



Update on the IASB's Extractive Activities Research Project

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Extractive activities project – research objective

- To take a “fresh look” at how to account for oil & gas and mineral reserves/resources
- Why?
 - IFRS 6 Exploration for and Evaluation of Mineral Resources is only an interim solution
 - existing IFRSs do not adequately address unique (or unusual) features of oil & gas and mining extractive activities
 - some question the relevance of existing practices in accounting for extractive activities

Research project team

- **An international project team of accounting standard setters is undertaking the research**
 - Australia, Canada, Norway & South Africa
- **Advisory panel is assisting the project team**
 - large and small oil & gas and mining companies
 - analysts and other users of financial reports
 - auditors
 - securities regulators (including SEC)
- **Advisory panel is geographically diverse**
 - Africa, Asia-Pacific, Europe & North America

Key research questions

- **When should an asset be recognised on the balance sheet?**
- **How should reserves/resources recognised on the balance sheet be measured?**
- **What reserves/resources information should be disclosed in the financial report?**
- **How should reserves/resources be defined?**

Asset recognition

- **Principle: must meet definition of an asset to be recognised in the balance sheet**
 - expenditures that do not relate to a recognised asset are expensed
 - focus has often been on activities, not asset definition
- **An asset is a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity (IASB Framework)**

Asset recognition

- **What is the asset?**
 - Initially legal rights to explore
 - Exploration results in knowledge
 - Ultimately (we hope!) reserves are identified
- **In this continuum, when can an asset be initially recognised?**
 - when does entity have control over future benefits?
 - application of recognition criteria

Asset recognition

- **Exploration rights are an asset**
 - Point of initial recognition of an asset
- **Over time this asset is modified by**
 - Exploration which results in increased knowledge about the asset
 - Further legal rights e.g. development permits, environmental approvals

Asset recognition

- **Conclusions**

- This legal rights asset evolves from initial exploration to production
- Separate mineral resource asset is not recognised
- Communication about geological and legal rights uncertainty can be achieved through presentation and disclosure

Asset measurement

- **Historical cost?**

- verifiable, but ...
- cost has limited relevance to users
 - no correlation between finding & development costs incurred and the future cash flows that will be generated from the mining property
- impairment testing
 - IAS 36
 - exploration properties
 - what volumes?

Asset measurement

- **Fair value?**

- seems relevant (in principle), but ...
- requires many subjective assumptions and estimates
 - is it meaningful?
 - extent of disclosures required (FAS 157)
- time and effort
 - is it feasible? Cost/benefit?
 - update every year? Quarter?
- income statement implications

Asset measurement

- **Simplified fair value?**

- use standardised assumptions e.g. price to reduce subjectivity, increase comparability
 - U.S. requirement for standardised measure for oil & gas
- addresses some of the preparer concerns
- is the information relevant?
- income statement implications remain

User survey

- **34 users interviewed – sell-side, buy-side, debt rating agencies, lenders, venture capital**
- **Results**
 - limited usefulness in historical cost measurement of reserves/resources
 - limited interest in valuing reserves/resources on balance sheet, or as part of note disclosures (either fair value or current value)
 - want information to input into own models
 - disclosures are key

Disclosure

- **Very little disclosure requirements in IFRS for extractive activities/assets**
- **Disclosure requirements typically regulatory**
 - varies by regulator
- **Many companies disclose additional information outside regulatory filings**
 - not consistent
- **Including in IFRS would create a consistent base of disclosures by all IFRS companies**

Disclosure

- **Factors to consider:**

- Proved reserves? All reserves? Resources?
- Management's assumptions or standardised assumptions?
- Disclosure of assumptions?
- Disaggregation? By mineral? By continent? By country? By property?
- Same disclosures for mining and oil & gas?
- Disclose fair/simplified fair value?

Definitions

- **No single agreed definition of reserves or resources for the extractive industries**
- **IASB requested SPE (oil & gas) and CRIRSCO (mining) to identify opportunities for converging elements of their definitions**
- **Positive outcome**
 - new PRMS (oil & gas) improves comparability
 - a “mapping document” explains the similarities (and differences) between the systems and indicates broad equivalence
 - reserve and resource classifications can therefore provide the building blocks of the accounting model

Project timing

- **Discussion paper expected late 2008/early 2009**
 - Identify possible accounting alternatives
- **Expected key points**
 - Legal rights (even early stages) represent assets
 - Account at a property level
 - Both historical cost and fair value will be included
 - Reserve disclosures required

Project timing

- **Discussion paper and comments will be key input for IASB in developing an IFRS for extractive activity accounting**
 - Comments from industry critical
- **Timing of final standard dependent on many factors**

Questions





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