UK Endorsement Board

Dr Andreas Barckow
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29 November 2024

Dear Dr Barckow

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

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

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

3. There are currently approximately 1,400 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]

Overarching comments

4. As highlighted in the joint National Standard Setters letter[3] to the International Sustainability Standards Board (ISSB) on its Agenda Consultation, we consider

[1] UKEB calculation based on LSEG and Eikon data, May 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 information in the UK and Ireland produced by the Bureau Van Dijk, a Moody's analytics company), Company Watch financial analytics and other proprietary data.
[3] National Standard Setters Sustainability Forum Joint Letter paragraphs 4 – 9

that maintaining close alignment and connectivity between financial and sustainability reporting is paramount to ensuring that the information produced for investors is compatible.

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

6. We, therefore, welcome the IASB's development of these examples. We agree that providing illustrative examples should contribute to an improvement in reporting the effects of climate-related, and other, uncertainties in the financial statements[4]. It is also clear to us that the IASB has listened to feedback during their development. For more detail, please refer to paragraphs A2-A4 in Appendix A.

Materiality

7. The IASB's definition of materiality is intended to result in disclosures that are likely to have a direct effect on investor decision-making. This definition requires an application of judgement by preparers and auditors and demands an application of a qualitative assessment in addition to a quantitative assessment.

8. We welcome the IASB's approach to illustrate the application of qualitative materiality, as demonstrated in the first two examples, and consider that these examples should be helpful in encouraging an effective application of qualitative judgements. In particular, the increasing relevance of climate-related matters to investor decision-making in recent years will inevitably impact the relative importance of qualitative materiality judgements, notwithstanding the lack of any quantitatively material financial impact at this stage. To emphasise this point, it would be helpful if the examples explained more clearly the facts and circumstances where information may not be quantitively material but can be deemed to be qualitatively material. For more detail, please refer to paragraphs A5-A7 in Appendix A.

9. We are also concerned that undue emphasis has been placed on paragraph 31 of IAS 1 *Presentation of Financial Statements*. That paragraph requires entities to consider whether to provide additional disclosures when compliance with other IFRS is insufficient to enable users to understand the impact of particular transactions. However, we consider that the overarching requirements of IAS 1, including paragraphs 17 (c) and 112 (c), are also relevant here and should be referenced in the examples.

10. Further, the use of different words in examples one and two from those in the standard has caused confusion. Paragraphs 17(c) and 31 refer to 'impact' of

4 Subject to points noted in paragraphs A10 to A23 in Appendix A.

transactions whereas the illustrative examples refer to the ‘effect’ and ‘lack of effect’. We would suggest that the examples use consistent wording to that used in the standard as they are meant to be illustrative in nature. For more detail, please refer to paragraphs A8-A9 in Appendix A.

Approach to developing illustrative examples

11. We are generally supportive of the IASB’s approach to developing the examples and, in particular, that the examples should illustrate how an entity applies the requirements in IFRS Accounting Standards (BC14). We also agree with the approach of focusing the examples on the requirements that are among the most relevant for reporting the effects of climate-related and other uncertainties in the financial statements. However, in principle, we consider that non-mandatory illustrative examples are not a substitute for standard setting, together with the associated due process, and should not be used to drive changes in accepted practice.

12. We consider that the examples could be enhanced by including more scenarios where climate-related or other uncertainties have an impact on the financial statements. This would help to illustrate when the disclosures belong within the boundary of the financial statements, rather than in other general purpose financial reports. For more detail, please refer to paragraphs A15, A17 and A19 in Appendix A.

13. We have other comments on the fact patterns and technical content of the examples. Our comments are aimed at enhancing the relevance of the illustrations and supporting connectivity. These are included in the paragraphs A17 to A23 in Appendix A.

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

Yours sincerely

Pauline Wallace
Chair
UK Endorsement Board

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

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

(a) Improvements in reporting

A1. We agree that providing illustrative examples should improve the current level of reporting for the effects of climate-related and other uncertainties in the financial statements. We include below some comments on certain unintended consequences and areas where we consider that the examples could be further improved.

Connectivity

A2. While we recognise the challenges of delivering guidance, as sustainability reporting is expected to evolve soon, it is also clear that demand for clarity regarding connectivity is urgent and necessary in all jurisdictions that apply IASB's standards, and which are now committed to providing sustainability information to investors. Jurisdictions representing over half the global economy by GDP have now taken steps towards aligning with, or adopting, ISSB standards[5]. In other jurisdictions, such as the EU where companies are expecting to apply ESRS, recent activity indicates that there is expected to be a high degree of interoperability with ISSB standards.

A3. As highlighted in the joint National Standard Setters letter to the ISSB on its Agenda Consultation, we consider that maintaining close alignment and connectivity between financial and sustainability reporting is paramount to ensuring that the information produced for investors is compatible. We are encouraged that one of the objectives set out in the ED (BC21) is to illustrate the provision of connected information in general purpose financial reports and to reinforce compatibility with IFRS Sustainability Disclosure Standards.

A4. The UKEB research into connectivity[6] highlighted that stakeholders are seeking clarity on how the IFRS Foundation's two sets of standards are intended to work together in practice. As examples one and two are specifically intended to reinforce compatibility with IFRS Sustainability Disclosure Standards, the IASB may wish to consider reflecting, in future educational materials, fact patterns where an entity has applied the requirements of sustainability disclosures, e.g. to disclose how sustainability-related risks and opportunities have affected an entity's financial position, financial performance, and cash flows.

Materiality

A5. In relation to the materiality judgements and the disclosure, or not, of additional information illustrated in examples one and two, we are encouraged that the examples illustrate the application of qualitative materiality. Users have consistently emphasised that materiality assessments should involve both quantitative and qualitative judgements.

A6. In addition, we consider it would be helpful to reference examples C and K from the IFRS Practice Statement 2 *Making Materiality Judgements* in illustrative examples one and two as they explain how an entity could consider qualitative factors when making materiality judgments.

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

6 A Study in Connectivity: Analysis of 2022 UK Company Annual Reports (UKEB 2023)

A7. We support the separation of the final sentence in paragraph 31[7] of IAS 1 in IFRS 18 *Presentation and Disclosure in Financial Statements* and consider that it may help to emphasise this aspect of the requirement.

A8. However, we believe that the illustrations appear to go beyond the wording of paragraph 31 of IAS 1. For example, the paragraph does not include any reference to the requirement to disclose a lack of material effect. However, as paragraph 31 also requires entities to consider whether to provide additional disclosures, links should also be made to paragraphs 17 (c) which requires additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impacts and 112 (c) which requires the provision of information that is not presented elsewhere in the financial statements, but is relevant to an understanding of them.

A9. We consider that reference to the overarching requirements of IAS 1, including paragraphs 17(c) and 112(c) in the relevant illustrative examples would mitigate the potential unintended consequences of obfuscation from boiler plate disclosures of immaterial items in the financial statements.

(b) Illustrative examples accompanying IFRS Accounting Standards

A10. In general, we agree that the IASB's proposal to include the examples as accompanying illustrative material to the relevant accounting standards should provide stakeholders with accessible and relevant guidance when using those standards. We note, that in principle, we consider that non-mandatory illustrative examples are not a substitute for standard setting, together with the associated due process, and should not be used to drive changes in requirements.

A11. Whilst the examples are not mandatory, and so do not add or change any IFRS accounting requirements, we anticipate that they will be useful to stakeholders when they are considering accounting for relevant business transactions. We are aware that IASB guidance is often referred to by both preparers and auditors when determining accounting policies and disclosures.

A12. We note in BC45 of the ED that, in addition to including the examples in the relevant accounting standards, the IASB may also group the examples and publish them as a single document. We consider that this would be useful as, without this, some stakeholders may struggle to understand the connections, for example to

[7] 'Some IFRSs specify information that is required to be included in the financial statements, which includes the notes. An entity need not provide a specific disclosure required by an IFRS if the information resulting from that disclosure is not material. This is the case even if the IFRS contains a list of specific requirements or describes them as minimum requirements. An entity shall also consider whether to provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users of financial statements to understand the impact of particular transactions, other events and conditions on the entity's financial position, and financial performance.' (IAS 1, paragraph 31)

the context of materiality to the individual examples when included in different standards.

Question 2 — Approach to developing illustrative examples
Examples 1–8 in this Exposure Draft illustrate how an entity applies specific requirements in IFRS Accounting Standards. The IASB decided to focus the examples on requirements: (a) that are among the most relevant for reporting the effects of climate-related and other uncertainties in the financial statements; and (b) that are likely to address the concerns that information about the effects of climate-related risks in the financial statements is insufficient or appears to be inconsistent with information provided in general purpose financial reports outside the financial statements. Paragraphs BC10–BC42 of the Basis for Conclusions further explain the IASB's overall considerations in developing the examples and the objective and rationale for each example. Do you agree with the IASB's approach to developing the examples? In particular, do you agree with the selection of requirements and fact patterns illustrated in the examples and the technical content of the examples? Please explain why or why not. If you disagree, please explain what you would suggest instead and why.

A13. We are generally supportive of the IASB's approach to developing the examples and that the examples should illustrate how an entity applies the requirements in IFRS Accounting Standards (BC14). We also agree with the approach of focusing the examples on the requirements that are among the most relevant for reporting the effects of climate related and other uncertainties in financial statements.

A14. We support the use of standalone examples but also consider walk-through examples would be beneficial. We appreciate that walk-through examples are significantly more complex to develop and would take longer to build a consensus. The IASB may wish to consider developing more in-depth examples, as the next phase of work, with the ISSB.

A15. We note that few of the examples illustrate circumstances when there is an impact on the financial statements. In our view it would be helpful if the IASB provided an additional example where a climate-related, or other uncertainty, does result in an impact on the financial statements. Please also refer to paragraph A17 and A19.

A16. We have some comments on the fact patterns and technical content of the examples. Our comments are aimed at helping to enhance the relevance of the illustrations and to support connectivity. These are included in the paragraphs that follow.

Specific comments on examples

A17. Stakeholders advised us that the key challenges in practice relating to the application of IAS 36 *Impairment of Assets* are connectivity between climate-related scenarios and impairment assumptions, the effects on expected cash flows (beyond a five-year period) and how those may affect asset terminal values. The IASB may wish to consider if some of these aspects could be reflected in example three[8] to make it more applicable, or potentially considered for a future joint illustrative example with the ISSB.

A18. We support the clarification provided in example four[9] regarding IAS 1 paragraph 125. While stakeholders acknowledge some confusion in practice, it was generally considered that this paragraph was applied consistently for sources of estimation uncertainty with a significant risk of material adjustment within the next financial year.

A19. We suggest that example four could be improved by providing the rationale for the entity performing impairment testing at a CGU level. The IASB may wish to consider aligning the fact pattern more closely to the requirements of IAS 36 paragraph 67 (a) and (b). In addition, we recommend that any impact on the useful economic lives of the non-current assets should also be considered in the fact pattern. Users emphasised that they considered sensitivity and scenario analysis as material information and recommended these were referenced in the fact pattern of the example.

A20. Example six[10] provides a helpful illustration of climate-related factors considered when the entity assesses materiality. We suggest that including direct references to IFRS 7 paragraph 33 (qualitative disclosures), and paragraph 34 (quantitative disclosures), would help clarify the approach taken.

A21. In relation to example seven[11], the illustration is based on an ‘increasing risk’ which may require the accelerated closure of facilities. However, the type and significance of the risk is not made explicit. The IASB may wish to consider providing further clarity to ensure consistent application.

A22. Stakeholders also advised us that the most relevant challenge, in practice, relates to situations where assets may need to be replaced or repurposed due to climate-related risks, and the potential implications for impairment, reduction in useful economic life and consequential acceleration of depreciation and potential decommissioning provisions. The IASB may wish to consider if some of these

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8 Disclosure of assumptions: specific requirements (IAS 36)
9 Disclosure of assumptions: general requirements (IAS 1/IAS 8)
10 Disclosure about credit risk (IFRS 7)
11 Disclosure about decommissioning and restoration provisions (IAS 37)

aspects could be reflected in example seven to enhance its relevance, or potentially included in a future joint illustrative example with the ISSB.

A23. We also consider that it would be helpful to clarify in example eight[12] how materiality was assessed and how the disaggregation information resulted in decision useful information for users.

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

A24. We do not consider that any transition implementation requirements are necessary as there has not been a change to the accounting standards.

12 Disclosure of disaggregate information (IFRS 18)