Deloitte.

Alert # 2006/2
Issued 3 February 2006

Accounting alert

Analysis of the latest accounting developments delivered to you via e-mail

This Accounting Alert provides an outline of some of the significant areas that may impact financial reporting for annual reporting periods ending 31 December 2005.

December 2005 Financial Reporting Update

The information in this *Accounting alert* is designed as a series of consideration points arising from new and revised accounting pronouncements and ASIC class orders issued since 30 June 2005.

Topics considered include:

- Amendments to Australian Accounting Standards AASB 121, 1023, 139, 124 & AAS 25
- Introduction of Australian Accounting Standard AASB 7
- IFRIC Interpretations
- UIG Interpretations and Guidance
- ASIC Class Orders and amendments.

Amendments to Australian Accounting Standards

Amendments to Australian Accounting Standard AASB 121

In January 2006 the Australian Accounting Standards Board ('AASB') released an amendment to AASB 121 *'The Effects of Changes in Foreign Exchange Rates – Net Investment in a Foreign Operation'*. The amendment will apply to all annual reporting periods ending on or after 31 December 2006 with early adoption permitted for annual reporting periods that begin on or after 1 January 2005.

A requirement of AASB 121 (issued in July 2004) is that a monetary item can be part of the reporting entity's net investment in a foreign operation provided the monetary item is denominated in the functional currency of either the reporting entity or the foreign operation.

The amendment clarifies that a monetary item forming part of the entity's net investment in a foreign operation:

- may be receivable from or payable to any subsidiary of the group
- may be denominated in the functional currency of the reporting entity, the foreign operation or any other currency.

The amendment further clarifies that, based on the principle that the exchange differences on the monetary item form part of the entity's net investment in the foreign operation, the exchange differences are reclassified to the foreign currency translation reserve in the financial statements that include the foreign operation and the reporting entity.

Introduction of Australian Accounting Standard AASB 7

AASB 7 'Financial Instruments: Disclosure' introduces increased disclosure requirements beyond those required under AASB 132 'Financial Instruments: Disclosure and Presentation'

In September 2005 the AASB released AASB 7 *'Financial Instruments: Disclosure'*. The objective of this standard is to combine and enhance the disclosure requirements in relation to the risk exposures arising from financial instruments that are currently set out in AASB 132 '*Financial Instruments: Disclosure and Presentation'* and AASB 130 '*Financial Statements of Banks and Similar Financial Institutions'*.

AASB 7 is effective for all periods commencing on or after 1 January 2007 with early application encouraged. AASB 130 and much of AASB 132 will be replaced on the adoption of this standard.

A number of the disclosures required by AASB 7 have been taken directly from AASB 132 and AASB 130 with minor wording changes. There are six significant additional disclosures that are introduced by this standard:

- disclosure in respect of loans and receivables and financial liabilities classified as fair value through profit or loss
- reconciliation of impairment provisions where the provision is not netted off against the financial asset
- disclosure of ineffectiveness recognised in profit or loss in respect of cash flow hedges and hedges of net investments in foreign operations
- disclosure of all adjustments arising from fair value hedges
- carrying amount and net gain or loss recognised for each class of financial asset
- sensitivity analysis for each type of market risk.

Revision of Australian Accounting Standard AASB 124

In December 2005 the AASB released revised AASB 124 '*Related Party Disclosures'* ('AASB 124'), effective for annual reporting periods ending on or after 31 December 2005. AASB 124 supersedes both AASB 1046 '*Director and Executive Disclosures by Disclosing Entities'* (as amended by AASB 1046A) ('AASB 1046') and AAS 22 *Related Party Disclosures* ('AAS 22').

Major changes resulting from the revised AASB 124 include:

- the application of AASB 124 to not-for-profit companies
- disclosure of compensation and share based payments
- further disclosure requirements in accordance with s.300A, Regulation 2M.3.03 and Regulation 2M.6.04
- changes to comparative disclosure requirements and parent entity relief
- significant impact for managed schemes.

Financial guarantee contracts: Amendment of Australian Accounting Standard AASB 139

Refer also to NAAS Accounting Alert 2005/13

AASB 139 now governs financial guarantee contracts.

In September 2005 the AASB released Amending Standard AASB 2005-09 which amends AASB 4 *Insurance Contracts* ('AASB 4'), AASB 1023 '*General Insurance Contracts'* ('AASB 1023'), AASB 132 and AASB 139. The amendments to AASB 139 and AASB 4 are effective for annual periods beginning on or after 1 January 2006, with earlier application encouraged.

These amendments include:

- increasing the scope of AASB 139 to include financial guarantee contracts
- requiring such contracts to be measured at fair value on initial recognition and subsequently at the greater of:
  - the amount determined in accordance with AASB 137 '*Provisions, Contingent Liabilities and Contingent Assets'* ('AASB 137'); and
  - the amount initially recognised less amortisation recognised in accordance with AASB 118 '*Revenue'* ('AASB 118')
- excluding rights to reimbursements for expenditure required to settle provisions or liabilities recognised under AASB 137 from the scope of AASB 139.

Fair value through profit and loss: Amendment of Australian Accounting Standard AASB 139

Refer also to NAAS Accounting Alert 2005/6

In June 2005 the AASB released Amending Standard AASB 2005-06 which amends AASB 139. The amendment is effective for all annual reporting periods commencing on or after 1 January 2006. Entities are entitled to early adopt the amendment as a part of the adoption of A-IFRS. The amendment restricts entities from designating any financial asset or financial liability as 'at fair value through profit or loss' to specific financial assets and financial liabilities.

Amendment to Australian Accounting Standard AASB 1023

Amendments to AASB 1023 change the way the liability adequacy test is performed.

In December 2005 the AASB released Amending Standard 2005-12 which amends AASB 1023 and AASB 1038. The amendment is effective for annual reporting periods ending on or after 31 December 2005. Entities are entitled to early adopt the amendment as a part of the adoption of A-IFRS. The amendments include:

- changing the way in which the liability adequacy test is performed under AASB 1023, as well as requiring additional disclosure in relation to this test
- amends AASB 1023 to allow insurers to adopt different probability of adequacy in performing the liability adequacy test to that adopted in determining the outstanding claims liability.

Amendment to Australian Accounting Standard AAS 25

In December 2005 the AASB released Amending Standard AASB 2005-13. AASB 2005-13 amends AAS 25 '*Financial Reporting by Superannuation Plans*' ('AAS 25') and is effective for annual reporting periods ending on or after 31 December 2005.

AAS 25 requires superannuation plans to measure assets at net market values and to recognise the change in net market values as a component of revenue for the reporting period. These requirements override the requirements in other Accounting Standards in respect of recognising and measuring assets, including AASB 132 '*Financial Instruments: Disclosure and Presentation*' ('AASB 132') and AASB 139 '*Financial Instruments: Recognition and Measurement*' ('AASB 139') in respect of financial assets. However, AAS 25 does not contain recognition and measurement requirements for financial liabilities held by superannuation plans, which include hedging instruments and derivatives. The AASB noted that there was some uncertainty whether the requirement to net market value assets should be applied to financial instruments that can change from debit balances to credit balances, or whether the AASB 132 and AASB 139 requirements apply when an instrument has a credit balance.

Amendments to AASB 25 clarify that liabilities held by superannuation plans are measured at their net market values.

This amendment to AAS 25 clarifies that financial liabilities held by superannuation plans are measured at their net market values and any changes in value are recognised in the profit or loss for the reporting period.

Urgent Issues Group (UIG) and International Financial Reporting Interpretations Committee (IFRIC) issues

Over the past six months a number of interpretations have been released by both IFRIC and the UIG. These interpretations are available from the AASB website (www.aasb.com.au). Below is a summary of these interpretations.

Urgent Issues Group Interpretation 4

Urgent Issues Group Interpretation 4 '*Determining whether an Arrangement contains a Lease*' ('UIG 4') was released during June 2005 and is effective 1 January 2006, although early adoption is encouraged.

UIG 4 provides guidance for determining whether arrangements that are not in the legal form of a lease but convey a right to use an asset should be accounted for as a lease under AASB 117 '*Leases*'.

Urgent Issues Group Interpretation 5

Urgent Issues Group Interpretation 5 *'Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Fund'* ('UIG 5') was released during June 2005 and is effective 1 January 2006, although early adoption is encouraged.

UIG 5 clarifies the accounting treatment by contributors of interests held in funds established to fund some or all of the costs of decommissioning assets or undertaken rehabilitation or restoration work.

Urgent Issues Group Interpretation 6

Urgent Issues Group Interpretation 6 '*Liabilities arising from participating in a Specific Market – Waste Electrical and Electronic Equipment'* ('UIG 6') was released during October 2005 and is effective 1 December 2005.

UIG 6 clarifies when a liability arises under the European Union's Directive on Waste Electrical and Electronic Equipment in relation to the cost of waste management for the decommissioning of electrical and electronic equipment. This interpretation has limited impact in Australia as it is based on International Financial Reporting Interpretation Committee Interpretations 6 ('IFRIC 6'), which relates to a specific European directive.

Urgent Issues Group Interpretation 1052

UIG Interpretation 1052 amends the method of accounting for tax consolidation in order to be consistent with A-IFRS.

Urgent Issues Group Interpretation 1052 *'Tax Consolidation Accounting'* was released during June 2005 and is effective 1 January 2005. UIG 1052 amends the method of accounting for tax consolidation in order to be consistent with A-IFRS.

The following are notable amendments to the tax consolidation accounting method:

- consolidated current and deferred tax balances to be allocated to each entity within the tax-consolidated group
- head entity to assume current tax liability and any deferred taxes arising from unused tax losses
- recognition of intercompany balances based on tax funding agreement
- differences between the amount assumed by the head entity and amounts recognised under the tax funding agreement accounted for as contribution to or distributions from equity participants.

Urgent Issues Group Guidance

Guidance is now available on the AASB website regarding issues removed from the UIG agenda.

Details of items removed from, or not taken to the Urgent Issues Group agenda are now available on the AASB website (www.aasb.com.au), along with any available guidance on the treatment of these issues.

Recent issues not added to the agenda include:

Inventory rebates and settlement discounts AASB 102 *'Inventories'*

Guidance was issued on a number of points involving inventory rebates and settlement discounts.

- settlement discounts should be deducted from the cost of inventories
- rebates that purely refund selling expenses should not be deducted from the cost of inventories while rebates and discounts received as a reduction in the purchase price of inventories should be taken into consideration when measuring the cost of inventories.

Direct costs affecting a financial instrument's effective interest rate AASB 139 *'Financial Instruments: Recognition and Management'*

Guidance is provided on the conflict between AASB 139 and AASB 118 on costs to be included as transaction costs. The guidance provided indicates that AASB 139 refers only to incremental costs and that the appendix guidance in AASB 118 does not override the specific requirements of AASB 139.

Employee share loan plans
AASB 2 *'Share-based payment'*

The issue considered was whether an employee share loan should be considered part of a share-based payment, in turn treating the entire arrangement as an option, or whether the loan should be accounted for as a financial asset.

Guidance received from IFRIC on the matter indicates that when the loan for the shares has recourse only to the shares, the issue of shares should be treated as an option grant for which the options are exercised on the date or dates when the loan is repaid.

Classification of long service leave liabilities
AASB 119 *'Employee Benefits'* &
AASB 132 *'Financial Instruments: Disclosure and Presentation'*

Upon advice from IFRIC, the UIG guidance suggests that the employee benefits are covered by AASB 119 rather than AASB 132.

Capitalised software
AASB 138 *'Intangible Assets'* & AASB 116 *'Property, Plant & Equipment'*

Guidance provided on the AASB website suggests that Capitalised software should be treated as an intangible asset according to paragraph 4 of AASB 138. However, as stated in the aforementioned paragraph, judgement is required in distinguishing property, plant and equipment from intangible assets.

Recent ASIC releases and amendments

The following are developments from the Australian Securities and Investments Commission ('ASIC') released during the past six months.

Additional month for first financial reports under A-IFRS for most unlisted entities
CO 05/637

Changes to financial report lodgement dates for unlisted entities.

The lodgement date of financial reports for unlisted entities has been extended for one month for financial years commencing from 1 January 2005 to 31 December 2005.

Anomalies preventing certain large proprietary companies from being grandfathered
CO 05/638

This class order replaces class order CO 98/99. One of the key pre-conditions for relief is that the financial report of the large proprietary company must be audited before the deadline for reporting to members. This class order extends the deadline for reporting to members by one month for financial years commencing from 1 January 2005 to 31 December 2005 (both inclusive).

Application of accounting standards by non-reporting entities
CO 05/639

Non-reporting entities may now take advantage of the recognition and measurement concessions available under AASB 1.

Allows non-reporting entities to take advantage of the recognition and measurement concessions available under AASB 1 *'First-time Adoption of Australian Equivalents to International Financial Reporting Standards'*.

Miscellaneous amendments to financial reporting class orders
CO 05/641

Class orders amended were CO 98/2395 *'Transfer of information from the directors' report'* and CO 98/0100 *'Rounding in financial reports and directors' reports'*. These changes relate to the introduction of A-IFRS and CLERP-9.

Combining financial reports of stapled security issuers
CO 05/642

Allows issuers of stapled securities to include their financial statements and the consolidated financial statements of the stapled group in adjacent columns in one financial report.

Combining registered scheme financial reports
CO 05/644

Allows related registered schemes with a common responsible entity to include their financial statements in adjacent columns in a single financial report where there is a facility for investors to switch monies between the related schemes.

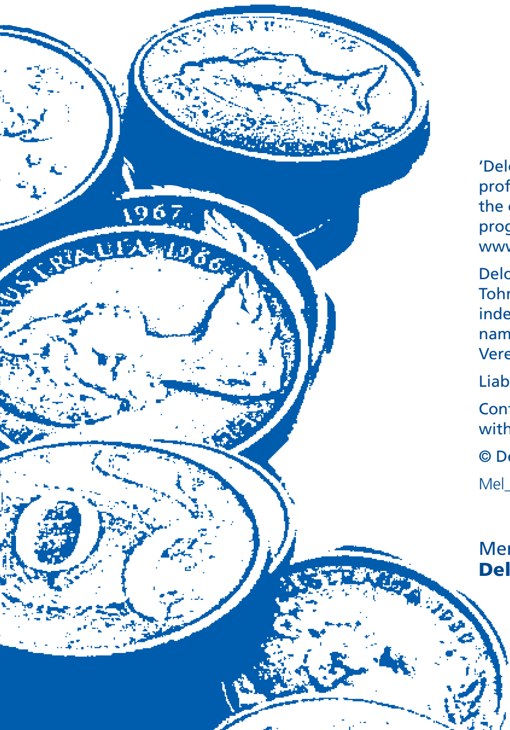
Reporting requirements for non-reporting entities
ASIC Guide

Replaces IR 00/025 and provides guidance on the application of the reporting entity concept and the reporting obligations of non-reporting entities.

Feedback and assistance

We welcome your feedback on the matters covered in this *Accounting Alert* – please email your comments to accounting_alerts@deloitte.com.au

For assistance in applying the requirements outlined above, please contact your local Deloitte office or contact our Lead National Technical Partner, Bruce Porter on +61 (0) 3 9208 7490, or by e-mail to bruporter@deloitte.com.au



Mel_01/06_016558

Member of
Deloitte Touche Tohmatsu