

Accounting Alert

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

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Recent Exposure Drafts

The Financial Reporting Standards Board (FRSB) continues to issue exposure drafts as part of the convergence process with International Financial Reporting Standards (IFRS). The following exposure drafts have been recently issued for comment:

ED NZ IAS-11: *Construction Contracts*

New Zealand Standard Affected

FRS-14: *Accounting for Construction Contracts*

Major Changes to Existing Practice

- There are no significant differences to current practice. The FRSB notes that the scope of ED NZ IAS-11 appears to be narrower than the current FRS-14 as it specifically applies to accounting for construction contracts in the financial statements of contractors, whereas FRS-14 applies to all construction contracts. However the FRSB states that it considers that any entity engaging in a construction contract is a contractor for the purposes of the proposed standard.
- Entities which currently apply differential reporting exemptions may need to comply with the full measurement requirements of the standard once the New Zealand financial reporting framework is determined.
- Additional disclosures are required – for example contract revenue recognised in the period, methods used to determine contract revenue recognised in the period, and methods used to determine the stage of completion of contracts in progress.

ED NZ IAS-16: *Property, Plant and Equipment*

New Zealand Standard Affected

FRS-3: *Accounting for Property, Plant and Equipment*

In addition some development properties currently accounted for under SSAP-17: *Accounting for Investment Properties and Properties Intended for Sale* will fall under ED NZ IAS-16.

Major Changes to Existing Practice

- FRS-3 allows revaluation movements to be offset within a class of property, plant and equipment – only net revaluation deficits are recognised as an expense. ED NZ IAS-16 does not allow the offset of revaluation gains and losses within classes. Each individual asset has to be separately accounted for with revaluation deficits below historical cost expensed and revaluation gains recognised in the revaluation reserve. This may result in a higher expense than under FRS-3.



For more information visit:

- IASplus.com - a Deloitte website detailing IFRS "as it happens" as well as reporting on the current and proposed output of the IASB.
- deloitte.co.nz for New Zealand based publications including this Accounting Alert.

ED NZ IAS-19: *Employee Benefits*

New Zealand Standard Affected

There is no current New Zealand standard.

Major Changes to Existing Practice

ED NZ IAS-19 outlines the accounting requirements for all forms of consideration given by an entity in exchange for employee services including short term benefits, post-employment benefits, other long-term benefits, termination benefits and equity compensation benefits.

The underlying principle is that the cost of providing employee benefits should be recognised in the period in which the benefit is earned by the employee, rather than when it is paid or payable.

Short term employee benefits

Recognise expense in the period the employee has rendered the service.

Post-employment benefits

Post employment benefits include defined contribution and defined benefit plans. Under defined contribution plans the entity's legal or constructive obligation is limited to the amount that it agrees to contribute. An expense/liability is recognised when an employee has rendered service in exchange for those contributions.

Under defined benefit plans the entity's obligation is to provide benefits as agreed to current and former employees. This exposes the entity to actuarial and investment risk. If benefits cost more than expected, or investment returns are worse than expected, an entity's obligation may be increased.

The amount recognised in the balance sheet comprises the present value of the defined benefit obligation (present value of expected future payments required to settle the obligation resulting from employee service in the current and prior periods), reduced by the fair value of any plan assets at balance date. The Projected Unit Credit Method must be used to determine the obligations.

A net asset may be recognised in certain circumstances. Currently IAS-19 permits a "corridor approach" which allows an entity to defer the recognition of certain actuarial gains and losses that fall within a defined "corridor". The IASB has indicated its intention to remove the corridor approach and require full recognition of the actuarial gains and losses, however the timing for this change is uncertain.

Other long-term benefits

Long term employee benefits should be recognised and measured in much the same way as benefits under a defined benefit plan.

Termination benefits

An entity should recognise termination benefits when it is demonstrably committed to either terminate an employee(s) employment before the normal retirement date, or provide termination benefits as a result of an offer made in order to encourage voluntary redundancy.

Equity compensation benefits

These benefits are where an employee is entitled to receive equity instruments issued by the entity (or its parent), or the amount of the entity's obligation to employees depends on the future price of the entity's equity instruments. The exposure draft requires disclosures - recognition and measurement requirements are contained in ED-2: *Share-Based Payment* (released as ED-93 in New Zealand).

ED-95: *Employee Benefits*

As there is no current New Zealand standard comparable to IAS-19, the FRSB proposes to adopt the requirements of IAS-19 (as released in ED NZ IAS-19) as a New Zealand Financial Reporting Standard (FRS) for periods beginning on or after 1 January 2005. As a result all entities preparing general purpose financial reports will need to comply with the FRS finalised from ED-95. ED-95 and ED NZ IAS-19 are substantially the same except for some transitional provisions and differential reporting concessions in ED-95. The corridor approach for defined benefit schemes is retained in ED-95.

The transitional requirements proposed in ED-95 require entities to recognise any revenue or expense adjustments in the statement of movements in equity as an adjustment against equity at the beginning of the period in which an entity first complies with the standard.

Entities with defined benefit plans must recognise the present value of the defined benefit obligation less the fair value of any plan assets at balance date.



The New Zealand Financial Reporting Standards Board will issue these standards as finalised converged NZ IAS/ NZ IFRS once the IASB has completed their work.

IASB Update

The IASB is committed to providing a "stable platform" for the transition to IFRS. This means issuing all the new and revised standards that entities will be required to comply with on adoption of IFRS by 31 March 2004. Any changes to standards, or new standards, released after 31 March 2004 will not be applicable for years beginning in 2005 in order to ensure that entities have a clear starting point.

By the end of 2003 the IASB plans to issue:

- The 12 finalised "improvements project" standards
- Amended IAS-32 and IAS-39 (without the proposed portfolio hedging amendments)
- Exposure draft on extractive industries.

By 31 March 2004 the IASB plans to issue finalised standards for:

- Share-based payments (ED-2)
- Business combinations - phase 1 (ED-3)
- Portfolio hedging (amendments to IAS-39)
- Insurance contracts - phase 1 (ED-5)
- Asset disposals and discontinued operations (ED-4)

Preliminary final drafts of the improvements standards are being made available on the IASB's secure site for subscribers. These 'preliminary final' standards may have some final changes made in the process to prepare printed versions. At present IAS 2, 10, 16, 17, 21, 24, 27, 28 and 40 are available.

Each final standard, basis for conclusions and implementation guidance will be available for purchase from the IASB.

Guidance Issued for Accounting by Trusts

In October the FRSB issued Exposure Draft *Guidance Notes on the Application of Generally Accepted Accounting Practice by Trusts*. The Trustees Act 1956 and case law requires Trustees to "keep proper accounts and records for a trust" and to "prepare accounts promptly and produce them whenever required by beneficiaries or their agents". Whether a trust should prepare general purpose financial reports, which are required to comply with generally accepted accounting practice (GAAP) will depend on a case by case basis and is not covered in this exposure draft. However the FRSB has noted that, especially with regard to trading or more complex trusts with differing classes of beneficiaries, the courts have indirectly supported general purpose financial statements which comply with professional accounting standards.

As a result, the FRSB has developed some guidance to assist trustees in complying with professional accounting standards when preparing general purpose financial reports for trusts, covering the following topics:

- The parties to a trust and the types of trusts
- Accountability and financial reporting
- Equity of the trust, including owners of a trust
- Acquisition, revaluation and disposal of assets by a trust
- Liabilities of a trust, including gifting by the settler, payments to beneficiaries, tax liabilities and post balance date events
- Presentation of financial statements and disclosure of related party transactions
- Consolidations, and
- Differential reporting.



The exposure draft may result in significant accounting changes by trusts

The guidance provided may result in significant accounting changes by trusts. For example, as the owners of a trust are the beneficiaries:

- payments made to a beneficiary are distributions to owners and must therefore be separately disclosed in the Statement of Movements in Equity.
- payments made to beneficiaries prior to a decision by the Trustees (which should be minuted) are advances and should be debited to the beneficiary's current account. A distribution can only be recognised when a distribution decision is made - otherwise there is no constructive obligation.
- the settlement of assets on a trust is not a contribution by an owner and must therefore be recognised as revenue.

The exposure draft is available from the Institute at www.icanz.co.nz. Submissions are due by 15 May 2004.

Important Dates

The FRSB's timetable is aligned to that of the IASB. As the IASB issues standards, the FRSB will issue them as NZ IAS or NZ IFRS having made additions, where necessary, to ensure the standards are sector neutral. As a result the NZ agenda is subject to change as deliberations of the IASB proceed.

An up to date timetable is available at: www.iasplus.com/agenda/timetabl.htm

Keep track of these important dates for responding on Exposure Drafts to the FRSB.

Comment Due 31 January 2004:

- ED NZ IFRS-1: *First-time Adoption of International Financial Reporting Standards*
- ED IAS-14: *Segment Reporting*
- ED FRS-34A: *Life Insurance Activities*
- ED FRS-35A: *Financial Reporting of Insurance Activities*

Comment Due 28 February 2004:

- ED NZ IAS-11: *Construction Contracts*
- ED NZ IAS-16: *Property, Plant and Equipment*
- ED NZ IAS-19: *Employee Benefits* / ED-95: *Employee Benefits*

All exposure drafts are available through the Institute's website: www.icanz.co.nz

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