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International Accounting Standards Board
30 Cannon Street
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Comments on the Discussion Paper *Extractive Activities*

To the Board Members:

The Japanese Institute of Certified Public Accountants appreciates the continued efforts of the international project team, and welcomes the opportunity to comment on the discussion paper *Extractive Activities.* As the discussion paper was not prepared by the International Accounting Standards Board (IASB) following a usual due process, we hope that future discussions in the development of relevant standards, the IASB considers the contents covered by the discussion paper in light of the IASB Framework, as well as gives thorough consideration to consistency with other IFRSs.

Following are comments on matters that we believe require particular consideration from the perspective of practical application.

Question 6 – Minerals or oil and gas asset measurement model

Chapter 4 identifies current value (such as fair value) and historical cost as potential measurement bases for minerals and oil and gas properties. The research found that, in general, users think that measuring these assets at either historical cost or current value would provide only limited relevant information. The project team's view is that these assets should be measured at historical cost but that detailed disclosure about the entity's minerals or oil and gas properties should be provided to enhance the relevance of the financial statements (see Chapters 5 and 6). In your view, what measurement basis should be used for minerals and oil and gas properties and why? This could include measurement bases that were not considered in the discussion paper. In your response, please explain how this measurement basis would satisfy the qualitative characteristics of useful financial information.

Comment:

We believe that historical cost should be used as the measurement basis for minerals and oil and gas properties. The reason for this is the high degree of uncertainty involved in the fair value measurement of minerals and oil and gas properties. Therefore it is virtually impossible to measure such assets with any level of reliability. Specific reasons are as follows:

(a) The method of measurement based on current value (fair value) could be another option. However, when estimating current value (fair value), the high level of uncertainty involved in estimating various factors such as "commodity prices that reflect future market prices," "reserves," and "extracting costs," makes it difficult to measure the amount to be recognized with an acceptable level of reliability. This could, in the end, potentially disadvantage both the preparers and the users of financial statements, while also rendering the audit of accounting estimates more difficult.

(b) If, as indicated by the feedback from users of financial statements, only limited information, be it historical cost or current value, is to be disclosed to the users, from the perspective of striking a balance between costs and benefits, we agree with the view of the project team that the historical cost method is the most suitable accounting policy.

(c) In terms of necessary information relating to current value, we believe that it would be possible to provide information that will contribute to the users' decision making through disclosures made in the notes to the financial statements.

It should be noted that even under the current IFRS, accounting treatment based on historical cost is applied in cases where an entity holds directly minerals and oil and gas properties; and in cases where an entity holds such assets, through its subsidiaries and affiliates, under consolidation or the equity method. However, when investments to such assets are made through entities other than its subsidiaries and affiliates, regardless of whether such entities are listed or not ,current IFRS 9 *Financial Instruments* require measurement at fair value of the investment (FVTPL or FVTOCI). This lack of consistency in the required accounting treatment has become a subject of concern to us. Thus, we believe that, until new IFRSs are established with regard to extractive activities, such investments should be exempt from the application of IFRS 9.

Question 7 – Testing exploration properties for impairment

Chapter 4 also considers various alternatives for testing exploration properties for impairment. The project team's view is that exploration properties should not be tested for impairment in accordance with IAS 36 Impairment of Assets. Instead, the project team recommends that an exploration property should be written down to its recoverable amount in those cases where management has enough information to make this determination. Because this information is not likely to be available for most exploration properties while exploration and evaluation activities are continuing, the project team recommends that, for those exploration properties, management should:

(a) write down an exploration property only when, in its judgement, there is a high likelihood that the carrying amount will not be recoverable in full; and

(b) apply a separate set of indicators to assess whether its exploration properties can continue to be recognised as assets.

Do you agree with the project team's recommendations on impairment? If not, what type of impairment test do you think should apply to exploration properties?

Comment:

We agree.

However, the establishment of standards unique to a particular industry should be made only on a limited basis within IFRS, principle-based standards. As the discussion paper was not prepared by IASB following a usual due process, during the revision and development of policy of the IFRSs, as a whole, careful consideration should be given regarding the implications of allowing exceptions exclusively to exploration properties of minerals and oil and gas.

Question 9 – Types of disclosure that would meet the disclosure objectives

Also in Chapter 5, the project team proposes that the types of information that should be disclosed include: (a) quantities of proved reserves and proved plus probable reserves, with the disclosure of reserve quantities presented separately by commodity and by material geographical areas; (b) the main assumptions used in estimating reserves quantities, and a sensitivity analysis; (c) a reconciliation of changes in the estimate of reserves quantities from year to year; (d) a current value measurement that corresponds to reserves quantities disclosed with a reconciliation of changes in the current value measurement from year to year; (e) separate identification of production revenues by commodity; and (f) separate identification of the exploration, development and production cash flows for the current period and as a time series over a defined period (such as five years). Would disclosure of this information be relevant and sufficient for users? Are there any other types of information that should be disclosed? Should this information be required to be disclosed as part of a complete set of financial statements?

Comment:

We do not agree with the following points:

(a) According to paragraph 5.32 and 5.34 of the discussion paper, interests held by equity-method investees are not to be included in said entity's required disclosures. However, in light of convergence with U.S.GAAP, we believe that such interests should be included within the scope of disclosures.

(b) We expresses concern over the sensitivity analysis required by the discussion paper, in that it will necessitate undue burden on the preparers of financial statements, and that the usefulness of such information is questionable. We believe that, in this respect, importance should be attached to sufficient research and other enquiries to determine potential impact of different assumptions on estimation of reserve quantities.

(d) In terms of the measurement of current value (fair value), it will be essential to establish thorough guidance that takes into account practical application.

(e) and (f) None of the other IFRSs make such disclosure requirements on business activities that could lead to undue burden on the preparers of financial statements.

Question 10 – Publish What You Pay disclosure proposals

Chapter 6 discusses the disclosure proposals put forward by the Publish What You Pay coalition of non-governmental organisations. The project team's research found that the disclosure of payments made to governments provides information that would be of use to capital providers in making their investment and lending decisions. It also found that providing information on some categories of payments to governments might be difficult (and costly) for some entities, depending on the type of payment and their internal information systems. In your view, is a requirement to disclose, in the notes to the financial statements, the payments made by an entity to governments on a country-by-country basis justifiable on cost-benefit grounds? In your response, please identify the benefits and the costs associated with the disclosure of payments to governments on a country-by-country basis.

Comment:

We do not agree.

We believe that it is not appropriate to put undue burden exclusively on the preparers of financial statements of this particular industry. Also, such requirements are not appropriate from the perspective of accounting standards, on the following grounds.

(a) Although such information would be useful to a certain extent, we believe that such requirements go beyond the purpose of disclosure in financial statements, as envisioned by IAS 1 *Presentation of Financial Statements.* It is inappropriate to put undue burden on the preparers of financial statements in this particular industry.

(b) If such disclosure requirements were to be made on this industry, we would need to carefully consider the necessity for making requirements for similar information in other industries. Therefore, we believe that it is necessary to consider broader issues which are beyond the scope of this project, and require consideration through the usual due process.

Yours faithfully,

Keiko Kishigami
Executive Board Member－Accounting Standards
The Japanese Institute of Certified Public Accountants