UKEB UK Endorsement Board

Dr Andreas Barckow
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(Date)

Dear Dr Barckow

Request for Information: *Third Agenda Consultation*

The UK Endorsement Board (UKEB) is responsible for endorsement and adoption of IFRS for use in the UK and therefore is the UK's National Standard Setter for IFRS. The UKEB also leads the UK's engagement with the IFRS Foundation (Foundation) on the development of new standards, amendments and interpretations. This letter forms part of those influencing activities and is intended to contribute to the International Accounting Standards Board's (IASB) 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.

We welcome the opportunity to respond to the IASB's *Third Agenda Consultation*. We performed both desk-based research and outreach with our stakeholders to assess the implications for the IASB's future work plan. Our comments on the IASB's Request for Information (RFI) summarise that work and outreach. For detailed responses to the questions in the RFI please see appendix 1 to this letter.

IASB's strategic direction and balance of activities

1. At a strategic level we recommend that the IASB reallocates resource to ensure that it:

    a) retains sufficient flexibility in its workplan to address the interaction between IFRS and any future international sustainability standards developed by its proposed sister Board, the International Sustainability Standards Board (ISSB). As a minimum, we think this will need to include co-ordination with the ISSB on any areas of overlap;

    b) allocates more resource to its work on digital financial reporting. This work should explore how advances in technology are changing the way investors consume information and assess the extent to which any changes are needed to the IFRS taxonomy and the way in which the Board writes Standards;

    c) adds to its work on Standards development a structured and cohesive research plan which anticipates and addresses emerging issues. To help alleviate pressure on IASB's resources, the IASB could coordinate with National Standard

Setters' research programmes. If an agreement on the scope of the research project can be achieved, then drawing on local expertise and knowledge base in certain jurisdictions may help build capacity and expedite project delivery; and

d) resources the areas identified in a-c above by pausing the projects on the Second Comprehensive Review of IFRS for SMEs and Management Commentary and rationalising the Extractive Activities projects from its current work plan. The IASB's mission is to develop Standards that bring transparency, accountability and efficiency to financial markets around the world and we recommend that in a time of resource constraint, the most pressing projects underpinning this core mission are prioritised. IFRS for SMEs is non-mandatory, and none of our stakeholders identified it as currently requiring a comprehensive review. The IFRS reporters in the UK are more interested in the project on Reduced Disclosures for Subsidiaries that are SMEs. Management Commentary is also non-mandatory and before proceeding with work on that project it is important to develop an understanding of whether any of its requirements are likely to be incorporated in the work of the ISSB. The Extractive Activities project could be addressed by educational material.

2. Our recommendations are in line with the rising influence on corporate reporting of ESG[1] and sustainability[2] reporting as well as the increasing use of technology in the production and consumption of corporate reports[3]. We anticipate that these influences will continue to increase over the IASB's coming work cycle.

Priority projects

3. Our desk-based research and initial outreach with stakeholders clearly identified three high-priority projects for IASB's next work cycle. The projects address emerging corporate reporting issues which should be prioritised in order for Standards to remain relevant. The projects are climate-related risk, intangibles, and statement of cash flows.

4. We recommend the following scope for these projects:

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1 The rise of ESG reporting is evidenced, for example, by: The IFRS Foundation's consultation on sustainability, the SEC's March 2021 announcement of the formation of a climate and ESG task force, and the Bank of England's stress testing for climate-related risk.

2 We note that the terms ESG reporting and sustainability reporting are often used interchangeably. However, we believe that sustainability reporting is broader in scope than ESG reporting and encompasses reporting on value creation or erosion through any aspect of the entity's activities. For example, we believe sustainability reporting could encompass areas such as business processes, supply chains, brands, customer loyalty, and financial resilience. Our interpretation is aligned to the following statement from the IFRS Foundation's feedback statement on sustainability: '*The Trustees recognise the importance for the public interest of reporting standards that address enterprise value—which capture expected value creation (or erosion) for investors in the short, medium and long term and is interdependent with value creation for stakeholders in the context of social and environmental imperatives. The Trustees understand, based on the feedback to the Consultation Paper, that consistent and comparable disclosures on sustainability matters are needed to bring transparency to financial markets and provide investors with information useful in assessing a company's enterprise value*' (IFRS Foundation Trustees Feedback Statement on the Consultation on Sustainability Reporting | April 2021 page 11).

3 The increased use of technology in digital reporting is evidenced by, for example: the requirement for UK entities which prepare consolidated accounts in line with IFRS to i. apply the European Single Electronic Format (ESEF) for financial years beginning on or after 1 January 2021 ii. tag, in XBRL, basic financial information iii. tag notes to the accounts for financial years starting on or after 1 January 2022.

a) **Climate-related risk** – our outreach identified that the scope of this project should build on the IASB's previous work in this area[4] and should consist of a cross-standard review to identify and resolve any potential areas of interaction between IFRS and future sustainability standards on climate-related risk.[5] In addition to the potential amendments to IAS 1 and IAS 36 to capture long-dated climate risk identified in the RFI, this would include consideration of, for example, implications for IFRS 9 *Financial Instruments* of the classification of ESG bonds; implications for IFRS 10 *Consolidated Financial Statements* of whether renewable energy funds meet the investment entity criteria; and implications for IFRS 8 *Operating Segments* of changes in the regulatory environment due to climate-related risk.

b) **Intangible assets** – our outreach with stakeholders indicated that this is a key area for development. A comprehensive review of IAS 38 *Intangible Assets* is necessary to address the extent to which it captures relevant information on intangibles, including crypto-currencies, pollutant pricing mechanisms, software, and development costs. The project should also consider whether more relevant information would be provided if intangible assets held for investment or for trading, such as crypto-currencies or pollutant pricing mechanisms, were addressed within the scope of other IFRS Standards.

c) **Statement of cash flows** – our stakeholders, in particular investors, advised us that recent events have once again reiterated the need for a comprehensive review of IAS 7 *Statement of Cash Flows*. Specifically, this should address whether current voluntary disclosures[6] should be mandated and whether a review of the statement of cash flows categories in line with the IASB's Exposure Draft *General Presentation and Disclosures* could improve comparability. It should also address whether a statement of cash flows specifically for financial institutions should be developed and whether the definition of cash and cash equivalents should be updated.

4 IASB's November 2019 article 'IFRS Standards and climate-related disclosures' and November 2020 educational material 'Effects of climate-related matters on financial statements' explain how IFRS Standards recognise the effect of climate-related matters on financial statements in November 2020

5 Climate is identified as the initial priority area for the development of sustainability standards in the IFRS Foundation Trustees Feedback Statement on the Consultation on Sustainability Reporting | April 2021.

6 IAS 7 paragraph 50 encourages disclosure of i. Amount of undrawn borrowing facilities that may be available for future operating activities and to settle capital commitments ii. The aggregate amount of cash flows that represent increases in operating capacity separately from those cash flows that are required to maintain operating capacity iii. The amount of cash flows arising from the operating, investing and financing activities of each reportable segment

<u>**Thematic approach**</u>

5. Where projects impact multiple Standards, we suggest that IASB applies a thematic approach, whereby amendments to all relevant Standards are addressed as part of the same project and an overarching objective. This approach allows for more consistency across Standards and has potential for greater efficiency in the Standard-setting process.

6. A thematic approach would be effective for the climate-related risk and intangibles projects outlined above and we note that a similar approach has been deployed by IASB in the Disclosure Initiative project. We illustrate a thematic approach to the climate-related risk and intangibles projects in Appendix 2.

7. In addition, high-priority projects could be grouped by a theme, for example on the theme of retaining relevance. A unifying theme could provide a consistent focus for project scoping and for stakeholder communications.

If you would like to discuss these comments, please contact the project team at agendaconsultation@endorsement-board.uk .

Yours sincerely

Pauline Wallace
Chair
UK Endorsement Board

Appendix 1 Response to questions in IASB's Request for Information *Third Agenda Consultation*
Appendix 2 Illustration of thematic approach

Appendix 1: Questions on *Third Agenda Consultation*

Question 1: Strategic direction and balance of the Board's activities
The Board's main activities include: • developing new IFRS Standards and major amendments to IFRS Standards; • maintaining IFRS Standards and supporting their consistent application; • developing and maintaining the *IFRS for SMEs* Standard; • supporting digital financial reporting by developing and maintaining the IFRS Taxonomy; • improving the understandability and accessibility of the Standards; and • engaging with stakeholders. Paragraphs 14–18 and Table 1 provide an overview of the Board's main activities and the current level of focus for each activity. We would like your feedback on the overall balance of our main activities. Should the Board increase, leave unchanged or decrease its current level of focus for each main activity? Why or why not? You can also specify the types of work within each main activity that the Board should increase or decrease, including your reasons for such changes. Should the Board undertake any other activities within the current scope of its work?

A1 The current allocation of resource across IASB's different activity areas is broadly appropriate.

A2 However, we recommend that IASB:

a) Within its activity on new IFRS, major amendments, and maintenance and consistent application:

(i) Retains sufficient flexibility in its workplan to address the interaction between IFRS and any future international sustainability standards developed by its proposed sister Board, the International Sustainability Standards Board (ISSB).

(ii) Incorporates a more visible and structured research programme so that responses are developed in real-time for emerging issues. Collaborating with NSS may be an efficient way of achieving this.

b) Allocates more resource to digital reporting since it is anticipated that digital tagging and consumption of financial information will become more prevalent.

c) Allocates more resource to the priorities identified above by pausing the Second Comprehensive Review of IFRS for SMEs and the Management Commentary projects on its current work plan and rationalising the Extractive Activities project from its current work plan. IFRS for SMEs is non-mandatory and in our initial outreach stakeholders have not indicated a need for the Second Comprehensive Review of SMEs. IFRS reporters in the UK are more interested in the project on Reduced Disclosures for Subsidiaries that are SMEs. Management Commentary is also non-mandatory and before proceeding with work on that project it is important to develop an understanding of whether any of its requirements are likely to be incorporated in the work of the ISSB. The Extractive Activities project could be addressed by educational material.

Question 2: Criteria for assessing the priority of financial reporting issues that could be added to the Board's work plan
Paragraph 21 discusses the criteria the Board proposes to continue using when assessing the priority of financial reporting issues that could be added to its work plan. Do you think the Board has identified the right criteria to use? Why or why not? Should the Board consider any other criteria? If so, what additional criteria should be considered and why?

A3 We recommend that two of the IASB's criteria are redrafted:

a) There is a risk that application issues are captured by the second criterion: '*whether there is a deficiency in the way companies report the type of transaction or activity in financial report*.' We do not think that this is the IASB's intention. We recommend that this criterion is redrafted as '*whether there is a deficiency in the Standards for reporting this type of transaction or activity*.'

b) The third criterion considers: '*the type of companies the matter is likely to affect, including whether the matter is more prevalent in some jurisdictions than in others*.' This suggests that some sectors and jurisdictions will be prioritised over others. Our view is that prevalence should be considered across all sectors and jurisdictions. We therefore recommend that this criterion is redrafted as '*the extent to which the matter is prevalent across jurisdictions and sectors*.'

A4 We recommend that an additional criterion is added. This criterion should assess whether the project is expected to remain relevant when it reaches implementation stage. The addition of this criteria would prevent projects of limited long-term relevance being added to the work plan.

A5 We recommend that the first criterion is redrafted in consultation documents so that it is consistent with the wording in the IASB's due process handbook, referring to *'users'* rather than '*investors*.'

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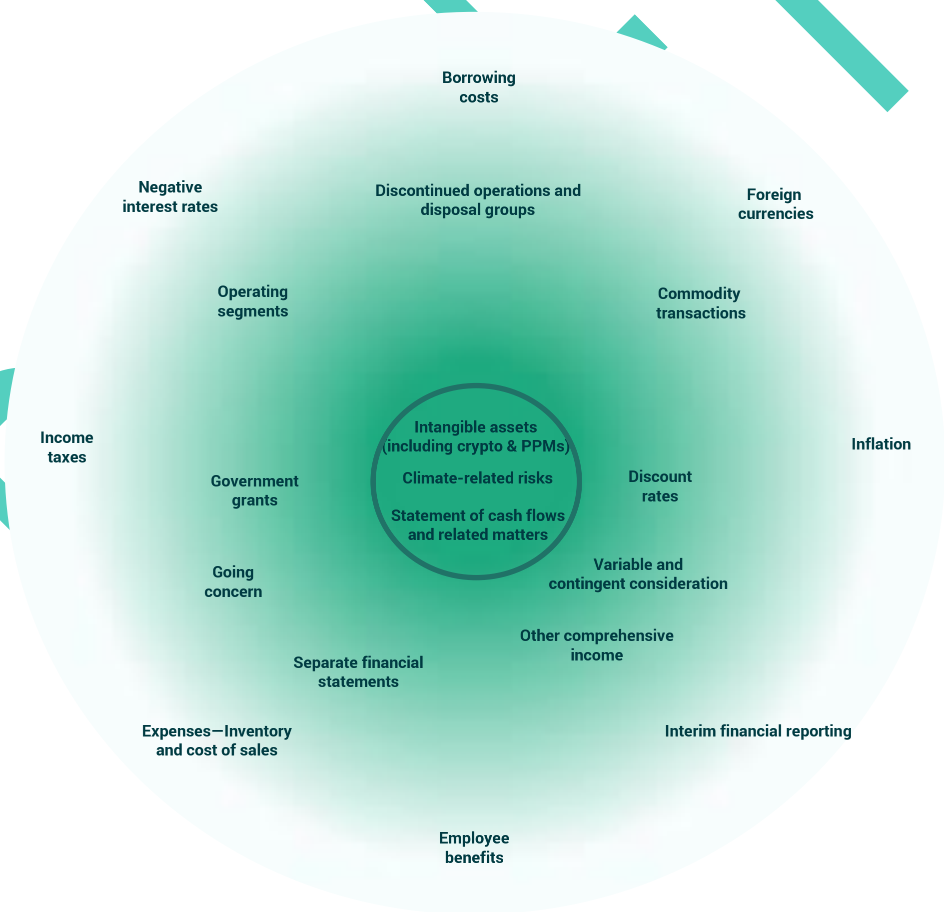
Question 3: Financial reporting issues that could be added to the Board's work plan
Paragraphs 24–28 provide an overview of financial reporting issues that could be added to the Board's work plan. What priority would you give each of the potential projects described in Appendix B—high, medium or low—considering the Board's capacity to add financial reporting issues to its work plan for 2022 to 2026 (see paragraphs 27–28)? If you have no opinion, please say so. Please provide information that explains your prioritisation and whether your prioritisation refers to all or only some aspects of the potential projects. The Board is particularly interested in explanations for potential projects that you rate a high or low priority. Should the Board add any financial reporting issues not described in Appendix B to its work plan for 2022 to 2026? You can suggest as many issues as you consider necessary taking into consideration the Board's capacity to add financial reporting issues to its work plan for 2022 to 2026 (see paragraphs 27–28). To help the Board analyse the feedback, when possible, please explain: the nature of the issue; and why you think the issue is important.

A6 The chart below illustrates our recommended prioritisation of potential projects and is based on feedback from our initial outreach with UK stakeholders and our own desk-based research. The highest priority projects are closest to the centre.



A7 The three highest priority projects are: climate-related risks, intangible assets, and statement of cash flows and related matters. These projects relate to emerging corporate reporting issues which need to be addressed in order for Standards to remain relevant to the business environment over the coming decade.

A8 We recommend that these projects are scoped as follows:

a) Climate-related risk

(i) As proposed by IASB, amendments to IAS 1 and IAS 36 to ensure long-dated impacts of climate-related risk are reflected in the measurement of assets and liabilities.

(ii) In addition, to identify and address potential areas of interaction between IFRS and future sustainability standards on climate-related risk[7]; for example, implications for IFRS 9 *Financial Instruments* of the classification of ESG bonds; implications for IFRS 10 *Consolidated Financial Statements* of whether renewable energy funds meet the investment entity criteria and implications for IFRS 8 *Operating Segments* of changes in the regulatory environment due to climate-related risk.

b) Intangibles

(i) As proposed by IASB, a comprehensive review of IAS 38. Specifically, this review should address:

(ii) The extent to which IAS 38 captures relevant information on intangibles, including those which are becoming more prevalent, such as crypto-currencies, pollutant pricing mechanisms, software, and development costs, and;

(iii) Whether a separate standard for non-financial assets held for investment would provide more relevant information where intangibles such as crypto-currencies and emissions trading rights are held for investment

c) Statement of cash flows

(i) As specified by IASB, a comprehensive review of IAS 7. Specifically, this should address whether:

(ii) Current voluntary disclosures[8] should be mandated;

(iii) Building on the *General Presentation and Disclosures* ED work on the statement of profit or loss, a review of statement of cash flows categories could improve comparability; and

(iv) Whether a statement of cash flows specifically for financial institutions should be developed.

(v) Whether the definition of cash and cash equivalents should be updated.

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7 Climate is identified as the initial priority area for the development of sustainability standards in the IFRS Foundation Trustees Feedback Statement on the Consultation on Sustainability Reporting | April 2021.

8 IAS 7 paragraph 50 encourages disclosure of i. Amount of undrawn borrowing facilities that may be available for future operating activities and to settle capital commitments ii. The aggregate amount of cash flows that represent increases in operating capacity separately from those cash flows that are required to maintain operating capacity iii. The amount of cash flows arising from the operating, investing and financing activities of each reportable segment

A8 We propose that the pollutant pricing mechanisms and crypto-currency projects are addressed within the intangibles project.

A9 For the climate-related risk and intangibles projects, which involve multiple Standards, we recommend that a thematic approach is taken, whereby the impact across multiple Standards is considered as part of the same project. This approach supports consistency across Standards and potential efficiencies in the standard-setting process. See Appendix 2 for an illustration of the thematic approach.

A10 Our stakeholder outreach and research work highlighted that the remaining projects set out in the IASB's Agenda Consultation are low priority. We include our rationale below:

Project listed by the RFI[9]	IASB proposed scope per RFI	UKEB rationale for low priority[10]
Borrowing costs	Review the definition of borrowing costs and qualifying assets in IAS 23.	Low potential for a principles-based solution. A review of a selected sample of FTSE 350 financial statements indicated this is not a prevalent or pervasive issue.
Commodities	Develop accounting guidance for commodity loan transactions and other transactions involving commodities.	Where entities hold commodities solely for investment purposes, guidance could be developed as part of a project on non-financial assets held solely for investment purposes. A review of a selected sample of FTSE 350 financial statements indicated commodity loan transactions are not frequent in the UK.
Discontinued operations and disposal groups	Reconsider the single line-item presentation and develop more effective disclosures, or, undertake a comprehensive review of IFRS 5.	Investors and preparers have raised matters on the application of IFRS 5. In January 2016 the Interpretation Committee concluded that most of these matters would be best addressed by the planned post-implementation review of IFRS 5. We agree with this conclusion.
Discount rates	Reconsider discount rate requirements in all IFRS Standards and, when appropriate, eliminate variations in present value measurement techniques.	Whilst there are variations in permitted and required discount rates across IFRS Standards, these can be addressed on a project by project basis (e.g. Business Combinations, Goodwill and Impairment Project addressed IAS 36 discount rate requirements) and the post-implementation reviews of IFRS 15, IFRS 16 and IFRS 17 which will fall due over the IASB's next work cycle.
Employee benefits	Develop accounting requirements for hybrid pension plans; or, review IAS 19 requirements on discount rates; or, undertake a comprehensive review of IAS 19.	A review of a sample of annual reports for FTSE 350 entities identified that hybrid pension plans are becoming more common for UK IFRS reporters. IASB has issued preliminary guidance on how to apply IAS 19 to hybrid pension

9 Projects in this table are presented in alphabetical order.
10 UKEB rationale incorporates stakeholder input from initial outreach.

Project listed by the RFI[9]	IASB proposed scope per RFI	UKEB rationale for low priority[10]
		plans. The guidance provides an interim solution, so the issue is not acute. A review of IAS 19 requirements on discount rates could be undertaken as part of a broader project on discount rates.
Expenses	Develop an IFRS standard for cost of sales, using the principles of IFRS 15; develop detailed guidance on classification of expenses by function in profit or loss; develop enhanced disclosures.	IASB's *General Presentation and Disclosures* project addresses classification of expenses and disclosures on expenses. During outreach on the Primary Financial Statements project, UK stakeholders did not request further guidance on the areas proposed in the project scope. The feasibility of achieving a solution that works across multiple jurisdictions is low.
Foreign currencies	Targeted project to improve aspects of IAS 21, or, a comprehensive review of IAS 21.	Stakeholders have not identified IAS 21 as a priority project in our initial outreach.
Going concern	Develop enhanced disclosure requirements for the going concern assumption; develop accounting requirements for entities that are no longer a going concern.	IFRS Standards already contain the principles for effective disclosure of key assumptions and judgements made in determining whether an entity is a going concern. Mandating enhanced disclosure requirements may undermine the existing principles-based approach. If disclosures are inadequate, this is an application issue rather than a deficiency in financial reporting standards.
Government grants	Address optionality in accounting treatment of government grants and address inconsistency with the Conceptual Framework.	Whilst there are inconsistencies with the Conceptual Framework and optionality within the Standard, these are generally understood and stakeholders tell us that they do not cause significant problems in practice. Our desk-based research indicates that government grants only affect a minority of UK IFRS reporters and are not expected to be significant in value by the time a project would be completed.
Inflation	Assess whether it would be feasible to extend the scope of IAS 29 *Financial Reporting in Hyperinflationary Economies* to cover economies subject to only high inflation, without amending other requirements of IAS 29.	High inflation is not a prevalent or acute issue for UK IFRS reporters (even those with subsidiaries in inflationary economies). The Bank of England's May 2021 Monetary Policy Committee report predicts that UK inflation will not exceed 2% in the medium term.
Interim reporting	Develop enhanced disclosure requirements and clarify what transition disclosures are required in the first year of applying a new Standard.	Stakeholders have not identified this as an issue in our initial outreach. The FRC's thematic review on interim reporting (May 2021) indicates interim reporting is working effectively in the UK.

Project listed by the RFI[9]	IASB proposed scope per RFI	UKEB rationale for low priority[10]
Negative interest rates	Develop accounting requirements for negative interest rates.	While negative interest rates are possible in the UK, their impact on financial statements is unlikely to be pervasive because they are likely to remain close to zero and because they are unlikely to last for extended periods of time.
Operating segments	Review aggregation criteria and improve disclosures.	While operating segment information is important to investors, IASB's 2013 post-implementation review of IFRS 8 concluded that the Standard achieved its objectives and improved disclosures in this area. IFRS 8 is converged with US GAAP Topic ASC 280 which increases the difficulty of making changes to this Standard. We note that FASB's current agenda includes a review of this topic and will monitor the situation.
Other comprehensive income	Review all IFRS Standards for consistency with the Conceptual Framework principles for the classification of income and expenses in other comprehensive income.	The potential complexity of this project and challenges in finding a solution that would work across multiple jurisdictions mean that it is unlikely that timely progress would be made, and so this projects is not a priority in a time of resource constraint.
Separate financial statements	Review of IAS 27 Separate Financial Statements; clarify the accounting in separate financial statements for some transactions between a parent and its subsidiaries; develop more effective disclosures.	This topic has been considered in previous agenda consultations and has not been added to IASB's work plan. The complexity of the project combined with the limited capacity of the Board means it is unlikely that timely progress would be made on the project.
Tax	Improve tax disclosures and develop accounting guidance for emerging types of taxes.	While some investor groups have identified the need for greater tax transparency, the feasibility of developing a solution that works across multiple jurisdictions is low given the complexity of this topic. Accounting guidance on emerging types of taxes (such as carbon taxes) could be developed within the scope of the *'Climate-related risks and other emerging risks'* project.
Variable and contingent consideration	Develop a consistent approach to reporting variable and contingent consideration for all IFRS Standards.	While there is diversity in practice in reporting transactions involving variable and contingent consideration, these transactions are not sufficiently prevalent in practice to justify a high priority project at a time of resource constraint.

Question 4: Other comments
Do you have any other comments on the Board's activities and work plan? Appendix A provides a summary of the Board's current work plan.

A12 We recommend that IASB undertakes projects on a thematic basis.

A13 One way of achieving this is to take a cross-standard approach, as taken by IASB in the Disclosure Initiative. We support this approach as it supports consistency across Standards and efficiencies in the standard-setting process.

A14 In addition, projects could be grouped by theme, for example by the theme of retaining relevance as discussed above. Grouping projects by theme could help to retain focus on strategic rationale and the user needs the projects are intended to address. Such a focus could be helpful for communicating the benefits of projects, and at the project scoping stage. [See Appendix 2 for an illustration of the thematic approach.]

A15 Our stakeholders, particularly users, identified supply chain finance as an additional high-priority potential project. We note that following IASB's June board meeting a project on supply chain finance has been added to its current work plan, and so we have not included it in our list of priority projects for the IASB's 2022 – 2026 work plan.

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Appendix 2 Illustration of Thematic Approach

Projects	IAS 1	IAS 2	IAS 16	IAS 36	IAS 37	IAS 38	IFRS 8	IFRS 9	IFRS 10	Non-financial assets held for investment (new standard)
Climate-related risk	●	●	●	●	●	●	●	●	●	
Intangibles		●		●		●		●		●

Explanatory note:

Under the thematic approach, the impact of projects across Standards is considered. For example, for the climate-related risk project would look across multiple standards and explore:

(i) IASB's proposed amendments to IAS 1 and IAS 36 to ensure long-dated impacts of climate-related risk are reflected in the measurement of assets and liabilities

(ii) Implications for IFRS 9 *Financial Instruments* of the classification of ESG bonds

(iii) Implications for IFRS 10 *Consolidated Financial Statements* of whether renewable energy funds meet the investment entity criteria

(iv) Implications for IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* of whether environmental damage meets the recognition criteria for provisions

(v) Implications for IAS 38 *Intangible Assets* of whether investment in development of climate-risk reduction technologies meets the development cost capitalisation criteria

(vi) Whether additional educational material is needed for:

   a) Implications for IFRS 8 *Operating Segments* of changes in the regulatory environment due to climate-related risk.

   b) Implications for IAS 2 *Inventories* and IAS 16 *Property Plant and Equipment* due to climate-related risk.

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