UK Endorsement Board

UKEB letter to IASB on connectivity matters

Executive Summary

Project Type	Influencing
Project Scope	Limited Scope
Purpose of the paper	
The purpose of this paper is to present a draft letter to the IASB Chair for Board consideration and approval. The letter contains recommendations for a strategic and comprehensive approach to address users' connectivity needs between IFRS Sustainability Disclosure Standards and IFRS Accounting Standards.	
Summary of the Issue	
At the January 2024 UKEB meeting the Board agreed to submit a response to the IFRS Interpretations Committee's Tentative Agenda Decision: *Climate-related Commitments (IAS 37)* (the TAD), given its likely impact on UK companies. At that meeting, the Board considered there were wider strategic issues that would merit a separate letter to the IASB, provide its view on some of the points to highlight to the IASB and agreed that a draft letter would be tabled for its consideration at the February 2024 meeting. Annex A contains a draft of a letter that reflects the Board's feedback at the January 2024 meeting. In February 2024 the Board agenda had to be reprioritised, resulting in consideration of the draft letter being postponed to the March 2024 meeting. In the intervening period, the IASB has published draft examples to illustrate how to apply requirements in IFRS Accounting Standards to report the effects of climate-related and other uncertainties in the financial statements. The letter is part of the UKEB remit and workplan in relation to Connectivity as noted on the UKEB Regulatory Strategy[1].	
Decisions for the Board	
The Board is asked whether it wishes to submit the letter to the IASB. If the letter is to be submitted, the Board is asked to consider and approve the draft letter to the IASB Chair presented at Appendix A.	

[1] Regulatory Strategy 2023/24: Other Corporate Reporting Projects - Connectivity (Dependent on ISSB decision on agenda priorities) page 16

Recommendation
The UKEB Secretariat recommends that the Board submits the letter to the IASB and, subject to any amendments arising at this meeting, approves the letter at Annex A.
Appendix
Appendix A [Draft] UKEB letter to IASB on connectivity matters

UK Endorsement Board

Appendix A: UKEB letter to IASB on connectivity matters

Dr Andreas Barckow
Chairman
International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London
E14 4HD

X March 2024

Dear Dr Barckow,

IASB's strategic approach to the connectivity between IFRS Sustainability Disclosure Standards and IFRS Accounting Standards

1. The UK Endorsement Board (UKEB) is responsible for the endorsement and adoption of IFRS Accounting Standards for use in the UK and is, therefore, the UK's National Standard Setter for IFRS Accounting Standards. The UKEB also leads the UK's engagement with the IFRS Foundation on the development of new standards, amendments, and interpretations.

2. This letter is intended to contribute to the 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]

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1 UKEB calculation based on London Stock Exchange Group (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.

4. The UK Government has requested[3] that the UKEB also considers the overlap between the standards issued by the IASB and the ISSB, until the establishment of a legislative framework for adoption of IFRS Sustainability Disclosure Standards is in place.

5. We commend the IASB and ISSB for holding their first joint meeting, in January 2024, to discuss connectivity between their respective reporting requirements, and for the examples developed as part of the *Climate related and Other Uncertainties in the Financial Statements* project. We encourage both the IASB and ISSB to continue their efforts to address the needs of users of financial statements and sustainability reporting.

6. We also commend the IASB for the additional work it has added to its and the IFRS Interpretations Committee (the Committee)'s agenda to address specific standard setting and interpretation requests from stakeholders, such as in relation to the application of IAS 36 *Impairment of Assets* and Climate-related Commitments (IAS 37).

7. However, as noted in the UKEB's response[4] to the Committee on the TAD, while we agree with the overall technical accounting conclusion, we have concerns regarding the wider strategic context of the questions posed to the Committee. UK stakeholder feedback and our own research have clearly identified that the reporting in company financial statements, in relation to financial impacts arising from climate-related risks and companies' commitments to net zero, still has some way to go to address user needs. Several other respondents to the IAS 37 TAD also referred to this wider need, in addition to the Committee members themselves, at their November 2023 meeting.

8. Stakeholders are hopeful that where IFRS Sustainability Disclosure Standards are adopted, as mandatory standards, the sustainability disclosures may help meet many of the user needs. However, the implementation roadmaps and the level of alignment to the ISSB issued standards are still in development in most jurisdictions, so for some considerable time there is likely to be a gap in reporting guidance that we think the IASB could proactively address.

9. The IASB should be aware that in some jurisdictions existing requirements mean a degree of pre-existing alignment with the ISSB standards. For example, in the UK, reporting on TCFD and greenhouse gas emissions, cornerstones of reporting under IFRS S2, is already embedded in law. Jurisdictions, such as the UK, with some existing alignment are ahead of the curve in understanding user needs for

3 Letter from Lord Callanan to the International Sustainability Standards Board regarding their exposure drafts IFRS S1 and IFRS S2 (August 2022)

4 UKEB Final Comment Letter - IFRS IC – Tentative Agenda Decision Climate-related Commitments (February 2024)

additional work needed on developing connectivity between the sustainability disclosures and the information in the financial statements.

10. As such, we consider that the IASB, working together with the ISSB, has the opportunity to address the needs of users of financial statements to ensure connectivity is built in from the outset. Below we set out our suggestions for the IASB to consider.

Wider stakeholder feedback on the Committee's TAD

11. We recognise the work the IASB is undertaking on its active project Provisions – Targeted Improvements. We welcome proposed steps to enhance the standard's alignment with the Conceptual Framework for Financial Reporting and to clarify application of the standard's principles. However, while we acknowledge the project's relatively narrow scope, we think the IASB could consider addressing some of the stakeholder feedback[5] received on the Committee's TAD, that suggested potential amendments to IAS 37. This could include clarifying, within the standard itself, the interaction between constructive obligations and the recognition of provisions, and developing clearer application guidance on:

    a) when net zero and similar commitments might create a constructive obligation; and,

    b) when an entity has a present obligation for costs that becomes payable only when a particular measure (e.g. its emissions) exceeds a specified threshold.

Scope of the *Climate-related and Other Uncertainties in the Financial Statements* project

12. Stakeholders remain concerned about whether the scope of the *Climate-related and Other Uncertainties in the Financial Statements* project is wide enough to adequately address reporting of climate-related risks and opportunities, including but not limited to, company net zero commitments.

13. We suggest that the IASB might usefully broaden the project scope, to include areas such as adding reciprocal requirements for connected information (per IFRS S1 paragraph 21[6]) and requiring the use of consistent data and assumptions

5 Feedback included that from the UKEB Final Comment Letter and other stakeholders, as highlighted in IASB Staff agenda paper 2A Climate-related-commitments-comment-letter-analysis, paragraph 53.

6 IFRS S1 Connected information, paragraph 21 (b) (ii) the connections between disclosures provided by the entity across its sustainability-related financial disclosures and other general purpose financial reports published by the entity—such as its related financial statements.

(per IFRS S1 paragraph 23[7]), as initially proposed by the IASB staff at the IASB September 2023 meeting[8].

14. We recognise the work the IASB is undertaking to develop examples and welcome the broad scope of the draft examples presented at the IASB's March 2024 meeting. However, we consider that the draft examples do not directly address connectivity; that is, how the financial disclosures might link to the sustainability disclosures, as requested by stakeholders. The IASB could bridge the gap by enhancing the examples to explicitly illustrate connectivity with the 'front half' of the Annual Report.

15. Our initial stakeholder feedback on the draft examples indicates that, while they are considered helpful, there is still some work required to avoid unrealistic expectations from users. Some suggestions from UK stakeholders include:

    a) that the examples could helpfully provide illustrative disclosures to show how the financial statement disclosures might connect to the related sustainability disclosures; and,

    b) that any confusion around the application of IAS 1 (paragraph 125) should be separately addressed and that paragraph 31 of IAS 1 may be being overextended given the macroeconomic nature of the climate risk.

16. We recommend the IASB consider developing a comprehensive case study or case studies – potentially jointly with the ISSB – to demonstrate the '*other accounting implications*', highlighted in the Committee's IAS 37 TAD, and their interaction with sustainability reporting. In our view, such case studies (or 'walk through' examples) could better illustrate companies real-world decision-making and, therefore, be more helpful to stakeholders.

17. While we appreciate that they would probably need to be issued as educational material initially, they could provide clarity for a broad range of stakeholders, including investors who may not be familiar with the specifics of the accounting requirements, on for example:

    a) the circumstances in which climate commitments would and would not result in the recognition of a provision;

    b) how net zero commitments do, or do not, affect the recognition and measurement of other items in the financial statements;

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7 IFRS S1 Connected information, paragraph 23 Data and assumptions used in preparing the sustainability-related financial disclosures shall be consistent—to the extent possible considering the requirements of IFRS Accounting Standards or other applicable GAAP—with the corresponding data and assumptions used in preparing the related financial statements.

8 Climate-related Risks in the Financial Statements - Potential actions (IASB September 2023), paragraph 4(a)(ii).

c) the extent to which asset decommissioning provisions provide a useful analogy when considering such commitments; and

d) the disclosures that might be required, including under IAS 1 about the judgements made in applying the entity's accounting policies.

18. As practice develops the IASB may wish to keep under consideration the possibility of standard setting so that the principles of the examples become enforceable.

Pollutant Pricing Mechanisms project

19. As noted in the UKEB response to the IASB PPM survey, the current lack of clarity in IFRS Accounting Standards regarding accounting for carbon credits has resulted in diversity of practice. Carbon credit programmes have become increasingly common in recent years. However, with governments moving to charging for such credits, the proliferation of voluntary schemes and their increasing use by companies as part of their Net Zero strategies, their volume and value are expected to become much more significant in the near future. Additionally, governments, including the UK Government, are starting to develop similar credit schemes for other sustainability matters[9].

20. In this respect, we consider that circumstances have changed since the IASB's most recent agenda consultation. Stakeholders tell us that they now routinely need to manage systemic sustainability risk and see carbon credit schemes as part of their mitigation strategies.

21. While we recognise the constraints on resources and potential implications for other IASB projects, our advice would be for the IASB to consider promoting *Pollutant Pricing Mechanisms*[10] from the reserve list to the active work plan to enhance the relevance and comparability of reported financial information.

Transparency of joint working between the IASB and ISSB

22. We appreciate that the IASB and ISSB have different remits and have reassured stakeholders that despite this, connectivity between their operations, processes and products of the boards should be considered as 'business as usual'. However, as noted at the joint board meeting, despite not being asked, stakeholders emphasised the importance of connectivity in their responses to the recent ISSB Request for Information.

23. Clearly, connectivity between the two sets of standards and its active consideration by both Boards is important to stakeholders. Transparency is

9 For example, UK Emissions Trading Scheme, the Climate Change Levy, Carbon Price Support and Landfill Tax.

10 IFRS - IASB pipeline projects.

important for stakeholders to understand the decisions being made and their implications for existing financial and sustainability reporting requirements. We therefore, recommend that the Boards aim for as much transparency as possible, on technical matters. For example, the two Boards could:

a) publicly discuss how they are addressing connectivity issues as they develop their individual projects and in any tentative decisions they make;

b) set out the areas of connectivity within their workplans, together with the related timelines for those projects; and,

c) seek stakeholder feedback regarding connectivity implications as part of their future respective Agenda Consultations.

Management Commentary project

24. In our view, amendments to *Practice Statements* may not be the right vehicle to meet users' needs. We note that they are not endorsed for use in most jurisdictions, including the UK, and are, therefore, not mandatory. The IASB may wish to consider de-prioritising the *Management Commentary* project.

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

Yours sincerely

Pauline Wallace
Chair
UK Endorsement Board

c.c. Mr. Emmanuel Faber, Chairman, International Sustainability Standards Board