10 November 2008

To: Members of the Hong Kong Institute of CPAs
All other interested parties

INVITATION TO COMMENT ON IASB EXPOSURE DRAFT OF *PROPOSED AMENDMENTS TO IFRS 1 – ADDITIONAL EXEMPTIONS FOR FIRST-TIME ADOPTERS*

Comments to be received by 6 January 2009

The Hong Kong Institute of Certified Public Accountants' (Institute) Financial Reporting Standards Committee (FRSC) is seeking comments on the IASB Exposure Draft which has been posted on the Institute's website at:
www.hkicpa.org.hk/professionaltechnical/accounting/exposuredraft/content.php.

The Exposure Draft proposes amendments to IFRS 1 *First-time Adoption of International Financial Reporting Standards*. The proposals address the retrospective application of IFRSs in selected areas and are aimed at ensuring that entities applying IFRSs will not face undue cost or effort in the transition process.

The Exposure Draft proposes:

- to exempt companies from retrospective application of IFRSs for oil and gas assets using the full cost method and for operations subject to rate regulation; and

- to exempt companies with existing leasing contracts accounted for in accordance with IFRIC 4 *Determining whether an Arrangement contains a Lease* from reassessing the classification of those contracts according to IFRSs when the same classification has previously been made in accordance with national GAAP.

--- A summary of the main proposals in the Exposure Draft is set out in the Appendix.

In accordance with the Institute's Convergence Due Process, comments are invited from any interested party. The FRSC would like to hear from both those who do agree and those who do not agree with the proposals contained in the IASB Exposure Draft.

Comments should be supported by specific reasoning and should be submitted in written form.

To allow your comments on the IASB Exposure Draft to be considered, they are requested to be received by the Institute on or before **6 January 2009**.

Comments may be sent by mail, fax or e-mail to:

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Comments will be acknowledged and may be made available for public review unless otherwise requested by the contributor.

Appendix

<u>Summary of the main proposals in the Exposure Draft</u>

(1) Deemed cost for oil and gas assets and for operations subject to rate regulation

(a) Deemed cost for oil and gas assets

The Exposure Draft proposes that an entity that used the full cost method (that is, exploration and development costs for properties in development or in production are accounted for in cost centres that include all properties in a large geographical area) for oil and gas assets under its previous GAAP may elect, at the date of transition to IFRSs:

- to measure its exploration and evaluation assets using amounts determined under previous GAAP; and
- to measure oil and gas assets in the development or production phases by allocating the amount determined under previous GAAP to the underlying assets on a pro rata basis using reserve volumes or reserve values as of the date of transition to IFRSs.

Entities would also be required to test exploration and evaluation assets and oil and gas assets in the development and production phases for impairment at the date of transition to IFRSs in accordance with IFRS 6 *Exploration for and Evaluation of Mineral Resources* and IAS 36 *Impairment of Assets* respectively and to recognise any identified impairment loss.

If an entity uses the exemption described above, it must disclose that fact and the basis on which it allocated the carrying amounts to the underlying assets.

(b) Deemed cost for assets used in operations subject to rate regulation

The Exposure Draft also proposes an exemption that would allow an entity subject to rate regulation to use carrying amount of items of property, plant and equipment under previous GAAP as their deemed cost at the date of transition to IFRSs. However, the exemption would be available only when both retrospective restatement and using fair value as deemed cost are impracticable. An entity would apply this election on an item-by-item basis.

For the purpose of the proposed exemption, operations are subject to rate regulation if they provide services or products to customers at prices (that is, rates) established by legislation, an independent regulator or other authorised body that are designed to recover the cost of providing the services or products and allow the entity to earn a determined return on investment.

At the date of transition to IFRSs, an entity shall test each item for which this exemption is used for impairment in accordance with IAS 36 and to recognise any identified impairment loss.

(2) Reassessment of whether an arrangement contains a lease

Under IFRIC 4 *Determining whether an Arrangement contains a Lease*, the assessment as to whether an arrangement contains a lease is made at the inception of the arrangement. IFRS 1 currently permits an exemption for first-time adopters which allows them to undertake that assessment for existing arrangements based on facts and circumstances at the date of transition to IFRSs. However, if this exemption is not availed of, the entity is required to refer to facts and circumstances at the inception of the arrangement.

The Exposure Draft acknowledges that some entities may have previously applied IFRIC 4 (or an identical requirement) at a date other than the inception of the arrangement and proposes that such entities should not be required to reassess that conclusion when they adopt IFRSs.