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## **Extractive Activities Cover Note**

### **Objective**

- 1 The objective of this session is to:
  - (a) provide an update on the Extractive Activities research project; and
  - (b) seek EFRAG TEG-CFSS members' input about the scope and direction of the project in preparation for the IASB's discussion in Q2 2021.

### **Background**

- 2 The IASB is in the process of considering evidence to help it decide whether to start a project to develop proposals to replace or amend IFRS 6 *Exploration for and Evaluation of Mineral Resources*.
  - (a) IFRS 6 is addressing the accounting for exploration and evaluation expenditure (E&E) and does not specify an accounting policy for such expenditure but requires entities to do so.
  - (b) IFRS 6 provides entities with a temporary exemption from parts of the hierarchy in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* in developing an accounting policy for exploration and evaluation expenditure.
- 3 *In March 2018* the IASB commenced its research project on Extractive Activities by asking the national standard-setters, whose staff contributed to the 2010 Discussion Paper *Extractive Activities* (the DP), being Australia, Canada, Norway and South Africa, to inform the IASB of any significant developments in extractive activities since the publication of the Discussion Paper. The 2010 DP had the following key themes from feedback:
  - (a) Support for a project, mixed views on scope of project.
  - (b) Support for 'reserve' and 'resource' definitions, concerns on how to incorporate into a Standard.
  - (c) Support for initial asset recognition, disagreement that subsequent activities always result in an asset.
  - (d) Support for historic cost measurement, request for more guidance on depreciation and unit of account.
  - (e) Disagreement about need for an exception to the impairment model.
  - (f) Mixed views on what additional disclosure is required.
- 4 *In September 2019*, the IASB also considered relevant feedback from the Discussion Paper as part of that evidence and considered the potential effect on the analysis and proposals in the Discussion Paper of new Standards, amendments

## *Extractive Activities – Cover Note*

and other Board documents issued by the Board, and other relevant changes, since the Discussion Paper was published.

- 5 *In June 2020*, the IASB considered a summary of feedback from additional outreach activities with national standard-setters and other stakeholders from jurisdictions which also have significant extractive industries in order to determine:
  - (a) what problems, if any, entities with extractive activities have applying IFRS Standards; and
  - (b) whether the primary users of financial statements of entities with extractive activities are obtaining all the information they need for these entities.
- 6 The key themes from that feedback were:
  - (a) There continues to be mixed views about the potential scope of this project, with some supporting that the project be expanded to all extractive activities.
  - (b) There are a range of application challenges related to IFRS 6 and other IFRS Standards, but not all respondents expect standard-setting as a response to these challenges.
  - (c) There is diversity between jurisdictional requirements related to reserve and resource classification systems, but there are mixed views whether IFRS Standards should require the disclosure of reserve and resource information.
  - (d) Voluntary disclosures, which go beyond the requirements of IFRS Standards, are common.
- 7 *In July 2020*, the IASB considered:
  - (a) How activities within the scope of IFRS 6 would be accounted for in the absence of that Standard, applying the requirements in IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*. Research findings indicate that, in the absence of IFRS 6, applying the requirements in IAS 16 and IAS 38, a majority of E&E expenditure would likely be expensed.
  - (b) Academic evidence on extractive activities and topics relevant to IFRS 6. Key takeaways from that evidence were:
    - (i) Accounting policies developed applying requirements of IFRS 6 are diverse.
    - (ii) E&E assets of oil and gas entities are value relevant, however the evidence on the value relevance of E&E assets of minerals entities is mixed.
    - (iii) Disclosures of information about reserves and resources is diverse and improving disclosures is associated with stronger market reaction to reserve announcements.
    - (iv) Analysts develop more private information and produce more accurate forecasts for extractives entities with more E&E expenditure.
    - (v) Some researchers believe the extractive industries influenced the IFRS 6 standard-setting process.
- 8 *In September 2020*, the IASB considered the diversity of reserve and resource classification systems and of the regulatory requirements for the disclosure of reserve and resource information.
- 9 *In October 2020*, the IASB considered whether there are jurisdictional accounting requirements for exploration and evaluation (E&E) expenditure that differ from the requirements in IFRS 6 and the diversity of accounting policies developed applying the requirements of IFRS 6. Key findings indicate:

## *Extractive Activities – Cover Note*

- (a) Accounting policies developed applying IFRS 6 are diverse and the source of this diversity is generally due to (i) the extent (how much and when) to which the entity recognises E&E expenditure as an asset; and (ii) the unit of account an entity decides to apply.
  - (b) Some jurisdictions require entities to apply a specific accounting policy.
  - (c) Industry trends are present (e.g. successful efforts and full-cost methods primarily adopted in the oil and gas industry; accounting policies which expense most E&E expenditure are more likely to be adopted by minerals entities, although capitalisation policies are more common).
- 10 *In February 2021*, the IASB held an educational session which explained further extractive activities in the minerals and oil and gas industries and some of the financial reporting challenges that arise in those industries.

### **Summary of feedback to IASB staff so far**

- 11 The IASB consulted various stakeholders (users, preparers, national standard-setters and special interest) so far. Key themes from users this far included the following:

#### *Non-IFRS information / disclosure outside the financial statements*

- (a) Lack of consistency and comparability of non-IFRS information disclosed outside the financial statements.
- (b) Focus is on non-GAAP performance measures, cash measures, reserves and resources.
- (c) Non-IFRS information (especially cash and cost measures) is generally required to complement and enhance users understanding of the financial statements and this information is not always publicly available.
- (d) Reserve and resource information is generally more useful to users than information on exploration and evaluation expenditure, however many still view exploration and evaluation expenditure as important.

#### *IFRS information - financial statement disclosure*

- (e) Effects of climate-change and environmental issues and obligations are not clear.
- (f) More information on management's judgements and assumptions for all activities.
- (g) Lack of consistency and comparability in accounting for E&E expenditure in the financial statements is a concern but majority would prefer improved disclosures about E&E expenditure rather than a prescribed accounting policy.
- (h) E&E expenditure information is more important for smaller companies.
- (i) Accounting policy disclosure is often not clear enough to understand how an entity accounts for its material E&E expenditure.
- (j) Information about rehabilitation / restoration obligations.

- 12 Key themes of feedback from preparers and auditors

#### *IFRS 6 application challenges*

- (a) Developing an appropriate accounting policy;
- (b) Identifying an appropriate unit of account;
- (c) Lack of defined terms (technical feasibility and commercial viability);
- (d) Impairment assessment of E&E assets; and

## Extractive Activities – Cover Note

- (e) Concerns about changes to IFRS 6 as it is currently aligned with US GAAP.

### *Other IFRS application challenges*

- (f) Accounting of complex arrangements during the exploration and evaluation phase (farm out arrangements, etc.);
  - (g) Application of IFRS Standards to assets simultaneously in development and production stage;
  - (h) Application of particular requirements in IFRS Standards issued or published after 2010 (IFRS 11 *Joint Arrangements*, IFRS 15 *Revenue from Contracts with Customers*, etc.); and
  - (i) Lack of guidance on applying existing IFRS Standards to particular aspects of extractive activities (IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* on rehabilitation obligations, IAS 16 depreciation etc.)
- 13 EFRAG activities In March 2020, the EFRAG Secretariat reached out to EFRAG TEG-CFSS members to request input on evidence about:
- (a) What problems, if any, there are with applying IFRS 6 by entities with extractive activities; and
  - (b) Whether the primary users of financial statements of entities with extractive activities are obtaining all the information they need for these entities.
- 14 The jurisdictions that responded indicated that no significant mining entities in their jurisdictions are reporting under IFRS Standards.

### **Project direction**

- 15 The IASB Staff have heard mixed views about the scope of the project and stakeholders suggested the following (with an assessment of the size of the project):
- (a) *Do nothing* – IFRS 6 is working and no amendments are needed. **(None)**
  - (b) *Improve disclosures (Amend IFRS 6)* - Amend IFRS 6 to improve disclosures about E&E expenditure (especially accounting policy disclosures). Disclosures should be extended to include information about reserves and resources. **(Small large if extended to reserves)**
  - (c) *Improve consistency and comparability (Amend IFRS 6)* – Amend IFRS 6 to limit accounting policy choices and provide guidance on other areas of E&E expenditure. For example, guidance on impairment on E&E assets and other IFRS 6 topics. **(Medium)**
  - (d) *Scope to IAS 38 (replace IFRS 6)* – Consider E&E assets as part of a larger project which would revisit the accounting for intangible assets and the eventual withdrawal of IFRS 6. **(Large)**
  - (e) *Develop a standard for all extractive activities (replace IFRS 6)* – develop accounting requirements for all types of extractive activities and not only E&E expenditure and the eventual withdrawal of IFRS 6. **(Large)**
- 16 However, the IASB Staff suggested that the scope could have different objectives from those identified above and therefore the final project scope might not coincide with those in paragraph 15. They suggested that the scope should address all the following identified from the feedback received:
- (a) Activities in the scope of IFRS 6 (reducing diversity and provide better information on of E&E expenditure, improve the accounting and application of other topics covered by IFRS 6 and those that are not);
  - (b) Reserve and resource information (to provide better quality information of reserves and resources in the financial statements);

## *Extractive Activities – Cover Note*

- (c) Activities outside the scope of IFRS 6 (to develop a standalone standard for all extractive activities and improve the application of other IFRSs for extractive activities); and
- (d) Other activities which include the accounting for E&E expenditure and other similar expenditure consistently.

### **Key feedback relevant to IASBS Staff scope suggestions**

#### *Activities in IFRS 6 scope (only)*

- 17 Accounting policy
  - (a) Significant diversity in the accounting policies developed by entities.
  - (b) Some oil and gas preparers consider IFRS 6 helpful, allowing the industry to adopt similar accounting policies (e.g. successful efforts).
  - (c) Accounting policy disclosures are often not clear enough for users to understand how an entity accounts for its material E&E expenditure.
- 18 Mixed views were received from users, but most agree
  - (a) The diversity of accounting policies is not a significant issue.
  - (b) E&E expenditure information is important.
  - (c) Improving the quality of information being disclosed about accounting policies for E&E expenditure, and about E&E expenditure in general, would be most helpful.

#### *Activities outside IFRS 6 scope*

- 19 Main IASB Staff observations were:
  - (a) Some stakeholders support developing a standard which addresses all extractive activities.
  - (b) Stakeholders identified challenges applying particular requirements in other IFRS Standards to extractive activities—most challenges are similar to those faced by entities in other industries but in some cases may be particularly difficult for entities with extractive activities due to the inherent uncertainty and judgement involved—some diversity in practice identified.
  - (c) Active or future IASB projects might consider some of these application challenges (i.e. projects that are not just focused on extractive activities and which may address these challenges as part of their scope).

#### **Questions for EFRAG TEG-CFSS**

- 20 Paragraphs 17 - 19 list key evidence the relevant to the consideration of the scope suggestions. Is there additional evidence you think should be considered?

### **Factors to help define the problem**

- 21 The IASB Staff proposed some factors that could be considered whether the matters identified from their research should be addressed.
  - (a) Does the matter identified affect all entities or is it specific to entities with extractive activities?
  - (b) Does the matter identified relate to activities in the scope of IFRS 6?
  - (c) Does the matter identified give rise to diversity in the treatment of similar transactions?
  - (d) Is the matter identified one for which the IASB could significantly improve the accounting?

## *Extractive Activities – Cover Note*

- (e) Does the matter identified have a material effect on users of financial statements?

### **Question for EFRAG TEG-CFSS**

- 22 Paragraph 0 lists the factors the IASB Staff think the IASB Board should consider determining whether a matter highlighted should be addressed.
- (a) Do you agree with these factors?
  - (b) Are there additional factors you think the IASB Board should consider when deciding what the scope of the project should be?

- 23 Paper 06-02, Appendix A include an update on the research activities undertaken by the IASB Staff.

### **Question for EFRAG TEG-CFSS**

- 24 Do you have any additional comments?

### **Agenda Papers**

- 25 In addition to this cover note, agenda paper 06-02 – *ASAF Extractive Activities* – has been provided for the session.