

Post-conversion IFRS issues for Canadian miners

The IASB's 2009 extractive
industries discussion paper





In August 2009, the International Accounting Standards Board's (IASB) Working Group on Extractive Industries published a Working Draft of a Discussion Paper (the "DP") outlining its preliminary conclusions on significant financial reporting matters in extractive industries. While the conclusions of the DP do not affect the conversion of Canadian entities to International Financial Reporting Standards (IFRS) in 2011, they will likely form the basis for a potential future IASB project on extractive industries.

IFRS is intended to be a set of high quality, principles-based and transparent standards that will enhance the comparability and informativeness of financial statements on a global basis. In the extractive industries sector, it is not clear that the objectives of comparability and informativeness have been accomplished. Existing IFRS standards, notably IFRS 6 governing the treatment of exploration and evaluation activities, permit a wide variety of practices. The IASB has recognized that such divergent practices are inconsistent with its goals and in 2004 initiated a research project to improve financial reporting in this area. The Board has yet to decide whether to add a formal project on extractive industries to its active agenda: a final standard would likely be effective only after several years as an active project. No new standards from this project are expected until 2014 at the earliest.

The proposals in the DP, meanwhile, are an interesting combination of convention and innovation. They include:

- **The adoption** of a single template for the classification of mining reserves and resources based on the CRIRSCO model that views reserves as proven, probable, and possible.
- **The conclusion** that both fair value and "standardized measures" of current value are conceptually sound measures of resource assets, although weaknesses in each approach are recognized.
- **The recommendation** that exploration assets would be measured as the sum of the historical cost of legal rights plus all subsequent exploration and evaluation activities. The unit of account would be based on legally contiguous rights or prospects.
- **The position** that the immediate expensing of exploration and evaluation activities is not appropriate; exploration properties would be tested for impairment whenever evidence is available that full recovery is unlikely.
- **The inclusion** in financial statements of extensive disclosure of : proved reserves and proved and probable reserves by commodity and by country or material project; a current value measurement such as a standardized measure of discounted cash flows; and production revenues by commodity and costs by stage of development over five years on the same basis as reserve quantities.
- **The presentation** in the notes of sensitivity analyses showing the sensitivity of reserve quantity estimates to changes in commodity price assumptions.
- **A consideration** (without a recommendation) that entities publish the aggregate amounts paid to governments in all forms, including royalties, taxes, signature bonuses, and other payments.

While this project is in the research stage, it will presumably culminate in a proposal to the IASB to develop a full-fledged IFRS standard on extractive industries. Preparers should consider providing input to the Working Party's deliberations: views on capitalizing exploration expenditures, on the nature and extent of the disclosure, and on the general ability of financial statements to meet the needs of users without incurring excessive costs or disclosing competitively sensitive information would be useful in the Working Party's development of its final positions.

Responding to the issues

We understand the priorities of entities in the Canadian mining sector in the short-run should be on the execution of a successful conversion to IFRS. The Extractive Industries project will not affect the conversion of Canadian mining companies to IFRS for the 2011 reporting year. It is also important to note that the DP is a research paper, not a proposal to establish an IFRS standard. It is incomplete and likely to undergo further development before its completion, the next step after which would be to determine whether the IASB believes it should formally commence developing an IFRS standard on the topics addressed in the DP. Extensive discussion and consultation will ensue before the DP proceeds to IFRS accounting standards

While the issues in the DP do not directly affect the standards governing the conversion in 2011, mining entities should seriously consider the challenges the Working Group addresses, and the entities should consider providing comments on the combination of measurement, classification and disclosure provisions the Working Group proposes. Undoubtedly, the conceptual basis for the proposed treatment of exploration and evaluation stage assets provided in the DP is an interesting perspective on the financial reporting process in the exploration and development stage.

In many cases, the additional information proposed as disclosure in the DP is already published by Canadian entities in regulatory filings. Thus, it may not have incremental information value or cost to assemble, at least on an annual basis. However, that observation does not address the concern that the financial statements are published quarterly in Canada. Would the disclosure proposed in the DP also have to be updated quarterly? Furthermore, the inclusion of

such information even on an annual basis may make the financial statements so voluminous as to be unwieldy. For smaller entities, the inclusion of such information in the financial statements may not pose significant logistical challenges, but for entities with many locations the financial statements may become extremely long.

The Working Group has in fact solicited input on the DP in its current form as it labours to conclude the research phase of the project. Post the conversion process, it would behoove Canadian preparers to monitor this project and make their views known on as timely basis as possible. For further discussion of the issues raised in the DP, see www.deloitte.ca for a copy of the Deloitte Canada publication: "Blending convention with innovation: The IASB Working Group's Extractive Industries' 2009 Discussion Paper"

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