

**PROVISION FOR DECOMMISSIONING: THEORY AND REALITY IN SPAIN**

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**Abstract**

The international accounting harmonization has led to the repeal of accounting rules and the adoption of a new accounting model in Spain, the abandonment of the 1990 Plan and the implementation of 2008 Plan, based on the IFRS issued by the International Accounting Standards Board (IASB). This change of model entails, the abolition of the reversion fund concept that occasionally collects future outlays for retirement, dismantling and similar ones.

This paper analyzes one of the novelties, singularity and the registration of the costs of dismantling, rehabilitation or withdrawal. The recent Spanish rule ICAC 01/03/2013 develops those regulations. Our purpose of this inquiry is to present global changes affecting the rubric of the property, plant and equipment (PP&E), then focuses on the treatment of the costs of dismantling, discusses the experience of the first year of application contrasting such information with the published one at the level of consolidated financial statements under IFRS and simultaneously explores aspects not solved by current legislation.

**Keywords:** Provision for decommissioning, withdrawal, restoration, rehabilitation, plant and equipment, environmental liability, European Union regulations

**INTRODUCTION**

The study of these accounting problems has significant social interest, because environmental regulations are increasingly demanding in terms of rehabilitation of land (for example contaminated by the activity of the factory installed there) decommissioning of infrastructure (eg platforms oil after ending the exploitation of nuclear power plants that have reached the end of its useful life and must be dismantled), restoration of the environmental surroundings (eg closure of quarries and mines, involving costs of reforestation, planting of trees, crops, etc.)

It may be noted that the impact of these dismantling works and similar ones affects not only the cost of the manufactured goods. In some sectors, such as the generation of electricity, these dismantling actions and similar ones impact on the rate of light which ends up by being paid by the households, the families. This is why the appropriate accounting treatment of these items allows correctly reflect the negative externalities that involve the forced dismantling, decontamination business.... The financial information accordingly prepared that facilitates governments, investors and citizens can accurately measure the economic impact of these activities.

To read the new annual accounts for the financial year 2008, it is easy to warn that the composition of the rubric of property, plant and equipment (in later PP&E) differs between the

2008 balance and the balance 2007, as well as the assessment. For the financial year 2008, with the implementation of the new PGC 2008 accounting information users encounter in the individual balance sheet a new concept of PP&E, grafted in our legislation for the sake of IFRS accounting harmonization. This implies that items until 2007 were not included among the PP&E are reflected in the balance of 2008, but there are also situations on the opposite side, assets that until 2007 were included as PP&E from the financial year 2008 contained in other headings of the balance sheet or may even have disappeared (would be the case with the transferred PP&E in leasing)

The new framework accounting of Plan 2008, faced with the usual conception of PP&E excludes elements traditionally considered as such (by use or destination reasons) and incorporates others, usually unrelated to this rubric, by reasons of possession. At the same time, it leaves unresolved the cataloguing of other elements, or at least we have failed to find a reference that spin out of application in PGC 2008. As an example of some special situations, we emphasize the following:

(a) The permanent assets that the company keeps such as real estate and investment properties for capital gains (IAS 40) are contained in the balance sheet outside PP&E. Traditionally, the user of the financial statements found these elements reflected between the PP&E. In the case of companies in the real estate sector the boundary between PP&E, real estate, stocks and 58 () ANCMV at times will be complex task, as well as the possible reclassifications between the different headings above.

(b) The so-called biological assets (IAS 41), not addressed in the new Plan 2008 but we do find them disaggregated and differentiated in the Circular 1/2005 of 1 April, the CNMV, which amends the models of public periodic information of CAs of securities admitted to trading on stock exchanges. In our view, even in the absence of this category at the new Plan 2008, we believe that we should differentiate in accountable way with the above nomenclature, as stated in the Circular 1/2005 or own IFRS.

(c) Differentiation of material assets which have been leased by third parties under operating leases. This informative breakdown does appear for example, in Circular 4/2004 of the Bank of Spain. In the case of a company manufacturer of an asset (e.g. machinery) that sold it but that also immediately gives it in operating rental basis, will be raised doubts as to catalog the asset either as inventory or as an PP&E. The decision is not trivial and certainly there is no clear pattern that prescribes when it has to register as PP&E and amortized, or keep it in stock. (In a large European car company listed and IFRS experience we have seen that in rent operating less than a year is accounted as an existence assets and their subsequent disposal as more turnover.) (Conversely, if the rent exceeds one year, asset appears as PP&E ceded to third parties and is therefore subject to depreciation).

(d) in the opposite direction, assets available to the company under leasing contracts, were traditionally excluded from the PP&E not being owned by the company, however now it shall set

forth under this heading. The requirement of property has been replaced by the control. According to the Conceptual framework, an asset "is a resource controlled by the company as a result of past events, of which the enterprise expects to obtain economic benefits in the future." This definition of asset is derived from assets owned by the company, which usually were included in the PP&E, now by "control" have been transferred to a third party not recorded between the PP&E. This would be the case of those elements that the company has given for rent for long periods and conditions for determining that there really is a transfer of the risks and the advantages inherent to the property.

However, the difficulty will be to determine if certain rentals with or without option to buy entail the transfer of the risks and advantages of the ownership of the loaned asset. According to the new Plan 2008, in a lease an asset purchase agreement, it shall be presumed that all the benefits and risks incident to ownership, transfer substantially when there is no reasonable doubt that is going to exercise that option. Similarly and unless there is evidence to the contrary, such transfer shall be presumed although there is no option to purchase, among others, in the following cases:

I. lease contracts in which the ownership of the asset is transferred, or their conditions be deduced to be transferred to the lessee at the end of the lease term.

II. Contracts in which the lease term coincides or cover most of the economic life of the asset, and always the conditions agreed it transpires from the economic rationality of the maintenance of the cession of use. The term of the lease is the period not revocable for which the lessee has contracted the lease of the asset, together with any additional period in which it is entitled to continue with the rental, with or without additional payment, provided that at the start of the lease, it is reasonable to think that I the tenant will take such a choice.

III. in cases where, at the beginning of the lease, the present value of minimum payments agreed to lease assume virtually all of the fair value of the leased asset.

IV. When the special characteristics of the assets of the lease make that its usefulness is restricted to the lessee.

V. The lessee may cancel the rental contract and the losses incurred by the lessor because of such cancellation were assumed by the lessee.

VI. Outcomes arising from fluctuations in the fair value of the residual amount lies on the lessee.

VII. the lessee has the possibility of extending the lease for a second period, with some lease payments that are substantially lower than the usual market.

The list is extensive, but not exclusively, can - rather you must - add other cases in which manifests the transfer of risks and advantages above indicated.

(e) also deserve a thorough analysis to those elements of the PP&E that, in application of the rule of assessment 2008 PGC 7<sup>a</sup>, have to be submitted in the balance sheet separately from the rest of

the assets to be classified as ANCMV, non-current assets held for sale, or as part of a disposal assets group classified as such. The new accounting framework shift these elements to another heading of the balance sheet, so the reader must modify the concept of PP&E which over the years has internalized, and that underlying inexorably at first heritage reading out of the stock of a company.

The list of requirements for the reclassification from the PP&E to the subgroup (58)-ANCMV requires interpretations and prosecutions that are not always simple, but with obvious implications for the asset, financial and economic image showing the company with one or another location in the balance sheet.

(f) in the balance sheets of companies occasionally could be found recorded between the PP&E works of art (paintings, sculptures, libraries,...), jewelry, antiques, etc. The permanence and the tangibility of these elements does not have suspicions, but their purpose or application is more questionable. In the IAS and Plan 2008 we were unable to find any reference to these assets that occasionally integrate the assets of the companies. Can we considered that the mere showcasing of a painting, a statue.... already meets an administrative purpose such as mere ornamentation, or should we treat them in property investment?

In general, plant and equipment usually reach a significant portion of the assets of the companies. In particular, utilities and industrial companies maintained a very high proportion of plant and equipment within its asset.

Delimitation of fixed assets and the amount that will be reflected in the financial statements will have a direct effect on the image projected itself the company. This incidence can come in several ways:

- (a) From measures of solvency.
- (b) From investment measures.
- (c) From the role of efficiency and profitability measures.
- (d) From measures of financial flows.
- (e) From measures for the evaluation of the company.

In particular the measures of solvency and profitability are affected most by the definition and valuation of the PP&E. The costs of decommissioning have impact in the quantification of the PP&E and hence, the measures of solvency and profitability of the companies concerned. In the following paragraphs we will analyse these costs.

## **REGISTRATION AND VALUATION OF THE COSTS OF DECOMMISSIONING AND RELATED COSTS.**

Together with the variation of the concept of PP&E, new PGC 2008 is also an important change in the valuation of the property, plant and equipment of the company with respect to the 1990 PGC. We will then analyze the criterion of activation of the decommissioning costs, standard involving a capital difference compared to the last regulation.

### **COSTS OF DECOMMISSIONING AND RETIREMENT**

In the 2nd valuation rule of the new Plan 2008 the components of the cost of the elements of the PP&E are detailed, namely:

(a) The purchase price, which includes the costs for the entry into operation.

(b) the estimated costs of dismantling or removal of the element, for example: when constructing a factory on land leased for 30 years, commitment to tear down the factory and restore the field at the end of the rental; the dismantling of the nuclear power plant of Zaria, rehabilitation of landfills, underground or open pit of harmful substances storage tanks; rehabilitation of quarries; mining,...

New Plan 2008 provides account **143. Provision for dismantling, removal and rehabilitation of plant and equipment**, indicating that it is up to the estimated amount of the costs of dismantling or removal of fixed assets, as well as the rehabilitation of the place on the settling. The company may incur these obligations at the time of acquiring assets or to use it for a certain period of time.

When incurred in this obligation at the time of purchase assets or arise as a result of using the plant with purpose other than to the production of stock, its motion is as follows:

a) it shall be paid:

a1) to the birth of the obligation, or by subsequent changes in its amount involving an increase in the provision, with charge, generally, to the subgroup 21 accounts.

a2) for the amount of the adjustments arising from the updating of values, with 660 account.

(b) it will load:

b1) at the end of the exercise, by decreases in the amount of the provision caused by a new estimate of the amount, with payment, generally, accounts of the subgroup 21.

b2) when provision, with payment, is applied generally to accounts of the 57 subgroup.

What traditionally was called negative residual value, that is, the costs to be incurred at the end of the useful life of the PP&E in the accounting of the IASB and the new Plan 2008 model constitute an integral part of the cost of the item and must therefore appear at the balance sheet assets.

In the 1990 Plan usually these costs were provided over the useful life of the asset, creating an item in the liabilities of the balance that was finally applied to cover the costs of the removal or dismantling. In the new Plan 2008, such costs are activated from the beginning as more value of the investment, and simultaneously reflected a liability (provision) for identical estimated amount.

Given that the activated amount continues to be an initial estimate of the expected costs, it will often happen that this approach will experience changes in subsequent periods. The Plan has nothing on these circumstances, but the interpretation IFRIC 1 "changes in existing decommissioning liabilities, restoration and similar" occupies the accounting reflection of these alterations in the amount of formed provisions; the answer depends on the valuation approach for IM:

(a) In the assets valued at cost, increases / decreases in the provision are added / subtracted from the cost of the asset

(b) In the assets valued according to the method of the revaluation, such increases / decreases in the provision have as counterpart the reserves of revaluation account or the income statement, depending on the case.

New Plan 2008 only regards the valuation of the PP&E by the cost, accordingly, (apart from the necessary updates to the estimated amount of the provision resulting from the passage of time and the approximation to the date of termination of the provision) will be necessary to increase / reduce the amount of the provision when the estimated final amount of the necessary provision has experienced significant variations.

This approach introduces complexity in the reading and interpretation of the variations in the economic structure of the company. The amount of PP&E that looks at the balance sheet may experience oscillations in its value does not correspond with additions in the composition of the PP&E. In this manner, using the cost method, a specific asset may experience increases in their assessment of the balance sheet, when it is justified by an increase in the provision necessary to assume the inherent future decommissioning costs.

The costs of dismantling that are activated as greater value of the investment will involve a larger base of amortization of the element in question. For non depreciable PP&E, for example a site for sports facilities, land of mines, quarries or agricultural land, which includes the costs of future restoration work on the ground, as investment will have to repay the element in the amount attributable to the provision; over the years that asset helps generate profits. That is, investment in land should be broken down into a non depreciable portion and another one subjected to depreciation. This is a very important conceptual change with respect to the Plan1990, in which land and other natural goods were not subject to amortization.

The addition that incorporates the new Plan2008 to detail the movements of the 143 account deserves a special comment, since it says that when incurred in the obligation of dismantling "as

a result of having used the assets to produce stock, their motion will be similar to the one pointed out for the account 142 provision for other responsibilities". We interpret that laconic demonstration as that the charge would not be held in the PP&E account but in an account of the expenses of Group 6.

The Plan 2008 draft, dated February 2007 - included also the mention of the costs of decommissioning, but without mentioning the use of the asset in the production of inventories. The wording was as follows: "Also, part of the value of plant and equipment, the initial estimate of the value of the obligations arising from the decommissioning or retirement and other associated with the aforementioned asset, such as the costs of rehabilitation of the site on which sits, provided that these obligations will give rise to registration of supplies, in accordance with the rule applicable to these valuation".

Given that the reversion fund has disappeared from the new Plan there will be situations of costs of withdrawal, rehabilitation, dismantling and the like whose accounting inexorably has to redirect towards the provisions that we analyze. Thus the query no. 2, BOICAC 74, with regard to the re-qualification of the carrying amounts in the 1990 Plan as bottom reversal, indicates that administrative concession agreement can be derived "provisions for dismantling, removal and rehabilitation, as incurred in the obligation at the time of purchase a plant and, according to the norm of recording and valuation 2nd"the ' be part of the value of fixed assets, the initial estimate of the current value of the obligations arising from the dismantling, removal and others associated with the asset, such as the costs of rehabilitation of the site on which sits".

It is further alleged that "if obligations are incurred - dismantling and similar - as a result of using assets in the productive activity of the company, those obligations shall be recorded during the period in which the obligation to go generating with account of expenditure which corresponds". We see how the hue which alleges that the ICAC is different from that referred to in the definition of the account (143), the progressive obligation is not limited to the use of the asset in the production of stock, but by using "productive activity", diffuse and vague expression that can be understood that normally reach the totality of the activities of a company.

### **COMMUNITY REGULATORY BACKGROUND.**

If we go to the IFRS we note that this issue is not peaceful and it has experienced ups and downs in the past versions. The version of IAS 16 until 1998 not embodied any reference to the activation of the decommissioning costs. Subsequently, Regulation EC No. 1725 / 2003 (OJ 10 13, 2003) - that it matches the IAS 16 revised 1998 - when detailed cost components, yes includes:

"The cost of property, plant and equipment comprises its purchase price, including import tariffs and non-recoverable excise appeals on the acquisition, as well as any costs directly related to the start-up of the asset for the use to which it is intended." Any possible discount or discount of the price will be deducted to arrive at the cost of the item.

Examples of directly related costs are:

- (a) The cost of physical site preparation;
- (b) The costs of initial delivery and handling or subsequent transport;
- (c) Installation costs;
- (d) Professional fees, such as those paid to architects or engineers; and
- (e) the estimated costs of dismantling and moving the asset as well as those related to the restoration of its location, to the extent that should be considered as a provision for future expenses, as set out in IAS 37, provisions, contingent liabilities and contingent assets."

But according to the existing version, the Regulation EC 2238 / 2004 (OJ 12 31, 2004), the components of the cost of an PP&E include:

- (a) The purchase price, including import tariffs and non-recoverable excise appeals on the acquisition, after deducting any commercial discount or reduction in the price;
- (b) Any costs directly related to the location of the asset in the workplace and in the conditions so that it can operate in the manner provided by the Directorate;
- (c) the initial estimate of the costs of dismantling or removal of the element, as well as the rehabilitation of the site on which sits, when they constitute obligations incurred by the entity as a result of using the element for a given period, with purposes other than the production of inventories during that period.

And it is added in paragraph 18 that "the organization apply IAS 2 inventories, to account for the costs arising from the obligations by dismantling, removal and rehabilitation of the site on which sits the element incurred during a specific period as a result of having used the element to produce inventories." "The costs accounted for under IAS 16 or IAS 2 obligations will be recognized and measured according to IAS 37 provisions, assets, contingent liabilities and contingent".

Thus, it is not until the release of 2004 when it is mentioned that the costs of dismantling and similar linked to assets used in the production of stock, do not affect the cost of the asset or register as an "immediate provision".

One possible interpretation to the paragraph above, would be to consider that the provision for decommissioning is being recognized progressively - charged to the Group's 6 - to PP&E is used in the production of inventories, expenditures which would form part of the cost of production of the exercise. This procedure does not imply an increase in the subject to the future dismantling PP&E, or a higher cost of depreciation or provision contained in the balance sheet for the current value of the amount estimated for the decommissioning.



The interpretation and application of this regulation raises relevant unknowns, namely:

1. Is a given PP&E subjected to dismantling affected or not by future costs as it applies to provide services / transfer or lease to third parties / destination for administrative uses stock production? What is the reason to discriminate on the basis of the given, why the use services is not is equated to the manufacture of goods?

2 - The provision thus endowed progressively does meet the definition and valuation of the liabilities which establishes the framework?

3 The part of the estimated future cost but not provisioned would be a contingent liability or not reported in memory?

4 - What will be the criteria for distributing the estimated cost of dismantling between the years of production of stock, the expected production volume, the years of useful life of the PP&E? , etc.

#### **ENVIRONMENTAL LIABILITIES REFLECT UPON THE RECOMMENDATION OF THE COMMISSION - 05 30, 2001.**

In 2001, the European Union addressed the problem of recognition and valuation of the liabilities environmental through the Commission recommendation of 30 May 2001 concerning the recognition, measurement and the publication of environmental issues in the annual accounts and annual corporate reports, published in the OJEC of 06 13, 2001.

Paragraph 4 of the usual recommendation envisages that it is recognized an environmental responsibility when a reliable estimate of the costs of the obligation can be performed. If, on the date of the balance sheet, there is an obligation whose nature has been defined clearly and that can generate an output stream of resources involving economic benefits, but don't have certainty in the amount or the date, in this case, would recognize a provision, provided that a reliable estimate of the amount of the obligation can be done.

Uncertainties about the date or the amount are due for example to the sanitation technologies in permanent evolution and the nature and extent of sanitation operations to be carried out. In the few cases in which there can be a reliable estimate of the costs, responsibility must be recognized, but must inform the contingent liability.

The European Commission advocates the registration of a provision for the restoration of contaminated sites and the costs of decommissioning, but allows another option.

It is clear that the expenditure related to the tasks of restoration of contaminated sites, elimination of the by-products of accumulated waste and closing or disposal of fixed assets that the company is obliged to make shall recognized in an accountable way.

"Environmental responsibility for restoration of contaminated sites, elimination or closure should be recognised on the date that they begin the company's operations and is born as a result, the obligation." The recognition of this responsibility must not be postponed until they complete the activity or the polluted site has closed. If it is recognized the responsibility, the estimated expenditure will be included as part of the cost of the asset akin to dismantle or remove. This capitalized expenditure subsequently amortised as part of the depreciable amount of the related asset. During the exploitation could cause new damage; "the obligation of the company to restore them is born when environmental damage occurs."

"For the costs of restoration of contaminated sites and dismantling of operations in the long term, the accounting treatment referred to in the previous point is preferred." This accounting treatment is permitted with a gradual increase in the provision for such costs, which is the other option. The company can recognize costs of closure of plants in the long run over the period relating to the operations. "A part of the costs is charged as an expense in each reporting period, showing the resulting balance sheet as a separate responsibility"

The European Commission therefore raises two options:

(A) - preferred, to account for a provision at the beginning of the activity by incorporating more valuable asset to dismantle.

(B) - the alternative, to give gradually a provision during the years of operation, charged to the results.

The choice of one or another criterion presents conceptual dilemmas of scale. So, option A implies that the more polluting, more damage, more burdensome is the asset, more value will have it. Also borrowing is altered by a high debt and asset incorporates a "historic" cost but rather future I margin.

For its part, the choice of option B, progressive creation of a provision, obscured the true value of liabilities which underlies the present incurring high costs future obligation.

In our opinion, new Plan does not provide this option, but the two possible treatments do, since they consider the gradual provision of (143) provision for dismantling when the PP&E is used to produce inventories.

**DECOMMISSIONING COSTS: NEED TO DIFFERENTIATE BETWEEN IMMEDIATE AND PROGRESSIVE ONES.**

In the light of the foregoing analysis, we consider that the regulations should make explicit clearly two possible ACEs, differentiating the following situations:

(a) Cases of "obligation or immediate damage": when an obligation and the outflow of resources is inescapable, and compulsory from the moment of the completion of the installation, or by the mere construction of an installation, entry into service of a farm, that regardless of the level of

exploitation or use of the operation or installation in question. For example, the dismantling of an oil platform, the demolition of a nuclear power station, future overthrow of buildings constructed on foreign soil with temporary concession, inevitable future obligations relating to contracts of lease, etc.

In these cases, it is necessary to initially account for the provision and its counterpart as more of an asset value.

This inescapable obligation motivated by a change in the regulation or a modification in the company's policy, so that subsequent to the entry into operation of the installation would emerge an unavoidable obligation to engage in future decommissioning costs, duty that would not be linked with the production of stock level or the level of operation of the facility may also arise. These situations would correspond to changes in accounting estimates and therefore should register prospectively (present value of future obligation and amortization of the higher cost of the asset in the years remaining).

(b) Assumptions of "obligation or progressive damage": when the degradation is progressive, as the installation is being exploited, keeping a proportionality with the level of production or exploitation of the underlying business.

In these cases, the provision does not arise at the initial moment, but progressively as one cost for the period in which the activity is developed. For example, the obligation to restore the well created with the operation of a quarry pit, as going deeper underground increases the total future disbursement to restore the place.

Also in this case it could happen that a rule after the entry into operation of the asset should make an alteration in the rate of provision of "progressive provision", in which case it does not need to be considered a mistake or change of approach, but you'll have to correct the excess/defect of provision against results.

(c) Of course, there may be business where coexist both impairments coexist simultaneously, immediate obligations and others that are generated in a progressive manner. In such situations will require determining accurately both types of obligations, the birth of responsibilities and register it as appropriate.

In any case, the "immediate provision" should be calculated on the basis of the present value of the best - most likely scenario - estimate of future costs to incur. Subsequently, any change in the estimates (evolution of technology, legislation, or deadline) will be prospectively - exception error or change in criteria-

Variations in the estimated amount of the provision, derived from

-changes in the expiration date,

-variation of the amount of resources needed to meet the obligation, and

-variations in the rate of employed update,

These modifications are incorporated as plus/minus value of the asset affected.

Finally, we have to comment two additional situations related to the decommissioning costs incurred by third parties and the situations in which the entity itself develops with its media the tasks of dismantling foreseen.

- (i) if there are third parties that assume full or partial costs of decommissioning (users of the facilities, Government, insurance,...), but the company has not been released from legal, contractual or implicit obligation to dismantle, it should register all of the provision. Simultaneously, if necessary, you can count a right of being paid on the third one involved by the share of decommissioning power. This appropriation would be subjected to financial update, as is the case with the provision.
- (ii) if the company carries out the tasks of dismantling within their means, should register as an expense the costs incurred and the Sub-group (79-) an excess of supply, while in the Plan 2008 no account is provided.

## **CASES OF COMPANIES**

According to the paragraph number 5. 2 of the normal memory model, in the breakdown of the heading of plant and equipment are required:

*Information about:*

*(a) Costs estimated dismantling, removal and rehabilitation, including as a higher value of the assets, specifying the circumstances taken into account for their valuation.*

In the list of companies we have analyzed, no breakdown presents the information provided by Dr 1514 / 2007 in their individual accounts, and only in the consolidated accounts they provide a little more detail, but also it remains small, not giving the proper interpretation of the movements made, of their own balance of the provision and its counterpart in the asset.

### **FERSA 2008 GROUP:**

In the chapter of the plant and equipment it is indicated that are part of the cost those provisions for dismantling, existing by contract, which are recorded in the implementation underway for its current value as a higher amount of assets (with counterpart provisions) and are depreciated over the lifetime of the Park.

Subsequently, the note 13 provisions consists a provision for decommissioning with a balance of 589.000€ without further explanation and also created completely during the financial year 2008, that the aforementioned provision had a zero balance at the close of the

Financial years 2006 and 2007. Instead, another accounted for provision (401.000€ for responsibilities) has really earned three large paragraphs of details.

COAL GROUP VASCO-LEONESA 2008:

The company only indicates in the heading for the presentation of the property, plant and equipment "In the case of open-air holdings, future costs that society must face in relation to the restoration of them are incorporated into assets for its current value with subscription to the heading "Provisions in the long term".

"The section on "Environmental proceedings" indicates that "society has incorporated a provision to deal with the costs of restoration and maintenance of the land affected by mining, whose amount to 12 31, 2008 is 7.067.000€." In this exercise, the provision for environmental proceedings has provisioned into 1.098.000€, financed by financial costs (244,000€, approximately 4% of the previous balance) and charged to other operating (854.000€) expenses.

Please note that SA not delimits the activated rehabilitation provisions of other provisions of gradual staffing, making impossible to know the amount of the costs of decommissioning, restoration and withdrawal enabled.

GROUP ABERTIS 2008:

When it comes to the chapter of provisions, there is not a single reference to the provisions for decommissioning and similar, or in the heading of plant and equipment reflected any detail of the activated provisions.

GROUP ENDESA 2008:

It can be seen that the provision for closure of facilities is nourished partially with amounts charged to operating expenses.

GROUP IBERDROLA 2008:

The memory of the group reported that "there are provisions to deal with a number of costs required to undertake the work of dismantling their nuclear and thermal power stations, wind parks, as well as certain installations of electricity distribution in whose burying is committed".

The provisions include an account of "provision for cost of closure of facilities" with 741 million €. No other significant detail is provided in this regard, and if you go to the referenced note 4.t only know that the Group activates the costs of dismantling and fitting out of land, as provided with the existing rules. Apparently, society deals with jointly the costs of burying of facilities and the costs of dismantling.

GROUP REPSOL 2008:

Memory only indicates the part of the cost of plant and the present value of future expenditures estimated for the dismantling, removal and rehabilitation of the physical location where it sits.

Details are scarce, and the heading of provisions includes a provision for dismantling of fields for 1, 101 million €, but apparently not all this amount corresponds to "immediate obligation" provisions, but rather includes "progressive provisions" that are annually provided against results for the year.

GROUP ABENGOA 2005:

In the year 2005 we find an example of gradual provision for decommissioning, but in their report they only include these brief descriptions:

- "In addition, in response to its functionality, certain assets (security for waste deposits) are amortized based on the volume of incoming waste facilities." "Given that in addition there is an obligation to meet certain costs in connection with the closure of their plants that will give the corresponding provisions on an annual basis on the basis of the above-mentioned volume of waste."

GROUP ENAGAS 2005:

On the occasion of the transition from the PGC to IFRS, the Group ENAGAS recognized provision for dismantling providing the following explanation in memory:

GROUP COAL COTO 2005:

In 2005 this company explained that it would be affected by the restoration of exploited mine open pit, and these brief descriptions included in his memory: -the cost of property, plant and equipment includes:

GROUP CEPSA 2007:

Memory only states that the PP&E is valued at the cost price, which includes the estimated present value of costs of abandonment which group CEPSA, must face that in appropriate cases.

Also they omit details, and the heading of provisions contains the account of "other provisions", which a total balance of 128 million €, include other risks as well as provisions for abandonment of fields of crude oil production. There is no further breakdown of the activated provisions.

GROUP TOTAL 2008 (France):

More clarifying and transparent is the information provided by this company. In addition to indicate that it activates the costs of rehabilitation of oil holdings, under the heading of provisions that show specific detail for the costs of rehabilitation.

GROUP EDF 2007 (France):

It is the best example of transparency and breakdown that we have found about the costs of decommissioning and the like. In a first reading it stresses the important breakdown of information presented in the report, as well as the high amount of future commitments primarily linked to the exploitation of thermal and nuclear power stations.

In addition, displays a good example of the need to differentiate between the provisions of "progressive staffing" - linked to the level of exploitation of the Central - and provisions for "immediate obligation" - registered as higher assets since the beginning- Thus, the first are accounted for in "Provisions pour avail du cycle nuclear", while the latter are reflected in the rubric of "Provisions pour deconstruction et deniers course"

But the question is not peaceful, and thus, in the year 2007 they reported us that there was a reclassification of provisions for the costs of radioactive waste management, given that a decree of the Government of France (from 23/02/2007) forcing companies gleaned this concept of the total of the previous cost of dismantling themselves. Previously these costs (4.869 billion €, to 31/12/06) as provisions for decommissioning (deconstruction).

(1) - Provisions for the after the closure of the nuclear cycle, approximately 17.5 billion euros, (9.4% of the total asset).

Costs linked to the management of used nuclear fuel and the subsequent costs for the management of radioactive waste are itemized.

Looking into the details, the report specifies the amount provisioned but also the estimated future costs to incur. So, on the basis of the existing economic conditions to 31/12/07, the costs that EDF support as result of the closure of power stations in operation would amount to 36.257 million €.

(2) - With respect to the costs of decommissioning of nuclear and thermal plants its amount (13,654 million €, 7% of total assets), determined on the basis of studies and is updated in accordance with the evolution of the activities and recent information. This provision is counterpart to a heading of the asset. Also there has been another asset, a right for future payment on third parties committed to assume part of the cost of such dismantlement.

Also in this case it is shown with the amount provisioned, the amount of the total estimated future decommissioning costs (23.988 million €)

### **ANALYTICAL IMPLICATIONS OF THE ACCOUNTING FOR THE COSTS OF DECOMMISSIONING AND RETIREMENT**

The most important impacts of the new accounting criterion are, among others, as follows:

(1) On the side of the clearance certificate:

(a) The capitalization of the amount of the costs of dismantling constitutes an increase of the economic structure of the company. It is shown as a higher investment an amount that has not been met, which an outflow of resources is provided for in the future. This bulge of assets improves the heritage image on the side of the economic structure.

(b) The recognition in the liabilities of the provision, is a punishment to the financial structure to enter a debt that will reduce the weight of the self-financing and increase the ratio of debt.

Suppose the following data in Table 1:

Assets		PN+Liabilities	
Facilities (cost 100 + 80 provision)	180	Equity	350
Other assets	320	Provision dismantling	80
		Other payable liabilities	70
	500		500

Table 1. Assets and PN+Liabilities

The relations of indebtedness that we would get according to Plan 1990 and new Plan 2008 would be:

Required / own funds according to Plan 1990 =  $70/350 = 0.20$ .

Required / own funds according to new Plan 2008 =  $150/350 = 0.43$ .

It can be seen that if the company is financed by equity investment in plant and equipment, without going to indebtedness, by the mere registration of a provision for dismantling its debt ratio will worsen. It should be noted that the level of deterioration in the debt ratio will depend on the extent of the provision, amount that can be achieved very significant figures in sectors where environmental legislation obliges to repair or reconstruct the natural space of exploitation at the end of the same (case of mining, quarrying, wind power plants, oil rigs,...), as well as in sectors that operate with equipment and highly polluting materials whose elimination or final withdrawal will entail substantial outlays (for example): - nuclear power plants - electrical companies, petrochemical companies, etc.).

(2) Effect on profitability:

Activation of estimated decommissioning costs affect the calculation of the economic returns (ROI) and financial (ROE) of the company. Ceteris paribus, the same result should correlate with



a higher amount of investment. Accordingly the accounting ROI for the company will be aggrieved with the criterion of accounting for the costs of dismantling and similar provisions in new Plan 2008.

The impact on the results of this accounting, translates into a greater amount of allocations to amortisation, which will normally be internalized as higher cost of production made with that asset. While there would be no quantitative impact on the result (the allocation to the provision of the 1990 Plan is replaced by a greater amortization in new Plan 2008), one could speak of a qualitative impact on the results. If there were further alterations in the amount of spending finally accounted, the ROE also would be affected. It could happen that, insofar as amortisation costs normally follows a linear distribution but the financial update of the provision is growing, the new accounting method involves lighter cost early and more burdensome in recent years.

Singular importance can acquire the ROI effect for regulated companies (electric, water, highways, and in general public utilities) whose rates may come determined based on a minimum return on investment. The increase in assets experienced by the company with the implementation of the new Plan 2008 also means a greater demand for income that reward investment and may therefore lead to a rise in rates. It would not be surprising therefore that regulated companies receive positively this accounting policy if her they can move to fees, while simultaneously punished its high debt ratio.

For purposes of EBITDA, the higher cost of depreciation would have no impact

(3) Efficiency in the use of assets:

Efficiency in the use of assets will be apparently worsened as a result of higher volumes of investment and the same level of income.

(4) The financial cost:

Another significant impact comes by the side of the financial cost half of the company. To emerge total liabilities, the provision, which does not meet any financial cost, will alter the average cost of funding measures. In this manner, as a result of the updating of the provision, the mere passage of time will generate interest expenses that are not paid but reflect the continuous capitalisation of the discounted value of the provision. With this action, grow enforceable remedies, and simultaneously generates a higher financial cost, which can alter the average cost of foreign funding until then calculated.

(5) Effect on the cash flows:

The increase in assets and accounting for the provision does not imply any movement of cash flows, so it should have no impact for the purpose of the cash flows. However there may be an effect induced by the tax on profits, if deemed deductible depreciation of activated decommissioning costs and financial costs that emerge with the capitalization/des-actualization continued the aforementioned provision.

However, such an accounting approach is valuable for the determination of the future output of cash flows; information provided by the provision by dismantling facilitates the projection of future payments.

## **CONCLUSIONS**

- 1) The new model of financial information is a significant change from the Spanish accounting model in aspects of delimitation, registration and evaluation of plant and equipment. The incorporation of the future costs of dismantling alters the appraisals and the traditional historical cost concept.
- 2) Greater complexity in the implementation of the accounting evaluative criteria for new Plan 2008 fully affects the registration under this heading. The regulations are not precise enough to know accurately when it is necessary to recognise immediately the provision (damage/immediate obligations) and in supposed recognition has to be gradual (progressive damage/obligations).
- 3) The little experience, and inadequate regulation may lead to accounting information that does not cast sufficient light to correctly interpret the financial and economic consequences arising from these inescapable future commitments, obligations that can reach relevant amounts in certain sectors of activity.
- 4) The reading of the annual accounts of Spanish listed companies do not allow to know about the underlying assumptions, estimates, applied discount rates or just a light sensitivity analysis of provisions for decommissioning and the like. Information required by the Plan is omitted in the memory. The provisions of "immediate obligation" occur when combined with other "progressive provisions". It would be desirable to have a separate, similar detail for example provided in the memory of EDF.
- 5) Will have to be that are normatively clarifications issues such as: If the construction of a nuclear power station or a facility to be dismantled at the end of its useful life, requires a period of construction, for example 5 years, what date should it incorporate the "immediate provision" of decommissioning, at the beginning, as it is being built, at the end of construction or at the time of start-up operating conditions? b. If the provision is established before the entry into operation, it would activate the financial costs of providing update? c. it is accounted for, pay off, deteriorate, adjuster... asset decommissioning of separately about the underlying active object of the dismantling? What the recoverable value of an asset that must be dismantled? d. how to differentiate the "immediate supplies and progressive provisions"
- 6) In addition to the heading we have analysed, we have to target other questions offered by the new Plan 2008 heading of equally relevant PP&E here. Among other issues to address in the future we emphasize the mandatory capitalization of borrowing costs especially when advance funding is provided to the manufacturer of the plant and to receive; the boundary between the PP&E and real estate investments as well as possible/allowed/prohibited reclassifications between these headings and holdings: PP&E assets transferred on lease; the calculation of the

deterioration of the PP&E and in particular the determination of the recoverable value; the accounting separate from the different components of a same PP&E with special emphasis on the difficulty of the initial breakdown that corresponds to the first great repair costs; the PP&E with no definite useful life and its amortization/impairment (works of art, trophies, paintings, ....); among others.

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