

Straight away

IFRS bulletin from PricewaterhouseCoopers

The Extractive Activities project at the IASB opens the door to potential radical changes to financial reporting for mining and oil & gas

What is the issue?

There is little guidance on the accounting for exploration, development and production of minerals and oil & gas in current IFRS. The Extractive Activities Discussion Paper (DP), published in draft form on 10 August 2009, is the first step towards an IFRS for these activities.

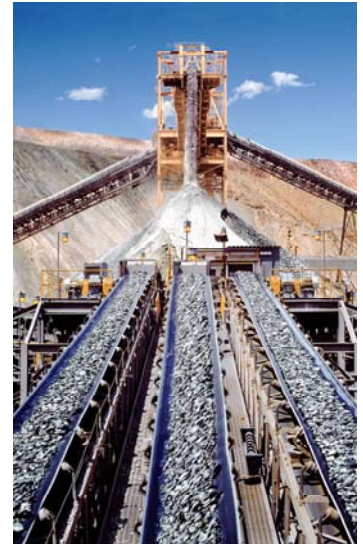
The DP considers the financial reporting issues for extractive activities and provides views on:

- the definitions of reserves and resources for financial reporting purposes
- the basis for recognising mineral and oil & gas assets
- initial and subsequent measurement of mineral and oil & gas assets
- disclosures.

The draft DP was written by four national standard setters at the request of the IASB. The work was led by the Australian Accounting Standards Board with participation from Canada, Norway and South Africa. The DP will be published formally by the IASB in Quarter 1, 2010, with an invitation to comment. Publishing a DP in draft form is an unusual step and it is not clear whether or how much the recommendations may change prior to formal publication, as it is yet to be reviewed by the IASB.

The key recommendations in the draft DP are:

1. A single financial reporting model for mining and oil & gas activities. The main business activities (i.e. exploration, evaluation, development and production) and the risks and uncertainties are very similar for both industries.
2. Reserves and resources definitions for financial reporting should be the definitions of the Committee for Mineral Reserves International Reporting Standards (CRIRSCO) and the equivalent definitions of the Society of Petroleum Engineers (SPE).
3. Mineral and oil & gas assets are recognised when a legal right to explore is acquired. Information gained from exploration and evaluation activities, as well as development activities, represent enhancement of the exploration / reserves & resources asset.
 - a. The level of detail / aggregation at which assets are recognised and presented (known as the 'unit of account') is initially the geographical area of the exploration right. This is refined over time as exploration and development plans are developed, ultimately resulting in one or more units of account, generally at the level of the individual mine or field.
 - b. The components approach used for property, plant and equipment is applicable for the components of a mineral or oil & gas asset.
4. Mineral and oil & gas assets should be measured at historical cost, supplemented by disclosure of volume and current value of reserves. The historical cost recommendation was driven by:
 - a. Views of analysts, suggesting that current values included in financial statements would be used primarily as a comparison for the analysts' own current value calculations; and



- b. Cost / benefit concerns from preparers that fair values would not provide sufficient benefits to users. The use of standardised measures to determine a current value other than fair value addresses some of these concerns, but is less likely to be relevant to a user's understanding of the entity's net future cash inflows.
5. Detailed disclosures in the financial statements of:
- a. Reserve quantities, by commodity, and by country or project (where material) including:
 - i. Proved reserves and proved and probable reserves
 - ii. Estimation methods and assumptions
 - iii. Sensitivity analysis to the main economic assumptions (e.g. price assumptions, exchange rate assumptions)
 - iv. Reconciliation of changes in reserve quantities
 - b. Either current value or fair value measurement of proved and probable reserves, by major geographical region:
 - i. Standardised measure or fair value estimate
 - ii. Preparation basis and assumptions
 - iii. Sensitivity analysis
 - iv. Reconciliation of changes in reserve values
 - c. Production revenues by commodity
 - d. Costs, disaggregated in the same way as reserve quantities, with a 5-year track record, of:
 - i. Exploration costs
 - ii. Development costs
 - iii. Production costs
6. Scoped out of the project are issues common to other industries, such as revenue recognition, inventory valuation, decommissioning obligations or joint arrangements.

The DP also considers the proposals from the Publish What You Pay (PWYP) campaign. PWYP is a global civil society coalition that campaigns for the mandatory disclosure of company payments and government revenues from the oil, gas, and mining sector. The PWYP proposals suggest similar disclosure as above, but generally in more detail and on a country-by-country basis. They also propose country-by-country disclosure of all payments to governments (e.g. income taxes, royalties). The project team's proposals involve the use of materiality to determine what disclosures should be presented. However, the project team recognises that some of the additional disclosures proposed by PWYP may be important for making informed investment and lending decisions. They suggest further study to see if additional disclosures meet the cost-benefit test, in particular country-by-country disclosure of payments to governments.

Am I affected?

The project team's draft recommendations, if carried through to an IFRS, may have a far-reaching impact. The recommendations will affect all stages of upstream mining and oil & gas; from capitalisation of exploration costs, through to detailed disclosure of proved and probable reserve volumes and values on a disaggregated basis.

What do I need to do?

The draft DP is available on the IASB website¹ now. The formal publication, with invitation to comment, is expected in Quarter 1 2010, with a 6 month comment period. That provides approximately just 12 months from now to analyse and digest the recommendations, to assess the practical consequences and respond to the IASB's recommendations. Now is the time to start to explore the impact on your business with your local PricewaterhouseCoopers extractive industries specialist.

¹ <http://www.iasb.org/NR/rdonlyres/23F1424B-05E4-4BD1-AFD8-382125765D8E/0/ExtractivesDPworkingdraft10August2009.pdf>