



# HM TREASURY

## Financial Reporting Advisory Board Paper

### INTERNATIONAL FINANCIAL REPORTING STANDARD (IFRS) 1 *FIRST TIME ADOPTION OF INTERNATIONAL FINANCIAL REPORTING STANDARDS*

<b>Issue:</b>	The implementation of IFRS 1, which deals with the first time adoption of IFRSs.
<b>Impact on guidance:</b>	The proposed text in Annex A relates to the IFRS-based FReM.
<b>IAS/IFRS adaptation?</b>	No
<b>IPSAS compliant?</b>	N/A
<b>Interpretation for the public sector context?</b>	Yes: it is proposed to allow the use of UK GAAP-based comparative figures in the first IFRS-based accounts.
<b>Impact on budgetary regime?</b>	The impact on the budgetary regime of individual IASs/IFRSs is considered in the papers dealing with those IASs/IFRSs
<b>Alignment with National Accounts</b>	Questions on the alignment with National Accounts of individual IASs/IFRSs are considered in the papers dealing with those IASs/IFRSs.
<b>Impact on Estimates?</b>	The impact on Estimates of individual IASs/IFRSs is considered in the papers dealing with those IASs/IFRSs
<b>Recommendation:</b>	The FRAB is invited to note the proposals in the paper, and to approve the implementation of IFRS 1.
<b>Timing:</b>	Not yet known: depends on future decision on date for moving to EU-adopted IFRS.

## DETAIL

### *Background*

1. IFRS 1 deals with the first time adoption of international accounting standards. It describes in some detail how the first IFRS-based financial statements are to be determined; the key feature is whether those statements contain an explicit and unreserved statement of compliance with IFRSs.

Accounts prepared in accordance with the FReM will thus need to include such a statement. In general, IFRS 1 requires an entity to comply with each IFRS effective at the reporting date for its first IFRS-based financial statements.

2. It will be necessary for the entity to prepare an opening balance sheet at the date of transition to IFRSs which will form the starting point for its accounting under IFRSs. This balance sheet need not be presented in the first IFRS-based financial statements. Thus, if a move to IFRS-based accounts is planned for (say) 2008-09, it will be necessary to prepare an IFRS-based balance sheet at 1 April 2008 that may differ from the UK GAAP-based balance sheet at 31 March 2008.

3. Subject to some limited exemptions in specified areas on cost/benefit grounds, the opening IFRS balance sheet will:

- Recognise all assets and liabilities whose recognition is required by IFRSs;
- Not recognise items as assets and liabilities if IFRSs do not permit such recognition;
- Reclassify items that were recognised under previous GAAP as one type of asset, liability or component of equity, but are a different type of asset, liability or component of equity under IFRSs; and
- Apply IFRSs in measuring all recognised assets and liabilities.

4. Where the adoption of IFRSs results in differences between the closing balance sheet and the opening balance sheet, those differences shall be recognised directly in retained earnings (eg the General Fund) at the date of transition to IFRSs.

5. However, the standard provides for two categories of exceptions to the principle that an entity's opening IFRS balance sheet shall comply with each IFRS:

- Exemptions from some requirements of other IFRSs;
- Prohibition of retrospective application of some requirements of other IFRSs.

6. This paper does not comment on all the examples quoted in the IFRS<sup>1</sup>, but the following are considered to be most relevant in a public sector context:

*(i) Fair value or revaluation as deemed cost*

7. The opening IFRS balance sheet should record property, plant and equipment at their fair values. However, it is possible to use a previous valuation if that revaluation was broadly comparable to (a) fair value or (b) cost or depreciated cost under IFRSs adjusted to reflect changes in a general or specific index.

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<sup>1</sup> The exemptions listed in IFRS 1 cover business combinations; fair value or revaluation as deemed costs; employee benefits; cumulative translation differences; compound financial instruments; assets and liabilities of subsidiaries, associates and joint ventures; designation of previously recognised financial instruments; share-based payment transactions; insurance contracts; decommissioning liabilities included in the cost of property, plant, and equipment; leases; and fair value measurement of financial assets or financial liabilities at initial recognition.

8. It is considered likely that the valuation methods adopted by central government entities will satisfy one or other of the above criteria and, on the face of it, there seems little need for a separate assessment of fair values on the adoption of IFRSs.

*(ii) Employee benefits*

9. IAS 19 *Employee Benefits* allows an entity to use the option of using a “corridor” approach in recognising actuarial gains and losses, and IFRS 1 provides guidance on the implications of the initial adoption of IAS 19. However, central government bodies are not permitted to use the corridor approach, and the dispensations allowed by IFRS 1 will not be relevant.

10. IFRS 1 requires the first set of IFRS-based accounts to include comparative figures for the balance sheet, income statement, cash flow statement and notes based on IFRSs. However, to avoid complications with reconciling these figures with those used in previous Estimates and accounts, the proposal is to allow the first IFRS-based accounts to include comparative figures from the previous UK-GAAP based accounts, unless there are material differences between figures determined on a UK-GAAP and IFRS basis.

***Impact on disclosures in resource and other accounts***

11. The impact on the disclosures in resource and other accounts is given in the papers relating to the relevant IFRS.

***IAS/IFRS compliance***

12. Other than the proposal to allow the use of UK GAAP based comparative figures in the opening IFRS-based accounts, the proposals are consistent with IFRS 1.

***IPSAS compliance***

13. There is no IPSAS on this subject.

***The IFRS-based Government Financial Reporting Manual***

14. See Annex A for the proposed amendments to IFRS-based FReM.

***Impact on the budgetary regime***

15. The impact of individual IASs/IFRSs is considered in the papers relating to those IASs/IFRSs.

***Summary and recommendation***

16. This paper considers the points made in IFRS1 *The First Time Adoption of International Accounting Standards*, and recommends that, subject to allowing the use of UK GAAP-based comparative figures in the opening IFRS-based accounts, it is adopted.

## **PROPOSED TEXT FOR THE IRFS-BASED GOVERNMENT FINANCIAL REPORTING MANUAL**

### **IFRS 1: FIRST TIME ADOPTION OF INTERNATIONAL REPORTING STANDARDS**

#### ***Applicability***

IFRS 1 applies, as interpreted.

#### ***Objective of IFRS 1***

The objective of IFRS 1 is to ensure that an entity's first IFRS financial statements, and its interim financial reports for part of the period covered by those financial statements, contain high quality information that:

- Is transparent for users and comparable over all periods presented;
- Provides a suitable starting point for accounting under International Financial Reporting Standards; and
- Can be generated at a cost that does not exceed the benefits to users.

#### ***Interpretations of IFRS 1 for the public sector context***

The following interpretation of IFRS 1 for the public sector context applies

#### ***Comparative figures***

Bodies to which this Manual applies may use UK GAAP-based comparative figures in their first IFRS-based accounts unless there are material differences between the figures determined on a UK GAAP basis and on an IFRS basis.