



# Is AASB 6 still fit for purpose?

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# Background of IFRS 6

1998

- Extractive Industries Project announced

2000

- Issues Paper released

2004

- IFRS 6 released

2010

- Reassessment of IFRS 6

2018

- Revise or replace IFRS 6
- IFRS 6 still for purpose?



# Australia's equivalent of IFRS 6 – AASB 6

AASB 6 is largely consistent with IFRS 6, except for the inclusion of additional Australia-specific paragraphs relating to the scope, measurement and recognition of E&E expenditures

IFRS 6 allows companies to adopt their treatment of choice, typically the full cost or successful efforts method or a variation thereof while AASB 6 narrows treatment by specifying the use of the Area-Of-Interest method for Australian companies

- *An area-of-interest refers to an individual geological area whereby the presence of a mineral deposit or an oil or natural gas field is considered favourable or has been proved to exist. ... In most cases, an area-of-interest will comprise a single mine or deposit or a separate oil or gas field (AASB 6, Para. AUS7.3).*

# Method

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Phase 1 is a survey of the current disclosure practices from the 2018 Annual Reports of 98 companies listed on the Australian Stock Exchange (ASX)

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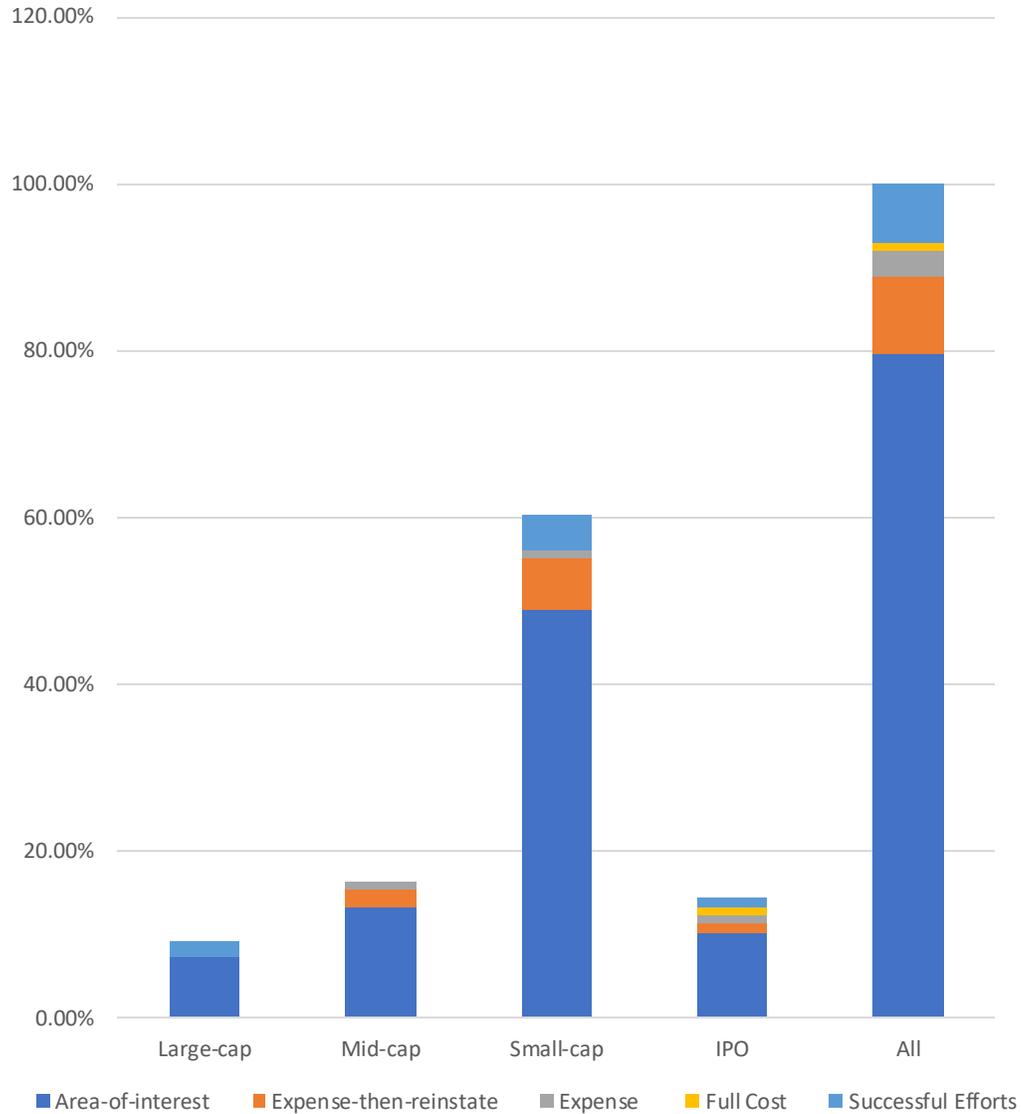
Phase 2 considered whether any significant regulatory or other industry-relevant changes had impacted reporting practices since the IASB last examined this issue at the time of their 2010 Discussion Paper

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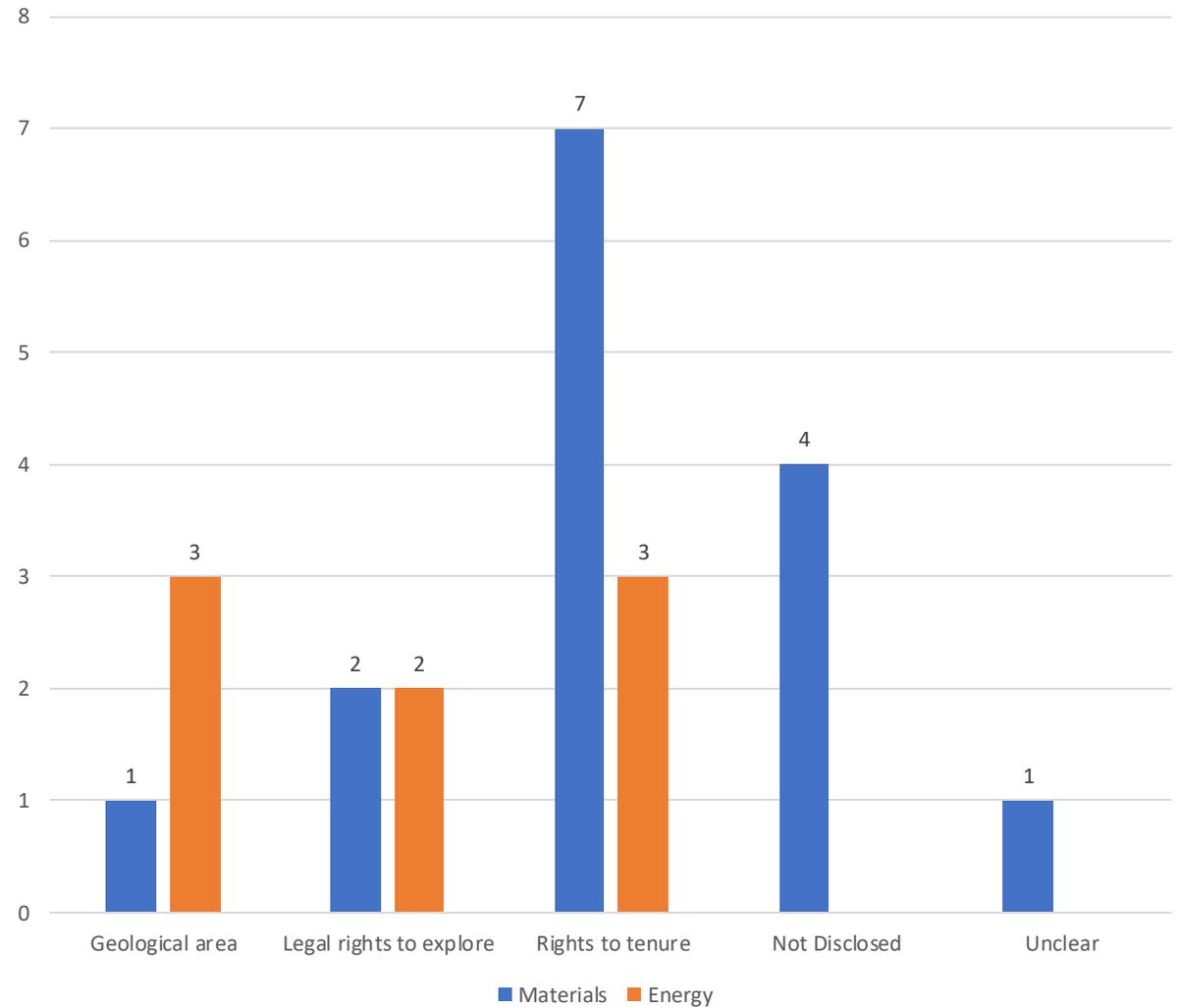
Phase 3 included interviews conducted with industry stakeholders

- Interviewees comprised eight preparers of financial statements, including two junior, and six large; two regulators; and two accountants from Big 4 firms

# Accounting method for E&E assets



# How AOI is defined?



# Is an extractive industries standard needed?

Interviewees believed that extractive industries standard was important and in need of revisiting, especially on the issue of guidance

- *...between the release of the Discussion Paper in 2010 and where we're at today, not much has changed from a standard-setting perspective. In terms of IFRS6...that is an area where there is still lack of clarity as to what the accounting should be*
- *...we would see it as an application-guidance issue...we have to borrow [from other standards] because [an issue] is not spelled out in AASB 6)*

Lack of guidance led to impediments in practice and the interpretation of accounting reports

- *...Unless you really have good knowledge of the accounting choices people are making, you wouldn't realise people can actually do whatever they want*

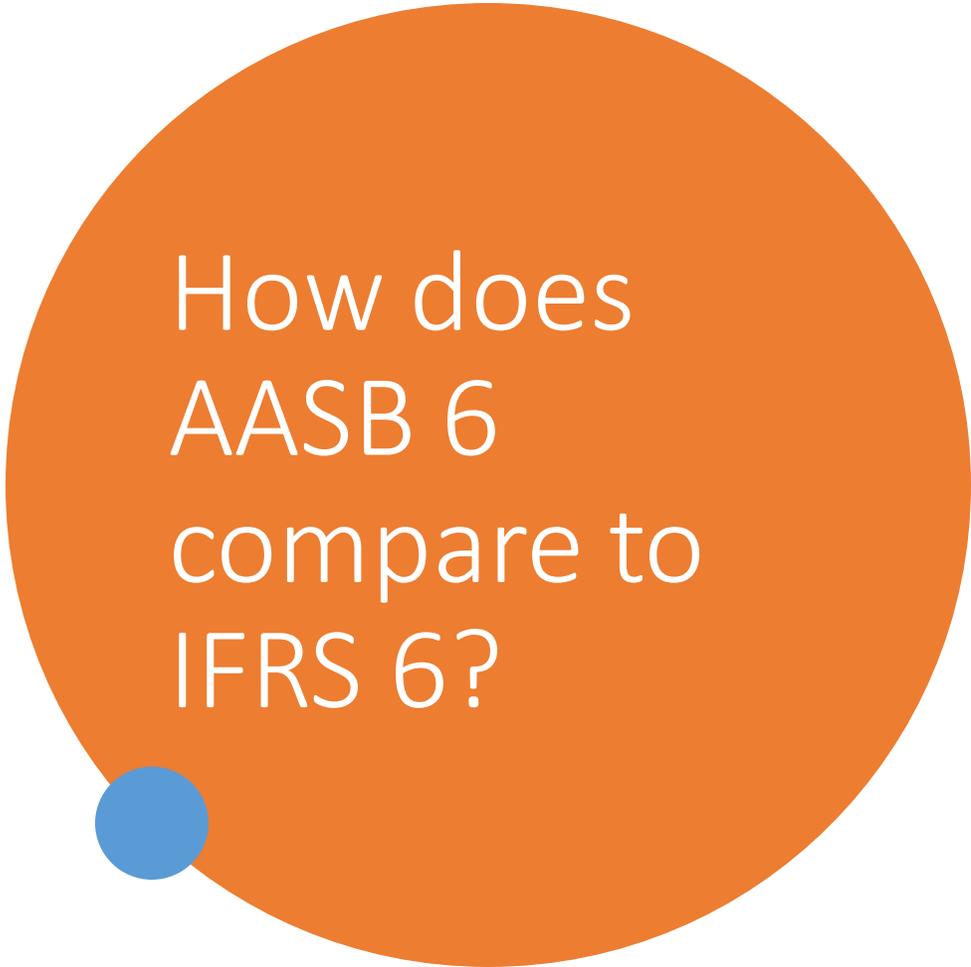
# Implications of limited guidance

## Limited guidance affords companies significant flexibility

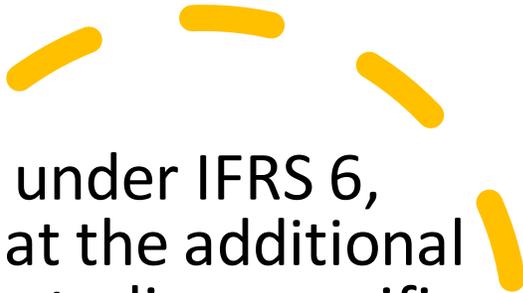
- *...we are able to build up an argument that “I can keep this expenditure on the books because in some way it supports my interpretation of this area*

Requires too much reliance on external guidance such as the IFRS publication “Financial Reporting in Oil and Gas” and “Financial Reporting in Mining”

- *...having flexibility is good, but there are cases where we struggle to get guidance when we need it...whether that’s from the accounting firms or speaking to peers in the industry, we kind of look around to others for an answer*



## How does AASB 6 compare to IFRS 6?



Despite flexibility permitted under IFRS 6, many interviewees noted that the additional guidance provided by the Australian-specific sections of AASB 6 as an improvement

- ...*The move to IFRS was seen as a positive move to standardise practice in the industry, resulting in less cowboys out there*
- ...*[however] there's no doubt that the Australian version of the standard, AASB 6, is far superior to the IFRS one*
- ...*Our starting point is the area-of-interest. I think that makes sense, and I think it's good that we actually have had that added in, because it gives that clarity that the international version doesn't*

# New standards

- Recent amendments to standards have affected extractive industries reporting
  - changes to leasing
    - Lease accounting becomes even more complicated in situations where a company is carrying out capital works as part of a mine closure. If, for example, an owned asset is built on leased land, there is an issue around whether the *closure rehabilitation obligation is part of the tangible asset or part of the leased asset*
  - revenue recognition
  - definition of assets and liabilities
- Importance of closure and rehabilitation obligations increases in future, knowing how to account for them is going to become critical
  - *...there is not a huge amount of guidance on [this]*

# Industry resources

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- Industry resources helpful for determining assessment of resources are the JORC Code for the mining industry, and the PRMS Guidelines for the oil and gas industry
- These resources provide guidance for the definition, classification, and estimation of mineral and oil and gas reserves
  - ...key to determining what the *production profile and useful life of the assets* are
  - ....*critical to understanding company value...and drive a lot of the accounting achievement*
  - ...very important when looking at *impairments for cash generating units*
  - ...I think it is fair to say that it [the *JORC statement*] carries the gravitas that an audit report would carry

# Environmental sustainability

- Increasing environmental obligations as part of the changing profile of the extractive industries sector
- Focus on sustainability has resulted in an increase in the number of contracts embedding financial penalties and termination clauses for breaches or non-performance in environmental performance
  - ...*climate change and the **accounting treatment of carbon-offsets and 'assets', especially the determination of impairment** regardless of whether there is a market or not*
  - ...*thermal coal industry in particular are "getting a lot of pressure from financiers, from shareholders, from insurers...And I think life is a whole lot more difficult for them*
  - ...*focus on a **low-carbon economy has meant discounting because of the implications of climate change***

# Changes in financing, commodities and technology

Extractive operations have also become more complex as different types of commodities, such as coal seam gas (CSG), have become commercially viable as a result of technological developments in extraction techniques

- *...people are still trying to get their heads around how you account for this thing*
- ambiguity about the definition of a reserve and resource (AASB, 2018) leading to questions around the *“impairment of a CSG asset”*

## Innovative financing

- streaming arrangements where a right to a certain percentage or amount of future production is exchanged for a significantly discounted upfront payment
- ...arrangements and contracts can be “extremely complex” and “do not find a natural ‘home’ in the IFRS accounting standards” (PricewaterhouseCoopers, 2015, p.1)

# Summary of findings

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- Significant changes giving rise to accounting policies and reporting issues
  - Impairment of E&E assets
  - Closure obligations
  - New leasing standard
- Changes in activities and emergence of new industries such as CSG and new technologies expanded nature and scope of deposits
- JORC is primary reserves and resource classification system used
  - Use in measurement, should it be extended to valuation?
- Changes in the regulatory environment and the uncertainty around the future treatment of climate change impact
  - hardening credit market for coal industry leads to alternative financing

# Recommendations

- Proceed with the development of amendments to IFRS 6 to enhance disclosure requirements
  - Flexibility impeded comparability leading to less decision usefulness
  - Dedicated extractive industries standard to enable its unique characteristics to be accommodated, particularly with respect to the risk/reward business model and the hybrid tangible/intangible nature of E&E assets
- Additional guidance on criteria for
  - Expense vs. capitalisation
  - Impairment
  - Joint financing arrangements
  - Merging mining practices
  - Definition and scope of area of interest

