KPMG

Insights into Mining

Adoption of IFRS 15

KPMG survey shows some challenges in applying the new revenue standard

In the first quarter of 2018, most mining companies adopted IFRS 15 *Revenue from Contracts with Customers* ("IFRS 15"). KPMG surveyed the disclosures of 25 global precious metal and base metal producers on the adoption of IFRS 15. While the impact of adoption was expected to be less significant for mining companies compared to industries with more complex revenue arrangements, we found there were some challenges in applying the new rules.

Background

IFRS 15 *Revenue from Contracts with Customers* specifies how and when an entity applying IFRS will recognize revenue. The standard also requires entities to provide users of financial statements with more informative and relevant disclosures regarding the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer. The standard provides a single, principles-based five-step model to be applied to all contracts with customers. IFRS 15 replaces IAS 11 *Construction Contracts*, *IAS 18 Revenue* and certain other IFRIC interpretations and applies to annual reporting periods beginning on or after January 1, 2018 with early adoption permitted.

Adoption

IFRS 15 offers a choice of transition options. Using the full retrospective method, an entity can choose to apply the new standard to all of its contracts and retrospectively adjust each comparative period presented in its financial statements. Alternatively, an entity can apply the modified retrospective method by recognizing the cumulative effect of applying IFRS 15 at the date of initial application and making no adjustments to its comparative information.

Of the companies that disclosed quantitative impacts due to the adoption of IFRS 15, the majority (8 out of 10) elected to apply the modified retrospective approach and therefore did not restate comparative information in their financial statements.

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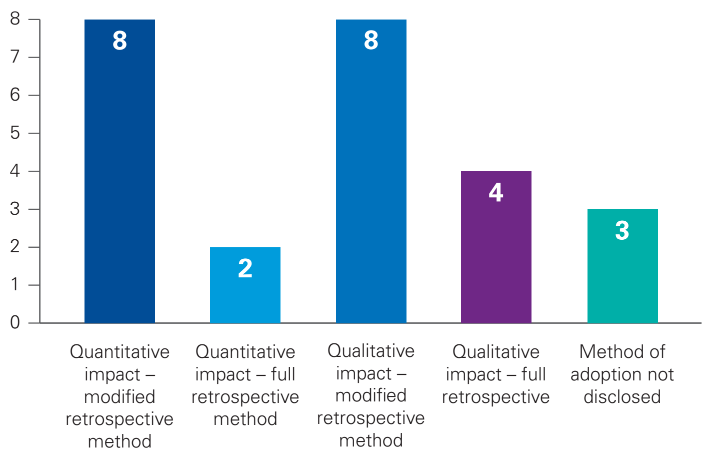
Most mining companies not quantitatively impacted by IFRS 15 still disclosed the adoption method applied, and the modified retrospective approach was again the predominant adoption approach applied (8 out of 12). Three mining companies were not quantitatively impacted by IFRS 15 and did not disclose the method of adoption applied.

Method of adoption



Source: KPMG analysis

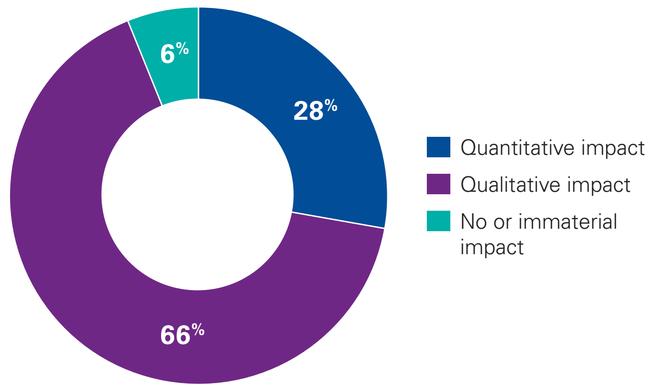
Impact on mining companies

While IFRS 15 impacted most of the mining companies surveyed in some form, there was a mix between quantitative impacts on the financial results of mining companies and impacts that had some other non-quantitative impact on mining companies' financial statements. Of the 25 companies surveyed, 10 disclosed a quantitative impact as a result of the adoption of IFRS 15 and 23 companies had non-quantitative impacts related to changes in accounting policies or amended disclosures to their financial statements. Only two companies disclosed that there was no impact or an immaterial impact as a result of the IFRS 15 transition.

The quantitative impacts related to:

- IFRS 15 impact on timing and amount of revenue recognized;
- IFRS 15 impact on streaming contracts or deferred revenue;
- IFRS 15 impact on disclosures.

IFRS 15 overall impact



Source: KPMG analysis

Timing and amount of revenue recognized

The five-step model provided under IFRS 15 may impact the timing and amount of revenue recognized for companies implementing the new standard as revenue is no longer recognized when risks and rewards of ownership pass to the customer but when a customer obtains control of the goods or services.

For the mining companies surveyed, differences in timing of recognition of revenue for the sale of metals sold at spot market price were minimal. Only one mining company disclosed an impact on timing of revenue recognition in this regard. In this instance, as a result of applying IFRS 15, revenue was recognized on settlement date (the date when control passes) and not contract date (date when risk and rewards of ownership passed).

Freight

In accordance with IFRS 15's five-step model, entities are required to identify performance obligations included in each contract. As defined under the new standard, freight services may represent a separate performance obligation. As such, upon transition mining companies were required to consider whether it may be necessary to allocate part of the transaction price to a distinct freight service, with that element being recognized when, or as, that service is provided (i.e. at a different date than the revenue for shipment of commodities). Of the 25 companies surveyed, eight disclosed that the provision of freight services represented a separate performance obligation, and therefore had an impact on timing of revenue recognition. For all eight companies, the impact of recognizing the separate performance obligation related to timing of revenue recognition was not considered material to their financial statements and accordingly, no adjustment was recorded.

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Provisional pricing

In connection with the adoption of IFRS 15, mining companies also assessed whether there were any impacts on revenue recognition related to concentrate sales under contracts containing provisional price adjustment terms. Such contracts are common in the mining industry – 15 of the mining companies surveyed sell some form of concentrate. All companies concluded that there was no change in the timing of revenue recognition as a result of the adoption of IFRS 15, as the provisional price adjustments between the point of revenue recognition and final settlement are accounted for as part of the receivable in accordance with IFRS 9 *Financial Instruments*. However, 11 out of the 15 companies updated their note disclosures to show provisional price adjustments as a separate source of revenue in line with the requirements of IFRS 15.

Streaming arrangements

Mining companies sometimes monetize a portion of future commodity production (normally future by-product production) by selling a specified portion of future production in return for an upfront payment at the time of signing the contract and ongoing payments as the commodity is produced. These arrangements are generally referred to as streaming arrangements.

Streaming arrangements are typically accounted for as either sales of the commodity (which would be contract with a customer, accounted for under IFRS 15), a financial liability in accordance with IFRS 9, or a sale of a portion of the mineral interest (which would be accounted for as a sale of an asset). Accounting for streaming arrangements is complex and highly dependent on the specific facts and circumstances of each transaction. While IFRS 15 does not provide any specific guidance on the accounting for streaming arrangements, the principals of IFRS 15 should be applied to streaming arrangements that are not accounted for as financial liabilities.

Of the 25 companies surveyed, six had streaming arrangements in place at January 1, 2018 with the majority of these companies disclosing that they account for these arrangements as sales of the commodity and account for the upfront payment as unearned revenue. Only one of the six companies with streaming arrangements did not record an adjustment to opening retained earnings as a result of the adoption of IFRS 15. The areas impacted by IFRS 15 were:

– *Significant financing component:*

  Under IFRS 15, where consideration is received in advance of the company's performance of its obligation, there is an inherent financing component in the transaction. When the period between receipt of consideration and revenue recognition is more than a year, the company is required to determine whether the financing component is significant to the contract.

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Of the five companies that disclosed an IFRS 15 impact related to streaming revenue, four had an opening retained earnings impact as a result of identifying a significant financing component in those contracts.

– *Variable consideration*

IFRS 15 requires that for contracts containing variable consideration, the transaction price be continually updated and re-allocated to the transferred goods and services. As a result of this requirement, certain mining companies we surveyed updated their accounting policies for revenue earned on streaming arrangements to require an adjustment to the transaction price per unit each time there is a change in the underlying production profile of the mine (such as an update to mineral reserves and resources which may impact the expected ounces to be delivered under the streaming arrangement). Such changes result in a retroactive adjustment to revenue in the period in which the change is made, reflecting the new production profile expected to be delivered under the streaming arrangement. This impacts the recognition of revenue related to the initial up-front payment received by companies as part of the streaming arrangements into which they had entered.

Of the six mining companies that had streaming arrangements, one showed an opening retained earnings impact to reflect the impact of variable consideration on their streaming arrangements, as it relates to a change in the expected ounces to be sold under their streaming arrangements and three companies disclosed the relevant concepts but concluded that it had no impact on their financial statements on adoption on January 1, 2018.

Additionally, four of the six companies disclosed that subsequent changes to expected deliveries under streaming arrangements will result in an adjustment to revenue in the period of change to retroactively adjust for the new quantity of ounces expected to be delivered under the contract.

– *Transfer of control*

The adoption of IFRS 15 introduced new requirements that revenue can only be recognized after the customer obtains control of a specified asset. All of the mining companies surveyed who accounted for their streaming arrangements as commodity sales contracts (i.e. contracts with a customer under IFRS 15), did not change the timing of revenue recognition on adoption of IFRS 15. However, one company, who accounted for their stream as a sale of mineral interest, determined that under IFRS 15 control transferred when they originally entered into the stream and effectively sold a portion of their mineral interest. This resulted in deferred consideration previously recognized on the balance sheet as unearned revenue prior to the adoption of IFRS 15 being recognized as an opening equity adjustment on January 1, 2018.

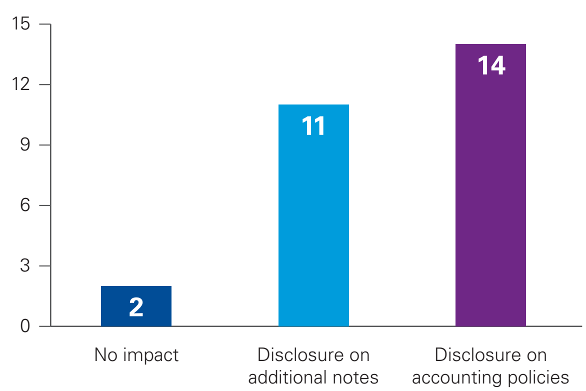
A summary of the treatment of deferral of revenue / income pre and post transition was as follows:

	Pre IFRS 15	Post IFRS 15
Deferral on balance sheet	6	5
No deferral on balance sheet	0	1

Disclosure

Of the 25 companies, 23 had a change to its financial statement disclosure as a result of the adoption of IFRS 15, either through accounting policy changes, additional information provided in the notes to the financial statements, or both. Two companies disclosed there was no impact on disclosure upon transition to IFRS 15.

Disclosure impact



Source: KPMG analysis

IFRS 15 requires an entity to disaggregate revenue recognized from contracts with customers into categories that depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors.

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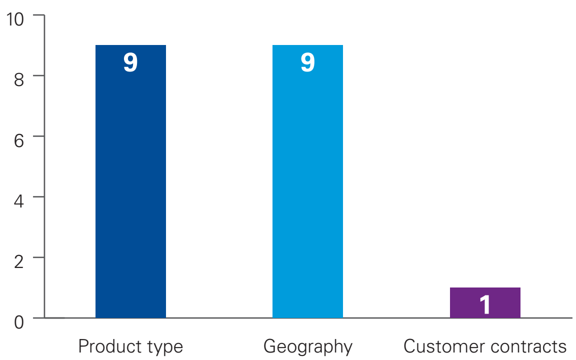
Of the 11 companies that provided additional information in the form of disaggregated information in their notes to the financial statements, the majority of areas of revenue disaggregation disclosed by companies included the following:

Additional information in financial statement notes



Source: KPMG analysis

Fourteen companies provided no additional disaggregated information in their financial statement disclosures as these companies were disclosing revenue in the segmented operations note prior to adoption of the new standard.

Recommendations

Overall, the impact of IFRS 15 on the mining companies surveyed was limited, and resulted in additional disclosures in the financial statements. Streaming arrangements continue to involve significant judgment and complexity and mining companies with such arrangements were impacted the most as a result of the adoption of IFRS 15. Since each streaming arrangement is unique, we advise companies to consult with their auditors and accounting advisors to understand the specific accounting impacts.

Contact us

If you would like to discuss this report in further detail, please contact your local KPMG professional.

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