EFRAG

European Financial Reporting Advisory Group

# The costs and benefits of implementing the IFRIC Interpretation 20 Stripping Costs in the Production Phase of a Surface Mine

## Introduction

1 Following discussions between the various parties involved in the EU endorsement process, the European Commission decided in 2007 that more extensive information than hitherto needs to be gathered on the costs and benefits of all new or revised Standards and Interpretations as part of the endorsement process. It has further been agreed that EFRAG will gather that information in the case of the IFRIC Interpretation 20 *Stripping Costs in the Production Phase of a Surface Mine* ('IFRIC 20').

2 EFRAG first considered how extensive the work would need to be. For some Standards or Interpretations, it might be necessary to carry out some fairly extensive work in order to understand fully the cost and benefit implications of the Standard or Interpretation being assessed. However, in the case of IFRIC 20, EFRAG's view is that the cost and benefit implications can be assessed by carrying out a more modest amount of work. The results of the consultations that EFRAG has carried out seem to confirm this. Therefore, as explained more fully in the main sections of this report, the approach that EFRAG has adopted has been to carry out detailed initial assessments of the likely costs and benefits of implementing the IFRIC 20 in the EU, to consult on the results of those initial assessments, and to finalise those assessments in the light of the comments received.

*EFRAG's endorsement advice*

3 EFRAG also carries out a technical assessment of all new and revised Standards and Interpretations issued by the IASB against the so-called endorsement criteria and provides the results of those technical assessments to the European Commission in the form of recommendations as to whether or not the Standard or Interpretation assessed should be endorsed for use in the EU. As part of those technical assessments, EFRAG gives consideration to the costs and benefits that would arise from implementing the new or revised Standard or Interpretation in the EU. EFRAG has therefore taken the conclusion at the end of this report into account in finalising its endorsement advice.

## A SUMMARY OF IFRIC 20

### Background

4 The IFRIC Interpretation Committee ('IFRS IC') had been requested to clarify the accounting treatment for stripping costs in the production phase of a surface mine because the lack of specific guidance in existing IFRSs had given rise to diversity in practice.

**The issue**

5 Entities engaged in surface mining often during the production phase of the mine need to remove mine waste material ('overburden') to gain access to mineral ore deposits. The removal of such waste material could result in a combination of ore and waste, which may contain some usable material, or it could instead allow the access to material that has a higher ratio of ore to waste.

**What has changed?**

6 IFRIC 20 *Stripping Costs in the Production Phase of a Surface Mine* ('IFRIC 20') provides guidance on recognition of production stripping costs as an asset and the initial and subsequent measurement of the stripping activity asset.

*Recognition*

7 To the extent that the benefit from the stripping activities is realised in the form of inventory produced, the entity shall account for the costs of that stripping activities in accordance whit the principles of IAS 2 *Inventories*. To the extent the benefit is improved access to ore, the entity shall recognise these costs as non-current assets, if further criteria in paragraph 9 of IFRIC 20 are met (i.e. 'stripping activity asset'). In addition, IFRIC 20 requires that the stripping activity asset be accounted as an enhancement of an existing asset and be classified according to the nature of the existing asset of which it is part.

*Initial measurement*

8 A stripping activity asset shall be initially measured at cost. Cost can be determined by considering both direct costs incurred to perform the activities and directly attributable overhead costs.

9 Costs related to incidental operations performed at the same time of the production stripping activities are recognised in profit and loss.

10 When the costs of the stripping activity asset and the inventory produced are not separately identifiable, entities are required to allocate such costs based on a relevant production measure.

*Subsequent measurement*

11 The stripping activity asset shall be measured, after initial recognition, at its cost or revalued amount less depreciation or amortisation and less any impairment losses in the same way as the asset that it is part of.

12 The depreciation or amortisation amount shall be allocated on a systematic basis over the useful life of the identified component of the ore body. In order to determine the depreciation or amortisation expense, the units of production method shall be applied unless another method is more appropriate.

**When does IFRIC 20 become effective?**

13 IFRIC 20 becomes effective for annual periods beginning on or after 1 January 2013 and the entities shall apply it to production stripping costs incurred on or after the beginning of the earliest period presented. Early application is allowed and the entities have to disclose this fact.

14 As at the beginning of the earliest period presented, any previously recognised asset balance that resulted from stripping activity undertaken during the production phase shall be reclassified as a part of an existing asset to which the stripping activity related, and depreciated or amortised in the same way as the asset that it is part of. If there is no identifiable component of the ore body to which that predecessor stripping asset relates, it shall be recognised in opening retained earnings at the beginning of the earliest period presented.

**EFRAG's initial analysis of the costs and benefits of IFRIC 20**

15 EFRAG carried out an initial assessment of the costs and benefits expected to arise for preparers and for users from implementing IFRIC 20, both in year one and in subsequent years. The results of EFRAG's initial assessment can be summarised as follows:

(a) *Costs* – EFRAG's initial assessment was that IFRIC 20 would result in some one-off costs and some incremental ongoing costs for some preparers, but that these costs were unlikely to be significant.

(b) *Benefits* – EFRAG's initial assessment was that preparers were likely to benefit from IFRIC 20, as it is likely to reduce the diversity of accounting in practice thus enhancing comparability and consistency of the information provided to all stakeholders.

16 EFRAG published its initial assessment and supporting analysis on 9 November 2011. It invited comments on the material by 9 December 2011. In response, EFRAG received seven comment letters. Three respondents agreed with EFRAG's assessment of the benefits of implementing the IFRIC 20 and the associated costs involved for users and preparers. The remaining four respondents did not comment specifically on EFRAG's initial assessment of the costs and benefits of implementing the IFRIC 20 in the EU, but supported EFRAG's recommendation that IFRIC 20 be adopted for use in Europe.

**EFRAG's final analysis of the costs and benefits of IFRIC 20**

17 Based on its initial analysis and stakeholders' views on that analysis, EFRAG's detailed final analysis of the costs and benefits of IFRIC 20 is presented in the paragraphs below.

*Cost for preparers*

18 EFRAG notes that changes introduced by IFRIC 20 require capturing or tracking new information, thus it is expected that some preparers will have to incur one-off costs to understand the new requirements and to train their employees; however these costs are not expected to be significant given that entities collect similar information already for management purposes.

19 Some incremental costs are expected in relation to documentation of the expenses which will be included into the stripping activity asset. EFRAG understands that those entities that did not capitalise stripping costs during production phase of a surface mine, did capitalise stripping costs in the pre-production phase of a surface mine. Therefore, they will not need to implement significant new systems to allow them to accounting for capitalised stripping costs as such. However, they will incur insignificant one-off costs in applying IFRIC 20 related to the change in accounting

policy that they need to make prospectively. Those costs will depend on the extent to which their current accounting practices differ from requirements under IFRIC 20.

20 EFRAG also understands that for those entities that currently capitalise stripping costs in the production phase of a surface mine, there will be not be any significant incremental costs as they will only need to make relatively minor changes to their accounting practices.

21 Finally, EFRAG foresees some effort to prepare, review and audit the stripping activity asset, with no significant incremental ongoing costs.

22 IFRIC 20 is to be applied prospectively from 1 January 2013, although earlier application is permitted. Thus, there are no costs that entities will incur regarding the restatement of comparative information.

23 In summary, EFRAG's assessment is that IFRIC 20 will result in some year one costs and some incremental ongoing costs for some preparers, but that these costs are unlikely to be significant.

*Costs for users*

24 EFRAG has carried out an assessment of the cost implications for users resulting from IFRIC 20 and it is not aware of any aspect of IFRIC 20 that will increase the costs users will incur in analysing the financial statements as a result of its adoption.

*Benefits for preparers and users*

25 EFRAG has carried out an assessment of the benefits for users and preparers resulting from IFRIC 20 and it has concluded that preparers and users are likely to benefit from its application.

26 EFRAG believes that IFRIC 20 is likely to reduce the diversity of accounting in practice thus enhancing comparability and consistency of the information provided.

*Conclusion*

27 Overall, EFRAG's assessment is that the benefits of reducing the diversity of accounting in practice are likely to outweigh the one-off costs of implementation and the ongoing costs of complying with IFRIC 20.

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