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Deloitte Touche Tohmatsu

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Mr. Kevin Stevenson, Chairman
International Financial Reporting Interpretations Committee
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Mr. Stevenson,

Changes in Decommissioning, Restoration and Similar Liabilities

Deloitte Touche Tohmatsu is pleased to comment on the International Financial Reporting Interpretations Committee's (IFRIC) Draft Interpretation — *Changes in Decommissioning, Restoration and Similar Liabilities* (the draft Interpretation or D2). We support the issuance of an IFRIC Interpretation on these changes to avoid inconsistencies developing in practice.

We do not believe the draft interpretation is the most appropriate interpretation of International Financial Reporting Standards (IFRS) for several reasons related to conceptual, practical and convergence concerns. In our view, IFRS should be interpreted differently to achieve a conceptually better and more operable approach that at the same time converges with U.S. GAAP.

Issues (a) and (b): Changes in estimates in cash flows and discount rates

The draft Interpretation is based on the notion that changes in estimated decommissioning, restoration and similar liabilities should be viewed as revising the initial liability and the historical cost of the related asset. We believe this is a revision of the asset's carrying amount and not its historical cost.

We note that under current IFRS, changes in the estimated outflow of resources embodying economic benefits of an asset (i.e. the recoverability of the asset) are generally attributed to and, therefore, accounted for, in current and future periods. For example, both IAS 16 *Property, Plant and Equipment* and IAS 36 *Impairment of Assets* treat a revaluation and impairment, respectively as an adjustment to the carrying amount of the asset only. That is, revaluation and impairment losses may be reversed. Additionally, both IAS 22 *Business Combinations* and ED 3 *Business Combinations* require changes in the value of assets acquired and liabilities assumed be allocated to current or future periods, with the exception of changes identified within a specified time period.

The change in estimate arises as a result of applying IAS 37, *Provisions, Contingent Liabilities and Contingent Assets* to measure the liability at the amount an entity would rationally pay to settle the obligation at the balance sheet date. As a default accounting treatment, a remeasurement of a provision should be recognised in the income statement immediately. Therefore, the interpretative question is whether the requirements of IAS 16.15(e) should also apply to any remeasurement of the liability subsequent to the initial recognition.

We believe an approach that distinguishes a change in estimate between prior, current and future periods is inconsistent with paragraph 27 of IAS 8, *Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies*. We acknowledge the discussion in BC 16 regarding the IFRIC's interpretation of IAS 8, but believe such a view changes the notion of what is meant by "prospective application".

Therefore, we believe that a change in the estimated outflow of resources embodying economic benefits or a change in the current market assessment of the discount rate in accordance with IAS 37, should be accounted for over the remaining life of the asset(s). Additionally, any change related to an asset that has been fully depreciated or expensed in prior periods should be recognised in the income statement in the period of the change. This approach will not result in an inappropriate amount being capitalised as stated in BC 12, because the entity is required to recognise the asset at or below its recoverable amount in accordance with IAS 36. We also believe a remeasurement that increases the liability should trigger an impairment test of the related asset, therefore, we encourage IFRIC to give clarification in the final Interpretation.

Practical concerns

In addition to our comments above, we believe the current draft Interpretation may be difficult to implement in practice. Indeed, we have concerns where the decommissioning liability relates to a series of assets or revalued assets. For example, where a series of assets with different useful lives is related to a decommissioning liability, determination of the appropriate split between prior, current and future periods would be onerous and costly without any discernible benefit over a prospective approach.

If the Interpretation is issued in its present form, we believe the following should be clarified:

- How the proposed Interpretation applies where an asset is carried at its revalued amount either under IAS 16 or upon first-time adoption. In such cases, we would expect fair value (as defined) to include the expected costs of decommissioning. Consequently, an adjustment of an asset already carried at fair value for a change in the decommissioning costs, would result in a double counting of a portion of these costs. We believe this should be addressed by stating how the change should be adjusted against the revaluation reserve or the income statement as appropriate.
- Where the depreciation charge is capitalised (e.g. as part of the cost of inventory), whether or not these costs should be increased or reduced to reflect the adjustments made on prior period depreciation.
- Whether the term "asset" in 5(a) refers to the entire asset, or just the decommissioning layer of the asset?

Convergence

We note the IASB's current efforts to converge standards globally around high quality solutions. We understand that the requirements in IAS 8 in accounting for a change in estimate are similar to those requirements under current U.S. GAAP. That is, changes in estimates should be attributed to current and future periods and, therefore, accounted for “prospectively”. We also note that under FASB Statement No. 143 *Accounting for Asset Retirement Obligations* (SFAS 143), changes in estimated cash flows are accounted for as changes in estimate and, therefore, attributed to and accounted for in current and future periods. Therefore, the proposal in D2 would diverge from current U.S. GAAP. While we acknowledge that full convergence with U.S. GAAP is not possible given differences in the accounting for changes in current discount rates, we encourage the final interpretation to converge to the greatest extent possible with U.S. GAAP.

We note that IAS 37.47 requires the use of a discount rate that reflects "current market assessments of the time value of money". We acknowledge the difference between SFAS 143 and IAS 37 with respect to the determination of the discount rate. We believe the issue of discounting should be reconsidered as part of the IASB' s measurement project, particularly given the effect this Interpretation will have on profit and loss of those entities that have significant decommissioning liabilities.

Issue (c), unwinding of the discount

We agree that any increase in the liability to reflect the passage of time should be recognised in the income statement as explained in BC 25.

We appreciate the opportunity to provide our comments. If you have any questions concerning our comments, please contact Ken Wild in London at (020) 7007 0907.

Sincerely,

Deloitte Touche Tohmatsu