Guide to International Financial Reporting Standards in Canada

IAS 16 *Property, Plant and Equipment*

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IAS 16
Property, Plant and Equipment

Preface

This publication is part of the Guide to International Financial Reporting Standards in Canada series published by the Chartered Professional Accountants of Canada (CPA Canada) to support its members.

The objective of this publication, IAS 16 Property, Plant and Equipment, is to help you understand IAS 16 and the IASB material that accompanies it. The publication begins with an introduction and standards update and then includes definitions, an overview chart, an analysis section, a section on accounting policies and one on significant judgments and estimates.

Every attempt has been made to use plain language and to avoid mere restatement of the IFRS standards although, where deemed necessary, specific wording from the standards is referred to.

This publication has been carefully prepared, but it necessarily contains information in summarized form and is, therefore, intended for general guidance only. It is not intended to be a substitute for detailed research or the exercise of professional judgment.

The overview section takes a high-level look at the key requirements of the standard in a chart format (the Overview chart). Specific “touchstone” references to IAS 16 are included in the Overview chart to help you navigate the standard. These are not meant to be comprehensive references, rather a
starting point for your research. The Analysis section analyzes the more com-
plex areas of the standard in more depth. Note that, where parts of the stan-
dard are more straightforward, they are included in the Overview chart only
as it is felt that this coverage is at a sufficient level.

Illustrations, examples and extracts have been used to explain a particular
concept and/or provide insight into how the standard is applied. Financial
statement note extracts have been selected to illustrate a particular point
but do not necessarily represent best practices.

Several features have been included to enhance understanding as follows:

1. Illustrations, including the following:
   - charts
   - decision trees
   - summaries

   These illustrations add value by summarizing, grouping, highlighting simi-
larities/differences and working through decision processes in applying
the standard.

2. Examples
   - IASB Illustrative Examples excerpts
   - IASB examples excerpted from the standard
   - other examples

   These examples add value by showing how a particular part of the standard
might be applied in a specific situation. Note that IAS 16 does not include
any illustrative examples and therefore the examples included in this publi-
cation are not authoritative.

3. Extracts from the IASB standards, including the following:
   - definitions
   - select quotes

   Even though every attempt has been made to use plain language, in some
cases, it has been important to use the specific wording in the standard to
get a point across.

4. Extracts from financial statements—financial statements of prominent
Canadian companies have been selected, including those that were recipi-
ents of the CPA Canada Corporate Reporting Awards. The report on the
Corporate Reporting Awards, including a list of winners, may be found at
www.cpacanada.ca.

The extracts included illustrate a particular aspect. It may be useful to
review the complete note, which may be found at www.sedar.com.
5. Non-IFRS Interpretations Committee insights—Items discussed but not taken to the IASB agenda, referred to as NIFRICs (Non-IFRICs), have been included because, in some cases, they provide insights into the standard setting decision processes.

6. IFRS Discussion Group (IDG) insights—references to IDG discussions. The IDG was established by the Canadian Accounting Standards Board (AcSB) in 2009. Its aim is to provide a public forum for the discussion of issues relating to IFRSs and to collect the views of Canadians experiencing issues in implementing IFRSs. These discussions are not meant to provide authoritative guidance; however, they do help clarify issues and allow interested parties to learn how others are working through their financial reporting issues and applying judgment in the application of IFRSs. These have been drawn from the publically available reports of the IDG meetings. The IDG’s meetings are recorded and audio webcasts are archived on the AcSB website (www.frascanada.ca). Discussants include preparers, practitioners, regulators and users of financial statements.

7. References to other relevant CPA Canada material.

8. This publication is part of a series with various publication dates. The dates have been noted on each publication.

Where necessary, icons have been used throughout the publication to refer to many of these features so the reader can easily distinguish the sources of the information.

Application insights explain, discuss and/or debate a particular IFRS application issue.

Application insights include:
• NIFRICs (Non-IFRICs)
• IFRS Discussion Group reports

Viewpoints refer to the Viewpoints: Applying IFRSs in the Mining Industry or the Viewpoints: Applying IFRSs in the Oil and Gas Industry—a series of papers that addresses specific IFRS application issues.

Examples illustrate how a particular part of an IFRS might be applied in a specific situation.
Statistics on particular IFRS application practices highlight common practices and/or application approaches.

Resources include references to other relevant CPA Canada material.

**Research Resources**
CPA Canada has compiled various IFRS technical summaries, practical application guides and frequently-asked-question documents aimed at supporting the understanding and application of IFRSs. For more information on IFRSs visit our website.

**Notice to Readers**
The Research, Guidance and Support Group of the Chartered Professional Accountants of Canada (CPA Canada) commissioned this publication as part of its continuing research program. The views and conclusions expressed in this publication are those of the authors. They have not been adopted, endorsed, approved or otherwise acted upon by a Board or Committee of CPA Canada or any Provincial Institute / Ordre. CPA Canada and the authors do not accept any responsibility or liability that might occur directly or indirectly as a consequence of the use, application or reliance on this material.
Introduction to IAS 16

IAS 16 prescribes the accounting treatment for property, plant and equipment (PP&E) held for use in the production or supply of goods or services, for rental to others or for administrative purposes, that are expected to be used for more than one period. IAS 16 allows an accounting policy choice for PP&E: items may be carried at cost or at a revalued amount.

IAS 16 provides guidance on what may, and what may not, be considered PP&E, the recognition and measurement of initial and subsequent costs and the derecognition of an item of PP&E.

IAS 16 includes a Basis for Conclusions document that summarizes the International Accounting Standards Board’s (IASB) considerations and conclusions in the development of this standard. IAS 16 does not include any illustrative examples.

The costs to dismantle, remove and restore items of PP&E are included in the carrying amount of the asset. IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*, provides guidance on accounting for the effect of changes in the measurement of existing decommissioning liabilities and discusses the related impact on PP&E.

IFRIC 18 *Transfers of Assets from Customers*, applies to the accounting for transfers of items of PP&E by entities that receive such transfers from their customers. This IFRIC provides guidance on the recognition and measurement of such asset transfers.

This publication is based on the requirements of IFRS standards and interpretations for annual periods beginning January 1, 2013. Where appropriate, for illustration purposes, certain note-disclosure examples are presented from financial statements with annual periods ending before January 1, 2013.

**This publication has not been updated since the publication date of June 2013. Readers are cautioned that certain aspects of IFRSs may have changed since the publication date.**
Standards Update

IASB

Methods of Depreciation and Amortization
In December 2012, the IASB issued an Exposure Draft (ED), Clarification of Acceptable Methods of Depreciation and Amortization (Proposed Amendments to IAS 16 and IAS 38), based on a submission from the IFRS Interpretations Committee. IAS 16.60 requires the depreciation method to reflect the pattern in which an asset’s future economic benefits are expected to be consumed. The proposed revisions are intended to clarify that revenue-based methods are not acceptable methods of depreciating or amortizing an item of PP&E or an intangible asset. This is because a revenue-based method reflects the economic benefits being generated from an asset rather than the expected pattern of consumption of the asset.

The proposed amendment also provides further guidance on the application of the diminishing balance method of depreciation. This proposed guidance clarifies that information about technical or commercial obsolescence of the output of the asset (product or service) is relevant for estimating the pattern of consumption of future economic benefits and the useful life of the asset. As an example, the ED notes that an expected future reduction in the unit selling price of the output, as a result of technical or commercial obsolescence, could be an indication of the diminution of the future economic benefits of the asset.

The comment period on this ED closed April 2, 2013, and the expected completion date is the fourth quarter of 2013.

Bearer Biological Assets
The IASB has a limited-scope project to amend IAS 41 to address bearer biological assets (e.g., grapevines, dairy cows, etc.). These assets are accounted for under IAS 41 at fair value less costs to sell based on the principle that the transformation of bearer biological assets is best reflected by fair value measurement. The counter argument is that mature bearer biological assets are not going through biological transformation and, as such, are similar to manufacturing assets and should be accounted for under IAS 16.

This project will focus on measurement of bearer biological assets that are plants. This ED was issued on June 26, 2013, and was available for comment until October 28, 2013.
Annual Improvements

2010—2012 cycle (ED issued May 2012)

The IASB proposes an amendment to IAS 16 to address concerns about the computation of accumulated depreciation at the date of a revaluation of PP&E for entities that apply the revaluation method to account for PP&E. The concern stems from differing practices in computing accumulated depreciation for a revalued item where the residual value, the useful life or the depreciation method is re-estimated before a revaluation.

When an item of PP&E is revalued, IAS 16 currently allows entities a choice to (1) restate accumulated depreciation proportionately with the change in the gross carrying amount of the asset, or (2) eliminate accumulated depreciation against the gross carrying amount of the asset. A problem arises with the use of method (1) if the residual value, useful life or depreciation method is re-estimated before a revaluation adjustment. In these situations, the restatement of accumulated depreciation proportionately would not result in the carrying amount of the asset being equal to the revalued asset amount less the revalued accumulated depreciation. The proposed amendment to IAS 16 (and IAS 38) would state that the accumulated depreciation is computed as the difference between the gross and net carrying amounts. The proposed amendment would also clarify that the determination of accumulated depreciation does not depend on the selection of the valuation technique.

A similar amendment is proposed in IAS 38 for intangible assets measured using the revaluation model.

It is expected that this amendment will be approved and issued in the fourth quarter of 2013 and will be effective for annual periods beginning on or after January 1, 2014, with early adoption permitted.

IFRIC

The Interpretations Committee received a request to address an issue related to contractual arrangements within the scope of IFRIC 12, Service Concession Arrangements. This request is to clarify in what circumstances contractual payments made by an operator under a service concession arrangement should:
1. be included in the measurement of an asset and liability at the start of the concession; or
2. be accounted for as executory in nature (i.e., be recognized as expenses as incurred over the term of the concession arrangement).
At the January 2013 meeting, the Interpretations Committee tentatively decided to recommend that the IASB amend IAS 16 to require the adjustments of the carrying amount of a financial liability, other than those adjustments for finance costs not eligible for capitalization in accordance with IAS 23, be recognized as corresponding adjustments to the cost of the asset to the extent that IAS 16 or IAS 38 requires them. The Interpretations Committee also decided to propose amendments to IFRIC 12.

Key Standards Referred to in This Publication
The following is a list of standards mentioned in this publication. Names of the standards have been included for the sake of clarity. The standards have been separated into two groups for purposes of this list—primary and secondary. The primary standards are the main standards that deal with the topic under discussion (in this publication—property, plant and equipment). The secondary standards are those referred to in this publication but not discussed in depth.

Primary standards:

- IAS 16 Property, Plant and Equipment
- IFRIC 1 Changes in Existing Decommissioning, Restoration and Similar Liabilities
- IFRIC 18 Transfers of Assets from Customers

Secondary standards:

- IFRS 2 Share-based Payments
- IFRS 5 Non-current Assets Held for Sale and Discontinued Operations
- IFRS 6 Exploration for and Evaluation of Mineral Resources
- IFRS 13 Fair Value Measurement
- IAS 1 Presentation of Financial Statements
- IAS 2 Inventories
- IAS 8 Accounting Policies, Changes in Estimates and Errors
- IAS 12 Income Taxes
- IAS 17 Leases
- IAS 18 Revenue
- IAS 20 Accounting for Government Grants and Disclosure of Government Assistance
- IAS 23 Borrowing Costs
- IAS 36 Impairment of Assets
- IAS 37 Provisions, Contingent Liabilities and Contingent Assets
- IAS 38 Intangible Assets
- IAS 40 Investment Property
- IAS 41 Agriculture
- IFRIC 12 Service Concession Arrangements
Subsequently, only the standard number will be referenced, not the name (e.g., IAS 36).

**IAS 16 Definitions**

[IAS 16.6]

These definitions were taken directly from IAS 16.

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Carrying amount</td>
<td>Carrying amount is the amount at which an asset is recognized after deducting any accumulated depreciation and accumulated impairment losses.</td>
</tr>
<tr>
<td>Cost</td>
<td>Cost is the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition or construction or, where applicable, the amount attributed to that asset when initially recognized in accordance with the specific requirements of other IFRSs (e.g., IFRS 2 Share-based Payment).</td>
</tr>
<tr>
<td>Depreciable amount</td>
<td>Depreciable amount is the cost of an asset or other amount substituted for cost less its residual value.</td>
</tr>
<tr>
<td>Depreciation</td>
<td>Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life.</td>
</tr>
<tr>
<td>Entity-specific value</td>
<td>Entity-specific value is the present value of the cash flows an entity expects to arise from the continuing use of an asset and from its disposal at the end of its useful life or expects to incur when settling a liability.</td>
</tr>
<tr>
<td>Fair value</td>
<td>Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. (See IFRS 13 Fair Value Measurement.)</td>
</tr>
<tr>
<td>Impairment loss</td>
<td>An impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount.</td>
</tr>
</tbody>
</table>
| Property, plant and equipment | Property, plant and equipment are tangible items that:
|                             | 1. are held for use in the production or supply of goods or services, for rental to others or for administrative purposes; and
|                             | 2. are expected to be used during more than one period.                                                                                                                                                                                                                                                                                                     |
| Recoverable amount          | Recoverable amount is the higher of an asset’s fair value less costs to sell and its value in use (VIU).                                                                                                                                                                                                                                                        |
| Residual amount             | The residual value of an asset is the estimated amount that an entity would currently obtain from disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.                                                                                                                                       |
| Useful life                 | Useful life is:
|                             | 1. the period over which an asset is expected to be available for use by an entity; or
|                             | 2. the number of production or similar units expected to be obtained from the asset by an entity.                                                                                                                                                                                                                                                            |
Overview of Key Requirements
The following chart provides a high-level overview of the key requirements of IAS 16 and accompanying IASB support materials. The intent is not to repeat the standard but to walk the reader through the main requirements in the standard and identify the areas where detailed guidance is given and where complexity in application exists. Areas of greater complexity will be covered in more detail under the Analysis section of this publication.

As mentioned in the Preface, specific “touchstone” references to IAS 16 have been inserted to help the reader navigate the standard. The referencing is not meant to be all-inclusive but rather to give a starting point for further research in the standard itself.

### KEY REQUIREMENTS OF IAS 16

#### Scope — IAS 16.2 – .5

<table>
<thead>
<tr>
<th>Assets Included within the Scope of IAS 16</th>
</tr>
</thead>
<tbody>
<tr>
<td>• PP&amp;E, including assets that are carried at revalued amounts</td>
</tr>
<tr>
<td>• PP&amp;E used to develop or maintain the assets shown as excluded from the scope of IAS 16</td>
</tr>
<tr>
<td>• measurement of investment property (IAS 40) accounted for using the cost model</td>
</tr>
<tr>
<td>• finance leases from the lessee perspective (other than the recognition criteria, which are included in IAS 17)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Assets Excluded from the Scope of IAS 16</th>
</tr>
</thead>
<tbody>
<tr>
<td>• PP&amp;E, classified as held for sale (IFRS 5)</td>
</tr>
<tr>
<td>• PP&amp;E where another standard requires or permits a different accounting treatment (e.g., investment property (IAS 40))</td>
</tr>
<tr>
<td>• intangible assets (IAS 38)</td>
</tr>
<tr>
<td>• biological assets related to agricultural activity (e.g., vines used to grow grapes (IAS 41))</td>
</tr>
<tr>
<td>• recognition and measurement of exploration and evaluation assets (IFRS 6)</td>
</tr>
<tr>
<td>• mineral rights and mineral reserves (e.g., oil and natural gas)</td>
</tr>
</tbody>
</table>

#### Recognition — IAS 16.7 – .14

General recognition criteria:
1. must be probable that an item of PP&E’s future economic benefits will flow to the entity; and
2. the item of PP&E’s cost can be measured reliably.

Items acquired for safety and environmental reasons, certain spare parts, standby equipment, servicing equipment and major inspection costs are recognized as they enable an entity to obtain future economic benefits from other assets.

#### Measurement at recognition — IAS 16.15 – .28

An entity considers the IAS 16 recognition criteria for all PP&E costs at the time they are incurred. These costs include costs incurred initially to acquire or construct an item of PP&E and costs incurred subsequently to add to or replace part of PP&E.

An item of PP&E should be recognized at cost, which is the amount of cash or cash equivalents paid, or the fair value of other consideration given, to acquire an asset at the time of its acquisition or construction.

There are specific elements to consider when assessing what contributes to the cost of an item of PP&E, particularly when such an item is self-constructed rather than acquired. IAS 16 provides guidance as to what cost elements should be included and those that should be excluded from the cost determination.
**KEY REQUIREMENTS OF IAS 16**

**Measurement at recognition—IAS 16.15–.28 (continued)**

IAS 16 provides specific guidance for revenue from incidental operations, self-constructed assets, non-monetary asset exchanges and costs of dismantling, removal and site restoration. Other cost consideration issues included in the analysis section of this publication include:

- borrowing costs;
- assets acquired using government grants; and
- assets transferred from customers.

A subsequent expenditure on an asset is not capitalized if it is not probable that it will create future economic benefit. The costs of day-to-day servicing of an item (i.e., repairs and maintenance) are recognized in profit and loss as incurred.

**Measurement after recognition—IAS 16.29–.66**

Choice of two accounting policies by class of PP&E:

- cost model; or
- revaluation model.

Significant guidance is provided for the application of the revaluation model, including:

- when it can be used;
- determining asset classes;
- frequency of revaluations; and
- recognition of revaluation increases and decreases.

Each part of PP&E that is significant to the overall cost of an item should be separately depreciated, regardless of the accounting policy choice to measure PP&E using the cost model or the revaluation model after recognition.

Depreciation is determined using the cost of an asset less its residual value over the estimated useful life of the asset.

Entities need to review, at least at each annual reporting date, the residual values of their PP&E assets, their estimated useful lives and the depreciation method used.

IAS 16 provides guidance on:

- when depreciation of an asset begins;
- how to determine an asset’s useful life;
- depreciation methods; and
- where depreciation is recognized.

An entity applies IAS 36 to determine whether an item of PP&E is impaired.

**Derecognition—IAS 16.67–.72**

The carrying amount of a PP&E item should be derecognized:

1. on disposal; or
2. when no future economic benefits are expected from its use or disposal.

The carrying amount of a replaced part should be derecognized upon replacement.

**Disclosure—IAS 16.73–.79**

Extensive disclosure requirements exist for each class of PP&E, including:

1. a reconciliation of the carrying amount at the beginning and end of the period (including additions, write-downs and depreciation);
2. the measurement basis for each class of PP&E (cost or revaluation);
3. the depreciation methods used;
4. the useful lives or depreciation rate used; and
5. specific information when the revaluation method is used.
Analysis of Relevant Issues
This section expands on certain areas of greater complexity and/or areas requiring significant judgment.

Scope
[IAS 16.2-.5]

Several other standards may be used in conjunction with, or in lieu of, IAS 16 to recognize and measure PP&E.

IAS 16 does not apply to investment property such as land and buildings used to earn rental income or held for capital appreciation purposes. Instead, the provisions of IAS 40 apply. The IAS 16 cost model is relevant in circumstances where this policy is chosen for subsequent measurement of investment properties.

The following examples look at the relationship between IAS 16 and IAS 40.

**APPLICATION EXAMPLES**
*Relationship between IAS 16 and IAS 40*

**Example**
Company ABC is in the manufacturing business and owns several plants (buildings and related machinery) across the country. Company ABC uses each of these plants to make products that will ultimately be sold to generate revenue.

These plants are not considered investment property as they are used in the production or supply of goods or services sold in the ordinary course of business. As such, they are recognized under IAS 16 using the requirements in this publication.

**Example**
Company DEF is in the real estate business and has invested in several buildings in many cities across the country. Company DEF derives its revenue from rental income and would recognize a capital gain or loss from the sale of these buildings.

These buildings are considered investment property because they are held to earn rentals and for capital appreciation purposes. As such, they are recognized under IAS 40. Under this standard, Company DEF may choose to measure the buildings after recognition by using either the fair value model or the cost model. Should it choose the cost model, the requirements of IAS 16 would apply.
Property, plant and equipment are used in the ordinary course of business in the production or supply of goods or services or for administrative purposes. Investment property is property held to earn rental revenue or for capital appreciation or both. When the use of a property changes from use in the business to investment property, the property’s cost and accumulated depreciation is reclassified from property, plant and equipment to investment property.

The following insight looks at accounting for the right to use land as to whether IAS 16, IAS 17 or IAS 38 applies.

**APPLICATION INSIGHTS**

**Purchase of right to use land**

<table>
<thead>
<tr>
<th>Source</th>
<th>NIFRIC</th>
</tr>
</thead>
<tbody>
<tr>
<td>Meeting Date</td>
<td>September 2012</td>
</tr>
</tbody>
</table>

The following insights were obtained from “IFRIC—items not taken onto the agenda” report.

**Issue**

In January 2012, the Interpretations Committee received a request to clarify whether the purchase of a right to use land should be accounted for as a:

- purchase of property, plant and equipment;
- purchase of an intangible asset; or
- lease of land.

In the fact pattern submitted, the laws and regulations in the jurisdiction concerned do not permit entities to own freehold title to land. Instead, entities can purchase the right to exploit or build on land. According to the submitter, there is diversity in practice in the jurisdiction on how to account for a land right.

**Reason for not adding to the IFRIC agenda**

The Interpretations Committee identified characteristics of a lease in the fact pattern considered, in accordance with the definition of a lease as defined in IAS 17. The Interpretations Committee noted that a lease could be indefinite via extensions or renewals and, therefore, the existence of an indefinite period does not prevent the ‘right to use’ from qualifying as a lease in accordance with IAS 17. The Interpretations Committee also noted that the lessee has the option to renew the right and that the useful life for depreciation purposes might include renewal periods. Judgement will need to be applied in making the assessment of the appropriate length of the depreciation period.

The Interpretations Committee, notwithstanding the preceding observations, noted that the particular fact pattern is specific to one jurisdiction. Consequently, the Interpretations Committee decided not to take this issue onto its agenda.

Details of the issues that have been considered by the IFRIC but not added to its agenda are available online at [www.ifrs.org/](http://www.ifrs.org/).
Recognition of Initial and Subsequent Costs

[IAS 16.7–.14]

IAS 16 does not specifically address what items constitute PP&E but provides general recognition guidance. The costs of an item of PP&E are capitalized only if:
1. it is probable that future economic benefits from the item will flow to the entity; and
2. the cost can be reliably measured.

The recognition criteria are based on the IASB’s Conceptual Framework for Financial Reporting.

Judgment may be required to determine whether particular costs qualify for recognition as PP&E in certain circumstances, some of which are outlined in the following sub-sections.

Items Acquired for Safety or Environmental Reasons

[IAS 16.11]

IAS 16 provides specific guidance for PP&E acquired for safety or environmental reasons. A distinction is made for such PP&E because these assets generally do not have a direct impact on increasing the future economic benefits of any existing piece of PP&E. They may, however, allow an entity to obtain future economic benefits from its other assets in excess of what it might have derived had it not acquired the safety or environmental PP&E.

APPLICATION EXAMPLE

Items acquired for safety or environmental reasons

Company ABC operates in the pharmaceutical industry. To run its plants it must abide by several environmental and chemical safety standards. To do so the company has hired several engineers to develop specific processes that will ensure compliance. It has also acquired specified quality control and monitoring equipment.

This equipment is not necessary for the production of goods and services, yet it is important for ensuring compliance with the environmental and chemical safety standards. The process development costs, as well as the equipment, are capitalized under IAS 16.
Spare Parts, Standby Equipment and Servicing Equipment
[IAS 16.8]

Items such as spare parts, standby equipment and servicing equipment are recognized as PP&E when they meet the definition of PP&E. Otherwise, such items are classified as inventory.

**EXTRACT 2—EXCERPT FROM SHERRITT INTERNATIONAL CORPORATION 2012 FINANCIAL STATEMENTS**

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

2.8 Property, plant and equipment (in part)

Plant, equipment and land (in part)

The Corporation recognizes major long-term spare parts and standby equipment as plant, equipment and land when the parts and equipment are significant and are expected to be used over a period greater than a year.

Subsequent Costs

**Repairs and Maintenance**
[IAS 16.12]

IAS 16 applies the general recognition criteria to subsequent costs incurred to add to or service a previously recognized PP&E item. A subsequent expenditure on an asset is capitalized only when it is probable that it will create future economic benefit. The costs of day-to-day servicing of an item are described as being required for the repair and maintenance of an item of PP&E and these costs are recognized in profit and loss as incurred.

**Replacement Parts**
[IAS 16.13]

Costs incurred subsequently in order to add to, replace part of, or service an item are capitalized if they meet the recognition criteria. In such cases, the standard requires an entity to derecognize the carrying amount of the part that has been replaced. This applies whether or not the replaced item has been separately identified and depreciated since acquisition. If the carrying amount of the replaced part cannot be identified, the cost of the replacement, suitably depreciated, can be used to estimate the carrying amount of the part being replaced and derecognized.
**EXTRACT 3—EXCERPT FROM AIR CANADA 2012 FINANCIAL STATEMENTS**

**NOTE 2—BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**J) Maintenance and repairs (in part)**

Maintenance and repair costs for both leased and owned aircraft are charged to Aircraft maintenance as incurred, with the exception of maintenance and repair costs related to return conditions on aircraft under operating lease, which are accrued over the term of the lease, and major maintenance expenditures on owned and finance leased aircraft, which are capitalized as described below in Note 2T.

**T) Property and equipment (in part)**

Major maintenance of airframes and engines, including replacement spares and parts, labour costs and/or third party maintenance service costs, are capitalized and amortized over the average expected life between major maintenance events. Major maintenance events typically consist of more complex inspections and servicing of the aircraft. All maintenance of fleet assets provided under power-by-the-hour contracts are charged to operating expenses in the income statement as incurred, respectively.

**EXTRACT 4—EXCERPT FROM SASKATCHEWAN TRANSPORTATION COMPANY 2012 FINANCIAL STATEMENTS**

**NOTE 4—SIGNIFICANT ACCOUNTING POLICIES**

**c. Property and equipment (in part)**

The costs of maintenance, repairs, renewals or replacements which do not extend productive life are charged to operations as incurred. The costs of replacements and improvements which extend productive life are capitalized. The cost of replacing part of an item of property and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Company and its cost can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing of property and equipment are recognized in total comprehensive loss as incurred.

**Major Inspections**

[IAS 16.14]

To continue operating, certain items of PP&E may require major inspections (for example: aircrafts, ships, etc.). When such major inspections take place, the costs are recognized as a separate component, if the recognition criteria are satisfied and amortized over the period between scheduled inspections. Once a scheduled inspection has taken place, any remaining carrying amount of the cost of the previous inspection (i.e., the unamortized portion) must be derecognized and the new inspection cost capitalized.
Measurement at Recognition

[IAS 16.15–.28]

PP&E is initially recognized at cost. Cost is the cash price equivalent or fair value of other consideration given at the recognition date. If payment is deferred beyond normal credit terms, the difference between the cash price equivalent and the total payment is recognized as interest over the period of credit unless such interest is capitalized in accordance with IAS 23. Cost includes all expenditures directly attributed to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.

IAS 16 provides guidance on the elements of the cost of an item of PP&E. The following illustration summarizes some elements of the cost of PP&E and some costs that are excluded. Note that this is not meant to be a comprehensive list.

ILLUSTRATION 1—INCLUDED AND EXCLUDED COSTS OF PP&E

<table>
<thead>
<tr>
<th>Included costs</th>
<th>Excluded costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>• purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates</td>
<td>• costs of opening a new facility</td>
</tr>
<tr>
<td>• costs of site preparation (e.g., surveying, clearing, leveling, grading, and other civil engineering tasks involved in preparing the site for construction)</td>
<td>• costs of introducing a new product or service (including costs of advertising and promotional activities)</td>
</tr>
<tr>
<td>• initial delivery and handling costs</td>
<td>• costs of conducting business in a new location or with a new class of customer, including costs of staff training</td>
</tr>
<tr>
<td>• installation and assembly costs</td>
<td>• administrative and general overhead costs</td>
</tr>
<tr>
<td>• costs of testing whether the asset is functioning properly, after deducting the net proceeds from selling any items produced while bringing the asset to that location and condition (such as samples produced when testing equipment)</td>
<td>• training costs, including those incurred for employees who must learn how to operate a new piece of equipment</td>
</tr>
<tr>
<td>• costs of employee benefits (including share-based payments) arising directly from the acquisition or construction of the PP&amp;E</td>
<td>• costs incurred while an item capable of operating in the manner intended by management has yet to be brought into use or is operated at less than full capacity</td>
</tr>
<tr>
<td>• professional fees (e.g., legal, architectural, engineering)</td>
<td>• initial operating losses, such as those incurred while demand for the item’s output builds up</td>
</tr>
<tr>
<td>• initial estimate of the costs of dismantling and removing the item and restoring the site where it is located to its original condition when an obligation to do so exists</td>
<td>• costs of relocating or reorganizing part or all of an entity’s operations</td>
</tr>
</tbody>
</table>
The following insight looks at costs of testing whether an asset is functioning properly and the treatment of any proceeds before the asset is ready for commercial production.

<table>
<thead>
<tr>
<th>APPLICATION INSIGHTS</th>
<th>Costs of testing</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Source</strong></td>
<td>NIFRIC</td>
</tr>
<tr>
<td><strong>Meeting Date</strong></td>
<td>July 2011</td>
</tr>
</tbody>
</table>

The following insights were obtained from “IFRIC—items not taken onto the agenda” report.

**Issue**

The Interpretations Committee received a request to clarify the accounting for sales proceeds from testing an asset before it is ready for commercial production. The submitted fact pattern is that of an industrial group with several autonomous plants being available for use at different times. This group is subject to regulation that requires it to identify a ‘commercial production date’ for the whole industrial complex. The question asked of the Committee is whether the proceeds from those plants already in operation can be offset against the costs of testing those plants that are not yet available for use.

**Reason for not adding to the IFRIC agenda**

The Committee noted that paragraph 17(e) of IAS 16 applies separately to each item of property, plant and equipment. It also observed that the ‘commercial production date’ referred to in the submission for the whole complex was a different concept from the ‘available for use’ assessment in paragraph 16(b) of IAS 16. The Committee thinks that the guidance in IAS 16 is sufficient to identify the date at which an item of property, plant and equipment is ‘available for use’ and, therefore, is sufficient to distinguish proceeds that reduce costs of testing an asset from revenue from commercial production.

As a result, the Committee does not expect diversity to arise in practice and therefore decided not to add this issue to its agenda.

Details of the issues that have been considered by the IFRIC but not added to its agenda are available online at [www.ifrs.org/](http://www.ifrs.org/).

**Costs of a Self-Constructed Asset**

[IAS 16.22]

The costs of a self-constructed asset are determined using the same principles as for an acquired asset. They normally include the direct costs of constructing the asset (e.g., the purchase price of raw materials including transportation, handling and other direct costs, and direct labour costs).
If an entity makes similar assets for sale in the normal course of business, the costs of the asset are usually the same as the costs of constructing an asset for sale. Therefore, any internal profits are excluded.

IAS 16 specifically excludes the cost of abnormal amounts of wasted material, labour or other resources incurred in self-constructing an asset.

**EXTRACT 6—EXCERPT FROM ROGERS COMMUNICATIONS INC. 2012 FINANCIAL STATEMENTS**

**NOTE 2—SIGNIFICANT ACCOUNTING POLICIES**

**(i) Recognition and measurement: (in part)**

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the assets to a working condition for their intended use, the costs of dismantling and removing the items and restoring the site on which they are located, and borrowing costs on qualifying assets. The determination of directly attributable costs involves significant management estimates. These estimates include certain direct labour and direct costs associated with the acquisition, construction, development or betterment of the Company’s network are capitalized to PP&E, and interest costs which are capitalized during construction and development of certain PP&E.

**Borrowing Costs**

[IAS 23.1 and .5]

IAS 23 establishes criteria for the recognition of borrowing costs as an element of the carrying amount of a qualifying asset. A qualifying asset is defined in IAS 23 as “an asset that necessarily takes a substantial period of time to get ready for its intended use or sale”. IAS 23 does not provide guidance on what constitutes a substantial period of time. This is a matter of judgment.

An entity must capitalize borrowing costs for qualifying assets that are directly attributable to the acquisition, construction or production of the qualifying asset.
EXTRACT 7—EXCERPT FROM POTASH CORPORATION OF SASKATCHEWAN INC.

2012 FINANCIAL STATEMENTS

NOTE 5—PROPERTY, PLANT AND EQUIPMENT

Accounting Policies (in part)

Borrowing costs directly attributable to the acquisition, construction or production of assets that necessarily take a substantial period of time to ready for their intended use are added to the cost of those assets, until such time as the assets are substantially ready for their intended use. The capitalization rate is based on the weighted average interest rate on all of the company’s outstanding third-party debt. All other borrowing costs are charged through finance costs in the period in which they are incurred.

Cessation of Cost Recognition

[IAS 16.20]

It should be noted that costs are no longer capitalized once the item is in the location and condition necessary for it to be capable of operating in the manner intended by management. This means that IAS 16 prohibits the recognition of relocation and reorganization costs, costs incurred after the asset is capable of being used and initial operating losses.

Income and Related Expenses of Incidental Operations

[IAS 16.21]

Incidental income derived from operating PP&E prior to its substantial completion and readiness for use is recognized as part of the cost of the asset provided it is necessary to bring the asset to its intended use.

Income and related expenses of incidental operations that are not necessary to bring an asset to the condition and location for its intended use, or that are incurred after the asset is already in the location and condition necessary for operating as intended, are recognized in profit or loss.

APPLICATION EXAMPLE

Incidental income

Company ABC is about to construct a condominium project near a golf course. Before construction begins, the land on which the project will be situated is being used as a place where golfers may practice prior to beginning their games. The golf company must pay a rental fee to Company ABC for the use of this land.

Revenues derived by ABC from the golf company are recognized in the period when earned as they are not required to bring the asset to the condition and location for its intended use.
Assets Acquired Using Government Grants

[IAS 16.28 and IAS 20.24]

For many industries, the acquisition of certain assets is made possible by government grants. Government grants may take the form of subsidies, forgivable loans or other similar mechanisms. IAS 20 prescribes the following treatment for government grants related to PP&E:

- recognize the grant as deferred income to be recognized in profit or loss on a systematic basis over the useful life of the asset; or
- deduct the grant in calculating the carrying amount of the asset. The grant is recognized in profit or loss over the life of a depreciable asset as a reduced depreciation expense.

EXTRACT 8—EXCERPT FROM CENOVUS ENERGY INC. 2012 FINANCIAL STATEMENTS

NOTE 3—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

R) Government Grants

Government grants are recognized at fair value when there is reasonable assurance that the grants will be received and the Company will comply with the conditions of the grant. Grants related to assets are recorded as a reduction of the asset’s carrying value and are depreciated over the useful life of the asset. Grants related to income are treated as a reduction of the related expense in the Consolidated Statements of Earnings and Comprehensive Income.

Assets Held under a Finance Lease

[IAS 16.4 and .27]

The initial measurement of cost for PP&E acquired under the form of a finance lease is determined under the provisions of IAS 17. Once a leased asset held under a finance lease has been recognized, its subsequent measurement follows the requirements in IAS 16 (e.g., use of the cost model or revaluation model and depreciation).

Non-Monetary Transactions

[IAS 16.24 – .26]

Where an entity acquires an item of PP&E in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets, measurement at fair value is prescribed unless the exchange transaction lacks commercial substance or the fair value of neither the asset received nor the asset given up is reliably measurable. If the acquired item is not measured at fair value, its cost is measured at the carrying amount of the asset given up.
An entity determines whether an exchange transaction has commercial substance by considering the extent to which its future cash flows are expected to change as a result of the transaction. An exchange transaction has commercial substance if:

- the configuration (i.e., risk, timing and amount) of the cash flows of the asset received differs from the configuration of the cash flows of the asset transferred; or
- the entity-specific value of the portion of the entity’s operations affected by the transaction changes as a result of the exchange; and
- the difference in the points above is significant relative to the fair value of the assets exchanged.

Recall that entity-specific value is the present value of the cash flows an entity expects to arise from the continuing use of an asset and from its disposal at the end of its useful life or expects to incur when settling a liability.

For the purpose of determining commercial substance, the entity-specific value of the portion of the entity’s operations affected by the transaction should reflect post-tax cash flows.

**EXTRACT 9—EXCERPT FROM THE GREAT CANADIAN GAMING CORPORATION 2012 FINANCIAL STATEMENTS**

**NOTE 3—CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS**

- **Fair value of assets acquired in business transactions with non-monetary consideration**

  The Company measures the fair value of assets acquired in business transactions with non-monetary consideration at the fair value of the asset given up or the fair value of the asset received, whichever is more reliably measurable. Measurement of fair value is based on an analysis of pertinent information that may include third-party asset appraisals, market values evidenced from similar transactions, and discounted cash flows.

**Transfers of Assets from Customers [IFRIC 18]**

In some industries, suppliers of goods or services require (or allow) their customers to contribute PP&E items (or cash to construct or acquire PP&E items) to support the customers’ ongoing access to a supply of goods or services. Examples include PP&E to connect to utilities such as gas, electricity or water and PP&E provided to an information outsourcing provider. The IFRS Interpretations Committee clarified the accounting treatment for how the entity receiving the PP&E recognizes the receipt of the assets (or cash specifically designated for the acquisition or construction of PP&E items) from its customers (IFRIC 18).

Essentially, that transfer is treated as a non-monetary transaction. Therefore, if a PP&E item received from a customer meets the definition of an asset (i.e., the item is a resource the entity controls as a result of past events and from which
future economic benefits are expected to flow), that item should be measured at fair value as a non-monetary transaction as described above. If, however, the customer continues to exercise control after ownership of the item is transferred, the item cannot be recognized as an asset.

It is important to note that government grants in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the entity’s operating activities are excluded from IFRIC 18 and should be accounted for under IAS 20. In addition, IFRIC 18 does not apply to agreements covering the transfer of infrastructure used in public-to-private service concession arrangements and falling within the scope of IFRIC 12.

The following insight looks at the issue of how IFRIC 18 applies to customer transfer of assets within the scope of IFRIC 18. Note the date of the NIFRIC. Even though some NIFRICs are older, they still provide some insight into how the standards are interpreted by the standard setters.

<table>
<thead>
<tr>
<th>APPLICATION INSIGHTS</th>
<th>Applicability of IFRIC 18 to the customer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Source</td>
<td>NIFRIC</td>
</tr>
<tr>
<td>Meeting Date</td>
<td>July 2009</td>
</tr>
</tbody>
</table>

The following insights were obtained from “IFRIC—items not taken onto the agenda” report.

**Issue**

The IFRIC received a request to provide guidance on how the customer should account for a transfer of assets that is in the scope of IFRIC 18 for the recipient. The IFRIC noted that IFRIC 18 addresses only the accounting by the recipient of the transferred assets.

The IFRIC also noted that the accounting by customers transferring assets should be consistent with the principles in IFRIC 18 that, in a normal trading transaction, transfers of assets include exchanges of other goods, services or both. The IFRIC noted that other IFRSs provide relevant guidance for accounting for the goods or services received or given up in the exchange transaction.

**Reason for not adding to the IFRIC agenda**

Therefore, the IFRIC concluded that the agenda criteria were not met mainly because IFRSs already provide relevant guidance, and it did not expect divergent interpretations in practice. Therefore, the IFRIC decided not to add this issue to its agenda.

Details of the issues that have been considered by the IFRIC but not added to its agenda are available online at www.ifrs.org/.
Subsequent Measurement
[IAS 16.29–.66]

IAS 16 permits entities to choose between two accounting policy models for subsequent measurement of PP&E:
• the cost model; or
• the revaluation model.

Cost Model
[IAS 16.30]

Under the cost model, once an item of PP&E is recognized as an asset, it is carried at its cost less any accumulated depreciation and any accumulated impairment losses. This is the traditional method of accounting for PP&E.

Revaluation Model
[IAS 16.31–.42]

Once a model is selected, it applies to an entire class of PP&E. Thus, if an item of PP&E is revalued, the entire class of PP&E to which that asset belongs has to be revalued to prevent selective revaluation. A class of PP&E is defined as a grouping of assets of a similar nature and use in an entity’s operations. The following illustration includes examples of separate asset classes identified in IAS 16.
ILLUSTRATION 2—APPLICATION OF THE REVALUATION MODEL

**Examples of separate asset classes**

<table>
<thead>
<tr>
<th>Asset Class</th>
</tr>
</thead>
<tbody>
<tr>
<td>Land</td>
</tr>
<tr>
<td>Land and buildings</td>
</tr>
<tr>
<td>Machinery</td>
</tr>
<tr>
<td>Ships</td>
</tr>
<tr>
<td>Aircraft</td>
</tr>
<tr>
<td>Motor vehicles</td>
</tr>
<tr>
<td>Furniture and fixtures</td>
</tr>
<tr>
<td>Office equipment</td>
</tr>
</tbody>
</table>

Judgment must be applied in the determination of PP&E asset classes. Each entity should analyze its specific operations to determine those classes. Asset classes may be narrower than those identified above. As an example, in the airline industry, engines or flight equipment may be considered specific asset classes rather than the more all-encompassing notion of “aircraft.”

The revaluation model is available to classes of PP&E whose fair value can be reliably measured. If the fair value cannot be reliably measured, the cost model must be selected.

Under the revaluation model, a class of PP&E is carried at its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is determined from a market perspective by applying the requirements of IFRS 13.

The revaluation model is generally used by companies having assets that tend to appreciate in value, such as buildings and land not accounted for under IAS 40. In particular, this model is informative for land assets since land is not depreciated and revaluation would reflect appreciation in value over time—although recent economic trends have shown that asset appreciation is not a guarantee.

As a matter of interest, few companies in Europe, Australia, Canada and other areas use the revaluation model and those that do limit its use to a few selected classes.
Selecting and Deselecting the Revaluation Model Policy

[IAS 8.14, .17, .19, .22-.25 and .29]

The change in accounting policy from the cost model to the revaluation model should be treated as a change in accounting policy in accordance with IAS 16 rather than IAS 8. The change is treated as a revaluation during the period the revaluation model is first applied and, therefore, prior periods are not adjusted. This means it is not necessary to restate prior periods for the carrying value and depreciation and impairment charges for the revalued items. This is an exception from the IAS 8 requirement to account for voluntary changes in accounting policies retrospectively.

Deselecting the revaluation model is more problematic. IAS 8 permits a voluntary change in accounting policy only if the change results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the entity’s financial position, financial performance or cash flows. The revaluation model is thought to provide information more relevant and reliable than that obtained under the cost model; therefore, it may be difficult to assert that the change results in more relevant information. However, circumstances such as a new limitation in determining a reliable fair value could force such a reversion. This could mean that the revaluation does not result in reliable information.

Thus, an entity choosing to revert back to the cost model would have to justify that choice under IAS 8 and apply the change retrospectively (i.e., as if it had always been applied), unless it is impracticable to do so. This means the entity would have to restate the carrying values, including accumulated depreciation and accumulated impairments and the effects on profit or loss and equity, as if the revaluation model had not been adopted as an accounting policy choice. The entity would also apply the IAS 8 disclosure requirements for a voluntary change in accounting policy.

Frequency of Revaluations

[IAS 16.31 and .34]

Companies should revalue their PP&E with sufficient regularity to ensure the carrying amount does not differ materially from what they would determine using fair value at the end of the reporting period.
The frequency of revaluations depends on the changes in the fair values of the PP&E items. If there is a material difference between the fair value of an asset and its carrying amount, it needs to be revalued. There is no requirement to conduct an annual revaluation of assets; if, however, the value of an asset fluctuates a great deal, it should be revalued annually. For example, where asset values change very little, they can possibly be revalued every three-to-five years.

The items within a class of PP&E are revalued simultaneously to avoid selective revaluation of assets and the reporting of amounts in the financial statements that are a mixture of costs and fair value.

**Accounting for a Revaluation**

[IAS 16.35 and .39–.40]

When a PP&E item is revalued, any accumulated depreciation at the date of the revaluation is treated in one of two ways:

1. It is restated proportionately with the change in the gross carrying amount of the asset so that the carrying amount of the asset after revaluation equals its revalued amount. This method is often used when an asset is revalued by applying an index to determine its replacement cost (see IFRS 13).
2. It is eliminated against the gross carrying amount of the asset and the net amount is restated to the asset’s revalued amount. This method is often used for buildings.

*Note: Refer to the Standards Update section in this publication. A proposed amendment to IAS 16 would change the guidance in (1) above and state that accumulated depreciation is computed as the difference between the gross and net carrying amounts. The amendment will also clarify that the determination of accumulated depreciation does not depend on the selection of the valuation technique.*

These two methods will result in the same net balance sheet amount for PP&E although the gross amounts reported (i.e., cost and accumulated depreciation) will differ. The effect on the income statement and the other comprehensive income will be the same.
The following illustration indicates the recognition of a change from a revaluation.

**ILLUSTRATION 3—RECOGNITION OF REVALUATION CHANGES**

| Initial revaluation increase | • included in other comprehensive income (OCI) and accumulated in equity under the heading “revaluation surplus”.
| Initial revaluation decrease | • included in profit or loss.
| Subsequent revaluation increase | • included in OCI and increases revaluation surplus unless it reverses a revaluation decrease of the same asset previously recognized in profit or loss.
| | • recognition in profit or loss is limited to the previously recognized decreases in that asset.
| | • no net gain should be recognized in income over the useful life of a revalued asset.
| Subsequent revaluation decrease | • included in profit or loss unless any credit balance exists in the revaluation surplus for that asset. In this case, the decrease is recognized in OCI and the revaluation surplus to the extent that any credit balance exists for that asset.
| | • carrying a negative revaluation reserve for any asset is not permitted.

The following three examples illustrate the calculation of a revaluation. Note that in the first two examples, the impact of depreciation has been ignored to simplify the calculations. The impact of depreciation is demonstrated in the third example. The following abbreviations are used in these examples:

CA = carrying amount  
FV = fair value  
OCI = other comprehensive income

**APPLICATION EXAMPLE**

Initial revaluation is an increase in carrying amount

This is a simplified example, excluding depreciation, to demonstrate recognition of revaluation adjustments.

ABC Ltd. has elected to use the revaluation model to account for its building. There is only one building in the asset class. The building cost is $500,000.

<table>
<thead>
<tr>
<th>Revaluation</th>
<th>FV</th>
<th>Difference between FV and CA</th>
<th>Recognized in OCI</th>
<th>Recognized in profit or loss</th>
</tr>
</thead>
<tbody>
<tr>
<td>#1</td>
<td>$600,000</td>
<td>+$100,000</td>
<td>+$100,000</td>
<td>0</td>
</tr>
<tr>
<td>#2</td>
<td>$400,000</td>
<td>-$200,000</td>
<td>-$100,000</td>
<td>-$100,000</td>
</tr>
<tr>
<td>#3</td>
<td>$750,000</td>
<td>+$350,000</td>
<td>+$250,000</td>
<td>+$100,000</td>
</tr>
</tbody>
</table>
APPLICATION EXAMPLE

Initial revaluation is an increase in carrying amount

At the first revaluation, a $100,000 increase in the carrying amount of the building and a corresponding increase in OCI is recognized. A revaluation surplus of $100,000 is included as a separate line item in equity.

At the second revaluation, the carrying amount of the building is decreased by $200,000, which represents the difference between the carrying amount of the building before revaluation ($600,000) and the revalued amount (fair value of $400,000). Because the second revaluation decreases the carrying amount, the decrease is applied first to the revaluation surplus balance. A reversal of $100,000 will be recognized in OCI and a loss of $100,000 will be recognized in profit or loss.

For the third revaluation, the carrying amount of the building has increased $350,000, which represents the difference between the carrying amount of the building before the revaluation ($400,000) and the revalued amount (fair value of $750,000). An amount of $100,000 is recognized in profit or loss to reverse the loss recognized in the previous revaluation. The remaining $250,000 is recognized in OCI. A revaluation surplus of $250,000 is included as a separate line item in equity.

APPLICATION EXAMPLE

Initial revaluation is a decrease in carrying amount

This is a simplified example, excluding depreciation, to demonstrate recognition of revaluation adjustments.

ABC Ltd. has elected the revaluation model to account for its building. There is only one building in the asset class. The building cost is $500,000.

<table>
<thead>
<tr>
<th>Revaluation</th>
<th>FV</th>
<th>Difference between FV and CA</th>
<th>Recognized in OCI</th>
<th>Recognized in profit or loss</th>
</tr>
</thead>
<tbody>
<tr>
<td>#1</td>
<td>$400,000</td>
<td>-$100,000</td>
<td>0</td>
<td>-$100,000</td>
</tr>
<tr>
<td>#2</td>
<td>$700,000</td>
<td>+$300,000</td>
<td>+$200,000</td>
<td>+$100,000</td>
</tr>
<tr>
<td>#3</td>
<td>$350,000</td>
<td>-$350,000</td>
<td>-$200,000</td>
<td>-$150,000</td>
</tr>
</tbody>
</table>

At the first revaluation, a $100,000 decrease in the carrying amount of the building and a corresponding charge to profit or loss is recognized (there is no revaluation surplus related this asset).

At the second revaluation, the carrying amount of the building is increased by $300,000, which represents the difference between the carrying amount of the building before revaluation ($400,000) and the revalued amount (fair value of $700,000). The $100,000 loss recognized for the previous revaluation is reversed, with the difference of $200,000 recognized in OCI. A revaluation surplus of $200,000 is included as a separate line item in equity.

For the third revaluation, the carrying amount of the building has decreased to $350,000, which represents the difference between the carrying amount of the building before the revaluation ($700,000) and the revalued amount (fair value of $350,000). The decrease is applied first to the revaluation surplus balance. A reversal of $200,000 will be recognized in OCI and a loss of $150,000 will be recognized in profit or loss.
APPLICATION EXAMPLE

Initial revaluation is a decrease in carrying amount

This example includes the impact of revaluation adjustments and the effect on depreciation.

ABC Ltd. has elected the revaluation model to account for its building. There is only one building in the asset class. The building cost is $1 million and is being depreciated on a straight-line basis over its estimated useful life of 20 years.

<table>
<thead>
<tr>
<th>Year</th>
<th>CA at the end of the year</th>
<th>FV at the end of the year</th>
<th>Difference CA - FA</th>
<th>Depreciation for the year (in profit or loss)</th>
<th>Revaluation recognized in OCI</th>
<th>Revaluation recognized in profit or loss</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>$950,000</td>
<td>$950,000</td>
<td>0</td>
<td>$50,000</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>2</td>
<td>$900,000</td>
<td>$900,000</td>
<td>0</td>
<td>$50,000</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>3</td>
<td>$850,000</td>
<td>$850,000</td>
<td>0</td>
<td>$50,000</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>4</td>
<td>$800,000</td>
<td>$600,000</td>
<td>-$200,000</td>
<td>$50,000</td>
<td>0</td>
<td>-$200,000</td>
</tr>
<tr>
<td>5</td>
<td>$562,500 ($600,000 – $37,500)</td>
<td>$562,500</td>
<td>0</td>
<td>$37,500</td>
<td>($600,000 / 16)</td>
<td>0</td>
</tr>
<tr>
<td>6</td>
<td>$525,000</td>
<td>$525,000</td>
<td>0</td>
<td>$37,500</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>7</td>
<td>$487,500</td>
<td>$700,000</td>
<td>+$212,500</td>
<td>$37,500</td>
<td>$50,000</td>
<td>$162,500</td>
</tr>
</tbody>
</table>

In years one through three the carrying amount approximates fair value. Depreciation is $50,000 yearly ($1,000,000 / 20 years).

At the end of the fourth year, when the carrying amount is $800,000, a revaluation results in a revaluation adjustment of -$200,000 recognized in profit or loss. Depreciation is $50,000 for year four but decreases to $37,500 for year five based on the carrying amount of $600,000 at the beginning of the year and an estimated remaining useful life of 16 years.

At the end of the seventh year, when the carrying amount is $487,500, the fair value is $700,000. This results in a revaluation adjustment of $212,500. To determine the amount to recognize in profit or loss, the loss previously recognized in profit or loss and the reduction in depreciation as a result of the revaluation adjustment need to be considered. The portion of the revaluation adjustment recognized in profit or loss is equal to $200,000 (the reversal of the previous revaluation loss) less an adjustment for the extra depreciation that would have been recognized in profit or loss without the revaluation adjustment (($50,000 – $37,500) × 3 years = $37,500). Thus $162,500 is a credit to profit or loss and the remainder is recognized in OCI ($212,500 – $162,500 = $50,000). A revaluation surplus of $50,000 is included as a separate line item in equity. This represents the excess of the carrying amount using the revaluation method ($700,000) over what it would have been using the cost method, with no revaluations recognized (($1,000,000 – ($50,000 × 7 years) = $750,000).
Transferring the Revaluation Surplus to Retained Earnings

[IAS 16.41]

A portion of the revaluation surplus related to the depreciated asset may be realized during the useful life of the asset by transferring an amount equivalent to the difference between the depreciation calculated on the asset’s revalued carrying amount and the depreciation calculated on its original cost from the revaluation surplus to retained earnings. These transfers do not go through profit or loss. Alternatively, the whole of the surplus can be transferred to retained earnings when the asset is retired or disposed of.

Costs of Dismantling, Removal and Site Restoration (Decommissioning Costs) and Changes to These Costs

[IAS 16.16 and .18, IAS 37.10, .14 and .36 and IFRIC 1]

Many entities have obligations to dismantle, remove and restore items of PP&E. Under IAS 16, the cost of an item of PP&E includes the costs an entity incurs for dismantling, removing the item and restoring the site on which it is located, either at acquisition or after having used the asset during a particular period for purposes other than to produce inventories during that period.

IAS 37 provides guidance on when these costs are recognized and how the amount is determined. A provision for decommissioning, site restoration and similar liabilities is recognized when:

1. the entity has a present obligation (legal or constructive\(^1\)) as a result of a past event;
2. an outflow of resources to settle the obligation is probable; and
3. a reliable estimate of the obligation can be made.

Obligations for dismantling, removal or site restoration are measured at management’s best estimate of the expenditure required to settle the obligation at the end of the reporting period. A corresponding cost is added to the carrying amount of the PP&E item.

IFRIC 1 was developed to provide guidance on changes in the measurement of an existing decommissioning or restoration obligation triggered by a change in the estimated timing or amount of the outflow of resources required to settle the obligation, or in the discount rate.

\(^1\) A constructive obligation is an obligation derived from an entity’s actions where an established pattern of past practice, published policy or a sufficiently specific current statement indicating to other parties that it will accept certain responsibilities have created a valid expectation on the part of other parties that the entity will discharge those responsibilities.
The following illustration summarizes the guidance in IFRIC 1.

**ILLUSTRATION 4—IFRIC 1—CHANGES IN EXISTING DECOMMISSIONING, RESTORATION AND SIMILAR LIABILITIES**

<table>
<thead>
<tr>
<th>Cost model used for PP&amp;E</th>
<th>Revaluation model used for PP&amp;E</th>
</tr>
</thead>
<tbody>
<tr>
<td>The change is added to, or deducted from, the costs of the related asset.</td>
<td>The change is recognized either in the revaluation surplus or deficit previously recognized.</td>
</tr>
<tr>
<td>• The amount deducted should not exceed the carrying amount of the asset. Any excess should be recognized in profit or loss.</td>
<td>• A decrease in the obligation is recognized in OCI and increases the revaluation surplus in equity unless it reverses a revaluation deficit recognized previously in profit or loss. If, so, this portion is recognized in profit or loss.</td>
</tr>
<tr>
<td>• An increase in the carrying amount of the asset as a result of an increase in the obligation may trigger an asset impairment test. If indicators of impairment exist, the asset should be tested in accordance with IAS 36 by comparing the carrying amount of the asset to its recoverable amount (i.e., higher of fair value less costs of disposal and VIU).</td>
<td>• If the liability decrease exceeds the carrying amount that would have been recognized had the asset been measured using the cost model, the excess is recognized in profit or loss.</td>
</tr>
<tr>
<td></td>
<td>• An increase in the obligation is recognized in profit or loss unless there is a credit balance in the revaluation surplus related to the asset. If so, the increase is recognized in OCI to the extent of the credit balance in the revaluation surplus in equity.</td>
</tr>
<tr>
<td></td>
<td>• The change in the obligation may be an indication that the asset has to be revalued. If a revaluation is necessary, the entire class has to be revalued.</td>
</tr>
</tbody>
</table>

Once the related asset has reached the end of its useful life, all subsequent changes in the liability must be recognized in profit or loss as they occur. Moreover, the unwinding of the discount should be recognized in profit or loss as a finance cost. Under IAS 23, capitalization is not permitted.
**EXTRACT 11—EXCERPT FROM HUSKY ENERGY INC. 2012 FINANCIAL STATEMENTS**

**NOTE 3—SIGNIFICANT ACCOUNTING POLICIES**

### i) Asset Retirement Obligations (“ARO”)

A liability is recognized for future legal or constructive retirement obligations associated with the Company’s assets. The Company has significant obligations to remove tangible assets and restore land after operations cease and the Company retires or relinquishes the asset. The retirement of Upstream and Downstream assets consists primarily of plugging and abandoning wells, removing and disposing of surface and subsea plant and equipment and facilities, and restoring land to a state required by regulation or contract. The amount recognized is the net present value of the estimated future expenditures determined in accordance with local conditions, current technology and current regulatory requirements. The obligation is calculated using the current estimated costs to retire the asset inflated to the estimated retirement date and then discounted using a credit-adjusted risk free discount rate. The liability is recorded in the period in which an obligation arises with a corresponding increase to the carrying value of the related asset. The liability is progressively accreted over time as the effect of discounting unwinds, creating an expense recognized in finance expenses. The costs capitalized to the related assets are amortized in a manner consistent with the depletion, depreciation and amortization of the underlying assets. Actual retirement expenditures are charged against the accumulated liability as incurred.

Liabilities for ARO are adjusted every reporting period for changes in estimates. These adjustments are accounted for as a change in the corresponding capitalized cost, except where a reduction in the provision is greater than the undepreciated capitalized cost of the related assets, in which case the capitalized cost is reduced to nil and the remaining adjustment is recognized in net earnings. In the case of closed sites, changes to estimated costs are recognized immediately in net earnings. Changes to the amount of capitalized costs will result in an adjustment to future depletion, depreciation and amortization, and finance expenses.

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**Depreciation**

[IAS 16.6 and .43–.62]

IAS 16 requires an annual charge to income for depreciation based on an allocation of the cost of an asset, less its residual value, over its useful life, including any idle period or period in which the asset is retired from active use. Depreciation may be nil, however, if a usage method is applied and there is no production from the asset.

The mechanics of depreciation are the same for the cost and revaluation model in that “cost” or “revalued amount,” less any residual value, is amortized over the useful life of an asset. Although, as we have seen in the application examples in the section on the application of the revaluation model, the mechanics of calculating the depreciation expense under the revaluation model may pose some difficulties, the determination of depreciation remains fundamentally the same under both models.

A depreciation charge for each period is recognized in profit or loss unless an asset’s future economic benefits are absorbed in producing other assets, in which case the depreciation charge is included in the carrying amount of those assets. For example, the depreciation of a manufacturing plant and equipment is included in the costs of conversion of inventories.
Component Accounting

[IAS 16.43–.47]

IAS 16 requires the application of component accounting. The main objective of component accounting is to ensure the costs of an asset’s significant components are depreciated over their appropriate useful lives, rather than the useful life of the asset taken as a whole. Note that a separate component can be either physical (e.g., a motor on an aircraft) or nonphysical (e.g., a major overhaul or inspection).

The allocation of cost to components requires judgment and careful analysis of facts and circumstances. There is no prescribed methodology for determining significant components.

One could, however, consider the use of a valuator to determine values of assets and components. Alternatively, insurance appraisal reports may have components listed for significant assets, which could be useful in determining the value of significant components. Where an entity has several locations (e.g., a company with relatively homogeneous manufacturing plants around the world) it might consider using a pilot-project approach. Under a pilot project, the company would pick one plant for evaluation by valuators, engineers or other appropriate personnel. Their findings would then be applied to the other plants in the organization and produce results not materially different from what might have been obtained had all individual plants been evaluated on their own. One must recall that the components must be significant to the overall asset. Therefore, the asset should not have a significant number of components.

Each component part of a PP&E item costing a significant amount in relation to the item’s total cost is depreciated separately. When, however, significant parts of a PP&E item have the same useful lives and depreciation method, they may be grouped together for depreciation purposes.

As an example, a building may have several components (e.g., the roof, door frames, walls, floors, elevators, escalators, etc.), but only some of these components may be considered significant. In addition, the walls, doorframes and floors may all have the same useful lives and can be grouped together.
ABC Ltd. acquires a building. An insurance valuator proposes that the building has two significant components (i.e., the roof and the elevators) representing 15% and 18% respectively of the relative fair value of the building. The building was acquired for $750,000 and its useful life was determined to be 50 years. The roof and elevators have an estimated useful life of 15 years and 25 years respectively. The building is measured using the cost model. For simplicity, residual value is deemed to be nil.

The components are depreciated as follows:

<table>
<thead>
<tr>
<th>Component</th>
<th>Carrying amount</th>
<th>Useful life</th>
<th>Depreciation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Roof (15%)</td>
<td>$112,500</td>
<td>15 years</td>
<td>$7,500</td>
</tr>
<tr>
<td>Elevator (18%)</td>
<td>$135,000</td>
<td>25 years</td>
<td>$5,400</td>
</tr>
<tr>
<td>Building (67%)</td>
<td>$502,500</td>
<td>50 years</td>
<td>$10,050</td>
</tr>
<tr>
<td>Total</td>
<td>$750,000</td>
<td></td>
<td>$22,950</td>
</tr>
</tbody>
</table>

If the building is depreciated as a single unit rather than as component parts, depreciation would be $15,000 ($750,000 / 50 years), which is relatively lower than $22,950 above.

EXTRACT 12—EXCERPT FROM AIR CANADA 2012 FINANCIAL STATEMENTS

NOTE 2—BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

T) Property and equipment (in part)

The Corporation allocates the amount initially recognized in respect of an item of property and equipment to its significant components and depreciates separately each component. Property and equipment are depreciated to estimated residual values based on the straight-line method over their estimated service lives. Aircraft and flight equipment are componentized into airframe, engine, and cabin interior equipment and modifications. Airframe and engines are depreciated over 20 to 25 years, with 10% to 20% estimated residual values. Cabin interior equipment and modifications are depreciated over the lesser of 5 years or the remaining useful life of the aircraft. Spare engines and related parts (“rotables”) are depreciated over the average remaining useful life of the fleet to which they relate with 10% to 20% estimated residual values. Cabin interior equipment and modifications to aircraft on operating leases are amortized over the term of the lease.

Buildings are depreciated on a straight-line basis over their useful lives not exceeding 50 years or the term of any related lease, whichever is less. Leasehold improvements are amortized over the lesser of the lease term or 5 years. Ground and other equipment is depreciated over 3 to 25 years.
Residual Value
[IAS 16.6 and .51-.54]

IAS 16.6 provides a detailed definition of the residual value of an asset. Residual value should reflect the amount an entity would currently receive from the disposal of an asset after deducting estimated costs of disposal if it were already of the age and in the condition expected at the end of its useful life.

IAS 16 requires an annual review of the residual value of an asset. If a change is required, it should be accounted for as a change in an accounting estimate (unless the change reflects a correction of an error).

EXTRACT 13—EXCERPT FROM WESTJET AIRLINES LTD. 2012 FINANCIAL STATEMENTS
NOTE 1—STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES
(j) Property and equipment (in part)

Estimated residual values of the Corporation's aircraft range between $4,000 and $6,000 per aircraft. Spare engines have a residual value equal to 10% of the original purchase price. Residual values, where applicable, are reviewed annually against prevailing market rates at the consolidated statement of financial position date.

Depreciation is recognized as long as the asset's carrying amount exceeds its residual value. In circumstances where the residual value of an asset increases to an amount greater than its carrying amount, the depreciation charge is zero until the residual value falls below the asset's carrying amount.

Useful Life
[IAS 16.6, .50-.51 and .56-.59]

The useful life of an asset is:
• the period over which an asset is expected to be available for use by an entity; or
• the number of production or similar units an entity expects to obtain from the asset.

The useful life of an asset is defined in terms of the asset's expected utility to the entity and may sometimes be shorter than its economic life.

The estimation of the useful life of an asset is a matter of judgment based on the experience of the entity with similar assets. The illustration below lists factors included in IAS 16 that should be considered in determining the expected useful life.
ILLUSTRATION 5—DETERMINING THE EXPECTED USEFUL LIFE OF AN ITEM OF PP&E

Examples of factors to consider in determining an asset’s expected useful life include:

- expected usage assessed by reference to the asset’s expected capacity or physical output.
- expected physical wear and tear, which depends on operational factors such as the number of shifts for which the asset is to be used, the repair and maintenance program and the care and maintenance of the asset while idle.
- technical or commercial obsolescence arising from changes or improvements in production, or from a change in the market demand for the product or service output of the asset.
- legal or similar limits on the use of the asset, such as the expiry dates of related leases.

Land and building are separate assets and accounted for separately. With some exceptions (e.g., quarries and landfill sites) land has an unlimited useful life and is not depreciated. In cases where land has a limited useful life, it is depreciated in a manner that reflects the benefits to be derived from it. If the cost of the land includes costs of site dismantlement, removal and restoration costs, these costs are depreciated over the period of benefits obtained by incurring those costs.

IAS 16 requires the useful life of an asset be reviewed on an annual basis; any changes are accounted for as a change in an accounting estimate.

EXTRACT 14—EXCERPT FROM NEWALTA CORPORATION 2012 FINANCIAL STATEMENTS

NOTE 2—SIGNIFICANT ACCOUNTING POLICIES

C) Property, plant and equipment (in part)

Landfill assets represent the costs of landfill available space, including original acquisition cost, incurred landfill construction and development costs, including gas collection systems installed during the operating life of the site, and capitalized landfill closure and post-closure costs. The cost of landfill assets, together with projected landfill construction and development costs for permitted capacity, is amortized on a per-unit basis as landfill space is consumed. Management annually updates landfill capacity estimates, based on survey information provided by independent engineers, and projected landfill construction and development costs. The impact on annual amortization expense of changes in estimated capacity and construction costs is accounted for prospectively.
The following viewpoint is industry specific and is included to illustrate some of the judgment involved in the determination of the useful life of an asset.

### Application Viewpoints

**Depletion of a Mine in the Production Phase: Useful Life of the Mine**

The Mining Industry Force on IFRSs has issued a Viewpoint discussing some of the accounting considerations for determining the useful life of a mine.

The Viewpoint Series is available online at [www.cpacanada.ca/ifrs](http://www.cpacanada.ca/ifrs)

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### Application Insights

**Useful life of leasehold improvements**

**Source**

IFRS Discussion group

The following insights were obtained from a publicly available IFRS Discussion Group report.

**Meeting Date**

April 19, 2012

**Topic**

IAS 16: Useful Life of Leasehold Improvements

**Insights**

IAS 16 *Property, Plant and Equipment* requires the depreciable amount of an asset to be allocated on a systematic basis over its useful life.

In determining a “lease term”, IAS 17 *Leases* requires that a renewal option not be reflected unless it is “reasonably certain” that the option will be exercised. The issue considered by the Group was whether the lease term represents the useful life for leasehold improvements under IAS 16 when the lessee is not reasonably certain it will exercise an option to extend a lease.

**Fact Pattern:**

- A lessee enters into an operating lease for an office property that has:
  - an initial term of five years; and
  - an option for the lessee to extend the lease for a further five years at market rates.
- Upon commencement of the lease term, the lessee:
  - spends $2 million on an immovable leasehold improvement specific to the property, that has an economic life of seven years; and
  - expects to exercise the extension option, but is not reasonably certain it will do so.

Should the useful life of the leasehold improvements be the shorter of the lease term and the asset’s economic life (i.e., five years) (View A) or the asset’s expected economic life (i.e., seven years) (View B)?

Proponents of View A refer to paragraph 56(d) of IAS 16 and the definition of lease term under IAS 17, arguing that a consistent approach to amortization should be used.

Proponents of View B give more weight to paragraphs 56(a) and 57 of IAS 16, focusing on the expected use of the asset.
**APPLICATION INSIGHTS**

**Useful life of leasehold improvements**

*The Group's Discussion*

Group members noted that it is difficult to understand how the lessee in this fact pattern can expect to exercise the extension option but not be reasonably certain it will do so. As a result, Group members questioned how often the fact pattern would occur in practice.

Several Group members observed that there is a relatively unclear distinction between expected and reasonably certain. They expressed the view that expected and reasonably certain do not represent different thresholds.

Group members also noted that, from a practical perspective, management would align the lease term with the economic life of significant leasehold improvements and, in most cases, a financial statement preparer would arrive at compatible approaches.

Group members made several other observations, including that there may be an economic incentive to renew the lease and that only IAS 16 applies to the amortization of the asset (i.e., IAS 17 does not apply).

The Group agreed that this issue should not be brought to the attention of the IFRS Interpretations Committee because the issue is not expected to arise in practice frequently.

Written reports and audio webcasts of the Group’s discussion for each agenda topic are available online at www.frascanada.ca.

**Depreciation Start Date**

[IAS 16.55]

Depreciation of an asset begins when the asset is available for use. This means that it should be in the location and condition necessary for it to be capable of operating in the manner intended by management.

The starting date for depreciating a major spare part or standby equipment classified as PP&E is generally the date it is available for use.

**APPLICATION EXAMPLE**

**Depreciation of standby equipment**

ABC Ltd. owns a specialized piece of equipment powered by a generator 24 hours a day, all year round. ABC also has another generator installed and ready for use should the operating generator break down.

The standby generator is classified as PP&E when it meets the definition of PP&E (i.e., held for use in the production or supply of goods and services, for rental to others, or for administrative purposes, and expected to be used during more than one period (IAS 16.8)). Since amortization should begin when the standby generator is “available for use,” it should be amortized as soon as it begins serving as a backup for the operating generator.

The method of amortization will depend on what is considered a systematic basis over its useful life. If the generator’s useful life is based on the passage of time, it will be amortized along with the one being used; if it is based on usage, there may be no measured amount of amortization until it is actually put into use.
Depreciation End Date
[IAS 16.55]
IAS 16 indicates depreciation of an asset ceases at the earlier of the date the asset is classified as held for sale (or included in a disposal group classified as held for sale), in accordance with IFRS 5, and the date the asset is derecognized.

Depreciation Method
[IAS 16.60–.61]
IAS 16 specifies that the depreciation method must closely reflect the way an entity consumes an asset’s future economic benefits over the asset’s estimated useful life.

An annual review of the depreciation method applied to an item of PP&E is required.

Acceptable Depreciation Methods
[IAS 16.62]
IAS 16 provides a variety of depreciation methods for allocating the depreciable amount of an asset on a systematic basis over its useful life, such as:
• the straight-line method (constant charge over the asset’s useful life);
• the diminishing balance method (decreasing charge over the asset’s useful life); and
• the units of production method (charge based on the expected use or output of the asset).

The standard is not prescriptive. Entities should choose the method that most closely reflects their expected pattern of consumption of the asset’s future economic benefits. That method should be applied consistently from period to period unless there is a change in the expected pattern of consumption of those future economic benefits.

As noted in the Standards Update section of this publication, in December 2012 the IASB issued an ED proposing a narrow-scope amendment to IAS 16. The objective of the proposed amendment is to ensure preparers do not use revenue-based methods to calculate charges for the depreciation or amortization of items of PP&E or intangible assets. The proposed amendment also provides further guidance in the application of the diminishing balance method.
In practice, oil and gas properties are depleted by analogy to IAS 16 and IAS 38. The unit of production method is most commonly used to deplete such assets. In a survey of select junior oil and gas company financial statements, 90% disclosed the use of proved and probable reserves for application of this method and 7% disclosed the use of proved reserves.

The publication is available online at www.cpacanada.ca/ifrs

The following two insights look at methods of depreciation. Note the date of the NIFRICs. Even though some NIFRICs are older, they still provide some insight into how the standards are interpreted by the standard setters.

### APPLICATION INSIGHTS

**Depreciation of fixed assets**

<table>
<thead>
<tr>
<th>Source</th>
<th>NIFRIC</th>
<th>Meeting Date</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>May 2004</td>
</tr>
</tbody>
</table>

The following insights were obtained from “IFRIC—items not taken onto the agenda” report.

**Issue**

The Committee considered a potential issue as to whether the production method of depreciation could be used under IAS 16 Property, Plant and Equipment if an asset is not consumed (worn down) directly in relation to the level of use. For example, if a road with a greater capacity than current demands is built, should depreciation in the initial period be lower than in later periods, if usage is expected to increase over the life of the asset?

**Reason for not adding to the IFRIC agenda**

The IFRIC agreed that this was foremost a conceptual area and decided not to add it to the IFRIC agenda. However, the IFRIC recommended that this topic be considered by the Board as part of the Concepts project.

Details of the issues that have been considered by the IFRIC but not added to its agenda are available online at www.ifrs.org/.
APPLICATION INSIGHTS
IAS 16 and IAS 17: Depreciation of assets leased under operating leases

<table>
<thead>
<tr>
<th>Source</th>
<th>NIFRIC</th>
</tr>
</thead>
<tbody>
<tr>
<td>Meeting Date</td>
<td>November 2004</td>
</tr>
</tbody>
</table>

The following insights were obtained from “IFRIC—items not taken onto the agenda” report.

**Issue**

The IFRIC considered whether interest methods of depreciation were permissible under IFRSs. Use of such methods would permit an entity to depreciate an asset that is not a receivable in much the same way as if it were a receivable, with the result that the depreciated amount of the asset reflects the present value of future net cash flow expected from it.

**Reason for not adding to the IFRIC agenda**

The IFRIC noted that, while deliberating certain issues related to service concessions, it had considered whether it would be appropriate to use an interest method of depreciation. In that discussion, it concluded that using an interest method of depreciation was not appropriate. The IFRIC concluded that there was nothing unique about assets leased under operating leases in service concessions that would cause it to reach a different conclusion about the use of interest methods of depreciation. It noted that the Basis for Conclusions in the future Interpretations on service concessions would include a discussion of its conclusions on interest methods of depreciation.

Details of the issues that have been considered by the IFRIC but not added to its agenda are available online at www.ifrs.org/.

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**Changes in Depreciation Method**

[IAS 16.61]

If there is a significant change in the expected pattern of consumption of an asset’s future economic benefits, the depreciation method should be adjusted to reflect the changed pattern. This change would be recognized as a change in accounting estimate (unless the change is to correct an error), in line with IAS 8.
Impairment and Compensation for Impairment

2.8 Property, plant and equipment (in part)

When the significant parts of an item of property, plant and equipment have varying useful lives, they are accounted for as separate components of property, plant and equipment. Depreciation is calculated based on the depreciable amount of the asset or significant component thereof, if applicable, which is the cost of the asset or significant component less its residual value. Depreciation is recognized using the straight-line method for each significant component of an item of property, plant and equipment and is recorded in “Selling, administrative and other expenses” in the Consolidated Statements of Net Earnings (Loss) and Comprehensive Income (Loss). The estimated useful lives are 2 to 13 years for equipment and fixtures and 10 to 50 years for buildings and building improvements. The estimated useful lives, residual values and depreciation methods for property, plant and equipment are reviewed annually and adjusted, if appropriate, with the effect of any changes in estimates accounted for on a prospective basis.

EXTRACT 15—EXCERPT FROM SEARS CANADA INC. 2012 FINANCIAL STATEMENTS

NOTE 2—SIGNIFICANT ACCOUNTING POLICIES

2.8 Property, plant and equipment (in part)

An impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount. Recoverable amount is defined in IAS 16 as the higher of an asset’s fair value less costs to sell or its VIU.

To determine whether a PP&E item is impaired, an entity applies IAS 36. This standard provides guidance as to when to assess impairment, how to determine the recoverable amount and when to recognize an impairment loss. It also provides guidance on reversal of impairment losses. When there is a subsequent increase in the recoverable amount of an impaired asset, the previously recognized impairment loss is reversed. For PP&E assets carried at cost, the amount of the recovery is limited to the carrying value of the asset that would have been determined (net of depreciation) had no impairment loss been recognized for the asset in prior years. This requirement means that an entity must be able to reconstruct the pre-impairment carrying amount of the asset.

EXTRACT 16—EXCERPT FROM ROYAL BANK OF CANADA 2012 FINANCIAL STATEMENTS

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, ESTIMATES AND JUDGMENTS

Premises and equipment (in part)

Premises and equipment are assessed for indicators of impairment at each reporting period. If there is an indication that an asset may be impaired, an impairment test is performed by comparing the asset’s carrying amount to its recoverable amount. Where it is not possible to estimate the recoverable amount of an individual asset, we estimate the recoverable amount of the CGU to which the asset belongs and test for impairment at the CGU level. An impairment charge is recorded to the extent the recoverable amount of an asset (or CGU), which is the higher of fair value less costs to sell and value in use, is less than its carrying amount. Value in use is the present value of the future cash flows expected to be derived from the asset (or CGU).

After the recognition of impairment, the depreciation charge is adjusted in future periods to reflect the asset’s revised carrying amount. If an impairment is later reversed, the carrying amount of the asset is revised to the lower of the asset’s recoverable amount and the carrying amount that would have been determined (net of depreciation) had there been no prior impairment loss. The depreciation charge in future periods is adjusted to reflect the revised carrying amount.

June 2013
Compensation for Impairment
[IAS 16.65]

If an entity receives third-party compensation for PP&E items that were impaired, lost or given up, the compensation is recognized in profit or loss when receivable.

Derecognition of PP&E
[IAS 16.67 -.72]

The carrying amount of an item of PP&E is derecognized:
• on disposal; or
• when no future economic benefits are expected from its use or disposal.

The disposal date is the date at which the criteria for recognizing revenue from the sale of goods in IAS 18 are met. IAS 17 applies to disposal by a sale and leaseback.

An entity is required to derecognize the carrying amount of a part of a PP&E item if that part has been replaced and the entity has included the cost of the replacement part in the carrying amount of the item. This is required even if the part was not a significant component and was, therefore, not depreciated separately.

When a PP&E item is disposed of, the gain or loss on disposal is included in profit or loss unless IAS 17 requires otherwise on the sale and leaseback of an asset. The gain or loss is determined as the difference between the net disposal proceeds, if any, and the carrying amount of the asset.

Consideration receivable is recognized at fair value and, if payment is deferred, the compensation is recognized at the cash price equivalent; any difference between the recognized amount and the nominal amount is recognized as interest revenue reflecting the effective yield on the receivable. The gain or loss arising from derecognition of a PP&E item is not classified as revenue.

The following insight looks at the issue of classification of revenue from the sale of assets held for rental. Note the date of the NIFRIC. Even though some NIFRICs are older, they still provide some insight into how the standards are interpreted by the standard setters.
### APPLICATION INSIGHTS

**IAS 16 Property, Plant and Equipment—Sale of assets held for rental**

<table>
<thead>
<tr>
<th>Source</th>
<th>NIFRIC</th>
</tr>
</thead>
<tbody>
<tr>
<td>Meeting Date</td>
<td>May 2007</td>
</tr>
</tbody>
</table>

The following insights were obtained from “IFRIC—items not taken onto the agenda” report.

**Issue**

The IFRIC was asked to provide guidance on the accounting for sales of assets held for rental. Some entities sell assets after renting them out to third parties. In such circumstances, it appears that the asset is manufactured or acquired with a dual intention, to rent it out and to sell it. The issue is whether the sale of such an asset should be presented gross (revenue and costs of sales) or net (gain or loss) in the income statement.

**Reason for not adding to the IFRIC agenda**

The IFRIC noted that IAS 16 paragraph 68 states that gains arising from derecognition of an item of property, plant and equipment shall not be classified as revenue. Also, when the asset is classified as held for sale under IFRS 5 Non-current Assets Held for Sale and Discontinued Operations, IFRS 5 paragraph 24 refers to the derecognition requirements of paragraphs 67–72 of IAS 16, thereby confirming that gains should not be classified as revenue. However, some believed that, in some limited circumstances, reporting gross revenue in the income statement would be consistent with the Framework paragraph 72, with IAS 18 Revenue, IAS 2 Inventories, and IAS 40 Investment Properties and with the prohibition on offsets in IAS 1 Presentation of Financial Statements.

For this reason, the IFRIC decided to draw the issue to the attention of the Board and not to take the item onto its own agenda.

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Details of the issues that have been considered by the IFRIC but not added to its agenda are available online at [www.ifrs.org/](http://www.ifrs.org/).

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### EXTRACT 17—EXCERPT FROM SHOPPERS DRUG MART CORPORATION 2012 FINANCIAL STATEMENTS

**NOTE 3—SIGNIFICANT ACCOUNTING POLICIES**

(i) **Property and Equipment and Investment Property (in part)**

(i) **Recognition and Measurement (in part)**

Gains and losses on disposal of an item of property and equipment are determined by comparing the proceeds from disposal with the carrying amount of property and equipment and are recognized net, within operating and administrative expenses, in net earnings.
An entity that, in the course of its ordinary activities, routinely sells PP&E items held for rental to others, should transfer such assets to inventory at their carrying amount when they cease to be rented and are held for sale. The proceeds from the sale of such assets should be recognized as revenue in accordance with IAS 18. In such cases, IFRS 5 does not apply.

**Disclosure**  
[IAS 16.73–.79]

For many entities, PP&E is a major part of the statement of financial position. The depreciation of these assets can have a material impact on profit or loss. Thus, it is not surprising that IAS 16 includes significant disclosure requirements. The following chart summarizes some of the disclosures relating to PP&E.

**ILLUSTRATION 6—SUMMARY OF SOME IAS 16 DISCLOSURE REQUIREMENTS**

<table>
<thead>
<tr>
<th>Type</th>
<th>Disclosure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Type</td>
<td>Disclosure</td>
</tr>
<tr>
<td>-------------------------------</td>
<td>---------------------------------------------------------------------------------------------------------------------------------------------</td>
</tr>
</tbody>
</table>
| Estimate changes              | • nature and effect of any change in a PP&E accounting estimate that has an effect in the current period or is expected to have an effect in subsequent periods  
• changes in estimate could relate to:  
  • residual values  
  • estimated costs of dismantling, removing and restoring items of PP&E  
  • useful lives  
  • depreciation methods |
| Revaluation model             | • effective date of revaluation  
• whether an independent valuer was involved  
• for each revalued PP&E class, the carrying amount that would have been recognized had the assets been carried under the cost model  
• the revaluation surplus, indicating the change for the period and any restrictions on the distribution of the balance to shareholders  
• additional disclosures required by IFRS 13  
• a change in the revaluation surplus arising from a change in the liability for an existing decommissioning, restoration or similar liability (IAS 1 requires disclosure in the statement of comprehensive income of each component of other comprehensive income or expense IFRIC 16(d)) |
| Constructed assets            | • the amount of expenditures recognized in the carrying amount of a PP&E item in the course of its construction |
| Impaired assets               | • the amount of compensation from third parties for items of PP&E that were impaired, lost or given up, included in profit or loss (if not separately presented in the statement of comprehensive income)  
• disclosures required by IAS 36 |
| Restrictions and commitments | • the existence and amounts of restrictions on title and PP&E pledged as security for liabilities  
• the amount of contractual commitments for the acquisition of PP&E |
| Disclosures encouraged but not required | • temporarily idle PP&E  
• fully depreciated PP&E still in use  
• PP&E retired from active use but not classified as held for sale  
• fair value of PP&E recognized under the cost model when materially different from the carrying amount |
IAS 16 suggests but does not require disclosure of the gross carrying amount of fully depreciated PP&E still in use. As IAS 16 requires a review of the useful life, residual value and depreciation method at least at each financial year-end, the existence of such assets is likely to be rare.

More general disclosure requirements under IAS 1 must also be met as they relate to PP&E. These include accounting policies, significant judgments made in applying accounting policies and sources of estimation uncertainty. Examples include:

- IAS 1.117 requires that the entity disclose a summary of significant accounting policies. This is especially important where there are accounting policy choices.
- IAS 1.122 requires disclosure of judgments made in the process of applying the entity’s accounting policies that have the most significant effect on the amounts recognized in the financial statements.
- IAS 1.125 requires disclosure of information about the future and other major sources of estimation uncertainty at the end of the reporting period that have a significant risk of resulting in material adjustment to the carrying amounts of assets and liabilities within the next financial year.

The following insight looks at the disclosure of temporarily idle assets or assets under construction when further construction has been postponed. Note the date of the NIFRIC. Even though some NIFRICs are older, they still provide some insight into how the standards are interpreted by the standard setters.
The following insights were obtained from “IFRIC—items not taken onto the agenda” report.

**Issue**

The IFRIC received a request for more guidance on the extent of required disclosures relating to property, plant and equipment temporarily idle or assets under construction when additional construction has been postponed. In accordance with paragraph 74(b) of IAS 16, an entity is required to disclose the amount of expenditures recognised in the carrying amount of an item of property, plant and equipment in the course of its construction. Paragraph 79(a) encourages an entity to disclose the amount of property, plant and equipment that is temporarily idle.

The IFRIC also noted that paragraph 112(c) of IAS 1 requires an entity to provide in the notes information that is not presented elsewhere in the financial statements that is relevant to their understanding. The IFRIC noted that disclosure regarding idle assets might be particularly relevant in the current economic environment. Consequently, the IFRIC expected that entities would provide information in addition to that specifically required by IAS 16 whenever idle assets or postponed construction projects become significant.

**Reason for not adding to the IFRIC agenda**

Given the requirements of IAS 16 and IAS 1, the IFRIC did not expect significant diversity in practice and decided not to add this issue to its agenda. However, the IFRIC recommended that the Board should undertake a review of all disclosures encouraged (but not required) by IFRSs with the objective of either confirming that they are required or eliminating them.
The following extract provides an example of a reconciliation of the carrying amounts of assets at the beginning and end of the period.

**EXTRACT 18—EXCERPT FROM TELUS CORPORATION 2012 FINANCIAL STATEMENTS**

**NOTE 15—PROPERTY, PLANT AND EQUIPMENT**

<table>
<thead>
<tr>
<th>(millions)</th>
<th>Network assets</th>
<th>Buildings and leasehold improvements</th>
<th>Assets under finance leases</th>
<th>Other</th>
<th>Land</th>
<th>Assets under construction</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>At cost</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>As at January 1, 2011</td>
<td>$22,691</td>
<td>$2,351</td>
<td>$21</td>
<td>$1,550</td>
<td>$49</td>
<td>$438</td>
<td>$27,100</td>
</tr>
<tr>
<td>Additions(^1)</td>
<td>516</td>
<td>20</td>
<td>1</td>
<td>41</td>
<td>7</td>
<td>887</td>
<td>1,472</td>
</tr>
<tr>
<td>Additions arising from business acquisitions (Note 16(a))</td>
<td>–</td>
<td>11</td>
<td>–</td>
<td>7</td>
<td>–</td>
<td>–</td>
<td>18</td>
</tr>
<tr>
<td>Dispositions, retirements and other (223)</td>
<td>(6)</td>
<td>1</td>
<td>(51)</td>
<td>[1]</td>
<td>–</td>
<td>(279)</td>
<td></td>
</tr>
<tr>
<td>Reclassifications</td>
<td>779</td>
<td>99</td>
<td>–</td>
<td>75</td>
<td>–</td>
<td>(663)</td>
<td>–</td>
</tr>
<tr>
<td>As at December 31, 2011</td>
<td>23,766</td>
<td>2,473</td>
<td>23</td>
<td>1,622</td>
<td>55</td>
<td>372</td>
<td>28,311</td>
</tr>
<tr>
<td>Additions(^1)</td>
<td>559</td>
<td>21</td>
<td>–</td>
<td>42</td>
<td>–</td>
<td>990</td>
<td>1,012</td>
</tr>
<tr>
<td>Additions arising from business acquisitions (Note 16(a))</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>2</td>
<td>–</td>
<td>–</td>
<td>2</td>
</tr>
<tr>
<td>Dispositions, retirements and other (1,129)</td>
<td>(16)</td>
<td>(17)</td>
<td>(60)</td>
<td>–</td>
<td>–</td>
<td>(1,226)</td>
<td></td>
</tr>
<tr>
<td>Reclassifications</td>
<td>795</td>
<td>142</td>
<td>–</td>
<td>38</td>
<td>–</td>
<td>(975)</td>
<td>–</td>
</tr>
<tr>
<td>As at December 31, 2012</td>
<td>$24,004</td>
<td>$2,620</td>
<td>$6</td>
<td>$1,624</td>
<td>$55</td>
<td>$377</td>
<td>$28,686</td>
</tr>
<tr>
<td><strong>Accumulated depreciation</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>As at January 1, 2011</td>
<td>$16,535</td>
<td>$1,443</td>
<td>$10</td>
<td>$1,261</td>
<td>–</td>
<td>–</td>
<td>$19,269</td>
</tr>
<tr>
<td>Depreciation</td>
<td>1,031</td>
<td>121</td>
<td>2</td>
<td>117</td>
<td>–</td>
<td>–</td>
<td>1,331</td>
</tr>
<tr>
<td>Dispositions, retirements and other (218)</td>
<td>(4)</td>
<td>8</td>
<td>(39)</td>
<td>–</td>
<td>–</td>
<td>(253)</td>
<td></td>
</tr>
<tr>
<td>As at December 31, 2011</td>
<td>17,428</td>
<td>1,560</td>
<td>20</td>
<td>1,399</td>
<td>–</td>
<td>–</td>
<td>20,347</td>
</tr>
<tr>
<td>Depreciation</td>
<td>1,132</td>
<td>126</td>
<td>3</td>
<td>101</td>
<td>–</td>
<td>–</td>
<td>1,422</td>
</tr>
<tr>
<td>Dispositions, retirements and other (1,127)</td>
<td>(16)</td>
<td>(17)</td>
<td>(60)</td>
<td>–</td>
<td>–</td>
<td>(1,248)</td>
<td></td>
</tr>
<tr>
<td>As at December 31, 2012</td>
<td>$17,439</td>
<td>$1,674</td>
<td>$6</td>
<td>$1,448</td>
<td>–</td>
<td>–</td>
<td>$20,521</td>
</tr>
<tr>
<td><strong>Net book value</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>As at December 31, 2011</td>
<td>$6,338</td>
<td>$913</td>
<td>$3</td>
<td>$283</td>
<td>$55</td>
<td>$372</td>
<td>$7,964</td>
</tr>
<tr>
<td>As at December 31, 2012</td>
<td>$6,511</td>
<td>$948</td>
<td>$–</td>
<td>$276</td>
<td>$55</td>
<td>$377</td>
<td>$8,165</td>
</tr>
</tbody>
</table>

\(^1\) For the year ended December 31, 2012, additions include $49 (2011 – $71) in respect of asset retirement obligations (see Note 19(a)).

The gross carrying amount of fully depreciated property, plant and equipment that was still in use as at December 31, 2012, was $2.9 billion (2011 – $3.0 billion). As at December 31, 2012, our contractual commitments for the acquisition of property, plant and equipment were $187 million over a period through to 2014 (2011 – $188 million over a period through to 2013).

**Accounting Policy Choices**

The following chart summarizes some significant accounting policy choices in IAS 16.

<table>
<thead>
<tr>
<th>Reference</th>
<th>Policy choice</th>
<th>Alternatives</th>
<th>Insights</th>
</tr>
</thead>
<tbody>
<tr>
<td>IAS 16.29</td>
<td>Measurement of PP&amp;E after recognition</td>
<td>1. Cost model 2. Revaluation model</td>
<td>The policy choice is made for each class of PP&amp;E and must apply to the entire class. A class of PP&amp;E is a grouping of assets of a similar nature and use in an entity’s operations.</td>
</tr>
<tr>
<td>Reference</td>
<td>Policy choice</td>
<td>Alternatives</td>
<td>Insights</td>
</tr>
<tr>
<td>-----------</td>
<td>--------------</td>
<td>--------------</td>
<td>----------</td>
</tr>
<tr>
<td>IAS 16.35</td>
<td>Revaluation of depreciable assets</td>
<td>When an item of PP&amp;E is revalued, any accumulated depreciation at the date of revaluation is treated in one of two ways:² &lt;br&gt;1. Restate proportionately with the change in the gross carrying amount of the asset so that the carrying amount of the asset after revaluation equals its revalued amount &lt;br&gt;2. Eliminate against the gross carrying amount of the asset and the net amount restated to the revalued amount of the asset</td>
<td>Alternative 1 is often used when an asset is revalued by means of applying an index to determine its replacement cost (see IFRS 13). Alternative 2 is often used for buildings.</td>
</tr>
<tr>
<td>IAS 16.41</td>
<td>Transferring revaluation surplus</td>
<td>1. Transfer revaluation surplus to retained earnings on asset derecognition &lt;br&gt;2. Transfer a relevant portion of the revaluation surplus to retained earnings as the asset is depreciated, with the balance remaining (if any) transferred on asset derecognition &lt;br&gt;3. No transfer of revaluation surplus to retained earnings</td>
<td>Alternative 1 may involve transferring the whole of the surplus when the asset is retired or disposed of. For alternative 2, the amount of the surplus transferred would be the difference between depreciation based on the revalued carrying amount of the asset and depreciation based on the asset’s original cost.</td>
</tr>
</tbody>
</table>

² Note: Refer to the Standards Update section in this publication. A proposed amendment to IAS 16 would change the guidance in (1) below and state that accumulated depreciation is computed as the difference between the gross and net carrying amounts. The amendment will also clarify that the determination of accumulated depreciation does not depend on the selection of the valuation technique.
The revaluation surplus transfers referred to in IAS 16.41 are implied to be at the option of the reporting entity, rather than being mandated by the Standard. There would, therefore, appear to be another alternative—to make no reserve transfer (alternative 3). That option would, however, result in the permanent retention of the portion of the revaluation reserve relating to assets that have been fully depreciated or disposed of.

Transfers from revaluation surplus to retained earnings are not made through profit or loss.
**Significant Judgments and Estimates**

The following chart summarizes some possible significant judgments and sources of estimation uncertainty required by IAS 16. This is not meant to be an exhaustive list and other judgments and/or estimates most certainly exist within IAS 16.

**ILLUSTRATION 7—SOME SIGNIFICANT JUDGMENTS AND SOURCES OF ESTIMATION UNCERTAINTY UNDER IAS 16**

<table>
<thead>
<tr>
<th>Judgments</th>
<th>Sources of estimation uncertainty</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Policy choice</strong></td>
<td><strong>Both cost model and revaluation model</strong></td>
</tr>
<tr>
<td>• whether to measure PP&amp;E using the cost model or the revaluation model value (IAS 16.29)</td>
<td>• determination of the residual value of a depreciable item of PP&amp;E</td>
</tr>
<tr>
<td></td>
<td>• determination of the useful life of a depreciable item of PP&amp;E</td>
</tr>
<tr>
<td></td>
<td>• timing and amount of costs of dismantling, removal and site restoration and changes to these costs</td>
</tr>
<tr>
<td></td>
<td>• discount rate to be used for the above</td>
</tr>
<tr>
<td></td>
<td>• recoverability of tangible capital assets</td>
</tr>
<tr>
<td></td>
<td>• estimate of the recoverable amount for impairment testing</td>
</tr>
<tr>
<td></td>
<td><strong>Revaluation model</strong></td>
</tr>
<tr>
<td></td>
<td>• determination of fair value of revalued items of PP&amp;E</td>
</tr>
<tr>
<td><strong>Both cost model and revaluation model</strong></td>
<td>• unit of measure for recognition of an item of PP&amp;E (i.e., the amount of aggregation)</td>
</tr>
<tr>
<td></td>
<td>• determination of which costs (initial and subsequent) meet the recognition criteria of IAS 16, including which costs are directly attributable (e.g., safety equipment, spare parts, replacement parts, inspection costs and costs for self-constructed assets)</td>
</tr>
<tr>
<td></td>
<td>• significant components of assets and the allocation of costs to components (for depreciation)</td>
</tr>
<tr>
<td></td>
<td>• selection of depreciation methods and depreciation start date</td>
</tr>
<tr>
<td></td>
<td>• how much detail to provide in note disclosures</td>
</tr>
<tr>
<td></td>
<td>• assessment of impairment under IAS 36</td>
</tr>
<tr>
<td></td>
<td>• when an item of PP&amp;E should be derecognized.</td>
</tr>
<tr>
<td><strong>Revaluation model</strong></td>
<td>• frequency of revaluations</td>
</tr>
<tr>
<td></td>
<td>• how to treat accumulated depreciation on revaluation of an item of PP&amp;E (IAS 16.35)</td>
</tr>
<tr>
<td></td>
<td>• when to transfer a revaluation surplus to retained earnings (IAS 16.41)</td>
</tr>
</tbody>
</table>
The preparation of the Company’s consolidated financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the end of the reporting period. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

However, uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods. In the process of applying the Company’s accounting policies, management has made the following judgments, estimates and assumptions which have the most significant effect on the amounts recognized in the consolidated financial statements:

- **Property, Plant and Equipment**

  Property, plant and equipment are stated at cost less accumulated depreciation, including any asset impairment losses. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets. The estimated useful lives of property, plant and equipment are reviewed on an annual basis. Assessing the reasonableness of the estimated useful lives of property, plant and equipment requires judgment and is based on currently available information. Property, plant and equipment are also reviewed for potential impairment on a regular basis or whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

  Changes in circumstances, such as technological advances and changes to business strategy can result in actual useful lives and future cash flows differing significantly from estimates. The assumptions used, including rates and methodologies, are reviewed on an ongoing basis to ensure they continue to be appropriate. Revisions to the estimated useful lives of property, plant and equipment or future cash flows constitute a change in accounting estimate and are applied prospectively.
### Appendix A — Acronyms Used

<table>
<thead>
<tr>
<th>Acronym</th>
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<tr>
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<td>Other comprehensive income</td>
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<td>Property, plant and equipment</td>
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