

VIEWPOINTS: Applying IFRSs in the Mining Industry

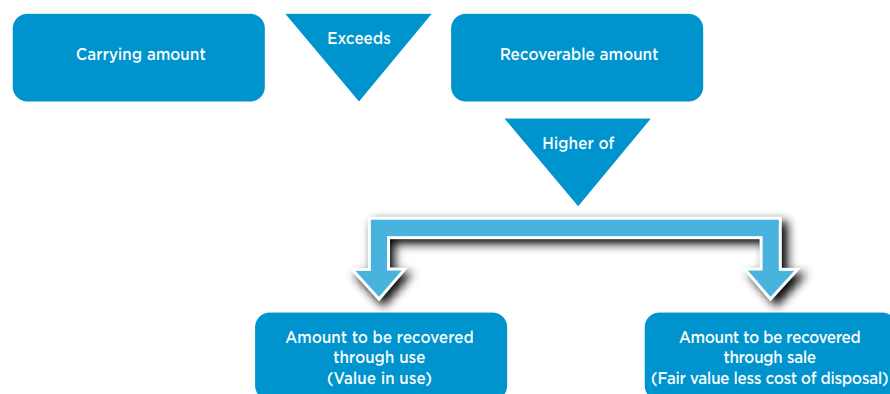
IMPAIRMENT OF EXPLORATION AND EVALUATION ASSETS

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Background

IAS 36 *Impairment of Assets* applies to the accounting for the impairment of all assets, including exploration and evaluation (E&E) assets.¹

IAS 36 prescribes the procedures that an entity applies to ensure that its assets are carried at no more than their recoverable amount, which is the higher of the amount to be recovered through use of the asset and the amount to be recovered through sale of the asset.



If an asset is carried at more than its recoverable amount, the asset is impaired and IAS 36 requires an entity to recognize an impairment loss.

IAS 36 also specifies when an entity should reverse an impairment loss.

¹ For more information, download the paper on *Exploration and Evaluation Expenditures* from www.cpacanada.ca/en/business-and-accounting-resources/financial-and-non-financial-reporting/international-financial-reporting-standards-ifs/publications/ifrs-6-impairment-of-explorationevaluation-assets

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Mining Industry Task Force on IFRSs

Canada's move to International Financial Reporting Standards (IFRSs) creates unique challenges for junior mining companies. Financial reporting in the sector is atypical due to significant differences in characteristics between junior mining companies and other types of companies. The Chartered Professional Accountants of Canada (CPA Canada) and the Prospectors and Developers Association of Canada (PDAC) created the Mining Industry Task Force on IFRSs to share views on IFRS application issues of relevance to junior mining companies. The task force's views are provided in a series of papers that are available through free download. These views are of particular interest to chief financial officers, controllers and auditors.

The views expressed in this series are non-authoritative and have not been formally endorsed by CPA Canada, PDAC or the organizations represented by the task force members.

It is important to note that although IAS 36 applies to the accounting for the impairment of E&E assets, IFRS 6 *Exploration for and Evaluation of Mineral Resources* modifies the requirements in IAS 36 with respect to:

- the indications of impairment; and
- the level at which impairment is tested.

Issue

How do the modifications in IFRS 6 affect the assessment of E&E assets for impairment?

Viewpoints

Indications of Impairment

IFRS 6 requires E&E assets to be assessed for impairment when facts and circumstances suggest that the carrying amount of an E&E asset may exceed its recoverable amount.

According to IFRS 6, one or more of the following facts and circumstances indicate that an entity should test E&E assets for impairment:

- a. the period for which the entity has the right to explore in the specific area has expired during the period or will expire in the near future, and is not expected to be renewed.
- b. substantive expenditure on further exploration for and evaluation of mineral resources in the specific area is neither budgeted nor planned.
- c. exploration for and evaluation of mineral resources in the specific area have not led to the discovery of commercially viable quantities of mineral resources and the entity has decided to discontinue such activities in the specific area.
- d. sufficient data exist to indicate that, although a development in the specific area is likely to proceed, the carrying amount of the E&E asset is unlikely to be recovered in full from successful development or by sale.

IFRS 6 clearly states that this list is not exhaustive. For example, the following additional facts and circumstances may also indicate that an entity should test E&E assets for impairment:

- a significant drop in mineral prices;
- a significant deterioration in the availability of equity financing;
- a delay in E&E activity; or
- a substantial decline in the share price of the mining entity.

For the purpose of assessing E&E assets for impairment, an entity applies guidance in IFRS 6 rather than IAS 36.

Unlike IAS 36, IFRS 6 does not explicitly require impairment testing of E&E assets when the carrying amount of the net assets of an entity is more than its market capitalization. However, market capitalization should not be ignored. When market capitalization is less than the carrying amount of an entity's net assets, an entity should carefully consider the reasons for this occurrence. This fact could be viewed as an indication that E&E assets might be impaired because of other reasons. Market capitalization metrics alone would not be indicative of impairment. An entity should then carefully consider the other, more relevant facts and circumstances (i.e., those listed in paragraph 20 of IFRS 6) to determine if an impairment test is required.²

Level at Which Impairment Is Tested

An entity is required by IFRS 6 to determine an accounting policy for allocating E&E assets to cash-generating units (CGUs) or groups of CGUs for the purpose of assessing such assets for impairment. Therefore, entities may test E&E assets for impairment at the level of reporting that reflects the way they manage their operations.

IAS 36 defines an asset's CGU as the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. A mining entity may, for example, identify the following as a CGU:

- a contiguous ore body or a property in the E&E phase; or
- a mine in the development or production phase.

E&E assets do not currently generate cash inflows; however, they may form a separate CGU when there is sufficient information about the mineral resources to estimate future cash inflows. In accordance with IFRS 6, the level identified by the entity for the purposes of testing E&E assets for impairment may comprise one or more CGUs.

In many cases, there is insufficient information about the mineral resources to estimate future cash inflows; therefore, E&E assets are often allocated to CGUs or groups of CGUs for the purpose of assessing such assets for impairment. This allocation may be based on the way in which the entity manages its operations, for example by mineral within a specific geographic area.

It is important to note that IFRS 6 stipulates that each CGU or group of CGUs to which an E&E asset is allocated must not be larger than an operating segment determined in accordance with IFRS 8 *Operating Segments*.

² For more details refer to IFRS Discussion Group report dated October 18, 2012.

The Mining Industry Task Force on IFRSs

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For more information on IFRSs visit www.cpacanada.ca/viewpointsmining.