Straight away

An overview of financial reporting developments

IASB amends IFRS 1: Exemption for severe hyperinflation and removal of fixed dates

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On December 20, the IASB issued two narrow amendments to IFRS 1, First-time adoption of International Financial Reporting Standards. The two amendments aim to simplify initial application of IFRS. This straight away highlights both amendments.

First amendment: Severe hyperinflation

What's new?

The first amendment to IFRS 1 creates an exemption when an entity that has been subject to severe hyperinflation resumes presenting, or presents for the first time, financial statements in accordance with IFRS. The exemption allows an entity to elect to measure certain assets and liabilities at fair value; and to use that fair value as the deemed cost in the opening IFRS statement of financial position.

The entity might be unable to prepare financial statements in accordance with IFRS for a period of time because it could not comply with IAS 29, Financial reporting in hyperinflationary economies, due to severe hyperinflation. The exemption applies where the entity is able to begin reporting in accordance with IFRS.

Key provisions

The amendment states that the currency of a hyperinflationary economy is subject to severe hyperinflation when:

- a reliable general price index is not available to all entities with transactions and balances in the currency; and
- exchangeability between the currency and a relatively stable foreign currency does not exist.

An entity's functional currency ceases to be subject to severe hyperinflation on the functional currency normalization date, which occurs:

- when one or both of the characteristics of severe hyperinflation no longer exist; or
- when the first-time adopter changes its functional currency to a currency that is not subject to severe hyperinflation.

The entity would be considered a first-time adopter when it resumes preparation of IFRS financial statements. The exemption applies to entities that were subject to severe hyperinflation and are adopting IFRS for the first time or have previously applied IFRS.

When an entity's date of transition to IFRS is on or after the functional currency normalization date, it may elect to measure assets and liabilities acquired before that date at fair value and use that fair value as its deemed cost in the opening IFRS statement of financial position.

IFRS 1 defines the date of transition as the beginning of the earliest period for which an entity presents comparative information under IFRS in its first IFRS financial statements. When the functional currency normalization date falls within the comparative period, that period may be less than 12 months, provided that a complete set of financial statements (as required by IAS 1) is provided for that shorter period.

The entity cannot comply with IFRS due to the severe hyperinflation in periods before the date of transition to IFRS, so the comparative information for this period cannot be prepared in accordance with IFRS. The entity should therefore consider whether disclosure of non-IFRS comparative information and historical summaries (e.g., selected financial data) in accordance with IFRS 1 would provide useful information to the users of the financial statements.

Am I affected?

The amendment is expected to have a limited impact as it is only available to entities whose functional currency was subject to severe hyperinflation. The Zimbabwean economy has been identified as an economy that was subject to severe hyperinflation until early 2009; the amendment is unlikely to apply in other territories at the moment.

The amendment would not change or allow any additional IFRS 1 exemptions for a reporting entity that has control, joint control or significant influence over an entity subject to severe hyperinflation, except to the extent that the reporting entity is also a first-time adopter.

What do I need to do?

The amendment is effective for annual periods beginning on or after July 1, 2011. Earlier application is permitted. Management of entities in hyper inflationary economies (like Zimbabwe), and first-time adopters that have interests in these entities should consider:

- their functional currency normalization date;
- their proposed date of transition to IFRS;
- whether the comparative period will be presented for a period shorter than 12 months; and
- the assets and liabilities they wish to measure at fair value on transition to IFRS.

If you have questions about this issue, please contact the PwC IFRS team or your engagement partner.

Second amendment: Removal of fixed dates

What's new?

The IASB has also amended IFRS 1 to eliminate references to fixed dates for one exception and one exemption, both dealing with financial assets and liabilities.

Key provisions

The first change requires first-time adopters to apply the de-recognition requirements of IFRS prospectively from the date of transition, rather than from January 1, 2004. This change eliminates the need for companies adopting IFRS for the first time to restate de-recognition transactions that occurred before the transition date to IFRS.

The second change relates to financial assets or liabilities recorded at fair value on initial recognition where the fair value is established through valuation techniques in the absence of an active market. The amendment allows the guidance in AG76 and AG76A of Appendix A of IAS 39, Financial Instruments: Recognition and Measurement, to be applied prospectively from the date of transition to IFRS rather than from October 25, 2002 or January 1, 2004. This means that a first-time adopter does not need to determine the fair value of financial assets and liabilities for periods prior to the date of transition. IFRS 9, Financial Instruments, has also been amended to reflect these changes.

Am I affected?

Entities that had derecognized financial assets or liabilities before the date of transition to IFRS will need to apply the de-recognition guidance from the date of transition, as it is a mandatory exception. The second change will only be relevant for entities that elect to use the exemption for fair value established by valuation techniques.

What do I need to do?

The amendment is effective for annual periods beginning on or after July 1, 2011. Earlier application is permitted.

If you have questions about this issue, please contact the PwC IFRS team or your engagement partner.