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Endorsement of the IFRS 1 *First-time Adoption of International Financial Reporting Standards*

Introduction, background and conclusions

Attachment 1: Effect study prepared by the European Financial Reporting Advisory Group (EFRAG)

Attachment 2: Endorsement advice prepared by EFRAG

1. EFFECT STUDY

The European Commission has agreed with the European Parliament that Effect Studies should be prepared for new accounting standards and interpretations up for endorsement in the European Union (EU). The Commission Services together with the European Financial Reporting Advisory Group (EFRAG) prepare these studies containing description of the accounting issues involved, results from stakeholder consultations as well as analysis of effects of using the new accounting rules in the EU.

EFRAG has prepared an Effect Study for the Amendments to IFRS 1 *First-time Adoption of International Financial Reporting Standards* (attached). As the EFRAG Effect Study refers to the Endorsement Advice, we also included it in attachments.

This cover note contains background information, comments and a conclusion by the Commission Services.

2. BACKGROUND ON THE RESTRUCTURED IFRS 1

Explanation of the issue

IFRS 1 establishes the requirements for preparation of financial statements in accordance with International Financial Reporting Standards for the first time. The standard defines transition and how it occurs, provides guidance on how to make transition, sets out exemptions from the requirements of IFRSs on first time adoption, prescribes disclosure requirements.

Since it was first issued in 2003 it has been amended several times to accommodate first-time adoption requirements of new or amended IFRSs, and as a result the text has become increasingly complex to understand and difficult to amend.

The objective of the revision of IFRS 1 (Restructured IFRS 1) is to improve the structure of the current standard making it easier to understand and to amend in the future. It does not introduce changes to the accounting requirements for first time adopters of International Financial Reporting Standards.

The Restructured IFRS 1, which replaces the current standard, will not change the current requirements of IFRS 1. The difference between the two standards is that under the Restructured IFRS 1 some paragraph have been moved, some outdated paragraph have been omitted and there have been minor wording changes consequential to those changes.

How is the issue dealt with currently?

The IASB was concerned that IFRS 1 First Time Adoption of International Standards was becoming unwieldy. Since it was issued it had been amended several times to accommodate first-time adoption requirements resulting from new or amended standards. Because of the way IFRS 1 is structured, these amendments make the standard less clear and complex to understand. Furthermore, in the future, as more amendments become necessary, this problem will become worse.

How do the Restructured IFRS 1 suggest dealing with the issue?

The IFRS 1 has been streamlined by moving some paragraph from the main body of the standard, which then contain the core requirements, to appendices and grouping them as follows:

- (a) Appendix B includes exceptions to the retrospective application.
- (b) Appendix C includes exemptions for business combinations.
- (c) Appendix D includes exemptions from other IFRSs.

In addition, outdated transitional provisions have been omitted, such as those which made reference to long past effective dates and minor wording changes have been introduced. Some wording changes—such as changing paragraph references to appendices—were necessary consequential changes of the amendments already described.

Furthermore, some references to GAAP or IFRS were changed from ‘under’ to ‘in accordance with’ but the intention is that those changes, and indeed all the changes being made, should have no impact on what the standard requires.

IASB and EFRAG consultations

The IASB carried out a consultation according to its due process. The proposal to revise IFRS 1 was part of an ED including miscellaneous amendments to 25 International Financial Reporting Standards (IFRSs). The IASB received 75 comment letters. Respondents agreed with the proposal to restructure IFRS 1.

EFRAG consulted publicly on its endorsement advise. Commentators to the EFRAG consultation were supportive to the proposal to recommend endorsement of revised IFRS 1. EFRAG has also carried out an assessment of the likely costs and benefits of implementing the Restructured IFRS 1.

3. EFFECT ANALYSIS

Main points identified in the EFRAG Effect Analysis

EFRAG firstly considered whether the changes made to existing IFRS 1 would have any effect on the financial reporting requirements and it conclude that they will have no effect on the financial reporting requirements of the standard.

Accordingly, in EFRAG’s view a detailed evaluation of the revised standard is not necessary. Instead, bearing in mind that EFRAG assessed the original version of IFRS 1 when it was issued and carried out an assessment about each of the changes subsequently made to the standard, EFRAG believes it is appropriate to limit its technical assessment of the Restructured IFRS 1 to asking whether there is any evidence from the application of the existing standard to suggest that EFRAG’s assessment of the original standard and subsequent revisions needs to be revised. EFRAG conclude that there no evidence that would suggest EFRAG’s prior assessment needs to be revised.

Costs for preparers and users

Taking into account that the Restructured IFRS 1 involves no changes in the requirements, EFRAG carried out less extensive work in order to understand fully the cost and benefit implications of the Standard being assessed.

The analysis conclude that the Restructured IFRS 1 will have no cost implications for EU preparers and users and will have no impact on the quality of the financial information provided.

EFRAG notes that the Restructured IFRS 1 will result in net benefits for those jurisdictions still to transition to IFRS and also for the IASB. The Commission Services share this analysis.

4. OVERALL COST-BENEFIT CONSIDERATIONS AND COMMISSION SERVICES CONCLUSIONS

On the basis of EFRAG's Effect Study, the Commission Services have considered the main costs and benefits of endorsing the Restructured IFRS 1 and concluded that the benefits of adopting the amendments outweigh the costs incurred.

The Commission Services believe that the Restructured IFRS 1 will have positive cost-benefit effects and that it should therefore be endorsed in the EU without delay.

Attachment 1



The cost and benefits of implementing the revision to IFRS 1 *First-time Adoption of International Financial Reporting Standards*

Introduction

1. Following discussions between the various parties involved in the EU endorsement process, the European Commission decided in 2007 that more extensive information than hitherto needs to be gathered on the costs and benefits of all new or revised Standards and Interpretations as part of the endorsement process. It has further been agreed that EFRAG will gather that information in the case of the revision to IFRS 1 *First-time Adoption of International Financial Reporting Standards* (Restructured IFRS 1).
2. EFRAG first considered how extensive the work would need to be. For some Standards or Interpretations, it might be necessary to carry out some fairly extensive work in order to understand fully the cost and benefit implications of the Standard or Interpretation being assessed. However, in the case of the Restructured IFRS 1, EFRAG's view is that the cost and benefit implications can be assessed by carrying out a more modest amount of work. (The results of the consultations EFRAG has carried out seem to confirm this). Therefore, as explained more fully in the main sections of the report, the approach EFRAG has adopted has been to carry out an initial assessment of the likely costs and benefits of implementing the revision in the EU, to consult on the results of that initial assessment, and to finalise the assessment in the light of the comments received.

EFRAG's endorsement advice

3. EFRAG also carries out a technical assessment of all new and revised Standards and Interpretations issued by the IASB and IFRIC against the so-called endorsement criteria and provides the results of those technical assessments to the European Commission in the form of recommendations as to whether or not the Standard or Interpretation assessed should be endorsed for use in the EU. As part of those technical assessments, EFRAG gives consideration to the costs and benefits that would arise from implementing the new or revised Standard or Interpretation in the EU. EFRAG has therefore taken the conclusion at the end of this report into account in finalising its endorsement advice.

A summary of the revision to IFRS 1

4. IFRS 1 provides guidance on the initial adoption of IFRS and provides a limited number of exemptions and exceptions as a practical solution for certain implementation issues. Since IFRS 1 was first issued in 2003 it has been amended several times to accommodate first-time adoption requirements of new or amended IFRSs, making the standard more complex than necessary and difficult to amend further.

5. The objective in replacing the existing IFRS 1 with the Restructured IFRS 1 is to make IFRS 1 easier to use and amend in the future. The intention is that the requirements should not change.
6. The main difference between the standards is that the existing standard has been restructured. This has been done by moving some paragraphs from the main body of the standard to appendices and grouping them as follows:
 - (a) Appendix B includes exceptions to the retrospective application.
 - (b) Appendix C includes exemptions for business combinations.
 - (c) Appendix D includes exemptions from other IFRSs.
7. In addition, outdated transitional provisions have been omitted. These provisions are those (such as now omitted paragraph 47E) which made reference to long past effective dates:

47E An entity shall apply amendments in paragraph 13(l) and 25G for annual periods beginning on or after 1 January 2005. If an entity applies the amendments to IAS 39 Financial Instruments: Recognition and Measurement—Transitional and Initial Recognition of Financial Assets and Financial Liabilities for an earlier period, these amendments shall be applied for that earlier period.
8. There have also been some minor wording changes. Some wording changes—such as changing paragraph references to appendices—were necessary consequential changes of the amendments already described. In addition, some references to GAAP or IFRS were changed from 'under' to 'in accordance with' but the intention is that those changes, and indeed all the changes being made, should have no impact on what the standard requires.
9. The Restructured IFRS 1 as issued in November 2008 required application for first IFRS financial statements for periods beginning on or after 1 January 2009. However, the IASB changed the effective date to 1 July 2009 at its December 2008 meeting to prevent potential problems arising from the interaction of this date with the effective dates of certain other IFRSs.

EFRAG's initial analysis of the costs and benefits of the revision to IFRS 1

10. EFRAG has considered whether, and if so to what extent, implementing the Restructured IFRS 1 in the EU might involve preparers or users incurring incremental costs, and whether those costs are likely to be exceeded by the benefits to be derived from its adoption.
11. The IASB's intention is that replacing existing IFRS 1 with the Restructured IFRS 1 will not result in any change in the requirements of IFRS; the objective is only to simplify the standard so that it is easier to use and easier to amend in the future. EFRAG's initial assessment was that there had indeed been no changes made to the requirements.
12. On that basis, EFRAG went on to tentatively conclude that:
 - (a) implementing the Restructured IFRS 1 would for some EU preparers result in some insignificant additional year one costs, but that those incremental costs

would overall be balanced out for EU preparers as a whole by cost savings arising from the simplification of the standard. As a result, EFRAG's tentative view was that the Restructured IFRS 1 was likely to have no cost implications for EU preparers overall;

- (b) the Restructured IFRS 1 would not have cost implications for users; and
 - (c) the Restructured IFRS 1 would have no impact on the quality of the financial information provided.
13. Thus, EFRAG's initial assessment was that the benefits and costs arising for preparers and users from implementing the Restructured IFRS 1 in the EU were likely to balance each other out. On the other hand, it seemed likely that the Restructured IFRS 1 would result in net benefits for those jurisdictions still to transition to IFRS and also for the IASB.
14. EFRAG published its initial assessment of the costs and benefits of implementing the Restructured IFRS 1 in the EU and supporting analysis on 27 January 2009 and invited comment on it until 13 March 2009. In response, EFRAG received 6 comment letters and all agreed with EFRAG's initial assessment and had no additional comments, although two stated they had not carried out a detailed examination of the effects involved EFRAG's final analysis of the costs and benefits of the revision to IFRS 1.

EFRAG's final analysis of the costs and benefits of the revision to IFRS 1

15. EFRAG's assessment is that the replacement of the existing IFRS 1 with the Restructured IFRS 1 will not result in any change in the requirements of IFRS.

Costs for preparers

16. As the requirements of IFRS will be unaffected by the implementation of Restructured IFRS 1, EFRAG's assessment is that there are unlikely to be any incremental costs for EU preparers arising from the revised standard except that, for stakeholders involved with multiple transitions to IFRS, it will be necessary to read and understand the new structure and this will involve those stakeholders some additional insignificant costs in year one.
17. The IASB intends the Restructured IFRS 1 to be less complex and therefore easier to understand and use. EFRAG believes this is likely to prove to be the case, which means that transitions are likely to involve lower costs in the future than in the past. EFRAG's assessment is, however, those cost savings are likely to be insignificant.
18. EFRAG believes that these additional (insignificant) costs and (insignificant) cost savings will broadly balance each other out in the case of EU preparers as a whole and that therefore overall the Restructured IFRS 1 will have no cost implications for EU preparers.

Costs for users

19. As users should not see any difference in the financial information provided under the Restructured IFRS 1, EFRAG's view is that users will not incur any additional costs as a result of the standard.

Benefits for preparers and users

20. As EFRAG's assessment is that the restructuring will have no effect on the actual requirements, it follows that its assessment is that Restructured IFRS 1 will have no impact on the information provided in financial statements. Thus, there will not be benefits arising from the implementation of Restructured IFRS 1, other than the cost savings discussed (and taken into account) already.

Conclusion

21. EFRAG's overall assessment is therefore that:
- (a) implementing the Restructured IFRS 1 will for some EU preparers result in some insignificant additional year one costs, but that those incremental costs will overall be balanced out for EU preparers as a whole by cost savings arising from the simplification of the standard. As a result, EFRAG believes that overall the Restructured IFRS 1 will have no cost implications for EU preparers;
 - (b) the Restructured IFRS 1 will not have cost implications for users and will also have no impact on the financial information provided.
22. Thus, EFRAG's assessment is that the benefits and costs arising for preparers and users from implementing the Restructured IFRS 1 in the EU will balance each other out. On the other hand, EFRAG believes that the Restructured IFRS 1 will result in net benefits for those jurisdictions still to transition to IFRS and also for the IASB.

EFRAG
30 March 2009

Attachment 2



Jörgen Holmquist
Director General
European Commission
Directorate General for the Internal Market
1049 Brussels

30 March 2009

Dear Mr. Holmquist

Adoption of the Revised Version of IFRS 1 *First-time Adoption of International Financial Reporting Standards*

Based on the requirements of the Regulation (EC) No 1606/2002 of the European Parliament and of the Council on the application of international accounting standards, we are pleased to provide our opinion on the adoption of the revised IFRS 1 *First-time Adoption of International Financial Reporting Standards* (Restructured IFRS 1), which was published in November 2008. The restructuring was proposed in an exposure draft on which EFRAG commented.

The Restructured IFRS 1 does not contain any technical changes to IFRS; rather it changes the order of the content of the standard to more easily accommodate future amendments that might become necessary. The Restructured IFRS 1 also removes from the standard outdated transition guidance and some minor wording changes. The Restructured IFRS 1 will apply for entities transitioning to IFRS for the first time for annual periods beginning on or after 1 July 2009.

EFRAG has carried out an evaluation of Restructured IFRS 1. As part of that process, EFRAG issued a draft assessment of the Restructured IFRS 1 against the EU endorsement criteria for public comment and, when finalising its advice and the content of this letter, it took the comments received in response into account. EFRAG's evaluation is based on input from standard setters, market participants and other interested parties, and its discussions of technical matters are open to the public.

EFRAG supports the Restructured IFRS 1 and has concluded that it meets the requirements of Regulation (EC) No 1606/2002 of the European Parliament and of the Council on the application of international accounting standards in that:

- it is not contrary to the 'true and fair principle' set out in Article 16(3) of Council Directive 83/349/EEC and Article 2(3) of Council Directive 78/660/EEC; and

EFRAG Endorsement Advice Letter on Revised Version of IFRS 1

- it meets the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management

For the reasons given above, EFRAG believes that it is in the European interest to adopt the Restructured IFRS 1 and, accordingly, EFRAG recommends its adoption. EFRAG's reasoning is explained in the attached 'Appendix – Basis for Conclusions'.

On behalf of the members of EFRAG, I should be happy to discuss our advice with you, other officials of the EU Commission or the Accounting Regulatory Committee as you may wish.

Yours sincerely
Stig Enevoldsen
EFRAG, Chairman

Appendix Basis for Conclusions

This appendix sets out the basis for the conclusions reached and for the recommendation made by EFRAG on the Revised IFRS 1 First-time Adoption of International Reporting Standards.

In its comment letters to the IASB, EFRAG points out that such letters are submitted in EFRAG's capacity as a contributor to the IASB's due process. They do not necessarily indicate the conclusions that would be reached by EFRAG in its capacity as advisor to the European Commission on endorsement of the final IFRS or Interpretation on the issue.

In the latter capacity, EFRAG's role is to make a recommendation about endorsement based on its assessment of the final IFRS or Interpretation against the European endorsement criteria, as currently defined. These are explicit criteria which have been designed specifically for application in the endorsement process, and therefore the conclusions reached on endorsement may be different from those arrived at by EFRAG in developing its comments on proposed IFRSs or Interpretations. Another reason for a difference is that EFRAG's thinking may evolve.

1. Compared to the previous version of IFRS 1 *First-time Adoption of International Reporting Standards*, the revised IFRS 1 (Restructured IFRS 1) repositions some paragraphs in existing IFRS 1 and omits some paragraphs that are now outdated. Some wording changes have also been made. However, the IASB's intention in making these changes has been to make no changes to what the standard requires.
2. Therefore, when evaluating the Restructured IFRS 1, EFRAG considered the following questions:
 - (a) Has any of the changes made had an effect on the requirements of IFRS 1?
 - (b) If the answer to that question is 'no', does the Restructured IFRS 1 meet the criteria for EU endorsement?
3. Having formed tentative views on these issues and prepared a draft assessment, EFRAG issued that draft assessment on 27 January 2009 and asked for comments on it by 13 March 2009. EFRAG has considered all the comments received, and all were supportive of EFRAG's tentative views.

Has any of the changes made had an effect on IFRS 1's requirements?

4. EFRAG considered whether the changes made to existing IFRS 1 have had an effect on the financial reporting requirements by considering first the restructuring amendments (and wording changes consequential to those restructuring amendments), then the omission of various paragraphs deemed to be redundant, then finally the other amendments made.
5. In EFRAG's view, the restructuring amendments (and wording changes consequential to those restructuring amendments) will have no effect on the financial reporting requirements of the standard. Furthermore, EFRAG agrees that the paragraphs that have been omitted from the Restructured IFRS 1 were indeed redundant. Finally, EFRAG believes that the other changes made are cosmetic and will have no impact on the standard's requirements.

Does the Restructured IFRS 1 meet the criteria for EU endorsement?

6. Since the Restructured IFRS 1 does not change the requirements of IFRS 1, in EFRAG's view a detailed evaluation of the revised standard is not necessary. Instead, bearing in mind that EFRAG assessed the original version of IFRS 1 when it was issued and concluded that it met the EU endorsement criteria, and that EFRAG carried out an assessment and reached the same conclusion about each of the changes subsequently made to the standard, EFRAG believes it is appropriate to limit its technical assessment of the Restructured IFRS 1 to asking whether there is any evidence from the application of the existing standard to suggest that EFRAG's assessment of the original standard and subsequent revisions needs to be revised.
7. In other words, EFRAG has considered the application of the existing IFRS 1 to evaluate whether the Restructured IFRS 1 meets the requirements of the European Parliament and of the Council on the application of international accounting standards and therefore whether the Restructured IFRS 1:
 - (a) is not contrary to the 'true and fair principle' set out in Article 16(3) of Council Directive 83/349/EEC and Article 2(3) of Council Directive 78/660/EEC; and
 - (b) meets the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management.

EFRAG has also considered whether it is in the European interest to adopt the Restructured IFRS 1.

8. EFRAG is not aware of any evidence from the application of the original IFRS 1 or subsequent amended versions that would suggest EFRAG's prior assessment needs to be revised. IFRS 1 inevitably involves compromising comparability and the requirements of IFRS generally in the short-term by allowing the—often optional—implementation of practical alternatives to the 'usual' IFRS requirements on initial application of IFRS, but by doing that it becomes possible for more entities to adopt IFRS—and that means more comparability globally and better financial reporting generally in the longer-term.
9. EFRAG is not aware of any reason to be concerned that the way this balance has previously been struck in IFRS 1 has created problems overall in terms of relevance, reliability, understandability or comparability. EFRAG is also not aware of any reason to believe that that balance is contrary to the true and fair view principle or is not in the European interest.

Conclusion

10. For the reasons set out above, EFRAG has concluded that the Restructured IFRS 1 satisfies the criteria for EU endorsement and that EFRAG should recommend its endorsement.