Project	**Extractive Activities**
Topic	**Accounting for stripping costs in the production phase – draft interpretation**

IFRIC [X] ACCOUNTING FOR STRIPPING COSTS IN THE PRODUCTION PHASE

References

Framework

IAS 16 *Property, Plant and Equipment*

IAS 38 *Intangible Assets*

IAS 1 *Presentation of Financial Statements*

Background

1. In surface mining operations, entities may find it necessary to remove mine waste materials (overburden) to gain access to mineral deposits, in order to extract minerals from that ore. This waste removal activity is known as 'stripping', and the costs incurred as a result of the activity are known as 'stripping costs'.

2. During the development phase of the mine (before production begins), it is generally accepted in practice that stripping costs are capitalised as part of the depreciable cost of building, developing and constructing the mine. Those capitalised costs are typically amortised over the life of the mine using the units of production method, once production begins.

A mining entity may continue to remove overburden and to incur stripping costs during the production phase of the mine. Stripping costs in the production phase may be part of the routine costs incurred during production. Production stripping costs may also be incurred as part of a concentrated and systematic effort to gain access to ore, often referred to in the mine industry as a 'stripping campaign'.

Scope

3. This [draft] Interpretation applies to waste removal costs that are incurred in surface mining activity, during the production phase of the mine.

Issue

4. The [draft] Interpretation addresses the following issues:

   (a) Is the definition of an asset met?

   (b) When shall the asset be recognised?

   (c) How shall the asset be initially measured?

   (d) How shall the asset be subsequently measured?

Consensus

Is the definition of an asset met?

5. An entity creates a benefit by undertaking stripping activity, which is of improved access to the ore to be mined. An entity shall assess whether the benefit meets the definition of an asset set out in the *Framework*. Paragraph 49(a) states that 'an asset is a resource controlled by an entity as a result of past events and from which future economic benefits are expected to flow to the entity.' The benefit of improved access to the ore will qualify as an asset when:

   (a) An entity controls the benefit created by the stripping activity, by either owning the land which it is mining, or owning the rights to mine the land;

(b) The benefit arises as a result of stripping activity, therefore ‘as a result of past events’, and

(c) A future economic benefit will flow to an entity through the reduced cost of accessing reserves that are expected to be economically recoverable in the future.

6. Where the improved access benefit meets the definition of an asset, it should be accounted for as an addition to or enhancement of an existing asset that has benefited from the stripping activity. In other words, this benefit will become a component of an existing asset, and is referred to in this [draft] Interpretation as the ‘stripping campaign component’.

7. An entity shall classify the stripping campaign component as tangible or intangible according to the nature of the existing asset that it is a part of.

8. Where the improved access benefit does not meet the definition of an asset, then the stripping costs should be accounted for as a cost of current production. This would be the case, for example, where stripping activity is routinely undertaken to access ore which will be mined in the current period.

When shall the asset be initially recognised?

9. The stripping campaign component shall be recognised as the stripping activity takes place.

10. The stripping campaign component shall be specifically associated with the section of ore benefiting from the stripping activity.

How shall the asset be initially measured?

11. The stripping campaign component shall be initially measured at cost; that is, the accumulation of costs incurred to perform the stripping activity.

12. The cost shall be comprised of the following:

(a) Costs directly attributable to the stripping activity, such as haulage, waste transportation, materials consumed, costs of machinery employed, labour and fuel, and

(b) An allocation of indirect costs attributable to the stripping activity, such as supervisors' salaries.

13. Recognition of costs in the stripping campaign component will cease when the stripping campaign ends. The stripping campaign will end when the entity has completed the waste removal activity necessary to access the ore to which the campaign is associated.

14. Some ancillary activities may occur in connection with preparing the mine for production, but are not necessary for the stripping campaign to continue as planned, for example, building an access road in the area in which the stripping campaign is taking place. The costs associated with these operations shall not be included in the cost of the stripping campaign component. These costs shall be recognised as assets or expense in accordance with other IFRSs.

How shall the asset be subsequently measured?

15. After initial recognition, the stripping campaign component shall be carried at its cost less amounts amortised and less any impairment charges.

16. The stripping campaign component shall be amortised in a rational and systematic manner, over the reserves that directly benefit from the stripping campaign. In the mining industry, the units of production method is generally the appropriate method.

17. The reserves used to amortise the stripping campaign component will normally differ from those used to amortise the mine and related life-of-mine assets, as the stripping campaign will normally only relate to a portion of the total reserves.

18. Once the extraction of the ore associated with the stripping campaign component ceases, any remaining balance on the component shall be fully amortised at that time.

19. The amortisation charge shall be added to the costs of current production.

20. An entity shall assess at the end of each reporting period whether there is any indication that the stripping campaign asset may be impaired, in accordance with IAS 36 *Impairment of Assets.*

Effective date

21. An entity shall apply this [draft] Interpretation for annual periods beginning on or after [date to be set at three months after the [draft] Interpretation is finalised]. If an entity applies this [draft] Interpretation for a period beginning before [date to be set at three months after the draft Interpretation is finalised], it shall disclose that fact.

Transition

22. An entity shall apply this [draft] Interpretation prospectively to stripping campaigns beginning on or after [date to be set 3 months after the draft Interpretation is finalised].

Basis for Conclusions on IFRIC Interpretation [X] *Accounting for Stripping Costs in the Production Phase*

This Basis for Conclusions accompanies, but is not part of, IFRIC [X].

Introduction

BC1 This Basis for Conclusions summarises the Committee's considerations in reaching its consensus. Individual Committee members gave greater weight to some factors than to others.

Background

BC2 The Committee received a request to issue guidance on the accounting for waste removal (stripping) costs incurred in the production phase of a mine. Accounting for production stripping costs is challenging because such costs incurred may benefit both future and current period production, and there is no specific guidance in IFRS addressing this issue.

BC3 Consequently, there is diversity in practice in accounting for production stripping costs – some entities expense production stripping costs as a cost of production, and some entities capitalise some or all production stripping costs, based on a life-of-mine ratio calculation, or similar basis. The Committee decided to develop a draft Interpretation in response to that divergence in practice.

Scope

BC4 This draft Interpretation proposes guidance on the accounting for stripping costs incurred in surface mining activity. In developing the draft Interpretation, the Committee decided to exclude oil and natural gas extraction and underground mining activities. The Committee understood that stripping activity occurs predominately in surface mining activities, and decided to confine the scope to these circumstances.

BC5 The Committee decided to exclude stripping costs incurred during the development phase of the mine, since the Committee became aware that there is not significant diversity in practice in this regard.

Consensus

Is the definition of an asset met?

BC6 The Committee decided that, by incurring costs to remove waste, an entity creates a benefit; that is, of improved access to the mineral ore body. An ore body that has been cleared of waste is more valuable to an entity than one where less or no waste has been removed. Access to reserves therefore becomes easier and less costly.

BC7 [Where the access benefit created by the stripping activity meets the definition of an asset, the Committee decided that the benefit created was more akin to an addition to or improvement of an existing asset, than an asset in its own right. It could be argued that stripping activity increases the value to the entity of the *land* under which the ore lies. This is consistent with the proposal in the Extractive Activities Discussion Paper, on how to account for mineral (and oil and gas) properties – as information is gained about the deposits through exploration and evaluation activities, and development work is undertaken, the mineral (or oil and gas) property is considered to be enhanced.]

BC8 [It could also be argued that stripping activity increases the value of the *ore* itself. Conceptually, whichever alternative is most applicable for the entity, an existing asset (land or ore) increases in value as a result of the stripping activity, rather than an entirely new, separate asset being created.]

BC9 [The Committee decided that it is not necessary for the Interpretation to define whether the benefit created by stripping activity is tangible or intangible in nature – this will follow the nature of the underlying asset to which the benefit relates.]

BC10 [The Committee decided that there is a difference between stripping activity that is 'routine', and that which takes the form of a specific and directed effort to gain access to a particular section of the ore.]

BC11 [Most surface mining operations will undertake routine stripping activity continuously just ahead of, or around, the ore currently being mined, to ensure that production continues without delay. The benefit created by routine stripping is unlikely to require recognition as an asset, since the ore being uncovered as a result is likely to be mined in the current period, and no potential future benefit to the entity exists. The costs of routine stripping should be accounted for as costs of current period production, similar to labour or fuel costs, for example.]

BC12 The Interpretation refers to a 'stripping campaign', in order to distinguish a significant and focused stripping effort from routine stripping. Such stripping campaigns are typically known about and planned for some time in advance of the event actually occurring. By nature, they involve a significant 'push back' or removal of waste material in order to widen or deepen an existing pit, or create a new, satellite pit. This activity is likely to have an enduring benefit – the area that has been accessed as a result may be mined over a number of future periods – and consequently, the definition of an asset will usually be met.

BC13 [There will be some circumstances when routine stripping, as distinct from a stripping campaign, may create a benefit that will be realised in a future period. The may arise, for example, when stripping is performed continuously as part of routine operations. The Committee decided that an entity would not necessarily need to capitalise the costs of such routine stripping. The entity would need to consider the significance and materiality of that benefit in determining whether capitalizing the costs of the routine stripping activity was necessary.]

When shall the asset be initially recognised?

BC14 The stripping campaign component is an accumulation of costs incurred, as a result of stripping activity, that meet asset recognition criteria (paragraph 49(a) of the *Framework)*. Therefore, the component is recognised as the stripping activity takes place.

BC15 At the same time as the component is recognised, it is important that the entity links the costs incurred with the ore that will be accessed through the stripping campaign. This specific identification approach links the stripping activity to the benefit created and is key to the subsequent amortisation of the asset, which will take place as the ore is mined.

How shall the asset be initially measured?

BC16 [The Committee decided to follow a similar principle as that in paragraph 20 of IAS 16 *Property, Plant and Equipment* in determining when the recognition of costs of a stripping campaign component should end. Paragraph 20 of IAS 16 states that recognition should cease when the item is ‘in the location and condition necessary for it to be capable of operating in the manner intended by management’. An entity incurs stripping costs with the ultimate goal of extracting ore from the land. Therefore, once a section of land is stripped to the extent required in order to achieve this objective, capitalisation of stripping costs relating to that section of land should cease.]

BC17 [Similarly, the Committee decided to follow the principle in paragraph 21 of IAS 16, to determine whether ancillary costs should be included in the measurement of the stripping campaign component. It is likely in practice that other development activities may take place at the same time and in the same area as the stripping activity, but are not of a waste-removal nature. The Committee was concerned that the costs relating to these ancillary activities would be capitalised to the stripping campaign component in error.]

How shall the asset be subsequently measured?

BC18 The Committee decided that the most rational and systematic way of amortising the cost of the stripping campaign component would be over the units of ore that benefited from the campaign. This is an application of the units of production method which is currently used in practice, but which is focused only on the ore that is directly accessed through the stripping campaign. [Therefore, an entity should never be in a position where a balance on a stripping campaign component remains after all the related ore has been extracted. If this is the case, any remaining balance on the component should be fully amortised at that time.]

Transition

BC19 [Due to the complex and lengthy nature of many mining operations, and the diversity of practice in respect of this issue, the Committee concluded that applying the change in accounting policy retrospectively to existing and on-going stripping campaigns would be unnecessarily onerous and impracticable. The Committee therefore decided that the draft Interpretation should require prospective application to stripping campaigns beginning on or after its effective date.]