UK Endorsement Board

Dr Andreas Barckow
Chairman
International Accounting Standards Board
Columbus Building
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Canary Wharf
London
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[XX 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*. To develop our [draft] response our work [to-date] has included in-house research and consultation with stakeholders in the UK, including academics, accounting firms and institutes, preparers and users of accounts. [Our work on these matters continues and will inform our final comment letter.]

4. We welcome 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

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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.

standard and over the years application challenges have arisen, resulting in the issuance of various IFRIC Interpretations and Agenda Decisions.

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

Provisions - recognition criteria

6. Whilst we support the objective of clarifying the recognition criteria, we are concerned that the current proposals may create new interpretation issues. We support the proposal to amend the examples in the *Guidance on implementing IAS 37* (Guidance). Updating the analysis of the existing examples to reflect the proposed amendments and adding new examples should improve understanding of the intended application of the proposed requirements and facilitate application of the concepts to different fact patterns. It is important, however, that the rationale for the treatment should be fully explained. We found it challenging to apply the same rationale to other fact patterns. We have therefore identified some areas where we consider that further work may be needed before the proposals are finalised to avoid the risk of unforeseen consequences and, potentially, increased diversity in practice.

   a) In relation to the transfer condition, we consider that a clear principle is needed in the standard to clarify the difference between a transfer and an exchange. 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. Without further clarification there is a risk of confusion and increased diversity in practice. [Appendix A paragraphs A8 – A12]

   b) Regarding the past-event condition, the underlying principle behind the requirements in relation to obligations to transfer an economic resource only if an entity takes two (or more) separate actions is not clear. How should an entity approach the separate identification of individual actions in order to apply the requirements to their specific circumstance? In particular, there is some confusion around the distinction between actions and measurement bases in the examples. Clarifying the underlying principle would facilitate consistent application across a variety of fact patterns. [Appendix A paragraphs A13 – A19]

   c) The analysis in some of the examples in the Guidance appears to be inconsistent or contradictory. For example, the analysis in Example 13B states that operating in a reporting period and operating on the last day of the same reporting periods are two separate actions. On the other hand, the proposed guidance for threshold triggered costs assumes that the generation of revenue during a period represents only one action[3]. In Appendix A we have identified these areas in more detail and provide recommendations that in our view would enhance the clarity and help reduce the risk of unintended consequences. [Appendix A paragraphs A17, A30 - A33]

d) 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. We therefore consider those requirements could be more helpful if they followed the new structure for the assessment proposed in the ED (i.e. disaggregating by obligation, transfer and past-event). [Appendix A paragraph A20]

Measurement

7. We welcome the proposed clarification on the expenditure required to settle an obligation. This should reduce diversity in practice and enhance comparability. However, we consider that further 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. [Appendix A paragraphs A21 – A22]

8. On balance we support the proposed amendment for an entity to use a discount rate that reflects the time value of money (represented by a risk-free rate) and "the risks surrounding the amount or timing of the expenditure required to settle the obligation", which we understand would exclude non-performance risk. We suggest clearly signalling in the Standard that the proposed amendment is an exception to the measurement principle in the *Conceptual Framework for Financial Reporting* (Conceptual Framework), introduced as a practical expedient to reduce diversity in practice and costs incurred in measurement. [Appendix A paragraphs A23 – A25]

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

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3 The IASB tentative decision on 'threshold-triggered costs', was based on view 3 in April 2024 - IASB staff Agenda Paper 22B 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).

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?

Updating the definition of a liability

A1. In principle we support updating the definition of a liability in IAS 37 to align it with the definition in the Conceptual Framework. We agree that this could help preparers of financial statements when developing an accounting policy for a transaction that is not specifically addressed by any IFRS Accounting Standard, by removing the need to make a judgement about which definition to apply.

A2. In addition, the updated definition provides the framework for the proposed amendments to the recognition criteria.

Provisions – recognition criteria

A3. Whilst we support the objective of clarifying the recognition criteria, we are concerned that the current proposals may create new interpretation issues.

A4. In particular, we have identified some aspects of the proposed amendments that in our view might benefit from further consideration and testing by applying to more real-life fact patterns.

No practical ability to avoid test

A5. We believe this is an area where judgement would be needed. Although we appreciate that it would not be possible to provide application guidance for every possible scenario as to the intended meaning of *no practical ability to avoid*, we recommend the IASB further considers whether the requirements are sufficiently clear to enable this concept to be applied consistently.

A6. Initial stakeholder engagement indicates that 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 such a test in two subtly different ways:

a) A no practical ability to avoid test is one of the elements 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) The past-event condition also includes a no practical ability to avoid test (ED paragraph 14Q). This arises 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.

A7. The interaction of the obligation and past event conditions can be confusing. We recommend the IASB describe more explicitly the difference between the two tests and how the test is intended to be applied when assessing the obligation condition and the past-event condition to facilitate consistent application.

Transfer/exchange of economic resources

A8. 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.

A9. The distinction between the two concepts is not always clear cut. For example, UKEB stakeholders have raised doubts 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.

A10. In addition, questions arise as to whether outsourcing the settlement of an obligation (to provide clean-up services, for instance, or staff training) can impact 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 entity outsourced the work needed to provide the clean-up service (as the transaction could be considered an exchange)?

A11. 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.

A12. These challenges have been recognised in the past by IFRIC agenda papers which have set out the difficulties in assessing the difference between exchange and transfer[4]. We therefore recommend that further clarity is provided in the standard to support understandability and reduce the risk of diversity in practice. A possible approach could include signposting within IAS 37 the relevant concepts from the Conceptual Framework, expanding the existing draft examples in the Guidance to more clearly articulate the conclusions. Some of the proposed examples, such as those illustrating levies, state whether the nature of the obligation is a transfer or exchange without explaining how such a conclusion might be reached.

Past-event condition

A13. In withdrawing IFRIC 21 the proposed amendments would be applicable to *all* obligations in the scope of IAS 37, not only levies. The risk of unintended consequences needs to be considered.

A14. For simple scenarios with few basic steps, the proposed amendments to the present obligation recognition criterion do not appear to present any particular difficulties. However, the conclusion is not so clear when applied to more complex fact patterns, such as certain levies, where an entity would need to consider the proposed requirements for obligations to transfer an economic resource *only if an entity takes two (or more) separate actions*.

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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…….."

A15. 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 terms and conditions of a contract, or in the case of a levy, such a mechanism would be the corresponding legislation.

A16. We consider that the underlying principle behind the requirements in relation to obligations to transfer an economic resource only if an entity takes two (or more) separate actions is not clear. Clearly identifying the underlying principle would facilitate consistent application across a variety of fact patterns.

A17. At present, it is difficult to rationalise precisely what leads to the identification of an 'action', and therefore to clearly understand the difference between some of the examples in the Guidance. It is also unclear how an entity should distinguish between actions and measurement bases. For example:

a) 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. We consider that the distinction between what is merely a measurement basis and what is considered to be an 'action' for purposes of the proposed amendments should be made clearer.

b) 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. We consider it would be helpful to explain the rationale for the differences from:

i. the proposed guidance for threshold-triggered costs (paragraph 14P), 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[5]); and

ii. 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.

5 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).

A18. Further testing of the proposals is needed to identify whether the requirements can be applied consistently across different fact patterns and whether they lead to a sensible accounting outcome.

A19. This is also applicable to the proposed requirements on *threshold-triggered costs*. In addition, 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, for example, to indicate what would take precedence if both requirements are relevant for the same fact pattern.

Application of the recognition and measurement rules – Restructuring

A20. 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. We therefore consider those requirements could be more helpful if they followed the new structure for the assessment proposed in the ED (i.e. disaggregating by obligation, transfer and past-event).

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?

A21. We support the proposed clarification of the costs an entity includes in estimating the future expenditure required to settle an obligation. The proposed requirements will reduce diversity in practice and enhance comparability, resulting in more useful information for users of accounts.

A22. However, further consideration should be given as to how the proposed amendment would be applied to certain obligations not settled by the provision of goods or services, such as legal claims. Our understanding is that entities do not currently consider legal costs in the measurement of an obligation for legal claims. Entities consider external legal costs to be a separate unit of account - an executory contract for which the entity will receive future legal services - and it is therefore not in the scope of IAS 37. It is not clear whether the amendments are intended to change current practice, and whether a distinction should be made, for example, between internal/external legal 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?

A23. On balance, 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 surrounding the amount or timing of the expenditure to settle the obligation", which we understand would exclude non-performance risk. Initial feedback suggests that the proposed requirements are supported by many stakeholders and would reduce diversity in practice.

A24. 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 amended is an exception to the measurement principle as envisaged in paragraph 6.92 of the Conceptual Framework.

A25. We also support the proposed requirement to disclose the discount rate(s) used and the approach used to determine such rate(s). We believe the proposed disclosures would result in useful information for users of accounts.

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?

A26. We broadly support the proposed retrospective application of the requirements, with the two exceptions in proposed paragraphs 94D and 94E, relating to the measurement requirements.

A27. 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).

A28. We understand the proposed exceptions are consistent with transitional provisions in previous IASB projects[6], 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).

6 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.

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?

A29. 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. 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?

A30. We support updating the decision tree in Section B of the *Guidance on implementing IAS 37*. It provides a useful visual aid for the proposed new recognition requirements.

A31. Overall, we support the proposed amendments to the illustrative examples in the *Guidance on implementing IAS 37*. Presenting all examples under a similar structure, analysing separately each of the three conditions in the first recognition criterion, enhances clarity and facilitates comparison of the technical analysis and conclusions for the different fact patterns presented.

A32. However, we consider the analysis in some of the examples could be perceived as inconsistent or contradictory. Refer to paragraphs A16 – A19 above.

A33. Finally, the IASB should in our view consider whether the examples, currently in the Guidance, should be transferred to the main body of the standard, as application guidance that is an integral part of the standard. We expect the Guidance to be relied on heavily by preparers and auditors and, in effect, to take on the weight of authoritative requirements. Including them as an integral part of the standard, as application guidance, would give them an appropriate level of prominence and authoritative status. Other IFRS Accounting Standards, such as IFRS 9 *Financial Instruments,* provide precedents for such an approach.

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*

A34. We recommend the IASB considers whether an exception to the measurement principle in IFRS 3 is needed for provisions in scope of IAS 37. 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 impact to profit or loss.]