

Government Loans
(Amendments to NZ IFRS 1)

GOVERNMENT LOANS
(AMENDMENTS TO NZ IFRS 1) (APRIL 2012)

Government Loans (Amendments to IFRS 1) is issued by the International Accounting Standards Board (IASB), 30 Cannon Street, London EC4M 6XH, United Kingdom.

Tel: +44 (0)20 7246 6410

Fax: +44 (0)20 7246 6411

Email: iasb@ifrs.org

Web: www.ifrs.org

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1st Floor, 30 Cannon Street, London EC4M 6XH, United Kingdom.

Tel: +44 (0)20 7332 2730 Fax: +44 (0)20 7332 2749

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INTRODUCTION

AMENDMENTS TO NZ IFRS 1 *FIRST-TIME ADOPTION OF NEW ZEALAND EQUIVALENTS TO INTERNATIONAL FINANCIAL REPORTING STANDARDS*

Introduction

This document sets out amendments to NZ IFRS 1 *First-time Adoption of New Zealand Equivalents to International Financial Reporting Standards*.

These amendments result from proposals in the IASB Exposure Draft *Government Loans* (proposed amendments to IFRS 1) that was published in October 2011.

The amendments add an exception to the retrospective application of NZ IFRSs to require that first-time adopters apply the requirements in NZ IFRS 9 *Financial Instruments* and NZ IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* prospectively to government loans existing at the date of transition to NZ IFRSs. This means that first-time adopters shall not recognise the corresponding benefit of the government loan at a below-market rate of interest as a government grant. However, entities may choose to apply the requirements of NZ IFRS 9 and nz IAS 20 to government loans retrospectively if the information needed to do so had been obtained at the time of initially accounting for that loan. These amendments give first-time adopters the same relief as existing preparers of NZ IFRS financial statements.

Entities are required to apply these amendments for annual periods beginning on or after 1 January 2013. Earlier application is permitted.

Amendments to NZ IFRS 1 *First-time Adoption of New Zealand Equivalents to International Financial Reporting Standards*

Paragraphs 39N and 39O are added and B1 is amended (new text is underlined and deleted text is struck through).

- 39N *Government Loans* (Amendments to NZ IFRS 1), issued in April 2012, added paragraphs B1(f) and B10-B12. An entity shall apply those paragraphs for annual periods beginning on or after 1 January 2013. Earlier application is permitted.
- 39O Paragraphs B10 and B11 refer to NZ IFRS 9. If an entity applies this NZ IFRS but does not yet apply NZ IFRS 9, the references in paragraphs B10 and B11 to IFRS 9 shall be read as references to NZ IAS 39 *Financial Instruments: Recognition and Measurement*.
- B1 An entity shall apply the following exceptions:
- (a) derecognition of financial assets and financial liabilities (paragraphs B2 and B3);
 - (b) hedge accounting (paragraphs B4–B6);
 - (c) non-controlling interests (paragraph B7);
 - (d) classification and measurement of financial assets (paragraph B8); ~~and~~
 - (e) embedded derivatives (paragraph B9); and
 - (f) government loans (paragraphs B10–B12).

After paragraph B9 a heading and paragraphs B10–B12 are added.

Government loans

- B10 A first-time adopter shall classify all government loans received as a financial liability or an equity instrument in accordance with NZ IAS 32 *Financial Instruments: Presentation*. Except as permitted by paragraph B11, a first-time adopter shall apply the requirements in NZ IFRS 9 *Financial Instruments* and NZ IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* prospectively to government loans existing at the date of transition to NZ IFRSs and shall not recognise the corresponding benefit of the government loan at a below-market rate of interest as a government grant. Consequently, if a first-time adopter did not, under its previous GAAP, recognise and measure a government loan at a below-market rate of interest on a basis consistent with NZ IFRS requirements, it shall use its previous GAAP carrying amount of the loan at the date of transition to NZ IFRSs as the carrying amount of the loan in the opening IFRS statement of financial position. An entity shall apply NZ IFRS 9 to the measurement of such loans after the date of transition to NZ IFRSs.
- B11 Despite paragraph B10, an entity may apply the requirements in NZ IFRS 9 and NZ IAS 20 retrospectively to any government loan originated before the date of transition to NZ IFRSs, provided that the information needed to do so had been obtained at the time of initially accounting for that loan.
- B12 The requirements and guidance in paragraphs B10 and B11 do not preclude an entity from being able to use the exemptions described in paragraphs D19–D19D relating to the designation of previously recognised financial instruments at fair value through profit or loss.

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.

Hans Hoogervorst	Chairman
Ian Mackintosh	Vice-Chairman
Stephen Cooper	
Philippe Danjou	
Jan Engström	
Patrick Finnegan	
Amaro Luiz de Oliveira Gomes	
Prabhakar Kalavacherla	
Patricia McConnell	
Takatsugu Ochi	
Paul Pacter	
Darrel Scott	
John T Smith	
Zhang Wei-Guo	

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

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

Paragraph BC74 is amended (new text is underlined and deleted text is struck through).

Retrospective designation

BC74 The Board considered practical implementation difficulties that could arise from the retrospective application of aspects of IAS 39:

- (a) hedge accounting (paragraphs BC75–BC80);
- (b) government loans (paragraphs BC80A–BC80E);
- ~~(b)~~(c) the treatment of cumulative fair value changes on available-for-sale financial assets at the date of transition to IFRSs (paragraphs BC81–BC83); and
- ~~(c)~~(d) ‘day 1’ gain or loss recognition (paragraph BC83A).

After paragraph BC80, a heading and paragraphs BC80A–BC80E are added

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 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.

GOVERNMENT LOANS
(AMENDMENTS TO NZ IFRS 1) (APRIL 2012)

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.

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

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

A heading, paragraphs IG66 and IG Example 12 are added. The editorial note after IG65 has been amended and moved accordingly.

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.

[Paragraphs IG667–IG200 reserved for possible guidance on future standards]

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.

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