



Asset Retirement Obligations (AROs)

Keeping current

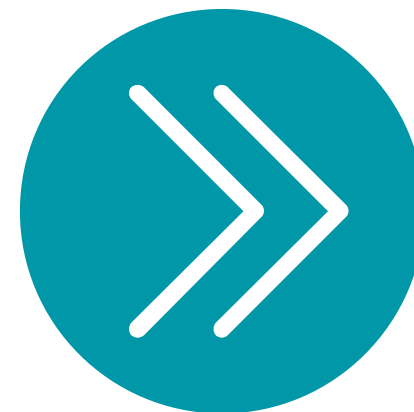
Agenda

- **Overview of the Standard Setting Process – Where are we now with ARO's?**
- **What is an Asset Retirement Obligation (ARO)?**
- **When to recognize an ARO**
- **How do you measure an ARO?**
- **What needs to be disclosed?**
- **Transition Options**
- **How would I go about implementing this standard?**
- **ARO's vs. Solid Waste Landfill and Post Closure Activities**
- **ARO's vs. Contaminated Sites**



Where are we now with AROs?

Due process



Where are we now with AROs? (cont'd)

Project status



Statement of principles

- Issued a statement of principles and comments were provided to the Public Sector Accounting Board (PSAB) in November 2014



Exposure draft

- Issued March 2017 and comments were due on June 15, 2017
- PS 3270 Solid Waste Closure and Post Closure Liability to be withdrawn



Next steps

- Final Standard expected to be approved by March 2018



Expected adoption date

- April 1, 2021
- Choice of prospective, retroactive, or modified retroactive

What is an asset retirement obligation?

An asset retirement obligation (ARO) is a **legal obligation** associated with the retirement of a tangible capital asset.

Examples of asset retirement obligations

Examples of Asset Retirement Obligations

- Decommissioning of a nuclear power plant
- Removal of asbestos from a building
- Retirement of equipment

Items that would not be asset retirement obligations

Items that would not be asset retirement obligations

- An unexpected contamination or spill
- Waste or by-products created by tangible capital assets

Infrastructure assets, such as roads and bridges, are usually never removed from service and therefore would not typically have asset retirement obligations associated with them.

Note: An asset retirement obligation can apply to an asset that is in productive use or not in productive use.

Polling question?

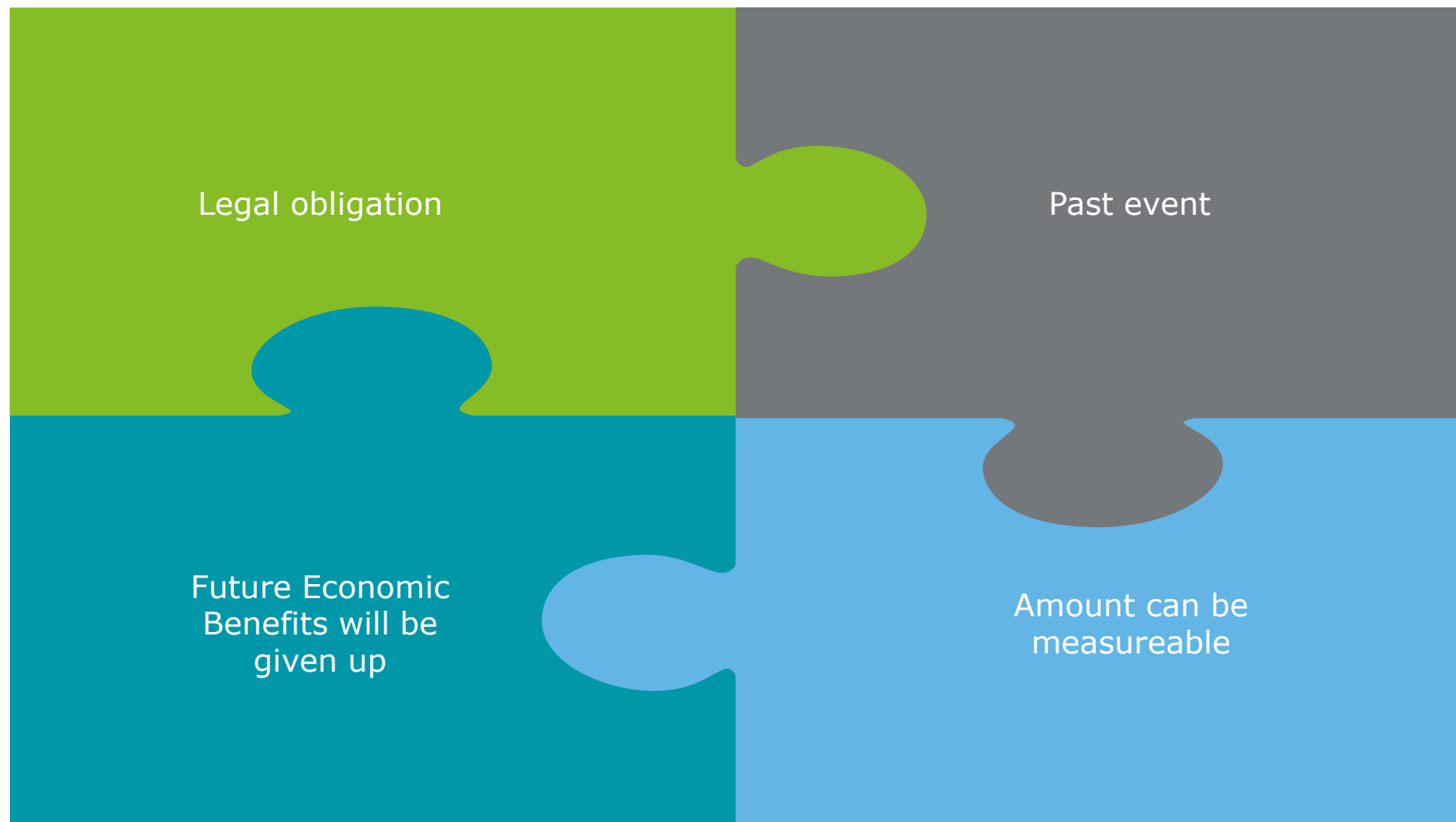
Do you think your organization will have an ARO to recognize?

- a) Yes
- b) No
- c) Finish the presentation and I will let you know



When should you recognize an ARO?

Recognition criteria



When should you recognize an ARO? (cont'd)

Recognition options

Typical ARO recognition entries

- The cost of the ARO should be recognized to expense in a rational and systematic manner

On Recognition:

- Dr. Tangible Capital Asset ARO
- Cr. ARO Liability

Throughout the remaining useful life of the asset

- Dr. ARO Amortization Expense
- Cr. Tangible Capital Asset ARO

Situations requiring additional considerations

1. ARO's associated with TCA's that are unrecognized must be expensed
2. ARO's for assets no longer in productive use must be expensed on recognition
3. ARO's for TCA's that are fully amortized would be recognized over the remaining useful life of the asset.

How do you measure an ARO?

Measurement on initial recognition

- **Management's best estimate** of the amount required to amortize a tangible capital asset
- Would include costs directly attributable to the asset retirement activities
 - Payroll and benefits
 - Equipment/facilities
 - Legal and other professional fees
 - TCA acquired with sole purpose of retiring TCA
 - Post-retirement maintenance and monitoring (integral to retirement)
- Present value technique is strongly encouraged but not necessarily required

How do you measure an ARO? (cont'd)

Subsequent measurement

Tangible capital asset

- ARO for TCA is amortized in a rational and systematic manner
- Review of obligation may change the estimate of the asset

Obligation

- Best estimate of the amount required to settle the obligation
- Review timing, amount of cash flow, and discount rate
- Passage of time accretion expense

Cash flow

- Cash flow to settle the obligation would typically occur at the end of the useful life of the asset
- Cash flow would draw down obligation that was previously set up

How do you measure an ARO? (cont'd)

Simplified ARO Example

- Assume that your organization is planning on demolishing a building that contains asbestos in 5 years
- The best estimate is that it will cost \$100 to remove the asbestos in 5 years
- An appropriate discount rate for your organization is 3%

	Obligation balance	Interest expense	Asset balance	Amortization expense	Total expense	Cash flow
Year 0	(\$86.26)		(\$86.26)			
Year 1	(\$88.85)	(\$2.59)	(\$69.01)	(\$17.25)	(\$19.84)	\$0.00
Year 2	(\$91.51)	(\$2.67)	(\$51.76)	(\$17.25)	(\$19.92)	\$0.00
Year 3	(\$94.26)	(\$2.75)	(\$34.50)	(\$17.25)	(\$20.00)	\$0.00
Year 4	(\$97.09)	(\$2.83)	(\$17.25)	(\$17.25)	(\$20.08)	\$0.00
Year 5	\$0.00	(\$2.91)	\$0.00	(\$17.25)	(\$20.16)	(\$100.00)
Total		(\$13.74)		(\$86.26)	(\$100.00)	

On recognition:

Dr. TCA ARO \$86.26
Cr. ARO \$86.26

Each year:

Dr. Accretion Expense
Dr. Amortization Expense
Cr. TCA ARO
Cr. ARO

On settlement:

Dr. ARO \$100
Cr. Cash \$100

Polling question

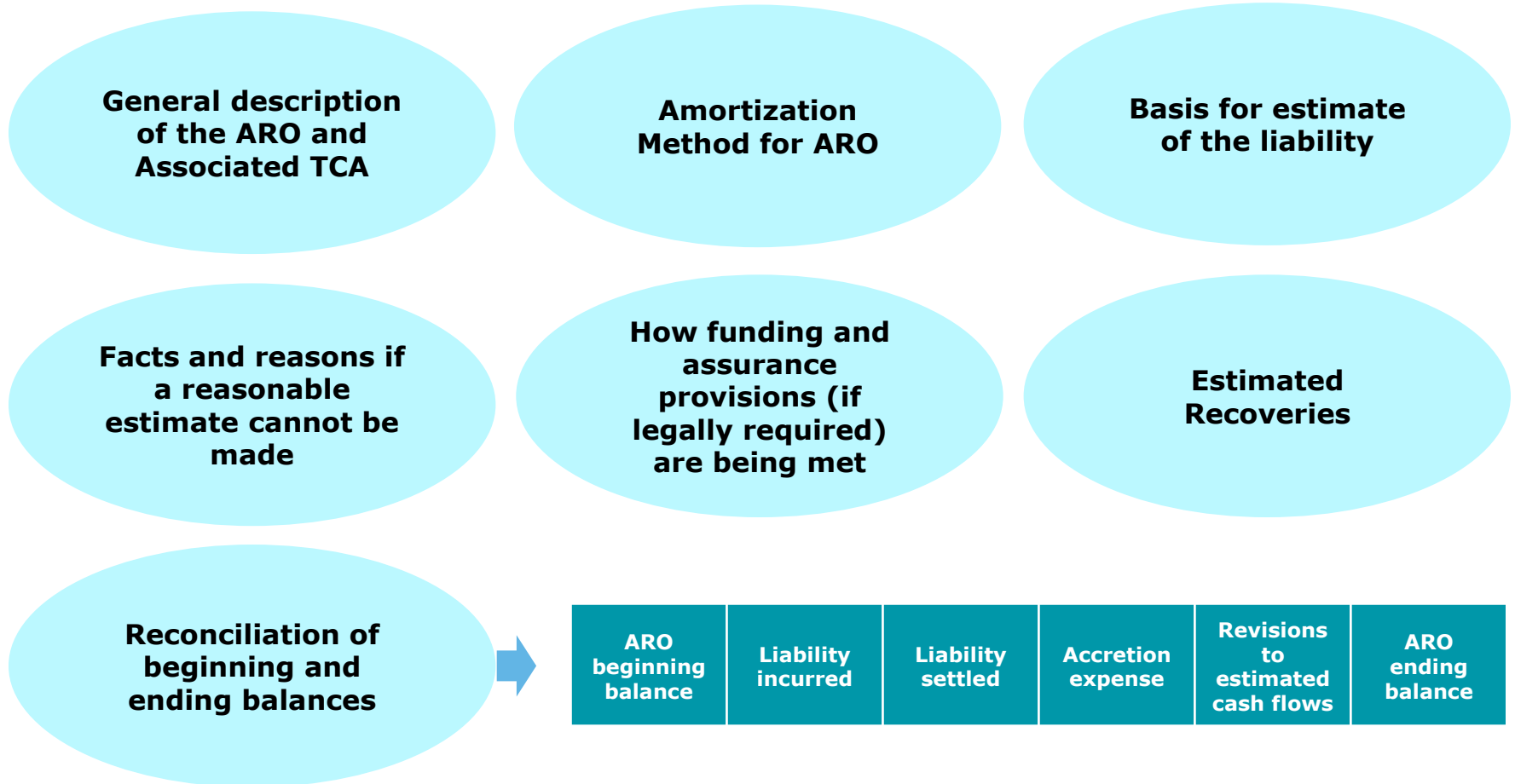
If you end up having an asset retirement obligation, will you use a present value technique to measure the liability?

- a) Yes
- b) No
- a) I will only use a present value technique if it results in a material difference and my auditor forces me to use one

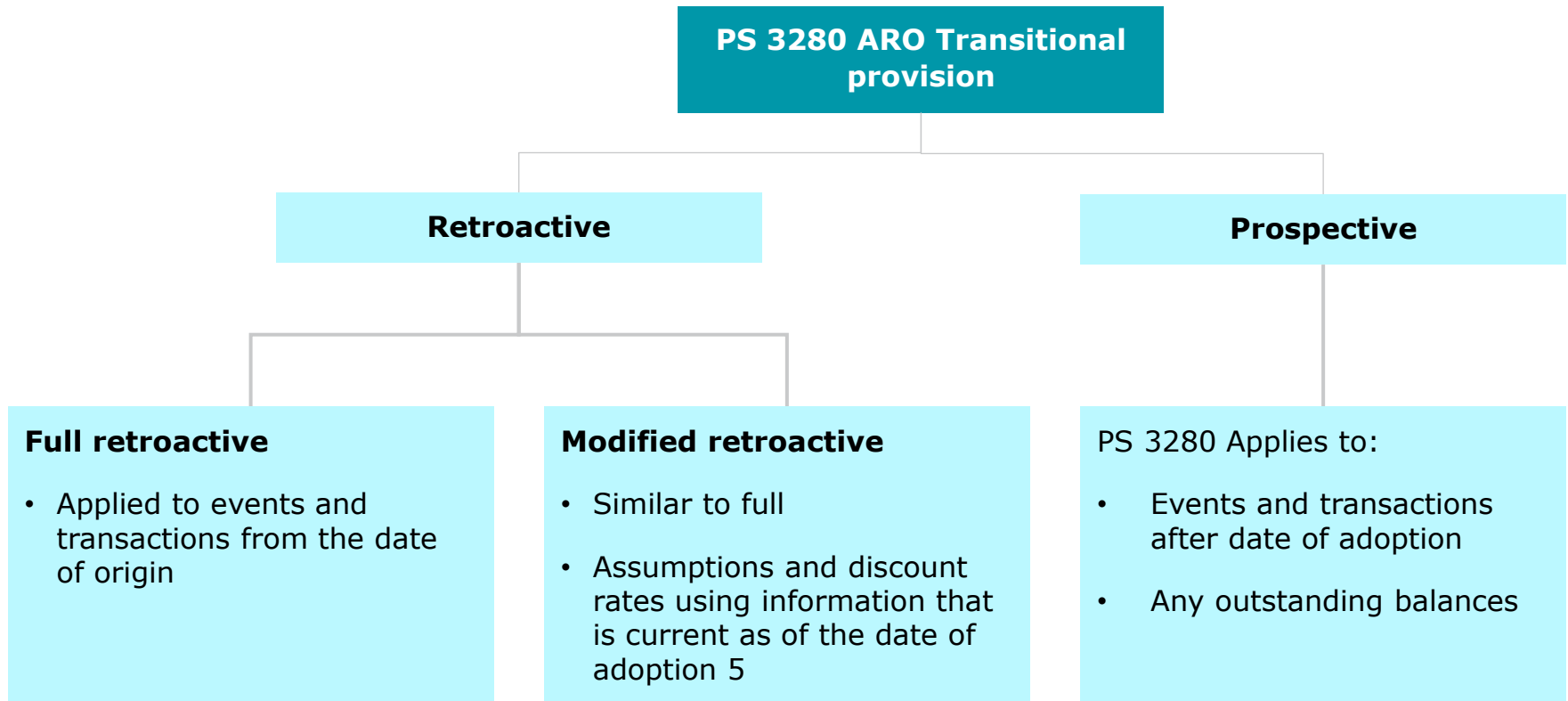


What needs to be disclosed

Disclosure requirements



Transition options



Polling question

Which transition method do you think your organization will use?

- a) Prospective
- b) Retroactive
- c) Modified Retroactive



How should I go about implementing this new standard?

	Phase 1		Phase 2		Phase 3	
	Scope	Plan	Design	Build	Implement	Review
Objective	<ul style="list-style-type: none"> Prepare a conversion plan based on a gap assessment between the current state and required future state (adoption of PS 3280) 		<ul style="list-style-type: none"> Perform comprehensive conversion 		<ul style="list-style-type: none"> Enable continued reporting 	
Accounting and reporting	<ul style="list-style-type: none"> Determine what information is needed to adopt the new standard, and determine how you are going to obtain it Consider how this information will need to be obtained in the future state 		<ul style="list-style-type: none"> Prepare for conversion by making policy and disclosure choices Design compliant internal/external reporting 		<ul style="list-style-type: none"> Prepare compliant financial statements and reporting Continually monitor developments in interpretive literature 	
Controls	<ul style="list-style-type: none"> Understand what internal controls are in place current and how they might be impacted by the adoption of the standard 		<ul style="list-style-type: none"> Design controls (Entity Level Controls, process controls and IT controls) to adopt PS 3280 		<ul style="list-style-type: none"> Develop approach for maintaining and updating control framework 	
Process and systems	<ul style="list-style-type: none"> Analyze impact to accounting, reporting, close consolidation, and reconciliation processes Evaluate the impact on financial systems and architecture 		<ul style="list-style-type: none"> Design future state accounting, reporting, close consolidation, and reconciliation processes Design future state IT systems to incorporate PS 3280 requirements 		<ul style="list-style-type: none"> Deploy future state accounting, reporting, close consolidation, and reconciliation processes Configure, convert/migrate, test, and deploy system enhancements 	
Training	<ul style="list-style-type: none"> Assess training and learning needs Conduct initial PS 3280 awareness training sessions 		<ul style="list-style-type: none"> Provide ongoing technical training (accounting) Initiate end-user training 		<ul style="list-style-type: none"> If required, provide ongoing technical training Consider training for stakeholders 	

How should I go about implementing this new standard? (cont'd)

- Have you done a lessons learned from the adoption of PS 3260 Contaminated Sites?
 - This standard will require strong interaction and communication between Finance and other parts of your organization

Start with a complete TCA Listing

Determine whether there are ARO's for TCA's not recorded

Leverage the work and logic used on the adoption of PS 3260 Contaminated Sites

Tag assets that could potentially have Asset Retirement Obligations – Investigate

Conclude on whether an ARO exists

PS 3280 vs. PS 3270

	PS 3280 ARO's	PS 3270 solid waste and post closure
Recognition of Liability	Recognized when obligation is known (up front)	Recognized as landfill is used
Recognition of Asset	Capitalization of ARO in most cases	No Asset is recognized
Expense Recognition	Accretion and amortization expense	Expense recognize as landfill is being used (volumetric basis)
Net Debt	Earlier impact on net debt due to upfront recognition	Impact on net debt over the operation life of the landfill

ARO's vs. Contaminated sites

	PS 3280 ARO's	PS 3260 contaminated sites
Trigger of Obligation	<ul style="list-style-type: none"> • Legal requirement to retire asset identified • Not necessarily related to contamination 	<ul style="list-style-type: none"> • Unexpected event • Contamination required
Type of obligation to recognized	<ul style="list-style-type: none"> • Legal obligations 	<ul style="list-style-type: none"> • All liabilities (directly responsible and assumed)
Measurement of Obligation	<ul style="list-style-type: none"> • Management's best estimate 	<ul style="list-style-type: none"> • Management's best estimate
Recognition of Asset	<ul style="list-style-type: none"> • Capitalization of ARO in most cases 	<ul style="list-style-type: none"> • N/A – Expensed
Expense Recognition	<ul style="list-style-type: none"> • Accretion and amortization expense 	<ul style="list-style-type: none"> • Upfront recognition of expense and accretion expense
Net Debt	<ul style="list-style-type: none"> • Impact on net debt is immediate 	<ul style="list-style-type: none"> • Impact on net debt is immediate

Polling question

How much effort do you think it will take for your organization to adopt this standard?

- a) Should be straight forward, not much effort
- b) We do expect there to be a significant amount of effort in adopting this standard
- c) We really have no idea and need to do an initial assessment



Q&A





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