



**INTERNATIONAL FEDERATION
OF ACCOUNTANTS**

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DATE: 20 JUNE 2003
MEMO TO: MEMBERS OF THE IFAC PUBLIC SECTOR COMMITTEE
FROM: LI LI LIAN AND AHMAD HAMIDI-RAVARI
SUBJECT: **IPSAS REVIEW AND UPDATE – HARMONIZATION WITH IFRSs**

ACTION REQUIRED

The Committee is asked to:

- **determine** whether to action an IPSAS Improvement Project.

AGENDA MATERIAL:

	Pages
15A.2 Overview of anticipated differences: IPSASs and IFRS as at March 2004	15.4-15.12
15A.3 Details of anticipated differences: IPSASs and IFRS as at March 2004	15.13-15.49

BACKGROUND

At the April 2003 meeting, the PSC noted that:

- IASB improvements and convergence projects will impact on current IPSASs;
- IPSASs should reflect the requirements in the equivalent IFRSs, unless there was a public sector specific reason for a difference;
- it was desirable that a stable platform of IPSASs, reflecting the IFRSs where appropriate, also be in place by the end of 2004, but that it may not be wise to change the recently completed IPSASs at this stage; and
- PSC would need to determine whether it needed to undertake its own improvements program.

Staff were directed to prepare a paper identifying current and anticipated differences between IPSASs and IFRSs as of the end of 2003 or early 2004 for consideration by the PSC at its July 2003 meeting.

The IASB General Improvements Project ED was issued in May 2002. The PSC submitted their comments on the ED in September 2002. (PSC submission has not been included in agenda materials for this meeting. The submission was included as item 21.4a in the agenda materials for the Hong Kong meeting in November 2002. It is available. Please advise if you wish to receive a copy.)

The IASB General Improvements Project mainly impacts 12 existing IASs (10 existing IPSASs) but has consequences for other IASs.

Agenda item 15A.2 provides an overview of the improvements proposed by the IASB, PSC comments on the proposed improvements, and the decisions made by the IASB to date on them. The summary also indicates how those IASB decisions will affect existing IPSASs.

Agenda item 15A.3 provides a more detailed review of the extent of changes agreed by the IASB and where possible, the impact of those changes on existing IPSASs in marked-up form. Staff note that it is not intended to go through the changes depicted in Agenda item 15A.3 at this meeting. It will be necessary to go through a 15A.3 type paper, if the PSC decides to action an IPSAS Improvement Project. Rather, at this meeting, it is intended to give, to the extent possible, a realistic picture of the extent of changes to IPSASs that Staff expect to arise from an IPSAS Improvement Project based on the improved IFRSs arising from the IASB Improvement Project.

ISSUES – To action an IPSAS Improvement Project?

The issues noted below are to be considered within the context of the existing PSC policy where IPSASs are based on IASs, unless there is a specific public sector issue that warrants a deviation.

Options available in regards to an IPSAS Improvement Project based on the IASB's General Improvement Project are:

- 1) Do nothing now; or
- 2) Action an IPSAS Improvement Project immediately.

Do Nothing Now

The benefits of doing nothing now are as follows:

- it allows PSC and staff resources to focus on public sector specific issues;
- it allows time for PSC to plan and perform its own improvements project. Such a project can incorporate the feedback from the works of the steering committees/working groups and the implementation of the improved IFRSs; and
- it may not be wise to revise the IPSASs so soon after their issue.

Doing nothing now also has some drawbacks:

- it will break the nexus between IPSASs and IASs/IFRSs;
- the IPSASs will need to be updated at some time in the future, therefore it is better to make available to entities intending to adopt IPSASs the improved IPSASs sooner rather than later. This will allow them to base their transition to IPSASs on improved Standards rather than going through the longer and more costly process of overhauling their previous systems to comply with existing IPSASs, and later, updating their systems again to apply the improved IPSASs; and
- while there may be benefits in having a full PSC improvements project (i.e. reviewing the full suite of IPSASs for any improvements in addition to the proposed improvements of the IASB), it is unlikely that there will be sufficient staff resources and PSC time to support this improvements project in the short to medium term.

Action an IPSAS Improvement Project Immediately

The benefits of immediate actioning an IPSAS Improvement Project are as follows.

- it maintains the nexus between IPSASs and IFRSs in accordance with the declared PSC policy;

- it allows entities intending to adopt IPSASs to base their transition to IPSASs on a set of improved and higher quality Standards;
- it allows the PSC to position itself such that there will not be considerable delay in issuing improved IPSASs which reflect the IFRSs issued as at 31 March 2004. (The IASB intends to issue revised Standards arising from their improvement and convergence projects by 31 March 2004. IASB's publication of any Standard after this date will not be effective for year 2005 transition to IFRSs. Therefore, Standards existing at 31 March 2004 will provide a stable platform for preparers of financial statements.); and
- it is anticipated that the IASB will issue improved IFRSs one or two at a time, rather than as one complete package. Actioning this Project now means that staff can begin to work on the "improved" IFRSs as they are issued and can bring EDs of the equivalent IPSASs to the PSC progressively over late 2003 and during 2004.

The drawbacks of immediate actioning of an IPSAS Improvement Project are possible pressure on PSC and Staff resources to deal with public sector specific projects.

Staff recommendation

Option ii – the immediate action of an IPSAS Improvement Project

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PROJECT MANAGER

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Overview of Anticipated Differences: IPSASs and IFRS as at March 2004

The table below summarizes the effect on 10 IPSASs of improvements to 12 IASs under the IASB's General Improvement Project. The improvements are based on IASB's decisions to date on changes proposed in the Improvement Project ED. Agenda item 15A.3 provides a more detailed review of the impact of these changes on existing IPSASs. It shows the impact of the change on existing IPSASs in marked-up form to the extent possible.

The table focuses on the questions raised in the Improvement Project ED. To highlight the extent of changes arising from the Project, the table also identifies the IPSAS paragraphs affected by other decisions of the IASB made when deliberating the improvement project and issues raised by commentators.

IASs Impacted/ Issues Raised in the ED/ Decisions made by IASB/ Submission by the PSC on Improvement ED	Expected Effect of IASB Decisions on Existing IPSASs	Detailed Changes identified in Item 15A.3 (page)
IAS 1, <i>Presentation of Financial Statements</i>	IPSAS 1 <i>Presentation of Financial Statements</i>	15.14
Note: The ED on IAS 1 has been so substantially changed that the IASB issued the improvement ED on IAS 1 as a clean copy.		
1) Tighten the existing requirements regarding departure from a requirement of an IFRS or Interpretation of International Financial Reporting Standard (IIFRS) to achieve fair presentation. PSC submission on the Improvement ED: Majority Agreed with the proposal. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 1 Para 28 – 30, 32-33: <ul style="list-style-type: none"> Split the current para 28 into 2 paragraphs Include additional disclosures when departing from requirements of an IPSAS Delete paras 32-33 	
2) To prohibit presentation of items of income and expense as 'extraordinary items' in the income statement and notes. PSC submission on the Improvement ED: <ul style="list-style-type: none"> Majority agreed that extraordinary items should not be described as "extraordinary items" on the face of the financial statements and should be reported above the line. Believes giving some emphasis to extraordinary items provides useful information to users. Suggested that IAS 1 should require more information regarding items that are 'extraordinary' and that the definition of extraordinary items be tightened as done in IPSASs. 	Affects IPSAS 1 & IPSAS 3: <ul style="list-style-type: none"> Delete IPSAS 1 para 101(f) Add IPSAS 1 para 103A Delete IPSAS 3 paras 14-25 	

IASs Impacted/ Issues Raised in the ED/ Decisions made by IASB/ Submission by the PSC on Improvement ED	Expected Effect of IASB Decisions on Existing IPSASs	Detailed Changes identified in Item 15A.3 (page)
Status of IASB deliberations on this issue: Agreed with the proposal.		
<p>3) Reclassification of long-term financial liability due to be settled within 12 months of balance sheet date as current liability, even if an agreement to refinance, or to reschedule payments, on a long-term basis is completed after the balance sheet date and before the financial statements are authorized for issue.</p> <p>PSC submission on the Improvement ED:</p> <ul style="list-style-type: none"> ◦ Majority Disagreed. ◦ Noted that irrespective of which approach IASB prefers, full disclosures are necessary. <p>Status of IASB deliberations on this issue: Agreed in accordance with definition of non-adjusting events after the balance sheet date in IAS 10, <i>Events After the Balance Sheet Date</i>.</p>	Affects IPSAS 1: <ul style="list-style-type: none"> • Amend para 86 	
<p>4a) Long-term financial liability that is payable on demand because the entity breached a condition of its loan agreement should be classified as current at the balance sheet date, even if the lender has agreed after the balance sheet date, and before the financial statements are authorized for issue, not to demand payment as a consequence of the breach.</p> <p>PSC submission on the Improvement ED: Majority Disagreed.</p> <p>Status of IASB deliberations on this issue: Agreed.</p>	Affects IPSAS 1: <ul style="list-style-type: none"> • Delete para 88 and replace with a new concept. 	
<p>4b) If a lender was entitled to demand immediate repayment of a loan because the entity breached a condition of its loan agreement, but agreed by the balance sheet date to provide a period of grace within which the entity can rectify the breach and during that time the lender cannot demand immediate repayment, the liability is classified as non-current if it is due for settlement, without that breach of the loan agreement, at least twelve months after the balance sheet date and:</p> <ul style="list-style-type: none"> (i) the entity rectifies the breach within the period of grace; or (ii) when the financial statements are authorized for issue, the period of grace is incomplete and it is probable that the breach will be rectified. <p>PSC submission on the Improvement ED: Agreed.</p> <p>Status of IASB deliberations on this issue: Agreed.</p>	Affects IPSAS 1: <ul style="list-style-type: none"> • Add new paragraphs 88A and 88B. 	

IASs Impacted/ Issues Raised in the ED/ Decisions made by IASB/ Submission by the PSC on Improvement ED	Expected Effect of IASB Decisions on Existing IPSASs	Detailed Changes identified in Item 15A.3 (page)
<p>5) Disclose the judgments made by management in applying accounting policies that have the most significant effect on the amounts of items recognized in the financial statements.</p> <p>PSC submission on the Improvement ED: Majority Agreed Status of IASB deliberations on this issue:</p> <ul style="list-style-type: none"> ◦ Agreed. ◦ Add additional guidance in applying this requirement. 	<p>Affects IPSAS 1:</p> <ul style="list-style-type: none"> • Add new paragraphs 132A and 132B 	
<p>6) Disclose key assumptions about the future and other sources of measurement uncertainty that have a significant risk of causing material adjustment to the carrying amount of assets and liabilities within the next financial year.</p> <p>PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.</p>	<p>Affects IPSAS 1:</p> <ul style="list-style-type: none"> • Add new paragraphs 132+1 – 132+1E 	
IAS 2, <i>Inventories</i>	IPSAS 12 <i>Inventories</i>	15.22
<p>1) Elimination of LIFO method.</p> <p>PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.</p>	<p>No effects on IPSASs</p>	
<p>2) Retain requirements of reversals of write-downs of inventories, when circumstances that caused the write-down ceased to exist, and the recognition of write-downs in profit and loss.</p> <p>PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.</p>	<p>No effects on IPSASs</p>	
Other paragraphs amended due to decisions made by the IASB when deliberating the Project and issues raised by commentators.	IPSAS 12 para: 1(c), 15	
IAS 8, <i>Net Profit or Loss for the Period, Fundamental Errors and Change in the Accounting Policies</i>	IPSAS 3, <i>Net Surplus or Deficit for the Period, Fundamental Errors and Changes in the Accounting Policies</i>	15.23
<p>Note: The ED on IAS 8 has been so substantially changed that the IASB issued the improvement ED on IAS 8 as a clean copy.</p>		

IASs Impacted/ Issues Raised in the ED/ Decisions made by IASB/ Submission by the PSC on Improvement ED	Expected Effect of IASB Decisions on Existing IPSASs	Detailed Changes identified in Item 15A.3 (page)
1) Eliminate the allowed alternative treatment for voluntary changes in accounting policies and correction of errors. PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 3: <ul style="list-style-type: none"> • Delete paras 45-47 • Delete paras 65-68 • Add new guidance that voluntary changes in accounting policies be applied retrospectively 	
2) Eliminate distinction between fundamental and material errors. PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 3: <ul style="list-style-type: none"> ◦ Amend para 6 ◦ Delete paras 38-40 	
IAS 10, <i>Events After Balance Sheet Date</i>	IPSAS 14 <i>Events After Balance Sheet Date</i>	15.27
If dividends declared after balance sheet date, an entity should not recognize those dividends as liability, but disclose them in the notes to the financial statements. PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 14: <ul style="list-style-type: none"> • Amend paras 13 and 15 	
IAS 15 <i>Information Reflecting the Effects of Changing Prices</i>	No equivalent PSC Pronouncement	15.28
Withdraw Standard PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.	Not Applicable	
IAS 16, <i>Property, Plant and Equipment (PPE)</i>	IPSAS 17 <i>Property, Plant and Equipment</i>	15.29
Most paragraphs in the existing IAS 16 have been amended.		
1) Exchanges of PPE should be measured at fair value, unless fair value of neither of the assets exchanged can be determined reliably. PSC submission on the Improvement ED: Majority Agreed. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 17: <ul style="list-style-type: none"> • Amend para 31 • Add new para 31A • Delete para 32 	
2) Exchanges of intangible assets should be measured at fair value, unless fair value of neither of the assets exchanged can be determined reliably. PSC submission on the Improvement ED: Agreed in principle because no IPSASs on intangible assets. Status of IASB deliberations on this issue: Agreed.	Not applicable	

IASs Impacted/ Issues Raised in the ED/ Decisions made by IASB/ Submission by the PSC on Improvement ED	Expected Effect of IASB Decisions on Existing IPSASs	Detailed Changes identified in Item 15A.3 (page)
<p>3) If PPE becomes temporarily idle, retired from active use or held for disposal – depreciation should not cease.</p> <p>PSC submission on the Improvement ED:</p> <ul style="list-style-type: none"> Concerned that the proposal may not be consistent with the depreciation requirements in paragraphs 41 – 52A of the ED, especially where the temporary idle period was intended and built into the estimate of the useful life; disagreed with the proposed changes to the wording in paragraph 59 (equivalent IPSAS para 72); and agreed those PPE should be tested for impairment annually. <p>Status of IASB deliberations on this issue: Agreed.</p>	<p>Affects IPSAS 17:</p> <ul style="list-style-type: none"> Amend para 72 	
Other paragraphs amended due to decisions made by the IASB when deliberating the Project and issues raised by commentators.	IPSAS 17: paras: 4, 28, 30+1A, 37, 32A-D, 65, possible new paras within paras 54-61	
IAS 17, <i>Leases</i>	IPSAS 13 <i>Leases</i>	15.32
<p>1) Lease of land and buildings should be split.</p> <p>PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.</p>	<p>Affects IPSAS 17:</p> <ul style="list-style-type: none"> Add paras 16A, 16B & 16C 	
<p>2) Initial direct costs in negotiating leases and incremental costs directly attributable to the lease transaction should be capitalized and allocated over the lease term.</p> <p>PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.</p>	<p>Affects IPSAS 13:</p> <ul style="list-style-type: none"> Add new definition (para 7) Add para 41A Delete para 45 Amend paras 47, 51 & 57 	
IAS 21, <i>The Effects of Changes in Foreign Exchange Rates</i>	IPSAS 4 <i>The Effect of Changes in Foreign Exchange Rates</i>	15.34
<p>Note:</p> <p>1) The ED on IAS 21 has been so substantially changed that the IASB issued the improvement ED on IAS 21 as a clean copy.</p> <p>2) The PSC did not review IAS 21 in detail, but agreed in principle to the proposed changes.</p>		
<p>1) New notion and definition of functional currency.</p> <p>PSC submission on the Improvement ED: Agreed in principle. Status of IASB deliberations on this issue: Agreed in principle.</p>	<p>Affects IPSAS 4:</p> <ul style="list-style-type: none"> New definition (para 9) Add guidance on how to determine functional currency 	

IASs Impacted/ Issues Raised in the ED/ Decisions made by IASB/ Submission by the PSC on Improvement ED	Expected Effect of IASB Decisions on Existing IPSASs	Detailed Changes identified in Item 15A.3 (page)
2) Reporting entity be permitted to choose its presentation currency (in the financial statements). PSC submission on the Improvement ED: Agreed in principle. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 4: <ul style="list-style-type: none"> Redraft and add guidance that a reporting entity is allowed to choose its presentation currency 	
3) Entities to translate financial statements into the presentation currencies using the same method as required for translating a foreign operation for inclusion in the reporting entity's financial statements. PSC submission on the Improvement ED: Agreed in principle. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 4: <ul style="list-style-type: none"> Delete paras 33-40, 57-79 Amend paras 41-54 	
4) Remove allowed alternative treatment to capitalise certain exchange differences. PSC submission on the Improvement ED: Agreed in principle. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 4: <ul style="list-style-type: none"> Delete paras 30-32 	
5) Goodwill and fair value adjustments to assets and liabilities that arise from the acquisition of foreign operations be treated as assets and liabilities of the foreign operations and translated at the closing rate. PSC submission on the Improvement ED: Agreed in principle. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 4: <ul style="list-style-type: none"> Remove para 46(b) 	
IAS 24, <i>Related Party Disclosures</i>	IPSAS 20 <i>Related Party Disclosures</i>	15.39
IPSAS 20 is drafted substantially differently from the existing IAS 24. Consequently, it is not possible to identify specific paragraphs affected by the Improvements Project. Changes made may be pervasive and require that IAS 24 be reviewed in its entirety rather than go through the issues raised by the IASB.		
1) Not require disclosure of management compensation, expense allowances and similar items paid in the course of an entity's operations. PSC submission on the Improvement ED: Majority disagreed. Status of IASB deliberations on this issue: Agreed.	See above	

IASs Impacted/ Issues Raised in the ED/ Decisions made by IASB/ Submission by the PSC on Improvement ED	Expected Effect of IASB Decisions on Existing IPSASs	Detailed Changes identified in Item 15A.3 (page)
2) Not require disclosure of related party transactions and outstanding balances in separate financial statements of parent of wholly-owned subsidiary that are made available with consolidated financial statements of the group to which that entity belongs. PSC submission on the Improvement ED: Majority disagreed. Status of IASB deliberations on this issue: Disagreed.	See above	
IAS 27, Consolidated Financial Statements and Accounting for Investments in Subsidiaries	IPSAS 6 Consolidated Financial Statements and Accounting for Controlled Entities	15.40
The proposed new name of the IAS 27 is Consolidated and Separate Financial Statements.		
1) Tighten circumstances where parent need not prepare consolidated financial statements. PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 6: <ul style="list-style-type: none"> • Amend paras 16, 17, 22, 53, 57 • Delete paras 18-20, 23 • Add para 22A, 53A, 58 	
2) Minority interests be presented within equity, but separately from parent shareholders' equity. PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 6: <ul style="list-style-type: none"> • Amend para 50 	
3) Investments in subsidiaries, jointly controlled entities and associates should be carried at cost or accounted for in accordance with IAS 39, <i>Financial Instruments: Recognition and Measurement</i> in the investor's separate financial statements. PSC submission on the Improvement ED: Majority Agreed. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 6: <ul style="list-style-type: none"> • Amend para 53 • Add para 53A 	
Other paragraphs amended due to decisions made by the IASB when deliberating the Project and issues raised by commentators.	IPSAS 6: paras: 3, 4, 7, possible 38A, paras 21-25	

IASs Impacted/ Issues Raised in the ED/ Decisions made by IASB/ Submission by the PSC on Improvement ED	Expected Effect of IASB Decisions on Existing IPSASs	Detailed Changes identified in Item 15A.3 (page)
IAS 28, <i>Accounting for Investment in Associates</i>	IPSAS 7 <i>Accounting for Investments in Associates</i>	15.45
Most paragraphs in the existing IAS 28 have been amended.		
1) IAS 28 and IAS 31, <i>Financial Reporting of Interests in Joint Ventures</i> , should not be applied to investments that otherwise would be associates or joint ventures held by venture capital organizations, mutual funds, unit trusts and similar entities if these investments are measured at fair value in accordance with IAS 39, <i>Financial Instruments: Recognition and Measurement</i> , when such measurement is well-established practice in those industries. PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 7: <ul style="list-style-type: none"> Amend para 1 	
2) When an associate incurs losses, the amount of what should be reduced to nil would include investments in equity of the associate and other interests such as long-term receivables. PSC submission on the Improvement ED: Majority Agreed. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 7: <ul style="list-style-type: none"> Amend para 36 Add paras 36A and 36B 	
IAS 33, <i>Earning per Share</i> PSC submission on the Improvement ED: The Standard is not relevant to the public sector.	Not relevant to the public sector	15.47
IAS 40, <i>Investment Property</i>	IPSAS 16 <i>Investment Property</i>	15.48
1) The definition of investment property should be changed to permit the inclusion of a property interest held under an operating lease provided that: a. the rest of the definition of investment property is met; and b. the lessee uses the fair value model set out in IAS 40. PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 16: <ul style="list-style-type: none"> Amend definition of investment property (para 6) Delete para 17 	
2) A lessee that classifies a property interest held under an operating lease as investment property should account for the lease as if it were a finance lease. PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Agreed.	Affects IPSAS 16: <ul style="list-style-type: none"> Delete para 17 Add para 334A 	

IASs Impacted/ Issues Raised in the ED/ Decisions made by IASB/ Submission by the PSC on Improvement ED	Expected Effect of IASB Decisions on Existing IPSASs	Detailed Changes identified in Item 15A.3 (page)
<p>3) IASB should not eliminate the choice between cost model and fair valued model, but keep the matter under review with a view to reconsidering the option to use the cost model in due course.</p> <p>PSC submission on the Improvement ED: Agreed. Status of IASB deliberations on this issue: Noted that majority of commentators agreed with proposal.</p>	<p>No effect on IPSASs</p>	

Agenda Item 15A.3
Details of anticipated differences: IPSASs and IFRS as at
March 2004

Note:

- 1) The changes to IPSAS paragraphs shown in marked-up form have not been approved by the PSC.
- 2) This document includes, where possible, the impact of the proposed changes by the IASB on existing IPSASs in marked-up form. Where IASB has provided a clean copy of the proposed revised Standard rather than a marked-up copy, Staff have highlighted such cases by noting that a full understanding of the extent of changes to that particular IAS is only possible if it is reviewed in its entirety rather than just reviewing the proposed changes. An overview of this Document is included as Agenda 15A.2.
- 3) It is not intended to go through the changes depicted in this document in the meeting. Rather, it is intended to give to the extent possible, a realistic picture of the extent of changes to IPSASs that Staff expect to arise from an IPSAS Improvement Project based on Improved IFRSs.

IAS 1, *Presentation of Financial Statements***Equivalent PSC Pronouncements: IPSAS 1 *Presentation of Financial Statements***

The revised IAS has been substantially restructured from the previous format – it was provided as a clean copy. Where possible, Staff have provided a mark-up version of the impact on relevant paragraphs in IPSAS 1, otherwise, Staff have provided an explanation of the impact of changes on the Standard.

Question 1

Do you agree with the proposed approach regarding departure from a requirement of an International Financial Reporting Standard or an Interpretation of an International Financial Reporting Standard to achieve a fair presentation (see proposed paragraphs 13-16)?

The proposed paragraphs 13-16 replace the existing paras 13-18 of IAS 1 (*Equivalent paras 28-30 and 32-35 of IPSAS 1*). Proposed para 15 now also requires that an entity provide additional disclosures when departing from requirements of an IFRS or Interpretation of an IFRS if compliance with the requirements would conflict with the objective of financial statements as set out in the IASB Conceptual Framework.

IASB Decision to date: Agreed with the proposal.

PSC Submission: Majority Agreed with proposed amendments

Effect on IPSASs: IPSAS 1 Para 28 – 30, 32-35

- a) To split the current para 28 into 2 paragraphs
- b) To include additional disclosures when departing from requirements of an IPSAS as noted in para 15 of the ED
- c) To delete paras 32 – 33 (the revised IAS no longer has the equivalent IPSAS para 32-33)

28 *In the extremely rare circumstances ~~in which~~ management concludes that compliance with a requirement in a Standard would be misleading, that it would conflict with the objective of financial statements, the entity shall depart from that requirement in the manner set out in paragraph 29 if the relevant regulatory framework requires or otherwise does not prohibit such a departure.*

29 *When an entity ~~and therefore that~~ departs from a requirement of an International Public Sector Accounting Standard, it shall ~~is necessary to achieve a fair presentation, an entity should~~ disclose:*

- (a) *that management has concluded that the financial statements fairly present the entity's financial position, financial performance and cash flows;*
- (b) *that it has complied in all material respects with applicable International Public Sector Accounting Standards except that it has departed from a Standard in order to achieve a fair presentation;*
- (c) *the Standard from which the entity has departed, the nature of the departure, including the treatment that the Standard would require, the reason why that treatment would be misleading in the circumstances, and the treatment adopted; and*
- (d) *the financial impact of the departure on the entity's net surplus or deficit, assets, liabilities, net assets/equity, and cash flows for each period presented.*

30. In the extremely rare circumstances in which management concludes that compliance with a requirement in an International Public Sector Accounting Standard would be so misleading that it would conflict with the objective of financial statements, and the relevant regulatory framework prohibits departure from the requirement, the entity shall, to the maximum extent possible, reduce the perceived misleading aspects of compliance by disclosing:
- (a) the Standard requiring the entity to report information concluded to be misleading, the nature of the requirement, and the reason why management has concluded that complying with that requirement is so misleading in the circumstances that it conflicts with the objective of financial statements; and
 - (b) for each period presented, the adjustments to each item in the financial statements that management has concluded would be necessary to achieve a fair presentation.
- ~~29. Financial statements may be described as being “based on” or “complying with the significant requirements of”, or “in compliance with the accounting requirements of” International Public Sector Accounting Standards. There may be no further information, although it is clear that significant disclosure requirements, if not accounting requirements, are not met. Such statements are misleading because they detract from the reliability and understandability of the financial statements.~~
- ~~30. In order to ensure that financial statements that claim compliance with International Public Sector Accounting Standards will meet the standards required by users internationally, this Standard includes an overall requirement that financial statements should give a fair presentation, guidance on how the fair presentation requirement is met, and further guidance for determining the extremely rare circumstances when a departure is necessary. It also requires prominent disclosure of the circumstances surrounding a departure. However, where an entity adopts International Public Sector Accounting Standards, the existence of conflicting national requirements (for example, where financial reporting requirements set by the government conflict with these Standards) is not, in itself, sufficient to justify a departure in financial statements that claim compliance with International Public Sector Accounting Standards.~~
- ~~32. In virtually all circumstances, a fair presentation is achieved by compliance in all material respects with applicable International Public Sector Accounting Standards. A fair presentation requires:~~
- ~~(a) selecting and applying accounting policies in accordance with paragraph 37;~~
 - ~~(b) presenting information, including accounting policies, in a manner which provides relevant, reliable, comparable and understandable information; and~~
 - ~~(c) providing additional disclosures when the requirements in International Public Sector Accounting Standards are insufficient to enable users to understand the impact of particular transactions or events on the entity’s financial position and financial performance.~~
- ~~33. In extremely rare circumstances, application of a specific requirement in an International Public Sector Accounting Standard might result in misleading financial statements. This will be the case only when the treatment required by the Standard is clearly inappropriate and thus a fair presentation cannot be achieved either by applying the Standard or through additional disclosure alone. Departure is not appropriate simply because another treatment would also give a fair presentation.~~
- ~~34. For the purposes of paragraphs 28-30, an item of information would conflict with the objective of financial statements when it does not represent faithfully the transactions or other events that it either purports to represent or could reasonably be expected to represent and, consequently, it would be likely to affect adversely economic decisions made by users of financial statements. When assessing whether a departure from complying with a specific requirement in International Public Sector Accounting Standards would be misleading that it would conflict with the objective of financial statements, is necessary, consideration is given to:~~

- (a) the objective of the requirement and why that objective is not achieved or is not relevant in the particular circumstances; and
- (b) the way in which the entity's circumstances differ from those of other entities which follow the requirement. There is a rebuttable presumption that if other entities in similar circumstances comply with the requirement, the entity's compliance with the requirement would not be so misleading that it would conflict with the objective of financial statements set out in the Standard.

~~35 Because the circumstances requiring a departure are expected to be extremely rare and the need for a departure will be a matter for considerable debate and subjective judgment, it is important that users are aware that the entity has not complied in all material respects with International Public Sector Accounting Standards. It is also important that they are given sufficient information to enable them to make an informed judgment on whether the departure is necessary and to calculate the adjustments that would be required to comply with the Standard.~~

QUESTION 2

Do you agree with prohibiting the presentation of items of income and expense as 'extraordinary items' in the income statement and the notes (see proposed paragraphs 78 and 79)?

Proposed paragraphs 78 and 79 prohibit an entity in presenting items of income and expense as 'extraordinary items' in the income statement and notes. There are no equivalent IPSAS paragraphs as they are new.

IASB Decision to date: Confirmed the prohibition to present extraordinary items in the income statement as proposed in para 78. The proposed para 79 was not accepted.

PSC Submission:

- Majority agreed that extraordinary items should not be described as "extraordinary items" on the face of the financial statements and should be reported above the line.
- Believes giving some emphasis to items meeting the definition of extraordinary items provides useful information to users. Suggested that IAS 1 should require the disclosure of more information regarding items that are 'extraordinary' and that the definition of extraordinary items be tightened and the definition in IPSAS be considered.

Effect on IPSASs (if IASB Decision are followed):

- a) Remove IPSAS 1 para 101(f) and add para 103(A).
- b) Remove IPSAS 3 paras 14-25. These paragraphs describe on how an extraordinary item is defined. (These paragraphs have not been provided in this paper.)

IPSAS 1 para 101

101 *As a minimum, the face of the statement of financial performance should include line items which present the following amounts:*

- (a) *revenue from operating activities;*
- (b) *surplus or deficit from operating activities;*

- (c) *finance costs;*
- (d) *share of net surpluses or deficits of associates and joint ventures accounted for using the equity method;*
- (e) *surplus or deficit from ordinary activities;*
- ~~(f) *extraordinary items;*~~
- (g) *minority interest share of net surplus or deficit; and*
- (h) *net surplus or deficit for the period.*

Additional line items, headings and sub-totals should be presented on the face of the statement of financial performance when required by an International Public Sector Accounting Standard, or when such presentation is necessary to present fairly the entity's financial performance.

103A *An entity shall not present any items of revenue and expense as extraordinary items, either on the face of statement of financial performance or in the notes.*

QUESTION 3

Do you agree that a long-term financial liability due to be settled within twelve months of the balance sheet date should be classified as a current liability, even if an agreement to refinance, or to reschedule payments, on a long-term basis is completed after the balance sheet date and before the financial statements are authorised for issue (see proposed paragraph 60)?

Proposed Paragraph 60

Proposed paragraph 60 amends the existing para 63 (*equivalent IPSAS para 86*). An entity will classify a financial liability as a current liability when it meets the criteria of proposed paragraph 60 (see proposed changes to IPSAS 1 para 86 below), as opposed to classifying it as a non-current liability, as currently required by the existing IAS 1.

IASB Decision to date: Agreed with the proposal. IASB noted that this treatment is in accordance with definition of non-adjusting events after the balance sheet date in IAS 10, *Events After the Balance Sheet Date*.

PSC Submission: Majority Disagreed with the proposal, but noted that irrespective of which approach IASB prefers, full disclosures are necessary.

Effect on IPSASs (if IASB's decision followed): Amend IPSAS 1 para 86 and change it from black letter to grey letter.

86 An entity ~~should continue to classify~~ies its long-term ~~interest-bearing~~financial liabilities as ~~non-current, even~~ when they are due to be settled within twelve months of the reporting date, even if:

- (a) the original term was for a period of more than twelve months; and
- ~~(b) the entity intends to refinance the obligation on a long-term basis; and~~
- ~~(c) that intention is supported by~~ an agreement to refinance, or to reschedule payments, on a long-term basis which is completed after the balance sheet date and before the financial statements are approved.

~~The amount of any liability that has been excluded from current liabilities in accordance with this paragraph, together with information in support of this presentation, should be disclosed in the notes to the statement of financial position.~~

QUESTION 4

Do you agree that:

- (a) a long-term financial liability that is payable on demand because the entity breached a condition of its loan agreement should be classified as current at the balance sheet date, even if the lender has agreed after the balance sheet date, and before the financial statements are authorised for issue, not to demand payment as a consequence of the breach (see proposed paragraph 62)?
- (b) if a lender was entitled to demand immediate repayment of a loan because the entity breached a condition of its loan agreement, but agreed by the balance sheet date to provide a period of grace within which the entity can rectify the breach and during that time the lender cannot demand immediate repayment, the liability is classified as non-current if it is due for settlement, without that breach of the loan agreement, at least twelve months after the balance sheet date and:
 - (i) the entity rectifies the breach within the period of grace; or
 - (ii) when the financial statements are authorised for issue, the period of grace is incomplete and it is probable that the breach will be rectified (see proposed paragraphs 63 and 64)?

Proposed Paragraph 62-64

The existing commentary para 65 (*equivalent IPSAS para 88*) has been replaced by proposed paragraphs 62-64.

IASB Decision to date:

- Agreed with proposal (a) above in accordance with the principles in IAS 10, *Events After the Balance Sheet Date*.
- Agreed with proposal (b), but added that if the breach of agreement was not rectified by the time the financial statements were authorized for issue, management should continue to classify the liability as non-current, and only if, the period of grace is for at least 12 months from the balance sheet date.

PSC Submission: Majority Disagreed with proposal (a) but Agreed with proposals (b).

Effect on IPSASs: IPSAS 1 para 88

IPSAS 1 will have to provide guidance on the issues discussed in Question 4 as IPSAS 1 does not explicitly discuss if a lender provides a period of grace to the borrower.

Currently, IPSAS 1 para 88 only states that if an entity has breached its borrowing covenants, and the liability is effectively payable on demand, the liability is classified as non-current only when the lender has agreed, prior to the approval of the financial statements, not to demand payment as a consequence of the breach and it is not probable that further breaches will occur within 12 months of the reporting date.

~~88. Some borrowing agreements incorporate undertakings (covenants) by the borrower which have the effect that the liability becomes payable on demand if certain conditions related to the borrower's financial position are breached. In these circumstances, if the conditions have been breached, the liability is classified as non-current only when:~~

- ~~(a) the lender has agreed, prior to the approval of the financial statements, not to demand payment as a consequence of the breach; and~~
- ~~(b) it is not probable that further breaches will occur within twelve months of the reporting date.~~

88. When an entity breaches an undertaking or covenant under a long-term loan agreement with the effect that the liability becomes payable on demand, the liability is classified as current at the reporting date, even if the lender has agreed, after the reporting date and before the approval of the financial statements, not to demand payment as a consequence of the breach.
89. However, if the lender has agreed by the reporting date to provide a period of grace within which the entity can rectify a breach of an undertaking or covenant under a long-term loan agreement and during that time the lender cannot demand immediate repayment, the liability is classified as non-current if it is due for settlement, without that breach of an undertaking or covenant, at least twelve months after the balance sheet date and:
- (a) the entity rectifies the breach within the period of grace; or
 - (b) when the financial statements are approval, the period of grace is incomplete and it is probable that the breach will be rectified.
90. In the circumstances described in paragraph 89, if the entity fails to rectify the breach within the period of grace, the failure confirms that, in substance, the loan was payable on demand at the balance sheet date and the liability is classified as current.

(NOTE: Para 90 may have to be updated based on the IASB decision that the period of grace described in para 90 is for at least 12 months from the reporting date.)

QUESTION 5

Do you agree that an entity should disclose the judgements made by management in applying the accounting policies that have the most significant effect on the amounts of items recognised in the financial statements (see proposed paragraphs 108 and 109)?

IASB Decision to date: Confirmed this decision and will include guidance in the revised Standard to assist preparers in applying this disclosure requirement.

PSC Submission: Majority agreed with proposed disclosure requirements.

Effect on IPSASs: Currently, IPSAS 1 does not require management's judgment in applying accounting policies. This may well require additional paragraphs as 132A and 132B in the 'Presentation of Accounting Policies' section of the IPSAS. But with the transfer of considerable material on accounting policies from IAS 1 to IAS 8, IPSAS 1 may not maintain its present section.

- 132A. An entity shall disclose, in the summary of significant accounting policies and/or other notes, the judgments made by management in applying the accounting policies that have the most significant effect on the amounts of items recognized in the financial statements.
- 132B. In applying accounting policies, management makes various judgements that can affect significantly the amounts of items recognized in the financial statements. For example, management makes judgments in determining whether financial assets are held-to maturity investments. Under paragraph 132A, an entity discloses those judgments made by management in applying accounting policies that have the most significant effect on the amounts of items recognised in the financial statements. These disclosures do not relate to the judgments disclosed under paragraph 132+1 (SEE Question 6 for more details). Some of these disclosures are required by other Standards. For example, IPSAS 6 Consolidated Financial Statements and Accounting for Controlled Entities, requires an entity to disclose the reasons why the entity's ownership interest does not constitute control, in respect of an investee that is not a subsidiary although more than half of its voting or potential voting power is owned directly or indirectly through subsidiaries.

QUESTION 6

Do you agree that an entity should disclose key assumptions about the future, and other sources of measurement uncertainty, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year (see proposed paragraphs 110-115)?

IASB Decision to date: Confirmed this decision. The IASB also agreed to include guidance in applying this disclosure requirement and to clarify that disclosure of measurement uncertainties for items using observed market prices at balance sheet date is not required.

PSC Submission: Agreed to the proposed disclosures.

Effect on IPSASs: Currently, IPSAS 1 (and other IPSASs) does not require the disclosure discussed in Question 6. This may well require additional paragraphs in the Standard. (Note: these mark-ups are provided as 132+1 as paragraph 133 of the existing IPSAS 1 was retained.)

Key Measurement Assumptions

132+1. An entity shall disclose in the notes information regarding key assumptions about the future, and other sources of measurement uncertainty, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year. In respect of those assets and liabilities, the notes shall include details of:

- (a) their nature; and**
- (b) their carrying amount as at the balance sheet date.**

132+1A The key assumptions and other sources of measurement uncertainty disclosed under paragraph 132+1 relate to the estimates that require management's most difficult, subjective or complex judgements. As the number of variables and assumptions affecting the possible future resolution of the uncertainties increases, those judgements become more subjective and complex, and the potential for a material adjustment to the carrying amounts of assets and liabilities normally increases accordingly.

132+1B The disclosures under paragraph 132+1 are presented in a manner that assists users of financial statements to understand the judgements management makes about the future. The nature and extent of the information provided vary according to the nature of the assumption and other circumstances. Examples of the types of disclosures made are:

- (a) the nature of the assumption or other measurement uncertainty;**
- (b) the sensitivity of carrying amounts to the methods, assumptions and estimates underlying their calculation, including the reasons for the sensitivity;**
- (c) the expected resolution of an uncertainty and the range of reasonably possible outcomes within the next financial year in respect of the carrying amounts of the assets and liabilities affected; and**
- (d) an explanation of changes made to past assumptions concerning those assets and liabilities, if the uncertainty remains unresolved.**

132+1C Examples of key assumptions disclosed under paragraph 132+1 are future interest rates, future changes in salaries, future changes in prices affecting other costs, and useful lives.

132+1D When it is not possible, without undue cost or effort, to disclose the extent of the possible effects of the assumption or other measurement uncertainty, the entity discloses that it is reasonably possible, based on existing knowledge, that changes in conditions within the next financial year could require a material adjustment to the carrying amount of the asset or

liability affected. In all cases, the entity discloses the nature and carrying amount of the asset or liability affected.

132+1E Some key assumptions referred to in paragraph 132+1 are disclosed under other Standards. For example, IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets*, requires disclosure, in certain circumstances, of major assumptions concerning future events affecting classes of provisions. In addition, IPSAS 15 *Financial Instruments: Disclosure and Presentation* requires disclosure of significant assumptions applied in estimating fair values of financial assets and financial liabilities that are carried at fair value.

IAS 2, Inventories
Equivalent PSC Pronouncements: IPSAS 12 Inventories

QUESTION 1

Do you agree with eliminating the allowed alternative of using the last-in first-out (LIFO) method for determining the cost of inventories under paragraphs 23 and 24 of IAS 2? (*No equivalent IPSAS para.*)

IASB Decision to date: Agreed to eliminate the LIFO option to determine the cost of inventories.

PSC Submission: Agreed with the removal of the LIFO method.

Effect on IPSAS: No effect. IPSAS 12 does not permit entities to adopt the LIFO method.

QUESTION 2

IAS 2 requires reversal of write-downs of inventories when the circumstances that previously caused inventories to be written down below cost no longer exist (paragraph 30). IAS 2 also requires the amount of any reversal of any write-down of inventories to be recognised in profit or loss (paragraph 31). Do you agree with retaining those requirements?

IASB Decision to date: Agreed to retain this requirement. Additionally, IASB agreed to exclude from the scope inventories of brokers/traders dealing with commodities and to require such inventory be measured at fair value with changes taken to the income statement.

PSC Submission: Agreed to the proposal.

Effect on IPSAS: (Paragraphs 35 and 37 are in substance identical to IAS 2, paragraphs 30 and 31.) Add new disclosure requirement in IPSAS 12 para 40

Disclosure

40. The financial statements ~~should~~ shall disclose:

- (f) the amount of any write-down of inventories recognized in accordance with paragraph 37.

Other Major paragraph changes to IPSAS 12 as a result of the Improvement Project

Topic	IPSAS Para No
Scope	
– To exclude inventories of brokers/traders dealing with commodities and require such inventories be measured at fair value and the changes in fair value be reflected in the income statement	Amend para 1(c)
Measurement of Inventories	
– Impact of deletion of alternative treatment in para 21 of IAS 21 (please refer to IAS 21 Q4 for more information)	Delete para 15

IAS 8, *Net Profit or Loss for the Period, Fundamental Errors and Changes in the Accounting Policies*
Equivalent PSC Pronouncements: IPSAS 3 *Net Surplus or Deficit for the Period, Fundamental Errors and Changes in Accounting Policies*

Note:

1. The proposed new name of the IAS 8 is Accounting Policies, Changes in Accounting Estimates and Errors.
2. The revised IAS has been substantially restructured from the previous format – it was provided as a clean copy. Where possible, Staff have provided a mark-up version of the impact on IPSAS 3, otherwise, Staff have provided an explanation on the impact of changes on the Standard.

QUESTION 1

Do you agree that the allowed alternative treatment should be eliminated for voluntary changes in accounting policies and corrections of errors, meaning that those changes and corrections should be accounted for retrospectively as if the new accounting policy had always been in use or the error had never occurred (see paragraphs 20, 21, 32 and 33)?

Proposed paragraphs 20, 21, 32 and 33 (there are no equivalent IPSASs paragraphs as these are new paragraphs introduced by the IASB.)

Voluntary Changes in Accounting Policies

20. *A change in an accounting policy other than a change made under paragraph 12 shall be applied retrospectively. Subject to paragraph 21, the opening balance of retained earnings for the earliest prior period presented and the other comparative amounts disclosed for each prior period presented shall be adjusted, where applicable, as if the new accounting policy had always been in use.*
21. *Comparative information presented for a particular prior period need not be restated if restating the information would require undue cost or effort. When comparative information for a particular prior period is not restated, the new accounting policy shall be applied to the balances of assets and liabilities as at the beginning of the next period and a corresponding adjustment shall be made to the opening balance of retained earnings for the next period.*

Errors

32. *The amount of the correction of an error shall be accounted for retrospectively. Subject to paragraph 33, an error shall be corrected by:*
 - (a) *either restating the comparative amounts for the prior period(s) in which the error occurred,*
 - (b) *or when the error occurred before the earliest prior period presented, restating the opening balance of retained earnings for that period so that the financial statements are presented as if the error had never occurred.*
33. *Comparative information presented for a particular prior period need not be restated if restating the information would require undue cost or effort. When comparative information for a particular prior period is not restated, the opening balance of retained earnings for the next period shall be restated for the cumulative effect of the error before the beginning of that period.*

IASB Decision to date: Confirmed the elimination of the allowed alternative treatment for voluntary changes in accounting policies and correction of errors.

PSC Submission: Agreed with the proposal.

Effect on IPSAS: IPSAS 3, para 45 – 47, 65 – 68

- a) IPSAS 3 paragraphs 45 – 47 currently allow the alternative treatment for correction of errors and all changes in accounting policies, which includes voluntary changes in accounting policies. Consequently, new requirements based on proposed paras 20, 21, 32, 33 of IAS 8, will have to be added that voluntary changes in accounting policies shall be applied retrospectively. Note, these requirements have not been provided in mark-up.
- b) The ED on IAS 8 also does not allow the allowed alternative treatment when changing accounting policies. Therefore, paragraphs 65 – 68 will have to be eliminated.

Fundamental Errors

Allowed Alternative Treatment

- ~~45. The amount of the correction of a fundamental error should be included in the determination of net surplus or deficit for the current period. Comparative information should be presented as reported in the financial statements of the prior period. Additional pro forma information, prepared in accordance with paragraph 41, should be presented unless it is impracticable to do so.~~
- ~~46. The correction of the fundamental error is included in the determination of the net surplus or deficit for the current period. However, additional information is presented, often as separate columns, to show the net surplus or deficit of the current period and any prior periods presented as if the fundamental error had been corrected in the period when it was made. It may be necessary to apply this accounting treatment in countries where the financial statements are required to include comparative information which agrees with the financial statements presented in prior periods.~~
- ~~47. An entity should disclose the following:~~
 - ~~(a) the nature of the fundamental error;~~
 - ~~(b) the amount of the correction included in each period for which pro forma information is presented and the amount of the correction relating to periods prior to those included in the pro forma information. If it is impracticable to present pro forma information, this fact should be disclosed; and~~
 - ~~(c) the amount of any correction recognized in net surplus or deficit for the current period.~~

Changes in Accounting Policies

Other Changes in Accounting Policies—Allowed Alternative Treatment

- ~~65. A change in accounting policy should be applied retrospectively unless the amount of any resulting adjustment that relates to prior periods is not reasonably determinable. Any resulting adjustment should be included in the determination of the net surplus or deficit for the current period. Comparative information should be presented as reported in the financial statements of the prior period. Additional pro forma comparative information, prepared in accordance with paragraph 60, should be presented unless it is impracticable to do so.~~
- ~~66. Adjustments resulting from a change in accounting policy are included in the determination of the net surplus or deficit for the period. However, additional comparative information is presented, often as separate columns, in order to show the net surplus or deficit and the financial position of the current period and any prior periods presented as if the new accounting policy had always been applied. It may be necessary to apply this accounting~~

~~treatment in countries where the financial statements are required to include comparative information which agrees with the financial statements presented in prior periods.~~

~~67. The change in accounting policy should be applied prospectively when the amount to be included in net surplus or deficit for the current period required by paragraph 65 cannot be reasonably determined.~~

~~68. When a change in accounting policy has a material effect on the current period or any prior period presented, or may have a material effect in subsequent periods, an entity should disclose the following:~~

~~(a) the reasons for the change;~~

~~(b) the amount of the adjustment recognized in net surplus or deficit in the current period; and~~

~~(c) the amount of the adjustment included in each period for which pro forma information is presented and the amount of the adjustment relating to periods prior to those included in the financial statements. If it is impracticable to present pro forma information, this fact should be disclosed.~~

QUESTION 2

Do you agree with eliminating the distinction between fundamental errors and other material errors (see paragraphs 32 and 33)?

IASB Decision to date: Agreed to eliminate the distinction.

PSC Submission: Agreed with the proposal.

Effect on IPSAS: IPSAS 3 paragraph 6, 38-40

6. *The following terms are used in this Standard with the meanings specified:*

~~Fundamental errors are errors discovered in the current period that are of such significance that the financial statements of one or more prior periods can no longer be considered to have been reliable at the date of their issue.~~

Errors are omissions from, and other misstatements of, the entity's financial statements for one or more prior periods that are discovered in the current period and relate to reliable information that:

(a) was available when those prior period financial statements were prepared; and

(b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.

Fundamental Errors

~~38. Errors in the preparation of the financial statements of one or more prior periods may be discovered in the current period. Errors may occur as a result of mathematical mistakes, mistakes in applying accounting policies, misinterpretation of facts, fraud or oversights. The correction of these errors is normally included in the determination of net surplus or deficit for the current period.~~

~~39. On rare occasions, an error has such a significant effect on the financial statements of one or more prior periods that those financial statements can no longer be considered to have been reliable at the date of their issue. These errors are referred to as fundamental errors. An example of a fundamental error is the omission of a major class of revenue or expense from the financial statements. The correction of fundamental errors that relate to prior periods~~

~~requires the restatement of the comparative information or the presentation of additional pro forma information.~~

40. ~~The e~~Corrections of ~~fundamental~~ errors ~~can be~~ distinguished from changes in accounting estimates. Accounting estimates by their nature are approximations that may need revision as additional information becomes known. For example, the gain or loss recognized on the outcome of a contingency which previously could not be estimated reliably does not constitute the correction of a fundamental error.

Other Issues on IAS 8 Agreed by the IASB
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- (i) *Materiality*: IASB agreed to include additional guidance on materiality either in IAS 8 or IAS 1.
Effect on IPSAS: Not sure as yet.
- (ii) *Hierarchy of Sources*: IASB agreed to provide additional guidance on application in practice of hierarchy of sources to be considered in the absence of a specific IFRS.
Effect on IPSAS: IPSAS 1 para 42 (note the equivalent IAS para in IAS 1 was moved to IAS 8).

IAS 10, *Events After the Balance Sheet Date*
Equivalent PSC Pronouncements: IPSAS 14 *Events After the Reporting Date*

Note: No Invitation to Comment on this IAS. But IAS 10 has been revised to amend paragraphs 11 and 12 of the Standard.

Dividends declared After Balance Sheet Date

Issue: To revise paragraphs 11 and 12 to indicate that if dividends are declared after the balance sheet date, an entity should not recognize those dividends as a liability at the balance sheet date, and the entity should disclose those dividends in the notes to the financial statements.

IASB Decision to date: Agreed with the proposal as a liability only when they meet the present obligations criteria in IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*. Dividends are not constructive obligations.

PSC Submission: Agreed with proposal.

Effect on IPSAS: IPSAS 14 paragraphs 13, 15

13. *If dividends or similar distributions are ~~proposed or~~ declared after the reporting date, an entity ~~shall~~ould not recognize those distributions as a liability at the reporting date.*

15. *~~If International Public Sector Accounting Standard IPSAS 1 Presentation of Financial Statements requires an entity to disclose the amount of~~ dividends or distributions to owners ~~are that were proposed or~~ declared after the reporting date but before the financial statements were ~~authorized for issue~~approved, the dividends are not recognized as a liability in the period covered by the financial statements because they do not meet the criteria of a present obligation in IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets*. Such dividends or similar distributions are disclosed in the notes to the financial statements in accordance with IPSAS 1 *Presentation of Financial Statements*. ~~Dividends and similar distributions do not include a return of capital. IPSAS 1 permits an entity to make this disclosure either:~~*
 - ~~(a) on the face of the statement of financial position as a separate component of net assets/equity; or~~*
 - ~~(b) in the notes to the financial statements.~~*

IAS 15, *Information Reflecting the Effects of Changing Prices*
There is no Equivalent PSC Pronouncement

IASB Decision to date: Confirmed withdrawal of the Standard.

Effect on IPSAS: No effect

PSC Submission: Agreed to the withdrawal.

IAS 16, Property, Plant and Equipment
Equivalent PSC Pronouncements: IPSAS 17 Property, Plant and Equipment

QUESTION 1

Do you agree that all exchanges of items of property, plant and equipment should be measured at fair value, except when the fair value of neither of the assets exchanged can be determined reliably (see paragraphs 21 and 21A)?

IASB Decision to date: Agreed with the proposal.

PSC Submission: Majority agreed in principle with the proposals.

Effect on IPSAS: IPSAS 17: amend para 31, add new para 31A and delete para 32
Exchanges of Assets

31. An item of property, plant and equipment may be acquired in exchange or part exchange for ~~a dissimilar~~another item of property, plant and equipment or other asset. Except when paragraph 31A applies, the cost of such an item is measured at the fair value of the asset received, which is equivalent to the fair value of the asset given up adjusted by the amount of any cash or cash equivalents transferred. The fair value of the asset received is used to measure its cost if it is more clearly evident than the fair value of the asset given up.
- 31A The cost of an item of property, plant and equipment acquired in exchange for a similar asset is measured at the carrying amount of the asset given up when the fair value of neither of the assets exchanged can be determined reliably. The entity will be unable to determine reliably the fair value of an item of property, plant and equipment when comparable market transactions are infrequent and alternative estimates of fair value (for example, based on discounted cash flow projections) cannot be calculated.
- ~~32. An item of property, plant and equipment may be acquired in exchange for a similar asset that has a similar use in the same line of business and which has a similar fair value. An item of property, plant and equipment may also be sold in exchange for an equity interest in a similar asset. In both cases, no gain or loss is recognized on the transaction. Instead, the cost of the new asset is the carrying amount of the asset given up. However, the fair value of the asset received may provide evidence of an impairment in the asset given up. Under these circumstances the asset given up is written down and this written down value assigned to the new asset. Examples of exchanges of similar assets include the exchange of buildings and other real estate, machinery, specialized equipment, and aircraft. If other assets such as cash are included as part of the exchange transaction this may indicate that the items exchanged do not have a similar value.~~

QUESTION 2

Do you agree that all exchanges of intangible assets should be measured at fair value, except when the fair value of neither of the assets exchanged can be determined reliably? (See the amendments in paragraphs 34-34B of IAS 38, Intangible Assets, proposed as a consequence of the proposal described in Question 1.)

IASB Decision to date: Agreed with the proposal.

PSC Submission: Agreed in principle with the proposal.

Effect on IPSASs: No impact. PSC does not have a Standard on intangible assets.

QUESTION 3

Do you agree that depreciation of an item of property, plant and equipment should not cease when it becomes temporarily idle or is retired from active use and held for disposal (see paragraph 59)? (Equivalent IPSAS para 72)

IASB Decision to date: Agreed with the proposal. IASB also noted that the continuing depreciation of items of property, plant and equipment held for disposal would be addressed separately in the Convergence project.

PSC Submission:

- Concerned that the proposal may not be entirely consistent with the depreciation requirements in paragraphs 41 – 52A of the ED, especially where the temporary idle period was intended and built into the estimate of the useful life;
- disagreed that consideration should be given to the appropriate depreciation in the aforementioned circumstance (in PSC Submissions 1st dot point) and do not support the change to the existing wording in paragraph 59; and
- agreed that assets that are in the abovementioned circumstances should be tested for impairment annually.

Effect on IPSAS (if IASB Decision is followed): IPSAS 17 paragraph 72

72. Depreciation of an item of Pproperty, plant and equipment ~~which does not cease when it becomes temporarily idle or~~ is retired from active use and held for disposal ~~is carried at its carrying amount at the date when the asset is retired from active use, unless the asset's depreciable amount has been allocated fully.~~ At least at each reporting date, an entity tests ~~the~~ such an asset for impairment under the relevant international or national accounting standard adopted in relation to impairment of assets and recognizes any impairment loss accordingly.

Other Issues on IAS 16 Discussed by the IASB

Residual value at each balance sheet date: IASB agreed to include guidance on depreciating an item of PPE when the review of residual value at the balance sheet date would result in an amount exceeding depreciated cost.

Effect on IPSAS: Affects depreciation section (paras 54-61)

Contributions and non-reciprocal transfers of assets: IASB agreed that the treatment of donated assets will be addressed within its Convergence project together with the revision of IAS 20, *Accounting for Government Grants and Disclosure of Government Assistance*. (Currently, the IASB anticipates to issue an ED on the revised Standard in 4th Q 2003.)

Other Major paragraph changes to IPSAS 16 as a result of the Improvement Project

IPSAS 17: Note nearly every paragraph in the existing IAS 16 has been marked-up.

Topic	IPSAS Para No
Scope	– Update para 4
Initial Measurement of PPE:	– Update para 28
Components of Cost:	– Add new paras 30+1A (IASB has agreed to amend the wording in this paragraph)
– Note that administration and general overhead costs are excluded from the cost of a PPE	
– Add new section on costs to dismantle and remove asset and restore its site	

Topic	IPSAS Para No
(New Section) Replacing and Renewing a Component – Provide new guidance on the components approach and to include guidance from the current SIC 23 <i>PPE – Major Inspection or Overhaul Costs</i>	– Move para 37 forward – add new guidance from the SIC mentioned (Para 32A – 32D).
Depreciation – Provide additional guidance on when management should start depreciating PPE	– Amend para 65

IAS 17, *Leases*
Equivalent PSC Pronouncements: IPSAS 13 *Leases*

QUESTION 1

Do you agree that when classifying a lease of land and buildings, the lease should be split into two elements – a lease of land and a lease of buildings? The land element is generally classified as an operating lease under paragraph 11 of IAS 17, *Leases* and the buildings element is classified as an operating or finance lease by applying the conditions in paragraphs 3-10 of IAS 17.

Paragraphs 3-10 of IAS 17 (*equivalent paragraphs 7-16 of IPSAS 13*) have not been changed. These paragraphs provide guidance and requirements on the definition and the classification of leases into finance or operating leases.

IASB Decision to date: Agreed with the proposal.

PSC Submission: Agree with the proposal.

Effect on IPSAS: IPSAS 17, add paragraphs 16A, 16B, 16C

Classification of Leases

16. Leases of land and buildings are classified as operating or finance leases in the same way as leases of other assets. However, a characteristic of land is that it normally has an indefinite economic life and, if title is not expected to pass to the lessee by the end of the lease term, the lessee does not receive substantially all of the risks and rewards incident to ownership. A premium paid for such a leasehold represents pre-paid lease payments which are amortized over the lease term in accordance with the pattern of benefits provided.

16A. For a lease of both land and buildings, the land and buildings elements are considered separately for the purposes of lease classification, unless title to both elements is expected to pass to the lessee by the end of the lease term. When the land has an indefinite economic life, the land element is classified as an operating lease unless title is expected to pass to the lessee by the end of the lease term, in accordance with paragraph 11 of this Standard. The buildings element is classified as a finance or operating lease in accordance with paragraphs 3-10 of this Standard.

16B. The minimum lease payments at the inception of a lease of land and buildings (including any up-front payments) are allocated between the land and the buildings elements in proportion to their relative fair values at the inception of the lease. If the lease payments cannot be allocated reliably between these two elements, the entire lease is classified as a finance lease, unless it is clear that both elements are operating leases (for the buildings elements, this may be the case for example when none of the situations in paragraphs 8 and 9 above exists), in which case the entire lease is classified as an operating lease.

16C. For a lease of land and buildings in which the value of the land element at the inception of the lease is immaterial, the land and buildings may be treated as a single unit for the purpose of lease classification and classified as a finance or operating lease in accordance with paragraphs 3-10 of this Standard. In such a case, the economic life of the buildings is regarded as the economic life of the entire leased asset.

QUESTION 2

Do you agree that when a lessor incurs initial direct costs in negotiating a lease, those costs should be capitalised and allocated over the lease term? Do you agree that only incremental costs that are directly attributable to the lease transaction should be capitalised in this way and that they should include those internal costs that are incremental and directly attributable?

IASB Decision to date: Agreed with the proposal.

PSC Submission: Agreed with the proposal.

Effect on IPSAS: IPSAS 13: add new definition (para 7), add new para 41A, delete para 45, amend para 47, 51 and 57

Definitions

7. Initial direct costs are incremental costs that are directly attributable to negotiating and arranging a lease, except for such costs incurred by manufacturer or dealer lessors.

Leases in the Financial Statements of Lessors

Finance Leases

41. Under a finance lease, substantially all the risks and rewards incident to legal ownership are transferred by the lessor, and thus the lease payment receivable is treated by the lessor as repayment of principal and finance revenue to reimburse and reward the lessor for its investment and services.
- 41A. Initial direct costs are often incurred by lessors in negotiating and arranging a lease. Such initial direct costs include amounts such as commissions, legal fees and internal costs that are incremental and directly attributable to negotiating and arranging the lease. For finance leases, these initial direct costs are included in the initial measurement of the finance lease receivable and reduce the amount of income recognized over the lease term.
- ~~45. Initial direct costs, such as commissions and legal fees, are often incurred by lessors in negotiating and arranging a lease. For finance leases, these initial direct costs are incurred to produce finance revenue and are either recognized immediately as an expense or allocated against revenue over the lease term.~~
46. *Manufacturer or trader lessors should recognize gains or losses on sale of assets in the statement of financial performance for the period, in accordance with the policy followed by the entity for outright sales.*
47. *If artificially low rates of interest are quoted, any gains or losses on sale of assets should be restricted to those which would apply if a commercial rate of interest were charged. Initial direct costs incurred by manufacturer or dealer lessors in connection with negotiating and arranging a lease should be recognized as an expense in the statement of financial performance at the inception of the lease.*
51. ~~Initial direct costs~~Costs incurred by a manufacturer or dealer lessor in connection with negotiating and arranging a lease are recognized as an expense at the commencement of the lease term because they are mainly related to earning the manufacturer's or trader's gain or loss on sale.
57. Initial direct costs incurred ~~specifically to earn revenues from an operating lease are either deferred and recognized as an expense over the lease term in proportion to the recognition of rent revenue, or recognized as an expense in the statement of financial performance in the period in which they are incurred by lessors in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognized as an expense over the lease term on the same basis as the lease income. Initial direct costs include commissions, legal fees and those internal costs that are incremental and directly attributable to negotiating and arranging the lease.~~

IAS 21, *The Effects of Changes in Foreign Exchange Rates*
Equivalent PSC Pronouncements: IPSAS 4 *The Effects of Changes in Foreign Exchange Rates*

Note:

1. PSC did not review the IAS ED 21 in detail, but agreed in principle with the proposed changes.
2. The revised IAS has been substantially restructured from the previous format – it was provided as a clean copy. Where possible, Staff have provided a mark-up version of the impact on IPSAS 4, otherwise, Staff have provided an explanation of the impact of changes on the Standard.

QUESTION 1

Do you agree with the proposed definition of function currency as “the currency of the primary economic environment in which the entity operates” and the guidance proposed in paragraphs 7 – 12 on how to determine what is an entity’s functional currency? (*No equivalent IPSAS para as these paragraphs are new.*)

Proposed Paragraphs 7 – 12 and proposed definition from paragraph 6

IASB has replaced the notion of ‘reporting currency’ in IAS 21 with two notions: functional currency and presentation currency. Definition of reporting currency currently used in existing IAS 21 and IPSAS 4 is the currency used in presenting the financial statements.

Definitions

6. *The following terms are used in this Standard with the meanings specified:*
Functional currency is the currency of the primary economic environment in which the entity operates.
Presentation currency is the currency in which the financial statements are presented.

Elaboration on the Definitions

Functional Currency

7. The primary economic environment in which an entity operates is normally the one in which it primarily generates and expends cash. An entity considers the following factors in determining its functional currency:
 - (a) the currency:
 - (i) in which sales prices for its goods and services are denominated and settled (or the currency that mainly influences sales prices, when that is different)
 - (ii) of the country whose competitive forces and regulations mainly determine the sales price of its goods and services.
 - (b) the currency in which labour, material and other costs of providing goods or services are denominated and settled (or the currency that mainly influences such costs, when that is different).
8. The following factors may also provide evidence of an entity’s functional currency:
 - (a) the currency in which funds from financing activities (ie issuing debt and equity instruments) are generated.
 - (b) the currency in which receipts from operating activities are usually retained.
9. When the entity is a foreign operation, the following additional factors are considered in determining the entity’s functional currency, and in particular whether its functional currency is the same as that of the reporting entity (the reporting entity being the entity that has the foreign operation as its subsidiary, branch, associate or joint venture):

- (a) whether the activities of the foreign operation are carried out as an extension of the reporting entity, rather than being carried out with a significant degree of autonomy. An example of the former is when the foreign operation only sells goods imported from the reporting entity and remits the proceeds to it. An example of the latter is when the operation accumulates cash and other monetary items, incurs expenses, generates income and arranges borrowings, all substantially in its local currency.
 - (b) whether transactions with the reporting entity are a high or low proportion of the foreign operation's activities.
 - (c) whether cash flows from the activities of the foreign operation directly affect the cash flows of the reporting entity and are readily available for remittance to it.
 - (d) whether cash flows from the activities of the foreign operation are sufficient to service existing and normally expected debt obligations without funds being made available by the reporting entity.
10. In cases when the above indicators are mixed and the functional currency is not obvious, management uses its judgement to determine the functional currency that most faithfully represents the economic effects of the underlying transactions, events and circumstances.
11. An entity's functional currency reflects the underlying transactions, events and circumstances that are relevant to it. Accordingly, once determined, the functional currency is not changed unless there is a change in those underlying transactions, events and circumstances.
12. If the functional currency is the currency of a hyperinflationary economy, the entity's financial statements are restated under IAS 29, Financial Reporting in Hyperinflationary Economies. An entity cannot avoid restatement under IAS 29 by, for example, adopting as its functional currency a currency other than the functional currency determined in accordance with this Standard (such as the functional currency of its parent).

IASB Decision to date:

- a) Revise drafting in para 7 to focus more directly on the importance of the primary economic environment in which the entity operates when determining an entity's functional currency.
- b) Clarify that para 7 is the leading paragraph and paras 8 and 9 provide additional guidance.

Effect on IPSAS: IPSAS 4:

- a) Add new definitions in para 9 (including functional currency); and
- b) provide further guidance on the definition on functional currency as per paragraphs 7-12 of the ED as quoted above.

QUESTION 2

Do you agree that a reporting entity (whether a group or a stand-alone entity) should be permitted to present its financial statements in any currency (or currencies) that it chooses?

IAS ED 21 paras 15-17 (*no equivalent IPSAS para as this is a new notion introduced by the IASB*) states that in preparing financial statements, an entity may either:

- (a) report in its functional currency. Foreign currency transactions will be translated into its functional currency;
- (b) choose its own presentation currency (please refer below for the definition of presentation currency) if it is a reporting entity that comprises of entities that use different functional currencies; or
- (c) choose its own presentation currency. If the presentation currency differs from the functional currency, the entity's results and financial position are translated into the presentation currency. (Para 52 requires the disclosure on

the reasons if an entity is using a different presentation currency from its functional currency.)

IASB Decision to date: Agreed with the proposal.

Effect on IPSAS:

- IPSAS 4 currently does not specify the type of currency in which an entity presents its financial statements. But, it notes that an entity would normally report in the currency of the country which it is domiciled (IPSAS 4 para 6).
- To harmonize with IAS ED 21, IPSAS 4 would note that the presentation currency could include the functional currency.

QUESTION 3

Do you agree that all entities should translate their financial statement into the presentation currency (or currencies) using the same method as is required for translating a foreign operation for inclusion in the reporting entity's financial statements (see paragraphs 37 & 40)? *(No equivalent IPSAS paras as these are new.)*

Proposed Paras 37 & 40

IASB proposed the removal of the distinction between integral foreign operations and foreign entities. This will result in:

- an entity that was previously classified as an integral foreign operation will have the same functional entity as the reporting entity; and
- only one translation method for foreign operations – that previously described in IAS 21 as applying to foreign entities. Therefore, the proposed paras 37 & 40 (as quoted below), are based on the existing paras 30 and 36 of IAS 21. *(Equivalent IPSAS paras 41 and 52).*

Use of a Presentation Currency other than the Functional Currency

Translation to the Presentation Currency

37. *The results and financial position of an entity whose functional currency is not the currency of a hyperinflationary economy shall be translated into a different presentation currency using the following procedures:*
- (a) *assets, liabilities and equity items other than those resulting from income and expenses recognised in the period, for each balance sheet presented (ie including comparatives) shall be translated at the closing rate at the date of that balance sheet;*
 - (b) *income and expenses recognised in the period, for each period presented (ie including comparatives) shall be translated at exchange rates at the dates of the transactions; and*
 - (c) *all resulting exchange differences shall be recognised as a separate component of equity.*
40. *The results and financial position of an entity whose functional currency is the currency of a hyperinflationary economy shall be translated into a different presentation currency using the following procedures:*
- (a) *all amounts (ie assets, liabilities, equity items, income items and expense items, including comparatives) shall be translated at the closing rate at the date of the most recent balance sheet, except that*
 - (b) *when amounts are being translated into the currency of a nonhyperinflationary economy, comparative amounts shall be those that were presented as current year*

amounts in the relevant prior year financial statements (ie not adjusted for either subsequent changes in the price level or subsequent changes in exchange rates).

IASB Decision to date: Agreed to the proposal, but noted that they will not specify the translation rate for equity items.

Effect on IPSAS:

- Delete any references which deal with the distinction of 'foreign operations that are integral to the entity' and 'foreign entities', namely paras 33-40 and 57-59; and
- Paras 41 to 54, which provide procedures and guidance to translating a foreign entity will have to be amended to reflect the new decisions made by IASB.

QUESTION 4

Do you agree that the allowed alternative to capitalize certain exchange differences in (existing) paragraph 21 of IAS 21 should be removed? (*Equivalent IPSAS para 31*)

Paragraph 21 of the existing IAS 21 is an alternative treatment for an entity when faced an exchange differences which affect its liabilities as a result of a severe devaluation or depreciation of currency against which there is no means of hedging.

IASB Decision to date: Agreed with the proposal.

Effect on IPSAS: Delete IPSAS 4 paras 30-32

Recognition of Exchange Differences

Allowed Alternative Treatment

~~30. The benchmark treatment for exchange differences dealt with in paragraph 31 is set out in paragraph 24.~~

~~31. Exchange differences may result from a severe devaluation or depreciation of a currency against which there is no practical means of hedging and that affects liabilities which cannot be settled and which arise directly on the recent acquisition of an asset invoiced in a foreign currency. Such exchange differences should be included in the carrying amount of the related asset.~~

~~32. Exchange differences are not included in the carrying amount of an asset when the entity is able to settle or hedge the foreign currency liability arising on the acquisition of the asset. However, exchange losses are part of the directly attributable costs of the asset when the liability cannot be settled and there is no practical means of hedging, for example when, as a result of exchange controls, there is a delay in obtaining foreign currency. Therefore, under the allowed alternative treatment, the cost of an asset invoiced in a foreign currency is regarded as the amount of reporting currency that the entity ultimately has to pay to settle its liabilities arising directly on the recent acquisition of the asset.~~

QUESTION 5

Do you agree that

- (a) goodwill and
- (b) fair value adjustments to assets and liabilities

that arise on the acquisition of a foreign operations should be treated as assets and liabilities of the foreign operation and translated at the closing rate (see paragraph 45)? *(No equivalent IPSAS para as IASB has updated the treatment of these items.)*

Background on Para 45

45. *Any 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 shall be treated as assets and liabilities of the foreign operation and shall be translated at the closing rate in accordance with paragraphs 37 and 40.*

(Note: Paras 37 and 40 were quoted in Question 3.)

Para 45 has been amended from the existing para 33 of IAS 21 (equivalent IPSAS para 46). Currently, para 33 notes that for goodwill and fair value adjustments to the carrying amounts of assets and liabilities arising from an acquisition of a foreign entity can be treated as either:

- a) as proposed in the new para 45 above; or
- b) assets and liabilities of the reporting entity which either are already expressed in the reporting currency or are non-monetary foreign currency items.

IASB Decision to date: Agreed with the proposal and to remove the option to treat these items as assets and liabilities of the acquirer/parent (option b of para 33).

Effect on IPSAS: IPSAS 4: Remove option (b) in para 46.

46. Any goodwill arising on the acquisition of a foreign ~~entity-operation~~ and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition of that foreign ~~entity-operation shall be~~ treated as ~~either:~~

- ~~(a) — assets and liabilities of the foreign entityoperation and translated at the closing rate in accordance with paragraph 41 (the reference to this paragraph will change as this paragraph will have to be updated to reflect the issues discussed in Question 3); or~~
- ~~(b) — assets and liabilities of the reporting entity which either are already expressed in the reporting currency or are non-monetary foreign currency items which are reported using the exchange rate at the date of the transaction in accordance with paragraph 20(b).~~

IAS 24, *Related Party Disclosures*
Equivalent PSC Pronouncements: IPSAS 20 *Related Party Disclosures*

IPSAS 20 is drafted substantially differently from the existing IAS 24. Consequently, it is not possible to identify specific paragraphs affected by the Improvements Project. Changes made may be pervasive and require that IAS 24 be reviewed in its entirety rather than go through the issues raised by the IASB.

QUESTION 1

Do you agree that the Standard should not require disclosure of management compensation, expense allowances and similar items paid in the ordinary course of an entity's operations (see paragraph 2)?

'Management' and 'compensation' would need to be defined, and measurement requirements for management compensation would need to be developed, if disclosure of these items were to be required. If commentators disagree with the Board's proposal, the Board would welcome suggestions on how to define 'management' and 'compensation'.

IASB Decision to date: Include in the revised Standard a requirement to disclose key management compensation. The Standard will include guidance to define 'compensation' of key management personnel.

PSC Submission: Majority disagreed with the proposal.

QUESTION 2

Do you agree that the Standard should not require disclosure of related party transactions and outstanding balances in the separate financial statements of a parent or a wholly-owned subsidiary that are made available or published with consolidated financial statements for the group to which that entity belongs (see paragraph 3)?

IASB Decision to date: Disagreed to the proposal above. There would be no exemptions to this requirement.

PSC Submission: Majority disagreed with the proposed amendment.

IAS 27, Consolidated Financial Statements and Accounting for Investments in Subsidiaries

Equivalent PSC Pronouncements: IPSAS 6 Consolidated Financial Statements and Accounting for Controlled Entities

Note: The proposed new name of the IAS 27 is Consolidated and Separate Financial Statements.

QUESTION 1

Do you agree that a parent need not prepare consolidated financial statements if all the criteria in paragraph 8 are met? (*IPSAS 6 para 16 is the equivalent para to the existing para 8 of IAS 27.*)

Paragraph 8:

A parent need not present consolidated financial statements to comply with International Financial Reporting Standards if and only if:

- (a) it is a wholly-owned subsidiary or the owners of the minority interests, including those not otherwise entitled to vote, unanimously agree that the parent need not present consolidated financial statements;
- (b) its securities are not publicly traded
- (c) it is not in the process of issuing securities in public securities market; and
- (d) the immediate or ultimate parent publishes consolidated financial statements that comply with International Financial Reporting Standards.

Such a parent shall prepare financial statements in accordance with the requirements in paragraph 29, 30, and 33 of this Standard for separate financial statements.]

IASB Decision to date: Agreed with the proposal and:

- agreed to add the exemption to intermediate parent of any of the exempted entities listed above that prepare consolidated financial statements. Such exempted parents would account their investments in associates using the equity method;
- considered the practical difficulties of obtaining agreement with minority shareholders for non-consolidation. IASB agreed that the exemption be made available to a parent that has informed minority shareholders and these shareholders have not objected to the non-consolidation of financial statements; and
- agreed to clarify the wording in para 8(b) and 8(c).

PSC Submission: Agreed with the proposal.

Effect on IPSAS: IPSAS 6

- a) Amend para 16 to the harmonize with the proposed para 8 of the revised IAS
- b) Amend paras 17, 22, 53, 57
- c) Delete paras 18-20, 23
- d) Add para 22A, 53A, 58

Scope

3. ~~Consolidated financial statements are encompassed by the term "financial statements" included in the Preface to International Public Sector Accounting Standards. Therefore, consolidated financial statements are prepared in accordance with International Public Sector Accounting Standards. Separate financial statements are financial statements prepared in addition to consolidated financial statements prepared in accordance with the requirements of this Standard, or in addition to financial statements prepared in accordance with the~~

requirements in IPSAS 7 *Accounting for Investments in Associates* or in IPSAS 8 *Financial Reporting of Interests in Joint Ventures*. Separate financial statements are also those financial statements described in paragraphs 16 and 17.

Presentation of Consolidated Financial Statements

16. *A parent need not present consolidated financial statements to comply with International Public Sector Accounting Standards if and only if:*

- (a) it is a wholly-owned controlling entity or the owners of the minority interests, including those not otherwise entitled to vote, unanimously agree that the parent need not present consolidated financial statements;*
- (b) its securities are not publicly traded;*
- (c) it is not in the process of issuing securities in public securities markets; and*
- (d) the immediate or ultimate parent publishes consolidated financial statements that comply with International Financial Reporting Standards.*

Such a parent shall prepare financial statements in accordance with the requirements in paragraphs 29, 30, and 33 of this Standard for separate financial statements.

~~*A controlling entity that is a wholly owned controlled entity, or is virtually wholly owned, need not present consolidated financial statements provided users of such financial statements are unlikely to exist or their information needs are met by the controlling entity's consolidated financial statements; or, in the case of one that is virtually wholly owned, the controlling entity obtains the approval of the owners of the minority interest. Such a controlling entity should disclose the reasons why consolidated financial statements have not been presented together with the bases on which controlled entities are accounted for in its separate financial statements. The name and the principal address of its controlling entity that publishes consolidated financial statements should also be disclosed.*~~

17. ~~Users of the financial statements of a controlling entity are usually concerned with, and need to be informed about, the financial affairs of the economic entity as a whole. This need may be served by consolidated financial statements, which present financial information about the economic entity as a single entity without regard for the legal boundaries of the separate legal entities. The financial statements of such a controlling entity as is described in paragraph 16, and prepared in accordance with paragraphs 53, 54 and 58, are the only financial statements prepared for the entity.~~

18. ~~A controlling entity that is itself wholly owned by another entity may not always present consolidated financial statements since such statements may not be required by its controlling entity and the needs of other users may be best served by the consolidated financial statements of its controlling entity. However, in the public sector many controlling entities that are either wholly owned or virtually wholly owned, represent key sectors or activities of a government and the purpose of this Standard is not to exempt such entities from preparing consolidated financial statements. In this situation the information needs of certain users may not be served by the consolidated financial statements at a whole-of-government level alone. In many jurisdictions governments have recognized this and have legislated the financial reporting requirements of such entities.~~

19. ~~In some countries, a controlling entity is also exempted from presenting consolidated financial statements if it is virtually wholly owned by another entity and the controlling entity obtains the approval of the owners of the minority interest. Virtually wholly owned is often taken to mean that the controlling entity owns 90% or more of the voting power.~~

20. ~~In some instances, an economic entity will include a number of intermediate controlling entities. For example, whilst a department of health may be the ultimate controlling entity, there may be intermediate controlling entities at the local or regional health authority level. Accountability and reporting requirements in each jurisdiction may specify which entities are required to (or exempted from the requirement to) prepare consolidated financial statements. Where there is no specific reporting requirement for an intermediate controlling entity to~~

Note: Para 16 (b) and (c) may be changed due to the recent IASB decision to provide clarification on their wording. IASB also agreed to add new exemption to intermediate parent of the exempted entities listed.

~~prepare consolidated financial statements for which users are likely to exist, intermediate controlling entities are to prepare and publish consolidated financial statements.~~

Scope of Consolidated Financial Statements

22. A controlled entity ~~should~~ shall be excluded from consolidation when:
- (a) ~~control is intended to be temporary because the controlled entity is acquired and held exclusively with a view to its subsequent disposal within twelve months from acquisition in the near future; or~~
 - (b) ~~it operates under severe external long-term restrictions which prevent the controlling entity from benefiting from its activities~~
23. ~~Such Investments in controlled entities should~~ shall be accounted for ~~as if they are investments in accordance with International Accounting Standard IAS 39, Financial Instruments: Recognition and Measurement, at fair value with changes in fair value included in the surplus and deficit of the period of the change provides guidance on accounting for investments.~~
- 22A. ~~A subsidiary is not excluded from consolidation simply because the controlled entity is a venture capital organization, mutual fund, unit trust or similar entity.~~

Accounting for Controlled Entities in a Controlling Entity's Separate Financial Statements

53. ~~In a controlling entity's~~ When separate financial statements are prepared, controlled entities, jointly controlled entities and associates that are consolidated, proportionately consolidated or accounted for under the equity method ~~included in the consolidated financial statements prepared in accordance with the requirements of this Standard or in financial statements prepared in accordance with the requirements of IPSAS 8 Financial Reporting of Interests in Joint Ventures, or in IPSAS 7 Accounting for Investments in Associates~~ should ~~shall~~ be accounted for either:
- (a) ~~accounted for using the equity method as described in IPSAS 7 or~~
 - (b) ~~accounted for as an investment~~ in the controlling entity's separate financial statements as described in paragraph 3 of this Standard. The same method shall be applied for each category of investments.
- 53A. ~~This Standard does not mandate which entities publish separate financial statements. Paragraphs 53, 54 and 58 apply when an entity prepares separate financial statements that purport to comply with International Public Sector Accounting Standards.~~
54. ~~Controlled entities, jointly controlled entities and associates that are excluded from accounted for in accordance with IAS 39 in the consolidated financial statements ion should~~ shall be accounted for in the same way in the investor's separate financial statements and in the financial statements of a parent that need not present consolidated as investments in the controlling entity's separate financial statements.

Disclosure

57. ~~In addition to those disclosures required by paragraph 16, the following disclosures should~~ shall be made in consolidated financial statements:
- (a) ~~in consolidated financial statements, a list of significant controlled entities including the name, the jurisdiction in which it operates (when it is different from that of the controlling entity), proportion of ownership interest and, where that interest is in the form of shares, the proportion of voting power held (only where this is different from the proportionate ownership interest);~~
 - (b) ~~in consolidated financial statements, where applicable:~~

- ~~(ia) the fact that a controlled entity is not consolidated, in accordance with paragraph 22 of this Standard, because control is temporary; the reasons for not consolidating a controlled entity;~~
 - ~~(iib) summarized financial information of controlled entities that are not consolidated, either individually or in groups, including the amounts of total assets, total liabilities, revenues and profit or loss~~
 - ~~(ic) the name of any controlled entity in which the controlling entity holds an ownership interest and/or voting rights of 50%, together with an explanation of how control exists;~~
 - ~~(iicd) the name of for a controlled entity or investee of any entity in which an ownership interest or potential ownership interest of more than 50% is held but which is not a controlled entity, together with an explanation of the reasons why the ownership does not constitute control does not exist; and~~
 - ~~(iv) the effect of the acquisition and disposal of controlled entities on the financial position at the reporting date, the results for the reporting period and on the corresponding amounts for the preceding period; and~~
 - ~~(e) the reporting date of the financial statements of a controlled entity when such financial statements are used to prepare consolidated financial statements and are as of a reporting date or for a period that is different from that of the controlled entity, and the reason for using a different reporting date or different period; and~~
 - ~~(f) the nature and extent of any restrictions on the ability of subsidiaries to transfer funds to the controlled entity in the form of cash dividends, repayment of loans or advances (ie borrowing arrangements, regulatory restraints etc).~~
 - ~~(e) in the controlling entity's separate financial statements, a description of the method used to account for controlled entities.~~
58. The following disclosures shall be made in the investor's separate financial statements and in the financial statements of a parent that need not present consolidated financial statements:
- (a) the reasons why separate financial statements are prepared;
 - (b) the name of the immediate or ultimate parent and a reference to the consolidated financial statements and or the financial statements in which associates and jointly controlled entities are accounted for under the equity method or proportionate consolidation method in accordance with IPSAS 7 and IPSAS 8; and
 - (c) a description of the method used to account for investments in subsidiaries, associates and jointly controlled entities.

QUESTION 2

Do you agree that minority interests should be presented in the consolidated balance sheet within equity, separately from the parent shareholders' equity (see paragraph 26)?

(The equivalent para in IPSAS 6 is para 50.)

IASB Decision to date: Agreed with the above proposal.

PSC Submission: Agreed with the proposal.

Effect on IPSAS: IPSAS 6 para 50

Consolidation Procedures

50. Minority interests ~~should~~ shall be presented in the consolidated statement of financial position within equity, separately from ~~liabilities and the controlling entity's net~~

*assets/equity. Minority interests in the net surplus or deficit of the economic entity **should** shall also be separately presented.*

QUESTION 3

Do you agree that investments in subsidiaries, jointly controlled entities and associates that are consolidated, proportionately consolidated or accounted for under the equity method in the consolidated financial statements should be either carried at cost or accounted for in accordance with IAS 39, Financial Instruments: Recognition and Measurement, in the investor's separate financial statements (paragraph 29)? (*Equivalent IPSAS para 53*)

Do you agree that if investments in subsidiaries, jointly controlled entities and associates that are accounted for in accordance with IAS 39 in the consolidated financial statements, then such investments should be accounted for in the same way in the investor's separate financial statements (paragraph 30)? (*Equivalent IPSAS para – None*)

IASB Decision to date: Agreed with the proposals.

PSC Submission: Majority agreed to the proposals.

Effect on IPSAS: IPSAS 6: Amend para 53 and add para 53A (please refer to Question 1 for marked-up version)

Other Issues on IAS 27 Discussed by the IASB

(i) *Exemption from consolidation based on temporary control:*

IASB agreed to include a requirement that management should actively seek a buyer for subsidiaries that are held for temporary control. If the reporting entity did not dispose the subsidiary within 12 months, the subsidiary should be consolidated as of the date of acquisition under the Business Combination Standard with restatement of appropriate prior periods. The 12 months presumptive could be rebutted when relevant regulatory approvals have not been received or they have granted a longer timeframe to dispose the subsidiary.

Effect on IPSAS: Affects Scope commentary (IPSAS 6 Paras 21-25).

Other Major paragraph changes to IPSAS 6 as a result of the Improvement Project

IPSAS 6: Note nearly every paragraph in the existing IAS 27 has been marked-up.

Topic	IPSAS Para No
Scope	
– Investments in subsidiaries made by venture capital organizations or similar entities should be consolidated and noted that the principles of consolidation were based on the concept of 'control' rather than ownership	– New para 4A – Delete para 3, 4, 7
Scope of Consolidated Financial Statements	
– Include additional guidance on potential voting rights and allocation of ownership interest to assess whether an entity controls another entity	– Add possible para 38A

IAS 28, *Accounting for Investments in Associates*
Equivalent PSC Pronouncements: IPSAS 7 *Accounting for Investments in Associates*

QUESTION 1

Do you agree that IAS 28 and IAS 31, Financial Reporting of Interests in Joint Ventures, should not apply to investments that otherwise would be associates or joint ventures held by venture capital organisations, mutual funds, unit trusts and similar entities if these investments are measured at fair value in accordance with IAS 39, Financial Instruments: Recognition and Measurement, when such measurement is well-established practice in those industries (see paragraph 1)? (Equivalent IPSAS para 1)

IASB Decision to date: Agreed with the proposal.

PSC Submission: Agreed with the proposal.

Effect on IPSAS: IPSAS 7: Amend para 1

Scope

1. An entity which prepares and presents financial statements under the accrual basis of accounting ~~should~~ shall apply this Standard in accounting by an investor for investments in associates where the investment in the associate leads to the holding of an ownership interest in the form of a shareholding or other formal equity structure. However, it does not apply to investments in associates held by venture capital organizations, mutual funds, unit trust and similar entities that are measured at fair value in accordance with International Accounting Standard IAS 39, Financial Instruments: Recognition and Measurement, when such measurement is well-established practice in those industries. When such investments are measured at fair value, changes in fair value are included in profit and loss in the period of change.

QUESTION 2

Do you agree that the amount to be reduced to nil when an associate incurs losses should include not only investments in the equity of the associate but also other interests such as long-term receivables (paragraph 22)? (Equivalent IPSAS para 36)

IASB Decision to date:

- a) Agreed that receivables for which good collateral existed (e.g. secured loans) should not be included in the amount to be reduced to nil when an associate incurs losses.
- b) IASB clarified that:
 - i. the amount to be reduced to nil when an associate incurs losses should include only long term interests, which are in substance part of the net investment; and
 - ii. investor applies IAS 39 to determine whether any additional impairment losses is recognized with respect to the net investment and with respect to items that are not part of the net investment.

PSC Submission: Majority agreed with proposed amendments.

Effect on IPSAS: IPSAS 7: amend para 36, add paras 36A and 36B

36. If, ~~under the equity method,~~ an investor's share of deficits of an associate equals or exceeds ~~the carrying amount of an investment,~~ its interest in the associate, the investor ~~ordinarily~~ discontinues ~~recognizing including~~ its share of further losses. The interest in an associate is the carrying amount of the investment in the associate under the equity method plus items that, in substance, form part of the investor's investment in equity of the associate. For example, an item for which settlement is neither planned nor likely to occur in the foreseeable future is, in substance, an extension to, or deduction from, the entity's investment in equity. Such items may include preferred shares and long-term receivables or loans but do not include trade receivables or trade payables. The investment is reported at nil value. Additional losses are provided for to the extent that the investor has incurred obligations or made payments on behalf of the associate to satisfy obligations of the associate that the investor has guaranteed or otherwise committed. If the associate subsequently reports surpluses, the investor resumes including its share of those surpluses only after its share of surpluses equals the share of net deficits not recognized.
- 36A. Losses recognised under the equity method in excess of the investor's ordinary shares investment are applied to the other components of the investor's interest in an associate in the order of their seniority (ie priority in liquidation). The investor applies the requirements of IAS 39, Financial Instruments: Recognition and Measurement, to determine whether any additional impairment loss is recognised with respect to the other components of the investor's interest.
- 36B. After the investor's interest is reduced to nil, additional losses are provided for, and a liability is recognised, only to the extent that the investor has incurred obligations or made payments on behalf of the associate. If the associate subsequently reports profits, the investor resumes recognising its share of those profits only after its share of the profits equals the share of net losses not recognised.

IAS 33, *Earnings Per Share*
Equivalent PSC Pronouncements: Not relevant to the public sector

IAS 40, *Investment Property*
Equivalent PSC Pronouncements: IPSAS 16 *Investment Property*

QUESTION 1

Do you agree that the definition of investment property should be changed to permit the inclusion of a property interest held under an operating lease provided that:

- (a) the rest of the definition of investment property is met; and
- (b) the lessee uses the fair value model set out in IAS 40, paragraphs 27-49? (*Equivalent IPSAS paras 35-57*)

IASB Decision to date: Agreed the proposal.

PSC Submission: Agreed with the proposal.

Effect on IPSAS: IPSAS 16: amend para 6, delete para 17

Definitions

6. *The following terms are used in this Standard with the meanings specified:*

***Investment property** is property (land or a building – or part of a building – or both) held to earn rentals or for capital appreciation or both, rather than for:*

- (a) *use in the production or supply of goods or services or for administrative purposes; or*
- (b) *sale in the ordinary course of operations.*

A property interest that is held by a lessee under an operating lease may be classified as investment property if and only if, in addition to the above condition being met, the lessee uses the fair value model set out in paragraphs 35-57 of this Standard. A lessee that uses the cost model set out in this Standard shall not classify property held under an operating lease as investment property.

- ~~17. Under IPSAS 13, a lessee does not capitalize property held under an operating lease. Therefore, the lessee does not treat its interest in such property as investment property.~~

QUESTION 2

Do you agree that a lessee that classifies a property interest held under an operating lease as investment property should account for the lease as if it were a finance lease?

IASB Decision to date: Agreed the proposal.

PSC Submission: Agreed with the proposal.

Effect on IPSAS: IPSAS 16: delete para 17, add new para 34A

Definitions

- ~~17. Under IPSAS 13, a lessee does not capitalize property held under an operating lease. Therefore, the lessee does not treat its interest in such property as investment property.~~

Measurement Subsequent to Initial Recognition

- 34A. A lessee that classifies a property interest held under an operating lease as investment property shall account for that property interest as if it were subject to a finance lease by applying paragraphs 20-27 and 32 of IPSAS 13 Leases.*

QUESTION 3

Do you agree that the Board should not eliminate the choice between the cost model and the fair value model in the Improvements project, but should keep the matter under review with a view to reconsidering the option to use the cost model in due course?

IASB Decision to date: Noted that, in general, commentators agreed with this decision.

PSC Submission: Agreed with the proposal.

Effect on IPSAS: No change.



**INTERNATIONAL FEDERATION
OF ACCOUNTANTS**

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DATE: 20 JUNE 2003
MEMO TO: MEMBERS OF THE IFAC PUBLIC SECTOR COMMITTEE
FROM: AHMAD HAMIDI-RAVARI AND LI LI LIAN
SUBJECT: **FIRST-TIME ADOPTION OF IFRSs**

ACTION REQUIRED

The Committee is asked to:

- **determine** whether to action a project on the first-time adoption of IPSASs.

AGENDA MATERIAL:

	Pages
15B.2 Summary of IFRS 1, <i>First Time Adoption of International Financial Reporting Standards</i>	15.51-15.54
15B.3 IFRS 1, <i>First Time Adoption of International Financial Reporting Standards</i>	15.55-15.76

BACKGROUND

At the April 2003 meeting, the PSC agreed to consider whether it should develop guidance on first-time adoption of IPSASs to reflect the equivalent to that for first-time adoption of IFRSs.

IFRS 1 *First-time Adoption of International Financial Reporting Standards* was issued on 19 June 2003. It applies if an entity's first IFRS financial statements are for a period beginning on or after 1 January 2004. Agenda 15B.2 provides a summary of the provisions of the Standard.

As IFRS 1 was only recently published, Staff have not had the opportunity to undertake a detailed analysis of the Standard. However, a priori, there seems to be a case for the PSC to develop a similar Standard if for no other reason than constituents will want to know whether the principles underlying IFRS 1 also apply to the first-time adoption of IPSASs.

At the forthcoming meeting, Staff will provide the Committee with a verbal update on progress in reviewing IFRS 1 and on evolving views about the need to action a project for an IPSAS equivalent.

Ahmad Hamidi-Ravari
PROJECT MANAGER

Li Li Lian
ASSISTANT PROJECT MANAGER

IFRS 1: The First-time Adoption of International Financial Reporting Standards – A Summary

1. Background

- 1.1 IFRS 1, First-time Adoption of International Financial Reporting Standards was issued on 19 June 2003. It replaces SIC-8 *First-time Application of IASs as the Primary Basis of Accounting*. It applies if an entity's first IFRS financial statements are for a period beginning on or after 1 January 2004. Earlier application is encouraged.

2. Scope

- 2.1 IFRS 1 applies to an entity's first IFRS financial statements and each interim financial report for any part of the period covered by its first IFRS financial statements. The first IFRS financial statements are the first annual financial statements in which the entity adopts IFRSs by an "explicit and unreserved" statement of compliance with IFRSs.
- 2.2 The Standard does not apply to changes in accounting policies made by an entity that already applies IFRSs. These changes are the subject of requirements in IAS 8 *Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies* and specific transitional provisions of other IFRSs.

3. Recognition and Measurement

- 3.1 The first-time adopter needs to prepare an opening balance sheet at the date of transition to IFRSs. The date of transition is defined by IFRS 1 as the beginning of the earliest period for which it presents full comparative information under IFRSs in its first IFRS financial statement. Thus if the first IFRS financial statements are for the year ending 31 December 2005, the opening balance sheet will need to be prepared at 1 January of 2004.
- 3.2 The first-time adopter should comply with each IFRS that is effective at the reporting date for its first IFRS financial statements. The following briefly sets out steps to be taken in preparing the opening IFRS balance sheet:
- (i) Recognition of all assets and liabilities whose recognition is required by IFRSs. These include items never recognised under previous GAAP. For example, application of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* may result in the recognition of provisions such as those for restructuring costs, onerous contracts and decommissioning that have not been required under previous GAAP. Another example would be recognition of derivatives as required by IAS 39 *Financial Instruments: Recognition and Measurement*.

- (ii) Derecognition of all assets and liabilities that have been recognised under GAAP if the IFRSs do not permit recognition of those items. For example provisions may have been made under previous GAAP for future operating losses, major overhauls or other items whose recognition as liabilities is not warranted under IAS 37. Such provisions should be eliminated in the opening IFRS balance sheet. Another example would be the derecognition of expenditure that has been recognised as intangible assets under previous GAAP such as start up costs, pre-operating costs and research costs because IAS 38 *Intangible Assets* does not permit their recognition as intangible assets.
- (iii) Classification of all recognised assets and liabilities in accordance with IFRSs. Thus the entity may have to reclassify certain items in the opening IFRS balance sheet. For example, dividends declared or proposed after the balance sheet date cannot be recognised as a liability at the balance sheet date under IAS 10 *Events After the Balance Sheet Date*. They are reclassified as a component of retained earnings in the opening IFRS balance sheet.
- (iv) Application of IFRSs in measurement of all recognised assets and liabilities. Except for exceptions set out in paragraph 4.1 below, the first-time adopter would use the measurement principles in IFRSs effective at the reporting date for the first IFRS financial statements.

4. Optional Exemptions from Retrospective Application

- 4.1 The following sets out exemptions from the requirements of other IFRSs that a first-time adopter may use:

(a) business combinations:

A first-time adopter may elect not to apply IAS 22 *Business Combinations* to most aspects of business combinations that occurred before the date of transition to IFRSs. Appendix B to IFRS 1 contains the requirements that the entity should apply to business combinations that the entity recognised before the date of transition to IFRSs.

(b) fair value or revaluation as deemed cost

A first-time adopter may elect to treat the fair value of an item of property, plant and equipment (PPE) at the date of transition to IFRSs as its deemed cost at that date. It may also elect to use a previous GAAP revaluation of an item of property, plant and equipment at, or before, the date of transition to IFRSs as deemed cost at the date of the revaluation, if the revaluation was, at the date of the revaluation, broadly comparable to:

- (i) fair value; or
- (ii) cost or depreciated cost under IFRSs, adjusted to reflect, for example, changes in a general or specific price index.

The said elections can also be made in respect of investment property (if cost model in IAS 40 is applied) and intangibles that meet the restrictive criteria set out in the Standard.

Moreover, if a first-time adopter have established a deemed cost under previous GAAP for some or all of its assets and liabilities by measuring them at their fair value because of an event such as a privatization or initial public offering, it may elect to use those fair values as deemed cost for IFRSs.

(c) employee benefits

For a defined benefit plan, a first-time adopter may elect to recognise all cumulative actuarial gains and losses at the date of transition to IFRSs, even if it uses the corridor approach for later actuarial gains and losses. If a first-time adopter uses this exemption, it should apply it to all defined benefit plans.

(d) cumulative translation differences

A first-time adopter may elect not to identify existing cumulative translation differences as a separate component of equity. Under this exemption, the cumulative translation differences for all foreign operations are deemed to be zero at the date of transition to IFRSs and the gain or loss on a subsequent disposal of any foreign operation would only include translation differences that arose after the date of transition to IFRSs.

(e) compound financial instruments

Under IAS 32 *Financial Instruments: Disclosure and Presentation* an entity should split a compound financial instrument at inception into separate liability and equity components. If the liability component is no longer outstanding, retrospective application of IAS 32 involves 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. However, under IFRS 1, a first-time adopter need not separate these two portions if the liability component is no longer outstanding at the date of transition to IFRSs.

The Standard specifies how these exemptions operate if a parent become a first-time adopter earlier or later than its subsidiary or associate or joint venture.

5. Prohibition of Retrospective Application

- 5.1 The transitional provisions in other IFRSs do not, in general, apply to a first-time adopter. However, the Standard prohibits full retrospective application of IFRSs in the following cases:
- (i) A first-time adopter should not recognise financial assets or financial liabilities derecognised under previous GAAP in a financial year beginning before 1 January 2001 (effective date of IAS 39).
 - (ii) Based on the transitional provisions of IAS 39, a first-time adopter should apply that Standard prospectively for hedge accounting.
 - (iii) A first-time adopter treats the receipt of information received after the date of transition to IFRSs about estimates that it had made under previous GAAP, as a non-adjusting event under IAS 10 *Events After the Balance Sheet Date*. This provision does not apply to cases where the estimates need adjustment for any differences in accounting policies or where there is objective evidence that the estimates were in error.

6. Presentation and Disclosure

- 6.1 The Standard does not provide exemptions from the presentation and disclosure requirements in other IFRSs. Under IAS 1 *Presentation of Financial Statements*, an entity's first IFRS financial statements should include at least one year of comparative information under IFRSs. Any additional comparative information not complying with IFRSs must be prominently labeled and the nature of the main adjustments that would make that information comply with IFRSs should be disclosed. If an entity did not present financial statements for previous periods, its first IFRS financial statements should disclose that fact.
- 6.2 The Standard requires disclosures that explain how the transition from previous GAAP to IFRSs affected the reported financial position financial performance and cash flows of the entity. Specific disclosures are also required where fair values are used as deemed cost.

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