UK Endorsement Board

Dr Andreas Barckow
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28 November 2024

Dear Dr Barckow

Exposure Draft IASB/ED/2024/6 *Climate-related and Other Uncertainties in the Financial Statements* - Proposed illustrative examples

1. The UK Endorsement Board (UKEB) is responsible for endorsement and adoption of IFRS Accounting Standards for use in the UK and therefore is the UK's National Standard Setter for IFRS Accounting Standards. The UKEB leads the UK's engagement with the IFRS Foundation on the development of new standards, amendments, and interpretations. In addition, the Department for Business and Trade has asked the UKEB to consider the overlap between IASB and ISSB issued standards.

2. This letter is intended to contribute to the IFRS Foundation's due process. The views expressed by the UKEB in this letter are separate from, and will not necessarily affect the conclusions in, any endorsement and adoption assessment on new or amended international accounting standards undertaken by the UKEB.

3. There are currently approximately 1,500 entities with equity listed on the London Stock Exchange that prepare their financial statements in accordance with IFRS.[1] In addition, UK law allows unlisted companies the option to use IFRS and approximately 14,000 such companies currently take up this option.[2]

Overarching comments

4. As highlighted in the joint National Standard Setters letter to the International Sustainability Standards Board (ISSB) on its Agenda Consultation, we consider that maintaining close alignment and connectivity between financial and

[1] UKEB calculation based on LSEG and Eikon data, May 2023. This calculation includes companies listed on the Main market as well as on the Alternative Investment Market (AIM).

[2] UKEB estimate based on FAME (company information in the UK and Ireland produced by the Bureau Van Dijk, a Moody's analytics company), Company Watch financial analytics and other proprietary data.

sustainability reporting is paramount to ensuring that the information produced for investors is compatible and comparable.

5. We recognise the challenges of delivering guidance as sustainability reporting continues to evolve. We commend the IASB for its work to help provide clarity regarding connectivity for all jurisdictions that apply IFRS Accounting Standards and are now committed to providing sustainability information to investors.

6. We therefore welcome the IASB's development of these examples. We agree that providing illustrative examples should improve reporting for the effects of climate-related and other uncertainties in the financial statements. It is also clear to us that the IASB has listened to feedback during their development.

7. However, we have identified some aspects of the guidance which may be better addressed by standard setting. In particular, we are concerned that the guidance goes beyond current understanding of the requirements of paragraph 31 of IAS 1 *Presentation of Financial Statements*. We also consider that the implication that 'lack of effect' is required to be considered for disclosure does not illustrate the original intention and wording of the standard; it appears more akin to interpretation.

8. In relation to paragraph 125 of IAS 1, we welcome the clarification provided in example 4. However, if user needs are not being met due to the lack of disclosure of uncertainties expected to result in changes to carrying values after more than one year, additional disclosure requirements may be necessary.

9. We consider that the examples could be enhanced by including a scenario where there is an impact on the financial statements.

10. For further information please refer to paragraphs A1 to A10 in Appendix A.

Approach to developing illustrative examples

10. We are generally supportive of the IASB's approach to developing the examples and in particular that the examples should illustrate how an entity applies the requirements in IFRS Accounting Standards (BC14). We also agree with the approach of focusing the examples on the requirements that are among the most relevant for reporting the effects of climate related and other uncertainties in financial statements.

11. We do however have some comments on the fact patterns and technical content of the examples. Our comments are aimed at enhancing the relevance of the illustrations and supporting connectivity. These are included in the paragraphs A11 to A19 in Appendix A.

12. If you have any questions about this response, please contact the project team at UKEndorsementBoard@endorsement-board.uk.

Yours sincerely

Pauline Wallace
Chair
UK Endorsement Board

Appendix A: Exposure Draft *Climate-related and Other Uncertainties in the Financial Statements – Proposed illustrative examples*

Question 1 — Providing illustrative examples
The IASB is proposing to provide eight examples illustrating how an entity applies the requirements in IFRS Accounting Standards to report the effects of climate-related and other uncertainties in its financial statements. The IASB expects the examples will help to improve the reporting of these effects in the financial statements, including by helping to strengthen connections between an entity's general purpose financial reports. Paragraphs BC1–BC9 of the Basis for Conclusions further explain the IASB's rationale for this proposal. (a) Do you agree that providing examples would help improve the reporting of the effects of climate-related and other uncertainties in the financial statements? Why or why not? If you disagree, please explain what you would suggest instead and why. The IASB is proposing to include the examples as illustrative examples accompanying IFRS Accounting Standards instead of publishing them as educational materials or including them in the Standards. Paragraphs BC43–BC45 of the Basis for Conclusions further explain the IASB's rationale for this proposal. (b) Do you agree with including the examples as illustrative examples accompanying IFRS Accounting Standards? Why or why not? If you disagree, please explain what you would suggest instead and why.

(a) Improvements in reporting

A1. While we recognise the challenges of delivering guidance as sustainability reporting is expected to evolve in the near future, it is also clear that demand for clarity regarding connectivity is urgent and necessary in all jurisdictions that apply IASB's standards and are now committed to providing sustainability information to investors. Jurisdictions representing over half the global economy by GDP have now taken steps towards aligning with or adopting ISSB standards[3]. In other jurisdictions, such as the EU where companies are expected to apply ESRS, recent activity indicates that there is expected to be a high degree of interoperability with ISSB standards.

Connectivity

A2. As highlighted in the joint National Standard Setters letter[4] to the ISSB on its Agenda Consultation, we consider that maintaining close alignment and connectivity between financial and sustainability reporting is paramount to ensuring that the information produced for investors is compatible and comparable. We are encouraged that one of the objectives set out in the ED (BC21) is to illustrate the provision of connected information in general purpose financial reports and to reinforce compatibility with IFRS Sustainability Disclosure Standards.

A3. We agree that providing illustrative examples should improve the current level of reporting for the effects of climate-related and other uncertainties in the financial statements. We include below some comments on certain unintended consequences and areas where we consider that the examples could be further improved.

Standard setting and other solutions

A4. We have identified some aspects of the guidance in respect of which the IASB may wish to consider standard setting as the guidance provided may be going beyond current understanding of those requirements.

a) Examples one[5] and five[6] appear to illustrate instances where materiality judgements based on IAS 1 paragraph 31 lead to additional disclosures. However, this may place too much reliance on a requirement that is intended to apply when compliance with other IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions. We understand that in current practice this requirement is used in relatively rare situations.

b) We also note that examples one and two[7] suggests that a 'lack of effect' also needs to be considered for disclosure. This appears to be inconsistent with the original intention of IAS 1 paragraph 31. It may be unclear to stakeholders the extent to which disclosing items which do not have a material effect on an entity's financial statements provides useful

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3 Jurisdictions representing over half the global economy by GDP take steps towards ISSB Standards (IFRS Foundation 2024)

4 National Standard Setters Sustainability Forum Joint Letter paragraphs 4 – 9 (UKEB 2023).

5 Materiality judgements leading to additional disclosures (IAS 1/IFRS 18)

6 Disclosure of assumptions: additional disclosures (IAS 1/IFRS 18)

7 Materiality judgements not leading to additional disclosures (IAS 1/IFRS 18)

information. The IASB may wish to consider whether using paragraph 112(c) of IAS 1 would be more appropriate as it relates to '…information that is not presented elsewhere in the financial statements, but is relevant to an understanding of any of them.' Alternatively, the IASB may need to review this paragraph for a potential amendment if it is not achieving its intended purpose.

c) We support the clarification provided in example four[8] regarding IAS 1 paragraph 125 but are concerned that the illustration may now place too much reliance on this paragraph. If user needs are not being met due to the lack of disclosure of uncertainties expected to result in changes to carrying values after more than one year, then additional disclosure requirements may be necessary.

Use of climate focused examples as analogies for other uncertainties

A5. We are concerned about potential unintended consequences if the climate focused examples are used as analogies for all 'other' uncertainties. The IASB may wish to provide more context to help frame primary users' expectations that these examples relate to all sustainability-related risks. Alternatively, additional fact patterns or examples that cover a wider variety of uncertainties, such as risks arising from nature, human capital, or artificial intelligence, may provide the range of examples that could be analogised in future as other sustainability risks are identified.

Example where there is a financial statements impact

A6. We note that the examples do not illustrate circumstances when there is an impact on the financial statements. Users have advised us that this is a key area where they perceive a disconnect across general purpose financial reports. The IASB may wish to consider providing an example where a climate-related or other uncertainty does result in an impact on the financial statements.

Interaction of IFRS accounting standards with sustainability disclosure standards

A7. The UKEB research into connectivity[9] highlighted stakeholder feedback that they are seeking clarity on how the IFRS Foundation's two sets of standards are intended to work together in practice. We consider that the IASB could deliver this by incorporating in some of the examples references to, or illustrative connections with, sustainability disclosure standards. As examples one and two are specifically intended to reinforce compatibility with Sustainability Disclosure Standards, the IASB may wish to consider reflecting in the fact pattern where the entity has applied the requirements of sustainability disclosure standards, for

8 Disclosure of assumptions: general requirements (IAS 1/IAS 8)
9 A Study in Connectivity: Analysis of 2022 UK Company Annual Reports (UKEB 2023)

example to disclose how sustainability-related risks and opportunities have affected an entity's financial position, financial performance, and cash flows. This approach may provide a more direct connection across the general-purpose financial reports and provide a clearer context for the relevant financial statement disclosures.

(b) Illustrative examples accompanying IFRS Accounting Standards

A8. In general, we agree that the IASB's proposal to include the examples as accompanying illustrative material to the relevant accounting standards should provide stakeholders with accessible and relevant guidance when using those standards. We note however, that there are some areas where other standard setting solutions may be required (see paragraph A4 above).

A9. Whilst the examples are not mandatory, and so do not add or change any IFRS accounting requirements, we anticipate that they will be useful to stakeholders when they are considering accounting for relevant business transactions. We are aware that IASB guidance is often referred to by auditors when engaging with entities on their application of the standards.

A10. We note in BC45 of the ED that, in addition to including the examples in the relevant accounting standards, the IASB may also group the examples and publish them as a single document. We consider that this would be useful as, without this, some stakeholders may struggle to understand the connections, for example to the context of materiality to the individual examples when included in different standards.

Question 2 — Approach to developing illustrative examples
Examples 1–8 in this Exposure Draft illustrate how an entity applies specific requirements in IFRS Accounting Standards. The IASB decided to focus the examples on requirements: (a) that are among the most relevant for reporting the effects of climate-related and other uncertainties in the financial statements; and (b) that are likely to address the concerns that information about the effects of climate-related risks in the financial statements is insufficient or appears to be inconsistent with information provided in general purpose financial reports outside the financial statements. Paragraphs BC10–BC42 of the Basis for Conclusions further explain the IASB's overall considerations in developing the examples and the objective and rationale for each example.

Do you agree with the IASB's approach to developing the examples? In particular, do you agree with the selection of requirements and fact patterns illustrated in the examples and the technical content of the examples?

Please explain why or why not. If you disagree, please explain what you would suggest instead and why.

A11. We are generally supportive of the IASB's approach to developing the examples and in particular that the examples should illustrate how an entity applies the requirements in IFRS Accounting Standards (BC14). We also agree with the approach of focusing the examples on the requirements that are among the most relevant for reporting the effects of climate related and other uncertainties in financial statements.

A12. We do however have some comments on the fact patterns and technical content of the examples. Our comments are aimed at helping enhance the relevance of the illustrations and to support connectivity. These are included in the paragraphs that follow.

Use of standalone examples

A13. We support the use of standalone examples but also consider walk-through examples would be beneficial. We appreciate that walk-through examples are significantly more complex to develop and would take longer to build a consensus. The IASB may wish to consider developing more in-depth examples, as the next phase of work with the ISSB.

Specific comments on examples

A14. In relation to materiality judgements and the disclosure of additional information, we are concerned that examples one and two only reference the qualitative aspect of materiality. We suggest the IASB consider emphasising in each example that there is a single definition of materiality, and concluding on it requires consideration of both quantitative and qualitative aspects.

A15. In relation to assumptions and other sources of estimation uncertainty, stakeholders have advised in relation to IAS 36 *Impairment of Assets* that there are current challenges in practice with connectivity between climate-related scenarios and impairment assumptions, the effects on expected cash flows (beyond a five-year period) and how those may affect asset terminal values. The IASB may wish to consider if some of these aspects could be reflected in example three[10] or potentially included in a future joint illustrative example with the ISSB.

[10] Disclosure of assumptions: specific requirements (IAS 36)

A16. We suggest that example four could be improved by providing the rationale for the entity performing impairment testing at a CGU level. The IASB may wish to consider aligning the fact pattern more closely to the requirements of IAS 36 paragraph 67 (a) and (b). In addition, we recommend that any impact on the useful economic lives of the non-current assets should also be considered in the fact pattern.

A17. We suggest that including direct references to IFRS 7 paragraph 33 (qualitative disclosures) and paragraph 34 (quantitative disclosures) and illustrating their application would help clarify the approach in example six[11].

A18. In relation to example seven[12], stakeholders have advised us that the most relevant challenges in practice relate to cases when assets may need to be replaced or repurposed due to climate-related risks and the potential implications for impairment, reduction in useful economic life and consequential acceleration of depreciation and potential decommissioning provisions. The IASB may wish to consider if some of these aspects could be reflected in example seven or potentially included in a future joint illustrative example with the ISSB.

A19. We also consider that it would be helpful to clarify in example eight how materiality was assessed and how the disaggregation resulted in material information. For example, if an entity with a diverse fixed asset base used an income statement-based materiality to disaggregate their assets with differing climate-related risk characteristics, this may result in very granular disclosures which may not produce useful information.

Question 3 — Other comments
Do you have any other comments on the Exposure Draft?

A20. We note that paragraph BC9(a) of the ED says that feedback from the ED will help the IASB determine whether other actions, including standard setting, might be necessary. However, it is unclear to us whether answers to the questions asked in the ED, which focus on the illustrative examples, will necessarily provide that evidence.

11 Disclosure about credit risk (IFRS 7)
12 Disclosure about decommissioning and restoration provisions (IAS 37)