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A Digital Learning Platform for Generation Z:
Passport to IFRS®

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IFRS® Standard 1 First-Time Adoption of International Financial Reporting Standards

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CASE STUDY – IFRS 1 FIRST-TIME ADOPTION OF INTERNATIONAL FINANCIAL REPORTING STANDARDS

Introduction

Transition of the financial reporting from national accounting standards to IFRS standards is a complicated procedure, in which recognition and measurement of each article of assets and liabilities needs to be addressed. IFRS 1 Standard provides guidelines for entities adopting IFRS for the first time in order for the transition to be as smooth as possible, and for the result of it to comply with the requirements of users of financial statement information regarding its reliability and relevance.

Aim of this case study is to provide understanding of the essence of the requirements for entities once they decide to prepare their financial statements according to IFRS Standards. The case study addresses the following issues and clarifies the following:

- first, how to identify, when an entity should be treated as the first-time adopter of IFRS Standards;
- second, to get familiar with the requirements for application and for disclosure.

The Case Information

In year 20X9, entity A decided to start trading its shares at the stock exchange. It used to prepare its financial statements in accordance with the national accounting standards. In order to be able to join the stock exchange, it needs to start reporting in accordance with the IFRS Standards. Entity A took a decision to start applying IFRS Standards to its financial reporting starting year 20X9. Its reporting year coincides with the calendar year. Entity A used to comparative on a year-to-year information in its previous reporting.

Later, it is revealed that from year 20X1 to 20X4, entity A used to report in accordance with IFRS Standards and made an explicit and unreserved statement confirming this fact. In year 20X5, after the change of the shareholders, the decision was to return to reporting under the national accounting standards. In year 20X9, the shareholders of entity A decided to start reporting according IFRS Standards with the financial statements starting with 20X9.

It is known that other companies operating in the market apply different accounting standards. Entity B used to prepare financial reports according to the national standards. In year 20X9, it decided to start reporting in accordance with the IFRS Standards and declaring the compliance with the IFRS Standards. Entity C used to prepare financial statements according to IFRS Standards, but only for internal use without confirmation that they comply with the IFRS Standards. In year 20X9, it decided start declaring that its financial statements comply with the IFRS Standards. Entity D was just established in year 20X9 and is going to prepare its first financial statements ever. It had decided that these statements should be prepared according to IFRS Standards.

Discussion Questions

1. Please identify the date of transition to IFRS Standards, first reporting period as well as the comparative period and explain the importance of identification of all listed dates in the case of entity A.
2. Please identify which of entities (A, B, C, D) should be treated as the first-time adopters of IFRS Standards in 20x9. Explain why this identification is important.
3. The general rule is the retrospective application of the accounting in accordance with IFRS Standards in the opening statement of the financial position. However, there are some exceptions for application prospectively. Please discuss why retrospective application is better than prospective. What kind of exceptions there could be, and why they are important.
4. What specific requirements for disclosures are stated in IFRS 1 Standards and why are they important?

SOLUTION OF CASE STUDY – IFRS 1 FIRST-TIME ADOPTION OF INTERNATIONAL FINANCIAL REPORTING STANDARDS

1. IFRS 1 requires for the first time adopters to prepare the opening balance sheet at the date of transition. In this standard, **date of transition to IFRS Standards** refers to the first day of the earliest period for which the entity presents the full comparative information under the IFRS Standards in its first IFRS Standard financial reports. So, in the case of entity A, as it used reporting according to IFRS Standards for financial statements from 20X1 to 20x4 with an explicit and unreserved statement confirming this fact, the date of transition to IFRS Standards would be 01.01.20X0.

   The first IFRS reporting period is the first reporting period, for which the entity prepares the financial reports in accordance with IFRS Standards. Since entity A made the decision to start applying IFRS Standards to its financial reporting starting year 20X1 and its reporting year coincides with the calendar year, therefore, the first IFRS reporting period will be the financial reporting period for the calendar year 20X1.

   IFRS Standards do not require more than one year of comparative information and entity A also used to prepare comparative on a year-to-year information in its previous reporting. Since the first IFRS reporting period for entity A is year 20X1, the comparative period shall be year 20X0.

   All these dates are important for the further application of procedures established in IFRS 1. For example, the first-time adopter is required to recognize assets and liabilities with the provisions of IFRS and derecognize assets and liabilities that do not comply with IFRS in the opening balance sheet at the date of transition.

2. Entity A is not the first-time adopter of IFRS Standards in year 20X9 as it had reported previously according to the IFRS Standards. All other entities listed are first-time adopters of IFRS Standards because the entity is treated as the first-time adopter of IFRS Standards in cases when:

   - it's most recent financial reports have been prepared according to the national standards (this is the case of entity B);
   - it's most recent financial reports have been prepared according to the IFRS Standards, but without confirmation that they complied with the IFRS Standards (this is the case of entity C);
   - it has not prepared any financial statements at all (this is the case of entity D).

   The identification whether an entity is the first-time adopter of IFRS Standards is important as this determines if requirements of IFRS 1 Standard would be applied. The first-time adopter must comply with all IFRS Standards effective at the reporting date. However, specific transitional provisions of separate standards are not applied to a first-time adopter. Therefore, first-time adopter of IFRS Standards prepares its opening balance sheet in accordance to the provisions set in IFRS 1 Standard.

3. The retrospective application of the accounting in accordance with IFRS Standards allows presenting information of the previous reporting period, as if an entity has always presented its financial statements in accordance with IFRS. This allows users of the financial information compare the results and financial position of the entity with the previous reporting period. However, in some areas, it is difficult to make changes retrospectively. For example, measuring fair value of financial assets at their initial recognition. In addition, there could be situations when the costs of retrospective application would exceed the benefits to the users of the information of financial statements. Therefore, these areas are identified in IFRS 1 Standard with certain optional and mandatory exceptions to the general principle of retrospective application. These exceptions serve as guidelines for entities when identifying areas, in which retrospective application is obligatory. In addition, they provide the entities with the right to apply the optional exceptions only in part, fully or not at all, in cases when it is possible to calculate the effect of transitions to the IFRS reporting reliably.

4. In cases of most entities that are recognised as first-time adopters of IFRS Standards, new areas of disclosure will be added or broadened, as there might be differences between the requirements of IFRS and national accounting standards. However, besides the requirements for disclosures according to specific IFRS Standards requirements, when submitting its first financial statement according to IFRS Standards, a first-time adopter will have to explain how the transition from the national reporting standards to IFRS Standards affect its financial position, financial performance and cash flows.