STAFF PAPER

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IASB Meeting

Project	Extractive Activities		
Paper topic	Disclosure		
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Objective

1. Since issuing the 2010 *Extractive Activities* Discussion Paper (Discussion Paper), the Board has:
   - (a) issued the *Conceptual Framework for Financial Reporting* in March 2018; and
   - (b) commenced the Disclosure Initiative as part of Better Communication in Financial Reporting—the objective of which is to improve the effectiveness of communication of information in entities' financial statements.
2. The purpose of this paper is to summarise what effect, if any, the projects under the Disclosure Initiative umbrella and the 2018 *Conceptual Framework for Financial Reporting* (2018 *Conceptual Framework*) have on the disclosure considerations and proposals in the Discussion Paper.
3. There are no questions for the Board in this Agenda Paper, but the staff would welcome any comments from Board members.

Overview

4. This paper is structured as follows:

(a) Summary (paragraphs 5–7);

(b) Background (paragraphs 8–22);

(c) 2018 *Conceptual Framework for Financial Reporting* (paragraphs 23–25);

(d) Disclosure Initiative (paragraphs 26–36);

(e) Management Commentary (paragraphs 37–40);

(f) Appendix A—Extracts from ***October 2010 Agenda Paper 7A Comment letter summary***;

(g) Appendix B—Extracts from the 2018 *Conceptual Framework for Financial Reporting*.

Summary

5. Following the issue of clarifications and guidance around the application of materiality to disclosure, the specific disclosure proposals in the Discussion Paper as detailed in paragraphs 8-10 below would not require disclosure by an entity if the information resulting from a specific disclosure proposal was immaterial (paragraphs 30–31).

6. Some of the disclosure objectives and specific disclosure proposals in the Discussion Paper may no longer be appropriate. This is because:

   (a) in applying the new guidance in Chapter 7 of the 2018 *Conceptual Framework*, the proposals for disclosure objectives and disclosure of specific information may no longer be appropriate (see paragraphs 23-25); and

   (b) the way in which disclosure objectives are written has developed since 2010 and may be subject to change again based on the outcome of the testing of the guidance for the Board to use when developing and drafting disclosure objectives and requirements (see paragraphs 32-36).

7. Staff also observe that the disclosure needs of stakeholders may have changed since 2010 so that some of the disclosure objectives and specific disclosure proposals may no longer be appropriate.

Background

Disclosure objectives

8. In Chapter 5 of the Discussion Paper, the project team proposed that the disclosure objectives for extractive activities should be to enable users of financial statements to evaluate:

   (a) the value attributable to an entity's minerals or oil and gas properties;

   (b) the contribution of those assets to current period financial performance; and

   (c) the nature and extent of risks and uncertainties associated with those assets.

Disclosure of specific information

9. The project team proposed 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).

10. The project team also proposed that entities should disclose proved reserves and, separately, the sum of proved and probable reserves so that users are provided with both a high confidence estimate and a best estimate of the quantity of minerals or oil and gas that the entity expects to be able to economically extract. The project team suggested that entities might also wish to disclose information on their resource estimates.

Questions in the Discussion Paper

11. Questions 8 and 9 of the Discussion Paper asked respondents the following:

Question 8 – Disclosure objectives

In Chapter 5 the project team proposes that the disclosure objectives for extractive activities are to enable users of financial reports to evaluate:

a) the value attributable to an entity's minerals or oil and gas properties;

b) the contribution of those assets to current period financial performance; and

c) the nature and extent of risks and uncertainties associated with those assets.

Do you agree with those objectives for disclosure? If not, what should be the disclosure objectives for an IFRS for extractive activities and why?

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 be required to be disclosed as part of a complete set of financial statements?

Summary of feedback received on the Discussion Paper

12. The following is a summary of the comment letter analysis which was presented to the Board in October 2010[1]. Extracts of the detailed comment letter analysis from October 2010 are located in Appendix A.

Disclosure objectives

13. Most respondents supported the disclosure objectives listed in paragraph 8.

14. Respondents also commented on whether the disclosure of reserve and resource information should be included in the notes to the financial statements or in management commentary. In the Discussion Paper, the project team proposed that the disclosures could be presented elsewhere in information published with the financial statements rather than in the notes to the financial statements.

15. The issue is relevant because the securities laws and regulations in most jurisdictions require an audit opinion on the financial statements. Many minerals and oil and gas entities and industry consultants advised that auditing reserve and resource disclosures would impose a significant cost, be time intensive and would divert geological and engineering expertise away from business functions and towards compliance functions. Most users consulted by the project team agreed that the cost of auditing such disclosure would outweigh the benefits they would obtain from that assurance process.

Disclosure of specific information

16. Many respondents, including mining entities and users, supported the disclosure of proved and probable reserve quantities. However, the views from the oil and

[1] See ***October 2010 Agenda Paper 7A***

gas entities varied—some supported the proposal while others did not support the disclosure of probable reserves.

17. Respondents also agreed with disclosing reserve quantities on a disaggregated basis although there were different views on the appropriate level of geographical disaggregation.

18. Almost all respondents agreed that information on the main assumptions used in estimated reserves and quantities should be disclosed. However, most respondents disagreed with the proposal to supplement the reserves quantity disclosure with a sensitivity analysis. They considered that the sensitivity analysis would have limited practical benefit and would be excessively costly to prepare.

19. There was significant support for entities to disclose a reconciliation of the change in their reserve quantity estimates from year-to-year.

20. Almost all respondents disagreed with disclosing information about fair value or another type of current value measurement of an entity's minerals or oil and gas properties for the same reasons for not supporting using fair value as a measurement basis.

21. Many respondents expressed general support for the disclosure of information about revenues and costs, although views differed on the level of detail that should be provided.

22. Despite most respondents supporting the disclosure proposals, many expressed the following concerns about the overall disclosure proposals:

    (a) the amount of disclosure proposed is excessive and would be costly to prepare;

    (b) some of the proposed disclosures appear to be responding to the wants rather than the needs of users; and

    (c) some of the proposed disclosures either duplicate or are inconsistent with existing disclosure requirements in capital market regulations.

2018 *Conceptual Framework for Financial Reporting*

23. The 2018 *Conceptual Framework* introduced a chapter on presentation and disclosure (see Appendix B), for which there is no equivalent in the 2010 *Conceptual Framework for Financial Reporting*. This chapter provides guidance on:

    (a) presentation and disclosure as communication tools (see paragraphs 7.1–7.3 of the 2018 *Conceptual Framework*);

    (b) presentation and disclosure objectives and principles (see paragraphs 7.4–7.6 of the 2018 *Conceptual Framework*);

    (c) classification (see paragraphs 7.7–7.19 of the 2018 *Conceptual Framework*); and

    (d) aggregation (see paragraphs 7.20–7.22 of the 2018 *Conceptual Framework*).

24. In particular, paragraph 7.3 of the 2018 *Conceptual Framework* states that:

> …when making decisions about presentation and disclosure, it is important to consider whether the benefits provided to users of financial statements by presenting or disclosing particular information are likely to justify the costs of providing and using that information.

25. Staff consider that, in applying the guidance in Chapter 7 of the 2018 *Conceptual Framework*, it is possible that some of the proposals for disclosure objectives and disclosure of specific information may no longer be appropriate.

Disclosure Initiative

26. In January 2013 the Board set up a public discussion forum on financial reporting disclosure following feedback from the 2011 Agenda Consultation. Based on the forum, the Board learnt that there are three main concerns about information disclosed in the financial statements: not enough relevant information, too much irrelevant information and ineffective communication of information. These are collectively referred to as the 'disclosure problem'.

27. Consequently, in 2013, the Board started the Disclosure Initiative, a package of projects that included targeted actions to improve the effectiveness of disclosures in IFRS Standards and to help entities apply better judgment when preparing financial statements.

28. As part of the Disclosure Initiative, the Board has completed a number of projects, that staff consider may have an effect on the analysis and project proposals in relation to disclosure (see paragraphs 30–31):

    (a) December 2014 Amendments to IAS 1 *Presentation of Financial Statements*—included amendments designed to encourage entities to apply judgment in determining what information to disclose in their financial statements. These amendments became effective for annual periods beginning on or after 1 January 2016;

    (b) September 2017 IFRS Practice Statement 2 *Making Materiality Judgments* (Materiality Practice Statement)—provides entities with guidance in deciding whether information is material when preparing general purpose financial reports based on IFRS Standards; and

    (c) October 2018 *Definition of Material* (Amendments to IAS 1 and IAS 8)—clarified the definition of material and how it should be applied by:

        (i) including in the definition guidance that until now has featured elsewhere in IFRS Standards;

        (ii) improving the explanations accompanying the definition; and

        (iii) ensuring that the definition of material is consistent across all IFRS Standards.

        These amendments will become effective for annual periods beginning on or after 1 January 2020 with early application permitted.

29. The Board also has additional Disclosure Initiative projects on its work plan, one of which may affect the considerations and proposals for disclosure. The Targeted Standards-level Review of Disclosures project (TSLR project) aims to help

stakeholders improve the usefulness of disclosures for the primary users of financial statements (see paragraphs 32–36).

Materiality

30. The completed projects listed in paragraph 28 focus on the concept of materiality. These projects are a result of the Board's efforts to help entities make better materiality judgements to assist in addressing the 'disclosure problem' (see paragraph 26). In doing so, an entity will be better equipped to determine what information to disclose in their general purpose financial statements. For example:

    (a) the 2014 amendments to IAS 1 clarify that materiality applies to the financial statements as a whole and that the inclusion of immaterial information can reduce the usefulness of financial disclosures; and

    (b) the Materiality Practice Statement discusses and demonstrates an approach to making materiality judgements (ie 'the four-step materiality process').

31. Consequently, there is greater clarity that an entity would not be required to disclose the information required by the specific disclosure proposals as detailed in paragraph 9 and 10 if that information would be immaterial. This may address concerns some respondents had regarding the specific disclosure proposals being onerous (see paragraph 22).

Targeted Standards-level Review of Disclosure

32. In its response to the Board's request for an update on Extractive Activities, the Canadian Accounting Standards Board (AcSB) suggested staff consider revisiting the disclosure objectives and specific disclosure proposals in light of the draft disclosure framework developed as part of the TSLR project.

33. To help entities make more useful disclosures, the TSLR project is seeking to:

    (a) develop guidance for the Board itself to use when developing and drafting disclosure requirements (ie the 'draft disclosure framework'). The Board will initially develop this guidance as a set of Board decisions, and it will seek formal stakeholder feedback when the guidance is subsequently used as part of standard-setting; and

(b) test the draft guidance for the Board by applying it to the disclosure requirements in IAS 19 *Employee Benefits* and IFRS 13 *Fair Value Measurement*. The aim of the test is to improve the guidance for the Board and the disclosure requirements in the selected Standard(s).

34. The draft disclosure framework to which the AcSB referred to is the guidance for the Board itself to use when developing and drafting disclosure objectives and disclosure requirements and can be summarised in three steps:

(a) Step 1—how the Board will use disclosure objectives. In its May 2018 meeting, the Board tentatively decided to[2]:

(i) explicitly state the objective(s) of each disclosure requirement and clearly link each requirement with the related objective(s); and

(ii) use high-level, catch-all disclosure objectives within individual Standards to prompt entities preparing financial statements to consider as a whole the disclosure relating to a topic and whether the information provided meets users' information needs for that topic;

(b) Step 2—how the Board will develop the content of disclosure objectives and requirements. In its June 2018 meeting, the Board tentatively decided that, when developing disclosure objectives and requirements[3]:

(i) a member of the IFRS Taxonomy team be assigned to each of the Board's active projects in an advisory capacity; and

(ii) the Board use a focused methodology to develop the content of disclosure objectives and requirements (ie stakeholder engagement);

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[2] See ***May 2018 Agenda Paper 11B***

[3] See ***June 2018 Agenda Paper 11C***

(c) Step 3—how the Board will draft disclosure objectives and requirements. In its July 2018 meeting, the Board tentatively decided that effective communication can be addressed through three areas[4]:

(i) the use of language;

(ii) formatting and presentation of disclosure objectives and requirements within IFRS Standards; and

(iii) leveraging requirements and guidance across IFRS Standards and other IFRS publications.

35. The TSLR project is still in progress and consequently the draft guidance for the Board itself to use when developing and drafting disclosure objectives and requirements is in the process of being tested and may be subject to change.

36. However, if the draft guidance were to be applied to the project team disclosure proposals in the Discussion Paper, it could result in different outcomes. This is because:

(a) the disclosure objectives which were proposed by the project team may not be appropriate or complete when considering:

(i) ‘disclosure objectives’ as defined using the draft guidance; and

(ii) the way in which writing disclosure objectives has evolved since 2010—for example, disclosure objectives are more descriptive and specific in newer Standards;

(b) staff would seek stakeholder engagement to better understand what needs to be disclosed and why. The disclosure needs of stakeholders may have changed since 2010 so that some of the specific disclosure proposals may no longer be appropriate.

[4] See ***July 2018 Agenda Paper 11C***

Management Commentary

37. In November 2017, the Board added a project to its agenda to revise and update IFRS Practice Statement 1 *Management Commentary* (IFRS Practice Statement 1).

38. IFRS Practice Statement 1 provides a broad, non-mandatory framework for the presentation of management commentary that relates to financial statements prepared applying IFRS Standards. IFRS Practice Statement 1 focuses on what is relevant to the unique circumstances of the entity by setting out the principles, qualitative characteristics and elements of management commentary that are necessary to provide users of financial reports with useful information.

39. The project to update IFRS Practice Statement 1 will explore opportunities to support more rigorous discussion in management commentary to help users better understand the factors affecting the future performance of entities. The project will consider how management commentary could complement and support the financial statements. In particular the project will consider:

    (a) developments from other narrative reporting; and

    (b) whether and how to address acknowledged gaps in narrative reporting practice.

40. The Management Commentary project will be monitored to assess if any outcomes may affect the analysis and project proposals for disclosure of extractive activities.

Appendix A—Extracts from *October 2010 Agenda Paper 7A Comment letter summary*

General concerns

A1. Most respondents supported those disclosure objectives. However, many respondents expressed the following general concerns with the disclosure proposals:

(a) the amount of disclosure proposed is excessive and would be costly to prepare;

(b) some of the proposed disclosures appear to be responding to the wants rather than needs of users;

(c) the proposed disclosures would represent a significant change in disclosure practices for oil and gas entities that have only recently updated their reserve reporting systems and processes to comply with the US SEC's disclosure requirements that were revised in 2008; and

(d) some of the proposed disclosures either duplicate or are inconsistent with existing disclosure requirements in capital market regulations. Because of this risk, respondents urged the Board to work with regulators and the FASB in developing the disclosure requirements for an IFRS.

Location of the disclosures and audit implications

A2. Respondents also commented on whether the disclosure of reserve information should be included in the notes to the financial statements or in management commentary. The issue is relevant because the securities laws and regulations in most jurisdictions require an audit opinion on the financial statements and notes. In the DP, the project team proposed that, consistent with existing practices, the disclosures could be presented elsewhere in information published with the financial statements rather than in the notes to the financial statements. This is because many minerals and oil and gas entities and industry consultants advised that auditing reserve disclosures would impose a significant cost, be time intensive and would divert geological and engineering expertise away from business functions and towards compliance functions. Furthermore, most users consulted by the project team agreed that the costs of auditing reserves disclosure would outweigh the benefits they would obtain from that assurance process.

A3. Respondents to the DP agreed with the project team's proposal to locate the disclosures outside the notes to the financial statements. However, a respondent commented that a change in location of the disclosures specified by a future IFRS may not necessarily mean that those disclosures would not be required to be audited. The respondent said:

> *The IASB should be mindful of the interaction of national law and IFRS. Information required to be included in the financial statements by an IFRS may well come*

> *automatically into the scope of the audit opinion on the financial statements, whether or not this was the Board's intention. (CL#65)*

A4. As an alternative to specifying disclosure requirements in a future IFRS, some respondents suggested that the Board should publish its views on disclosures in a 'best practice' guide that would form part of the Board's forthcoming management commentary IFRS Practice Statement.

Specific disclosure proposals

Quantities of reserves

A5. Many respondents, including mining entities and users, supported the disclosure of proved and probable reserve quantities.

A6. However, the views from respondents from the oil and gas industry varied. Some respondents supported the project team's proposals. Other respondents, typically entities that are among the largest oil and gas entities in the world, did not support the mandatory disclosure of probable reserves. As one such respondent explained:

> *Mandatory reserve quantity disclosures should be limited to proved reserves. The disclosure of probable reserves should be optional given the inherent increase in uncertainty associated with probable reserves, the significant added cost for companies to develop high quality and consistent estimates, the diversity of practice in the determination of probable reserves, and the differences in how those reserves are used by companies in making future investment decisions. (CL#32)*

A7. Respondents agreed with disclosing reserve quantities on a disaggregated basis although there were different views on the level of geographical disaggregation that is appropriate. Some respondents suggested that a future standard should not be too prescriptive in defining the level of aggregation for reserves disclosures. Instead, they suggested including a principle to indicate that reserve quantities should be disclosed at the level of detail that is sufficient to understand an entity's operations.

A8. In late 2008, the US SEC revised its oil and gas reserve definition and disclosure rules. Among other things, the revised rules require more detailed geographical disclosure of reserve quantities (although potentially less detailed than the project team proposes) and permit the voluntary disclosure of probable reserve quantities. Thus, in addition to the feedback received in response to this DP, the disclosure practices that emerge from these revised requirements could also inform the Board in any future deliberations on reserve disclosures.

Main assumptions

A9. The majority of respondents agreed that information on the main assumptions used in estimating reserves quantities should be disclosed. The main concern identified in responses related to the disclosure of the commodity price that is used to estimate reserves. The project team proposed that reserve estimates should be prepared using a market participant's assumption of the commodity price. That approach would seem to be consistent with the Board's fair value measurement hierarchy. However, many industry respondents as well as almost all users consulted during the research project expressed a strong preference for using a historical price assumption (eg a 12 month or 3 year historical average price). Although a reserves estimate prepared using a forecast commodity should produce a more representatively faithful estimate of the economically recoverable quantities of minerals or oil and gas, the arguments for using a historical price include:

(a) a historical price can be determined objectively and thus that component of the reserves estimate can be prepared consistently between entities; and

(b) an entity might be disclosing commercially sensitive information if it discloses a forecast price assumption that resembles its own price assumption (ie similar to a Level 3 input).

A10. Most respondents disagreed with the project team's proposal to supplement the reserves quantity disclosure with a sensitivity analysis. They considered that the sensitivity analysis would have limited practical benefit and would be excessively costly to prepare. For example:

> *The determination of reserves (and resources) information is a complex process involving numerous variables, assumptions and processes. In practice, determining reserves is very dependent on long-term prices for the contained commodity as it determines the 'cut-off' between economic and uneconomic resources. The calculation process can therefore be extremely laborious and in some sectors it can take many months to reflect new variables, particularly long term commodity prices. Furthermore, the outcomes from further exploration cannot be determined in advance even though it has a direct impact on reported reserves.*
>
> *Because of these factors, we believe the sensitivity analysis disclosure cannot be justified due to cost-benefit concerns and also because the information may not be useful or relevant to the users of the financial statements because of the uncertainties involved. We therefore recommend that the Board relies on the existing disclosure requirements relating to significant judgements and sources of estimation of uncertainty already contained in* IAS 1 *Presentation of Financial Statements. (CL#90)*

Reconciliation of changes in reserve quantities

A11. There was significant support for entities to disclose a reconciliation of the changes in their reserve quantity estimates from the previous year to the current year. A user representative remarked on the importance of a reconciliation separately showing the effects of changes and changes in facts. That respondent provided an example of a tabular reconciliation format that could be used to communicate that information.

Current value measurement disclosures

A12. Almost all respondents disagreed with disclosing information about fair value or another type of current measurement of an entity's minerals or oil and gas properties. Many suggested that the reasons against measuring those properties at fair value in the statement of financial position also apply to the disclosure of such measurements. The following comment from a user identified some of the challenges with such a measurement:

> *…we have serious reservations about the practical feasibility and use of such disclosures. Given the complexity of interrelationship between commodities that naturally co-exist (co- and by-products), commodity prices, costs, taxation, exchange rates, discount rates, production rates, stripping ratios, grade decay and restitution costs, the usefulness of any disclosure with regard to value (as opposed to the revenues and costs in any particular historic reporting period) will be limited unless all of the underlying assumptions are also disclosed. Yet we would not regard it as reasonable to expect a company to disclose these assumptions in a formal public document, as they are commercially sensitive. This is true for all companies, whether large or small. (CL#139)*

Disclosure of production revenues and exploration, development and production cash flows

A13. Many respondents expressed general support for the disclosure of information about revenues and costs, although views differed on the level of detail that should be provided (eg geographic breakdowns). In addition, some suggested that the Board would need to consider:

(a) defining the costs that should be included in each category;

(b) whether the costs should be presented as cash flow information or as accrual information; and

(c) whether these disclosures should include (or be limited to) performance measures such as unit prices and unit production costs.

Appendix B—Extracts from the 2018 *Conceptual Framework for Financial Reporting*

Presentation and disclosure as communication tools

7.1 A reporting entity communicates information about its assets, liabilities, equity, income and expenses by presenting and disclosing information in its financial statements.

7.2 Effective communication of information in financial statements makes that information more relevant and contributes to a faithful representation of an entity's assets, liabilities, equity, income and expenses. It also enhances the understandability and comparability of information in financial statements. Effective communication of information in financial statements requires:

(a) focusing on presentation and disclosure objectives and principles rather than focusing on rules;

(b) classifying information in a manner that groups similar items and separates dissimilar items; and

(c) aggregating information in such a way that it is not obscured either by unnecessary detail or by excessive aggregation.

7.3 Just as cost constrains other financial reporting decisions, it also constrains decisions about presentation and disclosure. Hence, in making decisions about presentation and disclosure, it is important to consider whether the benefits provided to users of financial statements by presenting or disclosing particular information are likely to justify the costs of providing and using that information.

Presentation and disclosure objectives and principles

7.4 To facilitate effective communication of information in financial statements, when developing presentation and disclosure requirements in Standards a balance is needed between:

(a) giving entities the flexibility to provide relevant information that faithfully represents the entity's assets, liabilities, equity, income and expenses; and

(b) requiring information that is comparable, both from period to period for a reporting entity and in a single reporting period across entities.

7.5 Including presentation and disclosure objectives in Standards supports effective communication in financial statements because such objectives help entities to identify useful information and to decide how to communicate that information in the most effective manner.

7.6 Effective communication in financial statements is also supported by considering the following principles:

(a) entity-specific information is more useful than standardised descriptions, sometimes referred to as 'boilerplate'; and

(b) duplication of information in different parts of the financial statements is usually unnecessary and can make financial statements less understandable.

…