

ERRATUM

Implementation Guidance accompanying AASB 1

The Australian Accounting Standards Board (AASB) issued the Implementation Guidance to AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards*, the Australian equivalent of IFRS 1 *First-time Adoption of International Financial Reporting Standards*, when it made AASB 1 on 15 July 2004.

Subsequent to that date, it has emerged that the Implementation Guidance needs to be corrected in two areas:

- Australian guidance on life insurance; and
- amendments consequential to IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*.

In the first instance, the corrections in E1 of this Erratum clarify that the exemption from restating comparative information, in relation to application of the new Standards addressing life insurance, applies only to insurance contracts and does not extend to the EMVONA (Excess of Market Value Over Net Assets) asset recognised by many life insurance companies. The original illustrative example, AIG Example A100, is replaced by the version in this Erratum, and a sentence clarifying the position is added to paragraph AIG100.3.

In the second instance, the corrections in E2 of this Erratum do not change the treatment on transition but the original illustrative example, illustrating the treatment if the exemption in respect of comparatives was not chosen, is replaced by the illustrative example in this Erratum, illustrating the treatment if the exemption in respect of comparatives is chosen. The paragraphs that refer to this, IG13 and IG201-IG203, are amended to reflect the change and paragraph IG204 is deleted as it becomes redundant.

The corrections in this Erratum will be included in the Implementation Guidance to AASB 1 when next re-issued.

This Erratum is available on the AASB website (www.aasb.com.au) as a separate document and it will be provided with printed copies of AASB 1 purchased from the AASB. The document that this Erratum corrects, the Implementation Guidance accompanying AASB 1, will be amended on the AASB website as from 1 November 2004.



ERRATUM

Implementation Guidance accompanying AASB 1

<i>E1: Amendments re EMVONA assets</i>

Life insurance

- AIG100.1 A life insurer, under the 1998 version of AASB 1038 *Life Insurance Business*, recognises as a separate asset, in its consolidated financial statements, the excess of the net market values of interests in subsidiaries over the net amount (the “EMVONA asset”) of the assets and liabilities of those subsidiaries that are recognised in the consolidated financial statements.
- AIG100.2 The EMVONA asset is inconsistent with the requirements of AASB 127 *Consolidated and Separate Financial Statements* (which requires line-by-line consolidation of all subsidiaries) and AASB 138 *Intangible Assets* (to the extent that the EMVONA asset comprises internally generated goodwill). AASB 138 allows the recognition of acquired goodwill but does not allow the recognition of internally generated goodwill. AASB 138 notes that differences between the market value of an entity and the carrying amount of its identifiable net assets at any time may capture a range of factors that affect the value of the entity and such differences do not represent the cost of intangible assets controlled by the entity. The EMVONA asset is, therefore, not allowable under the revised AASB 1038 *Life Insurance Contracts* (issued 2004).
- AIG100.3 On transition to the revised version of AASB 1038 (issued 2004), the EMVONA asset is reversed against retained earnings. A life insurer would subsequently determine the amount of acquired goodwill that arose on acquisition of each subsidiary, assess this acquired goodwill for impairment under AASB 136 and recognise acquired goodwill less accumulated impairment losses in retained earnings. This is done at the start of the comparative period since the choice of not restating comparative information (in paragraph 36A(a) of AASB 1) applies only to insurance contracts.

AIG Example A100: Life insurance – EMVONA asset

BACKGROUND

Life insurer A's first Australian-equivalents-to-IFRSs financial report has a reporting date of 30 June 2006. As at 30 June 2004, the EMVONA asset is \$20m. On initial recognition of the subsidiary, this included acquired goodwill of \$7m.

APPLICATION OF REQUIREMENTS

Irrespective of whether life insurer A chooses, in accordance with the exemptions in paragraph 36A of AASB 1, not to restate comparative information relating to its insurance contracts in its financial report for the period ending 30 June 2006, it will not include \$20m for the EMVONA asset in its comparative information. The date of transition in respect of this asset is 1 July 2004 (even though the date of transition for insurance contracts covered by paragraph 36A(a) may be 1 July 2005). Life insurer A reverses the EMVONA asset against retained earnings on 1 July 2004 (see journal entry 1 below).

In respect of the purchased goodwill estimated at \$7m at the date of acquisition of the subsidiary, life insurer A decides to recognise all business combinations from that date in accordance with AASB 3 *Business Combinations*. It assesses the \$7m goodwill relating to that subsidiary under AASB 138 *Intangible Assets* and, in accordance with AASB 136 *Impairment of Assets*, determines that accumulated impairment losses as at 1 July 2004 are \$2m. It reinstates \$5m goodwill as an asset (see journal entry 2 below).

Consolidated retained earnings as at 1 July 2004 would be adjusted as follows:

- | | | | |
|----|---|-------|-------|
| 1. | DR Retained earnings | \$20m | |
| | CR EMVONA asset | | \$20m |
| | <i>To reverse the EMVONA asset</i> | | |
| 2. | DR Intangible asset – acquired goodwill | \$5m | |
| | CR Retained earnings | | \$5m |
| | <i>To reinstate acquired goodwill less accumulated impairment losses allowable under AASB 136 (\$7m less \$2m impairment)</i> | | |

E2: Amendments consequential to IFRIC 1

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 AASB 137 *Provisions, Contingent Liabilities and Contingent Assets* in

recognising and measuring any resulting provision. The entity applies AASB 116 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 UIG Interpretation 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities* identified in AASB 1048 *Interpretation and Application of Standards* as corresponding to IFRIC 1. However, paragraph 25E of AASB 1 provides an exemption for changes that occurred before the date of transition to Australian equivalents to IFRSs, and prescribes an alternative treatment where the exemption is used. An example of the first-time adoption of this Interpretation, which illustrates the use of this exemption, is given at paragraphs IG201-IG203.

.....

UIG Interpretations Corresponding to IASB Interpretations

UIG Interpretations corresponding to the IASB Interpretations are identified in AASB 1048 *Interpretation and Application of Standards*.

Changes in existing decommissioning, restoration and similar liabilities

IG201 AASB 116 *Property, Plant and Equipment* 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. AASB 137 *Provisions, Contingent Liabilities and Contingent Assets* requires the liability, both initially and subsequently, to be measured at the amount required to settle the present obligation at the reporting date, reflecting a current market-based discount rate.

IG202 UIG Interpretation 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*, identified in AASB 1048 as corresponding to IFRIC 1, 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 25E of AASB 1 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 Australian equivalents to IFRSs 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 Australian-equivalents-to-IFRSs financial report has a reporting date of 30 June 2006 and includes comparative information for 2004/05 only. Its date of transition to Australian equivalents to IFRSs is therefore 1 July 2004.

The entity acquired an energy plant on 1 July 2001, with a life of 40 years.

As at the date of transition to Australian equivalents to IFRSs, 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 July 2001.

APPLICATION OF REQUIREMENTS

The decommissioning liability recognised at the transition date is 77 (470 discounted for 37 years at 5 per cent).

Discounting this liability back for a further three years to 1 July 2001 gives an estimated liability at acquisition, to be included in the cost of the asset, of 67. Accumulated depreciation on the asset is $67 \times 3/40 = 5$.

The amounts recognised in the opening Australian-equivalents-to-IFRSs balance sheet on the date of transition to Australian equivalents to IFRSs (1 July 2004) are, in summary:

Decommissioning cost included in cost of plant	67
Accumulated depreciation	(5)
Decommissioning liability	<u>(77)</u>
Net assets/retained earnings	<u>(15)</u>