Events after the Reporting Period

IG2 Except as described in paragraph IG3, an entity applies IAS 10 in determining whether:

- (a) its opening IFRS statement of financial position reflects an event that occurred after the date of transition to IFRSs; and
- (b) comparative amounts in its first IFRS financial statements reflect an event that occurred after the end of that comparative period.

IG3 Paragraphs 14–17 of the IFRS require some modifications to the principles in IAS 10 when a first-time adopter determines whether changes in estimates are adjusting or non-adjusting events at the date of transition to IFRSs (or, when applicable, the end of the comparative period). Cases 1 and 2 below illustrate those modifications. In case 3 below, paragraphs 14–17 of the IFRS do not require modifications to the principles in IAS 10.

- (a) Case 1—Previous GAAP required estimates of similar items for the date of transition to IFRSs, using an accounting policy that is consistent with IFRSs. In this case, the estimates in accordance with IFRSs need to be consistent with estimates made for that date in accordance with previous GAAP, unless there is objective evidence that those estimates were in error (see IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*). The entity reports later revisions to those estimates as events of the period in which it makes the revisions, rather than as adjusting events resulting from the receipt of further evidence about conditions that existed at the date of transition to IFRSs.
- (b) Case 2—Previous GAAP required estimates of similar items for the date of transition to IFRSs, but the entity made those estimates using accounting policies that are not consistent with its accounting policies in accordance with IFRSs. In this case, the estimates in accordance with IFRSs need to be consistent with the estimates required in accordance with previous GAAP for that date (unless there is objective evidence that those estimates were in error), after adjusting for the difference in accounting policies. The opening IFRS statement of financial position reflects those adjustments for the difference in accounting policies. As in case 1, the entity reports later revisions to those estimates as events of the period in which it makes the revisions.

For example, previous GAAP may have required an entity to recognise and measure provisions on a basis consistent with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, except that the previous GAAP measurement was on an undiscounted basis. In this example, the entity uses the estimates in accordance with previous GAAP as inputs in making the discounted measurement required by IAS 37.

- (c) Case 3—Previous GAAP did not require estimates of similar items for the date of transition to IFRSs. Estimates in accordance with IFRSs for that date reflect conditions existing at that date. In particular, estimates of market prices, interest rates or foreign exchange rates at the date of transition to IFRSs reflect market conditions at that date. This is consistent with the distinction in IAS 10 between adjusting events after the reporting period and non-adjusting events after the reporting period.

IG Example 1 Estimates**Background**

Entity A's first IFRS financial statements are for a period that ends on 31 December 20X5 and include comparative information for one year. In its previous GAAP financial statements for 31 December 20X3 and 20X4, entity A:

- (a) made estimates of accrued expenses and provisions at those dates;
- (b) accounted on a cash basis for a defined benefit pension plan; and
- (c) did not recognise a provision for a court case arising from events that occurred in September 20X4. When the court case was concluded on 30 June 20X5, entity A was required to pay CU1,000^a and paid this on 10 July 20X5.

In preparing its first IFRS financial statements, entity A concludes that its estimates in accordance with previous GAAP of accrued expenses and provisions at 31 December 20X3 and 20X4 were made on a basis consistent with its accounting policies in accordance with IFRSs. Although some of the accruals and provisions turned out to be overestimates and others to be underestimates, entity A concludes that its estimates were reasonable and that, therefore, no error had occurred. As a result, accounting for those overestimates and underestimates involves the routine adjustment of estimates in accordance with IAS 8.

Application of requirements

In preparing its opening IFRS statement of financial position at 1 January 20X4 and in its comparative statement of financial position at 31 December 20X4, entity A:

- (a) does not adjust the previous estimates for accrued expenses and provisions; and
- (b) makes estimates (in the form of actuarial assumptions) necessary to account for the pension plan in accordance with IAS 19 *Employee Benefits*. Entity A's actuarial assumptions at 1 January 20X4 and 31 December 20X4 do not reflect conditions that arose after those dates. For example, entity A's:
 - (i) discount rates at 1 January 20X4 and 31 December 20X4 for the pension plan and for provisions reflect market conditions at those dates; and
 - (ii) actuarial assumptions at 1 January 20X4 and 31 December 20X4 about future employee turnover rates do not reflect conditions that arose after those dates—such as a significant increase in estimated employee turnover rates as a result of a curtailment of the pension plan in 20X5.

The treatment of the court case at 31 December 20X4 depends on the reason why entity A did not recognise a provision in accordance with previous GAAP at that date.

Assumption 1 – Previous GAAP was consistent with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. Entity A concluded that the recognition criteria were not met. In this case, entity A's assumptions in accordance with IFRSs are consistent with its assumptions in accordance with previous GAAP. Therefore, entity A does not recognise a provision at 31 December 20X4.

Assumption 2 – Previous GAAP was not consistent with IAS 37. Therefore, entity A develops estimates in accordance with IAS 37. Under IAS 37, an entity determines whether an obligation exists at the end of the reporting period by taking account of all available evidence, including any additional evidence provided by events after the reporting period. Similarly, in accordance with IAS 10 *Events after the Reporting Period*, the resolution of a court case after the reporting period is an adjusting event after the reporting period if it confirms that the entity had a present obligation at that date. In this instance, the resolution of the court case confirms that entity A had a liability in September 20X4 (when the events occurred that gave rise to the court case). Therefore, entity A recognises a provision at 31 December 20X4. Entity A measures that provision by discounting the CU1,000 paid on 10 July 20X5 to its present value, using a discount rate that complies with IAS 37 and reflects market conditions at 31 December 20X4.

[a] In this guidance monetary amounts are denominated in 'currency units (CU)'.

IG4 Paragraphs 14–17 of the IFRS do not override requirements in other IFRSs that base classifications or measurements on circumstances existing at a particular date. Examples include:

- (a) the distinction between finance leases and operating leases for a lessor (see IFRS 16 *Leases* and paragraph IG14);
- (b) the restrictions in IAS 38 *Intangible Assets* that prohibit capitalisation of expenditure on an internally generated intangible asset if the asset did not qualify for recognition when the expenditure was incurred; and
- (c) the distinction between financial liabilities and equity instruments (see IAS 32 *Financial Instruments: Presentation*).

IAS 12 *Income Taxes*

- IG5 An entity applies IAS 12 to temporary differences between the carrying amount of the assets and liabilities in its opening IFRS statement of financial position and their tax bases.
- IG6 In accordance with IAS 12, the measurement of current and deferred tax reflects tax rates and tax laws that have been enacted or substantively enacted by the end of the reporting period. An entity accounts for the effect of changes in tax rates and tax laws when those changes are enacted or substantively enacted.

IAS 16 *Property, Plant and Equipment*

- IG7 If an entity's depreciation methods and rates in accordance with previous GAAP are acceptable in accordance with IFRSs, it accounts for any change in estimated useful life or depreciation pattern prospectively from when it makes that change in estimate (paragraphs 14 and 15 of the IFRS and paragraph 61 of IAS 16). However, in some cases, an entity's depreciation methods and rates in accordance with previous GAAP may differ from those that would be acceptable in accordance with IFRSs (for example, if they were adopted solely for tax purposes and do not reflect a reasonable estimate of the asset's useful life). If those differences have a material effect on the financial statements, the entity adjusts accumulated depreciation in its opening IFRS statement of financial position retrospectively so that it complies with IFRSs.
- IG8 An entity may elect to use one of the following amounts as the deemed cost of an item of property, plant and equipment:
- fair value at the date of transition to IFRSs (paragraph D5 of the IFRS), in which case the entity gives the disclosures required by paragraph 30 of the IFRS;
 - a revaluation in accordance with previous GAAP that meets the criteria in paragraph D6 of the IFRS;
 - fair value at the date of an event such as a privatisation or initial public offering (paragraph D8 of the IFRS);
 - an allocation of an amount determined under previous GAAP that meets the criteria in paragraph D8A of the IFRS; or
 - the carrying amount under previous GAAP of an item of property, plant and equipment that is used, or was previously used, in operations subject to rate regulation (paragraph D8B of the IFRS).
- IG9 Subsequent depreciation is based on that deemed cost and starts from the date for which the entity established the deemed cost.
- IG10 If an entity chooses as its accounting policy the revaluation model in IAS 16 for some or all classes of property, plant and equipment, it presents the cumulative revaluation surplus as a separate component of equity. The revaluation surplus at the date of transition to IFRSs is based on a comparison of the carrying amount of the asset at that date with its cost or deemed cost. If the deemed cost is the fair value at the date of transition to IFRSs, the entity gives the disclosures required by paragraph 30 of the IFRS.
- IG11 If revaluations in accordance with previous GAAP did not satisfy the criteria in paragraph D6 or D8 of the IFRS, an entity measures the revalued assets in its opening statement of financial position on one of the following bases:
- cost (or deemed cost) less any accumulated depreciation and any accumulated impairment losses under the cost model in IAS 16;
 - deemed cost, being the fair value at the date of transition to IFRSs (paragraph D5 of the IFRS); or
 - revalued amount, if the entity adopts the revaluation model in IAS 16 as its accounting policy in accordance with IFRSs for all items of property, plant and equipment in the same class.
- IG12 IAS 16 requires each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item to be depreciated separately. However, IAS 16 does not prescribe the unit of measure for recognition of an asset, ie what constitutes an item of property, plant and equipment. Thus, judgement is required in applying the recognition criteria to an entity's specific circumstances (see IAS 16 paragraphs 9 and 43).
- IG13 In some cases, the construction or commissioning of an asset results in an obligation for an entity to dismantle or remove the asset and restore the site on which the asset stands. An entity applies IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* in recognising and measuring any resulting provision. The entity applies IAS 16 in determining the resulting amount included in the cost of the asset, before depreciation and impairment losses. Items such as depreciation and, when applicable, impairment losses cause differences between the carrying amount of the liability and the amount included in the carrying amount of the asset. An

entity accounts for changes in such liabilities in accordance with IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*. However, paragraph D21 of IFRS 1 provides an exemption for changes that occurred before the date of transition to IFRSs, and prescribes an alternative treatment where the exemption is used. An example of the first-time adoption of IFRIC 1, which illustrates the use of this exemption, is given at paragraphs IG201–IG203.

IFRS 16 Leases

IG14 At the date of transition to IFRSs, a lessor classifies leases as operating leases or finance leases on the basis of circumstances existing at the inception of the lease (IFRS 16, paragraph 66). Lease classification is reassessed only if there is a lease modification. Changes in estimates (for example, changes in estimates of the economic life or of the residual value of the underlying asset) or changes in circumstances (for example, default by the lessee) do not give rise to a new classification of a lease.

IG15 [Deleted]

IG16 [Deleted]

IFRS 15 Revenue from Contracts with Customers

IG17 If an entity has received amounts that do not yet qualify for recognition as revenue in accordance with IFRS 15 (for example, the proceeds of a sale that does not qualify for revenue recognition), the entity recognises a liability in its opening IFRS statement of financial position and measures that liability at the amount received, adjusted if appropriate for a significant financing component in accordance with IFRS 15.

IAS 19 Employee Benefits

IG18 [Deleted]

IG19 An entity's actuarial assumptions at the date of transition to IFRSs are consistent with actuarial assumptions made for the same date in accordance with previous GAAP (after adjustments to reflect any difference in accounting policies), unless there is objective evidence that those assumptions were in error (paragraph 14 of the IFRS). The impact of any later revisions to those assumptions is an actuarial gain or loss of the period in which the entity makes the revisions.

IG20 An entity may need to make actuarial assumptions at the date of transition to IFRSs that were not necessary in accordance with its previous GAAP. Such actuarial assumptions do not reflect conditions that arose after the date of transition to IFRSs. In particular, discount rates and the fair value of plan assets at the date of transition to IFRSs reflect market conditions at that date. Similarly, the entity's actuarial assumptions at the date of transition to IFRSs about future employee turnover rates do not reflect a significant increase in estimated employee turnover rates as a result of a curtailment of the pension plan that occurred after the date of transition to IFRSs (paragraph 16 of the IFRS).

IG21 In many cases, an entity's first IFRS financial statements will reflect measurements of employee benefit obligations at three dates: the end of the first IFRS reporting period, the date of the comparative statement of financial position and the date of transition to IFRSs. IAS 19 encourages an entity to involve a qualified actuary in the measurement of all material post-employment benefit obligations. To minimise costs, an entity may request a qualified actuary to carry out a detailed actuarial valuation at one or two of these dates and roll the valuation(s) forward or back to the other date(s). Any such roll forward or roll back reflects any material transactions and other material events (including changes in market prices and interest rates) between those dates (IAS 19 paragraph 57).

IAS 21 The Effects of Changes in Foreign Exchange Rates

IG21A An entity may, in accordance with previous GAAP, have treated goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition of that foreign operation as assets and liabilities of the entity rather than as assets and liabilities of the foreign operation. If so, the entity is permitted to apply prospectively the requirements of paragraph 47 of IAS 21 to all acquisitions occurring after the date of transition to IFRSs.

IFRS 3 *Business Combinations*

IG22 The following examples illustrate the effect of Appendix C of the IFRS, assuming that a first-time adopter uses the exemption.

IG Example 2 Business combination	
Background	
<p>Entity B's first IFRS financial statements are for a period that ends on 31 December 20X5 and include comparative information for 20X4 only. On 1 July 20X1, entity B acquired 100 per cent of subsidiary C. In accordance with its previous GAAP, entity B:</p>	
<ul style="list-style-type: none"> (a) classified the business combination as an acquisition by entity B. (b) measured the assets acquired and liabilities assumed at the following amounts in accordance with previous GAAP at 31 December 20X3 (date of transition to IFRSs): <ul style="list-style-type: none"> (i) identifiable assets less liabilities for which IFRSs require cost-based measurement at a date after the business combination: CU200 (with a tax base of CU150 and an applicable tax rate of 30 per cent). (ii) pension liability (for which the present value of the defined benefit obligation measured in accordance with IAS 19 <i>Employee Benefits</i> is CU130 and the fair value of plan assets is CU100): nil (because entity B used a pay as you go cash method of accounting for pensions in accordance with its previous GAAP). The tax base of the pension liability is also nil. (iii) goodwill: CU180. (c) did not, at the acquisition date, recognise deferred tax arising from temporary differences associated with the identifiable assets acquired and liabilities assumed. 	
Application of requirements	
<p>In its opening (consolidated) IFRS statement of financial position, entity B:</p>	
<ul style="list-style-type: none"> (a) classifies the business combination as an acquisition by entity B even if the business combination would have qualified in accordance with IFRS 3 as a reverse acquisition by subsidiary C (paragraph C4(a) of the IFRS). (b) does not adjust the accumulated amortisation of goodwill. Entity B tests the goodwill for impairment in accordance with IAS 36 <i>Impairment of Assets</i> and recognises any resulting impairment loss, based on conditions that existed at the date of transition to IFRSs. If no impairment exists, the carrying amount of the goodwill remains at CU180 (paragraph C4(g) of the IFRS). (c) for those net identifiable assets acquired for which IFRSs require cost-based measurement at a date after the business combination, treats their carrying amount in accordance with previous GAAP immediately after the business combination as their deemed cost at that date (paragraph C4(e) of the IFRS). 	
<i>continued...</i>	

...continued

IG Example 2 Business combination

- (d) does not restate the accumulated depreciation and amortisation of the net identifiable assets in (c), unless the depreciation methods and rates in accordance with previous GAAP result in amounts that differ materially from those required in accordance with IFRSs (for example, if they were adopted solely for tax purposes and do not reflect a reasonable estimate of the asset's useful life in accordance with IFRSs). If no such restatement is made, the carrying amount of those assets in the opening IFRS statement of financial position equals their carrying amount in accordance with previous GAAP at the date of transition to IFRSs (CU200) (paragraph IG7).
- (e) if there is any indication that identifiable assets are impaired, tests those assets for impairment, based on conditions that existed at the date of transition to IFRSs (see IAS 36).
- (f) recognises the pension liability, and measures it, at the present value of the defined benefit obligation (CU130) less the fair value of the plan assets (CU100), giving a carrying amount of CU30, with a corresponding debit of CU30 to retained earnings (paragraph C4(d) of the IFRS). However, if subsidiary C had already adopted IFRSs in an earlier period, entity B would measure the pension liability at the same amount as in subsidiary C's financial statements (paragraph D17 of the IFRS and IG Example 9).
- (g) recognises a net deferred tax liability of CU6 (CU20 at 30 per cent) arising from:
- (i) the taxable temporary difference of CU50 (CU200 less CU150) associated with the identifiable assets acquired and non-pension liabilities assumed, less
 - (ii) the deductible temporary difference of CU30 (CU30 less nil) associated with the pension liability.

The entity recognises the resulting increase in the deferred tax liability as a deduction from retained earnings (paragraph C4(k) of the IFRS). If a taxable temporary difference arises from the initial recognition of the goodwill, entity B does not recognise the resulting deferred tax liability (paragraph 15(a) of IAS 12 *Income Taxes*).

IG Example 3 Business combination—restructuring provision

Background

Entity D's first IFRS financial statements are for a period that ends on 31 December 20X5 and include comparative information for 20X4 only. On 1 July 20X3, entity D acquired 100 per cent of subsidiary E. In accordance with its previous GAAP, entity D recognised an (undiscounted) restructuring provision of CU100 that would not have qualified as an identifiable liability in accordance with IFRS 3. The recognition of this restructuring provision increased goodwill by CU100. At 31 December 20X3 (date of transition to IFRSs), entity D:

- (a) had paid restructuring costs of CU60; and
- (b) estimated that it would pay further costs of CU40 in 20X4, and that the effects of discounting were immaterial. At 31 December 20X3, those further costs did not qualify for recognition as a provision in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

Application of requirements

In its opening IFRS statement of financial position, entity D:

- (a) does not recognise a restructuring provision (paragraph C4(c) of the IFRS).
- (b) does not adjust the amount assigned to goodwill. However, entity D tests the goodwill for impairment in accordance with IAS 36 *Impairment of Assets*, and recognises any resulting impairment loss (paragraph C4(g) of the IFRS).
- (c) as a result of (a) and (b), reports retained earnings in its opening IFRS statement of financial position that are higher by CU40 (before income taxes, and before recognising any impairment loss) than in the statement of financial position at the same date in accordance with previous GAAP.

IG Example 4 Business combination—intangible assets**Background**

Entity F's first IFRS financial statements are for a period that ends on 31 December 20X5 and include comparative information for 20X4 only. On 1 July 20X1 entity F acquired 75 per cent of subsidiary G. In accordance with its previous GAAP, entity F assigned an initial carrying amount of CU200 to intangible assets that would not have qualified for recognition in accordance with IAS 38 *Intangible Assets*. The tax base of the intangible assets was nil, giving rise to a deferred tax liability (at 30 per cent) of CU60.

On 31 December 20X3 (the date of transition to IFRSs) the carrying amount of the intangible assets in accordance with previous GAAP was CU160, and the carrying amount of the related deferred tax liability was CU48 (30 per cent of CU160).

Application of requirements

Because the intangible assets do not qualify for recognition as separate assets in accordance with IAS 38, entity F transfers them to goodwill, together with the related deferred tax liability (CU48) and non-controlling interests (paragraph C4(g)(i) of the IFRS). The related non-controlling interests amount to CU28 (25 per cent of [CU160 – CU48 = CU112]). Thus, the increase in goodwill is CU84—intangible assets (CU160) less deferred tax liability (CU48) less non-controlling interests (CU28).

Entity F tests the goodwill for impairment in accordance with IAS 36 *Impairment of Assets* and recognises any resulting impairment loss, based on conditions that existed at the date of transition to IFRSs (paragraph C4(g)(ii) of the IFRS).

IG Example 5 Business combination—goodwill deducted from equity and treatment of related intangible assets**Background**

Entity H acquired a subsidiary before the date of transition to IFRSs. In accordance with its previous GAAP, entity H:

- (a) recognised goodwill as an immediate deduction from equity;
- (b) recognised an intangible asset of the subsidiary that does not qualify for recognition as an asset in accordance with IAS 38 *Intangible Assets*; and
- (c) did not recognise an intangible asset of the subsidiary that would qualify in accordance with IAS 38 for recognition as an asset in the financial statements of the subsidiary. The subsidiary held the asset at the date of its acquisition by entity H.

Application of requirements

In its opening IFRS statement of financial position, entity H:

- (a) does not recognise the goodwill, as it did not recognise the goodwill as an asset in accordance with previous GAAP (paragraph C4(g)–(i) of the IFRS).
- (b) does not recognise the intangible asset that does not qualify for recognition as an asset in accordance with IAS 38. Because entity H deducted goodwill from equity in accordance with its previous GAAP, the elimination of this intangible asset reduces retained earnings (paragraph C4(c)(ii) of the IFRS).
- (c) recognises the intangible asset that qualifies in accordance with IAS 38 for recognition as an asset in the financial statements of the subsidiary, even though the amount assigned to it in accordance with previous GAAP in entity H's consolidated financial statements was nil (paragraph C4(f) of the IFRS). The recognition criteria in IAS 38 include the availability of a reliable measurement of cost (paragraphs IG45–IG48) and entity H measures the asset at cost less accumulated depreciation and less any impairment losses identified in accordance with IAS 36 *Impairment of Assets*. Because entity H deducted goodwill from equity in accordance with its previous GAAP, the recognition of this intangible asset increases retained earnings (paragraph C4(c)(ii) of the IFRS). However, if this intangible asset had been subsumed in goodwill recognised as an asset in accordance with previous GAAP, entity H would have decreased the carrying amount of that goodwill accordingly (and, if applicable, adjusted deferred tax and non-controlling interests) (paragraph C4(g)(i) of the IFRS).

IG Example 6 Business combination—subsidiary not consolidated in accordance with previous GAAP**Background**

Parent J's date of transition to IFRSs is 1 January 20X4. In accordance with its previous GAAP, parent J did not consolidate its 75 per cent subsidiary K, acquired in a business combination on 15 July 20X1. On 1 January 20X4:

- (a) the cost of parent J's investment in subsidiary K is CU180.
- (b) in accordance with IFRSs, subsidiary K would measure its assets at CU500 and its liabilities (including deferred tax in accordance with IAS 12) at CU300. On this basis, subsidiary K's net assets are CU200 in accordance with IFRSs.

Application of requirements

Parent J consolidates subsidiary K. The consolidated statement of financial position at 1 January 20X4 includes:

- (a) subsidiary K's assets at CU500 and liabilities at CU300;
- (b) non-controlling interests of CU50 (25 per cent of [CU500 – CU300]); and
- (c) goodwill of CU30 (cost of CU180 less 75 per cent of [CU500 – CU300]) (paragraph C4(j) of the IFRS). Parent J tests the goodwill for impairment in accordance with IAS 36 *Impairment of Assets* and recognises any resulting impairment loss, based on conditions that existed at the date of transition to IFRSs (paragraph C4(g)(ii) of the IFRS).

IG Example 7 Business combination—lease in which the acquiree was a lessee not capitalised in accordance with previous GAAP**Background**

Parent L's date of transition to IFRSs is 1 January 20X4. Parent L acquired subsidiary M on 15 January 20X1 and did not capitalise leases in which subsidiary M was a lessee. If subsidiary M prepared financial statements in accordance with IFRSs, it would recognise lease liabilities of CU300 and right-of-use assets of CU250 at 1 January 20X4.

Application of requirements

Parent L has elected not to apply the transition reliefs in paragraphs D9 and D9B–D9E of this Standard. In its consolidated opening IFRS statement of financial position, parent L recognises lease liabilities of CU300 and right-of-use assets of CU250, and charges CU50 to retained earnings (paragraph C4(f)).

IAS 23 Borrowing Costs

IG23 On first adopting IFRSs, an entity begins capitalising borrowing costs (IAS 23 as revised in 2007). In accordance with paragraph D23 of the IFRS, an entity:

- (a) capitalises borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009 or the date of transition to IFRSs (whichever is later);
- (b) may elect to designate any date before 1 January 2009 or the date of transition to IFRSs (whichever is later) and to capitalise borrowing costs relating to all qualifying assets for which the commencement date for capitalisation is on or after that date.

However, if the entity established a deemed cost for an asset, the entity does not capitalise borrowing costs incurred before the date of the measurement that established the deemed cost.

IG24 IAS 23 requires disclosure of interest capitalised during the period. Neither IAS 23 nor the IFRS requires disclosure of the cumulative amount capitalised.

IG25 [Deleted]

IFRS 10 Consolidated Financial Statements

IG26 A first-time adopter consolidates all subsidiaries (as defined in IFRS 10), unless IFRS 107 requires otherwise.

IG27 If a first-time adopter did not consolidate a subsidiary in accordance with previous GAAP, then:

- (a) in its consolidated financial statements, the first-time adopter measures the subsidiary's assets and liabilities at the same carrying amounts as in the IFRS financial statements of the subsidiary, after adjusting for consolidation procedures and for the effects of the business combination in which it acquired the subsidiary (paragraph D17 of the IFRS). If the subsidiary has not adopted IFRSs in its financial statements, the carrying amounts described in the previous sentence are those that IFRSs would require in those financial statements (paragraph C4(j) of the IFRS).
- (b) if the parent acquired the subsidiary in a business combination before the date of transition to IFRS, the parent recognises goodwill, as explained in IG Example 6.
- (c) if the parent did not acquire the subsidiary in a business combination because it created the subsidiary, the parent does not recognise goodwill.

IG28 When a first-time adopter adjusts the carrying amounts of assets and liabilities of its subsidiaries in preparing its opening IFRS statement of financial position, this may affect non-controlling interests and deferred tax.

IG29 IG Examples 8 and 9 illustrate paragraphs D16 and D17 of the IFRS, which address cases where a parent and its subsidiary become first-time adopters at different dates.

IG Example 8 Parent adopts IFRSs before subsidiary

Background

Parent N presents its (consolidated) first IFRS financial statements in 20X5. Its foreign subsidiary O, wholly owned by parent N since formation, prepares information in accordance with IFRSs for internal consolidation purposes from that date, but subsidiary O does not present its first IFRS financial statements until 20X7.

Application of requirements

If subsidiary O applies paragraph D16(a) of the IFRS, the carrying amounts of its assets and liabilities are the same in both its opening IFRS statement of financial position at 1 January 20X6 and parent N's consolidated statement of financial position (except for adjustments for consolidation procedures) and are based on parent N's date of transition to IFRSs.

Alternatively, subsidiary O may, in accordance with paragraph D16(b) of the IFRS, measure all its assets or liabilities based on its own date of transition to IFRSs (1 January 20X6). However, the fact that subsidiary O becomes a first-time adopter in 20X7 does not change the carrying amounts of its assets and liabilities in parent N's consolidated financial statements.

IG Example 9 Subsidiary adopts IFRSs before parent

Background

Parent P presents its (consolidated) first IFRS financial statements in 20X7. Its foreign subsidiary Q, wholly owned by parent P since formation, presented its first IFRS financial statements in 20X5. Until 20X7, subsidiary Q prepared information for internal consolidation purposes in accordance with parent P's previous GAAP.

Application of requirements

The carrying amounts of subsidiary Q's assets and liabilities at 1 January 20X6 are the same in both parent P's (consolidated) opening IFRS statement of financial position and subsidiary Q's financial statements (except for adjustments for consolidation procedures) and are based on subsidiary Q's date of transition to IFRSs. The fact that parent P becomes a first-time adopter in 20X7 does not change those carrying amounts (paragraph D17 of the IFRS).

IG30 Paragraphs D16 and D17 of the IFRS do not override the following requirements:

- (a) to apply Appendix C of the IFRS to assets acquired, and liabilities assumed, in a business combination that occurred before the acquirer's date of transition to IFRSs. However, the acquirer applies paragraph D17 to new assets acquired, and liabilities assumed, by the acquiree after that business combination and still held at the acquirer's date of transition to IFRSs.
- (b) to apply the rest of the IFRS in measuring all assets and liabilities for which paragraphs D16 and D17 are not relevant.

- (c) to give all disclosures required by the IFRS as of the first-time adopter's own date of transition to IFRSs.
- IG31 Paragraph D16 of the IFRS applies if a subsidiary becomes a first-time adopter later than its parent, for example if the subsidiary previously prepared a reporting package in accordance with IFRSs for consolidation purposes but did not present a full set of financial statements in accordance with IFRSs. This may be relevant not only when a subsidiary's reporting package complies fully with the recognition and measurement requirements of IFRSs, but also when it is adjusted centrally for matters such as review of events after the reporting period and central allocation of pension costs. For the disclosure required by paragraph 26 of the IFRS, adjustments made centrally to an unpublished reporting package are not corrections of errors. However, paragraph D16 does not permit a subsidiary to ignore misstatements that are immaterial to the consolidated financial statements of its parent but material to its own financial statements.

IAS 29 Financial Reporting in Hyperinflationary Economies

- IG32 An entity complies with IAS 21 *The Effects of Changes in Foreign Exchange Rates* in determining its functional currency and presentation currency. When the entity prepares its opening IFRS statement of financial position, it applies IAS 29 to any periods during which the economy of the functional currency or presentation currency was hyperinflationary.
- IG33 An entity may elect to use the fair value of an item of property, plant and equipment at the date of transition to IFRSs as its deemed cost at that date (paragraph D5 of the IFRS), in which case it gives the disclosures required by paragraph 30 of the IFRS.
- IG34 If an entity elects to use the exemptions in paragraphs D5–D8 of the IFRS, it applies IAS 29 to periods after the date for which the revalued amount or fair value was determined.

IAS 32 Financial Instruments: Presentation

- IG35 In its opening IFRS statement of financial position, an entity applies the criteria in IAS 32 to classify financial instruments issued (or components of compound instruments issued) as either financial liabilities or equity instruments in accordance with the substance of the contractual arrangement when the instrument first satisfied the recognition criteria in IAS 32 (paragraphs 15 and 30), without considering events after that date (other than changes to the terms of the instruments).
- IG36 For compound instruments outstanding at the date of transition to IFRSs, an entity determines the initial carrying amounts of the components on the basis of circumstances existing when the instrument was issued (IAS 32 paragraph 30). An entity determines those carrying amounts using the version of IAS 32 effective at the end of its first IFRS reporting period. If the liability component is no longer outstanding at the date of transition to IFRSs, a first-time adopter need not separate the initial equity component of the instrument from the cumulative interest accreted on the liability component (paragraph D18 of the IFRS).

IAS 34 Interim Financial Reporting

- IG37 IAS 34 applies if an entity is required, or elects, to present an interim financial report in accordance with IFRSs. Accordingly, neither IAS 34 nor the IFRS requires an entity:
- (a) to present interim financial reports that comply with IAS 34; or
 - (b) to prepare new versions of interim financial reports presented in accordance with previous GAAP. However, if an entity does prepare an interim financial report in accordance with IAS 34 for part of the period covered by its first IFRS financial statements, the entity restates the comparative information presented in that report so that it complies with IFRSs.
- IG38 An entity applies the IFRS in each interim financial report that it presents in accordance with IAS 34 for part of the period covered by its first IFRS financial statements. In particular, paragraph 32 of the IFRS requires an entity to disclose various reconciliations (see IG Example 10).

IG Example 10 Interim financial reporting**Background**

Entity R's first IFRS financial statements are for a period that ends on 31 December 20X5, and its first interim financial report in accordance with IAS 34 is for the quarter ended 31 March 20X5. Entity R prepared previous GAAP annual financial statements for the year ended 31 December 20X4, and prepared quarterly reports throughout 20X4.

Application of requirements

In each quarterly interim financial report for 20X5, entity R includes reconciliations of:

- (a) its equity in accordance with previous GAAP at the end of the comparable quarter of 20X4 to its equity in accordance with IFRSs at that date; and
- (b) its total comprehensive income (or, if it did not report such a total, profit or loss) in accordance with previous GAAP for the comparable quarter of 20X4 (current and year to date) to its total comprehensive income in accordance with IFRSs.

In addition to the reconciliations required by (a) and (b) and the disclosures required by IAS 34, entity R's interim financial report for the first quarter of 20X5 includes reconciliations of (or a cross-reference to another published document that includes these reconciliations):

- (a) its equity in accordance with previous GAAP at 1 January 20X4 and 31 December 20X4 to its equity in accordance with IFRSs at those dates; and
- (b) its total comprehensive income (or, if it did not report such a total, profit or loss) for 20X4 in accordance with previous GAAP to its total comprehensive income for 20X4 in accordance with IFRSs.

Each of the above reconciliations gives sufficient detail to enable users to understand the material adjustments to the statement of financial position and statement of comprehensive income. Entity R also explains the material adjustments to the statement of cash flows.

If entity R becomes aware of errors made in accordance with previous GAAP, the reconciliations distinguish the correction of those errors from changes in accounting policies.

If entity R did not, in its most recent annual financial statements in accordance with previous GAAP, disclose information material to an understanding of the current interim period, its interim financial reports for 20X5 disclose that information or include a cross-reference to another published document that includes it (paragraph 33 of the IFRS).

IAS 36 *Impairment of Assets* and IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*

IG39 An entity applies IAS 36 in:

- (a) determining whether any impairment loss exists at the date of transition to IFRSs; and
- (b) measuring any impairment loss that exists at that date, and reversing any impairment loss that no longer exists at that date. An entity's first IFRS financial statements include the disclosures that IAS 36 would have required if the entity had recognised those impairment losses or reversals in the period beginning with the date of transition to IFRSs (paragraph 24(c) of the IFRS).

IG40 The estimates used to determine whether an entity recognises an impairment loss or provision (and to measure any such impairment loss or provision) at the date of transition to IFRSs are consistent with estimates made for the same date in accordance with previous GAAP (after adjustments to reflect any difference in accounting policies), unless there is objective evidence that those estimates were in error (paragraphs 14 and 15 of the IFRS). The entity reports the impact of any later revisions to those estimates as an event of the period in which it makes the revisions.

IG41 In assessing whether it needs to recognise an impairment loss or provision (and in measuring any such impairment loss or provision) at the date of transition to IFRSs, an entity may need to make estimates for that date that were not necessary in accordance with its previous GAAP. Such estimates and assumptions do not reflect conditions that arose after the date of transition to IFRSs (paragraph 16 of the IFRS).

IG42 The transitional provisions in IAS 36 and IAS 37 do not apply to an entity's opening IFRS statement of financial position (paragraph 9 of the IFRS).

IG43 IAS 36 requires the reversal of impairment losses in some cases. If an entity's opening IFRS statement of financial position reflects impairment losses, the entity recognises any later reversal of those impairment losses

in profit or loss (except when IAS 36 requires the entity to treat that reversal as a revaluation). This applies to both impairment losses recognised in accordance with previous GAAP and additional impairment losses recognised on transition to IFRSs.

IAS 38 Intangible Assets

- IG44 An entity's opening IFRS statement of financial position:
- (a) excludes all intangible assets and other intangible items that do not meet the criteria for recognition in accordance with IAS 38 at the date of transition to IFRSs; and
 - (b) includes all intangible assets that meet the recognition criteria in IAS 38 at that date, except for intangible assets acquired in a business combination that were not recognised in the acquirer's consolidated statement of financial position in accordance with previous GAAP and also would not qualify for recognition in accordance with IAS 38 in the separate statement of financial position of the acquiree (see paragraph C4(f) of the IFRS).
- IG45 The criteria in IAS 38 require an entity to recognise an intangible asset if, and only if:
- (a) it is probable that the future economic benefits that are attributable to the asset will flow to the entity; and
 - (b) the cost of the asset can be measured reliably.
- IAS 38 supplements these two criteria with further, more specific, criteria for internally generated intangible assets.
- IG46 In accordance with paragraphs 65 and 71 of IAS 38, an entity capitalises the costs of creating internally generated intangible assets prospectively from the date when the recognition criteria are met. IAS 38 does not permit an entity to use hindsight to conclude retrospectively that these recognition criteria are met. Therefore, even if an entity concludes retrospectively that a future inflow of economic benefits from an internally generated intangible asset is probable and the entity is able to reconstruct the costs reliably, IAS 38 prohibits it from capitalising the costs incurred before the date when the entity both:
- (a) concludes, based on an assessment made and documented at the date of that conclusion, that it is probable that future economic benefits from the asset will flow to the entity; and
 - (b) has a reliable system for accumulating the costs of internally generated intangible assets when, or shortly after, they are incurred.
- IG47 If an internally generated intangible asset qualifies for recognition at the date of transition to IFRSs, an entity recognises the asset in its opening IFRS statement of financial position even if it had recognised the related expenditure as an expense in accordance with previous GAAP. If the asset does not qualify for recognition in accordance with IAS 38 until a later date, its cost is the sum of the expenditure incurred from that later date.
- IG48 The criteria discussed in paragraph IG45 also apply to an intangible asset acquired separately. In many cases, contemporaneous documentation prepared to support the decision to acquire the asset will contain an assessment of the future economic benefits. Furthermore, as explained in paragraph 26 of IAS 38, the cost of a separately acquired intangible asset can usually be measured reliably.
- IG49 For an intangible asset acquired in a business combination before the date of transition to IFRSs, its carrying amount in accordance with previous GAAP immediately after the business combination is its deemed cost in accordance with IFRSs at that date (paragraph C4(e) of the IFRS). If that carrying amount was zero, the acquirer does not recognise the intangible asset in its consolidated opening IFRS statement of financial position, unless it would qualify in accordance with IAS 38, applying the criteria discussed in paragraphs IG45–IG48, for recognition at the date of transition to IFRSs in the statement of financial position of the acquiree (paragraph C4(f) of the IFRS). If those recognition criteria are met, the acquirer measures the asset on the basis that IAS 38 would require in the statement of financial position of the acquiree. The resulting adjustment affects goodwill (paragraph C4(g)(i) of the IFRS).
- IG50 A first-time adopter may elect to use the fair value of an intangible asset at the date of an event such as a privatisation or initial public offering as its deemed cost at the date of that event (paragraph D8 of the IFRS), provided that the intangible asset qualifies for recognition in accordance with IAS 38 (paragraph 10 of the IFRS). In addition, if, and only if, an intangible asset meets both the recognition criteria in IAS 38 (including reliable measurement of original cost) and the criteria in IAS 38 for revaluation (including the existence of an active market), a first-time adopter may elect to use one of the following amounts as its deemed cost (paragraph D7 of the IFRS):
- (a) fair value at the date of transition to IFRSs (paragraph D5 of the IFRS), in which case the entity gives the disclosures required by paragraph 30 of the IFRS; or

(b) a revaluation in accordance with previous GAAP that meets the criteria in paragraph D6 of the IFRS.

IG51 If an entity's amortisation methods and rates in accordance with previous GAAP would be acceptable in accordance with IFRSs, the entity does not restate the accumulated amortisation in its opening IFRS statement of financial position. Instead, the entity accounts for any change in estimated useful life or amortisation pattern prospectively from the period when it makes that change in estimate (paragraph 14 of the IFRS and paragraph 104 of IAS 38). However, in some cases, an entity's amortisation methods and rates in accordance with previous GAAP may differ from those that would be acceptable in accordance with IFRSs (for example, if they were adopted solely for tax purposes and do not reflect a reasonable estimate of the asset's useful life). If those differences have a material effect on the financial statements, the entity adjusts the accumulated amortisation in its opening IFRS statement of financial position retrospectively so that it complies with IFRSs (paragraph 14 of the IFRS). However, if an entity uses the exemption in paragraph D8B, it uses the carrying amount of the intangible asset at the date of transition to IFRSs as deemed cost as if it had acquired an intangible asset with the same remaining service potential for that amount at the date of transition to IFRSs. Subsequent amortisation is based on that deemed cost and starts from the date of transition to IFRSs.

IFRS 9 *Financial Instruments*

IG52 An entity recognises and measures all financial assets and financial liabilities in its opening IFRS statement of financial position in accordance with IFRS 9, except as specified in paragraphs B2–B6 of the IFRS, which address derecognition and hedge accounting.

Recognition

IG53 An entity recognises all financial assets and financial liabilities (including all derivatives) that qualify for recognition in accordance with IFRS 9 and have not yet qualified for derecognition in accordance with IFRS 9, except non-derivative financial assets and non-derivative financial liabilities derecognised in accordance with previous GAAP before the date of transition to IFRSs, to which the entity does not choose to apply paragraph B3 (see paragraphs B2 and B3 of the IFRS). For example, an entity that does not apply paragraph B3 does not recognise assets transferred in a securitisation, transfer or other derecognition transaction that occurred before the date of transition to IFRSs if those transactions qualified for derecognition in accordance with previous GAAP. However, if the entity uses the same securitisation arrangement or other derecognition arrangement for further transfers after the date of transition to IFRSs, those further transfers qualify for derecognition only if they meet the derecognition criteria of IFRS 9.

IG54 An entity does not recognise financial assets and financial liabilities that do not qualify for recognition in accordance with IFRS 9, or have already qualified for derecognition in accordance with IFRS 9.

Embedded derivatives

IG55 When IFRS 9 requires an entity to separate an embedded derivative from a host contract, the initial carrying amounts of the components at the date when the instrument first satisfies the recognition criteria in IFRS 9 reflect circumstances at that date (IFRS 9 paragraph 4.3.3). If the entity cannot determine the initial carrying amounts of the embedded derivative and host contract reliably, it measures the entire combined contract as at fair value through profit or loss (IFRS 9 paragraph 4.3.6).

Measurement

IG56 In preparing its opening IFRS statement of financial position, an entity applies the criteria in IFRS 9 to classify financial instruments on the basis of the facts and circumstances that exist at the date of transition to IFRSs. The resulting classifications are applied retrospectively.

IG57 For those financial assets and financial liabilities measured at amortised cost in the opening IFRS statement of financial position, an entity determines the gross carrying amount of the financial assets and the amortised cost of the financial liabilities on the basis of circumstances existing when the assets and liabilities first satisfied the recognition criteria in IFRS 9. However, if the entity acquired those financial assets and financial liabilities in a past business combination, their carrying amount in accordance with previous GAAP immediately following the business combination is their deemed cost in accordance with IFRSs at that date (paragraph C4(e) of the IFRS).

IG58 [Deleted]

Transition adjustments

- IG58A An entity shall treat an adjustment to the carrying amount of a financial asset or financial liability as a transition adjustment to be recognised in the opening balance of retained earnings (or another component of equity, as appropriate) at the date of transition to IFRSs only to the extent that it results from adopting IFRS 9. Because all derivatives, other than those that are financial guarantee contracts, a commitment to provide a loan at a below-market interest rate, a loan commitment that is subject to the impairment requirements of IFRS 9 or are designated and effective hedging instruments, are measured at fair value through profit or loss, the differences between the previous carrying amount (which may have been zero) and the fair value of the derivatives are recognised as an adjustment of the balance of retained earnings at the beginning of the financial year in which IFRS 9 is initially applied (other than for a derivative that is a financial guarantee contract, a commitment to provide a loan at a below-market interest rate or a designated and effective hedging instrument).
- IG58B IAS 8 (as revised in 2003) applies to adjustments resulting from changes in estimates. If an entity is unable to determine whether a particular portion of the adjustment is a transition adjustment or a change in estimate, it treats that portion as a change in accounting estimate in accordance with IAS 8, with appropriate disclosures (IAS 8 paragraphs 32–40).
- IG59 An entity may, in accordance with its previous GAAP, have measured investments at fair value and recognised the revaluation gain outside profit or loss. If an investment is classified as at fair value through profit or loss, the pre-IFRS 9 revaluation gain that had been recognised outside profit or loss is reclassified into retained earnings on initial application of IFRS 9. If, on initial application of IFRS 9, an investment is measured at fair value through other comprehensive income in accordance with paragraph 4.1.2A of IFRS 9 or is designated at fair value through other comprehensive income in accordance with paragraph 5.7.5 of IFRS 9, then the pre-IFRS 9 revaluation gain is recognised in a separate component of equity. Subsequently, the entity recognises gains and losses on the financial asset in other comprehensive income (except dividends, which are recognised in profit or loss) and accumulates the cumulative gains and losses in that separate component of equity. Subsequently, the entity recognises gains and losses on these financial assets in accordance with IFRS 9.

Hedge accounting

- IG60 Paragraphs B4–B6 of the IFRS deal with hedge accounting. The designation and documentation of a hedge relationship must be completed on or before the date of transition to IFRSs if the hedge relationship is to qualify for hedge accounting from that date. Hedge accounting can be applied prospectively only from the date that the hedge relationship is fully designated and documented.
- IG60A An entity may, in accordance with its previous GAAP, have deferred or not recognised gains and losses on a fair value hedge of a hedged item that is not measured at fair value. For such a fair value hedge, an entity adjusts the carrying amount of the hedged item at the date of transition to IFRSs. The adjustment is the lower of:
- that portion of the cumulative change in the fair value of the hedged item that was not recognised in accordance with previous GAAP; and
 - that portion of the cumulative change in the fair value of the hedging instrument and, in accordance with previous GAAP, was either (i) not recognised or (ii) deferred in the statement of financial position as an asset or liability.
- IG60B An entity may, in accordance with its previous GAAP, have deferred gains and losses on a cash flow hedge of a forecast transaction. If, at the date of transition to IFRSs, the hedged forecast transaction is not highly probable, but is expected to occur, the entire deferred gain or loss is recognised in the cash flow hedge reserve within equity. Any net cumulative gain or loss that has been reclassified to the cash flow hedge reserve on initial application of IFRS 9 remains there until (a) the forecast transaction subsequently results in the recognition of a non-financial asset or non-financial liability, (b) the forecast transaction affects profit or loss or (c) subsequently circumstances change and the forecast transaction is no longer expected to occur, in which case any related net cumulative gain or loss is reclassified from the cash flow hedge reserve to profit or loss. If the hedging instrument is still held, but the hedge does not qualify as a cash flow hedge in accordance with IFRS 9, hedge accounting is no longer appropriate starting from the date of transition to IFRSs.

IAS 40 Investment Property

- IG61 An entity that adopts the fair value model in IAS 40 measures its investment property at fair value at the date of transition to IFRSs. The transitional requirements of IAS 40 do not apply (paragraph 9 of the IFRS).
- IG62 An entity that adopts the cost model in IAS 40 applies paragraphs IG7–IG13 on property, plant and equipment.

Explanation of transition to IFRSs

IG63 Paragraphs 24(a) and (b), 25 and 26 of the IFRS require a first-time adopter to disclose reconciliations that give sufficient detail to enable users to understand the material adjustments to the statement of financial position, statement of comprehensive income and, if applicable, statement of cash flows. Paragraph 24(a) and (b) requires specific reconciliations of equity and total comprehensive income. IG Example 11 shows one way of satisfying these requirements.

IG Example 11 Reconciliation of equity and total comprehensive income				
Background				
An entity first adopted IFRSs in 20X5, with a date of transition to IFRSs of 1 January 20X4. Its last financial statements in accordance with previous GAAP were for the year ended 31 December 20X4.				
Application of requirements				
The entity's first IFRS financial statements include the reconciliations and related notes shown below.				
Among other things, this example includes a reconciliation of equity at the date of transition to IFRSs (1 January 20X4). The IFRS also requires a reconciliation at the end of the last period presented in accordance with previous GAAP (not included in this example).				
In practice, it may be helpful to include cross-references to accounting policies and supporting analyses that give further explanation of the adjustments shown in the reconciliations below.				
If a first-time adopter becomes aware of errors made in accordance with previous GAAP, the reconciliations distinguish the correction of those errors from changes in accounting policies (paragraph 26 of the IFRS). This example does not illustrate disclosure of a correction of an error.				
Reconciliation of equity at 1 January 20X4 (date of transition to IFRSs)				
Note		<i>Previous GAAP</i>	<i>Effect of transition to IFRSs</i>	<i>IFRSs</i>
		<i>CU</i>	<i>CU</i>	<i>CU</i>
1	Property, plant and equipment	8,299	100	8,399
2	Goodwill	1,220	150	1,370
2	Intangible assets	208	(150)	58
3	Financial assets	3,471	420	3,891
	Total non-current assets	13,198	520	13,718
	Trade and other receivables	3,710	0	3,710
4	Inventories	2,962	400	3,362
5	Other receivables	333	431	764
	Cash and cash equivalents	748	0	748
	Total current assets	7,753	831	8,584
	Total assets	20,951	1,351	22,302
				<i>continued...</i>

...continued

IG Example 11 Reconciliation of equity and total comprehensive income**Reconciliation of equity at 1 January 20X4 (date of transition to IFRSs)**

Note	Previous GAAP	Effect of transition to IFRSs	IFRSs	
	CU	CU	CU	
	Interest-bearing loans	9,396	0	9,396
	Trade and other payables	4,124	0	4,124
6	Employee benefits	0	66	66
7	Restructuring provision	250	(250)	0
	Current tax liability	42	0	42
8	Deferred tax liability	579	460	1,039
	Total liabilities	14,391	276	14,667
	Total assets less total liabilities	6,560	1,075	7,635
	Issued capital	1,500	0	1,500
5	Cash flow hedge reserve	0	302	302
9	Retained earnings	5,060	773	5,833
	Total equity	6,560	1,075	7,635

Notes to the reconciliation of equity at 1 January 20X4:

- 1 Depreciation was influenced by tax requirements in accordance with previous GAAP, but in accordance with IFRSs reflects the useful life of the assets. The cumulative adjustment increased the carrying amount of property, plant and equipment by 100.
- 2 Intangible assets in accordance with previous GAAP included CU150 for items that are transferred to goodwill because they do not qualify for recognition as intangible assets in accordance with IFRSs.
- 3 Financial assets are all classified as at fair value through profit or loss in accordance with IFRSs and are carried at their fair value of CU3,891. They were carried at cost of CU3,471 in accordance with previous GAAP. The resulting gains of CU294 (CU420, less related deferred tax of CU126) are included in retained earnings.
- 4 Inventories include fixed and variable production overhead of CU400 in accordance with IFRSs, but this overhead was excluded in accordance with previous GAAP.
- 5 Unrealised gains of CU431 on unmatured forward foreign exchange contracts are recognised in accordance with IFRSs, but were not recognised in accordance with previous GAAP. The resulting gains of CU302 (CU431, less related deferred tax of CU129) are included in the cash flow hedge reserve because the contracts hedge forecast sales.
- 6 A pension liability of CU66 is recognised in accordance with IFRSs, but was not recognised in accordance with previous GAAP, which used a cash basis.

continued...

*...continued***IG Example 11 Reconciliation of equity and total comprehensive income**

7 A restructuring provision of CU250 relating to head office activities was recognised in accordance with previous GAAP, but does not qualify for recognition as a liability in accordance with IFRSs.

8 The above changes increased the deferred tax liability as follows:

	CU
Cash flow hedge reserve (note 5)	129
Retained earnings	331
Increase in deferred tax liability	<u>460</u>

Because the tax base at 1 January 20X4 of the items reclassified from intangible assets to goodwill (note 2) equalled their carrying amount at that date, the reclassification did not affect deferred tax liabilities.

9 The adjustments to retained earnings are as follows:

	CU
Depreciation (note 1)	100
Financial assets (note 3)	420
Production overhead (note 4)	400
Pension liability (note 6)	(66)
Restructuring provision (note 7)	250
Tax effect of the above	(331)
Total adjustment to retained earnings	<u>773</u>

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IG Example 11 Reconciliation of equity and total comprehensive income

Reconciliation of total comprehensive income for 20X4

Note	Previous GAAP CU	Effect of transition to IFRSs CU	IFRSs CU
Revenue	20,910	0	20,910
1,2,3 Cost of sales	(15,283)	(97)	(15,380)
Gross profit	5,627	(97)	5,530
6 Other income	0	180	180
1 Distribution costs	(1,907)	(30)	(1,937)
1,4 Administrative expenses	(2,842)	(300)	(3,142)
Finance income	1,446	0	1,446
Finance costs	(1,902)	0	(1,902)
Profit before tax	422	(247)	175
5 Tax expense	(158)	74	(84)
Profit (loss) for the year	264	(173)	91
7 Cash flow hedges	0	(40)	(40)
8 Tax relating to other comprehensive income	0	(29)	(29)
Other comprehensive income	0	(69)	(69)
Total comprehensive income	264	(242)	22

Notes to the reconciliation of total comprehensive income for 20X4:

- 1 A pension liability is recognised in accordance with IFRSs, but was not recognised in accordance with previous GAAP. The pension liability increased by CU130 during 20X4, which caused increases in cost of sales (CU50), distribution costs (CU30) and administrative expenses (CU50).
- 2 Cost of sales is higher by CU47 in accordance with IFRSs because inventories include fixed and variable production overhead in accordance with IFRSs but not in accordance with previous GAAP.
- 3 Depreciation was influenced by tax requirements in accordance with previous GAAP, but reflects the useful life of the assets in accordance with IFRSs. The effect on the profit for 20X4 was not material.
- 4 A restructuring provision of CU250 was recognised in accordance with previous GAAP at 1 January 20X4, but did not qualify for recognition in accordance with IFRSs until the year ended 31 December 20X4. This increases administrative expenses for 20X4 in accordance with IFRSs.
- 5 Adjustments 1–4 above lead to a reduction of CU128 in deferred tax expense.
- 6 Financial assets at fair value through profit or loss increased in value by CU180 during 20X4. They were carried at cost in accordance with previous GAAP. Fair value changes have been included in ‘Other income’.

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IG Example 11 Reconciliation of equity and total comprehensive income

7 The fair value of forward foreign exchange contracts that are effective hedges of forecast transactions decreased by CU40 during 20X4.

8 Adjustments 6 and 7 above lead to an increase of CU29 in deferred tax expense.

Explanation of material adjustments to the statement of cash flows for 20X4:

Income taxes of CU133 paid during 20X4 are classified as operating cash flows in accordance with IFRSs, but were included in a separate category of tax cash flows in accordance with previous GAAP. There are no other material differences between the statement of cash flows presented in accordance with IFRSs and the statement of cash flows presented in accordance with previous GAAP.

IFRS 2 Share-based Payment

IG64 A first-time adopter is encouraged, but not required, to apply IFRS 2 *Share-based Payment* to equity instruments that were granted after 7 November 2002 that vested before the later of (a) the date of transition to IFRSs and (b) 1 January 2005.

IG65 For example, if an entity's date of transition to IFRSs is 1 January 2004, the entity applies IFRS 2 to shares, share options or other equity instruments that were granted after 7 November 2002 and had not yet vested at 1 January 2005. Conversely, if an entity's date of transition to IFRSs is 1 January 2010, the entity applies IFRS 2 to shares, share options or other equity instruments that were granted after 7 November 2002 and had not yet vested at 1 January 2010.

IAS 20 Accounting for Government Grants and Disclosure of Government Assistance

IG66 Paragraph B10 of the IFRS requires a first-time adopter to use its previous GAAP carrying amount of government loans existing at the date of transition to IFRS as the IFRS carrying amount of such loans at that date. A first-time adopter applies IAS 32 *Financial Instruments: Presentation* to classify such a loan as a financial liability or an equity instrument. Subsequently, the first-time adopter applies IFRS 9 to such a loan. To do so, the entity calculates the effective interest rate by comparing the carrying amount of the loan at the date of transition to IFRSs with the amount and timing of expected repayments to the government. IG Example 12 illustrates accounting for such a loan.

IG Example 12 Government loan at a below-market rate of interest at the date of transition to IFRSs

To encourage entities to expand their operations in a specified development zone where it is difficult for entities to obtain financing for their projects, the government provides loans at a below-market rate of interest to fund the purchase of manufacturing equipment.

Entity S's date of transition to IFRSs is 1 January 20X2.

In accordance with the development scheme, in 20X0 Entity S receives a loan at a below-market rate of interest from the government for CU100,000. Under previous GAAP, Entity S accounted for the loan as equity and the carrying amount under previous GAAP was CU100,000 at the date of transition to IFRSs. The amount repayable will be CU103,030 at 1 January 20X5.

No other payment is required under the terms of the loan and there are no future performance conditions attached to the loan. The information needed to measure the fair value of the loan was not obtained at the time of initially accounting for the loan.

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IG Example 12 Government loan at a below-market rate of interest at the date of transition to IFRSs

The loan meets the definition of a financial liability in accordance with IAS 32. Entity S therefore reclassifies the government loan as a liability. It also uses the previous GAAP carrying amount of the loan at the date of transition to IFRSs as the carrying amount of the loan in the opening IFRS statement of financial position. Entity S therefore reclassifies the amount of CU100,000 from equity to liability in the opening IFRS statement of financial position. In order to measure the loan after the date of transition to IFRSs, the effective interest rate starting 1 January 20X2 is calculated as below:

$$= \sqrt[3]{\left(\frac{103,000}{100,000}\right)} - 1$$

$$= 0.01$$

The carrying amounts of the loan are as follows:

Date	Carrying amount	Interest expense	Interest payable
	CU	CU	CU
1 January 20X2	100,000		
31 December 20X2	101,000	1,000	1,000
31 December 20X3	102,010	1,010	2,010
31 December 20X4	103,030	1,020	3,030

[Paragraphs IG67–IG200 reserved for possible guidance on future standards]

IFRIC Interpretations

IFRIC 1 Changes in Existing Decommissioning, Restoration and Similar Liabilities

- IG201 IAS 16 requires the cost of an item of property, plant and equipment to include the initial estimate of the costs of dismantling and removing the asset and restoring the site on which it is located. IAS 37 requires the liability, both initially and subsequently, to be measured at the amount required to settle the present obligation at the end of the reporting period, reflecting a current market-based discount rate.
- IG202 IFRIC 1 requires that, subject to specified conditions, changes in an existing decommissioning, restoration or similar liability are added to or deducted from the cost of the related asset. The resulting depreciable amount of the asset is depreciated over its useful life, and the periodic unwinding of the discount on the liability is recognised in profit or loss as it occurs.
- IG203 Paragraph D21 of IFRS 1 provides a transitional exemption. Instead of retrospectively accounting for changes in this way, entities can include in the depreciated cost of the asset an amount calculated by discounting the liability at the date of transition to IFRSs back to, and depreciating it from, when the liability was first incurred. IG Example 201 illustrates the effect of applying this exemption, assuming that the entity accounts for its property, plant and equipment using the cost model.

IG Example 201 Changes in existing decommissioning, restoration and similar liabilities	
Background	
An entity’s first IFRS financial statements are for a period that ends on 31 December 20X5 and include comparative information for 20X4 only. Its date of transition to IFRSs is therefore 1 January 20X4.	
The entity acquired an energy plant on 1 January 20X1, with a life of 40 years.	
As at the date of transition to IFRSs, the entity estimates the decommissioning cost in 37 years’ time to be 470, and estimates that the appropriate risk-adjusted discount rate for the liability is 5 per cent. It judges that the appropriate discount rate has not changed since 1 January 20X1.	
Application of requirements	
The decommissioning liability recognised at the transition date is CU77 (CU470 discounted for 37 years at 5 per cent).	
Discounting this liability back for a further three years to 1 January 20X1 gives an estimated liability at acquisition, to be included in the cost of the asset, of CU67. Accumulated depreciation on the asset is $CU67 \times 3/40 = CU5$.	
The amounts recognised in the opening IFRS statement of financial position on the date of transition to IFRSs (1 January 20X4) are, in summary:	
	CU
Decommissioning cost included in cost of plant	67
Accumulated depreciation	(5)
Decommissioning liability	(77)
Net assets/retained earnings	<u>(15)</u>

IG204–IG206 [Deleted]

Table of Concordance

This table shows how the contents of the superseded version of IFRS 1 and the revised version of IFRS 1 correspond.

Superseded IFRS 1 paragraph	Revised IFRS 1 paragraph	Superseded IFRS 1 paragraph	Revised IFRS 1 paragraph	Superseded IFRS 1 paragraph	Revised IFRS 1 paragraph
1	1	25A	D19	38	23
2	2	25B	D2	39	24
3	3	25C	D3	40	25
4	4	25D	D4	41	26
5	5	25E	D21	42	27
6	6	25F	D9	43	28
7	7	25G	D20	43A	29
8	8	25H	D22	44	30
9	9	25I	D23	44A	31
10	10	26	B1	45	32
11	11	27	B2	46	33
12	12	27A	B3	47	34
13	D1	28	B4	47A	None
14	19	29	B5	47B	None
15	None	30	B6	47C	None
16	D5	31	14	47D	None
17	D6	32	15	47E	None
18	D7	33	16	47F	None
19	D8	34	17	47G	35
20	D10	34A	None	47H	None
20A	D11	34B	None	47I	36
21	D12	34C	B7	47J	37
22	D13	35	20	47K	38
23	D18	36	21	47L	39
23A	D14	36A	None	None	40
23B	D15	36B	None	Appendix A	Appendix A
24	D16	36C	None	Appendix B	Appendix C
25	D17	37	22	None	13, 18