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### **Invitation to Comment: Draft Comment Letter – Third Agenda Consultation**

We welcome the opportunity to provide input on the Draft Comment Letter. Early engagement to influence IASB activities is an important part of the UK's endorsement processes.

KPMG LLP is part of a global network of firms. Views on IFRSs are determined globally by KPMG International Standards Group. The KPMG network of firms' response to the Third Agenda Consultation has not yet been finalised and will be provided publicly to the IASB in due course. In advance of the finalisation of global views the comments in this letter are the preliminary views of KPMG LLP only.

We agree with the themes identified by the UKEB as priority areas and support the thematic approach proposed.

Narrative reporting is an important part of communicating the information that users need. Numerical financial statement information cannot provide all of that information. This is particularly the case in the priority areas, for example:

- A range of different information is relevant to the communication of climate risks and performance. Financial statement information on climate risks is only one part of the information picture.
- There are "intangible" value drivers in modern businesses that inevitably will not meet any re-worked definition of intangible assets. We expect that narrative reporting will have an increasingly important role to play in explaining these drivers.

As such, we don't agree that the project on management commentary should be paused or discontinued. The IASB, working with the ISSB, have an opportunity to develop a global approach to narrative reporting to the benefit of capital markets.

We also disagree with some of the specific recommendations in the Draft Comment Letter as explained in our detailed responses to the questions posed in the invitation to comment in Appendix 1.

Please contact us if you wish to discuss this response further. Contact details are set out in a separate document.

Yours faithfully

KPMG LLP

## Appendix 1: Response to specific questions in the Invitation to Comment

### A Strategic direction and allocation of resources

1. Do you agree with the UKEB's recommendations in those paragraphs [A1 and A2 of the Draft Comment Letter]? Please explain why or why not.

We agree that the allocation of resource is broadly appropriate. However, we also agree with the UKEB that it is important that the IASB's resource planning includes flexibility to address interaction with the proposed ISSB. We also believe it will be important for the IASB and ISSB to set clear processes for working together to avoid duplication and to support coherent reporting.

See our response to question 7 for comments regarding UKEB recommendations of projects to be paused (A2(c)).

### B Criteria for assessing the priority of financial reporting issues that could be added to the Board's work plan

2. Do you agree with the UKEB's recommendations in those paragraphs [A3-A5 of the Draft Comment Letter]? Please explain why or why not.

We generally agree with the criteria set out in the IASB's RFI. However, we also agree with the recommendations of the UKEB in paragraphs A3(b), A4 and A5 of the Draft Comment Letter.

We agree with the UKEB that there is a risk that application issues are inadvertently captured by second criterion [paragraph A3(a) of the Draft Comment Letter]. However, we think that the re-drafting proposed by the UKEB would mean that the criterion inappropriately focusses on the accounting standards without taking into account whether issues in the standards actually result in significant problems for users in practice. For example, there may be accounting standards that contain inconsistencies or are hard to apply, but which either do not have a material effect in practice, or for which accounting practice has developed such that reporting meets user needs despite the standard-level deficiency. We therefore do not agree that criterion 2 should be redrafted in a way that removes reference to reporting in practice. If the criterion is re-drafted to address the risk of capturing application issues, then we would recommend wording such as "whether there is a deficiency in the way companies report the type of transaction or activity and whether that deficiency can be remedied through standard-setting". Such wording would retain the link to issues in accounting practice, but would also address the importance of a standard-setting solution.

### C Priority projects

3. Do you agree that the three highest priority projects for IASB are: climate-related risk, intangibles, and statement of cash flows? Please explain why or why not.

We agree that these three areas are high priority. They are generally areas in which standard setting can make a difference to significantly enhance the usefulness of corporate reporting for users addressing issues that will be relevant in the future.

We set out below comments on the proposed scope of the projects in the Draft Comment Letter

### **Climate related risk**

It is important that the requirements of the Standards enable preparers to reflect the financial impact of climate related risk in their financial statements and to provide users with the information that they need in relation to the financial statement implications of climate related risks.

We believe that a project to ensure that the Standards are fit for purpose in this area should start by assessing whether fundamental change to accounting standards is actually required. We think that it may be the case that educational material, or more practical guidance on reflecting climate in IAS 36 recoverable amount calculations may be more appropriate than fundamental changes to standards.

The communication of climate related risks to users can't be addressed solely by the financial statements. Narrative reporting on value drivers, business model and business risks is an important part of the overall provision of climate-related information to the market. A project on communication of climate risks should address how financial statements fit into this overall picture. This will need to take into account the work of the ISSB as well as narrative reporting more generally through management commentary. Therefore, the management commentary project remains important (see response to Q7).

We also believe that the IASB's existing project to develop disclosure objectives should reflect user needs for information in the financial statements, which would be expected to include climate related information in some cases.

We do not support the simple proposed changes to IAS 1.125 and IAS 36.33(b) that are outlined in the RFI [B11 (a) and (b)]. As such, we do not agree with paragraph A8 (a)(i) of the Draft Comment Letter. The proposed changes in the form suggested in the RFI will not "ensure long-dated effects of climate related risk are reflected in measurement" and we think will not have much effect:

- Removing the reference to "the next financial year" in IAS 1.125 would not alone promote more extensive disclosure. A broader project, perhaps linked to the development of specific disclosure objectives, would be necessary to clarify what is really meant by estimation uncertainty and what form of information is expected to be material.
- It is inevitable that cash flow projections to assess the recoverable amount of cash generating units will cover periods longer than five years. It should be irrelevant to the outcome whether risks in later periods are reflected through a) the use of detailed forecasts or b) the application of a steady or declining growth

rate, together with discounting (the 'terminal value'). Removing the rebuttable maximum 5-year period for cash flow projections to be based on budgets [IAS 36.33(b)] would not have a significant effect and may give false confidence of the precision of this estimate. Any project on IAS 36 would necessarily be more extensive.

We believe that developing an accounting framework for pollutant pricing mechanisms is extremely important. We think this is a separate activity to the proposed project on intangibles because accounting for such mechanisms is much broader in scope and would need to deal with matters such as accounting for potential liabilities associated with pollution. As different jurisdictions develop different mechanisms for pollutant pricing it is vital that there is a globally coherent approach to reflecting these schemes in financial statements. The range of possible regulatory responses increases the scope of a project on pollutant pricing mechanisms, likely covering taxes and levies as well as provisions and different forms of asset. This will be a large, challenging project, but one that we think is necessary for financial statements to remain relevant.

## **Intangibles**

We agree that a major project on intangibles is a high priority. This should be a comprehensive review including of the definition of intangible assets. Earnings are increasingly driven by intangible value drivers that were not envisaged when accounting standards were first developed.

There are "intangible" value drivers in modern businesses that inevitably will not meet any re-worked definition of intangible assets. We expect that narrative reporting will have an increasingly important role to play in explaining these drivers. As such, the IASB guidance on management commentary should be part of the thematic approach to this project.

## **Statement of Cash Flows**

We agree that a comprehensive review of IAS 7 is a high priority. The project should be informed by user outreach with the aim that the statement of cash flows provides the information on performance that users require. Cash performance is fundamental information, particularly as business activities, and the related accounting, become more complex.

The starting point must be the information that is relevant to users. The accounting, presentation and disclosure requirements must then be clear enough to be applied using the concept of materiality as the relevant benchmark.

For preparers to consistently make disclosure materiality decisions, clear disclosure objectives and clear guidance for preparers on applying materiality to disclosures are necessary. This disclosure approach is relevant across the financial statements, not only to cash flow information, and should be covered through existing projects on presentation and disclosure.

The UKEB suggest [A8(c)(ii)] that the project should consider the degree to which the disclosures in IAS 7.50 should be mandated. In our view, mandating disclosures is not meaningful in financial statements driven by materiality judgements. Rather, we consider that the priority of the IASB should be to develop improved guidance for preparers on how to assess materiality from the perspective of the users of the financial statement, particularly the materiality of narrative disclosures.

4. Do you agree that the remaining projects identified in IASB's Request for Information are low priority? Please explain why or why not.

We agree that the three priority areas outlined in the Draft Comment Letter capture the new projects that are the highest priority for the UK.

Other potential new projects that are discussed in the RFI are lower priority for the UK, although we expect that other jurisdictions may have different priorities. Some of the remaining projects discussed in the RFI are higher priority than others, but given resource constraints we agree that it is sensible for the UKEB's response to focus on identifying the highest priority areas.

#### **D. Other comments**

5. Do you agree with the UKEB's recommendation that the climate related risk and intangibles projects should be approached thematically, considering their impact across all Standards to support consistency and efficiency? Please explain why or why not.
6. Do you have any other comments on the thematic approach proposed in the UKEB's DCL?

We agree that it will be important for projects to take into account the cross-cutting nature of the matters under consideration to support consistency of accounting standards. Such a thematic approach is likely to need careful planning to keep the scope of projects manageable while gaining the benefits of considering the effects across more than one standard.

7. Do you have any comments on the projects identified in the UKEB's draft comment letter for pause or rationalisation from the IASB's work plan in order to free up resources?

The IASB will naturally have to consider resource pressure as it sets its final agenda. However, there are existing projects that remain a priority. For example, the extensive work on presentation and disclosures has not yet been finalised. There are real opportunities within those projects to make a real difference to the quality of financial reporting; for example, in developing guidance to help preparers make materiality decisions regarding disclosures. It is important that such key projects are completed.

We recommend that the IASB consider generating some additional criteria to assist in prioritising between projects of similar levels of importance. Those would be a second step following the criteria set out in the agenda consultation.

We don't agree that the Management Commentary project should be paused. Historic, numerical financial statement information cannot provide users with all the information they need. This is particularly the case in areas that we think are high priority for the IASB: climate risk and intangibles. Although the UK does not directly apply the IASB management commentary guidance, it is in the long-term interests of capital markets, including the UK, for there to be consistent and effective narrative reporting globally. The IASB is well placed, working with the proposed ISSB, to create an effective global regime in this area.

We also note that some of the issues explored in the extractive activities project are key issues that would be expected to be picked up in any project on intangibles.