

# Ontario's Office of the Comptroller General, Office of the Provincial Controller Division's response to IPSASB's Exposure Draft (ED) 92: "Tangible Natural Resources"

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Following is Ontario's Office of the Comptroller General, Office of the Provincial Controller Division's (Ontario's OCG/OPCD) response to IPSASB's Exposure Draft 92 (ED 92) on Tangible Natural Resources.

The Province of Ontario follows the standards in the CPA Canada Public Sector Accounting (PSA) Handbook in the preparation of its public accounts. However, considering the Public Sector Accounting Board (PSAB) in Canada has adopted an international strategy of "adapt IPSAS" when developing new standards and has changed its GAAP hierarchy, where the PSA Handbook is silent, to require IPSAS to be the prime secondary source of GAAP, Ontario's OCG/OPCD considers it important to communicate our views on certain IPSASB issued documents for comment. As the PSA Handbook has no specific guidance on the accounting for natural resources, and considering there is limited preparer representation on IPSASB, following is Ontario's OCG/OPCD position on the content of Exposure Draft 92, Tangible Natural Resources. We have chosen to provide overall comments rather than to respond directly to the specific questions included in the Exposure Draft.

As background, Governments in Canada own large quantities of land including parks. Ontario's crown land represents 87% of the Province (<https://www.ontario.ca/page/crown-land>). Ontario Parks manages some 340 provincial parks. In area, Ontario is approximately 1.076 million km<sup>2</sup>. There are over 30,000 known species in Ontario. Scientists have assessed the status of 17,867 of them. Of these, 9,918 have been categorized broadly as either being secure or of conservation concern. Ontario therefore controls and is populated by a large number and quantity of natural resources.

Ontario's OCG/OPCD strongly encourages IPSASB to revisit the objective of this project and to consider whether the proposals in ED 92 have achieved what was intended. Ontario's OCG/OPCD has concerns that the reporting of tangible natural resources by governments under this standard will result in misleading reporting for financial statement users and be extremely onerous to implement. Our two main concerns are as follows:

### **Reporting of tangible natural resources will be misleading**

IPSASB undertook this project as governments often have little idea of the monetary value of natural resources prior to granting the right to exploit or extract these resources to third parties. Guidance was to encourage better fiscal and environmental decisions. Instead IPSASB has developed ED 92, guidance addressing the recognition, measurement and disclosure of tangible natural resource held for conservation. Natural resources held for conservation are being managed and protected from degradation. Rights to exploit or extract these resources are not being granted to third parties. Conservation is maintaining the current state of a tangible natural resource for the benefit of its citizens in future generations. The government's role is that of stewardship. Guidance being proposed doesn't reflect the purpose and objective of natural resources held for conservation. It will not result in better fiscal, environmental or policy decisions.

Recording natural resources held for conservation on the Statement of Financial Position suggests a government is controlling resources beyond what is truly available to meet its future financial obligations. While these resources do have operational capacity as they assist in reaching sustainable development and climate change objectives, they are largely non-depreciable and therefore will not need to be replaced, nor will they be used to pay obligations. Assigning a monetary value is not appropriate to understand a government's financial position or its future financial needs. It will also not demonstrate stewardship of a government's tangible natural resource as only limited such resources will be reported due to measurement uncertainty. It results in some tangible natural resources being recorded at market value or replacement value which provides no benefit to financial statement users. These valuations are very subjective and provide no purpose for decision making.

Ontario's OCG/OPCD therefore encourages IPSASB to amend its proposed guidance in ED 92 to reflect the purpose and objective of natural resources held by governments for conservation. We have included two alternatives later in our response letter which will better meet financial statement user needs, allow governments to discharge their stewardship responsibilities, while also considering costs versus benefits for financial statement preparers.

## Guidance will be extremely onerous to apply

Ontario's OCG/OPCD is very concerned about applying the requirements in ED 92. As a reminder we have some 340 provincial parks and 30,000 species. This is just a start to the natural resources held by the Province. ED 92 would require the Province to analyze for each of its parks and other natural resources:

- Their use and any programs under which it is being conserved and managed, and consequentially the unit of account,
- Control of the resource, and
- Basis of measurement or alternatively why a basis of measurement is not able to be determined.

Based on this analysis, the Province would need to determine: under which IPSAS the particular natural resource is addressed, whether recognition criteria are met, and whether the unit of account is appropriate or needs to be more detailed. Many of these assessments are subjective. Each of these assessments takes time. Determining the unit of account may result in such analysis being required for multiple components of the park. One park could contain thousands of different types of subsoil resources, living resources and water. There are over 30,000 known species in Ontario. Each of these resources is somewhat different regarding its societal and environmental purpose and may be managed under different government programs. A significant initial and annual effort will be required to review and update quantities of natural resources, depreciation periods, impairments, measurements, etc. A rebuttable presumption does not remove the need for preparers to consider the life of each resource. Annual updates will take considerable time and effort. Depreciation and impairment expenses will introduce budgeting challenges and appropriation issues that are not likely to be well understood.

The application guidance suggests by focusing on programs relating to naturally occurring items, an entity will not need to individually analyze each naturally occurring item within its jurisdiction. This shows a lack of understanding of the number and diversity of government programs. Auditors will expect to see how a government has addressed completeness with respect to implementation of this standard. Demonstrating completeness will be a significant challenge. The standard shows a lack of understanding of the operations of government, and the resulting challenges, effort and time that will be required.

The application and implementation guidance in ED 92 is not sufficiently detailed to truly assist a preparer government in adopting this standard for example only a superficial case is considered in relation to determining the appropriate unit of account. We would recommend IPSASB provide a detailed analysis for a sample park. Additionally, IPSASB should develop a full listing of subsoil resources and living resources that need to be considered so both the

Board and stakeholders are aware of the extent of the analysis that may in some cases be required.

Therefore, Ontario's OCG/OPCD both considers the proposed reporting of tangible natural resources held for conservation to be misleading to the public and other financial statement users, and extremely onerous to implement and apply. It would result in the use of a significant amount of public funds and not properly reflect how a government is managing its natural resources held for conservation. The cost of implementation will greatly exceed any benefit provided.

### **Alternatives to report on natural resources held for conservation**

As mentioned IPSASB should revisit the objective of this project and if reporting natural resources held for conservation is the objective, Ontario's OCG/OPCD would strongly encourage the Board to consider developing some general note disclosure requirements and/or introduce voluntary reporting outside of financial statements. These approaches may be considered together or as alternative approaches.

#### *1. Develop general note disclosure requirements*

General purpose financial statements are intended to assist governments in fulfilling their reporting objective of accountability (i.e. did the government do what it said it would do). General purpose financial statements are by nature general purpose, they are not intended to meet the needs of all stakeholders. There is a tradeoff between complexity and understandability when developing reporting requirements. General purpose financial statements are not intended to be at a granular level but rather indicate the overall financial position and results of operation of the government. These statements are therefore referred to as general purpose.

Ontario's OCG/OPCD considers that when governments purchase a parcel of land, they are acquiring its associated natural resources as well. The land would be reported at cost. Historical cost is the primary basis of measurement in the PSA Handbook. The cost of a piece of land with known natural resources reflects those natural resources. The land as a whole would be inventoried and recorded on the financial statements and therefore be subject to stewardship and accountability. This should be a sufficient level of detail for financial statement users of general-purpose financial statements. For crown lands not purchased or contributed to the Province, general disclosure to provide awareness should be sufficient. These lands are being held for conservation.

The PSAB recently issued an Exposure Draft, Tangible Capital Assets. In this Exposure Draft, PSAB indicates "... acknowledges that works of art and historical treasures are property that has cultural, aesthetic or historical value that is worth preserving perpetually. However, given

the challenges associated with determining a reasonable estimate of the future benefits associated with such property, there is no recognition in a public sector entity's financial statements. The existence of such property is disclosed in the notes to the financial statements." Works of art and historical treasures are similar to tangible natural resources held for conservation in that government is acting as stewards for both these type of items and there is significant challenges in estimating future benefits. Tangible natural resources should therefore be similarly not recognized in financial statements, rather disclosed in the notes.

Therefore, if public awareness of the natural resources a government holds for conservation is the objective of this IPSASB project, Ontario's OCG/OPCD would encourage the Board to develop some general note disclosure requirements to be included in general purpose financial statements. Disclosure would inform the public the government is holding land for conservation for which the government is acting as steward over its maintenance for future generation. This is sufficient detail to be included in general purpose financial statements.

## *2. Develop guidance for voluntary reporting outside of financial statements*

Inventorying of natural resources, estimating quantities and/or values and demonstrating stewardship of individual natural resources held for conservation seems much more suited for voluntary reporting outside of financial statements. Reporting which are management's best estimate and do not require to be audited. For example, in the Canadian Public Sector Accounting Handbook, there is Statement of Recommended Practice (SORP)-3, *Assessment of Tangible Capital Assets*, for public sector entities that choose to prepare and report on the physical condition of their tangible capital assets. This guidance is voluntary and provides detailed information, beyond the mandate of public accounts. We consider reporting on natural resources to be better suited for reports outside of financial statements prepared by management on a best effort basis.

Therefore, Ontario's OCG/OPCD recommends IPSASB develop note disclosure requirements for general purpose financial statements and/or guidance for voluntary reporting outside of financial statements to report on natural resources held by a government for conservation purposes.

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Some other comments Ontario's OCG/OPCD has on ED 92 are:

- Paragraph 6. discusses classes of tangible natural resources, while paragraph 11. includes a discussion on units of account. Two different groupings of natural resources creates unnecessary complexity and confusion for financial statements preparers and users.

- When there is no financial capacity but there is operational capacity for a natural resource, how do you determine a valuation, how do you put a price on nature when it offers so many benefits, such as education, tradition, spiritual health, and mental well-being? How do you audit such valuations when these determinations and inputs are subjective? Historical cost is the primary basis of measurement in the PSA Handbook. The application and implementation guidance does not provide sufficient details to assist preparers in determining measurement.
- We also have concern regarding service potential in relation to natural resources considering the objective of sustainable development. Service potential is the capacity to provide services that contribute to achieving the entity's objectives without necessarily generating net cash inflows. Most natural resources assist in reaching sustainable development and climate change objectives. For example, forests have service potential as they contribute to biodiversity which in turn leads to maintaining air, water and soil quality. Most controlled natural resources will therefore meet the definition of an asset. They may not meet the recognition criteria due to measurability and therefore be unrecognized assets, but they would be considered to be assets. This would require note disclosure as proposed in ED 92 including: the difficulties in obtaining a reliable measurement that prevented recognition; the significance of the unrecognized natural resource(s) in relation to delivery of the entity's objectives; and information regarding their nature and quantities. This would be an onerous exercise as there may be many unrecognized natural resources with little benefit provided to the financial statement users. Both recording and/or detailed disclosure might also suggest to financial statement users the ability to monetize these natural resources which is not the intent, and which would be at the expense of climate change and conservation objectives.

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Ontario's OCG/OPCD appreciates the opportunity to respond to IPSASB to assist in their deliberations on this matter. I would be pleased to elaborate on any of the above comments. Thank you for your consideration.