
**FINANCIAL
REPORTING STANDARD**

FRS 101

Guidance on Implementing
**First-time Adoption of
Financial Reporting Standards**

This Guidance is applicable for annual reporting period beginning on
1 January 2023.

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Guidance on implementing FRS 101 *First-time Adoption of Financial Reporting Standards*

This guidance accompanies, but is not part of, FRS 101.

Introduction

IG1 This implementation guidance:

- (a) explains how the requirements of the FRS interact with the requirements of some other FRSs (paragraphs IG2–IG62, IG64 and IG65). This explanation addresses those FRSs that are most likely to involve questions that are specific to first-time adopters.
- (b) includes an illustrative example to show how a first-time adopter might disclose how the transition to FRSs affected its reported financial position, financial performance and cash flows, as required by paragraphs 24(a) and (b), 25 and 26 of the FRS (paragraph IG63).

FRS 10 *Events after the Reporting Period*

IG2 Except as described in paragraph IG3, an entity applies FRS 10 in determining whether:

- (a) its opening FRS statement of financial position reflects an event that occurred after the date of transition to FRSs; and
- (b) comparative amounts in its first FRS financial statements reflect an event that occurred after the end of that comparative period.

IG3 Paragraphs 14–17 of the FRS require some modifications to the principles in FRS 10 when a first-time adopter determines whether changes in estimates are adjusting or non-adjusting events at the date of transition to FRSs (or, when applicable, the end of the comparative period). Cases 1 and 2 below illustrate those modifications. In case 3 below, paragraphs 14–17 of the FRS do not require modifications to the principles in FRS 10.

- (a) Case 1—Previous GAAP required estimates of similar items for the date of transition to FRSs, using an accounting policy that is consistent with FRSs. In this case, the estimates in accordance with FRSs need to be consistent with estimates made for that date in accordance with previous GAAP, unless there is objective evidence that those estimates were in error (see FRS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*). The entity reports later revisions to those estimates as events of the period in which it makes the revisions, rather than as adjusting events resulting from the receipt of further evidence about conditions that existed at the date of transition to FRSs.
- (b) Case 2—Previous GAAP required estimates of similar items for the date of transition to FRSs, but the entity made those estimates using accounting policies that are not consistent with its accounting policies in accordance with FRSs. In this case, the estimates in accordance with FRSs need to be consistent with the estimates required in accordance with previous GAAP for that date (unless there is objective evidence that those estimates were in error), after adjusting for the difference in accounting policies. The opening FRS statement of financial position reflects those adjustments for the difference in accounting policies. As in case 1, the entity reports later revisions to those estimates as events of the period in which it makes the revisions.

For example, previous GAAP may have required an entity to recognise and measure provisions on a basis consistent with FRS 37 *Provisions, Contingent Liabilities and Contingent Assets*, except that the previous GAAP measurement was on an undiscounted basis. In this example, the entity uses the estimates in accordance with previous GAAP as inputs in making the discounted measurement required by FRS 37.

- (c) Case 3—Previous GAAP did not require estimates of similar items for the date of transition to FRSs. Estimates in accordance with FRSs for that date reflect conditions existing at that date. In particular, estimates of market prices, interest rates or foreign exchange rates at the date of transition to FRSs reflect market conditions at that date. This is consistent with the distinction in FRS 10 between adjusting events after the reporting period and non-adjusting events after the reporting period.

IG Example 1 Estimates
<p>Background</p> <p>Entity A's first FRS financial statements are for a period that ends on 31 December 20X5 and include comparative information for one year. In its previous GAAP financial statements for 31 December 20X3 and 20X4, entity A:</p> <ul style="list-style-type: none"> (a) made estimates of accrued expenses and provisions at those dates; (b) accounted on a cash basis for a defined benefit pension plan; and (c) did not recognise a provision for a court case arising from events that occurred in September 20X4. When the court case was concluded on 30 June 20X5, entity A was required to pay CU1,000¹ and paid this on 10 July 20X5. <p>In preparing its first FRS financial statements, entity A concludes that its estimates in accordance with previous GAAP of accrued expenses and provisions at 31 December 20X3 and 20X4 were made on a basis consistent with its accounting policies in accordance with FRSs. Although some of the accruals and provisions turned out to be overestimates and others to be underestimates, entity A concludes that its estimates were reasonable and that, therefore, no error had occurred. As a result, accounting for those overestimates and underestimates involves the routine adjustment of estimates in accordance with FRS 8.</p> <p style="text-align: right;"><i>continued...</i></p>

¹ In this guidance monetary amounts are denominated in 'currency units (CU)'.

...continued

IG Example 1 Estimates

Application of requirements

In preparing its opening FRS statement of financial position at 1 January 20X4 and in its comparative statement of financial position at 31 December 20X4, entity A:

- (a) does not adjust the previous estimates for accrued expenses and provisions; and
- (b) makes estimates (in the form of actuarial assumptions) necessary to account for the pension plan in accordance with FRS 19 *Employee Benefits*. Entity A's actuarial assumptions at 1 January 20X4 and 31 December 20X4 do not reflect conditions that arose after those dates. For example, entity A's:
 - (i) discount rates at 1 January 20X4 and 31 December 20X4 for the pension plan and for provisions reflect market conditions at those dates; and
 - (ii) actuarial assumptions at 1 January 20X4 and 31 December 20X4 about future employee turnover rates do not reflect conditions that arose after those dates—such as a significant increase in estimated employee turnover rates as a result of a curtailment of the pension plan in 20X5.

The treatment of the court case at 31 December 20X4 depends on the reason why entity A did not recognise a provision in accordance with previous GAAP at that date.

Assumption 1 – Previous GAAP was consistent with FRS 37 *Provisions, Contingent Liabilities and Contingent Assets*. Entity A concluded that the recognition criteria were not met. In this case, entity A's assumptions in accordance with FRSs are consistent with its assumptions in accordance with previous GAAP. Therefore, entity A does not recognise a provision at 31 December 20X4.

Assumption 2 – Previous GAAP was not consistent with FRS 37. Therefore, entity A develops estimates in accordance with FRS 37. Under FRS 37, an entity determines whether an obligation exists at the end of the reporting period by taking account of all available evidence, including any additional evidence provided by events after the reporting period. Similarly, in accordance with FRS 10 *Events after the Reporting Period*, the resolution of a court case after the reporting period is an adjusting event after the reporting period if it confirms that the entity had a present obligation at that date. In this instance, the resolution of the court case confirms that entity A had a liability in September 20X4 (when the events occurred that gave rise to the court case). Therefore, entity A recognises a provision at 31 December 20X4. Entity A measures that provision by discounting the CU1,000 paid on 10 July 20X5 to its present value, using a discount rate that complies with FRS 37 and reflects market conditions at 31 December 20X4.

- IG4 Paragraphs 14–17 of the FRS do not override requirements in other FRSs that base classifications or measurements on circumstances existing at a particular date. Examples include:
- (a) the distinction between finance leases and operating leases for a lessor (see FRS 116 *Leases* and paragraph IG14);
 - (b) the restrictions in FRS 38 *Intangible Assets* that prohibit capitalisation of expenditure on an internally generated intangible asset if the asset did not qualify for recognition when the expenditure was incurred; and
 - (c) the distinction between financial liabilities and equity instruments (see FRS 32 *Financial Instruments: Presentation*).

FRS 12 *Income Taxes*

- IG5 An entity applies FRS 12 to temporary differences between the carrying amount of the assets and liabilities in its opening FRS statement of financial position and their tax bases.
- IG6 In accordance with FRS 12, the measurement of current and deferred tax reflects tax rates and tax laws that have been enacted or substantively enacted by the end of the reporting period. An entity accounts for the effect of changes in tax rates and tax laws when those changes are enacted or substantively enacted.

FRS 16 *Property, Plant and Equipment*

- IG7 If an entity's depreciation methods and rates in accordance with previous GAAP are acceptable in accordance with FRSs, it accounts for any change in estimated useful life or depreciation pattern prospectively from when it makes that change in estimate (paragraphs 14 and 15 of the FRS and paragraph 61 of FRS 16). However, in some cases, an entity's depreciation methods and rates in accordance with previous GAAP may differ from those that would be acceptable in accordance with FRSs (for example, if they were adopted solely for tax purposes and do not reflect a reasonable estimate of the asset's useful life). If those differences have a material effect on the financial statements, the entity adjusts accumulated depreciation in its opening FRS statement of financial position retrospectively so that it complies with FRSs.
- IG8 An entity may elect to use one of the following amounts as the deemed cost of an item of property, plant and equipment:
- (a) fair value at the date of transition to FRSs (paragraph D5 of the FRS), in which case the entity gives the disclosures required by paragraph 30 of the FRS;
 - (b) a revaluation in accordance with previous GAAP that meets the criteria in paragraph D6 of the FRS;
 - (c) fair value at the date of an event such as a privatisation or initial public offering (paragraph D8 of the FRS);
 - (d) an allocation of an amount determined under previous GAAP that meets the criteria in paragraph D8A of the FRS; or
 - (e) the carrying amount under previous GAAP of an item of property, plant and equipment that is used, or was previously used, in operations subject to rate regulation (paragraph D8B of the FRS).
- IG9 Subsequent depreciation is based on that deemed cost and starts from the date for which the entity established the deemed cost.

- IG10 If an entity chooses as its accounting policy the revaluation model in FRS 16 for some or all classes of property, plant and equipment, it presents the cumulative revaluation surplus as a separate component of equity. The revaluation surplus at the date of transition to FRSs is based on a comparison of the carrying amount of the asset at that date with its cost or deemed cost. If the deemed cost is the fair value at the date of transition to FRSs, the entity gives the disclosures required by paragraph 30 of the FRS.
- IG11 If revaluations in accordance with previous GAAP did not satisfy the criteria in paragraph D6 or D8 of the FRS, an entity measures the revalued assets in its opening statement of financial position on one of the following bases:
- (a) cost (or deemed cost) less any accumulated depreciation and any accumulated impairment losses under the cost model in FRS 16;
 - (b) deemed cost, being the fair value at the date of transition to FRSs (paragraph D5 of the FRS); or
 - (c) revalued amount, if the entity adopts the revaluation model in FRS 16 as its accounting policy in accordance with FRSs for all items of property, plant and equipment in the same class.
- IG12 FRS 16 requires each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item to be depreciated separately. However, FRS 16 does not prescribe the unit of measure for recognition of an asset, ie what constitutes an item of property, plant and equipment. Thus, judgement is required in applying the recognition criteria to an entity's specific circumstances (see FRS 16 paragraphs 9 and 43).
- IG13 In some cases, the construction or commissioning of an asset results in an obligation for an entity to dismantle or remove the asset and restore the site on which the asset stands. An entity applies FRS 37 *Provisions, Contingent Liabilities and Contingent Assets* in recognising and measuring any resulting provision. The entity applies FRS 16 in determining the resulting amount included in the cost of the asset, before depreciation and impairment losses. Items such as depreciation and, when applicable, impairment losses cause differences between the carrying amount of the liability and the amount included in the carrying amount of the asset. An entity accounts for changes in such liabilities in accordance with INT FRS 101 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*. However, paragraph D21 of FRS 101 provides an exemption for changes that occurred before the date of transition to FRSs, and prescribes an alternative treatment where the exemption is used. An example of the first-time adoption of INT FRS 101, which illustrates the use of this exemption, is given at paragraphs IG201–IG203.

FRS 116 Leases

- IG14 At the date of transition to FRSs, a lessor classifies leases as operating leases or finance leases on the basis of circumstances existing at the inception of the lease (FRS 116 paragraph 66). Lease classification is reassessed only if there is a lease modification. Changes in estimates (for example, changes in estimates of the economic life or of the residual value of the underlying asset) or changes in circumstances (for example, default by the lessee) do not give rise to a new classification of a lease.

IG15 - [Deleted]
IG16

FRS 115 Revenue from Contracts with Customers

- IG17 If an entity has received amounts that do not yet qualify for recognition as revenue in accordance with FRS 115 (for example, the proceeds of a sale that does not qualify for revenue recognition), the entity recognises a liability in its opening FRS statement of financial

position and measures that liability at the amount received, adjusted (if appropriate) for a significant financing component in accordance with FRS 115.

FRS 19 Employee Benefits

IG18 [Deleted]

IG19 An entity's actuarial assumptions at the date of transition to FRSs are consistent with actuarial assumptions made for the same date in accordance with previous GAAP (after adjustments to reflect any difference in accounting policies), unless there is objective evidence that those assumptions were in error (paragraph 14 of the FRS). The impact of any later revisions to those assumptions is an actuarial gain or loss of the period in which the entity makes the revisions.

IG20 An entity may need to make actuarial assumptions at the date of transition to FRSs that were not necessary in accordance with its previous GAAP. Such actuarial assumptions do not reflect conditions that arose after the date of transition to FRSs. In particular, discount rates and the fair value of plan assets at the date of transition to FRSs reflect market conditions at that date. Similarly, the entity's actuarial assumptions at the date of transition to FRSs about future employee turnover rates do not reflect a significant increase in estimated employee turnover rates as a result of a curtailment of the pension plan that occurred after the date of transition to FRSs (paragraph 16 of the FRS).

IG21 In many cases, an entity's first FRS financial statements will reflect measurements of employee benefit obligations at three dates: the end of the first FRS reporting period, the date of the comparative statement of financial position and the date of transition to FRSs. FRS 19 encourages an entity to involve a qualified actuary in the measurement of all material post-employment benefit obligations. To minimise costs, an entity may request a qualified actuary to carry out a detailed actuarial valuation at one or two of these dates and roll the valuation(s) forward or back to the other date(s). Any such roll forward or roll back reflects any material transactions and other material events (including changes in market prices and interest rates) between those dates (FRS 19 paragraph 57).

FRS 21 The Effects of Changes in Foreign Exchange Rates

IG21A An entity may, in accordance with previous GAAP, have treated 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 as assets and liabilities of the entity rather than as assets and liabilities of the foreign operation. If so, the entity is permitted to apply prospectively the requirements of paragraph 47 of FRS 21 to all acquisitions occurring after the date of transition to FRSs.

FRS 103 Business Combinations

IG22 The following examples illustrate the effect of Appendix C of the FRS, assuming that a first-time adopter uses the exemption.

IG Example 2 Business combination**Background**

Entity B's first FRS financial statements are for a period that ends on 31 December 20X5 and include comparative information for 20X4 only. On 1 July 20X1, entity B acquired 100 per cent of subsidiary C. In accordance with its previous GAAP, entity B:

- (a) classified the business combination as an acquisition by entity B.
- (b) measured the assets acquired and liabilities assumed at the following amounts in accordance with previous GAAP at 31 December 20X3 (date of transition to FRSs):
 - (i) identifiable assets less liabilities for which FRSs require cost-based measurement at a date after the business combination: CU200 (with a tax base of CU150 and an applicable tax rate of 30 per cent).
 - (ii) pension liability (for which the present value of the defined benefit obligation measured in accordance with FRS 19 *Employee Benefits* is CU130 and the fair value of plan assets is CU100): nil (because entity B used a pay as you go cash method of accounting for pensions in accordance with its previous GAAP). The tax base of the pension liability is also nil.
 - (iii) goodwill: CU180.
- (c) did not, at the acquisition date, recognise deferred tax arising from temporary differences associated with the identifiable assets acquired and liabilities assumed.

Application of requirements

In its opening (consolidated) FRS statement of financial position, entity B:

- (a) classifies the business combination as an acquisition by entity B even if the business combination would have qualified in accordance with FRS 103 as a reverse acquisition by subsidiary C (paragraph C4(a) of the FRS).
- (b) does not adjust the accumulated amortisation of goodwill. Entity B tests the goodwill for impairment in accordance with FRS 36 *Impairment of Assets* and recognises any resulting impairment loss, based on conditions that existed at the date of transition to FRSs. If no impairment exists, the carrying amount of the goodwill remains at CU180 (paragraph C4(g) of the FRS).
- (c) for those net identifiable assets acquired for which FRSs require cost-based measurement at a date after the business combination, treats their carrying amount in accordance with previous GAAP immediately after the business combination as their deemed cost at that date (paragraph C4(e) of the FRS).
- (d) does not restate the accumulated depreciation and amortisation of the net identifiable assets in (c), unless the depreciation methods and rates in accordance with previous GAAP result in amounts that differ materially from those required in accordance with FRSs (for example, if they were adopted solely for tax purposes and do not reflect a reasonable estimate of the asset's useful life in accordance with FRSs). If no such restatement is made, the carrying amount of those assets in the opening FRS statement of financial position equals their carrying amount in accordance with previous GAAP at the date of transition to FRSs (CU200) (paragraph IG7).

continued...

...continued**IG Example 2 Business combination**

- (e) if there is any indication that identifiable assets are impaired, tests those assets for impairment, based on conditions that existed at the date of transition to FRSs (see FRS 36).
- (f) recognises the pension liability, and measures it, at the present value of the defined benefit obligation (CU130) less the fair value of the plan assets (CU100), giving a carrying amount of CU30, with a corresponding debit of CU30 to retained earnings (paragraph C4(d) of the FRS). However, if subsidiary C had already adopted FRSs in an earlier period, entity B would measure the pension liability at the same amount as in subsidiary C's financial statements (paragraph D17 of the FRS and IG Example 9).
- (g) recognises a net deferred tax liability of CU6 (CU20 at 30 per cent) arising from:
- (i) the taxable temporary difference of CU50 (CU200 less CU150) associated with the identifiable assets acquired and non-pension liabilities assumed, less
 - (ii) the deductible temporary difference of CU30 (CU30 less nil) associated with the pension liability.

The entity recognises the resulting increase in the deferred tax liability as a deduction from retained earnings (paragraph C4(k) of the FRS). If a taxable temporary difference arises from the initial recognition of the goodwill, entity B does not recognise the resulting deferred tax liability (paragraph 15(a) of FRS 12 *Income Taxes*).

IG Example 3 Business combination—restructuring provision**Background**

Entity D's first FRS financial statements are for a period that ends on 31 December 20X5 and include comparative information for 20X4 only. On 1 July 20X3, entity D acquired 100 per cent of subsidiary E. In accordance with its previous GAAP, entity D recognised an (undiscounted) restructuring provision of CU100 that would not have qualified as an identifiable liability in accordance with FRS 103. The recognition of this restructuring provision increased goodwill by CU100. At 31 December 20X3 (date of transition to FRSs), entity D:

- (a) had paid restructuring costs of CU60; and
- (b) estimated that it would pay further costs of CU40 in 20X4, and that the effects of discounting were immaterial. At 31 December 20X3, those further costs did not qualify for recognition as a provision in accordance with FRS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

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IG Example 3 Business combination—restructuring provision

Application of requirements

In its opening FRS statement of financial position, entity D:

- (a) does not recognise a restructuring provision (paragraph C4(c) of the FRS).
- (b) does not adjust the amount assigned to goodwill. However, entity D tests the goodwill for impairment in accordance with FRS 36 *Impairment of Assets*, and recognises any resulting impairment loss (paragraph C4(g) of the FRS).
- (c) as a result of (a) and (b), reports retained earnings in its opening FRS statement of financial position that are higher by CU40 (before income taxes, and before recognising any impairment loss) than in the statement of financial position at the same date in accordance with previous GAAP.

IG Example 4 Business combination—intangible assets

Background

Entity F's first FRS financial statements are for a period that ends on 31 December 20X5 and include comparative information for 20X4 only. On 1 July 20X1 entity F acquired 75 per cent of subsidiary G. In accordance with its previous GAAP, entity F assigned an initial carrying amount of CU200 to intangible assets that would not have qualified for recognition in accordance with FRS 38 *Intangible Assets*. The tax base of the intangible assets was nil, giving rise to a deferred tax liability (at 30 per cent) of CU60.

On 31 December 20X3 (the date of transition to FRSs) the carrying amount of the intangible assets in accordance with previous GAAP was CU160, and the carrying amount of the related deferred tax liability was CU48 (30 per cent of CU160).

Application of requirements

Because the intangible assets do not qualify for recognition as separate assets in accordance with FRS 38, entity F transfers them to goodwill, together with the related deferred tax liability (CU48) and non-controlling interests (paragraph C4(g)(i) of the FRS). The related non-controlling interests amount to CU28 (25 per cent of [CU160 – CU48 = CU112]). Thus, the increase in goodwill is CU84—intangible assets (CU160) less deferred tax liability (CU48) less non-controlling interests (CU28).

Entity F tests the goodwill for impairment in accordance with FRS 36 *Impairment of Assets* and recognises any resulting impairment loss, based on conditions that existed at the date of transition to FRSs (paragraph C4(g)(ii) of the FRS).

IG Example 5 Business combination—goodwill deducted from equity and treatment of related intangible assets
Background

Entity H acquired a subsidiary before the date of transition to FRSs. In accordance with its previous GAAP, entity H:

- (a) recognised goodwill as an immediate deduction from equity;
- (b) recognised an intangible asset of the subsidiary that does not qualify for recognition as an asset in accordance with FRS 38 *Intangible Assets*; and
- (c) did not recognise an intangible asset of the subsidiary that would qualify in accordance with FRS 38 for recognition as an asset in the financial statements of the subsidiary. The subsidiary held the asset at the date of its acquisition by entity H.

Application of requirements

In its opening FRS statement of financial position, entity H:

- (a) does not recognise the goodwill, as it did not recognise the goodwill as an asset in accordance with previous GAAP (paragraph C4(g)–(i) of the FRS).
- (b) does not recognise the intangible asset that does not qualify for recognition as an asset in accordance with FRS 38. Because entity H deducted goodwill from equity in accordance with its previous GAAP, the elimination of this intangible asset reduces retained earnings (paragraph C4(c)(ii) of the FRS).
- (c) recognises the intangible asset that qualifies in accordance with FRS 38 for recognition as an asset in the financial statements of the subsidiary, even though the amount assigned to it in accordance with previous GAAP in entity H's consolidated financial statements was nil (paragraph C4(f) of the FRS). The recognition criteria in FRS 38 include the availability of a reliable measurement of cost (paragraphs IG45–IG48) and entity H measures the asset at cost less accumulated depreciation and less any impairment losses identified in accordance with FRS 36 *Impairment of Assets*. Because entity H deducted goodwill from equity in accordance with its previous GAAP, the recognition of this intangible asset increases retained earnings (paragraph C4(c)(ii) of the FRS). However, if this intangible asset had been subsumed in goodwill recognised as an asset in accordance with previous GAAP, entity H would have decreased the carrying amount of that goodwill accordingly (and, if applicable, adjusted deferred tax and non-controlling interests) (paragraph C4(g)(i) of the FRS).

IG Example 6 Business combination—subsidiary not consolidated in accordance with previous GAAP**Background**

Parent J's date of transition to FRSs is 1 January 20X4. In accordance with its previous GAAP, parent J did not consolidate its 75 per cent subsidiary K, acquired in a business combination on 15 July 20X1. On 1 January 20X4:

- (a) the cost of parent J's investment in subsidiary K is CU180.
- (b) in accordance with FRSs, subsidiary K would measure its assets at CU500 and its liabilities (including deferred tax in accordance with FRS 12 *Income Taxes*) at CU300. On this basis, subsidiary K's net assets are CU200 in accordance with FRSs.

Application of requirements

Parent J consolidates subsidiary K. The consolidated statement of financial position at 1 January 20X4 includes:

- (a) subsidiary K's assets at CU500 and liabilities at CU300;
- (b) non-controlling interests of CU50 (25 per cent of [CU500 – CU300]); and
- (c) goodwill of CU30 (cost of CU180 less 75 per cent of [CU500 – CU300]) (paragraph C4(j) of the FRS). Parent J tests the goodwill for impairment in accordance with FRS 36 *Impairment of Assets* and recognises any resulting impairment loss, based on conditions that existed at the date of transition to FRSs (paragraph C4(g)(ii) of the FRS).

IG Example 7 Business combination—lease in which the acquiree was a lessee not capitalised in accordance with previous GAAP**Background**

Parent L's date of transition to FRSs is 1 January 20X4. Parent L acquired subsidiary M on 15 January 20X1 and did not capitalise leases in which subsidiary M was a lessee. If subsidiary M prepared financial statements in accordance with FRSs, it would recognise lease liabilities of CU300 and right-of-use assets of CU250 at 1 January 20X4.

Application of requirements

Parent L has elected not to apply the transition reliefs in paragraphs D9 and D9B-D9E of this Standard. In its consolidated opening FRS statement of financial position, parent L recognises lease liabilities of CU300 and right-of-use assets of CU250, and charges CU50 to retained earnings (paragraph C4(f)).

FRS 23 *Borrowing Costs*

IG23 On first adopting FRSs, an entity begins capitalising borrowing costs (FRS 23 as revised in 2007). In accordance with paragraph D23 of the FRS, an entity:

- (a) capitalises borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009 or the date of transition to FRSs (whichever is later);
- (b) may elect to designate any date before 1 January 2009 or the date of transition to FRSs (whichever is later) and to capitalise borrowing costs relating to all qualifying assets for which the commencement date for capitalisation is on or after that date.

However, if the entity established a deemed cost for an asset, the entity does not capitalise borrowing costs incurred before the date of the measurement that established the deemed cost.

IG24 FRS 23 requires disclosure of interest capitalised during the period. Neither FRS 23 nor the FRS requires disclosure of the cumulative amount capitalised.

IG25 [Deleted]

FRS 110 *Consolidated Financial Statements*

IG26 A first-time adopter consolidates all subsidiaries (as defined in FRS 110), unless FRS 110 requires otherwise.

IG27 If a first-time adopter did not consolidate a subsidiary in accordance with previous GAAP, then:

- (a) in its consolidated financial statements, the first-time adopter measures the subsidiary's assets and liabilities at the same carrying amounts as in the FRS financial statements of the subsidiary, after adjusting for consolidation procedures and for the effects of the business combination in which it acquired the subsidiary (paragraph D17 of the FRS). If the subsidiary has not adopted FRSs in its financial statements, the carrying amounts described in the previous sentence are those that FRSs would require in those financial statements (paragraph C4(j) of the FRS).
- (b) if the parent acquired the subsidiary in a business combination before the date of transition to FRS, the parent recognises goodwill, as explained in IG Example 6.
- (c) if the parent did not acquire the subsidiary in a business combination because it created the subsidiary, the parent does not recognise goodwill.

IG28 When a first-time adopter adjusts the carrying amounts of assets and liabilities of its subsidiaries in preparing its opening FRS statement of financial position, this may affect non-controlling interests and deferred tax.

IG29 IG Examples 8 and 9 illustrate paragraphs D16 and D17 of the FRS, which address cases where a parent and its subsidiary become first-time adopters at different dates.

IG Example 8 Parent adopts FRSs before subsidiary

Background

Parent N presents its (consolidated) first FRS financial statements in 20X5. Its foreign subsidiary O, wholly owned by parent N since formation, prepares information in accordance with FRSs for internal consolidation purposes from that date, but subsidiary O does not present its first FRS financial statements until 20X7.

Application of requirements

If subsidiary O applies paragraph D16(a) of the FRS, the carrying amounts of its assets and liabilities are the same in both its opening FRS statement of financial position at 1 January 20X6 and parent N's consolidated statement of financial position (except for adjustments for consolidation procedures) and are based on parent N's date of transition to FRSs.

Alternatively, subsidiary O may, in accordance with paragraph D16(b) of the FRS, measure all its assets or liabilities based on its own date of transition to FRSs (1 January 20X6). However, the fact that subsidiary O becomes a first-time adopter in 20X7 does not change the carrying amounts of its assets and liabilities in parent N's consolidated financial statements.

IG Example 9 Subsidiary adopts FRSs before parent

Background

Parent P presents its (consolidated) first FRS financial statements in 20X7. Its foreign subsidiary Q, wholly owned by parent P since formation, presented its first FRS financial statements in 20X5. Until 20X7, subsidiary Q prepared information for internal consolidation purposes in accordance with parent P's previous GAAP.

Application of requirements

The carrying amounts of subsidiary Q's assets and liabilities at 1 January 20X6 are the same in both parent P's (consolidated) opening FRS statement of financial position and subsidiary Q's financial statements (except for adjustments for consolidation procedures) and are based on subsidiary Q's date of transition to FRSs. The fact that parent P becomes a first-time adopter in 20X7 does not change those carrying amounts (paragraph D17 of the FRS).

IG30 Paragraphs D16 and D17 of the FRS do not override the following requirements:

- (a) to apply Appendix C of the FRS to assets acquired, and liabilities assumed, in a business combination that occurred before the acquirer's date of transition to FRSs. However, the acquirer applies paragraph D17 to new assets acquired, and liabilities assumed, by the acquiree after that business combination and still held at the acquirer's date of transition to FRSs.
- (b) to apply the rest of the FRS in measuring all assets and liabilities for which paragraphs D16 and D17 are not relevant.
- (c) to give all disclosures required by the FRS as of the first-time adopter's own date of transition to FRSs.

IG31 Paragraph D16 of the FRS applies if a subsidiary becomes a first-time adopter later than its parent, for example if the subsidiary previously prepared a reporting package in accordance with FRSs for consolidation purposes but did not present a full set of financial statements in accordance with FRSs. This may be relevant not only when a subsidiary's reporting package complies fully with the recognition and measurement requirements of FRSs, but also when it is adjusted centrally for matters such as review of events after the reporting period and central allocation of pension costs. For the disclosure required by paragraph 26 of the FRS, adjustments made centrally to an unpublished reporting package are not corrections of errors. However, paragraph D16 does not permit a subsidiary to ignore misstatements that are immaterial to the consolidated financial statements of its parent but material to its own financial statements.

FRS 29 Financial Reporting in Hyperinflationary Economies

IG32 An entity complies with FRS 21 *The Effects of Changes in Foreign Exchange Rates* in determining its functional currency and presentation currency. When the entity prepares its opening FRS statement of financial position, it applies FRS 29 to any periods during which the economy of the functional currency or presentation currency was hyperinflationary.

IG33 An entity may elect to use the fair value of an item of property, plant and equipment at the date of transition to FRSs as its deemed cost at that date (paragraph D5 of the FRS), in which case it gives the disclosures required by paragraph 30 of the FRS.

IG34 If an entity elects to use the exemptions in paragraphs D5–D8 of the FRS, it applies FRS 29 to periods after the date for which the revalued amount or fair value was determined.

FRS 32 Financial Instruments: Presentation

IG35 In its opening FRS statement of financial position, an entity applies the criteria in FRS 32 to classify financial instruments issued (or components of compound instruments issued) as either financial liabilities or equity instruments in accordance with the substance of the contractual arrangement when the instrument first satisfied the recognition criteria in FRS 32 (paragraphs 15 and 30), without considering events after that date (other than changes to the terms of the instruments).

IG36 For compound instruments outstanding at the date of transition to FRSs, an entity determines the initial carrying amounts of the components on the basis of circumstances existing when the instrument was issued (FRS 32 paragraph 30). An entity determines those carrying amounts using the version of FRS 32 effective at the end of its first FRS reporting period. If the liability component is no longer outstanding at the date of transition to FRSs, a first-time adopter need not separate the initial equity component of the instrument from the cumulative interest accreted on the liability component (paragraph D18 of the FRS).

FRS 34 Interim Financial Reporting

IG37 FRS 34 applies if an entity is required, or elects, to present an interim financial report in accordance with FRSs. Accordingly, neither FRS 34 nor the FRS requires an entity:

- (a) to present interim financial reports that comply with FRS 34; or
- (b) to prepare new versions of interim financial reports presented in accordance with previous GAAP. However, if an entity does prepare an interim financial report in accordance with FRS 34 for part of the period covered by its first FRS financial statements, the entity restates the comparative information presented in that report so that it complies with FRSs.

- IG38 An entity applies the FRS in each interim financial report that it presents in accordance with FRS 34 for part of the period covered by its first FRS financial statements. In particular, paragraph 32 of the FRS requires an entity to disclose various reconciliations (see IG Example 10).

IG Example 10 Interim financial reporting
<p>Background</p> <p>Entity R's first FRS financial statements are for a period that ends on 31 December 20X5, and its first interim financial report in accordance with FRS 34 is for the quarter ended 31 March 20X5. Entity R prepared previous GAAP annual financial statements for the year ended 31 December 20X4, and prepared quarterly reports throughout 20X4.</p> <p>Application of requirements</p> <p>In each quarterly interim financial report for 20X5, entity R includes reconciliations of:</p> <ul style="list-style-type: none"> (a) its equity in accordance with previous GAAP at the end of the comparable quarter of 20X4 to its equity in accordance with FRSs at that date; and (b) its total comprehensive income (or, if it did not report such a total, profit or loss) in accordance with previous GAAP for the comparable quarter of 20X4 (current and year to date) to its total comprehensive income in accordance with FRSs. <p>In addition to the reconciliations required by (a) and (b) and the disclosures required by FRS 34, entity R's interim financial report for the first quarter of 20X5 includes reconciliations of (or a cross-reference to another published document that includes these reconciliations):</p> <ul style="list-style-type: none"> (a) its equity in accordance with previous GAAP at 1 January 20X4 and 31 December 20X4 to its equity in accordance with FRSs at those dates; and (b) its total comprehensive income (or, if it did not report such a total, profit or loss) for 20X4 in accordance with previous GAAP to its total comprehensive income for 20X4 in accordance with FRSs. <p>Each of the above reconciliations gives sufficient detail to enable users to understand the material adjustments to the statement of financial position and statement of comprehensive income. Entity R also explains the material adjustments to the statement of cash flows.</p> <p>If entity R becomes aware of errors made in accordance with previous GAAP, the reconciliations distinguish the correction of those errors from changes in accounting policies.</p> <p>If entity R did not, in its most recent annual financial statements in accordance with previous GAAP, disclose information material to an understanding of the current interim period, its interim financial reports for 20X5 disclose that information or include a cross-reference to another published document that includes it (paragraph 33 of the FRS).</p>

FRS 36 Impairment of Assets and FRS 37 Provisions, Contingent Liabilities and Contingent Assets

- IG39 An entity applies FRS 36 in:
- (a) determining whether any impairment loss exists at the date of transition to FRSs; and
 - (b) measuring any impairment loss that exists at that date, and reversing any impairment loss that no longer exists at that date. An entity's first FRS financial statements include the disclosures that FRS 36 would have required if the entity had recognised

those impairment losses or reversals in the period beginning with the date of transition to FRSs (paragraph 24(c) of the FRS).

- IG40 The estimates used to determine whether an entity recognises an impairment loss or provision (and to measure any such impairment loss or provision) at the date of transition to FRSs are consistent with estimates made for the same date in accordance with previous GAAP (after adjustments to reflect any difference in accounting policies), unless there is objective evidence that those estimates were in error (paragraphs 14 and 15 of the FRS). The entity reports the impact of any later revisions to those estimates as an event of the period in which it makes the revisions.
- IG41 In assessing whether it needs to recognise an impairment loss or provision (and in measuring any such impairment loss or provision) at the date of transition to FRSs, an entity may need to make estimates for that date that were not necessary in accordance with its previous GAAP. Such estimates and assumptions do not reflect conditions that arose after the date of transition to FRSs (paragraph 16 of the FRS).
- IG42 The transitional provisions in FRS 36 and FRS 37 do not apply to an entity's opening FRS statement of financial position (paragraph 9 of the FRS).
- IG43 FRS 36 requires the reversal of impairment losses in some cases. If an entity's opening FRS statement of financial position reflects impairment losses, the entity recognises any later reversal of those impairment losses in profit or loss (except when FRS 36 requires the entity to treat that reversal as a revaluation). This applies to both impairment losses recognised in accordance with previous GAAP and additional impairment losses recognised on transition to FRSs.

FRS 38 *Intangible Assets*

- IG44 An entity's opening FRS statement of financial position:
- (a) excludes all intangible assets and other intangible items that do not meet the criteria for recognition in accordance with FRS 38 at the date of transition to FRSs; and
 - (b) includes all intangible assets that meet the recognition criteria in FRS 38 at that date, except for intangible assets acquired in a business combination that were not recognised in the acquirer's consolidated statement of financial position in accordance with previous GAAP and also would not qualify for recognition in accordance with FRS 38 in the separate statement of financial position of the acquiree (see paragraph C4(f) of the FRS).
- IG45 The criteria in FRS 38 require an entity to recognise an intangible asset if, and only if:
- (a) it is probable that the future economic benefits that are attributable to the asset will flow to the entity; and
 - (b) the cost of the asset can be measured reliably.
- FRS 38 supplements these two criteria with further, more specific, criteria for internally generated intangible assets.
- IG46 In accordance with paragraphs 65 and 71 of FRS 38, an entity capitalises the costs of creating internally generated intangible assets prospectively from the date when the recognition criteria are met. FRS 38 does not permit an entity to use hindsight to conclude retrospectively that these recognition criteria are met. Therefore, even if an entity concludes retrospectively that a future inflow of economic benefits from an internally generated intangible asset is probable and the entity is able to reconstruct the costs reliably, FRS 38 prohibits it from capitalising the costs incurred before the date when the entity both:

- (a) concludes, based on an assessment made and documented at the date of that conclusion, that it is probable that future economic benefits from the asset will flow to the entity; and
 - (b) has a reliable system for accumulating the costs of internally generated intangible assets when, or shortly after, they are incurred.
- IG47 If an internally generated intangible asset qualifies for recognition at the date of transition to FRSs, an entity recognises the asset in its opening FRS statement of financial position even if it had recognised the related expenditure as an expense in accordance with previous GAAP. If the asset does not qualify for recognition in accordance with FRS 38 until a later date, its cost is the sum of the expenditure incurred from that later date.
- IG48 The criteria discussed in paragraph IG45 also apply to an intangible asset acquired separately. In many cases, contemporaneous documentation prepared to support the decision to acquire the asset will contain an assessment of the future economic benefits. Furthermore, as explained in paragraph 26 of FRS 38, the cost of a separately acquired intangible asset can usually be measured reliably.
- IG49 For an intangible asset acquired in a business combination before the date of transition to FRSs, its carrying amount in accordance with previous GAAP immediately after the business combination is its deemed cost in accordance with FRSs at that date (paragraph C4(e) of the FRS). If that carrying amount was zero, the acquirer does not recognise the intangible asset in its consolidated opening FRS statement of financial position, unless it would qualify in accordance with FRS 38, applying the criteria discussed in paragraphs IG45–IG48, for recognition at the date of transition to FRSs in the statement of financial position of the acquiree (paragraph C4(f) of the FRS). If those recognition criteria are met, the acquirer measures the asset on the basis that FRS 38 would require in the statement of financial position of the acquiree. The resulting adjustment affects goodwill (paragraph C4(g)(i) of the FRS).
- IG50 A first-time adopter may elect to use the fair value of an intangible asset at the date of an event such as a privatisation or initial public offering as its deemed cost at the date of that event (paragraph D8 of the FRS), provided that the intangible asset qualifies for recognition in accordance with FRS 38 (paragraph 10 of the FRS). In addition, if, and only if, an intangible asset meets both the recognition criteria in FRS 38 (including reliable measurement of original cost) and the criteria in FRS 38 for revaluation (including the existence of an active market), a first-time adopter may elect to use one of the following amounts as its deemed cost (paragraph D7 of the FRS):
- (a) fair value at the date of transition to FRSs (paragraph D5 of the FRS), in which case the entity gives the disclosures required by paragraph 30 of the FRS; or
 - (b) a revaluation in accordance with previous GAAP that meets the criteria in paragraph D6 of the FRS.
- IG51 If an entity's amortisation methods and rates in accordance with previous GAAP would be acceptable in accordance with FRSs, the entity does not restate the accumulated amortisation in its opening FRS statement of financial position. Instead, the entity accounts for any change in estimated useful life or amortisation pattern prospectively from the period when it makes that change in estimate (paragraph 14 of the FRS and paragraph 104 of FRS 38). However, in some cases, an entity's amortisation methods and rates in accordance with previous GAAP may differ from those that would be acceptable in accordance with FRSs (for example, if they were adopted solely for tax purposes and do not reflect a reasonable estimate of the asset's useful life). If those differences have a material effect on the financial statements, the entity adjusts the accumulated amortisation in its opening FRS statement of financial position retrospectively so that it complies with FRSs (paragraph 14 of the FRS). However, if an entity uses the exemption in paragraph D8B, it uses the carrying amount of the intangible asset at the date of transition to FRSs as deemed cost as if it had acquired an intangible asset with the same remaining service potential for that amount at the date of transition to FRSs.

Subsequent amortisation is based on that deemed cost and starts from the date of transition to FRSs.

FRS 109 *Financial Instruments*

- IG52 An entity recognises and measures all financial assets and financial liabilities in its opening FRS statement of financial position in accordance with FRS 109, except as specified in paragraphs B2–B6 of the FRS, which address derecognition and hedge accounting.

Recognition

- IG53 An entity recognises all financial assets and financial liabilities (including all derivatives) that qualify for recognition in accordance with FRS 109 and have not yet qualified for derecognition in accordance with FRS 109, except non-derivative financial assets and non-derivative financial liabilities derecognised in accordance with previous GAAP before the date of transition to FRSs, to which the entity does not choose to apply paragraph B3 (see paragraphs B2 and B3 of the FRS). For example, an entity that does not apply paragraph B3 does not recognise assets transferred in a securitisation, transfer or other derecognition transaction that occurred before the date of transition to FRSs if those transactions qualified for derecognition in accordance with previous GAAP. However, if the entity uses the same securitisation arrangement or other derecognition arrangement for further transfers after the date of transition to FRSs, those further transfers qualify for derecognition only if they meet the derecognition criteria of FRS 109.
- IG54 An entity does not recognise financial assets and financial liabilities that do not qualify for recognition in accordance with FRS 109, or have already qualified for derecognition in accordance with FRS 109.

Embedded derivatives

- IG55 When FRS 109 requires an entity to separate an embedded derivative from a host contract, the initial carrying amounts of the components at the date when the instrument first satisfies the recognition criteria in FRS 109 reflect circumstances at that date (FRS 109 paragraph 4.3.3). If the entity cannot determine the initial carrying amounts of the embedded derivative and host contract reliably, it measures the entire combined contract as at fair value through profit or loss (FRS 109 paragraph 4.3.6).

Measurement

- IG56 In preparing its opening FRS statement of financial position, an entity applies the criteria in FRS 109 to classify financial instruments on the basis of the facts and circumstances that exist at the date of transition to FRSs. The resulting classifications are applied retrospectively.
- IG57 For those financial assets and financial liabilities measured at amortised cost in the opening FRS statement of financial position, an entity determines the gross carrying amount of the financial assets and the amortised cost of the financial liabilities on the basis of circumstances existing when the assets and liabilities first satisfied the recognition criteria in FRS 109. However, if the entity acquired those financial assets and financial liabilities in a past business combination, their carrying amount in accordance with previous GAAP immediately following the business combination is their deemed cost in accordance with FRSs at that date (paragraph C4(e) of the FRS).
- IG58 [Deleted]

Transition adjustments

- IG58A An entity shall treat an adjustment to the carrying amount of a financial asset or financial liability as a transition adjustment to be recognised in the opening balance of retained

earnings (or another component of equity, as appropriate) at the date of transition to FRSs only to the extent that it results from adopting FRS 109. Because all derivatives, other than those that are financial guarantee contracts, a commitment to provide a loan at a below-market interest rate, a loan-commitment that is subject to the impairment requirements of FRS 109 or are designated and effective hedging instruments, are measured at fair value through profit or loss, the differences between the previous carrying amount (which may have been zero) and the fair value of the derivatives are recognised as an adjustment of the balance of retained earnings at the beginning of the financial year in which FRS 109 is initially applied (other than for a derivative that is a financial guarantee contract, a commitment to provide loan at a below-market interest rate or a designated and effective hedging instrument).

- IG58B FRS 8 (as revised in 2004) applies to adjustments resulting from changes in estimates. If an entity is unable to determine whether a particular portion of the adjustment is a transition adjustment or a change in estimate, it treats that portion as a change in accounting estimate in accordance with FRS 8, with appropriate disclosures (FRS 8 paragraphs 32–40).
- IG59 An entity may, in accordance with its previous GAAP, have measured investments at fair value and recognised the revaluation gain outside profit or loss. If an investment is classified as at fair value through profit or loss, the pre-FRS 109 revaluation gain that had been recognised outside profit or loss is reclassified into retained earnings on initial application of FRS 109. If, on initial application of FRS 109, an investment is measured at fair value through other comprehensive income in accordance with paragraph 4.1.2A of FRS 109 or is designated at fair value through other comprehensive income in accordance with paragraph 5.7.5 of FRS 109, then the pre-FRS 109 revaluation gain is recognised in a separate component of equity. Subsequently, the entity recognises gains and losses on these financial assets in accordance with FRS 109.

Hedge accounting

- IG60 Paragraphs B4–B6 of the FRS deal with hedge accounting. The designation and documentation of a hedge relationship must be completed on or before the date of transition to FRSs if the hedge relationship is to qualify for hedge accounting from that date. Hedge accounting can be applied prospectively only from the date that the hedge relationship is fully designated and documented.
- IG60A An entity may, in accordance with its previous GAAP, have deferred or not recognised gains and losses on a fair value hedge of a hedged item that is not measured at fair value. For such a fair value hedge, an entity adjusts the carrying amount of the hedged item at the date of transition to FRSs. The adjustment is the lower of:
- (a) that portion of the cumulative change in the fair value of the hedged item that was not recognised in accordance with previous GAAP; and
 - (b) that portion of the cumulative change in the fair value of the hedging instrument and, in accordance with previous GAAP, was either (i) not recognised or (ii) deferred in the statement of financial position as an asset or liability.
- IG60B An entity may, in accordance with its previous GAAP, have deferred gains and losses on a cash flow hedge of a forecast transaction. If, at the date of transition to FRSs, the hedged forecast transaction is not highly probable, but is expected to occur, the entire deferred gain or loss is recognised in the cash flow hedge reserve within equity. Any net cumulative gain or loss that has been reclassified to the cash flow hedge reserve on initial application of FRS 109 remains in equity until (a) the forecast transaction subsequently results in the recognition of a non-financial asset or non-financial liability, (b) the forecast transaction affects profit or loss or (c) subsequently circumstances change and the forecast transaction is no longer expected to occur, in which case any related net cumulative gain or loss is reclassified from the cash flow hedge reserve to profit or loss. If the hedging instrument is still held, but the hedge does not qualify as a cash flow hedge in accordance with FRS 109, hedge accounting is no longer appropriate starting from the date of transition to FRSs.

FRS 40 Investment Property

- IG61 An entity that adopts the fair value model in FRS 40 measures its investment property at fair value at the date of transition to FRSs. The transitional requirements of FRS 40 do not apply (paragraph 9 of the FRS).
- IG62 An entity that adopts the cost model in FRS 40 applies paragraphs IG7–IG13 on property, plant and equipment.

Explanation of transition to FRSs

- IG63 Paragraphs 24(a) and (b), 25 and 26 of the FRS require a first-time adopter to disclose reconciliations that give sufficient detail to enable users to understand the material adjustments to the statement of financial position, statement of comprehensive income and, if applicable, statement of cash flows. Paragraph 24(a) and (b) requires specific reconciliations of equity and total comprehensive income. IG Example 11 shows one way of satisfying these requirements.

IG Example 11 Reconciliation of equity and total comprehensive income

Background

An entity first adopted FRSs in 20X5, with a date of transition to FRSs of 1 January 20X4. Its last financial statements in accordance with previous GAAP were for the year ended 31 December 20X4.

Application of requirements

The entity's first FRS financial statements include the reconciliations and related notes shown below.

Among other things, this example includes a reconciliation of equity at the date of transition to FRSs (1 January 20X4). The FRS also requires a reconciliation at the end of the last period presented in accordance with previous GAAP (not included in this example).

In practice, it may be helpful to include cross-references to accounting policies and supporting analyses that give further explanation of the adjustments shown in the reconciliations below.

If a first-time adopter becomes aware of errors made in accordance with previous GAAP, the reconciliations distinguish the correction of those errors from changes in accounting policies (paragraph 26 of the FRS). This example does not illustrate disclosure of a correction of an error.

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IG Example 11 Reconciliation of equity and total comprehensive income

Reconciliation of equity at 1 January 20X4 (date of transition to FRSs)

Note		Previous GAAP	Effect of transition to FRSs	FRSs
		CU	CU	CU
1	Property, plant and equipment	8,299	100	8,399
2	Goodwill	1,220	150	1,370
2	Intangible assets	208	(150)	58
3	Financial assets	3,471	420	3,891
	Total non-current assets	13,198	520	13,718
	Trade and other receivables	3,710	0	3,710
4	Inventories	2,962	400	3,362
5	Other receivables	333	431	764
	Cash and cash equivalents	748	0	748
	Total current assets	7,753	831	8,584
	Total assets	20,951	1,351	22,302
	Interest-bearing loans	9,396	0	9,396
	Trade and other payables	4,124	0	4,124
6	Employee benefits	0	66	66
7	Restructuring provision	250	(250)	0
	Current tax liability	42	0	42
8	Deferred tax liability	579	460	1,039
	Total liabilities	14,391	276	14,667
	Total assets less total liabilities	6,560	1,075	7,635
	Issued capital	1,500	0	1,500
5	Cash flow hedge reserve	0	302	302
9	Retained earnings	5,060	773	5,833
	Total equity	6,560	1,075	7,635

continued...

*...continued***IG Example 11 Reconciliation of equity and total comprehensive income****Notes to the reconciliation of equity at 1 January 20X4:**

- 1 Depreciation was influenced by tax requirements in accordance with previous GAAP, but in accordance with FRSs reflects the useful life of the assets. The cumulative adjustment increased the carrying amount of property, plant and equipment by 100.
- 2 Intangible assets in accordance with previous GAAP included CU150 for items that are transferred to goodwill because they do not qualify for recognition as intangible assets in accordance with FRSs.
- 3 Financial assets are all classified as at fair value through profit or loss in accordance with FRSs and are carried at their fair value of CU3,891. They were carried at cost of CU3,471 in accordance with previous GAAP. The resulting gains of CU294 (CU420, less related deferred tax of CU126) are included in retained earnings.
- 4 Inventories include fixed and variable production overhead of CU400 in accordance with FRSs, but this overhead was excluded in accordance with previous GAAP.
- 5 Unrealised gains of CU431 on unmatured forward foreign exchange contracts are recognised in accordance with FRSs, but were not recognised in accordance with previous GAAP. The resulting gains of CU302 (CU431, less related deferred tax of CU129) are included in the cash flow hedge reserve because the contracts hedge forecast sales.
- 6 A pension liability of CU66 is recognised in accordance with FRSs, but was not recognised in accordance with previous GAAP, which used a cash basis.
- 7 A restructuring provision of CU250 relating to head office activities was recognised in accordance with previous GAAP, but does not qualify for recognition as a liability in accordance with FRSs.

- 8 The above changes increased the deferred tax liability as follows:

	CU
Cash flow hedge reserve (note 5)	129
Retained earnings	331
Increase in deferred tax liability	460

Because the tax base at 1 January 20X4 of the items reclassified from intangible assets to goodwill (note 2) equalled their carrying amount at that date, the reclassification did not affect deferred tax liabilities.

continued...

*...continued***IG Example 11 Reconciliation of equity and total comprehensive income**

9 The adjustments to retained earnings are as follows:

	CU
Depreciation (note 1)	100
Financial assets (note 3)	420
Production overhead (note 4)	400
Pension liability (note 6)	(66)
Restructuring provision (note 7)	250
Tax effect of the above	(331)
Total adjustment to retained earnings	<u>773</u>

Reconciliation of total comprehensive income for 20X4

Note		<i>Previous GAAP</i>	<i>Effect of transition to FRSs</i>	<i>FRSs</i>
		CU	CU	CU
	Revenue	20,910	0	20,910
1,2,3	Cost of sales	(15,283)	(97)	(15,380)
	Gross profit	5,627	(97)	5,530
6	Other income	0	180	180
1	Distribution costs	(1,907)	(30)	(1,937)
1,4	Administrative expenses	(2,842)	(300)	(3,142)
	Finance income	1,446	0	1,446
	Finance costs	(1,902)	0	(1,902)
	Profit before tax	422	(247)	175
5	Tax expense	(158)	74	(84)
	Profit (loss) for the year	264	(173)	91
7	Cash flow hedges	0	(40)	(40)
8	Tax relating to other comprehensive income	0	(29)	(29)
	Other comprehensive income	0	(69)	(69)
	Total comprehensive income	264	(242)	22

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IG Example 11 Reconciliation of equity and total comprehensive income

Notes to the reconciliation of total comprehensive income for 20X4:

- 1 A pension liability is recognised in accordance with FRSs, but was not recognised in accordance with previous GAAP. The pension liability increased by CU130 during 20X4, which caused increases in cost of sales (CU50), distribution costs (CU30) and administrative expenses (CU50).
- 2 Cost of sales is higher by CU47 in accordance with FRSs because inventories include fixed and variable production overhead in accordance with FRSs but not in accordance with previous GAAP.
- 3 Depreciation was influenced by tax requirements in accordance with previous GAAP, but reflects the useful life of the assets in accordance with FRSs. The effect on the profit for 20X4 was not material.
- 4 A restructuring provision of CU250 was recognised in accordance with previous GAAP at 1 January 20X4, but did not qualify for recognition in accordance with FRSs until the year ended 31 December 20X4. This increases administrative expenses for 20X4 in accordance with FRSs.
- 5 Adjustments 1–4 above lead to a reduction of CU128 in deferred tax expense.
- 6 Financial assets at fair value through profit or loss increased in value by CU180 during 20X4. They were carried at cost in accordance with previous GAAP. Fair value changes have been included in 'Other income'.
- 7 The fair value of forward foreign exchange contracts that are effective hedges of forecast transactions decreased by CU40 during 20X4.
- 8 Adjustments 6 and 7 above lead to an increase of CU29 in deferred tax expense.

Explanation of material adjustments to the statement of cash flows for 20X4:

Income taxes of CU133 paid during 20X4 are classified as operating cash flows in accordance with FRSs, but were included in a separate category of tax cash flows in accordance with previous GAAP. There are no other material differences between the statement of cash flows presented in accordance with FRSs and the statement of cash flows presented in accordance with previous GAAP.

FRS 102 *Share-based Payment*

- IG64 A first-time adopter is encouraged, but not required, to apply FRS 102 *Share-based Payment* to equity instruments that were granted after 22 November 2002 that vested before the later of (a) the date of transition to FRSs and (b) 1 January 2005.
- IG65 For example, if an entity's date of transition to FRSs is 1 January 2004, the entity applies FRS 102 to shares, share options or other equity instruments that were granted after 22 November 2002 and had not yet vested at 1 January 2005. Conversely, if an entity's date of transition to FRSs is 1 January 2010, the entity applies FRS 102 to shares, share options or other equity instruments that were granted after 22 November 2002 and had not yet vested at 1 January 2010.

FRS 20 Accounting for Government Grants and Disclosure of Government Assistance

IG66 Paragraph B10 of the FRS requires a first-time adopter to use its previous GAAP carrying amount of government loans existing at the date of transition to FRS as the FRS carrying amount of such loans at that date. A first-time adopter applies FRS 32 *Financial Instruments: Presentation* to classify such a loan as a financial liability or an equity instrument. Subsequently, the first-time adopter applies FRS 109 to such a loan. To do so, the entity calculates the effective interest rate by comparing the carrying amount of the loan at the date of transition to FRSs with the amount and timing of expected repayments to the government. IG Example 12 illustrates accounting for such a loan.

[Paragraphs IG67–IG200 reserved for possible guidance on future standards]

IG Example 12 Government loan at a below-market rate of interest at the date of transition to FRSs

To encourage entities to expand their operations in a specified development zone where it is difficult for entities to obtain financing for their projects, the government provides loans at a below-market rate of interest to fund the purchase of manufacturing equipment.

Entity S's date of transition to FRSs is 1 January 20X2.

In accordance with the development scheme, in 20X0 Entity S receives a loan at a below-market rate of interest from the government for CU100,000. Under previous GAAP, Entity S accounted for the loan as equity and the carrying amount under previous GAAP was CU100,000 at the date of transition to FRSs. The amount repayable will be CU103,030 at 1 January 20X5.

No other payment is required under the terms of the loan and there are no future performance conditions attached to the loan. The information needed to measure the fair value of the loan was not obtained at the time of initially accounting for the loan.

The loan meets the definition of a financial liability in accordance with FRS 32. Entity S therefore reclassifies the government loan as a liability. It also uses the previous GAAP carrying amount of the loan at the date of transition to FRSs as the carrying amount of the loan in the opening FRS statement of financial position. Entity S therefore reclassifies the amount of CU100,000 from equity to liability in the opening FRS statement of financial position. In order to measure the loan after the date of transition to FRSs, the effective interest rate starting 1 January 20X2 is calculated as below:

$$= \sqrt[3]{\left(\frac{103,000}{100,000}\right)} - 1$$

$$= 0.01$$

The carrying amounts of the loan are as follows:

Date	Carrying amount	Interest expense	Interest payable
	CU	CU	CU
1 January 20X2	100,000		
31 December 20X2	101,000	1,000	1,000
31 December 20X3	102,010	1,010	2,010
31 December 20X4	103,030	1,020	3,030

Interpretations of Financial Reporting Standards

INT FRS 101 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*

- IG201 FRS 16 requires the cost of an item of property, plant and equipment to include the initial estimate of the costs of dismantling and removing the asset and restoring the site on which it is located. FRS 37 requires the liability, both initially and subsequently, to be measured at the amount required to settle the present obligation at the end of the reporting period, reflecting a current market-based discount rate.
- IG202 INT FRS 101 requires that, subject to specified conditions, changes in an existing decommissioning, restoration or similar liability are added to or deducted from the cost of the related asset. The resulting depreciable amount of the asset is depreciated over its useful life, and the periodic unwinding of the discount on the liability is recognised in profit or loss as it occurs.
- IG203 Paragraph D21 of FRS 101 provides a transitional exemption. Instead of retrospectively accounting for changes in this way, entities can include in the depreciated cost of the asset an amount calculated by discounting the liability at the date of transition to FRSs back to, and depreciating it from, when the liability was first incurred. IG Example 201 illustrates the effect of applying this exemption, assuming that the entity accounts for its property, plant and equipment using the cost model.

IG Example 201 Changes in existing decommissioning, restoration and similar liabilities	
Background	
An entity's first FRS financial statements are for a period that ends on 31 December 20X5 and include comparative information for 20X4 only. Its date of transition to FRSs is therefore 1 January 20X4.	
The entity acquired an energy plant on 1 January 20X1, with a life of 40 years.	
As at the date of transition to FRSs, the entity estimates the decommissioning cost in 37 years' time to be 470, and estimates that the appropriate risk-adjusted discount rate for the liability is 5 per cent. It judges that the appropriate discount rate has not changed since 1 January 20X1.	
Application of requirements	
The decommissioning liability recognised at the transition date is CU77 (CU470 discounted for 37 years at 5 per cent).	
Discounting this liability back for a further three years to 1 January 20X1 gives an estimated liability at acquisition, to be included in the cost of the asset, of CU67. Accumulated depreciation on the asset is $CU67 \times 3/40 = CU5$.	
The amounts recognised in the opening FRS statement of financial position on the date of transition to FRSs (1 January 20X4) are, in summary:	
	CU
Decommissioning cost included in cost of plant	67
Accumulated depreciation	(5)
Decommissioning liability	(77)
Net assets/retained earnings	<u>(15)</u>

IG204- [Deleted]
IG206