EFRAG
European Financial Reporting Advisory Group

Jonathan Faull
Director General
European Commission
Directorate General for the Internal Market
1049 Brussels

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Dear Mr Faull

Adoption of IFRIC Interpretation 20 Stripping Costs in the Production Phase of a Surface Mine

Based on the requirements of the Regulation (EC) No 1606/2002 of the European Parliament and of the Council on the application of international accounting standards we are pleased to provide our opinion on the IFRIC Interpretation 20 *Stripping Costs in the Production Phase of a Surface Mine* ('IFRIC 20'), which was issued by the IASB on 19 October 2011. It was issued as an Exposure Draft in August 2010 and EFRAG commented on that draft.

The objective of IFRIC 20 is to provide guidance on recognition of production stripping costs as an asset and on the initial and subsequent measurement of the stripping activity asset in order to reduce the diversity in practice as to how entities account for stripping costs incurred in the production phase of a surface mine

IFRIC 20 becomes effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted, however entities shall disclose that fact.

EFRAG has carried out an evaluation of IFRIC 20. As part of that process, EFRAG issued its initial assessment for public comment and, when finalising its advice and the content of this letter, it took the comments received in response into account. EFRAG's evaluation is based on input from standard setters, market participants and other interested parties, and its discussions of technical matters are open to the public.

EFRAG supports IFRIC 20 and has concluded that it meets the requirements of the Regulation (EC) No 1606/2002 of the European Parliament and of the Council on the application of international accounting standards in that it:

- is not contrary to the principle of 'true and fair view' set out in Article 16(3) of Council Directive 83/349/EEC and Article 2(3) of Council Directive 78/660/EEC; and

- meets the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management.

For the reasons given above, EFRAG is not aware of any reason to believe that it is not conducive to the European public good to adopt IFRIC 20 and, accordingly, EFRAG recommends its adoption. EFRAG's reasoning is explained in the attached 'Appendix - Basis for Conclusions'.

On behalf of EFRAG, I should be happy to discuss our advice with you, other officials of the EU Commission or the Accounting Regulatory Committee as you may wish.

Yours sincerely

Françoise Flores
EFRAG Chairman

APPENDIX
BASIS FOR CONCLUSIONS

EFRAG'S TECHNICAL ASSESSMENT OF IFRIC 20 AGAINST THE ENDORSEMENT CRITERIA

This appendix sets out the basis for the conclusions reached, and for the recommendation made, by EFRAG on IFRIC Interpretation 20 Stripping Costs in the Production Phase of a Surface Mine *('IFRIC 20').*

In its comment letters to the IASB, EFRAG points out that such letters are submitted in EFRAG's capacity of contributing to the IASB's due process. They do not necessarily indicate the conclusions that would be reached by EFRAG in its capacity of advising the European Commission on endorsement of the definitive IFRS in the European Union and European Economic Area.

In the latter capacity, EFRAG's role is to make a recommendation about endorsement based on its assessment of the final IFRS or Interpretation against the technical criteria for the European endorsement, as currently defined. These are explicit criteria which have been designed specifically for application in the endorsement process, and therefore the conclusions reached on endorsement may be different from those arrived at by EFRAG in developing its comments on proposed IFRSs or Interpretations. Another reason for a difference is that EFRAG's thinking may evolve.

Does the accounting that results from the application of IFRIC 20 meet the technical criteria for EU endorsement?

1 In evaluating IFRIC 20, EFRAG asked itself four questions:

   (a) Is there an issue that needs to be addressed?

   (b) If there is an issue that needs to be addressed, is an Interpretation an appropriate way of addressing it?

   (c) Is IFRIC 20 a correct interpretation of existing IFRS?

   (d) Does the accounting that results from the application of IFRIC 20 meet the technical criteria for EU endorsement?

Is there an issue that needs to be addressed?

2 EFRAG understands that at the present there is diversity in practice as to how entities account for stripping costs incurred in the production phase of a surface mine. Currently, some entities capitalise these costs, while others recognise them as an expense. EFRAG agrees that this diversity is undesirable and is an issue that needs to be addressed.

Is an interpretation an appropriate way of addressing it?

3 An Interpretation is an appropriate way of addressing diversity in accounting practice if that diversity arises because of factors other than inconsistencies between IFRS. Furthermore, in EFRAG's view, Interpretations should not be used to address major issues.

4 EFRAG's assessment is that the diversity in practice that is the subject of IFRIC 20 falls into neither of these categories. As such, EFRAG has concluded that an Interpretation is an appropriate way of addressing the uncertainties relating to how an entity should account for stripping costs in the production phase of a surface mine.

Is IFRIC 20 a correct interpretation of existing IFRS?

5 EFRAG has considered whether IFRIC 20 is a correct interpretation of existing IFRS literature. IFRIC 20 addresses three main issues relating to how an entity should account for stripping costs in the production phase of a surface mine:

(a) recognition of production stripping costs as an asset;

(b) initial measurement of the stripping activity asset; and

(c) subsequent measurement of the stripping activity asset

6 For the reasons discussed below, EFRAG agrees that this is an appropriate interpretation of existing IFRS.

Recognition of production stripping costs as an asset

7 To the extent the benefit from the stripping activities is improved access to ore, IFRIC 20 requires that an entity shall recognise as a non-current asset the stripping costs incurred in the production phase of a surface mine (i.e. stripping activity asset) when they meet all of the following recognition criteria:

(a) It is probable that the future economic benefit (improved access to the ore body) associated with the stripping activity will flow to the entity;

(b) The entity can identify the component of the ore body for which access has been improved; and

(c) The costs relating to the improved access to the component can be measured reliably.

8 EFRAG agrees that this is an appropriate interpretation of existing IFRS as it is consistent with the requirements of IAS 16 *Property, Plants and Equipments* ('IAS 16') and IAS 38 *Intangible Assets* ('IAS 38').

Initial measurement of the stripping activity asset

9 A stripping activity asset shall be initially measured at cost, which includes both direct costs incurred to perform the activities and directly attributable overhead costs. However, costs related to incidental operations performed at the same time of the production stripping activities are recognised in profit and loss. If 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.

10 EFRAG agrees that this is an appropriate interpretation of existing IFRS.

Subsequent measurement of the stripping activity asset

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. 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.

12 EFRAG agrees that this is an appropriate interpretation of existing IFRS as it is consistent with the requirements of IAS 16 and IAS 38.

Does the accounting that results from the application of IFRIC 20 meet the technical criteria for EU endorsement?

13 EFRAG has considered whether IFRIC 20 meets the technical requirements of the European Parliament and of the Council on the application of international accounting standards, as set out in Regulation (EC) No 1606/2002, in other words that IFRIC 20:

(a) is not contrary to the principle of 'true and fair view' set out in Article 16(3) of Council Directive 83/349/EEC and Article 2(3) of Council Directive 78/660/EEC; and

(b) meets the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management.

EFRAG also considered, based only on evidence brought to its attention by constituents, whether it would be not conducive to the European public good to adopt IFRIC 20.

Relevance

14 Information is relevant when it influences the economic decisions of users by helping them evaluate past, present or future events or by confirming or correcting their past evaluations.

15 EFRAG considered whether IFRIC 20 would result in the provision of relevant information – in other words, information that has predictive value, confirmatory value or both – or whether it would result in the omission of relevant information.

16 IFRIC 20 treats a stripping activity asset as an addition to, or as an enhancement of, an existing asset. It requires that a stripping activity asset is classified as a tangible or intangible asset is the same as the existing asset. After initial recognition, the stripping activity asset is measured in the same way as the existing asset of which it is a part.

17 IFRIC 20 helps users in assessing the financial performance of an entity by requiring that stripping activity assets are accounted for in the same way as other improvement to existing tangible or intangible assets. Therefore, EFRAG concluded that the application of IFRIC 20 would result in provision of relevant information.

18 EFRAG's overall assessment is that IFRIC 20 would result in the provision of relevant information; and therefore it satisfies the relevance criterion.

Reliability

19 EFRAG also considered the reliability of the information that will be provided by applying IFRIC 20. Information has the quality of reliability when it is free from material error and bias and can be depended upon by users to represent faithfully what it either purports to represent or could reasonably be expected to represent, and is complete within the bounds of materiality and cost.

20 There are a number of aspects to the notion of reliability: freedom from material error and bias, faithful representation, and completeness.

21 IFRIC 20 requires recognition of a stripping activity asset only if the costs relating to that asset can be measured reliably. Furthermore, the requirements and guidance in IFRIC 20 are closely aligned with the requirements of IAS 16 and IAS 38. Therefore, in EFRAG's view, IFRIC 20 does not raise any significant new concerns.

22 EFRAG's overall assessment is that IFRIC 20 would raise no concerns about risk of error or bias; and therefore it satisfies the reliability criterion.

Comparability

23 The notion of comparability requires that like items and events are accounted for in a consistent way through time and by different entities, and that unlike items and events should be accounted for differently.

24 EFRAG has considered whether IFRIC 20 results in transactions that are:

(a) economically similar being accounted for differently; or

(b) transactions that are economically different being accounted for as if they are similar.

25 IFRIC 20 prescribes a single accounting treatment for stripping costs incurred in the production phase of a surface mine that removes the existing diversity in practice. In addition, it provides guidance that ensures consistent accounting for stripping costs and ensures comparability between entities. For these reasons, EFRAG's overall assessment is that IFRIC 20 satisfies the comparability criterion.

Understandability

26 The notion of understandability requires that the financial information provided should be readily understandable by users with a reasonable knowledge of business and economic activity and accounting and the willingness to study the information with reasonable diligence.

27 Although there are a number of aspects to the notion of 'understandability', EFRAG believes that most of the aspects are covered by the discussion above about relevance, reliability and comparability.

28 As a result, EFRAG believes that the main additional issue it needs to consider, in assessing whether the information resulting from the application of IFRIC 20 is understandable, is whether that information will be unduly complex.

29 EFRAG concluded that the information that results from the application of IFRIC 20 is understandable because, as noted above in the assessment of the reliability criterion, IFRIC 20 is closely aligned with the requirements of IAS 16 and IAS 38.

30 In EFRAG's view, IFRIC 20 does not introduce any new complexities that may impair understandability. Therefore, EFRAG's overall assessment is that IFRIC 20 satisfies the understandability criterion in all material respect.

True and Fair

31 EFRAG has concluded that the information resulting from the application of IFRIC 20 would not be contrary to the principle of true and fair view.

European public good

32 EFRAG is not aware of any reason to believe that it is not conducive to the European public good to adopt IFRIC 20.

Conclusion

33 For the reasons set out above, EFRAG has concluded that IFRIC 20 satisfies the technical criteria for EU endorsement and EFRAG should therefore recommend its endorsement.