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International Accounting Standards Board
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Re: *Discussion Paper Extractive Activities*

Dear Sir/Madam

We are pleased to provide our comments on the IASB Discussion Paper *Extractive Activities* ('the DP').

The OIC's main comments can be summarized as follows:

1. We believe that the DP does not provide a clear rationale for developing a separate accounting model for extractive activities. However, we think that the IASB should provide guidance for applying IFRSs to extractive activities for the following reasons: (i) diversity in practices across jurisdictions, (ii) difficulties that these entities face in applying current IFRSs.
2. We believe that a precise generally accepted definition of reserves and resources is crucial for this project. In order to increase the comparability, all the entities belonging to minerals and oil and gas industries should refer to the same definition of reserves and resources.
3. We think that the definition of the assets relating to extractive activities shall be based on the current Framework definition. Consequently we do not support the type of impairment test proposed in the DP (i.e. an asset exists until proven otherwise). In our view the IASB should first define the unit of account in a wider context (i.e. Framework) and then it should address the unit of account for extractive activities and consequently recognition and impairment requirements.

Our replies to IASB's questions are as follows.

Question 1 – Scope of extractive activities
In Chapter 1 the project team proposes that the scope of an extractive activities IFRS should include only upstream activities for minerals, oil and natural gas. Do you agree? Are there other similar activities that should also fall within the scope of an IFRS for extractive activities? If so, please explain what other activities should be included within its scope and why.

We believe that the IASB should develop application guidance on the upstream activities for minerals, oil and natural gas. Furthermore, we think there is a need of industry-specific guidance on the issues that are not clearly addressed by current IFRSs such as: accounting for production sharing agreements, farm-in and farm-out arrangements, and exchanges of licenses or information resulting from exploration activities.

Question 2 – Approach
Also in Chapter 1, the project team proposes that there should be a single accounting and disclosure model that applies to extractive activities in both the minerals industry and the oil and gas industry. Do you agree? If not, what requirements should be different for each industry and what is your justification for differentiating between the two industries?

As already mentioned we think that the DP does not provide a clear rationale for developing a separate accounting model for extractive activities and therefore we kindly suggest to IASB to clarify why it is necessary a separate accounting model for these activities. However, we agree that there is a need for appropriate disclosure of extractive activities.

Question 3 – Definitions of minerals and oil and gas reserves and resources
In Chapter 2 the project team proposes that the mineral reserve and resource definitions established by the Committee for Mineral Reserves International Reporting Standards and the oil and gas reserve and resource definitions established by the Society of Petroleum Engineers (in conjunction with other industry bodies) should be used in an IFRS for extractive activities. Do you agree? If not, how should minerals or oil and gas reserves and resources be defined for an IFRS?

We do not believe that the most important issue is the choice between the two alternatives proposed in the DP (i.e. to develop a new set of definitions of reserves and resources or to use an existing set of definitions). We believe that, in any case, the final outcome of this project should be a precise generally accepted definition of reserves and resources. Only in this way, the IASB can increase the comparability among all the entities belonging to minerals and oil and gas industries. To this object in view the IASB cannot ignore the SEC definitions and the other existing definitions.

Question 4 – Minerals or oil and gas asset recognition model - recognition
In Chapter 3 the project team proposes that legal rights, such as exploration rights or extraction rights, should form the basis of an asset referred to as a 'minerals or oil and gas property'. The property is recognised when the legal rights are acquired. Information obtained from subsequent exploration and evaluation activities and development works undertaken to access the minerals or oil and gas deposit would each be treated as enhancements of the legal rights. Do you agree with this analysis for the recognition of a minerals or oil and gas property? If not, what assets should be recognised and when should they be recognised initially?

We disagree with the proposed asset recognition model for the following reasons: (i) the asset definition is not consistent with the Framework, (ii) the separate recognition criterion is not justified, (iii) we do not support the removal of the probability criterion from the recognition requirements, (iv) we believe that the "asset continuum" or "asset enhancement" recognition model is not consistent with the accounting for other similar activities such as research and development.

Question 5 – Minerals or oil and gas asset recognition model - unit of account selection
Chapter 3 also explains that selecting the unit of account for a minerals or oil and gas property involves identifying the geographical boundaries of the unit of account and the items that should be combined with other items and recognised as a single asset.
The project team's view is that the geographical boundary of the unit of account would be defined initially on the basis of the exploration rights held. As exploration, evaluation and development activities take place, the unit of account would contract progressively until it becomes no greater than a single area, or group of contiguous areas, for which the legal rights are held and which is managed separately and would be expected to generate largely independent cash flows.
The project team's view is that the components approach in IAS 16 Property, Plant and Equipment would apply to determine the items that should be accounted for as a single asset.
Do you agree with this being the basis for selecting the unit of account of a minerals or oil and gas property? If not, what should be the unit of account and why?

We understand that the unit of account definition is crucial for this project, however we believe that the unit of account should be defined in the Framework project.

Question 6 – Minerals or oil and gas asset measurement model
Chapter 4 identifies current value (such as fair value) and historical cost as potential measurement bases for minerals and oil and gas properties. The research found that, in general, users think that measuring these assets at either historical cost or current value would provide only limited relevant information. The project team's view is that these assets should be measured at historical cost but that detailed disclosure about the entity's minerals or oil and gas properties should be provided to enhance the relevance of the financial statements (see Chapters 5 and 6).
In your view, what measurement basis should be used for minerals and oil and gas properties and why? This could include measurement bases that were not considered in the discussion paper. In your response, please explain how this measurement basis would satisfy the qualitative characteristics of useful financial information.

We agree that minerals or oil and gas assets should be measured at historical cost, because under current IFRSs, most non-financial assets are normally measured at historical cost.

Question 7 – Testing exploration properties for impairment
Chapter 4 also considers various alternatives for testing exploration properties for impairment. The project team's view is that exploration properties should not be tested for impairment in accordance with IAS 36 Impairment of Assets. Instead, the project team recommends that an exploration property should be written down to its recoverable amount in those cases where management has enough information to make this determination. Because this information is not likely to be available for most exploration properties while exploration and evaluation activities are continuing, the project team recommends that, for those exploration properties, management should:
(a) write down an exploration property only when, in its judgement, there is a high likelihood that the carrying amount will not be recoverable in full; and
(b) apply a separate set of indicators to assess whether its exploration properties can continue to be recognised as assets.

Do you agree with the project team's recommendations on impairment? If not, what type of impairment test do you think should apply to exploration properties?

We strongly disagree with the proposed presumption "an asset exists until it can be proved otherwise", because this presumption is not consistent with the Framework definition of an asset and could create a dangerous precedent that could have consequences beyond the extractive activities.

Question 8 – Disclosure objectives

In Chapter 5 the project team proposes that the disclosure objectives for extractive activities are to enable users of financial reports to evaluate:
(a) the value attributable to an entity's minerals or oil and gas properties;
(b) the contribution of those assets to current period financial performance; and
(c) the nature and extent of risks and uncertainties associated with those assets.
Do you agree with those objectives for disclosure? If not, what should be the disclosure objectives for an IFRS for extractive activities and why?

We support the disclosure objectives, however we believe that current value or fair value disclosures are costly and they do not provide useful information.

Question 9 – Types of disclosure that would meet the disclosure objectives

Also in Chapter 5, the project team proposes that the types of information that should be disclosed include:
(a) quantities of proved reserves and proved plus probable reserves, with the disclosure of reserve quantities presented separately by commodity and by material geographical areas;
(b) the main assumptions used in estimating reserves quantities, and a sensitivity analysis;
(c) a reconciliation of changes in the estimate of reserves quantities from year to year;
(d) a current value measurement that corresponds to reserves quantities disclosed with a reconciliation of changes in the current value measurement from year to year;
(e) separate identification of production revenues by commodity; and
(f) separate identification of the exploration, development and production cash flows for the current period and as a time series over a defined period (such as five years).
Would disclosure of this information be relevant and sufficient for users? Are there any other types of information that should be disclosed? Should this information be required to be disclosed as part of a complete set of financial statements?

We believe that the proposed disclosure is too voluminous and costly, especially the disclosure about probable and possible reserves.
As already mentioned we do not support the current value or fair value disclosures.
We agree that the quantity disclosures and the main assumptions used in estimating reserves quantities can provide useful information to users. However we think that a sensitivity analysis is not necessary because does not provide useful information and could be costly.
We think that an indication of when the production will begin can be useful.

Question 10 – Publish What You Pay disclosure proposals

Chapter 6 discusses the disclosure proposals put forward by the Publish What You Pay coalition of non-governmental organisations. The project team's research found that the disclosure of payments made to governments provides information that would be of use to capital providers in making their investment and lending decisions. It also found that providing information on some categories of payments to governments might be difficult (and costly) for some entities, depending on the type of payment and their internal information systems.

In your view, is a requirement to disclose, in the notes to the financial statements, the payments made by an entity to governments on a country-by-country basis justifiable on cost-benefit grounds? In your response, please identify the benefits and the costs associated with the disclosure of payments to governments on a country-by-country basis.

Whilst we understand the motivation of the Publish What You Pay (PWYP) coalition in putting forward its list of proposed disclosures, we think that the PWYP disclosures do not provide useful information to capital providers. These disclosures should be provided in financial statements different from IFRS financial statements. If the IASB believes that these disclosures are useful, all the entities should provide these disclosures and not solely the entities belonging to minerals and oil and gas industries.

If you have any queries concerning our comments, please do not hesitate to contact us.

Yours faithfully,
Angelo Casò
(Chairman)