

STAFF PAPER

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IASB Meeting

Project	Property, Plant and Equipment: Proceeds before Intended Use (Amendments to IAS 16)		
Paper topic	Project direction		
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Purpose and structure

1. The objectives of this paper are to:
 - (a) consider the feedback and insights obtained on the proposed amendments to IAS 16 *Property, Plant and Equipment—Proceeds before Intended Use* ([Exposure Draft](#));
 - (b) explore possible approaches for this project; and
 - (c) provide our recommendations to the Board on the direction of this project.
2. This paper is structured as follows:
 - (a) summary of staff recommendations (paragraphs 4-5);
 - (b) expected benefits of the proposed amendments (paragraphs 6-10);
 - (c) significant concerns raised about the proposed amendments (paragraphs 11-40);
 - (d) project direction (paragraphs 41-68);
 - (e) referring the matter of sales proceeds before intended use to the Board's research project on Extractive Activities (paragraphs 69-74); and
 - (f) staff recommendations (paragraphs 75-83).

3. This paper has two appendices:
 - (a) Appendix A—Summary of feedback from the IFRS Interpretations Committee (Committee) members in June 2018; and
 - (b) Appendix B—Summary of feedback from the Accounting Standards Advisory Forum (ASAF) in July 2018.

Summary of staff recommendations

4. We recommend the Board not amend IAS 16 to require an entity to recognise in profit or loss any proceeds from selling items produced before an item of property, plant and equipment (PPE) is available for use¹.
5. Instead, we recommend the Board:
 - (a) proceed with the proposed clarification of the meaning of ‘testing’ included in the Exposure Draft;
 - (b) require an entity to disclose the amount of any proceeds from selling items produced before an item of PPE is available for use; and
 - (c) consider addressing the matter of sales proceeds before intended use as part of its research project on Extractive Activities.

Expected benefits of the proposed amendments

6. When deciding on the direction of the project, we think the Board should consider the expected benefits of the proposed amendments—in particular the benefits of amending the measurement requirements in IAS 16 to require the recognition in profit or loss of any sales proceeds before intended use.
7. As a reminder, the Board developed the proposed amendments in response to a request to the Committee. The Committee’s work on the request indicated that entities apply diverse reporting methods in the reporting of sales proceeds before

¹ For ease of reference, this paper uses the phrases ‘available for use’ or ‘intended use’ to describe the point in time at which an item of property, plant and equipment is in the location and condition necessary for it to be capable of operating in the manner intended by management.

intended use. The Committee specifically observed that entities applying the measurement requirements in IAS 16 included as a reduction of an asset's directly attributable costs either:

- (a) the proceeds from selling items only from the testing phase of the asset; or
- (b) any sales proceeds earned before the asset is available for use.

Accordingly, the proposed amendments aimed to improve comparability of financial information between entities on the reporting of sales proceeds before intended use.

8. Furthermore, the proposed amendments were intended to provide users of financial statements with a representationally faithful picture of both the cost of an item of PPE and of an entity's total revenue (or income). Crediting proceeds before intended use against the cost of an item of PPE has a pervasive effect on an entity's financial statements. This is because such treatment reduces the depreciable amount of the associated item of PPE that might have a long useful life (in particular in the extractive industry). The accounting treatment also affects, positively in many cases, the computation of financial ratios based on an entity's total assets (such as the return on capital employed²). Accordingly, the proposed amendments aimed to provide a clearer picture of an entity's performance over time.
9. We note that the sales proceeds meet the definition of income in the 2018 *Conceptual Framework for Financial Reporting* and, thus, in our view, should be recognised in profit or loss. We do not consider the fact that such proceeds may fluctuate due to their nature, or are not within an entity's control, as compelling arguments to justify the reporting of such proceeds as a reduction of the cost of an item of PPE. We think that the requirements in paragraphs 17(e) of IAS 16 intended to set a practical expedient applying only to testing activities. The Board never extended the use of that expedient to other IFRS Standards (such as IAS 38 *Intangible Assets* which includes measurement requirements that are similar to those in IAS 16). The feedback to the Exposure Draft indicates that those requirements have been applied extensively in practice, even to assets that are not items of PPE. In this regard, the proposed amendments would result in requirements that would:

² This is a non-GAAP measure which is often computed as the ratio between Earnings Before Interest and Tax (EBIT) and Capital Employed (being the sum of fixed assets and working capital requirement).

- (a) have a robust conceptual basis; and
 - (b) improve discipline in the application of IFRS Standards.
10. As discussed Agenda Paper 12B prepared for this meeting, some respondents agreed that the proposed amendments would result in improvements to financial reporting, in particular by eliminating diversity in practice.

Significant concerns raised about the proposed amendments

11. However, as discussed in detail in Agenda Paper 12B, the proposed amendments have elicited mixed views among stakeholders. Many stakeholders expressed concerns about the Board’s proposals. In our view, there are four significant concerns that the Board should specifically consider when deciding on the direction of the project:
- (a) could the Board address the matter of proceeds before intended use without considering the broader matter of identifying when an item of PPE is available for use?
 - (b) would the requirement to allocate costs as a result of the proposed amendments result in diversity in practice?
 - (c) would the recognition in profit or loss of sales proceeds before intended use provide relevant information?
 - (d) would the expected benefits of amending the measurement requirements in IAS 16 exceed the costs of standard-setting?
12. We discussed these concerns in paragraphs 13-40 below.

Could the Board address the matter of proceeds before intended use without considering the broader matter of identifying when an item of PPE is available for use?

Stakeholders’ comments

13. Many stakeholders said the Board should consider clarifying or developing further requirements on assessing when an item of PPE is available for use. They said the Board should consider this matter rather than the accounting for sales proceeds before intended use.

14. Indeed, many of those stakeholders consider the existence of significant proceeds before intended use to be a conceptual inconsistency. In their view, an entity cannot generate significant proceeds from the use of an item of PPE if this item is not available for use. Accordingly, they view the diversity in accounting for sales proceeds before intended use as the consequence of an underlying problem, but not the problem itself.

Possible Board's response to stakeholders' comments

15. The Board could undertake a research project or a standard-setting project to clarify or develop further requirements on assessing when an item of PPE is available for use.
16. However, the Board explored whether it should clarify when an item of PPE is available for use during the development of the Exposure Draft—this is explained in paragraphs BC18-22 of the Exposure Draft. The Board concluded that it was possible to address the reporting matter of sales proceeds before intended use without considering the matter of when an item of PPE is available for use.
17. We continue to agree with the Board's decision not to undertake standard-setting on the matter of when an item of PPE is available for use. This is because:
- (a) such a project would be much broader than the proposed amendments would be. It might also require reconsideration of other requirements in IAS 16 and may have cross-cutting implications on other IFRS Standards.
 - (b) the Board has not obtained any new evidence other than the feedback on the Exposure Draft, that assessing when an asset is available for use is a matter requiring standard-setting.
 - (c) a majority of Committee and ASAF members did not support such an approach.
18. Additionally, we note that that the proposed amendments could be an effective way of limiting the possible effects of the diversity in how entities identify when an item of PPE is available for use. This is because the proposed amendments would:
- (a) clarify that testing whether an asset is functioning properly is not a financial assessment. In our view, this could also lead entities to conclude that

assessing whether an item of PPE is available for use is an assessment of its technical and physical performance and not a financial assessment.

- (b) require the recognition of all sales proceeds before intended use in profit or loss. In our view, this requirement would remove some of the tension on assessing when an asset is available for use. This is because, applying the proposed amendments, sales proceeds would be recognised in profit or loss regardless of whether they are earned before or after the asset is available for use.

- 19. Accordingly, we have not identified any new information that would change the Board’s decision not undertake standard-setting on clarifying when an item of PPE is available for use.

Would the requirement to allocate costs as a result of the proposed amendments result in diversity in practice?

Stakeholders’ comments

- 20. Many stakeholders said that identifying costs that relate to items produced and sold before an item of PPE is available for use and distinguishing such costs from other costs (cost allocation) would require extensive use of judgement and might result in diversity in reporting such costs.
- 21. In the view of those stakeholders, the potential diversity in the reporting of costs would offset any improvements to financial reporting resulting from recognising sales proceeds before intended use in profit or loss.
- 22. In contrast, a few stakeholders (non-extractive entities) indicated that such a cost allocation would not present a significant implementation challenge considering the experience that entities usually have in relation to cost management. Those stakeholders said the proposed amendments might not result in significant incremental diversity in reporting practices.

Possible Board’s response to stakeholders’ comments

- 23. The proposed amendments do not include any specific requirements on how an entity allocates costs. Consequently, some stakeholders suggested that the Board could limit potential diversity in cost allocation by proposing one of the following alternatives:

- (a) reminding stakeholders about the existing requirements in IAS 2 *Inventories*, IAS 16 or IFRIC 20 *Stripping Costs in the Production Phase of a Surface Mine* on how an entity applies its judgement to allocate costs;
 - (b) incorporating in IAS 16 the Board’s observations in paragraph BC9 of the Exposure Draft about the application of the requirements in IAS 2 and IAS 16;
 - (c) developing high-level principles on cost allocation; or
 - (d) developing detailed requirements or application guidance. For example, the Board could require the recognition in profit or loss of only particular costs of producing items sold (for example, only the direct costs of producing those items).
24. However, if the Board does not wish to develop principles or requirements on cost allocation, we think the Board should reconsider whether amending the measurement requirements in IAS 16 is appropriate.
25. In discussing the possible direction of this project in paragraphs 41-68 of this paper, we assessed whether and how the Board could respond to this concern.

Would the recognition in profit or loss of sales proceeds before intended use provide relevant information?

Stakeholders’ comments

26. Some preparers and investors questioned whether the recognition of such sales proceeds in profit or loss would provide relevant information. This is because, in their view, such proceeds have limited predictive value. Accordingly, they thought that the proposed amendments might result in:
- (a) users of financial statements making adjustments to financial information; and
 - (b) the increased use of non-GAAP measures.

Possible Board’s response to stakeholders’ comments

27. In our view, the recognition of sales proceeds before intended use in profit or loss provides relevant information. We agree that such proceeds may have limited predictive value, but we think that they have confirmatory value.
28. To mitigate concerns about the predictive value of such proceeds, the Board could proceed with the proposed amendments but also include specific presentation and

disclosure requirements. Such requirements would help users of financial statements identify the sales proceeds and their related costs and consequently help them tailor the financial information to meet their particular needs.

29. For instance, the presentation requirements could specify whether an entity presents:
 - (a) the sales proceeds as a separate line item in the statement of profit or loss; or
 - (b) the sales proceeds and their related production costs on a ‘gross’ or ‘net’ basis.
30. The disclosure requirements might include:
 - (a) the amount of any sales proceeds before intended use recognised in profit or loss;
 - (b) the amount of any costs allocated to profit and loss in respect of those sales proceeds; and
 - (c) the cost allocation methodology applied (if the final amendments are not prescriptive on this point).
31. We think such disclosure requirements would be particularly useful if an entity were to assess that the sales proceeds before intended use do not arise in the course of its ordinary activities. This is because, in such circumstances, the presentation and disclosure requirements in IFRS 15 *Revenue from Contracts with Customers* and IAS 2 might not apply to the proceeds and their production costs.
32. If the Board decided not to change the existing measurement requirements in IAS 16, the Board might still, at minimum, consider requiring disclosures of the amount of any sales proceeds included as a reduction of the directly attributable costs of an item of PPE.

Would the expected benefits of amending the measurement requirements in IAS 16 exceed the costs of standard-setting?

Stakeholders’ comments

33. Some stakeholders raised a question on whether the expected benefits of the proposed amendments, and in particular, the benefits of a standard-setting approach resulting in the recognition of sales proceeds before intended use in profit or loss, exceed the costs of standard-setting.

34. We explained the expected benefits of the proposed amendments in paragraphs 6-10 of this paper.
35. However, some stakeholders said that such benefits might be more limited than the Board had expected. In particular, the feedback and our additional follow-up activities confirm that the matter of sales proceeds before intended use affects the extractive industry more than other industries—for those other industries, we have no compelling evidence suggesting that such proceeds are material. Accordingly, some stakeholders suggested the Board consider the matter in the context of its research project on Extractive Activities.
36. Some stakeholders also said that the Board might have understated the standard-setting costs of amending the measurement requirements in IAS 16. Those stakeholders said the proposed amendments could result in:
- (a) additional implementation costs for preparers. Those costs might be:
 - (i) significant for preparers in the extractive industry. This is because performing a cost allocation would require tracking costs at a more granular level than with the extant requirements in IAS 16. In this industry, we understand such implementation costs might be significant for junior mining entities who may have less sophisticated costing systems than more mature entities in this industry.
 - (ii) not insignificant for preparers in other industries who would need to assess whether proceeds before intended use and any related production costs, are material.
 - (b) incremental costs of analysis for users of financial statements. As explained in paragraph 26 of this paper, some respondents said the proposed amendments would result in the recognition in profit or loss of income and expenses with limited predictive value. Furthermore, one investor with whom we met said the proposed amendments might result in additional volatility in the statement of profit or loss and other comprehensive income. Accordingly, users of financial statements might need to invest time and resources to understand the implications of the proposed amendments and how they affect the statement of profit or loss. We note that the existence of disclosure requirements could reduce those costs of analysis but would not eliminate them.

Possible Board's response to stakeholders' comments

37. Paragraphs 2.39-2.43 of the 2018 *Conceptual Framework for Financial Reporting* (Framework) define the principle of the cost constraint on useful financial reporting. Paragraph 2.38 of the Framework states:
- Reporting financial information imposes costs, and it is important that those costs are justified by the benefits of reporting that information.
38. The Board observed in paragraph BC3 of the Exposure Draft that the matter of sales proceeds before intended use mainly affects a few industries (such as the extractive industry). The feedback confirmed the Board's observation and thus, confirmed that the Board appropriately assessed the scope of entities to which the benefits of the proposed amendments would apply. The Board concluded that those benefits would be sufficiently widespread to justify standard-setting. However, we acknowledge that some stakeholders did not agree with the Board's conclusion and questioned whether amending the measurement requirements in IAS 16 for a limited number of industries would result in significant benefits.
39. In our view, if the Board were to conclude that there is too much uncertainty on the breadth of the expected benefits, and thus on the likelihood that they would exceed the expected costs of standard-setting, the Board might then choose not to amend the measurement requirements in IAS 16 and instead:
- (a) decide not to proceed with the project; or
 - (b) require entities to disclose the amount of sales proceeds included as a reduction of an asset's directly attributable costs. The Board could then use the disclosure requirement to:
 - (i) obtain more detailed information on the pervasiveness and materiality of the matter of proceeds before intended use; and
 - (ii) reassess, at a future date, the need to amend the measurement requirements in IAS 16.
40. In considering the project direction, we specifically considered stakeholders' concerns about the cost constraint.

Project direction

41. In the light of the significant concerns raised, we have identified three possible approaches that the Board could apply to this project.
42. We have provided a summary of those approaches in the table below and described them in further detail in paragraphs 44-68 of this paper.

Approach	Summary description
Modified ED	<ul style="list-style-type: none"> • Proceed with the proposed amendments ie amend the existing requirements in paragraph 17(e) of IAS 16 to: <ul style="list-style-type: none"> (i) prohibit deducting from the cost of an item of PPE any proceeds from items sold before the item of PPE is available for use and instead require their recognition in profit or loss (along with their related production cost), and (ii) clarify the meaning of ‘testing’. • In addition, develop: <ul style="list-style-type: none"> ○ requirements on how an entity determines the production cost of such proceeds (requirements or a principle on cost allocation); and ○ disclosure requirements on sales proceeds before intended use and their related production cost.
Testing and Disclosure	<ul style="list-style-type: none"> • Proceed with the proposed clarification to the meaning of ‘testing’ included in the Exposure Draft. • Do not proceed with the amendments to the measurement requirements in IAS 16—ie do not amend the existing requirements in paragraph 17(e) of IAS 16. • Instead, require that an entity discloses the amount of proceeds recognised as a reduction to the cost of an item of PPE.
Do not proceed	<ul style="list-style-type: none"> • Do not proceed with any of the proposed amendments.

43. If the Board were to decide to apply either the ‘Testing and Disclosure’ or the ‘Do not proceed’ approach, we think the Board could also consider addressing the matter of sales proceeds before intended use as part of its research project on Extractive Activities—we discussed this point in paragraphs 69-74 of this paper.

‘Modified ED’ approach

Description of the approach

44. Applying this approach, the Board would proceed with the proposed amendments but would incorporate some modifications.
45. We think that the modifications to the proposed amendments could include:
- (a) setting out principles or requirements regarding the identification of the costs of producing items sold. As described in paragraph 23 of this paper, there are several ways the Board could develop such principles or requirements. As a preliminary view, should the Board decide to proceed with this approach, we would recommend the Board consider developing high-level principles on cost allocation.
 - (b) incorporating specific disclosure requirements relating to the sale of items produced before an item of PPE is available for use. Those disclosures would include:
 - (i) the amount of sales proceeds recognised in profit or loss for the period; and
 - (ii) the amount of costs allocated to profit and loss in respect of those proceeds.
 - (c) introducing presentation requirements for such proceeds and their production cost (see paragraph 29 of this paper).

Staff comments

46. This approach³ has the merit of retaining all the expected benefits of the proposed amendments as described in paragraphs 6-10 of this paper while addressing the concerns raised in the feedback about:
- (a) the diversity in the reporting of costs that relate to items produced before an item of PPE is available for use; and
 - (b) whether the sales proceeds before intended use provide relevant information.
47. Nonetheless, because this approach would require an entity to recognise sales proceeds before intended use in profit or loss, this approach might not address stakeholders' concerns about the potential costs of the amendments as described in paragraph 36 of this paper.

Further steps required

48. If the Board were to proceed with this approach, we would come back with further analysis and detailed recommendations on:
- (a) principles or requirements on cost allocation; and
 - (b) possible disclosure and presentation requirements.
49. In our view, this approach may also require further outreach. This is because stakeholders expressed differing views on how prescriptive any cost identification and allocation requirements should be.
50. This approach might also require the Board to consider if any further analysis is needed to respond to some stakeholders' concerns that the benefits of the proposals might not exceed the costs that preparers and users would incur.
51. Overall, we think that this approach could add to the timeline and complexity of the project.

Feedback from the Committee and ASAF

52. Most Committee members supported this approach at the June 2018 Committee meeting. Regarding cost allocation:

³ This approach is similar to *Approach 2* that we presented to the Committee and ASAF.

- (a) some members said the Board should only provide high-level principles and not consider detailed or prescriptive requirements;
- (b) one member suggested that the Board consider developing cost allocation requirements similar to those in existing IFRS Standards; and
- (c) one member suggested the inclusion of only direct costs in the cost of items sold.

53. Two ASAF members supported this approach at the July 2018 ASAF meeting:

- (a) one member recommended that the Board develop high-level principles on cost allocation and suggested that the requirements in IAS 2 on cost allocation could be used to help develop any such principles.
- (b) one member, while expressing a preference for this approach, said a disclosure-focused approach may be more appropriate if the Board wants to proceed more quickly with any amendments to IAS 16.

‘Testing and Disclosure’ approach

Description of the approach

54. Applying this approach, the Board would:

- (a) amend IAS 16, as proposed in the Exposure Draft, to clarify the meaning of testing activities, and specify that testing whether an item of PPE is functioning properly is assessing the technical and physical performance of that asset (and not its financial performance).
- (b) not proceed with the amendments to the measurement requirements in IAS 16 as proposed, but instead introduce disclosure requirements to IAS 16 requiring an entity to disclose any sales proceeds credited against the cost of an item of PPE during the period.

Staff comments

55. This approach addresses the matter of sales proceeds before intended use through additional disclosure requirements rather than amendments to the measurement requirements in IAS 16 thereby alleviating the various concerns stakeholders expressed about cost allocation. In addition, we think such an approach is unlikely to

result in significant incremental costs for preparers and users. For example, the preparers with whom we met explained they could provide the information necessary to disclose the amount of proceeds before intended use at no significant incremental cost.

56. We also think this approach could enable the Board to monitor and reassess the matter at a future date. Additional disclosure requirements might help confirm whether the pervasiveness and the materiality of sales proceeds before intended use justify amending the measurement requirements in IAS 16. In other words, the Board could use this approach as an interim measure providing immediate benefits to the users of financial statements while also providing information that could be used by the Board if it decided to reassess the matter at a future date.
57. Furthermore, this approach could address some of the comments we received from stakeholders relating to the determination of when an asset is available for use. In particular:
- (a) requiring disclosure on the amount of proceeds before intended use could help:
 - (i) enforce greater discipline in assessing whether an item of PPE is available for use. We think this approach may lead an entity's management to validate that their assessment of available of use is appropriate, in particular if the amount of any such sales proceeds is material; and
 - (ii) the Board assess whether the matter of assessing when an item of PPE is available for use is a significant reporting matter.
 - (b) clarifying the meaning of testing activities may help an entity better identify when an item of PPE is available for use. We note that the feedback on the Exposure Draft has not raised any particular concern about this clarification.
58. Nonetheless, we acknowledge that this approach reduces the benefits of the proposed amendments as described in paragraphs in paragraphs 6-10 of this paper. In particular, this approach does not eliminate diversity in practice. We note however that this approach would provide greater transparency on how entities account for sales proceeds before intended use as well on the amounts of such proceeds.

Further steps required

59. If the Board were to apply this approach, we would come back with further analysis and recommendations on possible disclosure requirements.

Feedback from the Committee and ASAF

60. Two Committee members supported a disclosure-focused approach. In their view, the determination of when an item of PPE is available for use is the underlying matter for the Board to resolve.
61. Most ASAF members supported a disclosure-focused approach. Those members said additional disclosures may assist the Board in identifying:
- (a) the industries in which the matter of sales proceeds before intended use is a material matter.
 - (b) whether the matter that the Board should address is proceeds before intended use or the determination of when an item of PPE is available for use. In particular, one member (EFRAG) said that such disclosures may provide useful information and may result in a greater focus by management on when an item of PPE is available for use.
62. A number of ASAF members questioned whether the matter of proceeds before intended use was material for industries other than those operating in the extractive sector.

‘Do not proceed’ approach

Description of the approach

63. Applying this approach, the Board would not undertake any further work on this project at this stage—ie the Board would amend neither the measurement nor the disclosure requirements in IAS 16.
64. This approach assumes that the expected benefits of either the ‘Modified ED’ or the ‘Testing and Disclosure’ approaches are unlikely to exceed the cost of standard-setting.

Staff comments

65. There would be no costs to stakeholders if the Board decided not to proceed with any amendments but also no benefits.
66. In particular, we note that this approach would not address stakeholders' concerns about the existence of diversity in practice. This is because a decision not to proceed leaves the accounting matter that the Committee proposed to address unresolved, thereby resulting in no improvement in financial reporting. In particular, we think some stakeholders would still be concerned that:
 - (a) diversity in the application of the requirements in IAS 16 would continue and users of financial statements would have no specific information about the sales proceeds before intended use; and
 - (b) some entities would continue to apply the existing requirements in paragraph 17(e) of IAS 16 by analogy to assets that are not items of PPE.

Further steps required

67. If the Board were to proceed with this approach, we would propose not doing any further work on this project.

Feedback from the Committee and ASAF

68. When discussing the possible ways to move forward with the project with both the Committee and ASAF, we did not provide this approach as a possible alternative for consideration. Accordingly, we have no feedback to report to the Board.

Referring the matter of sales proceeds before intended use to the Board's research project on Extractive Activities

69. Some respondents to the Exposure Draft, as well as a few ASAF and Committee members, observed that the Board currently has a research project on Extractive Activities. They said that the Board could address the matter of proceeds before intended use in the context of this research project because the feedback indicates that this matter mainly affects the extractive industry.
70. The three approaches described in paragraphs 41-68 of this paper set out alternatives that would apply to entities in any industry. However, the Board could decide to

adopt an industry-specific approach and thus, might contemplate addressing the matter of sales proceeds before intended use for the extractive industry only.

71. Consequently, the Board might decide, as a supplementary step, to refer this matter to its research project on Extractive Activities—ie the Board could consider adding this matter to the scope of that project which, as yet, has not been defined. We think the Board could make such a decision to supplement either the:
 - (a) ‘Testing and Disclosure’ approach, or
 - (b) ‘Do not proceed’ approach.

72. This industry-specific approach could, for example, result in the development of specific measurement or disclosure requirements for entities operating in the extractive industry.

73. We agree that the Extractive Activities project might be an appropriate vehicle to consider the matter of sales proceeds before intended use. This is because we think this matter mainly affects the extractive industry. We also note that the feedback on the Exposure Draft, as well as the outcome of our follow-up activities, informed us of a number of related accounting matters specific to this industry—for example, assessing when the commercial phase of a mine starts or identifying ‘abnormal costs’. Such information could be helpful for the Board in the context of this research project.

74. However, in our view, there are limitations of referring the matter of sales proceeds before intended use to the Extractive Activities project:
 - (a) this research project has just started, and we do not yet know whether:
 - (i) it will be feasible to incorporate the matter of proceeds before intended use, as well as the related matters identified from the feedback received, into the scope of this project. We note that proceeds before intended use was not identified in the previous Discussion Papers on Extractive Activities as a financial reporting topic requiring investigation.
 - (ii) this research project will result in standard-setting, and if so, whether any such standard-setting will be industry-specific and the timing of any standard-setting.

- (b) if the Board were to develop specific requirements for extractive entities, and if some future evidence were to show that the matter of sales proceeds before intended use is material for entities in other industries, there is a risk that an approach that establishes requirements for extractive entities only might not be justified.

Staff recommendations

Recommendation on the possible ways to move forward

75. We recommend that the Board undertake narrow-scope standard-setting to address the matter of sales proceeds before intended use.
76. The feedback received from stakeholders confirms that there is diversity in the financial reporting of such proceeds. We think that narrow-scope standard setting will help to address the identified diversity.
77. We continue to think that the proposed amendments are conceptually sound and would result in greater consistency in the application of IAS 16 to sales proceeds before intended use.
78. However, if the Board were to proceed with amending the measurement requirements in IAS 16, we think that enhancements to the proposals, as described in the Modified ED Approach, would be required in order to address the concerns we have heard from stakeholders about cost allocation.
79. We also note that the feedback has confirmed that the matter is most prevalent in the extractive industry and, thus, it is within this industry that we would expect to see the main benefits of the proposed amendments. However, the feedback also indicates that the costs of the amendments might be more than originally anticipated by the Board for those entities affected by the amendments.
80. Accordingly, while we see the merits of proceeding with the ‘Modified ED’ approach, in consideration of the potential costs of the amendments and the fact that the matter predominantly affects the extractive industry, we think a disclosure-focused approach may be the most effective way for the Board to proceed with this project.

81. Therefore, on balance, we recommend that the Board proceed with the ‘Testing and Disclosure’ approach. We think this approach will provide useful information to our stakeholders at a cost that is not significant. The enhanced disclosures will also help inform the Board of the significance of the matter across all industries should the Board decide to reassess the matter at a future date.

Question 1 for the Board

Question 1—Do you agree with our recommendation not to proceed with the proposed amendments as exposed in the Exposure Draft, and instead proceed with the ‘Testing and Disclosure’ approach’ as outlined in paragraphs 54-62 of this paper?

Recommendation on whether to consider referring the matter to the Board’s research project on Extractive Activities

82. If the Board decides to proceed with either the ‘Testing and Disclosure’ or the ‘Do not proceed’ approach, we recommend the Board also consider whether to include the matter of sales proceeds before intended use as part of its research project on Extractive Activities.
83. This is because:
- (a) the feedback indicates that the matter of sales proceeds before intended use is material for entities operating in that industry; and
 - (b) such a project would help assess whether industry-specific requirements are necessary to provide users of financial statements with improved financial information—ie whether the Board should set out specific measurement or disclosure requirements for Extractive entities when they earn sales proceeds before intended use.

Question 2 for the Board

Question 2—If the Board decides to proceed with the ‘Testing and Disclosure’ or the ‘Do not proceed’ approach, do you agree with our recommendation to refer, as a supplemental step, the matter to the research project on Extractive Activities?

Appendix A—Summary of feedback from the Committee members in June 2018

- A1. At the June 2018 Committee meeting, the staff sought advice from Committee members on how best to proceed on this project.
- A2. Agenda Paper 7 to that meeting presented three possible approaches to move forward on the project. Those approaches were as follows:
- (a) Approach 1: proceed with the Exposure Draft as published.
 - (b) Approach 2: proceed with the Exposure Draft with some modifications (for example, adding (i) a principle and requirements on cost allocation; and/or (ii) disclosure requirements).
 - (c) Approach 3: proceed with additional disclosure requirements and consider possible alternative standard-setting approaches (for example, (i) clarify when an item of PPE is available for use; or (ii) address the matter within the Board’s research project on *Extractive Industries*).
- A3. Overall, Committee members were supportive of the Board proceeding with the project. They expressed general support for the recognition in profit or loss of proceeds received before an item of PPE is available for use, and also noted that the feedback confirmed that there is diversity in reporting practices for particular industry sectors with respect to those proceeds.
- A4. Most Committee members and observers who expressed a view supported Approach 2.
- A5. Some Committee members acknowledged that allocating costs might be difficult in some cases but, based on their experience, members said such allocation would be feasible. One Committee member said the requirement to allocate costs among different items is not new. A few members also suggested that Approach 2 could perhaps be supplemented by providing additional clarity about when an asset is available for use.
- A6. Some Committee members commented on the proposal within Approach 2 to develop principles and/or requirements on cost allocation:

- (a) almost all suggested that the Board provide only high level principles and/or requirements—one member said the Board should be cautious when doing so.
- (b) one member suggested that the Board consider developing cost allocation requirements similar to those already in existing IFRS Standards (such as IAS 2 or IFRIC 20).
- (c) one member suggested the inclusion of only direct costs in the cost of items sold (or otherwise developing specific presentation requirements for the proceeds and related production costs).

- A7. Many members supported the inclusion of specific disclosure requirements (as proposed within Approach 2). They think that disclosure is particularly important with respect to proceeds received before an item of PPE is available for use. One observer also suggested an additional disclosure requirement about when an item of PPE is available for use.
- A8. Two Committee members supported Approach 3, noting that in their view determining when an item of PPE is available for use is the underlying matter to resolve. One of those Committee members said proceeds before intended use might be material only for the extractive industry and, if so, might also suggest addressing the matter within the Board’s project on *Extractive Activities*.
- A9. Conversely, a number of Committee members recommending not pursuing Approach 3. They view Approach 3—addressing when an item of PPE is available for use—as a wider question that might take some considerable time without sufficient evidence that there is a wider question to resolve.

Appendix B—Summary of feedback from ASAF members (July 2018 ASAF meeting)⁴

- B1. ASAF members were asked for advice on the possible ways forward regarding the Exposure Draft [...]. ASAF members were provided with the feedback summary presented to the Board at its meeting in December 2017, as well as the feedback and analysis provided to the Committee at its meeting in June 2018.
- B2. ASAF members were presented with three possible approaches to move forward with the project. Those approaches were as follows:
- (a) Approach 1: Proceed with the Exposure Draft as published.
 - (b) Approach 2: Proceed with the Exposure Draft with some modifications (for example, adding (i) a principle and requirements on cost allocation; and/or (ii) disclosure requirements).
 - (c) Approach 3: Proceed with additional disclosure requirements and consider possible alternative standard-setting approaches (for example, (i) clarify when an item of PPE is available for use; or (ii) address the matter within the Board’s research project on Extractive Activities).
- B3. Many ASAF members supported Approach 3 or a variation of it. Those ASAF members also made the following comments:
- (a) The FASB, the DRSC and AASB/NZASB members supported Approach 3. Additional disclosure requirements of the amounts of proceeds earned before an item of PPE is available for use would help identify the industries affected. It would also potentially help the Board identify whether the matter to address is the accounting for proceeds before intended use, or determining when an item of PPE is available for use. The AASB/NZASB member suggested that if the Board were to proceed with the Exposure Draft, further requirements should be developed on the cost of producing items sold.
 - (b) The EFRAG member said Approach 3 is the approach closest to the EFRAG recommendation regarding the project. This member said

⁴ Excerpt from the [Summary note of the Accounting Standards Advisory Forum](#) (July 2018)

disclosures could provide useful information and might result in greater focus by management on when an item of PPE is available for use.

- (c) The ANC member observed that proceeds before intended use are not material for French entities and often do not exceed the cost of testing. This member said the Exposure Draft could result in implementation costs for entities with immaterial amounts of proceeds, and suggested that the Board focus on clarifying when an asset is available for use.
- (d) The ASBJ member and one jurisdiction of the AOSSG said the existing requirements in IAS 16 are well understood and, hence, did not support standard-setting other than additional disclosure requirements. The ASBJ member said developing disclosure requirements together with clarifying the definition of testing activities may improve the existing requirements in IAS 16.
- (e) The CASC member, as well several jurisdictions of the AOSSG, did not support Approach 2, in particular given the comments received relating to cost allocation. Accordingly, those members considered Approach 3 to be more appropriate.

B4. Two ASAF members supported Approach 2. They made the following comments:

- (a) The OIC member said it might be useful if the Board were to develop some high-level principles on cost allocation. This member also noted that IAS 2 includes requirements on cost allocation that could be used to develop such principles.
- (b) The AcSB member said the best way to move forward is Approach 2 but a combination of Approaches 2 and 3 might also be acceptable. Nonetheless, this member noted Approach 3 could be more appropriate should the Board wish to proceed more quickly. If proceeding with Approach 2, the AcSB member suggested that the Board develop further requirements on cost allocation. This member suggested possibly considering a cost allocation approach that would focus on direct costs but would not prohibit the inclusion of indirect costs.

B5. Only one jurisdiction of the AOSSG supported Approach 1.

- B6. A number of ASAF members questioned whether proceeds before intended use are material for industries other than the extractive industry. Some ASAF members suggested that the matter be addressed as part of the Extractive Activities project if it affects only this industry.
- B7. Some ASAF members made the following comments in this respect:
- (a) The AcSB member outlined the prevalence and materiality of the matter for Canadian extractive entities, noting that this is an important matter in Canada. This member noted that the assessment of the materiality of proceeds should not be limited to the annual financial statements, particularly when entities publish interim financial reports.
 - (b) The GLASS member said such proceeds could be material for junior mining entities but may not be material for larger mining entities. If such proceeds are material, this might indicate that the item of PPE is already available for use.
 - (c) The EFRAG member suggested that the Board perform an effect analysis to clarify the materiality of the matter.