



Our Ref.: C/FRSC

**Sent electronically through the IASB Website ([www.iasb.org](http://www.iasb.org))**

3 August 2010

International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH  
United Kingdom

Dear Sirs,

**[IASB Discussion Paper on \*Extractive Activities\*](#)**

The Hong Kong Institute of Certified Public Accountants is the only body authorised by law to promulgate financial reporting, auditing and ethical standards for professional accountants in Hong Kong. We welcome the opportunity to provide you with our comments on the captioned Discussion Paper.

We note that the Discussion Paper represents the preliminary views and recommendations of a project team and comments received on the Discussion Paper will assist the IASB in deciding whether a new accounting standard should be developed for extractive activities.

In general, we support the objective of developing guidance for companies operating in extractive industries given there is diversity in accounting practices across jurisdictions and within the industries.

We support the use of historical cost as the measurement basis for extractive activities discussed in the Discussion Paper. We also support the development of a set of disclosure requirements for extractive activities. However, we do not support the development of an accounting standard that is specific to extractive activities; rather we believe that the IASB should develop a set of principles-based standards in accordance with the Framework to meet the needs of all users. It is noted that the recognition proposals contained within the Discussion Paper do not appear to be consistent with the Framework. In addition, we are not convinced that the proposal to apply impairment rules other than those within IAS 36 has been sufficiently justified.

Our comments are discussed further below.

**Asset recognition**

It is noted that paragraph 3.11 of the Discussion Paper states that *"the asset recognition criteria are under review as part of the IASB/FASB conceptual framework project. Furthermore, in IFRS 3 Business Combinations and as part of the redeliberations on IAS 37 Provisions. Contingent Liabilities and Contingent Assets, the IASB has decided to include probability assessments in the measurement of an asset or liability rather than in determining whether the asset or liability should be recognized. Consequently, both the existing asset recognition criteria and the implications of*



*removing probability from asset recognition are considered in this analysis for completeness."*

First, we are concerned that asset recognition proposed in the Discussion Paper is not based on the definition of an asset under the current Conceptual Framework. We believe any change in principles including the definition and criteria for recognition of assets should be included in the project on the review of the Conceptual Framework.

Second, we would note that the proposals to recognize "additional costs" subsequent to the acquisition of exploration rights as an asset is not consistent with the recognition criteria of an asset under the current Conceptual Framework. The Discussion Paper argues that the subsequent costs are "integral and inseparable" from the legal rights and should be recognized as assets. However, it did not explain clearly how these subsequent costs can be treated as "enhancements" to the exploration rights to justify being recognized as assets.

In addition, the proposal for the "additional costs" is inconsistent with the current principles and accounting treatment for research and development costs ("R&D costs"). Currently, R&D costs are expensed as incurred and will only be capitalized if the product or project is determined to be technically and commercially feasible and the entity has sufficient resources and the intention to complete the development. We are concerned that the proposal may set a precedent and in future different models may be developed for different industries.

Therefore, we suggest that the IASB should express clearly the rationale why costs subsequent to the acquisition of exploration rights should be treated as "enhancements" to the rights and how these costs meet the recognition criteria of an asset under the Conceptual Framework.

### **Unit of account**

We note in paragraph 3.40 of the Discussion Paper that "The current IASB/FASB conceptual framework project has identified unit of account as an important issue, but this has not yet been addressed." We believe that the IASB should ensure the "unit of account" issue is resolved in the Conceptual Framework Project so that any proposed new accounting standard on extractive activities, as it relates to "unit of account", will be consistent with the Conceptual Framework.

### **Impairment of exploration rights and assets**

The Discussion Paper proposes that exploration assets should be written down only when there is a high likelihood that the carrying amount will not be recoverable in full.

The Discussion Paper argues that testing exploration property using IAS 36 *Impairment of Assets* may not be appropriate for recognition of impairment on exploration property. Paragraph 4.57 of the Discussion Paper tries to explain the need for a different approach and states that "there is no relationship between the cost of exploration activities and what is gained from that exploration" and "until sufficient information is available to evaluate the exploration results and reach a conclusion on whether economically recoverable quantities of mineral or oil and gas have been found, it is not possible to make any (reliable) judgments that the carrying amount of an



exploration property (ie the cost of the exploration rights and any subsequent exploration and evaluation activities) would be less than its recoverable amount."

The proposal appears to suggest that exploration property can continue to be carried as an asset and will not normally be impaired. We believe that this will result in the deferral of exploration expenses indefinitely on the presumption that commercially extractable resources will be found which may not be the case. We believe that as exploration rights normally have a specified time period during which exploration is allowed, exploration rights including "enhancements" should normally be amortised over the period of the rights. In the event that commercially extractable resources are discovered, the IASB may wish to further study and consider whether the cost of exploration rights may be transferred and be included as part of extractive assets if the exploration costs are expected to be recoverable through the sale of the extracted resource. This would be consistent with the current principle and accounting treatment for R&D costs.

If you have any questions on our comments, please do not hesitate to contact me at [ong@hki CPA.org.hk](mailto:ong@hki CPA.org.hk).

Yours faithfully,

Steve Ong, FCPA, FCA  
Director, Standard Setting Department

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