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Organización Internacional de Comisiones de Valores
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16 April 2004

Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear David

The International Organization of Securities Commissions (IOSCO) Standing Committee No. 1 on Multinational Disclosure and Accounting (SC1) thanks you for the opportunity to provide our thoughts regarding Exposure Draft 6, ***Exploration for and Evaluation of Mineral Resources*** (ED 6 or the [draft] IFRS). IOSCO is committed to promoting the integrity of international markets through promotion of high quality accounting standards, including rigorous application and enforcement.[1] Members of SC1 seek to further IOSCO's mission through thoughtful consideration of accounting and disclosure concerns and pursuit of improved transparency of global financial reporting. The comments we have provided herein reflect a general consensus among the members of SC1 and are not intended to include all the comments that might be provided by individual members on behalf of their respective jurisdictions.

SC 1 understands the efforts that the Board has taken to balance the need for uniform accounting standards with the cost of implementing a temporary standard. With this context in mind, SC1 supports, as an interim measure, the Board's decision to focus its efforts on a relatively short list of accounting and disclosure improvements for certain extractive activities. Therefore, we have provided responses to the Board's specific questions first, followed by additional comments regarding the "Reasons for issuing the [draft] IFRS" and "Measurement after recognition." In addition, we have provided some recommendations and areas of focus for Phase II of the project.

[1] See IOSCO website, www.iosco.org

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SC1 Comments to Specific Questions

Question 1: Definitions and Additional Guidance
The proposed IFRS includes definitions of exploration for and evaluation of mineral resources, exploration and evaluation expenditures, exploration and evaluation assets and a cash-generating unit for exploration and evaluation assets. The draft IFRS identifies expenditures that are excluded from the proposed definition of exploration and evaluation assets. Additional guidance is proposed in paragraph 7 to assist in identifying exploration and evaluation expenditures that are included in the definition of an exploration and evaluation asset (proposed paragraphs 7 and 8, Appendix A and paragraphs BC12-BC14 of the Basis for Conclusions).

Response
We appreciate the Board's efforts in paragraphs 7 and 8, as well as Appendix A, to provide additional guidance regarding the definitions of exploration and evaluation expenditures and assets. Such guidance will help preparers understand the Board's intent with regards to the initial measurement and recognition of such items. We do, however, recommend that the Board consider whether the terms contained in Appendix A and the guidance contained in paragraphs 4 through 8 can be expanded to help achieve this goal. For example, the definitions of the terms "evaluating technical feasibility and commercial viability of extracting a mineral resource" (paragraph 7(f)) and "administrative and other general overhead costs" (paragraph 8(b)) appear to be broad and could result in multiple interpretations.

Question 2: Method of Accounting for Exploration and Evaluation of Mineral Resources
(a) Paragraphs 10-12 of IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors specify sources of authoritative requirements and guidance an entity should consider in developing an accounting policy for an item if no IFRS applies specifically to that item. The proposals in the draft IFRS would exempt an entity from considering the sources in paragraphs 11 and 12 when assessing its existing accounting policies for exploration and evaluation expenditures by permitting an alternative treatment for the recognition and measurement of exploration and evaluation assets. In particular, the draft IFRS would permit an entity to continue to account for exploration and evaluation assets in accordance with the accounting policies applied in its most recent annual financial statements.

(b) The Exposure Draft proposes that an entity would continue to use its existing accounting policies in subsequent periods unless and until the entity changes its accounting policies in accordance with IAS 8 or the IASB issues new or revised Standards that encompass such activities (proposed paragraph 4 and paragraphs BC8-BC11 of the Basis for Conclusions).

Are these proposals appropriate? If not, why not?

Response
Question 2(a): SC1 understands the impracticalities of completing a comprehensive IFRS for the exploration and evaluation of mineral resources in advance of 1 January 2005. Therefore, as an interim measure, we concur with the Board's decision to allow the continued use of an entity's existing accounting policies unless and until the entity changes its accounting policies in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors.* However, in an effort to promote comparability across entities, it is our hope that entities applying the recognition provisions of this [draft] IFRS and those, as permitted by paragraph 4, continuing their existing policies would be limited to recognizing as assets those expenditures that relate to similar types of activities.

ED 6 requires that entities electing to continue their existing accounting policies amend those policies for the requirements noted in paragraph 8. Our concern is that without a similar requirement pertaining to paragraph 7, little progress will be made in closing the gap on current diversity in practice for asset recognition. To illustrate, paragraphs 4 and 5 imply that an entity may recognize as an exploration and evaluation asset expenditures relating to activities not mentioned in paragraph 7(a-f), as long as such recognition is permitted by its existing policies and the requirements of paragraph 8. We recommend that the Board reconsider its intentions regarding this matter and recommend that paragraph 4 and the second sentence of paragraph 5 be amended to also include a reference to paragraph 7.

Question 2(b): Subject to our response to Question 2(a), we support the Board's proposal.

Question 3: Cash-Generating Units for Exploration and Evaluation Assets
[Draft] IAS 36 requires entities to test non-current assets for impairment. The draft IFRS would permit an entity that has recognised exploration and evaluation assets to test them for impairment on the basis of a 'cash-generating unit for exploration and evaluation assets' rather than the cash-generating unit that might otherwise be required by [draft] IAS 36. This cash-generating unit for exploration and evaluation assets is used only to test for impairment exploration and evaluation assets recognised under proposed paragraph 4 (see proposed paragraphs 12 and 14 and paragraphs BC15-BC23 of the Basis for Conclusions).

Are the proposals appropriate? If not, why not? If you disagree with the proposal that exploration and evaluation assets should be subject to an impairment test under [draft] IAS 36, what criteria should be used to assess the recoverability of the carrying amount of exploration and evaluation assets?

Response
We agree that all non-current assets should be tested for impairment annually. However, based on our current understanding of ED 6, we do not support the use of a modified impairment model that utilizes a newly defined "cash-generating unit for exploration and evaluation assets".

Although we understand the Board's reasons for expanding the definition of cash generating units, we are concerned about using a cash generating unit model uniquely defined for 'exploration and evaluation assets' (especially one that is broader than the definition of cash generating units provided to other industries) for the following reasons:

- In order to promote consistent and comparative financial reporting, we do not believe the activities of entities participating in extractive activities should be treated in a different manner than business activities of other entities that follow the impairment testing guidance in IAS 36, *Impairment of Assets* (IAS 36);
- Entities that do not have exploration and evaluation activities may seek to analogize to the [draft] IFRS and apply a similar definition of cash generating units;
- The proposed model may inappropriately permit continued recognition of assets that will not provide future benefits to the entity. This may arise because the impairment testing model proposed in the [draft] IFRS standard may result in grouping unrelated proven assets with assets consisting of costs incurred in failed exploration activities, which are being tested for impairment. Such groupings of asset pools may prevent a valid recoverability analysis of certain impaired assets;
- It may prove particularly difficult to propose eliminating this temporary ED 6 model during Phase II, especially if the model becomes accepted industry practice; and finally,
- We do not believe that the IAS 36 definition of a 'cash-generating unit' would result in "inappropriate recognition of impairment losses." We do acknowledge that certain entities within extractive industries may have relatively smaller business units comprising their cash generating units, and consequently, may recognize more frequent impairment losses than entities with larger cash generating units. However, this result is not unique to the accounting for exploration and evaluation assets.

We believe that it is preferable for this IFRS to foster consistent application of IAS 36 for all entities, because such application will produce results that are comparable across industries, as well as between enterprises with mineral exploration and evaluation activities. Therefore, we recommend that the Board eliminate the option allowing an entity to assess and measure impairments based on cash generating units for exploration and evaluation assets.

Question 4: Identifying Exploration and Evaluation Assets That May be Impaired
The draft IFRS identifies indicators of impairment for exploration and evaluation assets. These indicators would be among the external and internal sources of information in paragraphs 9-13 of [draft] IAS 36 that an entity would consider when identifying whether such assets might be impaired (paragraph 13 and paragraphs BC24-BC26 of the Basis for Conclusions).

Are these indicators of impairment for exploration and evaluation assets appropriate? If not, why not? If you are of the view that additional or different indicators should be used in assessing whether such assets might be impaired, what indicators should be used and why?

Response
SC1 supports the Board's inclusion of a reference to IAS 36 as well as the additional guidance in paragraph 13 that identifies circumstances when exploration and evaluation assets may have become impaired. However, we do recommend that further clarification be provided in paragraph 13 and/or in Appendix A as to the intended meaning of the term "in the near future," as it is used in this [draft] IFRS and whether a similar application would apply if and when the term is used in other IFRS.

Question 5: Disclosure
To enhance comparability, the draft IFRS proposes to require entities to disclose information that identifies and explains the amounts in its financial statements that arise from the exploration for and evaluation of mineral resources (proposed paragraphs 15 and 16 and paragraphs BC32-BC34 of the Basis for Conclusions).

Are the proposed disclosures appropriate? If not, why not? Should additional disclosures be required? If so, what are they and why should they be required?

Response
SC1 agrees that improved disclosure should be an immediate focus of attention and therefore fully supports the inclusion of ED 6's paragraphs 15 and 16. We also feel the disclosure requirements of ED 6 could be further strengthened by requiring:

- A reconciliation of the exploration and evaluation asset(s)' carrying amount at the beginning and end of the reporting period, similar to the requirements of paragraph 118(e) of IAS 38, *Intangible Assets*;
- Disclosures consistent with those required by paragraphs 126-137 of IAS 36, with particular emphasis on the qualitative and quantitative disclosures of the cash generating units and any impairment losses as outlined in paragraph 130(d)(i-iii); and
- A complete and transparent analysis of exploration and evaluation expenditures, with particular emphasis on critical assumptions and estimates used in formulating a policy for capitalizing assets, including assets recorded as reserves.

Other Items Regarding ED 6

Paragraph IN 2: Reasons for Issuing the [draft] IFRS
Therefore, the Board wishes to provide guidance on the treatment of exploration and evaluation expenditures that will enhance comparability between entities while avoiding unnecessary disruption to the application of those treatments, pending a more complete consideration of the accounting issues involved.

Response
We recommend that the Board eliminate its reference to "...while avoiding unnecessary disruption to the application of those treatments, pending a more complete consideration of the accounting issues involved." The phrase appears to set an expectation that changes proposed by this [draft] IFRS are inconsequential and therefore should not result in any significant changes. While that may be true for many entities, it is not universally certain. For example, entities that have not previously applied impairment and recognition requirements similar to those required by paragraph 12 may, in fact, experience significant changes. Removing this phrase would mitigate the risk of a misconception diminishing the Board's intended convictions and thereby undermining the primary objective to "enhance comparability."

Paragraph 10: Measurement After Recognition
After recognition, an entity shall apply either the cost model or the revaluation model (see IAS 16 Property Plant and Equipment and [draft] IAS 38 Intangible Assets) to its exploration and evaluation assets.

Response
We are concerned that this paragraph could be interpreted to allow adoption of a revaluation model in the natural resource industry when, to the best of our knowledge, such an approach is not currently considered acceptable in any developed capital market. We believe this would be an unfortunate and unnecessary result from what the Board considers an interim standard designed to achieve limited improvements to current practices. We note that paragraph BC15 in the Basis for Conclusions suggests at least some Board members appear to share our concern.

On the basis of the definition of "exploration and evaluation assets" contained in ED 6, we are unclear as to whether such assets should be viewed as property, plant and equipment or as intangible assets. We are concerned that entities could view exploration and evaluation assets as representing a measurement of mineral reserves that, once established, could be remeasured at fair value in accordance with IAS 16. This could result in entities recognizing substantial increases in stockholder's equity in periods in which they identify extensive reserves. We believe it would be unwise to contemplate permitting such a significant shift from current cost based accounting practices until the comprehensive study envisaged as part of Phase II has been completed. Accordingly, we recommend that the Board amend paragraph 10 to preclude entities from using it as support for revaluing exploration and evaluation assets to reflect the fair value of underlying mineral reserves. We believe this would be consistent with the Board's goal of providing "...guidance on the treatment of exploration and evaluation expenditures that will enhance comparability between entities..." while not prejudging the Board's position on fundamental conceptual issues to be examined comprehensively in Phase II of the project.

Mineral reserve recognition and measurement methodology is a broad conceptual issue that will require the involvement of professional geologists who are knowledgeable about both the mining and oil and gas industries to establish appropriate standards for determination of reserve data. This is particularly important where such reserve data has direct recognition and measurement implications in the financial statements.

Comments for Phase II of Project
We are concerned about a variety of issues impacting the preparation and distribution of timely, relevant, comparable and meaningful financial data to investors. We have therefore developed a preliminary listing of objectives we believe warrant the Board's consideration during the next phase of this project. Although we refer to the next phase of this project as "Phase II" we acknowledge and suggest that in order to develop a "comprehensive basis of accounting" it may be necessary to break the next phase down into a series of smaller projects addressing similar items.

During Phase II we encourage the Board to consider comments raised following the issuance of the November 2000 Extractive Industries Issues paper with particular emphasis on the following:

- The need for a comprehensive project (or series of smaller projects) that includes *all* extractive activities. The current diversity of accounting practice and the lack of a "best model" provides the Board the opportunity to take a leadership role in the development of a new single comprehensive set of accounting principles and related disclosures for all upstream extractive activities;
- The need to develop a robust set of principles for capitalization of costs, particularly those relating to exploration activities; and
- Whether the various remaining scope exceptions for extractive industries that are contained in other IFRSs are still appropriate.

If you have any questions or need additional information on the recommendations and comments that we have provided, please contact me at 1.202.942.4400.

Sincerely,

Scott Taub

Scott Taub
Chair
IOSCO Standing Committee No. 1