

In depth

A look at current financial reporting issues

Revenue from contracts with customers *The standard is final – A comprehensive look at the new revenue model*

Mining industry supplement

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At a glance

On 28 May 2014, the IASB and FASB issued their long-awaited converged standard on revenue recognition.

Entities in the mining industry regularly enter into complex contractual arrangements relating to the sale of products. The complexities around pricing and delivery are likely to be affected to some extent by the new standard, including requirements to identify separate performance obligations and determine the extent to which transaction prices are subject to the risk of significant reversal. The new requirements could affect the timing and measurement of revenue recognised. There is also a significant increase in the disclosure required.

In depth INT 2014-02 is a comprehensive analysis of the new standard. This supplement highlights some of the areas that could create the most significant challenges for mining entities as they transition to the new standard.

Overview

Revenue recognition in the mining industry might appear to be simple. Revenue is generated through the supply of commodities in exchange for consideration. Complexities can arise, however, from certain types of contractual arrangements that are common to the industry, including partnerships with other entities and arrangements for which the consideration is based on future production. Agency arrangements, transportation services, provisionally-priced commodity sales contracts and long-term take-or-pay arrangements might also be impacted by the new revenue standard. The complexities in these areas can make the decision of when to recognise revenue under the new standard and how to measure it more challenging.

This supplement focuses on how the standard will impact entities in the mining industry and highlights potential differences with current practice under IFRS and U.S. GAAP. The examples and related discussions are intended to provide areas of focus to assist entities in evaluating the implications of the new standard.

Scope

The new revenue standard applies to contracts with customers and does not exclude extractive activities from its scope. Mining entities will need to use judgement as they evaluate whether or not the parties in the transaction have a vendor-customer relationship, and therefore fall within the scope of IFRS 15 or ASC 606.

Definition of a customer

A customer is a party that contracts with an entity to obtain goods or services that are the output of that entity's ordinary activities. The scope includes transactions with collaborators or partners if the collaborator or partner obtains goods or services that are the output of the entity's ordinary activities. It excludes transactions arising from arrangements where the parties are participating in an activity together and share the risks and benefits of that activity.

Production sharing arrangements

Governments are increasingly using production sharing arrangements (PSAs) to facilitate the exploration and production of their country's mineral resources by using the expertise of a commercial mining entity. In such arrangements, it might be challenging to determine whether the government is a customer, and therefore whether the arrangement is within the scope of IFRS 15. Under a typical PSA, a mining entity will be responsible for all of the exploration costs, as well as some or all of the development and production costs associated with the mineral interest. In return, the mining entity is usually entitled to a share of the production, which will allow the recovery of specified costs plus an agreed profit margin.

PSAs, including royalty agreements, are becoming more complex and the terms might vary even within the same jurisdiction. Governments often write specific legislation or regulations for each significant new field. Each PSA should be evaluated and accounted for in accordance with the substance of the arrangement to determine whether the government meets the definition of a customer and is within the scope of the standard:

- A PSA in which the government is not a customer is outside the scope of the new standard. The mining entity would recognise the construction of its own tangible assets and would apply other relevant guidance including guidance on property plant and equipment, intangible assets and exploration. Revenue would be recognised when the mining entity delivers its share of production to its customers. The cost of the share of production delivered to the government would be an operating cost.
- A PSA in which the government is a customer is in the scope of the new standard. The proposed guidance requires the operator to recognise revenue for the delivery of services, which might include exploration or construction services, in exchange for future production. The future production would be variable non-cash consideration and would affect the measurement of revenue.

Forward-selling contracts to finance development

Mineral exploration and development is a capital intensive process. Mining entities use different financing methods including structured transactions which involve selling future production from specified properties to a third-party "investor" for cash. This cash is used to fund the development of a promising prospect. Such structures come in many different forms (for example, silver streaming) and each needs to be carefully analysed to determine the appropriate accounting.

Our publication "[In depth – Alternative financing for extractive industries](#)" examines the accounting for these types of arrangements. The new standard might mean a significant change from current accounting practice for alternative financing arrangements. The complexity of these structures means that careful analysis will be required by mining companies before reaching a conclusion on the appropriate accounting.

Product exchanges

Mining companies often exchange mineral products, such as coal, with other mining companies to achieve operational objectives. A common term used to describe this is a “Buy-sell arrangement.” The objective of these arrangements is often to save transportation costs by exchanging product A in location X for product A in location Y.

The new standard scopes out non-monetary exchanges, specifically “*non-monetary exchanges between entities in the same line of business to facilitate sales to customers other than the parties to the exchange (for example an exchange of coal to fulfil demand on a timely basis in a specified location).*” Non-monetary exchanges should be accounted for based on other guidance.

The new standard is different than the guidance under previous IFRS. Non-monetary exchanges between entities in the same line of business that are not the end customer but are rather to facilitate sales to the end customer are outside the scope of the guidance, even if the exchange is of dissimilar products. This might widen the scope of transactions accounted for outside the scope of the standard.

The new standard also requires that there be a contract with a customer before revenue is recognised. A contract only exists if there is commercial substance (that is, the entity’s future cash flows are expected to change as a result of the contract). Judgement will be required to determine whether the contract has commercial substance. If there is no commercial substance to the exchange, the transaction is outside the scope of the standard and revenue should not likely be recorded.

Interaction with other standards

Contracts that are within the scope of other guidance under IFRS or U.S. GAAP, such as leases or financial instruments, are outside the scope of the new standard. The standard provides application guidance for evaluating contracts with repurchase agreements that will assist mining entities in determining whether the arrangement is a sale to a customer, a financing arrangement or a lease. This may impact some tolling agreements with smelters or refiners.

Recent developments

The Transition Resource Group (“TRG”) was formed by the FASB and IASB to advise the boards on implementation challenges. The TRG as well as the FASB and IASB continue to discuss potential actions in response to these challenges. Both boards have recently proposed changes to the standard that will be subject to relevant due process.

This supplement is based on the final standard issued in May 2014. Preparers should monitor developments in those discussions, and consider the impact on accounting. A summary of the discussions is available at [‘In Transition’](#).

Agency relationships

Mining entities will often engage in other activities in addition to selling extracted ore, such as providing transportation of product. It is important to identify whether a mining entity is acting as a principal or an agent in transactions as it is only when the entity is acting as a principal that they will be able to recognise revenue based on the gross amount received or receivable in respect of its performance under a sales contract. Entities acting as agents do not recognise revenue for any amounts received from a customer to be paid to the principal. Revenue is recognised for the commission or fee earned for facilitating the transfer of goods and services. Whether the entity is acting as agent or principal depends on the facts of the relationship, which can require significant judgement.

New standard	Current U.S. GAAP	Current IFRS
<p>Principal versus agent considerations</p> <p>An entity is the principal in an arrangement if it obtains control of the goods or services of another party in advance of transferring control of those goods or services to the customer.</p> <p>Obtaining title momentarily before transferring a good or service to a customer does not necessarily constitute control.</p> <p>An entity is an agent if its performance obligation is to arrange for another party to provide the goods or services.</p> <p>Indicators that the entity is an agent include:</p> <ul style="list-style-type: none"> • the other party is primarily responsible for fulfilment of the contract; • the entity does not have inventory risk; • the entity does not have latitude in establishing prices; • the entity does not have customer credit risk; and • the entity's consideration is in the form of a commission. <p>An agent recognises revenue for the commission or fee earned for facilitating the transfer of goods or services. Its consideration is the 'net' amount retained after paying the principal for the goods or services that were provided to the customer.</p>	<p>The determination of whether an entity is a principal or an agent is based on the following factors:</p> <ul style="list-style-type: none"> • Is the entity the primary obligor in the arrangement? • Does the entity have general inventory risk? • Does the entity have latitude in establishing pricing? • Does the entity change the good or service? • Is the entity involved in supplier selection? • Is the entity involved in determining product specifications? • Does the entity have physical inventory risk? • Does the entity have credit risk? • Is the entity's consideration in the form of a commission? <p>The first two factors above are considered to be weighted more heavily than the other factors.</p>	<p>The indicators that an entity is acting as principal are that the entity:</p> <ul style="list-style-type: none"> • has a contractual relationship with the customer – that is, the customer believes it is doing business with the principal; • is able to set the terms of the transactions, such as selling price and payment terms; • bears the risk associated with inventory; and • bears the credit risk. <p>An indicator that an entity is an agent is if the entity earns a pre-determined fee.</p>

Potential impact – both IFRS and U.S. GAAP

The indicators under the new standard are similar to the existing guidance but are provided in a new context. The indicators are designed to help entities determine if they obtain control of the goods or services before transferring control of those goods or services to the customer. The number and significance of judgements to determine whether the company is acting as a principal or agent appear to be increasing within the industry, particularly in relation to companies that provide value-added services to companies that mine ore or unprocessed mineral product. In addition, as compared to previous U.S. GAAP, the standard has fewer indicators and no longer weights some factors more than others.

Delivery – Cost, insurance and freight versus free on board

An entity will recognise revenue when (or as) a good or service is transferred to the customer and the customer obtains control of that good or service. Control of an asset refers to an entity's ability to direct the use of and obtain substantially all of the remaining benefits (that is, the potential cash inflows or savings in outflows) from the asset.

Resources are often extracted from remote locations and require transportation over great distances. Transportation by truck instead of railway can be a significant cost. There are two main variants of contracts that address future shipping costs – cost, insurance and freight (CIF) or free on board (FOB).

CIF contracts mean that the selling entity will have the responsibility to pay the costs, insurance and freight until the goods reach a final destination, such as a refinery or an end user. FOB contracts mean that the selling entity delivers the goods when the goods are delivered to an independent carrier. The buyer has to bear all costs and risk of loss to the goods from that point.

In both approaches, contractual terms mean that risk and title and therefore control of the commodity normally pass at the ship's rail, although the timing of revenue recognition could change under the new standard, depending on the terms of trade. The difference between the shipping terms affects which party is responsible for freight costs.

Cost, insurance and freight (CIF)

New standard	Current U.S. GAAP	Current IFRS
<p>Identifying separate performance obligations</p> <p>The new standard will require an entity to account for each distinct good or service as a separate performance obligation. Freight services may meet the definition of a distinct service.</p> <p>Satisfaction of performance obligations</p> <p>An entity recognises revenue when it satisfies a performance obligation by transferring a promised good or service to a customer. A good or service is transferred when the customer obtains control of that good or service. The new standard lists indicators of control transferring, including an unconditional obligation to pay, legal title, physical possession, transfer of risk and rewards and customer acceptance.</p> <p><i>Sales of goods:</i> Revenue is recognised at the point when control transfers to the customer. This will generally follow the terms of the contract and is usually when the goods pass the rail</p>	<p>Existing guidance focuses on whether delivery has occurred as a key determination of when revenue should be recognised.</p> <p>In CIF contracts, delivery occurs when the goods have passed the ship's rail, assuming the seller has transferred the significant risks and rewards of ownership, even if the seller is still responsible for paying the cost of transportation and insurance for goods while in-transit. However, a full understanding of the terms of trade is required to ensure that this is the case.</p>	<p>IAS 18 focuses on whether the entity has transferred to the buyer the significant risks and rewards of ownership of the goods as a key determination of when revenue should be recognised.</p> <p>Industry practice has been for the transfer of significant risks and rewards of ownership to occur when the goods have passed the ship's rail, even if the seller is still responsible for insuring the goods in-transit on the buyer's behalf. A full understanding of the terms of trade is required to ensure that this is the case.</p>

on a vessel selected by the buyer, at which point the buyer will control the goods.

Transportation: A performance obligation for transportation generally meets the criteria for a performance obligation that is settled over a period of time, and revenue will be recognised over the period of transfer to the customer. If it does not meet the criteria, the performance obligation would be settled at a point in time, and revenue would likely be recognised when the customer receives the goods.

Potential impact – both IFRS and U.S. GAAP

The new standard is generally not expected to change the point at which revenue is recognised for the performance obligation to provide goods. However, an entity should evaluate whether it has separate performance obligations for the goods and the freight services. This could mean recognition of a portion of the revenue when control of the goods passes and recognition over time for the portion of revenue relating to the freight services.

Factors which might indicate there is a separate performance obligation for transportation include:

- Specialism of any vehicles or technology involved with providing the transportation;
- Level of cost, distance or time associated with providing the transportation; and
- Whether the terms of the contract allow the customer to opt out of the transportation element and collect the commodity themselves.

There cannot be a separate performance obligation for an entity to transport its own goods (that is, prior to transfer of control of the goods to the customer).

Recent developments

The accounting for shipping and handling services is under discussion by the FASB and IASB. The FASB recently proposed a 'practical expedient' that provides U.S. GAAP preparers with an option to account for shipping and handling as a fulfilment cost, rather than as a promised good or service, when shipping and handling occurs after control has transferred to the customer. The IASB has not proposed a similar expedient but will perform further outreach with IFRS stakeholders to identify whether this is an issue. Preparers should monitor developments in those discussions, and consider the impact on accounting.

Example – Timing of revenue recognition in a CIF arrangement

Facts: The entity's revenue contracts are on a CIF basis. Copper concentrate is transported by rail from an offshore operation to the port where it is loaded on ship to be sent to a refinery in Asia. The refiner is the customer. The entity receives a provisional payment of 90% of the invoice raised 10 days after the concentrate has been unloaded from the ship into the destination port. The contracts contain a clause that states that the title of the copper concentrate passes on unloading the goods at the purchaser's facility.

Discussion: The revenue contract is on CIF terms; the seller therefore has to pay the costs, freight and insurance associated with shipping. There is also a specific clause that states that risk and title, and therefore control of the concentrate, only passes on unloading at the destination port. Revenue would be recognised at the date of unloading. This illustrates the importance of understanding the terms of trade in the contract, as this is what will determine the accounting. Shipping is not a separate performance obligation when an entity controls the goods until they are unloaded.

Free on board (FOB)

New standard	Current U.S. GAAP	Current IFRS
<p>Satisfaction of performance obligations</p> <p>An entity recognises revenue when it satisfies a performance obligation by transferring a promised good or service to a customer. A good or service is transferred when the customer obtains control of that good or service.</p> <p>The new standard lists indicators of control transferring, including an unconditional obligation to pay, legal title, physical possession, transfer of risk and rewards and customer acceptance.</p>	<p>Existing guidance focuses on whether delivery has occurred as a key determination of when revenue should be recognised.</p> <p>FOB contracts often stipulate that the purchaser will assume the risk of loss upon delivery of the product to an independent carrier and it is the purchaser's responsibility to pay for any freight or insurance costs beyond that point. The point at which the goods have passed the ship's rails is usually considered to be the point at which delivery has occurred. This is because the seller has no further obligations at that point.</p>	<p>IAS 18 focuses on when the entity has transferred to the buyer the significant risks and rewards of ownership of the goods.</p> <p>FOB contracts often stipulate that the purchaser will assume the risk of loss upon delivery of the product to an independent carrier and it is the purchaser's responsibility to pay for any freight or insurance costs beyond that point. The point at which the goods have passed the ship's rail is usually the point at which the transfer of significant risks and rewards of ownership is considered to have occurred. This is because the seller has no further obligations at that point.</p>

Potential impact – both IFRS and U.S. GAAP

The new standard is generally not expected to change the point at which revenue is recognised for the performance obligation to provide goods. However, an entity should evaluate whether they have a separate performance obligation for the freight services. This could mean recognition of a portion of the revenue when control of the goods passes and recognition over time for the portion of revenue relating to freight services.

Example – Timing of revenue recognition in a FOB arrangement

Facts: The entity's revenue contracts are on FOB basis. Copper concentrate is transported by rail from an offshore operation to the port, where it is loaded on a ship to be sent to a refinery in Asia. The refiner is the customer. The entity receives a provisional payment of 90% of the invoice raised 10 days after the concentrate has been unloaded from the ship into the destination port. The customer's obligation to pay arises when the goods pass the rail.

Discussion: The revenue contract is on FOB terms; the control of the goods transfer at the moment that the product passes the ship's rail, demonstrated by title, physical possession and an obligation to pay, passing to the buyer. As a result, revenue would be recognised upon delivery to the carrier.

Provisional pricing arrangements

Sales contracts for commodities often incorporate provisional pricing. Provisional pricing might arise for a variety of reasons:

- The time taken to transport the product might mean that the customer wishes to pay the market price at the date of eventual delivery at the final destination – in those situations, a provisional price is charged on the date control of the product initially transfers. The final price is generally an average market price for a particular future period or a final assayed amount.
- The product is being transported in concentrate form and the final quality and volume of component commodities will not be known until further processing at its final destination.

New standard	Current U.S. GAAP	Current IFRS
<p>Satisfaction of performance obligations</p> <p>The sales contract would be in the scope of the new standard. There will be a single performance obligation, being the delivery of the promised product. Revenue will be recognised when the performance obligation is satisfied, which is when the customer obtains control of the product.</p> <p>Determining the transaction price</p> <p>The entity will need to determine the transaction price, which is the amount of consideration it expects to be entitled to in the transaction.</p> <p>Management should first consider whether provisionally priced contracts include embedded derivatives that are in the scope of financial instrument guidance. A mining entity will apply the separation and/or measurement guidance in other standards first, and then apply the guidance in the revenue standard to the remaining portion of the contract.</p> <p>The transaction price might be variable or contingent on the outcome of future events, which would include provisional pricing arrangements.</p> <p>Variable consideration is subject to a constraint. The objective of the constraint is that an entity should recognise revenue as performance obligations are satisfied to the extent</p>	<p>Revenue from the sale of provisionally priced commodities is recognised when title passes to the customer, the price is determinable, and collectability is reasonably assured, which is generally the date of delivery.</p> <p>Revenue is measured based on the forward market price of the commodity or estimates of the content of concentrate at the date title passes.</p> <p>Price adjustment features in non-cancellable contracts that are based on quoted market prices for a date subsequent to the date of shipment or delivery are generally considered to be embedded derivatives that require separation from the host contract. This is because the forward price at which the contract is to be ultimately settled is not closely related to the spot price. In such instances, the host contract is the non-financial contract for the sale of the mineral concentrate at a future date, while the embedded derivative is the exposure to the price movements from the date of sale to the end of the quotational period.</p> <p>Where the initial revenue recognition is based on estimates of the content of concentrate, an adjustment is made when the product is delivered and processed and the final content is known. This adjustment is recognised in revenue.</p>	<p>Similar to U.S. GAAP.</p> <p>Revenue from the sale of provisionally priced commodities is recognised when the risks and rewards of ownership are transferred to the customer, which is generally the date of delivery.</p> <p>Revenue is measured based on the forward market price of the commodity or estimates of the content of concentrate at the date title passes.</p> <p>Where a future market price is to be used to settle a contract, at each subsequent period end the provisionally priced contracts are marked to market using the most up-to-date market prices with any resulting adjustments usually being recognised within revenue.</p> <p>Where the initial revenue recognition is based on estimates of the content of concentrate, an adjustment is made when the product is delivered and processed and the final content is known. Many entities recognise this adjustment in revenue.</p>

that a significant revenue reversal is not “probable” (U.S. GAAP) or “highly probable” (IFRS), in future periods. Such a reversal would occur if there is a significant downward adjustment of the cumulative amount of revenue recognised for that performance obligation.

Judgment will be required to determine if the amount to be recognised is subject to a significant reversal. The new standard has a list of factors that could increase the likelihood or magnitude of a revenue reversal.

Management’s estimate of the transaction price will be reassessed each reporting period.

Potential impact – both IFRS and U.S. GAAP

Judgment will be required to determine if the provisional pricing results in the identification of an embedded derivative or variable consideration. If the entity determines that the provisional pricing results in variable consideration, further judgement will be required to determine whether the estimated transaction price is subject to significant reversal. This might be particularly relevant where the final quantity and quality of product being delivered will not be known until processing at its destination. Where price is conditional upon the component elements of the product, this is more likely to be variable consideration.

Judgement will also be required to identify the point at which the variable consideration becomes unconditional, and is then considered a financial asset within the scope of IFRS 9/IAS 39 and ASC 310.

Where provisional pricing features represent embedded derivatives, mining entities would be required to continue to separate them and recognise and measure them in accordance with financial instrument guidance. However, given the revised presentation requirements in the new standard, it may no longer be appropriate to present movements in the embedded derivative in revenue from contracts with customers.

Example – Provisional pricing

Facts: An entity enters into a contract to sell 1,000 tons of copper concentrate to a customer on 1 December 20X4. The final price will be based on the London Metal Exchange (“LME”) copper price three months from the date of delivery.

Delivery takes place on 31 December 20X4 and control of the copper concentrate is transferred to the customer on that date. Final invoicing will take place on 31 March 20X5. The entity has a 31 December year-end.

The three-month forward copper price on 31 December is CU6,500 per ton. On 31 March 20X5 the copper price amounts to CU6,750 per ton.

Discussion: At contract inception (1 December 20X4), the entity will need to determine whether the provisional pricing mechanism represents an embedded derivative that needs to be separated from the host sales contract. Revenue will be recognised on 31 December 20X4, the date when control of the copper is transferred to the customer and the performance obligation is satisfied. Judgement will be required to identify the point at which the consideration becomes unconditional, and is then a financial asset within the scope of IFRS 9/IAS 39.

If the entity concludes that the provisional pricing is variable consideration and not a financial asset within the scope of IFRS 9/IAS 39, the entity would need to apply judgement in:

- estimating the variable sales price at 31 December 20X4; and
- determining whether the estimate meets the “probable” (U.S. GAAP)/“highly probable” (IFRS) test regarding the likelihood of significant reversal.

It should be probable/highly probable that the revenue would not be subject to a significant revenue reversal between 31 December 20X4 and 31 March 20X5. To the extent the entity were to report results on 31 January 20X5, before the final invoicing on 31 March 20X5, the estimate of the transaction price and revenue constraint would need to be reassessed.

Take-or-pay and similar long-term supply agreements

Long-term sales contracts are common in the mining industry. Producers and buyers may enter into sales contracts that are often a year or longer in duration to secure supply and reasonable pricing arrangements. Such contracts are often fundamental to supporting the business case or to finance, develop or continue activity at a particular mine.

Contracts will typically stipulate the sale of a set volume of product over the period at an agreed price. There are often clauses within the contract relating to price adjustment or escalation over the course of the contract to protect the producer and/or the seller from significant changes to the underlying assumptions in place at the time the contract was signed. Long-term commodity contracts frequently offer the counterparty flexibility and options in relation to the quantity of the commodity to be delivered under the contract.

Mining entities should continue to first assess whether these arrangements represents financial instruments or contain embedded derivatives that should be accounted for under the financial instruments standards (e.g., whether a contract with volume flexibility contains a written option that can be settled net in cash or another financial instrument). In addition, mining entities should continue to evaluate whether such arrangements convey the right to use a specific asset, and therefore constitute a lease under the leasing standards.

New standard	Current U.S. GAAP	Current IFRS
<p>Identifying the contract</p> <p>In relation to take-or-pay contracts, only the minimum amount specified would generally be considered a contract, as this is the only enforceable part of the agreement. Options in the contract to acquire additional volumes will likely be considered a separate contract at the time the customer exercises the option, unless such options provide the customer with a material right (e.g., an incremental discount). Where there is a material right, the option should be accounted for as a separate performance obligation in the original contract.</p> <p>It is likely that each unit of product will be considered a separate performance obligation (e.g., tonne of coal). This will require the total transaction price to be allocated to the separate performance obligations using standalone selling prices.</p> <p>Breakage</p> <p>Customers may not exercise all of their contractual rights to receive a good or service in the future. Unexercised rights are often referred to as breakage.</p>	<p>In the case of a supply contract with “take-or-pay” terms, revenue to be recognised on undelivered quantities is considered contingent, even though payment is due to the seller if the customer does not request all of the undelivered units. The underlying rationale is that, if the seller is not able to satisfy the buyer’s request for the products, the buyer is not obligated to pay the consideration.</p> <p>Even if the delivery of the quantities is probable and within the seller’s control, the risk that the products might not be delivered makes the consideration contingent upon delivery/performance.</p>	<p>Similar to U.S. GAAP.</p> <p>Revenue is recognised when the volumes of the product concerned, e.g., coal, are delivered and they are typically measured at market price or fixed price (as specified in the contract).</p> <p>Revenue related to volumes not taken, but paid for, is generally recognised at the end of the stated take-or-pay period if the customer is not able to make-up volumes in future take-or-pay periods. If the customer is entitled to make-up volumes in future take-or-pay periods, revenue is recognised either when the payment is applied to future volumes, or the right to make-up volumes expires.</p>

An entity should recognise estimated breakage as revenue in proportion to the pattern of exercised rights. Management might not be able to conclude whether there will be any breakage, or the extent of such breakage. In this case, they should consider the constraint on variable consideration, including the need to record any minimum amounts of breakage. Breakage that is not expected to occur should be recognised as revenue when the likelihood of the customer exercising its remaining rights becomes remote. The assessment should be updated at each reporting period.

In take-or-pay arrangements, this may mean that an entity may be able to recognise revenue in relation to breakage amounts in a period earlier than when the breakage occurs, provided that it can demonstrate it expects that the customer will not exercise these rights. Given the nature of these arrangements and the inherent uncertainty in being able to predict a customer's behaviour, it may be difficult to satisfy this requirement.

Potential impact – both IFRS and U.S. GAAP

The new standard will require mining entities to apply judgement in identifying the performance obligations, as well as the reasons for an price changes over the term of the arrangement. These judgements will determine whether the total transaction price is allocated and recognised based on stand-alone selling prices (e.g., using forward curves), contractual pricing, straight line or another basis. Mining entities will also have to consider whether such arrangements include a significant financing component that will have to be accounted for separately (see [In depth INT2014-02](#) for more details).

Disclosures

The revenue standard includes a number of extensive disclosure requirements intended to enable users of financial statements to understand the amount, timing, and judgements related to revenue recognition and corresponding cash flows arising from contracts with customers. We highlight below some of the more significant disclosure requirements, but the list is not all-inclusive.

The disclosures include qualitative and quantitative information about:

- contracts with customers;
- the significant judgements, and changes in judgements, made in applying the guidance to those contracts; and
- assets recognised from the costs to obtain or fulfil contracts with customers.

The disclosure requirements are more detailed than currently required under IFRS or U.S. GAAP and focus significantly on the judgements made by management. For example, they include specific disclosures of the estimates used and judgements made in determining the amount and timing of revenue recognition.

The new standard also requires an entity to disclose the amount of its remaining performance obligations and the expected timing of the satisfaction of those performance obligations for contracts with durations of greater than one year, and both quantitative and qualitative explanations of when amounts will be recognised as revenue. This requirement could have a significant impact on the mining industry, where long-term contracts are a significant portion of an entity's business.

Final thoughts

The above discussion does not address all aspects of the new standard. Companies should continue to evaluate how the new standard might change current business activities, including contract negotiations, key metrics (including debt covenants, surety, and prequalification capacity calculations), taxes, budgeting, controls and processes, information technology requirements, and accounting.

Entities are encouraged to monitor the discussions of the TRG. The TRG was established in 2014 to help the FASB and the IASB determine whether more implementation guidance is needed. The TRG will make no formal recommendations to the boards' or issue any guidance. Any views discussed by the TRG will be non-authoritative.

Entities will be required to apply the new revenue standard in the first interim period within annual reporting periods beginning on or after 15 December 2016 (U.S. GAAP) and 1 January 2017 (IFRS). Earlier adoption is permitted under IFRS, but not under U.S. GAAP. For non-public entities (U.S. GAAP only), the standard is effective for annual reporting periods beginning after 15 December 2017 and for interim reporting periods within annual reporting periods beginning after 15 December 2018. Earlier application is permitted for non-public entities; however, no earlier than 15 December 2016.

The IASB and FASB have proposed a deferral of the effective date of the new standard by one year until 1 January 2018. The IFRS proposal will retain the option for entities to early adopt the standard, while the FASB proposal will permit entities to adopt the new standard as of the original effective date. The IASB and FASB decisions are not final and the proposals are subject to each of the board's due process requirements, which include a period for public comment.

Entities can adopt the final standard retrospectively or use a simplified approach. Entities using the simplified approach will: (a) apply the revenue standard to all existing contracts as of the effective date and to contracts entered into subsequently; (b) recognise the cumulative effect of applying the new standard in the opening balance of retained earnings on the effective date; and (c) disclose, for existing and new contracts accounted for under the new revenue standard, the impact of adopting the standard on all affected financial statement line items in the period the standard is adopted. An entity that uses this approach must disclose this fact in its financial statements.

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Questions?

PwC clients who have questions about this *In depth* should contact their engagement partner.

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