



EUROPEAN COMMISSION

Internal Market and Services DG

FREE MOVEMENT OF CAPITAL, COMPANY LAW AND CORPORATE GOVERNANCE

Accounting

Brussels, 13 October 2009

MARKT F3 D(2009)

Endorsement of Amendment to
IFRS 1 Additional Exemptions for First-time Adopters

Introduction, background and conclusions

Attachment 1: Effect study prepared by the European Financial Reporting Advisory Group (EFRAG)

Attachment 2: Endorsement advice prepared by EFRAG

1. EFFECT STUDY

The European Commission has agreed with the European Parliament that Effect Studies should be prepared for new accounting standards and interpretations up for endorsement in the European Union (EU). The Commission Services together with the European Financial Reporting Advisory Group (EFRAG) prepare these studies containing description of the accounting issues involved, results from stakeholder consultations as well as analysis of effects of using the new accounting rules in the EU.

EFRAG has prepared an Effect Study for the Amendment to IFRS 1 *Additional Exemptions for First-time Adopters* (attached). As the EFRAG Effect Study refers to the Endorsement Advice, we also included it in attachments.

This cover note contains background information, comments and a conclusion by the Commission Services.

2. BACKGROUND ON THE AMENDMENT TO IFRS 1

Explanation of the issues

Generally when an entity prepares its first IFRS financial statements, it applies IFRS in full in its opening IFRS statement of financial position (i.e. balance sheet) when recognising and measuring assets and liabilities. However, IFRS 1 provides a limited number of exemptions and exceptions as a practical solution for certain implementation issues that arise on first-time adoption. The Amendment comprises three separate amendments, each of which introduces further or amends exemptions to existing IFRS for first-time adopters.

a) Deemed cost for oil and gas assets

Recognition and measurement of assets, depending on the accounting framework used, could be done at individual level (as required by international standard for 'Property, Plant and Equipment' – IAS 16) or at a more aggregated level (i.e. group of assets, as required by some local accounting rules). This issue, called "unit of account", is important because some individual items included in a group could not have been recognised on an individual level because they do not meet individually the criteria for such recognition. Thus depending of the unit of account applied, the items presented on the statement of financial position would not be the same.

Under some local accounting rules, it appears that for oil and gas activities the unit of account for some exploration and development costs is a large cost centre or geographical area. The first-time adoption of IFRS should have led to assessing if each items included in these groups meets the criteria for recognition on the statement of financial position, and if necessary, to re-measure them. However some information may not be available and so determining the opening IFRS financial statement of position would require significant extra work and cost.

b) Decommissioning, restoration and similar liabilities related to oil and gas assets above mentioned.

Under the international standard for 'Property, Plant and Equipment' – IAS 16, at inception and for any subsequent re-estimation, the cost of decommissioning and restoration related to an asset shall be added to the cost of this asset; in counterpart, a liability is recognised.

However, as mentioned above, the measurement of some assets related to oil and gas activities according to IFRS rules could raise difficulties at the date of transition to IFRS. Then the recognition of decommissioning and restoration costs against the cost of the asset could raise difficulties as well.

c) Reassessment of lease determination (independent from the two above-mentioned issues)

IFRIC 4 *Determining whether an Arrangement contains a Lease* specifies criteria for determining, at the inception of an arrangement and subsequently, whether it contains a lease.

Under existing IFRS, a first-time adopter can either apply IFRIC 4 retrospectively (and carry out re-assessments as required by IFRIC 4 for the periods before transition) or can apply it to arrangements existing at the start of the earliest period for which comparative information is presented on the basis of facts and circumstances existing at the start of that period.

It has been brought to the IASB's attention that some jurisdictions have national requirements that have the same effect as IFRIC 4, including the same transitional provisions. However, if a first-time adopter in such a jurisdiction has applied those requirements from a different date to the date in the transitional provisions of IFRIC 4, current IFRS would require the entity to reassess that accounting retrospectively on first-time adoption. The IASB believes this could result in additional costs with no obvious benefits.

How do the amended IFRS 1 suggest dealing with these issues?

a) Deemed cost for oil and gas assets

The Amendment allows entities with oil and gas activities moving to IFRS to use carrying amounts for oil and gas assets determined under their previous accounting rules. They further allow, for oil and gas assets used in the development and production phases, the entity to allocate the carrying amount of the cost centre as estimated under the previous local accounting rules on a pro rata basis to the underlying assets using either reserves quantities or values ('deemed cost' approach). In order to avoid overstatement, each underlying assets subsequently has to be tested for impairment.

b) Decommissioning, restoration and similar liabilities related to oil and gas assets above mentioned.

Those entities that use the exemption introduced by the current amendment to recognise and measure oil and gas assets will be required to measure decommissioning, restoration and similar liabilities in accordance with IFRS rules (IAS 37) and to recognise them against retained earnings (rather than by adjusting the cost of the assets).

c) Reassessment of lease determination (independent from the two above mentioned issues)

The Amendments provides an optional exemption for a first-time adopter to determine whether an arrangement contains a lease if the entity performed the same test under its previous accounting rules (provided that the application of their previous accounting rules would be expected to produce a similar result as IFRIC 4).

IASB and EFRAG consultations

The IASB carried out a consultation according to its due process. IASB published an exposure draft *Amendments to IFRS 1 First-time adoption of International Financial Reporting standards* on 25 September 2008 and received 96 comment letters. The final Amendments were issued on 23 July 2009

EFRAG consulted publicly on its endorsement advice. Commentators to the EFRAG consultation were supportive to the proposal to recommend endorsement of amendments of IFRS 1 "*First-time adoption of International Financial Reporting Standards*". EFRAG has also carried out an assessment of the likely costs and benefits of implementing the amendments.

3. EFFECT ANALYSIS

Main points identified in the EFRAG Effect Analysis

Improvement in consistency and in comparability

EFRAG's analysis concluded that this Amendment will enable more companies to adopt IFRS and over time result in greater comparability, even if it creates additional exemptions that could affect comparability in the short term.

Overall EFRAG concluded that the benefits arising from applying the amendments were likely to exceed the costs involved in its implementation.

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| <p>The Commission Services agree with the EFRAG analysis and conclude that the Amendment of IFRS 1 "<i>First-time Adoption of International Financial Reporting Standards</i>" will improve the overall quality and comparability of the financial information and therefore benefit users.</p> |
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Costs for preparers and users

EFRAG's analysis gives an overview of the expected incremental costs for preparers and users.

With regard to preparers, EFRAG concludes that one-time cost for the amendments related to 'Deemed cost for oil and gas assets' and 'Decommissioning, restoration and similar liabilities' will probably balance with each other (the former leading to incremental cost and the latter to cost savings). Concerning the third amendments, it should relieve a burden that currently exists for some entities.

With regards to users, on the one hand, the Amendment is likely to create additional but insignificant costs. However, on the other hand, the Amendment will make it possible for more entities to adopt IFRS and in consequence will strengthen the overall comparability of financial statements. As a result, EFRAG's overall assessment is that the Amendment would result in reduction in costs for users.

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| <p>EFRAG notes that the Amendment to IFRS 1 "<i>First-time Adoption of International Financial Reporting Standards</i>" is likely to result in benefits for both users and preparers. The Commission Services share this analysis.</p> |
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4. OVERALL COST-BENEFIT CONSIDERATIONS AND COMMISSION SERVICES CONCLUSIONS

On the basis of EFRAG's Effect Study, the Commission Services have considered the main costs and benefits of endorsing the Amendment to IFRS 1 "*First-time adoption of International Financial Reporting Standards*". The Services conclude that the benefits of the amendments outweigh the costs incurred.

The Commission services believe that the amendments to IFRS 1 will have positive cost-benefits effects and that they should therefore be endorsed in the EU without delay.



The costs and benefits of implementing the Amendments to IFRS 1 *Additional Exemptions for First-time Adopters*

Introduction

- 1 Following discussions between the various parties involved in the EU endorsement process, the European Commission decided in 2007 that more extensive information than hitherto needs to be gathered on the costs and benefits of all new or revised Standards and Interpretations as part of the endorsement process. It has further been agreed that EFRAG will gather that information in the case of the amendments to IFRS 1 *Additional Exemptions for First-time Adopters* (the Amendments).
- 2 EFRAG first considered how extensive the work would need to be. For some Standards or Interpretations, it might be necessary to carry out some fairly extensive work in order to understand fully the cost and benefit implications of the Standard or Interpretation being assessed. However, in the case of the Amendments, EFRAG's view is that the cost and benefit implications can be assessed by carrying out a more modest amount of work. (The results of the consultations EFRAG has carried out seem to confirm this.) Therefore, as explained more fully in the main sections of the report, the approach EFRAG has adopted has been to carry out an initial assessment of the likely costs and benefits of implementing the revision in the EU, to consult on the results of that initial assessment, and to finalise the assessment in the light of the comments received.

EFRAG's endorsement advice

- 3 EFRAG also carries out a technical assessment of all new and revised Standards and Interpretations issued by the IASB and IFRIC against the so-called endorsement criteria and provides the results of those technical assessments to the European Commission in the form of recommendations as to whether or not the Standard or Interpretation assessed should be endorsed for use in the EU. As part of those technical assessments, EFRAG gives consideration to the costs and benefits that would arise from implementing the new or revised Standard or Interpretation in the EU. EFRAG has therefore taken the conclusion at the end of this report into account in finalising its endorsement advice.

A summary of the Amendments

- 4 Generally when an entity prepares its first IFRS financial statements it applies IFRS in full in its opening IFRS statement of financial position when recognising and measuring assets and liabilities. However, IFRS 1 provides a limited number of exemptions and exceptions as a practical solution for certain implementation issues that arise on first-time adoption.

- 5 The Amendments comprise three separate amendments, each of which introduces further or amended exemptions to existing IFRS for first-time adopters.

Deemed cost for oil and gas assets

- 6 IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets* apply to the recognition and measurement of most assets under IFRS, including assets used in the development and production phases of oil and gas activities. IFRS 6 *Exploration and Evaluation of Mineral Resources* applies to the recognition and measurement of assets in the exploration and evaluation phases of oil and gas activities.
- 7 Certain entities with oil and gas activities are allowed under their local GAAP to recognise and measure assets using a different unit of account to that required under IFRS. These entities account for both exploration and development costs in large cost centres or geographical areas that might contain many oil and gas properties using a method often referred to as 'full cost accounting'. IAS 16 requires a smaller unit of account such as the individual property for oil and gas activities. As a result, the full cost method of accounting can include in the carrying amount of oil and gas assets unsuccessful exploration costs of prior periods that would have been expensed under IFRS.
- 8 Re-measuring oil and gas assets on first-time adoption in accordance with existing IFRS is difficult for some of these entities because either the information might not be available or the effort and associated costs to determine the opening IFRS statement of financial position might be very high.
- 9 The Amendments allow entities with oil and gas activities to transition to IFRS using carrying amounts for oil and gas assets determined under their previous GAAP. They further allow, for oil and gas assets used in the development and production phases, the entity to allocate the previous GAAP carrying amount of the cost centre on a pro rata basis to the underlying assets using either reserves quantities or values. The Amendments refer to this as measuring the assets at 'deemed cost'.
- 10 The Amendments ensure that the resulting asset amounts are not overstated by requiring them to be tested for impairment at the date of transition in accordance with IAS 36 *Impairment of Assets*.

Decommissioning, restoration and similar liabilities

- 11 IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* requires that an entity recognises a liability for the future costs to dismantle, remove and restore assets when it has an obligation to do so. IAS 16 requires the initial estimate of the amount of that liability to also be included as part of the cost of an item of property, plant and equipment. IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities* sets out the requirements that apply on the subsequent re-measurement of the obligation because of changes in the estimated future cash flows needed to settle the obligation. It explains that, if the assets are being measured on a cost basis, the remeasurement of the obligation should be adjusted against the carrying amount of the asset.
- 12 Although IFRS 1 already includes an exemption for first-time adopters from IFRIC 1's requirements for changes in existing decommissioning, restoration and similar liabilities that occurred before the date of transition to IFRS, the deemed cost exemption described above creates further issues for first-time adopters that are not addressed by that existing exemption. The Amendments address these issues by requiring an entity

that uses the deemed cost exemption to measure decommissioning, restoration and similar liabilities as at the date of transition to IFRS in accordance with IAS 37 and recognise directly in retained earnings (rather than by adjusting the cost of the asset) any difference between that amount and the amount of the liability under the entity's previous GAAP.

Reassessment of lease determination

- 13 IFRIC 4 *Determining whether an Arrangement contains a Lease* specifies criteria for determining, at the inception of an arrangement, whether it contains a lease. It also specifies when an arrangement should be subsequently reassessed.
- 14 Under existing IFRS, a first-time adopter can either apply IFRIC 4 retrospectively (and carry out re-assessments as required by IFRIC 4 for the periods before transition) or can apply it to arrangements existing at the start of the earliest period for which comparative information is presented on the basis of facts and circumstances existing at the start of that period.
- 15 It has been brought to the IASB's attention that some jurisdictions have national requirements that have the same effect as IFRIC 4, including the same transitional provisions. However, if a first-time adopter in such a jurisdiction has applied those requirements from a different date to the date in the transitional provisions of IFRIC 4, existing IFRS would require the entity to reassess that accounting retrospectively on first-time adoption. The IASB believes this could result in additional costs with no obvious benefits.
- 16 The Amendments seek to address this issue by providing an optional exemption for a first-time adopter if the entity made the same determination of whether an arrangement contains a lease under its previous GAAP, provided that the application of their previous GAAP would be expected to produce a similar result as IFRIC 4.

Effective date

- 17 Entities are required to apply the Amendments for annual periods beginning on or after 1 January 2010. Earlier application is permitted but must be disclosed.

EFRAG's initial analysis of the costs and benefits of the amendments to IFRS 1

- 18 EFRAG carried out an initial assessment of the costs and benefits expected to arise for preparers and for users both in year one and in subsequent years from implementing the Amendments in the EU.
- 19 The tentative conclusions reached about additional costs for preparers were that:
 - (a) the deemed cost and decommissioning, restoration and similar liability amendments are likely to be cost neutral for the preparers affected both in year one and on an ongoing basis; an
 - (b) the lease determination amendment is likely to result in year one cost savings for the preparers affected and no change in their ongoing costs.

Furthermore, as entities have a choice as to whether they implement the Amendments, EFRAG believed it could be assumed that an entity will implement one or more of the amendments set out only if it believes the benefits to it of implementation are likely to exceed the implementation costs involved.

- 20 EFRAG also tentatively concluded that the Amendments will involve users in additional but insignificant year one costs and ongoing costs. However, the Amendments will make it possible for more entities to adopt IFRS, and EFRAG's initial assessment was that will result in a significant reduction in costs for users. As a result, EFRAG's overall initial assessment was that the Amendments would result in reduction in costs for users.
- 21 As a result, EFRAG's overall tentative conclusion was that the benefits to be derived from implementing the Amendments in the EU are likely to exceed the costs involved.
- 22 EFRAG published its initial assessment and supporting analysis on 7 September 2009 and invited comment on the material by 7 October 2009. The results of this consultation can be summarised as follows:
- (a) where specific responses to the questions posed were provided by the respondents, respondents agreed with EFRAG's initial assessment as summarised above; and
 - (b) none of the other respondents indicated that they disagreed with EFRAG's initial assessment.

EFRAG's final analysis of the costs and benefits of the amendments to IFRS 1

- 23 Based on its initial analysis and on stakeholders' views on that analysis, EFRAG's detailed final analysis of the costs and benefits of implementing the Amendments in the EU is presented in the paragraphs below
- 24 IFRS 1 sets out exemptions to the normal requirements of IFRS that can be applied when an entity prepares its first set of financial statements in compliance with IFRS. The exemptions in IFRS 1 provide some relief from the normal requirements that would otherwise apply in order to ensure that the costs of adopting IFRS do not exceed the benefits.
- 25 The Amendments include additional exemptions in IFRS 1. The IASB's intention is that the additional exemptions in the Amendments should provide relief from the full retrospective application of IFRS for the measurement of oil and gas assets and for the determination of whether an arrangement involves a lease.

Costs for preparers

Deemed cost for oil and gas assets and implications for decommissioning, restoration and similar liabilities

- 26 EFRAG believes that an entity electing to take advantage of the deemed cost exemption available under the Amendments would be required for each oil and gas property to:
- (a) determine an amount to allocate to the property based on its pro rata share of reserve quantities or reserve values, and
 - (b) determine a 'value in use' under IAS 36 for the property as part of a transition date impairment test.
- 27 EFRAG thinks the cost to preparers of using fair value as the deemed value of oil and gas assets would be approximately the same as the cost to determine a 'value in use' under IAS 36. Thus, because the deemed cost approach involves calculating value in

use and doing some other things (determining an amount to allocate to oil and gas assets and carrying out an impairment test), EFRAG's assessment is that, compared to the existing fair value exemption, there will be an incremental one-time cost incurred by a preparer electing to measure its oil and gas properties at deemed cost.

- 28 Entities that elect to use the deemed cost exemption would be required to recognise any difference as at the IFRS transition date between decommissioning, restoration and similar liabilities measured in accordance with IAS 37 and those liabilities measured under their predecessor GAAP directly in retained earnings. EFRAG believes this additional requirement will provide one-time cost savings to those preparers as they will not need to estimate the amount that would have been included in the cost of the asset when the liability first arose and the subsequent accumulated depreciation.
- 29 EFRAG believes the additional costs referred to in paragraph 27 above and the cost savings referred to in paragraph 28 will probably broadly balance each other out.
- 30 EFRAG's assessment is that the deemed cost and decommissioning, restoration and similar liability amendments will involve preparers in no additional ongoing costs.
- 31 Perhaps more importantly, EFRAG notes that entities are not forced to use these amendments—they are optional—and will therefore use them only when they perceive the benefits to exceed the costs they will incur in implementing them.

Reassessment of lease determination

- 32 The third amendment imposes no additional burdens on preparers; rather, it relieves a burden than currently exists for some entities. EFRAG's assessment is that this will result in year one cost savings for those preparers affected by the amendment. It is unlikely that there will be any ongoing cost implications.

Costs for users

- 33 Prior to the deemed cost amendment, users would have had to deal with some entities using fair value and some using IFRS-based cost. Now some entities might use a deemed cost which could be calculated in a multitude of different ways. So, there will be a comparability issue; and in many cases also a quality of information (ie relevance) issue because deemed cost will not be as good a number as the number IFRS would have required an entity to present prior to the amendment. Thus, users are likely to incur additional analysis costs, both in year one and on an ongoing basis, to manage the comparability issue and to overcome the relevance issue. The other two amendments will have similar implications. EFRAG's assessment is however that these additional costs will not be significant.
- 34 Furthermore, EFRAG notes that the Amendments make it possible for such companies to transition to IFRS, and the more entities that are on the same set of accounting requirements, the lower the costs for users. EFRAG's assessment is that the result is likely to be significantly reduced costs for users.
- 35 EFRAG's overall assessment is that the benefits for users described in the preceding paragraph are likely to outweigh the additional costs for users described in paragraph 33.

Benefits for preparers and users

36 EFRAG's assessment is that the Amendments will not result in any benefits to preparers or users not already taken into account in the above assessments.

Conclusion

37 EFRAG's overall assessment is therefore that:

- (a) implementing the deemed cost and decommissioning, restoration and similar liability amendments is likely to be cost neutral, both in year one and on an ongoing basis, and implementing the lease determination amendment will result in year one cost savings and no change in ongoing costs. In any event, implementing the Amendments is optional, so preparers will implement them only if they believe the benefits that are likely to arise from implementation will exceed their implementation costs;
- (b) the Amendments are likely to involve users in additional but insignificant costs. On the other hand, the Amendments will make it possible for more entities to adopt IFRS, and EFRAG's assessment is that overall users will benefit from the Amendments.

38 EFRAG's assessment is therefore that the benefits arising from implementation of the Amendments in the EU are likely to exceed the costs of implementation.

39 During its consultation process, EFRAG did not become aware of any other factors that should be taken into account in assessing the costs and benefits of implementing the Amendments in the EU.

Stig Enevoldsen
EFRAG, Chairman
9 October 2009

Attachment 2



Jörgen Holmquist
Director General
European Commission
Directorate General for the Internal Market
1049 Brussels

9 October 2009

Dear Mr. Holmquist

Adoption of the Amendments to IFRS 1 *Additional Exemptions for First-time Adopters*

Based on the requirements of the Regulation (EC) No 1606/2002 of the European Parliament and of the Council on the application of international accounting standards, we are pleased to provide our opinion on the adoption of the Amendments to IFRS 1 *Additional Exemptions for First-time Adopters* (the Amendments), which were published in July 2009. The Amendments were proposed in an exposure draft on which EFRAG commented.

IFRS 1 provides guidance on the initial adoption of IFRS and, in doing so, provides a limited number of exemptions and exceptions as a practical solution for certain implementation issues that arise on first-time adoption. The Amendments introduce three new exemptions to existing IFRS for first-time adopters.

- One amendment provides for a new 'deemed cost' exemption for certain oil and gas assets.
- A second amendment is related to the first amendment and requires an entity that uses the deemed cost exemption to recognise directly in retained earnings any difference between the amount of decommissioning, restoration and similar liabilities as calculated under IFRS and the amount of the liability as calculated under the entity's previous GAAP.
- The third amendment provides an exemption from the requirement to carry out on transition to IFRS an IFRIC 4 assessment to determine whether the entity's arrangements contain leases if application an entity's previous GAAP would be expected to produce a similar result as IFRS.

The Amendments will apply for entities transitioning to IFRS for the first time for annual periods beginning on or after 1 January 2010.

EFRAG has carried out an evaluation of Amendments. As part of that process, EFRAG issued a draft assessment of the Amendments against the EU endorsement criteria for public comment and, when finalising its advice and the content of this letter, took the comments received in response into account. EFRAG's evaluation is based on input from standard setters, market participants and other interested parties, and its discussions of technical matters are open to the public.

EFRAG supports the Amendments and has concluded that they meet the requirements of Regulation (EC) No 1606/2002 of the European Parliament and of the Council on the application of international accounting standards in that:

- they are not contrary to the 'true and fair principle' set out in Article 16(3) of Council Directive 83/349/EEC and Article 2(3) of Council Directive 78/660/EEC; and
- they meet the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management.

For the reasons given above, EFRAG believes that it is in the European interest to adopt the Amendments and, accordingly, EFRAG recommends their adoption. EFRAG's reasoning is explained in the attached 'Appendix – Basis for Conclusions'.

On behalf of the members of EFRAG, I should be happy to discuss our advice with you, other officials of the EU Commission or the Accounting Regulatory Committee as you may wish.

Yours sincerely

Stig Enevoldsen
EFRAG, Chairman

Appendix Basis for Conclusions

This appendix sets out the basis for the conclusions reached and for the recommendation made by EFRAG on the Amendments to IFRS 1 First-time Adoption of International Financial Reporting Standards: Additional Exemptions for First-time Adopters.

In its comment letters to the IASB, EFRAG points out that such letters are submitted in EFRAG's capacity as a contributor to the IASB's due process. They do not necessarily indicate the conclusions that would be reached by EFRAG in its capacity as advisor to the European Commission on endorsement of the final IFRS or Interpretation on the issue.

In the latter capacity, EFRAG's role is to make a recommendation about endorsement based on its assessment of the final IFRS or Interpretation against the European endorsement criteria, as currently defined. These are explicit criteria which have been designed specifically for application in the endorsement process, and therefore the conclusions reached on endorsement may be different from those arrived by EFRAG in developing its comments on proposed IFRSs or Interpretations. Another reason for a difference is that EFRAG's thinking may evolve.

- 1 The Amendments to IFRS 1 *First-time Adoption of International Financial Reporting Standards: Additional Exemptions for First-time Adopters* (the Amendments) introduce three new exemptions to existing IFRS for first-time adopters. When evaluating the Amendments, EFRAG considered the following questions:
 - (a) Are the Amendments needed?
 - (b) Does the accounting that results from the application of the Amendments meet the criteria for EU endorsement?
- 2 Having formed tentative views on these issues and prepared a draft assessment, EFRAG issued that draft assessment on 7 September 2009 and asked for comments on it by 7 October 2009. EFRAG has considered all the comments received, and all were supportive of EFRAG's tentative conclusion that the Amendments met the EU endorsement criteria and EFRAG should recommend their endorsement.

Are the Amendments needed?

Deemed cost for oil and gas assets

- 3 The amendment, that allows entities transitioning to IFRS that use full cost accounting for their oil and gas assets to use deemed cost for those assets, is intended to provide relief in circumstances in which the information needed to determine IFRS cost is not available or, if the information is available, the costs to determine IFRS amounts are very high.
- 4 In such circumstances, under existing IFRS the entity is currently permitted to measure the assets at their transition date fair value. However, as the IASB explains in paragraph BC47B of the Amendments' Basis for Conclusions:

Determining the fair value of oil and gas assets is a complex process that begins with the difficult task of estimating the volume of reserves and resources. When the fair value amounts must be audited, determining significant inputs to the estimates generally requires the use of qualified external experts.

For entities with many oil and gas assets, the use of this fair value as deemed cost alternative would not meet the Board's stated intention of avoiding excessive cost (see paragraph BC41).

The IASB therefore concluded that it needed to amend IFRS 1 to introduce a third measurement basis to the options currently available.

- 5 In EFRAG's view, this third measurement basis might not be less costly than the existing fair value alternative but it is nevertheless needed to enable certain entities with oil and gas activities to transition to IFRS.

Decommissioning, restoration and similar liabilities

- 6 The amendment described above has consequences for the accounting treatment of changes in decommissioning, restoration and similar liabilities relating to oil and gas assets. Under existing IFRS, if those assets are accounted for on a cost basis, changes in related decommissioning, restoration and similar liabilities are accounted for by adjusting the asset's cost. However, if a first-time adopter is required to recognise a different amount of decommissioning, restoration and similar liabilities on transitioning to IFRS to the amount recognised immediately prior to transition, it cannot adjust that change to its liabilities against the asset's carrying amount if it also wishes to apply the deemed cost exemption (because the adjusted amount would not be deemed cost as defined).
- 7 EFRAG's assessment is that the IASB is correct in concluding that the result is that a consequential amendment needs to be made to the accounting treatment of changes in decommissioning, restoration and similar liabilities relating to oil and gas assets.

Reassessment of lease determination

- 8 The third amendment relates to the application of IFRIC 4 *Determining whether an Arrangement contains a Lease*. The IASB has identified a circumstance in which existing IFRS would require entities transitioning to IFRS to in effect re-apply the requirements they have been applying prior to IFRS, albeit with different 'as at' date. The IASB believes this could result in additional costs with no obvious benefits, and that an exemption is needed to prevent such a situation arising. EFRAG's assessment is that the IASB's analysis and conclusions are correct.

Does the accounting that results from the application of the Amendments meet the criteria for EU endorsement?

- 9 EFRAG has considered whether the Amendments meet the requirements of the European Parliament and of the Council on the application of international accounting standards, in other words that the Amendments:
 - are not contrary to the 'true and fair principle' set out in Article 16(3) of Council Directive 83/349/EEC and Article 2(3) of Council Directive 78/660/EEC; and
 - meet the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management.

EFRAG has also considered whether it is in the European interest to adopt the Amendments.

Comparability

- 10 The notion of comparability requires that like items and events are accounted for in a consistent way through time and by different entities, and that unlike items and events should be accounted for differently.
- 11 Existing IFRS permits entities to use one of two measurement bases for their oil and gas assets when transitioning to IFRS. The deemed cost amendment introduces a third measurement basis (deemed cost) for certain types of assets. Having a third possible measurement basis might initially reduce comparability (between first-time adopters and between first-time adopters and entities that already apply IFRS). On the other hand, EFRAG believes the amendment will make it possible for more entities to adopt IFRS and, as more entities apply the same set of standards, the more comparable financial statements will become generally. Indeed, IFRS 1 in its entirety involves compromising of comparability in the short-term, but by doing so it enables more entities to adopt IFRS; thus resulting over time in greater comparability. Similarly, the other two amendments might initially reduce comparability to a degree, but they also make it possible for more entities to adopt IFRS and, as such, to achieve greater comparability in the long-term
- 12 As a result, EFRAG's overall assessment is that the Amendments meet the comparability criterion.

Relevance

- 13 According to the Framework, information has the quality of relevance when it influences the economic decisions of users by helping them evaluate past, present or future events or by confirming or correcting their past evaluations.
- 14 EFRAG considered whether the Amendments would result in the provision of relevant information; in other words, information that has predictive value, confirmatory value or both. EFRAG's assessment about the Amendments' relevance is very similar to its assessment of comparability; there might be a slight, short-term deterioration in relevance, but it will make it possible for more entities to adopt IFRS, which will result in an overall improvement in the relevance of the information provided. For that reason, EFRAG's overall assessment is that the Amendments meet the relevance criterion.

Reliability

- 15 EFRAG also considered the reliability of the information that will be provided by applying the Amendments. The Framework explains that information has the quality of reliability when it is free from material error and bias and can be depended upon by users to represent faithfully that which it either purports to represent or could reasonably be expected to represent, and is complete within the bounds of materiality and cost.
- 16 The Amendments do not require any amounts to be estimated that are not being estimated currently under existing national requirements, which in the EU's case means national

requirements that are in accordance with the EU Accounting Directives. In EFRAG's view, such amounts will not give rise to reliability concerns.

Understandability

- 17 The notion of understandability requires that the financial information provided should be readily understandable by users with a reasonable knowledge of business and economic activity and accounting and the willingness to study the information with reasonable diligence. Although there are a number of aspects to the notion of 'understandability', EFRAG believes that most aspects are covered by the discussion above about relevance, reliability and comparability (because, for example, information that represents something as similar when it is in fact dissimilar is not comparable, and that lack of comparability will mean it is also not understandable). As a result, EFRAG believes that the main additional issue it needs to consider in assessing whether the information resulting from the application of the Amendments is understandable is whether that information will be unduly complex.
- 18 In EFRAG's view, the Amendments do not introduce any new complexities into the financial statements.

True and fair view

- 19 EFRAG has also concluded that there is no reason to believe that the information resulting from the application of the Amendments would be contrary to the true and fair view principle.

European interest

- 20 EFRAG is not aware of any reason to believe that it is in the European interest not to adopt the Amendments.

Conclusion

- 21 For the reasons set out above, EFRAG has concluded that the Amendments satisfy the criteria for EU endorsement and that EFRAG should recommend their endorsement.