Dr Andreas Barckow
Chairman
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Columbus Building
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12 March 2025

Dear Mr Barckow

Exposure Draft IASB/ED/2024/8 *Provisions – Targeted Improvements*

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 also leads the UK's engagement with the IFRS Foundation on the development of new standards, amendments and interpretations. 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.

2. There are currently approximately 1,400 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]

3. We welcome the opportunity to provide comment on the International Accounting Standards Board (IASB)'s Exposure Draft (ED) *Provisions – Targeted Improvements*.

4. To develop our response our work included in-house research (including consideration and testing of the ED proposals against real-life fact patterns relevant in the UK) and consultation with stakeholders in the UK, including academics, accounting firms and institutes, preparers, regulators and users of accounts.

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1 UKEB calculation based on LSEG and Eikon data, December 2024. 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 Watch and other proprietary data.

5. We commend the IASB's efforts to improve the clarity of the requirements in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. This is a long-standing Standard and over the years application challenges have arisen, resulting in the issuance of various IFRIC Interpretations and Agenda Decisions. However, while we support the targeted improvements to the measurement requirements, subject to some suggested enhancements, we have significant concerns about the amendments to the recognition criteria, as currently proposed.

6. Our main observations and recommendations are set out in the paragraphs that follow. Further detail and responses to the IASB's specific questions about the ED are included in the Appendix to this letter.

Recognition criteria

7. We are concerned that the proposed amendments to the recognition criteria lack clarity and are likely to increase the risk of diversity in practice and unintended consequences. This concern is also reflected in the feedback received from UK stakeholders.

8. In our view, the lack of clarity stems in part from the IASB's aim of combining a clarification of the general requirements for obligations in the scope of IAS 37 with a change in the timing of the recognition of certain levies. In the absence of any intention to change the timing of recognition for the majority of obligations in scope, these two objectives appear to conflict with each other.

9. We therefore recommend the IASB reconsiders its approach to improving the recognition criteria in IAS 37. We are not aware of significant diversity in practice in the application of IFRIC 21 *Levies* and we consider it is now well understood by stakeholders. In our view, the IASB should therefore assess whether the accounting for levies could be addressed more effectively if considered separately from the accounting for non-levy obligations. We consider the IASB's immediate focus should be on the clarification of the requirements relevant for non-levy obligations that have given rise to application challenges in the past.

10. In finalising the proposed amendments to the recognition criteria, there are a number of concerns that need to be addressed. These concerns relate to each of the proposed key elements within the present obligation recognition criterion (i.e. the obligation, transfer and past-event conditions) and would apply to both levies and non-levy obligations. Further details are presented in paragraphs A1 – A46 and A62 – A67.

Measurement – discount rates

11. We support the proposed amendment requiring entities to discount the future expenditure required to settle an obligation at a rate that reflects the time value of

money (represented by a risk-free rate)[3], with no adjustment for non-performance risk.

12. Excluding non-performance risk would create a disconnect with the measurement principle specified in IAS 37 paragraph 37 and is arguably difficult to reconcile with paragraphs 6.15 and 6.20 of the *Conceptual Framework for Financial Reporting* (Conceptual Framework). Consequently, we recommend the IASB clarifies that the proposed amendment is an exception to the measurement principle, as envisaged in paragraph 6.92 of the Conceptual Framework.

13. We also support the proposed disclosure requirements. However, we believe those could be further refined so they result in more useful information for users of accounts.

14. Further details are presented in Appendix A paragraphs A51 – A56.

Measurement – expenditure required to settle an obligation

15. We welcome the proposed clarification on the expenditure required to settle an obligation. However, we consider that further application guidance and examples should also be provided to facilitate consistent application.

16. In particular, we believe the IASB should clarify whether the proposed amendment would be applicable to all provisions or only those to be settled by providing goods or services. If the proposed clarification were applicable to all provisions, we consider that further guidance would be needed on how the requirements would be applied to obligations not settled by the provision of goods or services, such as legal claims.

17. Further details are presented in Appendix A paragraphs A48 – A50.

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

[3] And the risks surrounding the amount or timing of the expenditure required to settle the obligation if those risks are not reflected in the estimates of the future cash flows.

Appendix A: Questions on IASB/ED/2024/8 *Provisions – Targeted Improvements*

Question 1—Present obligation recognition criterion
The IASB proposes: • to update the definition of a liability in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* to align it with the definition in the *Conceptual Framework for Financial Reporting* (paragraph 10); • to align the wording of the recognition criterion that applies that definition (the present obligation recognition criterion) with the updated definition of a liability (paragraph 14(a)); • to amend the requirements for applying that criterion (paragraphs 14A-16 and 72-81); and • to make minor amendments to other paragraphs in IAS 37 that include words or phrases from the updated definition of a liability (Appendix A). The proposals include withdrawing IFRIC 6 *Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment* and IFRIC 21 *Levies* (paragraph 108). Paragraphs BC3-BC54 and BC86 of the Basis for Conclusions and Appendix A to the Basis for Conclusions explain the IASB's reasoning for these proposals. Do you agree with these proposals? Why or why not? If you disagree, which aspects do you disagree with and what would you suggest instead?

A1. As noted in our cover letter, the UKEB has significant concerns that the proposed amendments to the recognition criteria, as set out in the ED, lack clarity and are likely to increase the risk of diversity in practice and unintended consequences.

A2. We therefore recommend the IASB reconsiders its approach to improving IAS 37. We consider the IASB's immediate focus should be on the clarification of the requirements relevant for non-levy obligations that have given rise to application challenges in the past.

A3. If the IASB nevertheless decides to finalise the proposed amendments to the recognition criteria, we consider the IASB will need to address the concerns set out in the following paragraphs.

Obligation condition

A4. The use of the word 'obligation' in the first condition in paragraphs 14A and 14B seems inconsistent with the normal usage of that term in the English language. In accordance with 14B an entity has an obligation ***if:***

a) a mechanism is in place that imposes a responsibility on the entity ***if*** it obtains specific economic benefits or takes a specific action;

b) the responsibility is owed to another party; and

c) the entity has no practical ability to avoid discharging the responsibility ***if*** it obtains the specific economic benefits or takes the specific action.

A5. As currently proposed, therefore, the obligation condition tests the existence of a *conditional/contingent* obligation. We recommend the IASB reconsiders the terminology used. As currently proposed, there is a risk of confusion in particular in relation to the distinction between the obligation condition and the past-event condition.

A6. In addition, we note that the IASB proposes to replace the requirement in IAS 37 paragraph 17 that a legal obligation can be 'enforced by law' with a more detailed description of circumstances in which an entity would have no practical ability to avoid discharging a legal obligation. ED paragraph 14F introduces a form of economic compulsion in the 'no practical ability to avoid test' for legal obligations. The test requires an assessment of whether the economic consequences for the entity of not discharging the legal responsibility are expected to be *significantly worse* than the costs of discharging it.

A7. The proposed requirement has raised questions as to whether such an assessment should impact the recognition or only the measurement of a provision. For example, if the economic consequences for the entity of not discharging a legal responsibility were *not* expected to be *significantly worse*, but perhaps were expected to be *similar to* or *lower than* the costs of discharging it, we believe that the entity would still have an obligation. The impact of the proposed assessment in paragraph 14F(a)(ii) should then be reflected in the measurement of the provision (assuming all the recognition criteria were met). We recommend the IASB clarifies the proposed requirement.

A8. In addition, the proposals introduce the need for judgement as to what is considered to be 'significantly worse'. Although the proposed description is based on concepts in paragraph 4.34 of the Conceptual Framework, we observe that the terminology is not consistent. CF 4.34 uses the term 'significantly more adverse' and the ED 14F(a)(ii) 'significantly worse'. If the IASB decides to proceed with this proposal, we recommend aligning the terminology used and providing further guidance as to the intended application of this amendment.

Transfer condition

A9. The ED introduces into IAS 37 an explicit distinction between a *transfer* and an *exchange* of economic resources. The proposals have brought attention to a distinction that stakeholders might not necessarily have assessed specifically in the past. This creates the risk of unintended consequences, including perhaps the reassessment of entities' existing obligations.

A10. The distinction between the two concepts is not always clear cut. For example, there are mixed views over whether certain levies are transfers or exchanges. One view is to consider levies as non-reciprocal transactions in which an entity paying a levy receives no economic resources directly in exchange for the payment. An alternative view is that by paying a levy an entity receives, for example, a right to operate, similar to a licence. The proposed examples relating to levies state that the nature of the obligation is a transfer without explaining how such a conclusion might be reached.

A11. Questions also arise as to whether outsourcing the settlement of an obligation can affect recognition by converting it into an exchange. See further details under the heading 'Outsourcing vs internal costs' below.

A12. Challenges have been recognised in the past in IFRIC agenda papers which have set out the difficulties in assessing the difference between exchange and transfer[4].

A13. This is made particularly complex by the fact that the terms 'transfer' and 'exchange' are used widely in IFRS and not all usage seems consistent with the proposals in the ED. The ED seems to present the concept of transfer as a 'one-way' transaction, for which the entity gets nothing in return. Proposed paragraph 14L states: "An obligation to exchange economic resources with another party is not an obligation to transfer an economic resource to that party unless the terms of the exchange are unfavourable to the entity." This use of the term transfer is different from how it is currently used elsewhere in IAS 37 and in other IFRS Accounting Standards where it has a simple, neutral meaning, and where a transfer is part of an exchange (e.g. see IAS 37 paragraph 37 and IFRS 15 *Revenue from Contracts with Customers* paragraph 2).

A14. It is our understanding that the addition of the transfer condition is intended to reinforce the scope of the Standard. That is, that an entity does not recognise a provision for a future exchange transaction (an executory contract), unless that transaction is onerous. The question therefore arises as to whether the transfer

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4 For example, IFRS Interpretations Committee January 2013 meeting - Agenda Paper 16, in paragraph 11 IFRIC staff state "We do not think that the Interpretations Committee should introduce a new notion into IFRS, namely the notion of 'exchange transaction'. We think that determining whether a levy is an exchange transaction is highly subjective and that this will result in diversity in practice……."

condition is needed at all given that the scope of IAS 37 already excludes executory contracts (unless onerous). Also, in our view omitting the transfer condition would not change the conclusion of any of the proposed examples in the Guidance.

A15. Assuming the IASB goes ahead with the proposed transfer condition, we recommend the IASB considers refining the terminology[5] to improve the clarity in the Standard to support understandability and reduce the risk of diversity in practice. In any event, and in particular given the inconsistency with the use of the term elsewhere in IFRS Accounting Standards, we consider that more explanation is required.

A16. We also consider that the analysis in some of the examples in the Guidance should provide greater clarity as to why the relevant outflow of resources does or does not meet the transfer condition. For example:

a) ED Examples 1, 2 and 3 simply state that the obligation is expected to require the provision of repair, clean up or restoration services, but do not analyse why this represents a transfer within the terms of the proposals. See also A17-A18 below.

b) ED Example 6 –

i. Obligation to fit smoke filters: it would be helpful if the analysis explained whether it made a difference if the smoke filters were capitalised or expensed. If not, why not? (Contrast Example 11B which implies that the enhancement of future economic benefits embodied in the aircraft is the reason why the expenditure is not a transfer.)

ii. Obligation to pay fines: the analysis states that this obligation meets the transfer condition because “it is an obligation that has the potential to require the entity to pay cash.” However, that is insufficient to distinguish the obligation from an exchange, which might also require the payment of cash.

Outsourcing vs internal costs

A17. The introduction of the transfer condition also gives rise to questions as to whether outsourcing the settlement of an obligation (to provide clean-up services, for instance, or staff training) can affect recognition by converting it into an exchange. For example, would the assessment of the transfer condition in Examples 2A/2B of the Guidance change to be similar to that in Example 7 if the

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5 For example, to convey the notion that what seems to be meant is ‘net’ transfer.

entity outsourced the work needed to provide the clean-up service (as the transaction could be considered an exchange)?

A18. In our view, outsourcing the settlement of the obligation should not affect the assessment of such an obligation. Outsourcing results in the entity entering into a separate transaction, giving rise to a new obligation. The fundamental obligation (e.g. to clean up an operating site) is potentially owed to the Government on behalf of the public at large, while the outsourcing creates a new (contractual) obligation owed to a third party. Those are two separate obligations (or units of account) which should be assessed separately. We recommend the IASB makes this clearer in the Standard and/or the Guidance and revises Examples 2A, 2B and 7 to reflect this.

Past-event condition

A19. For simple scenarios with few basic steps, the proposed amendments to the past-event condition do not appear to present particular difficulties. However, the requirements are not so clear when applied to levies, and in particular when applying the requirement in proposed paragraph 14Q for obligations to transfer an economic resource *only if an entity takes two (or more) separate actions*.

A20. There is therefore a risk that diversity in practice could arise, and the same levy could be accounted for differently by entities within the same jurisdiction.

A21. In withdrawing IFRIC 21 *Levies* the proposed amendments would be applicable to *all* obligations in the scope of IAS 37, not only levies. The risk of unintended consequences is therefore an important matter that needs to be considered.

A22. Areas in which we consider further work is needed to enhance the clarity of the requirements include:

a) The term 'action' is not defined or explained in detail in the Amendments and questions therefore arise in relation to the identification of relevant actions when applying the Amendments. Refer to A23-A26.

b) The distinction between what is an action and what is a measurement basis is not clear. Refer to A27-A29.

c) Complexity is added by the requirement in proposed paragraph 14Q for obligations that arise only if an entity takes two (or more) separate actions. The question arises as to whether such guidance is needed for all obligations, or whether it could be limited to levies. Refer to A30-A36.

d) The intended application of the threshold-triggered costs requirement (in proposed paragraph 14P) is not clear for balance sheet thresholds. Further clarity is also needed on the potential interaction with other requirements within the Standard (such as paragraph 14Q). Refer to A37-A40.

e) It is not clear whether the reference to specific economic benefits is needed in the context of the assessment for obligations in the scope of IAS 37. Refer to A41-A43.

f) The proposals suggest removing the existing requirement in IAS 37 paragraph 18 (i.e. that no provision is recognised for costs that need to be incurred to operate in the future). In our view the IASB should consider retaining this well-understood articulation of this fundamental concept in the Standard. Refer to A44.

g) The distinction between the two no practical ability to avoid tests, in the obligation and the past-event conditions, and their proposed application, could be clearer. Refer to A45-A46.

Identifying actions

A23. Paragraphs 14N and 14O contain a reference to 'specific action', but 'action' is not defined in the proposed amendments. Without a clearer principle and/or a definition of 'action' different possible interpretations could arise as to the identification of actions, including for the same levy, by different entities within the same jurisdiction.

A24. We understand that the identification of the relevant actions(s) is not a question of management's judgement but based on the relevant 'mechanism' imposing the responsibility on the entity. For example, it could be the specific details of a constructive obligation, the terms and conditions of a contract or the requirements in legislation. However, that is not specifically stated in the proposed amendment to the Standard.

A25. We consider it would be helpful to include in the Standard the rationale in paragraph BC36, including that management would reach a conclusion by assessing all the relevant facts of the mechanism imposing the responsibility on the entity.

A26. In addition, at present it is difficult to rationalise precisely what leads to the identification of an 'action', and therefore to clearly understand the differences between the examples in the Guidance. We consider this should be more clearly articulated in the analysis and conclusions for the different examples presented in the Guidance.

Examples – Identifying actions

We consider the analysis of some of the examples proposed by the IASB could be perceived as confusing or even contradictory. For example:

- Example **13B** considers that there are *two distinct actions*, that is, operating in the entity's current annual reporting period and operating as a bank on the last day of

that same period. It is not clear from the fact pattern or the analysis why operating in the period is a separate action.

- It would be helpful to explain the rationale for the differences from the conclusion in **Example 13C**, where *only one action* is identified. By analogising to Example 13B, without further clarification it could be argued that ownership of the property throughout the year is an action, and an assessment would be needed as to whether the entity has a practical ability to avoid ownership of that property as of year-end.
- It would also be beneficial to explain the apparently different approach in the proposed guidance for **threshold-triggered costs**, which assumes that the generation of revenue during a period represents only one action (as noted in view 3 in April 2024 - IASB staff Agenda Paper 22B[6]).
- In considering the application of the proposed requirements to certain obligations relevant in the UK (such as bank levies) for which an amount is payable if an entity holds a specified level of deposits at a specified date, questions arise as to whether the relevant action is holding deposits at a specified date, the origination of deposits, or both.

  Given the proposed introduction of a 'no practical ability to avoid test', if the origination of deposits were considered an action, a subsequent question arises as to whether for term deposits a provision for the levy would therefore be accrued throughout the term of the deposit (assuming the other recognition criteria were met). Such an accrual could extend over more than one financial reporting period. We recommend the IASB provides application guidance to clarify the intended application of the proposals to such circumstances. Refer also to A40 for considerations on thresholds.

Distinction between action and measurement basis

A27. The challenges in the identification of actions also give rise to questions about the distinction between what is a measurement basis and what is an 'action' for purposes of the proposed amendments.

A28. At present, the examples in the Guidance (in particular Examples 13A – 13C) seem to blur this distinction. We therefore recommend that this distinction is made clearer in those examples to avoid the risk of diversity in practice.

6 The IASB tentative decision on threshold-triggered costs was based on view 3, which notes that irrespective of whether the measure of the entity's activity is below or above the threshold, there is only one activity (e.g. generating revenue or emitting gasses).

Examples – Distinction between action and measurement basis

- As proposed, **Example 13A** assumes that the generation of revenue in the market in 20X0 is an 'action'. However, given that the fact pattern notes that only entities operating in the market on 1 January 20X1 are within the scope of the levy, it could be argued that the generation of revenue during 20X0 is not an action but only the basis for measuring the obligation.
- There are levies where for practical reasons the measurement is based on an earlier reporting period. For example, the amount of **Bank of England Levy** payable is based on the average amount of deposits held in a specific three-month period prior to the start of the Levy Year (the Reference Period). However, where an institution has become an eligible institution during the Reference Period, the Bank of England may use such other period of no more than three months as it sees fit. Questions arise such as:
  a) Would the fact that an alternative measurement period could be applied in certain circumstances have an impact on the assessment of the relevant actions?
  b) Could the existence of an alternative measurement period support the argument that holding a specified amount of deposits in the Reference Period is not 'an action' (as it might not be directly applicable to all institutions in scope of the levy) but only a measurement basis?
  c) If holding a specified amount of deposits in the Reference Period was considered 'an action', would entities need to account for a provision (assuming all other recognition criteria are met) in the Reference Period? If so, would the recognition be at a point in time or accrued over the Reference Period, and would either of these be an appropriate accounting outcome?
- As noted above, **Example 13B** considers that there are *two actions*, that is, operating in the entity's current annual reporting period and operating as a bank on the last day of that period. We understand that the conclusion that there are two actions may depend on the fact that the amount charged is adjusted when the chargeable period is not equal to 12 months. This may imply that the operation as a bank during the period is also necessary to trigger the obligation and is not only a measurement basis. However, this is not clear from the fact pattern or explicit in the analysis. We recommend clarifying the rationale for the pro rata reduction to be considered an action and not a factor in measurement.

A29. We consider that, in addition to clarifying the principles and expanding the explanations of proposed Examples 13A – 13C, a possible way to reinforce the distinction between an action and a measurement basis could be by expanding the analysis of some of the proposed examples. It could potentially be done by adding an *alternative scenario* – with slightly modified facts from the *base*

scenario – explaining the rationale for reaching a different conclusion based on the different facts. For example, if in a base scenario it was concluded there were two separate actions, the alternative scenario could discuss what would need to be different for concluding that one of those actions was only a measurement basis.

Requirements for obligations that arise only if an entity takes two (or more) separate actions

A30. The requirement in proposed paragraph 14Q for obligations that arise only if an entity takes two (or more) separate actions adds complexity and has given rise to stakeholder confusion.

A31. We question whether the assessment in 14Q is needed for non-levies. The only situations where more than one action is identified in the IASB's proposed examples, for non-levies, are in the case of restructuring obligations (Examples 5A and 5B).

A32. In the case of these examples, the ED sets out that there are two actions (i.e. employing a person for at least a year and terminating the employee's contract). However, it is not wholly clear that employing a person for at least a year should constitute an action:

a) It can be argued that the question of whether an individual has been employed for a year determines whether there is an obligation, not whether there has been an action. In other words, it relates to the obligation condition, not the past event condition. If an individual has not been employed for a year, there is no mechanism that imposes an obligation ***if*** the entity terminates their contract. The only action is therefore the termination of the employee contract.

b) Alternatively, the past employment of a person might perhaps be viewed as a measurement basis. That is, the length of the employment dictates only the measurement of the liability. This argument reinforces the need for further clarity in relation to the distinction of actions from measurement bases as discussed in A27 – A29 above.

A33. Further, the IASB's conclusion that there are two actions introduces judgement over when termination of contracts becomes unavoidable, and could potentially bring forward recognition.

A34. Similar concerns would apply to the analysis and conclusion in respect of customer contracts in Example 5B, where again two actions are identified (i.e. entering into a contract with a customer and then terminating the contract). However, it can be argued that the contract provides the mechanism that imposes an obligation on the entity **if** the entity terminates the arrangement. Again,

therefore, entering into the contract might satisfy the obligation condition but is not necessarily relevant to the past-event condition.

A35. Further, if entering into a contract was considered an action, that could imply that every contractual arrangement an entity entered into would constitute a 'first action', potentially bringing such contract(s) in the scope of IAS 37. That would therefore require an assessment of the entity's practical ability to avoid any subsequent actions that might require an outflow of resources for every single contract an entity entered into.

A36. Given that we are not currently aware of significant issues with the accounting for restructuring obligations under the existing requirements in IAS 37, and the complexity noted in the above paragraphs, we recommend the IASB reconsiders whether the assessment in 14Q is really needed for non-levy obligations.

Threshold-triggered costs

A37. The proposed guidance on threshold-triggered costs seems clear and straightforward when it comes to assessing income statement-related thresholds. The resulting accounting outcome seems sensible. Although it might increase the level of estimation uncertainty as part of the assessment of the present obligation recognition criterion, in reaching a conclusion on whether a provision should be recognised, an entity would also need to consider whether the probable outflow criterion (IAS 37 14.b) and reliable estimate criterion (IAS 37 14.c) were met.

A38. However, it is not so clear whether and, if so, how the threshold-triggered cost guidance might apply when the threshold is a balance sheet-based measure, as it is in the case for some levies. A balance sheet measure does not generally accrue in a similar manner to an income statement measure and it could potentially remain at a similar level throughout a reporting period.

A39. In addition, we consider the interaction of the requirements in proposed paragraphs 14P (threshold-triggered costs) and 14Q (obligations triggered only if an entity takes two or more separate actions) should be made clearer, to indicate what would take precedence if both requirements were relevant for the same fact pattern.

A40. For example, the UK Bank Levy is charged if an entity is a bank or a building society at the end of its annual reporting period and its aggregate chargeable equity and liabilities (deposits) exceed a £20 billion allowance. Alternative views could arise on how the proposals apply:

a) Paragraph 14Q applies - an entity needs to identify the relevant actions to assess whether there is present obligation as a result of a past-event as of the reporting date. If an entity concluded that there is only one action (operating as a bank or building society at the end of its annual reporting period), and that action was met, a provision would be accounted for at a

point in time. Refer to paragraph A26 for alternative views on identifying actions.

b) Paragraph 14P applies – the £20 billion allowance is considered a threshold for purposes of the proposed amendments. If the bank concludes that it is probable that its chargeable equity and liabilities will exceed the specified £20 billion threshold and a reliable estimate can be made of the amount of the obligation, a provision is accumulated over time (i.e. potentially over the full reporting period).

Specific economic benefits

A41. The purpose of the reference to 'specific economic benefits' in the context of obligations in the scope of IAS 37 is not clear. To aid understanding of the proposed amendments, it would be helpful if the IASB provided an example of a circumstance where an entity has a present obligation that exists as a result of a past-event when the entity obtained specific economic benefits (as opposed to taking an action) and such an obligation is in the scope of IAS 37[7].

A42. However, if a reference to receiving economic benefits is not directly relevant to the assessment in IAS 37, we would suggest removing it to avoid confusion and/or unnecessary complexity.

A43. We acknowledge that proposed Example 6 (smoke filters), Example 7 (staff retraining), Example 11A (refurbishment costs – furnace lining) and Example 11B (refurbishment costs - aircraft overhaul) all mention in their analyses 'economic benefits'. However, in each case economic benefits are mentioned in the context of explaining that the fact pattern relates to a *future* economic exchange. In our view, omitting the reference to specific economic benefits would not change the conclusion for any of those examples, given that future economic exchanges are not in scope of IAS 37 (unless onerous) and therefore no provision is recognised. See also paragraph A65 below for further comment on this point.

Existing paragraph 18

A44. We note that the IASB proposes to remove the existing requirement in IAS 37 paragraph 18 that no provision is recognised for costs that need to be incurred to operate in the future. In our view, this requirement is a fundamental and well understood concept in the Standard. We consider that the IASB should consider retaining this articulation of the requirement in IAS 37 as it would enhance understanding and help reinforce the proposed principle in paragraphs 14N and 14O, reducing the risk of unintended consequences.

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7 That is, other than a future exchange transaction (executory contract) that is not onerous or an obligation in the scope of other IFRS Accounting Standards (such as IAS 19 *Employee Benefits* or IFRS 9 *Financial Instruments*).

No practical ability to avoid test

A45. Having the no practical ability to avoid test in two different aspects of the proposed amendments can be confusing. We understand that the proposed amendments introduce the test in two subtly different ways:

a) No practical ability to avoid test within the obligation condition (ED paragraphs 14B(c) and 14F). We understand this test is in effect a test of the 'strength of the mechanism' (i.e. legal or constructive) imposing the obligation.

b) No practical ability to avoid test within the past-event condition (ED paragraph 14Q). This arises only when two or more actions are needed to trigger the transfer of an economic resource. Here, however, we understand the test appears to relate not to the strength of the mechanism but to the realistic options available to management in relation to any remaining actions as of the reporting date.

A46. We recommend the IASB describes more explicitly, either in the Standard or in accompanying guidance that is integral to the Standard, the difference between the two tests and the intended application to facilitate consistent application.

Application of the recognition and measurement rules - Restructuring

A47. The IASB has proposed limited editorial amendments to the section in IAS 37 'Application of the recognition and measurement rules – Restructuring'. As proposed, some of the restructuring guidance could be perceived as confusing or inconsistent with other proposals in the ED. For example, proposed paragraph 72 states that "A present obligation for the costs of a restructuring arises only when an entity:….b) has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan ***or*** announcing its main features to those affected by it". This could be read by some as implying that an announcement is enough to create a present obligation. In our view, it would be a missed opportunity if the IASB were to amend IAS 37 without giving further consideration to the guidance in paragraphs 70 - 81.

Question 2—Measurement - Expenditure required to settle an obligation
The IASB proposes to specify the costs an entity includes in estimating the future expenditure required to settle an obligation (paragraph 40A). Paragraphs BC63 – BC66 of the Basis for Conclusions explain the IASB's reasoning for this proposal. Do you agree with this proposal? Why or why not? If you disagree, what would you suggest instead?

A48. We support the proposed clarification of the costs an entity includes in estimating the future expenditure required to settle an obligation. However, we consider that further application guidance and examples should also be provided to facilitate consistent application.

A49. In particular, we believe the IASB should clarify whether the proposed amendment would be applicable to all provisions or only those to be settled by providing goods or services[8].

A50. If the proposed amendment is applicable to all provisions, we consider that guidance is needed on how the requirements would be applied to obligations not settled by the provision of goods or services, such as legal claims, where it is our understanding that diversity in practice currently exists. Some entities consider external legal costs to be a separate unit of account - an executory contract for which the entity will receive future legal services - which are therefore not in the scope of IAS 37. More clarity is needed on the intended application of the amendments including, for example, whether a distinction should be made between internal/external costs.

Question 3—Discount rates
The IASB proposes to specify that an entity discounts the future expenditure required to settle an obligation at a rate (or rates) that reflect(s) the time value of money – represented by a risk-free rate – with no adjustment for non-performance risk (paragraphs 47-47A). The IASB also proposes to require an entity to disclose the discount rate (or rates) it has used and the approach it has used to determine that rate (or those rates) (paragraph 85(d)). Paragraphs BC67-BC85 of the Basis for Conclusions and Appendix B to the Basis for Conclusions explain the IASB's reasoning for these proposals. Do you agree with: a) The proposed discount rate requirements; and b) The proposed disclosure requirements? Why or why not? If you disagree, what would you suggest instead?

A51. We support the proposed amendment to require entities to discount the future expenditures expected to be required to settle an obligation at a rate (or rates) that reflect(s) the time value of money (represented by a risk-free rate) and "the risks

8 As mentioned in IASB Webcast: Exposure Draft Provisions - Targeted Improvements.

surrounding the amount or timing of the expenditure to settle the obligation", which we understand would exclude non-performance risk.

A52. The exclusion of non-performance risk in the measurement of a liability is not a new concept in IFRS Accounting Standards, as it is already required in IFRS 17 *Insurance Contracts*. We consider the proposed requirements would reduce diversity in practice.

A53. In this regard, we note that measuring a provision liability with no adjustment for non-performance risk would create a disconnect with the measurement principle specified in IAS 37 paragraph 37 and is arguably difficult to reconcile with paragraphs 6.15 and 6.20 of the Conceptual Framework. Consequently, we recommend the IASB considers clarifying that the proposed amendment is an exception to the measurement principle as envisaged in paragraph 6.92 of the Conceptual Framework.

A54. We also support the proposed requirement to disclose the discount rate(s) used and the approach used to determine such rate(s). However, we believe the proposed disclosures could be further refined so they result in more useful information for users of accounts. Our recommendations are provided below.

A55. During the development of the proposals in the ED, the IASB decided[9] against providing application guidance on how an entity determines what is an appropriate risk-free rate. In practice, even within the same jurisdiction, different views could arise as to which rates are risk-free, leading to a potentially significant impact in the measurement of long-term provisions. This situation is not apparent for users of accounts from existing disclosures in financial statements. We recommend the IASB considers requiring:

a) more granular disclosure in relation to the approach used to determine the discount rate - that is, disclosing not only the fact that the entity used a risk-free rate but also identifying the actual rate(s) used (e.g. UK gilt yields, swap rates or other); and

b) disclosure of a sensitivity analysis that shows how the amount of a provision would have been affected by changes in the discount rate used, if the effect of discounting is significant. Disclosure of the methods and assumptions in preparing the sensitivity analysis should also be required.

A56. IAS 37 currently requires entities to consider relevant risks and uncertainties in reaching the best estimate of a provision. However, the Standard does not provide detailed application guidance as to *how* those risks and uncertainties should be determined. We acknowledge that IAS 37 paragraph 85(b) requires disclosure of an indication of the uncertainties about the amount or timing of future outflows;

9 As noted in Basis for Conclusions paragraph BC81-BC82.

however, users of accounts demand more granular disclosure (including quantitative information) about the measurement uncertainty of provisions. They consider this information would allow them to make better informed decisions as part of their work. We recommend the IASB considers making the disclosure requirements on measurement uncertainty more specific.

Question 4—Transition requirements and effective date
4(a) Transition requirements The IASB proposes transition requirements for the proposed amendments (paragraphs 94B-94E). Paragraphs BC87-BC100 of the Basis for Conclusions explain the IASB's reasoning for these proposals. Do you agree with these proposals? Why or why not? If you disagree, which aspects do you disagree with and what would you suggest instead? **4(b) Effective date** If the IASB decides to amend IAS 37, it will decide on an effective date for the amendments that gives those applying IAS 37 sufficient time to prepare for the new requirements. Do you wish to highlight any factors the IASB should consider in assessing the time needed to prepare for the amendments proposed in this exposure draft?

A57. As noted in our cover letter, we support the proposed amendments to the measurement requirements in IAS 37, but we have significant concerns that the proposed amendments to the recognition criteria, as set out in the ED, lack clarity and are likely to increase the risk of diversity in practice and unintended consequences. We therefore recommend the IASB reconsiders its approach to improving the recognition criteria in IAS 37.

A58. We support the proposed retrospective application of the proposed measurement requirements, with the two exceptions in proposed paragraphs 94D and 94E. However, we have some concerns about the potential complexity introduced by proposing exceptions to be applied at two different dates:

a) The exception in relation to the costs an entity includes in the measurement of a provision is proposed to be applied as of the *date of initial application* (as defined in proposed paragraph 94B(b).

b) The exception in relation to the requirements on discount rates is proposed to be applied at the *transition date* (as defined in proposed paragraph 94B(a).

A59. We understand the proposed exceptions are consistent with transitional provisions in previous IASB projects[10], but we note that those were introduced at different times and were therefore not applied in combination. We recommend the IASB considers whether both exceptions should be applied at the same date (i.e. date of initial application or transition date).

A60. In addition, we suggest clarifying whether the discount rate to be used in applying the exception proposed in paragraph 94E is the rate that is current at the transition date or at the reporting date. Given the complexity of the transition requirement, we also recommend the IASB adds to the application guidance in IAS 37 an illustrative example (such as one based on the example presented at the IASB June 2024 meeting[11]).

Question 5— Disclosure requirements for subsidiaries without public accountability

The IASB proposes to add to IFRS 19 *Subsidiaries without Public Accountability: Disclosures* a requirement to disclose the discount rate (or rates) used in measuring a provision, but not to add a requirement to disclose the approach used to determine that rate (or those rates) (Appendix B).

Paragraphs BC101-BC105 of the Basis for Conclusions explain the IASB'S reasoning for this proposal.

Do you agree with this proposal? Why or why not? If you disagree, which proposal do you disagree with and what would suggest instead?

A61. We support the proposed requirement in IFRS 19 to disclose the discount rate (or rates) used in measuring a provision.

Question 6— Guidance on implementing IAS 37

The IASB proposes amendments to the *Guidance on implementing IAS 37 Provisions, Contingent Liabilities and Contingent Assets.* It proposes:

a) to expand the decision tree in Section B;

b) to update the analysis in the illustrative examples in Section C; and

c) to add illustrative examples to Section C.

Paragraphs BC55-BC62 of the Basis for Conclusions explain the IASB's reasoning for these proposals.

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10 Transitional provision to Amendment '*Onerous Contracts – Cost of Fulfilling a Contract*' issued in May 2020 and that provided to first-time adopters of IFRS Accounting Standards by IFRS 1 *First-time Adoption of International Financial Reporting Standards*, paragraph D21.

11 Example presented in IASB Agenda Paper 22B - June 2024 meeting.

Do you think the proposed decision tree and examples are helpful in illustrating the application of the requirements? If not, why not? Do you have any other comments on the proposed decision tree or illustrative examples?

A62. As noted in our cover letter, the UKEB has significant concerns that the proposed amendments to the recognition criteria, as set out in the ED, lack clarity and are likely to increase the risk of diversity in practice and unintended consequences. We therefore recommend the IASB reconsiders its approach to improving IAS 37.

A63. Our concerns about the proposed recognition criteria are reflected in the proposed amendments to the examples in the Guidance. If the IASB nevertheless decides to finalise the proposed amendments to the recognition criteria, we therefore consider the IASB will need to address the concerns set out in the following paragraphs.

A64. We consider the analysis in some of the examples is problematic and could even be perceived as inconsistent or contradictory. In our responses to Question 1 above we refer to several aspects of the examples that should be reconsidered, including:

a) Transfer condition – we consider the analysis of the relevant outflow in the examples needs enhancing to provide greater clarity over why the transfer condition is or is not met. See our comments in A9-A18.

b) 'Two or more actions' – We highlight the complexity of the proposed requirements in paragraph 14Q and question the need for such assessment for obligations other than levies. The IASB could consider whether those requirements could be limited to levies only. This would impact in particular the analysis for Examples 5A and 5B without changing their conclusion. See our comments in A30-A36.

c) Action vs measurement – We recommend further clarity in relation to the identification of relevant actions and the distinction between what is an action and what is a measurement basis for purposes of the proposed amendments. The examples in the Guidance, in particular Examples 13A – 13C, seem to blur this distinction. We therefore recommend that the distinction is made clearer in those examples to avoid the risk of diversity in practice. See our comments in A23-A29 above.

A65. In addition, as explained in paragraph A43 above, in our view the analysis for several examples is more complex than it needs to be because it refers to future exchange transactions when assessing the facts against the past event condition.

a) Proposed Example 6 (smoke filters), Example 7 (staff retraining), Example 11A (refurbishment costs – furnace lining) and Example 11B

(refurbishment costs - aircraft overhaul) all refer to *future* economic exchanges in the past-event analysis. We consider that this analysis of the past-event condition is not necessary and recommend omitting it to avoid confusion.

b) In those examples a past-event condition analysis would only be necessary for those obligations that are not future economic exchanges. For example, in the case of Example 6, the analysis would not be needed for the 'obligation to fit smoke filters' but would be relevant for the 'obligation to pay fines'.

c) Our recommendation is in line with the IASB's analysis in proposed Example 15, for which there is no analysis for the past-event condition in relation to the 'obligation to reduce emissions' and an analysis is only presented for the 'obligation to offset remaining emissions'.

A66. While we agree with the overall conclusion for Example 7 (no provision), in our view the analysis is unclear and hard to reconcile to other examples:

a) Obligation condition – it is not clear how the facts and analysis differ from those in other examples in which the obligation is assessed to be owed to the government, specific groups of individuals or society at large (see e.g. Examples 2, 6, and 11 amongst others). From the facts it might appear that the entity has no practical ability to avoid complying with financial services regulation: if it continues to operate after 20X1 it will have no practical ability to avoid incurring retraining costs ("will need to retrain … to ensure continued compliance…"). It does not seem convincing to argue that retraining will be carried out for the entity's own benefit – ultimately everything undertaken by an entity is for its own benefit - and it could be argued that it has a responsibility owed to customers. On the face of it there is a legal mechanism that imposes an obligation that cannot be avoided if the entity continues to operate.

b) Transfer condition – the analysis states that retraining staff will be an exchange transaction not a transfer. However, it is not clear how this example differs from Examples 2A and 2B, since clean-up services are also likely to involves sub-contracting work to third parties, but in those examples the transfer condition is considered to be met. The analysis in Example 7 could be read to imply that if the entity undertook retraining 'in-house' then the transfer condition might be met.

c) Past-event condition – the analysis refers to the future exchange transaction (receiving training services) which should in any event be out of scope of IAS 37. It would perhaps be simpler and more relevant to explain that the past-event condition is not met because the only triggering event would be operating post-20X1.

A67. Finally, in Example 14 the relevant legislation imposes a government target in relation to an entity's average fuel emissions resulting from car manufacturing. We recommend adding analysis in relation to threshold-triggered costs or clarifying why the Government target is not a threshold for these purposes.

Question 7—Other comments
Do you have comments on any other aspects of the proposals in the Exposure Draft?

Consequential amendment to IFRS 3 *Business Combinations*

A68. We recommend the IASB considers whether an exception to the measurement principle in IFRS 3 is needed for provisions in scope of IAS 37.

A69. The interaction of the measurement requirements in IFRS 3 (fair value measurement) and the measurement requirements in IAS 37 (discount rates with no adjustment for non-performance risk), could result in a Day 2 change to the amount of the provision. The corresponding impact could be on profit or loss or, in the case of decommissioning, restoration and similar liabilities, could result in:

a) an adjustment to the value of the related asset[12]; or

b) an adjustment to the revaluation surplus or deficit on the related asset[13].

12 If the related asset is measured using the cost model.

13 If the related asset is measured using the revaluation model.