

VIEWPOINTS: Applying IFRSs in the Mining Industry

BACKGROUND

Farm-out arrangements (sometimes referred to as risk-sharing arrangements) are common in the mining industry. A farm-out arrangement typically involves an entity (i.e., the farmor) agreeing to provide a working interest in a mining property to a third party (i.e., the farmee), provided that the farmee makes a cash payment to the farmor and/or incurs certain expenditures on the property to earn that interest. For example, assume that in a farm-out arrangement the farmor has a 100% interest in a mining property in the Yukon and agrees to provide a 20% working interest in that property, provided that the farmee makes a \$100,000 cash payment to the farmor and spends \$1,500,000 on exploration expenditures on the property over the next two years.

This publication addresses the farmor's accounting for a farm-out arrangement related to a project in the exploration and evaluation (E&E) phase,¹ where the farmee earns a direct interest in the project rather than an interest in a subsidiary company that holds the project.

ISSUE

How does a farmor account for the reduction in its interest in a project in the E&E phase as a result of a farm-out arrangement?

VIEWPOINTS

IFRS 6, *Exploration for and Evaluation of Mineral Resources*, provides a temporary exemption, which permits an entity to develop an accounting policy for the recognition and measurement of E&E assets without specifically considering certain requirements in IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*. Most are of the view that a farmor may also use this exemption to develop an accounting

¹ For more information, download *Background on Different Phases of Activities of a Mining Entity* from www.cica.ca/ifrs.

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 Canadian Institute of Chartered Accountants (CICA) 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 the CICA, PDAC or the organizations represented by the task force members.

policy to account for farm-out arrangements. The following is a common policy under this view:

- The farmor uses the carrying amount of the interest before the farm-out as the carrying amount for the portion of the interest retained.
- The farmor credits any cash consideration received against the carrying amount of the portion of the interest retained, with any excess included as a gain in profit or loss.
- The farmor does not record exploration expenditures on the property made by the farmee.

Although there are other possible policies under this view and other views (e.g., the view that IAS 16, *Property, Plant and Equipment*, applies to the accounting for farm-out arrangements), there does not appear to be much diversity – the policy described is most commonly used globally.

The Mining Industry Task Force on IFRSs

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