

Issues Paper – IFRS Interpretations Committee revised draft
Interpretation of DI/2010/1
Stripping Costs in the Production Phase of a Surface Mine

Purpose of this Paper

1. To seek the Board's view on whether staff should draft a letter to the IFRS Interpretations Committee (the Committee) to acknowledge its efforts to improve the draft Interpretation DI/2010/1 *Stripping Costs in the Production Phase of a Surface Mine*, but note that there are still fundamental concerns with the proposals that have not been sufficiently addressed in the revised draft Interpretation.
2. This paper includes:
 - (A) background to DI/2010/1 and the revised draft Interpretation; and
 - (B) an AASB staff analysis addressing the main issue and other interrelated issues identified in the revised draft Interpretation.

(A) Background

3. The Committee published DI/2010/1 (see Agenda paper 17.5) for comment in August 2010. DI/2010/1 proposed:
 - (a) capitalising production stripping costs that are part of a 'stripping campaign', as a component of the larger asset (i.e. the specific section of an ore body that becomes directly accessible as a result of the stripping campaign);
 - (b) depreciating/amortising the stripping campaign component over the expected useful life of the section of ore that becomes directly accessible as a result of the 'stripping campaign' (i.e. specific identification approach), based on the units of production method unless another method is more appropriate;
 - (c) accounting for routine stripping costs that are not incurred as part of a stripping campaign as a production cost in accordance with IAS 2 *Inventories*; and
 - (d) on transition, any existing stripping campaign component asset that cannot be directly associated with an identifiable section of the ore body and any existing stripping cost liability balances would be recognised in profit or loss at the beginning of the earliest period presented.

4. The AASB provided its comments on DI/2010/1 to the Committee in November 2010. Based on the feedback received from respondents, the Committee decided to amend the draft interpretation. IASB staff presented, as a staff paper, a revised draft Interpretation at the May 2011 Committee meeting (refer to Agenda paper 17.6). The revised draft Interpretation includes a revised principle for capitalisation of production stripping costs, and for the allocation of those costs between the current and future periods. Refer to **Appendix A** of this paper for the revised proposals, the comparative proposals in DI/2010/1, relevant AASB comments on DI/2010/1 and AASB staff comments/recommendations.

(B) Staff Analysis of remaining Key Issues

5. Although the Committee has made improvements in the revised draft Interpretation, AASB staff think the main issue and some interrelated issues have not been sufficiently addressed. The main issue is addressed in paragraph 6 below. The interrelated issues have been noted in paragraph 7 below and discussed in more detail in **Appendix A** of this paper.

Identification of the specific component of ore body (Issue No 1 in Appendix A)

6. The revised draft Interpretation in substance still proposes to attribute stripping costs to separately identifiable sections of ore body. In its submission to the Committee on DI/2010/1, the AASB disagreed with the proposed unit of account on the basis that the attribution of stripping costs to separately identifiable sections of ore is not a relevant or reliable depiction of how most mines operate. The AASB was concerned that the application of the proposed unit of account would be difficult for many mining entities to apply in practice, especially in complex scenarios. The AASB considered the componentising of one large body of ore that is not fully identifiable was an impracticable interpretation of the accounting principles. The AASB questioned whether the application of a specific identification approach may cause practical difficulties.
7. The main interrelated issues include the:
 - (a) new asset recognition criterion (Issue No 2 in Appendix A)
 - (b) limitation of the proposals to the production phase (Issue No 3 in Appendix A)
 - (c) allocation to the specific component of ore body (Issue No 6 in Appendix A)

Staff recommendation

AASB staff recommend writing to the Committee, acknowledging its efforts to improve the draft Interpretation, but noting that there are still fundamental concerns with the proposals that have not been sufficiently addressed.

Question for the Board

- (a) Does the Board wish to write a letter to IFRS Interpretation Committee incorporating the concerns addressed in this issues paper?
- (b) If so, does the Board wish to form a Subcommittee to finalise the letter?
- (c) If so, when does the Board propose doing so, considering IASB staff will be presenting a final draft Interpretation at the next Committee meeting on 7-8 July 2011?

Appendix A – Comparison of key proposals in DI/2010/1 and the revised draft Interpretation

No	DI/2010/1	Revised draft Interpretation	AASB comments on DI/2010/1	AASB staff comments/recommendations
1	<p>The costs of stripping activities that are part of a ‘stripping campaign’ (i.e. systematic efforts to gain access to a specific section of the ore body) shall be accounted for as an addition to, or an enhancement of, an existing asset. Accordingly, the costs incurred will be accounted for as a component of an existing asset, called a ‘stripping campaign component’.</p> <p>The stripping campaign component shall be specifically associated with the section of ore that becomes directly accessible as a result of the stripping activity.</p> <p>(refer to paragraphs 8 and 11 of DI/2010/1)</p>	<p>The stripping cost asset shall be accounted for as an addition to, or an enhancement of, an existing asset. In other words, the stripping cost asset will become a component of an existing asset.</p> <p>(refer to paragraph 12 of Agenda Paper 17.6)</p>	<p>The AASB considered the use of the term ‘stripping campaign’ unclear. The term has been removed in the revised draft Interpretation.</p> <p>The AASB disagreed with the proposed unit of account on the basis that the attribution of stripping costs to separately identifiable sections of ore is not a relevant or reliable depiction of how most mines operate. The AASB was concerned that the application of the proposed unit of account would be difficult for many mining entities to apply in practice, especially in complex scenarios. The AASB considered the componentising of one large body of ore that is not fully identifiable as an impracticable interpretation of the accounting principles. The AASB questioned whether the application of a specific identification approach may cause practical difficulties.</p>	<p>AASB staff note that ‘stripping campaign’ has been removed in the revised draft Interpretation.</p> <p>However, AASB staff are concerned that in substance the ‘allocation of costs to a specific section of ore body’ still applies, irrespective of the revisions to wording made to the revised draft Interpretation.</p>
2	<p>The benefit of improved access to the ore will qualify for recognition as part of (a component of) an existing asset when:</p>	<p>The Committee has introduced a revised principle for capitalisation, referred to as the recognition principle, which is:</p>	<p>No specific comments raised.</p>	<p>Staff note that the revised draft Interpretation includes a new recognition criterion (i.e. to identify the component of ore body for which access has been</p>

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	<p>(a) an entity controls the benefit created by the stripping activity;</p> <p>(b) the benefit arises as a result of stripping activity, and consequently ‘as a result of past events’; and</p> <p>(c) a future economic benefit will flow to an entity through improved access to the ore that is expected to be economically recoverable in the future. (refer to paragraph 7 of DI/2010/1)</p>	<p>An entity shall recognise production stripping costs as part of an asset if, and only if:</p> <p>(a) it is probable that the future economic benefits associated with the costs will flow to the entity; and</p> <p>(b) the costs can be measured with reliability.</p> <p>In order to recognise the stripping cost asset, the entity must be able to:</p> <p>(a) identify the component of ore body for which access has been improved; and</p> <p>(b) measure the costs relating to the improved access to that component with reliability.</p> <p>If the entity cannot identify the component of the ore body for which access has been improved, or cannot measure the costs relating to the improved access to the component with reliability, then the entity shall</p>		<p>improved) rather than interpreting the recognition criteria within the <i>Conceptual Framework</i>.</p> <p>Furthermore the identification of the component of the ore body for which access has been improved may be difficult to achieve in practice, especially in complex scenarios, such as multi-pit mining operations, where the entire asset is not fully identifiable and the full extent of the asset cannot be reliably determined or where stripping effectively occurs continuously. The consequential effect of this could result in mining entities inappropriately recognising all production stripping costs in profit or loss.</p> <p>AASB staff note in paragraphs BC8 and BC10 of the revised draft Interpretation that the Committee noted that it was imperative that the entity be able to identify the specific component of the ore body for which future access has been</p>

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		recognise these costs in profit or loss. (refer to paragraphs 8 and 11 of Agenda Paper 17.6)		improved. The specifically identified component of ore is crucial to the subsequent depreciation or amortisation of the stripping cost asset, which will take place as the ore is mined. Identifying specific components will require judgement. The Committee thinks, however, that an entity's mine plan will provide the information required, and will allow these judgements to be made with reasonable consistency. AASB staff still note these as issues.
3	This [draft] Interpretation applies to waste removal (stripping costs that are incurred in surface mining activity, during the production phase of the mine. (refer to paragraph 5 of DI/2010/1)	The scope remains the same as in DI/2010/1. (refer to paragraph 6 of Agenda Paper 17.6)	The AASB noted that it is unclear why the accounting for production stripping costs should be different from the accounting for pre-production stripping costs. 'Development phase' and 'production phase' are not defined in IFRSs, and proposing an interpretation that is only applicable to the production phase may create further diversity, because some entities might account for certain waste removal costs in the development phase, whilst others might account for the same costs as part of the	AASB staff note in paragraph BC5 of the revised draft Interpretation that the Committee decided not to include stripping costs incurred during the development phase of the mine, because the Committee became aware that there is not significant diversity in practice in this regard. Even so, AASB staff think that having a draft Interpretation that only applies to the production phase may create diversity and

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			production phase, resulting in two different accounting results. Therefore the AASB questioned whether the scope of DI/2010/1 is too narrow.	therefore recommend that this issue be readdressed with the Committee in a letter.
4	Routine stripping costs, which are not incurred as part of a ‘stripping campaign’, shall be accounted for as a production cost in accordance with IAS 2 <i>Inventories</i> . (refer to paragraph 9 of DI/2010/1)	To the extent that the benefit is realised in the current period in the form of inventory produced, the entity shall account for the costs in accordance with the principle of IAS 2. To the extent that the benefit is the improved access to ore that is to be realised (mined) in a future period, the entity shall recognise these costs as a long-term asset (i.e. a ‘ stripping cost asset ’). (refer to paragraph 9 of Agenda Paper 17.6)	The AASB was concerned that the lack of a clear definition for ‘stripping campaign’ could result in different interpretations of what gets expensed as routine costs and what gets capitalised as a stripping campaign.	As noted in Issue 1, concern about the definition of ‘stripping campaign’ has been removed as a result of the removal of the term. Despite this improvement, AASB staff think the principles in IAS 2 and IAS 16 <i>Property, Plant and Equipment</i> are clear and therefore do not consider it necessary to explicitly note the accounting principles from these two Standards within the revised Draft Interpretation. AASB staff note this as a new issue. AASB staff recommend that this point be raised with the Committee in a letter.
5	Initial measurement The ‘stripping campaign component’ shall be recognised initially at cost, being the accumulation of costs directly	The entity shall measure the stripping cost asset initially at cost, this being the accumulation of costs directly incurred to perform the stripping activity over	No significant comments.	The proposal remains the same. Staff generally do not have any concerns regarding the initial measurement principles.

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	<p>incurred to perform the stripping activity and an allocation of directly attributable costs. (refer to paragraph 14 of DI/2010/1)</p>	<p>the identified component of ore, plus an allocation of directly attributable overhead costs. (refer to paragraph 16 of Agenda Paper 17.6)</p>		
6	<p>Subsequent measurement Subsequent to initial recognition, the ‘stripping campaign component’ shall be carried at its cost less depreciation or amortisation, and less any impairment. It shall be depreciated or amortised over the expected useful life of the section of ore that becomes directly (emphasis added) accessible as a result of the stripping campaign (i.e. specific identification approach). The units of production method shall be applied, unless another method is more appropriate. (refer to paragraphs 16-17 of DI/2010/1)</p>	<p>After initial recognition, the stripping cost asset shall be carried at its cost less depreciation or amortisation, and less any impairment losses. The stripping cost asset shall be depreciated or amortised on a systematic basis, over the expected useful life of the identified component of the ore body that becomes more (emphasis added) accessible as a result of the stripping activity. The units of production method is applied unless another method is more appropriate. (refer to paragraph 20-21 of Agenda Paper 17.6)</p>	<p>The AASB disagreed that a stripping cost asset should be depreciated/amortised over the expected life of the specific section of ore body that becomes accessible, because this approach is not likely to be practicable for many mining operations where the extent of the ore body cannot be reliably measured. The AASB noted that in many cases the section of the ore body that is planned to be extracted may change as a result of operational circumstances. For example, additional ore bodies may be identified that were not part of the mine plan or it may be later determined that a section of ore may not be of a high quality and therefore not feasible to extract. These circumstances will only be determined once the stripping activities are in progress and access to the ore body is obtained, which will impact the</p>	<p>AASB staff notes that the wording ‘directly accessible’ has been replaced with ‘more accessible’, and therefore improved because the stripping activity can result in accessibility to a further part of the ore body, in addition to that ore which is made directly accessible, depending on the geology of the ore distribution. However the Interpretation still requires entities to depreciate/amortise the stripping cost asset based on the useful life of the identified component. Therefore, in substance the proposal remains the same. AASB staff note this as a remaining issue.</p>

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			allocation of stripping costs to particular sections of ore body that become directly accessible as a result of the stripping campaign.	
7	<p>Impairment</p> <p>The ‘stripping campaign component’ shall be subject to impairment testing in accordance with IAS 36 <i>Impairment of Assets</i>. (refer to paragraph 19 of DI/2010/1)</p>	<p>This guidance has been removed. Instead guidance in IAS 36 <i>Impairment of Assets</i> should be applied.</p>	<p>No significant comments.</p>	<p>No issues noted and no action required.</p>
8	<p>Transition</p> <p>On transition, any existing asset balance related to production stripping shall be reclassified as a component of the larger asset to which it relates. Any existing stripping campaign component of an asset that cannot be directly associated with an identifiable section of the ore body and any existing stripping cost liability balances shall be recognised in profit or loss at the beginning of the</p>	<p>Each existing stripping cost asset balance as at the date from which this [draft] Interpretation is applied, which resulted from stripping activity undertaken during the production phase, shall be reclassified as a component of the asset to which the stripping activity relates. If there is no identifiable component of the ore body to which that stripping cost asset can be directly associated, it shall be recognised in opening retained</p>	<p>The AASB agreed with the proposed transitional provisions in DI/2010/1.</p>	<p>The proposal remains the same. No action required.</p>

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	earliest period presented. (refer to paragraph 22 of DI/2010/1)	earnings at the beginning of the earliest period presented. (refer to paragraphs A3 and 4 of Agenda Paper 17.6)		

Note: AASB staff note that the paragraphs 17-19 of the revised draft interpretation of IASB D1/2010/1 (IASB staff paper) consider a ‘**residual cost approach**’ for allocating production stripping costs. This is not addressed in this paper because the Committee tentatively agreed at its May 2011 meeting not to prescribe any specific cost allocation approach for the measurement of the stripping cost asset. Therefore these proposals in the revised draft Interpretation are likely to be revised for the next Committee meeting.