IFRS 1 – First Time Adoption of International Financial Reporting Standards

Chinnsamy Ganesan B.Com FCA DISA(ICA)

Structure of the discussion

IFRS 1

- **Recap of conceptual differences**
- **First time adoption – issues in change over**
- **Requirements of IFRS**
- **Optional exemptions**
- **Mandatory Exceptions**
- **Getting ready for IFRS**

Issues in changeover

Recap

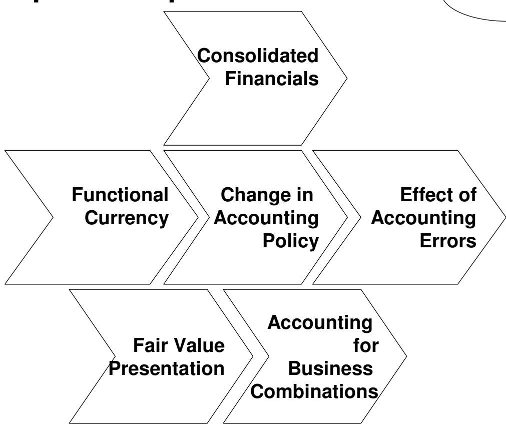
- **Magnitude of change anticipated**
  - **ICAI convergence paper**
    - **Only 5 Standards in line with IFRS**
    - **8 Standards require minor changes**
    - **10 Standards conceptually differs**
    - **8 Standards require regulatory changes**
- **Emphasis on Consolidated statements and not stand alone**

IFRS – ICAI Convergence Paper

No change	*Minor changes*	*Conceptual Difference*	*Regulatory changes*
AS 7	*AS 2*	*AS 13*	*AS 1*
AS 16	*AS 3*	*AS 15*	*AS 4*
AS 30	*AS 9*	*AS 17*	*AS 5*
AS 31	*AS 12*	*AS 18*	*AS 6*
AS 32	*AS 20*	*AS 19*	*AS 10*
	AS 24	*AS 21*	*AS 11*
	AS 26	*AS 22*	*AS 14*
	AS 28	*AS 23*	*AS 25*
		AS 27	
		AS 29	

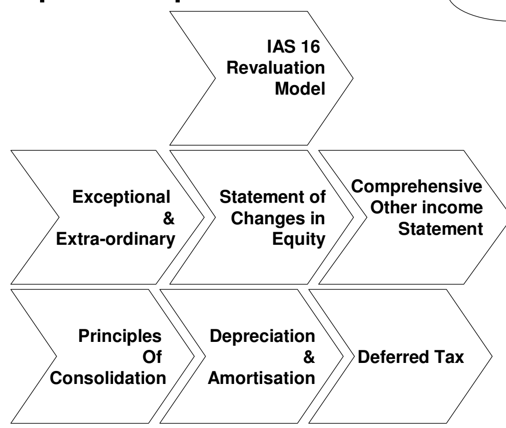
Recap - Conceptual Differences

IFRS



Recap - Conceptual Differences

IFRS



Issues in changeover

IFRS 1

- High level effects on performance and financial ratios
  - Board's awareness of strategic implications – volatility of reported performance measures
  - Impact on specific covenants or ratios that are important for the business
  - Implication on remuneration package, bonus and profit sharing arrangements
  - Impact on distributable reserves, EPS, tax liability etc.

Issues in changeover

IFRS 1

- Accounting and technical issues
  - Major accounting policy changes
  - IFRS 1 – application and choice of optional exemptions
- Consolidation
  - Definition of control is beyond equity ownership and board control
  - JCE will have to be equity accounted
  - SPEs to be consolidated
  - Exclusion from consolidation almost remote

Issues in changeover

IFRS 1

- Property, Plant and Equipment
  - Periodic assessment of useful life and residual value
  - Component approach mandatory – assessment to be carried out
  - Revaluation model – depreciation through income statement
- Taxation
  - Changes in tax legislations due to change in accounting language
  - Subsidiary level implications

Issues in changeover

IFRS 1

- Financial Instruments
  - Classifying and treating your financial instruments
  - Embedded derivatives
  - Hedge accounting
- Valuation issues
  - 50 to 75% of the Balance Sheet can be fair value
  - Availability of fair valuation experts
  - Assessing the impact of impairment of assets

First time adoption - Overview

IFRS 1

Principles

Exemptions & Exceptions

Disclosures

General Principles

IFRS 1

- Application
  - To the first IFRS financial statements
  - Each interim report under IAS 34 in the first period
- Requires
  - Identification of date of transition
  - Selection of accounting policies that comply with IFRSs
  - Preparation of an opening IFRS balance sheet
  - Preparation of the first IFRS financial statements

General Principles

IFRS 1

- IFRS 1 requires retrospective adoption of most IFRSs, BUT
  - There are specific exemptions and exceptions
  - The latest version of each IFRS will be applied
  - There is guidance on the use of previous estimates
  - The disclosure requirements are extensive

The dates to remember

IFRS 1

Date of transition

Date of adoption

Reporting Date

IFRS – Implementation Guidance

IFRS 1

identify the first IFRS financial statements

prepare an opening balance sheet at the date of transition to IFRS

select accounting polices that comply with the standards in force at the closing balance sheet date

apply them retrospectively to all of the periods presented

consider whether to apply any of the fifteen exemptions from retrospective application

apply the four mandatory exceptions from retrospective application

make extensive disclosures to explain the transition to IFRS

First IFRS Statement

IFRS 1

- the first annual financial statements to contain an "explicit and unreserved statement of compliance with IFRS"

Opening Balance Sheet

IFRS 1

- The starting point for all subsequent accounting under IFRS
- To be prepared at "the date of transition to IFRS“
- This is the beginning of the earliest period for which full comparative information is presented in accordance with IFRS
- The opening IFRS balance sheet
  - includes all the assets and liabilities that IFRS require
  - excludes any assets and liabilities that IFRS do not permit
  - classifies all assets, liabilities and equity in accordance with; and
  - measures all items in accordance with IFRS

Possible Exclusions

IFRS 1

- Deferred costs that do not meet the IFRS definition of an asset;
- Restructuring provisions where there is no legal or constructive obligation;
- General provisions or reserves where there is no legal or constructive obligation;
- Receivables for revenue where the risks and rewards of ownership have not been transferred to the buyer or the service has not been provided;
- Deferred tax assets where it is not probable there will be sufficient profits in future periods to recover the asset.

Possible Reclassifications

IFRS 1

- any amounts classified as equity under the previous GAAP that would meet the definition of a liability in IFRS;
- any assets and liabilities shown net under previous GAAP that cannot be offset under IFRS;
- any assets and liabilities that are not classified into those amounts that are current and those that are non-current in accordance with IFRS;
- investments that must be classified in accordance with IAS 39;

Possible differences

IFRS 1

- Deferred taxes in accordance with IAS 12
- Provisions in accordance with IAS 37
- Effect of business combinations

- Changes in accounting policies requiring retrospective adjustments
- Accounting errors requiring adjustment in earlier years
- Use of functional currency which is different than the recording currency

- Deferred Tax impact on consolidation
- Fair Value measurements

- PPE and intangible assets where the depreciation or amortisation period under previous GAAP does not comply with IFRS
- Capitalisation of borrowing costs and exchange differences
- Intangible assets having indefinite useful life

- Financial assets and liabilities that are measured in accordance with the requirements of IAS 39

Accounting Policies

IFRS 1

- The first IFRS financial statements are prepared using accounting policies that comply with the standards in force at the "reporting date"
- This is the closing balance sheet date for the first IFRS financial statements
- These polices are applied retrospectively to the opening IFRS balance sheet and all of the periods presented in the first IFRS financial statements.
- Successive versions of the same standard are not applied in different periods
  - The transition guidance in individual standards, and the guidance in IAS 8 for changes in accounting policies, apply to existing IFRS users, and are not applied by first-time adopters

Optional Exemptions - Summary

IFRS 1

- Business combinations
- Property, plant and equipment, investment properties, intangibles
- Employee benefits
- Cumulative translation adjustment
- Compound instruments
- Transition date for subsidiaries, associates and joint ventures
- Comparatives for financial Instruments
- Designation of financial assets and financial liabilities
- Decommissioning liabilities
- Share-based payments
- Insurance contracts
- Leases
- Exploration costs
- Fair value measurement of financial instruments at initial recognition
- Financial instruments Disclosure restatement

Mandatory Exceptions - Summary

IFRS 1

- Estimates
- Derecognition of financial assets and liabilities
- Assets held for sale
- Hedge accounting

Optional Exemptions

IFRS 1

- An entity is not required to restate business combinations that were recognised before the date of the transition to IFRS
- Fair value at the date of transition to IFRS may be used as deemed cost for any individual item of property, plant and equipment
- Employee benefits - Entities can choose either to:
  - recognise actuarial gains and losses in the income statement immediately;
  - recognise gains the gains and losses outside the income statement in a statement of recognised income and expense (SORIE); or
  - defer the gains and losses and recognise them in the income statement over a number of years

Optional Exemptions

IFRS 1

- The cumulative translation adjustment may be set to zero for all subsidiaries
- Management is not required to separately identify the two elements of the equity component if the liability component is not outstanding at the date of transition
- A subsidiary that adopts IFRS later than its parent can measure its assets and liabilities either at the carrying amounts included in the parent's consolidated financial statements or by applying IFRS 1 at its date of transition to IFRS
- An entity that has a date of adoption of IFRS prior to 1 January 2006 may choose not to restate its comparatives in accordance with IAS 32 and IAS 39
- IFRS 1 allows an entity to make the same classification for existing financial assets and financial liabilities when IAS 32 and IAS 39 are first applied

Optional Exemptions

IFRS 1

- IFRS 1 provides an exemption from full retrospective application of IFRIC 1 (changes made to a decommissioning liability, for which an asset is recognised, are recognised against the cost of the asset)
- A first-time adopter may choose to apply IFRS 2 (Share Based Payments) to other than equity instruments
- A first time adopter with an adoption date before 1 January 2006 need not restate comparatives in accordance with IFRS 4 (Insurance Contracts)
- A first-time adopter can follow the transitional provisions in IFRIC 4 (Lease Accounting Guidance)
- Management of an entity that adopts IFRS before 1 January 2006 and early adopts IFRS 6 can choose not to restate comparatives as per IFRS 6, "Exploration for and evaluation of mineral resources"

Optional Exemptions

IFRS 1

- Management of a first-time adopter has 3 options in applying IAS 39 requirements to financial instruments with no active market
  - retrospectively;
  - prospectively to transactions entered into after 25 October 2002 (i.e. the effective date of the equivalent US GAAP requirements); or
  - prospectively to transactions entered into after 1 January 2004 (i.e. the date of transaction to IFRS for many entities).
- The management of an entity that adopts IFRS before 1 January 2006 and early adopts IFRS 7 can choose not to restate the comparative accounting disclosures and comparative risk disclosures in accordance with IFRS 7 "Financial Instruments: Disclosures"

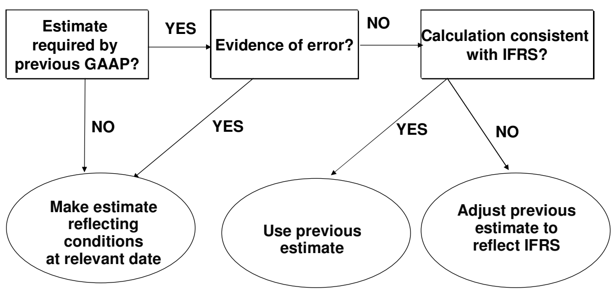
Mandatory Exceptions

IFRS 1

- IAS 39 is applied retrospectively to the derecognition of non-derivative financial assets and non-derivative financial liabilities. Such financial assets and liabilities derecognised before 1 January 2004 under previous GAAP are not recognised on the opening IFRS balance sheet
- A hedge relationship is not recognised in the opening balance sheet at the date of first application of IAS 32 and IAS 39 if it is of a type that is not permitted under IFRS
- An entity with a transition date before 1 January 2005 must apply the transitional provisions in IFRS 5. Consequently it is not permitted to apply IFRS 5 to the comparative period unless the valuation and other information needed to apply IFRS 5 were obtained at the time that the criteria were met

Mandatory Exceptions - Estimate

IFRS 1



Disclosures

IFRS 1

- The first IFRS financial statements should include a reconciliation of:
  - equity from the previous GAAP to IFRS at the date of transition and at the end of the last period presented in the entity's most recent financial statements under previous GAAP; and
  - net profit from the previous GAAP to IFRS for the last period in the entity's most recent financial statements under previous GAAP
- Other disclosures
  - The disclosures that IAS 36 requires are given when impairment losses are recognised in the opening IFRS balance sheet
  - The aggregate fair values and the aggregate adjustment to the previous carrying amounts are disclosed for each line item, when fair value is used as deemed cost
  - An entity should also explain material adjustments to the cash flow statement

Comparatives

IFRS 1

- The first IFRS financial statements should include at least one year of comparative information prepared in accordance with IFRS
- An entity can elect to present additional years of comparative information in accordance with IFRS, and this information might be required for regulatory purposes

Questions?

Thank you

ganesanca@yahoo.com