Accounting Standards Board

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Stig Enevoldsen
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commentletter@efrag.org

6 January 2009

Dear Stig

EFRAG's Draft Comment Letter on the IASB's ED 'Additional Exemptions for First-time Adopters: Proposed Amendments to IFRS 1'

Thank you for providing the Board with the opportunity to comment on your draft response to the International Accounting Standards Board's (IASB) exposure draft (ED) 'Additional Exemptions for First-time Adopters: Proposed Amendments to IFRS 1'.

The Board has responded directly to the IASB and a copy of our letter is attached.

We broadly agree with the conclusions EFRAG has reached in its draft comment letter. In our view, the response could be strengthened by including the rationale for EFRAG's position. In particular, it would be useful to make clear whether EFRAG is supporting the arguments on technical grounds or if it is the cost and benefit arguments that provide the compelling case.

Should you have any queries regarding our response please contact me, or Mario Abela, Project Director, on +44 20 7492 2442 or by email m.abela@frc-asb.org.uk.

Yours sincerely

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Detailed Responses to Questions

Oil and Gas Assets – Deemed Cost

Question to Constituents The proposed additional exemptions discussed above are available only in relation to oil and gas assets; not to extractive industry exploration and evaluation assets and extractive industry development and production assets in general. EFRAG is not aware of any demand for similar exemptions for other extractive industries, but would particularly welcome comment on the issue. Are you aware of any other extractive industries that may have similar problems at transition to IFRS as the ones described above and, if you are, please could you provide us with some information about the circumstances involved and your view as to whether the proposed exemption should be extended to cover such circumstances?
Proposed ASB Response: We note that some entities within Europe (in non-member states), such as state-owned companies (eg utilities) that have either been commercialised or privatised, may face similar issues in constructing their opening IFRS balance sheets because of fund-based accounting adopted in some jurisdictions. These entities are likely to face similar issues to the rate-regulated industries encompassed by the proposed amendment to IFRS 1.

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International Accounting Standards Board
30 Cannon Street
London EC4M 6XH

6 January 2009

Dear Sirs

Exposure Draft of proposed amendments to IFRS 1 'Additional Exemptions for First-time Adopters'

The ASB is responding to the Exposure Draft (ED) 'Additional Exemptions for First-time Adopters'. The ASB's responses to the questions asked in the ED are set in an Appendix to this letter.

We broadly support the proposed changes to IFRS 1 'First-time Adoption of International Financial Reporting Standards'. However, we would like to raise some concerns about the principles that underpin the proposed amendments.

The ASB appreciates that the transition to reporting under full International Financial Reporting Standards (IFRS) poses significant challenges for some entities. We also recognise that GAAP adopted in some jurisdictions permits accounting treatment that is not consistent with IFRS. Accordingly, it is a somewhat difficult challenge the IASB faces in encouraging entities to move to IFRS in having to balance the quality of financial reporting against cost and benefit considerations.

The ASB accepts the need to be somewhat pragmatic in the process of enabling entities to make the transition to IFRS. In particular, we note that the Board has an ongoing project on extractive industries and determining an appropriate methodology to account for oil and gas assets is complex and not easily resolved. We find the arguments put forward for assets of entities subject to rate regulation somewhat less convincing but note the exemption has been restricted to circumstances where it is impracticable to apply IFRS requirements.

We would appreciate clarification as to how rate regulated entities, after applying the transitional provisions, will be able to comply with IAS 36 going forward – particularly where the deemed cost provisions and impairment testing are to apply on an item by item basis. See our response to Question 3.

On a more general point, we are somewhat concerned about the growing list of exemptions in IFRS 1 and the lack of coherence in the rationale for relief provided to first-time adopters. In our view, IFRS 1 should set the minimum 'bar' for what constitutes credible and robust financial reporting at the point of transition. It would therefore be appropriate for the IASB to start from the objective of financial reporting in its *Framework* and develop a set of principles against which to judge what exemptions can be afforded without compromising the quality and usefulness of financial statements prepared under IFRS. In our view, in the absence of a set of clearly articulated principles, the request for exemptions will continue to grow as more jurisdictions adopt IFRS.

Should you have any queries regarding our response please contact me or
Mario Abela, Project Director, on 020 7492 2442 or by email m.abela@frc-asb.org.uk.

Yours sincerely

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Appendix – Response to Invitation to Comment

Deemed cost for oil and gas assets

Question 1

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 your propose and why?

Proposed ASB response:

The Board supports the proposed amendment.

We recognise the practical difficulties for entities making the transition to reporting under IFRS for the first-time. We also appreciate that it is necessary for the IASB to make allowances, on cost and benefits grounds, for entities constructing their opening IFRS balance sheet – particularly for oil and gas assets where the IASB's Extractive Industries project is addressing the appropriate accounting treatment for these assets.

On a more specific point, it is not clear to which 'assets' the exemption in paragraph 19A should apply. For example, do assets used to extract oil from 'tar sands' qualify? Similarly, does it extend to those assets used in the production of fuels from biological sources? Whilst it is clear that is not the IASB's intention for the proposed exemption to have broad application, once it is adopted in the Standard it becomes available to others that may be seeking relief and fall within its parameters.

In our view, the proposed definition of 'oil and gas assets' in paragraph 19A should be made more restrictive and reinforced by discussion of the term in the Basis for Conclusions. As the exemption applies to 'oil and gas assets' and not to the entities that hold them, there may be issues where an entity uses full cost accounting for all its extractive operations: (eg oil, gas and tar sands and the accounting policy applies to the first two but not the last) – the consequences for what is reported could prove confusing and unhelpful for users of the financial statements.

Oil and gas assets – disclosure

Question 2

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

Proposed ASB response:

The ASB supports the proposed disclosure requirements. However, to ensure that they adequately reflect the recognition and measurement requirements in paragraph 19A we think they should also require entities to disclose how they determined the recoverability of those assets at the date of transition. We do not believe that the disclosure requirements of IAS 36 would be triggered at transition and would be applied ordinarily at the end of the reporting period.

Deemed cost for operations subject to rate regulation

Question 3

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?

Proposed ASB response:

The Board supports the proposed amendment. However, we foresee a practical difficulty with applying the impairment test in IAS 36 given paragraph 19B states that entities "apply this election item by item". Accordingly, within a single class of assets, say 'transmission infrastructure', some items may be at cost, some at deemed cost and some at fair value. When it comes to assessing the recoverability of assets in that class or classes that form the cash generating unit, it is difficult for us to see how it will be meaningfully applied. It would be helpful if the IASB could clarify this point when finalising amendments to the Standard.

Leases

Question 4

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?

Proposed ASB response:

The Board supports this proposal on cost and benefit grounds. It may be worthwhile stating the presumption that in making a determination under IFRIC 4 under previous GAAP that a standard equivalent to IAS 17 'Leases' was effective in that jurisdiction. IFRIC 4 relies on the classification requirements contained in IAS 17 – if for some reason under previous GAAP the IAS 17-equivalent standard was modified, any assessment made for the purposes of applying IFRIC 4 may not satisfy the intention of paragraph 25F.

Assessments under previous GAAP before the date of transitions to IFRS

Question 5

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

Proposed ASB response:

The Board does not believe any further relief from IFRS 1 is required.