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Tricia O'Malley
IFRIC Coordinator
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
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Dear Tricia

***Exposure Draft Additional Exemptions for First-time Adopters:
Proposed Amendments to IFRS 1***

The Australian Accounting Standards Board (AASB) is pleased to submit its comments on the IASB's Exposure Draft *Additional Exemptions for First-time Adopters: Proposed Amendments to IFRS 1*. In formulating these comments, the AASB has sought views of Australian constituents.

The AASB does not support the relief being proposed for rate-regulated operations. Allowing amounts that do not form part of the cost of an asset to be capitalised is inconsistent with the *Framework*, and in the AASB's view insufficient justification has been provided to support the special treatment of these assets on first-time adoption. The AASB acknowledges that the proposals limit the relief to situations where it is impracticable to meet the existing requirements of IFRS 1 *First-time Adoption of International Financial Reporting Standards*, however the AASB is concerned that the Basis for Conclusions seems to imply that the impracticability hurdle in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* is similar to a cost-benefit test. This is not consistent with the AASB's understanding of the meaning of impracticable in IAS 8. The AASB is also concerned that the Basis does not adequately explain why entities with rate regulated assets may not be able to utilise the existing fair value as deemed cost exemption in paragraph 16 of IFRS 1.

The AASB agrees with the other proposed amendments, subject to some further refinements to the exemption proposed for entities using full cost accounting.

These points are explained further in the attached submission on the Exposure Draft. If you have any queries regarding any matters in this submission, please contact Raymond Yu (ryu@asb.gov.au) or me.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Bruce Porter'.

Bruce Porter
Acting Chairman

**Exposure Draft *Additional Exemptions for First-time Adopters:*
*Proposed Amendments to IFRS 1***

Question 1—Deemed cost for oil and gas assets

Do you agree with the proposed deemed cost option for entities using full cost accounting under previous GAAP? Why or why not? If not, what alternative do you propose and why?

The AASB is willing to support this proposed exemption for entities using full cost accounting provided that:

- (a) the exemption is limited to circumstances where it is impracticable to meet the existing requirements in IFRS 1 (consistent with the rate regulated asset exemption in the proposed paragraph 19B of this Exposure Draft), where impracticability is assessed on a basis consistent with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*;
- (b) the allocation of the full cost measurement amount to oil and gas assets in the development or production phases is required to be performed on a consistent and transparent basis. All allocations performed by an entity should use:
 - the volumes or values attributable to the same reserve categories (i.e. only proved resources, or only proved and probable reserves etc); and
 - where possible, only those reserve volumes or values that are publicly disclosed by the entity elsewhere in its financial statements. In other words, if an entity only discloses proved reserve volumes, it should not be permitted to allocate costs by using proved and probable reserves as the base; and
- (c) the IASB's reasons for granting this exemption are more clearly explained. Entities using full cost accounting that adopted IFRSs in 2005 did not receive similar relief and the Basis for Conclusions does not explain why relief is needed now but was not previously needed.

The AASB supports the proposed exemption because it is broadly comparable to the objective of IFRS 6, which is to make limited improvements to accounting for exploration and evaluation costs prior to the completion of the IASB's extractive activities project. Similarly, this proposed exemption is making limited improvements to full cost accounting – being to discontinue the recognition of the full-cost cost centre and to require an impairment test to be performed on the exploration and evaluation assets and oil and gas assets after the full cost measurement amount has been pushed down to these assets.

Question 2—Oil and gas assets—disclosure

Do you agree with the proposed disclosure requirements relating to the deemed cost option for oil and gas assets? Why or why not?

Disclosures for full cost accounting

The AASB agrees that entities utilising the full cost accounting exemption should disclose that fact.

The AASB agrees that entities utilising this exemption should provide further information that explains how the full-cost cost centre measurement amount was allocated to the underlying exploration and evaluation assets and oil and gas assets. The AASB suggests that some further guidance should be provided on the level of information required to be disclosed. For instance, a disclosure that simply says “The carrying amounts of the full-cost cost centres under previous GAAP have been allocated to the exploration and evaluation assets and oil and gas assets recognised under IFRSs on the basis of relative proved and probable reserves volumes” is not helpful to users of financial reports unless those reserve volumes are publicly disclosed by the entity elsewhere in the financial report. To provide meaningful information about the allocation, the disclosure should detail the reserve volumes or values used in the allocation and the carrying amounts of the underlying assets after the allocation is complete. Without this additional information, the AASB questions whether it is worthwhile requiring any disclosure of the cost allocation.

Disclosures for rate regulated operations

The AASB notes that no disclosures have been proposed for entities that use the exemption for rate regulated operations. The AASB recommends that entities using this exemption should also disclose that fact as well as disclosing the reasons why it was impracticable to determine the cost and fair value of these assets under IFRSs.

Question 3—Deemed cost for operations subject to rate regulation

Do you agree with the proposed deemed cost option for entities with operations subject to rate regulation? Why or why not? If not, what alternative do you propose and why?

The AASB disagrees with providing relief to rate regulated operations. In the AASB’s view, the Exposure Draft has not provided sufficient justification for exempting rate regulated assets from the general principle that amounts that do not form part of the cost of an asset (in accordance with IFRSs and the *Framework*) should be expensed.

The AASB’s concern is minimised to an extent by the fact that the exemption is only available if it is impracticable to apply existing IFRSs to the rate regulated assets. However, the AASB is concerned that the Basis for Conclusions (at paragraphs BC11-BC12) seems to be adopting a different meaning for ‘impracticable’ than its defined meaning in IAS 8, which is “applying a requirement is impracticable when the entity cannot apply it after making every reasonable effort to do so”. In the AASB’s view, the

following statements in the Basis are justifying why applying existing IFRSs is not practical or does not satisfy a cost-benefit test rather than why is it ‘impracticable’ (which the AASB understands to be a higher hurdle):

- (a) paragraph BC11: “...The restatement of property, plant and equipment to remove amounts not in compliance with IFRSs would require historical information that, given the typical age of some of the assets involved, is probably no longer available **and would be difficult to estimate**. Obtaining the fair value information necessary to use the exemption in paragraph 16 may also be impracticable, given **the lack of readily available fair value information** for those assets and **the difficulty in valuing the required number of assets in such capital-intensive operations all at one time**”
- (b) paragraph BC12: “The Board views the proposed exemption as consistent with the exemptions already found in IFRS 1 in that **it avoids excessive costs while meeting the objectives of the IFRS.**”

The AASB understands that the exemption would only apply if it is impracticable to determine either the rate regulated asset’s cost in accordance with IAS 16 or its fair value. The AASB considers that a fair value should be able to be estimated for rate regulated assets even if there is a “lack of readily available fair value information for those assets” (paragraph BC11). Paragraph 33 of IAS 16 indicates that an income or a depreciated replacement cost approach can be used to estimate fair value of property, plant and equipment assets, and the AASB expects that these measurement approaches should be able to be applied to estimate the fair value of rate regulated assets without it being impracticable. Moreover, proposed paragraph 19B would require an entity to test each rate regulated asset for impairment, which would generally require the determination of fair value in any case.

Question 4—Leases

Do you agree with the proposal not to require the reassessment of whether an arrangement contains a lease in the circumstances described in this exposure draft? Why or why not?

The AASB agrees.

Question 5—Assessments under previous GAAP before the date of transition to IFRSs

Do you agree that the situation referred to in Question 4 is the only one in which additional relief of this type is needed? If not, in what other situations is relief necessary and why?

The AASB is not aware of any other situation in which similar relief needs to be provided. The AASB recommends that this type of relief should only be provided on a case-by-case basis.

Drafting comments

Suggested amendments (new text is underlined and deleted text is marked by a strikethrough)	Justification
<p>19A ...</p> <p>The entity shall test exploration and evaluation assets and assets in the development and production phases for impairment at the date of transition to IFRSs in accordance with IFRS 6 <i>Exploration for and Evaluation of Mineral Resources</i> or IAS 36 <i>Impairment of Assets</i> respectively, <u>and, if necessary, reduce the amount determined in accordance with (a) or (b) above.</u></p> <p>...</p>	<p>The deleted text is explaining the operation of IFRS 6 and IAS 36 rather than imposing additional requirement. The AASB's view is that this explanation is not necessary and can be deleted.</p>
<p>19B ...</p> <p>If this is the case, a first-time adopter may elect to use the carrying amount of such an item at the date of transition to IFRSs if it is otherwise impracticable (as defined in IAS 8) to meet the requirements of this IFRS. An entity shall apply this election item by item. At the date of transition to IFRSs, an entity shall test each item for which this exemption is used for impairment in accordance with IAS 36, <u>and, if necessary, reduce the carrying amount.</u></p> <p>...</p>	<p><u>1st deletion:</u> The AASB is concerned that by noting that impracticable is defined in IAS 8, it may imply that any term that is defined in one IFRS and used in another does not necessarily take on its defined meaning unless specifically indicated.</p> <p><u>2nd deletion:</u> The deleted text is explaining the operation of IAS 36 rather than imposing additional requirement. The AASB's view is that this explanation is not necessary and can be deleted.</p>

