Thursday, 28 November 2024

Dr Andreas Barckow
Chair
International Accounting Standards Board
7 Westferry Circus
Canary Wharf
London E14 4HD
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Via online submission: www.ifrs.org

Dear Andreas

Exposure Draft: Climate-Related and Other Uncertainties in the Financial Statements (Proposed Illustrative Examples)

Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia represent over 310,000 professional accountants who work in diverse roles across public practice, commerce, industry, government and academia throughout Australia, New Zealand and internationally. We welcome the opportunity to provide feedback on the above Exposure Draft (the ED) and make this submission on behalf of our members and in the public interest.

We support the IASB's proactive approach to enhance transparency and consistency in reporting the effects of climate-related and other uncertainties in financial statements. We view these examples as a valuable first step in the IASB's work to clarify disclosure of climate-related and other uncertainties in the financial statements. While we appreciate the IASB's efforts to develop examples that reinforce compatibility with IFRS Sustainability Standards, our members continue to seek clarity on how the IFRS Accounting Standards and IFRS Sustainability Standards are intended to function together in practice. To meet the demand for guidance, we encourage IASB to develop additional examples and educational materials in the future to aid in reporting on the effects of climate-related and other uncertainties in the financial statements, with reference to how IFRS Accounting Standards and IFRS Sustainability Standards interrelate.

The need to establish connectivity and alignment between financial statements, sustainability reports and other reports is growing, to ensure clear linkages between the information contained in different reports produced by an entity to fulfil its financial and sustainability reporting obligations. We expect the IASB and the ISSB will need to consider undertaking a more detailed assessment of the Standards they develop and issue in due course to address this matter.

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Our outreach activities undertaken with members and stakeholders when developing this submission indicates an expectation for illustrative examples that outline more ambiguous scenarios relating to climate-related impacts where the decision on whether to disclose information is not as obvious. While the proposed examples provide a solid foundation for discussions on the disclosure of climate-related and other uncertainties in the financial statements, they primarily present predetermined conclusions and restate requirements already outlined in the IFRS Accounting Standards. In their current form, members felt that the scenarios presented in the illustrative examples were overly simplistic, limiting their relevance when considering complex and subjective climate-related impacts in practice.

We recognise the intent of stand-alone examples to target specific matters of stakeholder concern, however the narrow fact patterns provide limited context when considering the broader impact of climate-related and other uncertainties in the financial statements. We suggest that some of the examples are adapted to be walk-through examples with broader fact patterns, demonstrating application of underlying concepts and the decision process behind the conclusions. Feedback received from members suggests it would be useful to develop a decision tree to accompany the illustrative examples, that will graphically signpost the scenarios and the relevant illustrative examples. In addition, some stakeholders have indicated a preference for inclusion of illustrative disclosures where relevant to aid in preparing the notes to the financial statements.

Our members have also noted the absence of industry diversity in the examples. Currently, the examples are predominantly focused on capital-intensive and manufacturing industries. While we understand the IASB's intent to set out fact patterns at a high level to be applicable to a variety of industries, members have indicated that examples incorporating industries such as insurance, agriculture, healthcare, and the energy sector would be most useful.

Finally, while we agree in principle with including these as illustrative examples accompanying the IFRS Accounting Standards, we emphasise that the documents in which some are proposed to be located are not freely publicly available on the IFRS Foundation website. Accordingly, we strongly suggest that the IASB proceeds with the proposition in paragraph BC45 to group the examples in a single document. We recommend this document is published as educational material to allow greater flexibility in developing further supplementary content and provide a single resource for users seeking more detailed information.

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Our detailed responses to the specific questions raised in the ED are provided in the **Attachment** to this letter. Should you have any questions about the matters raised in this submission or wish to discuss them further, please contact either Amir Ghandar (CA ANZ) at Amir.Ghandar@charteredaccountantsanz.com or Ram Subramanian (CPA Australia) at Ram.Subramanian@cpaaustralia.com.au.

Sincerely,

Simon Grant FCA
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Chartered Accountants Australia and New Zealand

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Attachment

Responses to consultation questions

1. Providing illustrative examples

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.

We agree that providing examples will aid in improving reporting of the effects of climate-related and other uncertainties in the financial statements. While the proposed illustrative examples in the ED are a valuable step in encouraging discussion of such issues, we have identified areas of improvement through member and stakeholder outreach. These recommendations are detailed in our response to Question 2.

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.

We agree in principle with including the examples as *Illustrative Examples* accompanying the IFRS Accounting Standards. These illustrative examples, while non-mandatory, provide valuable guidance and do not necessitate amendments to the existing IFRS Accounting Standards.

We recognise that some IASB literature is housed behind a paywall for reasonable purposes, and it is up to jurisdictional standards setters to obtain a license and make the material available locally. However, we believe in this instance given the global focus and rapid pace of change involved in dealing with climate risk disclosures, impacting users, preparers, and auditors, that making the illustrative material freely available to as wide an audience as possible is critical.

We note that only Examples 3 and 7 are proposed to be included in *Illustrative Examples* which are available at no cost on the IFRS Foundation website, and hence easily accessible. To the contrary, we note that the following examples would only be accessible at a cost:

- Examples 1, 2, 4, 5 are proposed to be added to the IAS 1 *Implementation Guidance* which is not freely publicly available on the IFRS Foundation website. This is presumably because there are no *Illustrative Examples* for IAS 1. Although we acknowledge that this is only applicable for reporting periods before an entity applies IFRS 18.
- Example 6 is proposed to be added to the IFRS 7 *Implementation Guidance* which is not freely publicly available on the IFRS Foundation website. This is presumably because there are no *Illustrative Examples* for IFRS 7.
- Examples 1, 2, 4, 5, 8 are proposed to be added to the IFRS 18 *Illustrative Examples.* However, neither the standard or *Illustrative Examples* appear to have been published on the IFRS Foundation website as yet.

Access to *Implementation Guidance* on the IFRS Foundation website requires a paid subscription which may be cost prohibitive for some and therefore pose a barrier to access, meaning the examples may not provide the desired benefit and the project may not achieve its objective. To enhance accessibility and utility, we recommend that the IASB proceeds with the proposition in BC45 to also publish the examples as a single document, provided it is publicly available at no cost. This will allow consideration of the examples in the context of one another, which members have indicated is beneficial.

We recommend that the IASB consider using these illustrative examples as the foundation for **separate educational material**. This allows greater flexibility to provide further content and will serve as a valuable resource for users seeking more detailed guidance. Additionally, our members have indicated that including decision tree guiding users on selecting the relevant example for specific circumstances would be particularly useful. If Example 5 is omitted, our view is that the IASB could incorporate these examples into the already published educational materials on the effects of climate-related matters on financial statements, to enhance its usefulness. Alternatively, if additional examples incorporating other types of uncertainties are included, the collection should be published in a separate educational material document.

2. 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.

Feedback received suggests that the fact patterns illustrated in the examples do not include the more ambiguous elements for which guidance is most required. Generally, the examples repeat the content of the IFRS Accounting Standards and do not align with member expectations for demonstration of application of underlying concepts and consequentially the logic behind the conclusions made. We have obtained the below feedback on the IASB's approach to developing the examples.

Linkage to IFRS Sustainability Standards

While we appreciate the IASB's efforts to develop examples that reinforce compatibility with IFRS Sustainability Standards, our members continue to seek clarity on how the IFRS Accounting Standards and IFRS Sustainability Standards are intended to function together in practice. While Examples 1 and 2 reference disclosures outside of the financial statements, the other examples do not raise correlations, namely with the requirements of the IFRS S2 requirements for disclosure of the current and anticipated financial impacts of climate-related risks and opportunities. The need to establish connectivity and alignment between financial statements, sustainability reports and other reports is growing, and clear linkages between the information contained in different reports are needed to effectively fulfil its financial and sustainability reporting obligations. To achieve the goal of full connectivity between financial and sustainability reporting, further significant work needs to be undertaken, likely in the form of a dedicated and combined IASB/ISSB project that explore all aspects of the interrelationships between information presented in both financial and sustainability reports, to ascertain how best to ensure such information reflects a seamless representation of the underlying activities.

Stand-alone or walk-through structure

We acknowledge that the stand-alone example structure is useful for addressing specific stakeholder concerns. However, there are concerns that the narrow fact patterns provide limited context when considering the wider impact of such uncertainties. Some stakeholders have expressed that the examples are too "rules-based", which may lead to misconceptions that the outcome only applies to identical situations. While we recognise that this is an inherent limitation of illustrative examples, we believe that more comprehensive examples will better achieve the IASB's goal of demonstrating how principles and requirements can apply to a wider range of uncertainties.

To address this, we suggest adapting some examples into broader scenarios, characteristic of walk-through examples. These examples should focus on the application of underlying concepts and the decision-making process behind the conclusions. In practice, management must evaluate a variety of real-world scenarios and factors, weighing each one carefully to arrive at a reasonable conclusion. Examples that illustrate how different factors may be prioritised depending on an entity's specific circumstances would provide more practical, nuanced guidance and better support preparers in applying judgment. Additionally, we recommend incorporating variations in the basic fact patterns, which may lead to different outcomes. This could be supported by decision trees that outline the hierarchy of considerations whilst applying different standards.

Applicability to different types of uncertainties

Several members felt that the IASB's intention for the examples to be sufficiently high level to apply equally to other types of uncertainty was not entirely achieved. Given their topical nature, users are unlikely to deduce that climate-specific examples can be applied to other scenarios. These members suggested either omitting the single example that does not directly concern a climate-related uncertainty (Example 5) or incorporating additional examples of other types of uncertainties to improve the balance of the selection.

Narrow industry range

It is also worth raising that some members expressed disappointment in the narrow range of industries included in the examples. Currently, the examples are predominately focused on capital-intensive and manufacturing industries. While we acknowledge the IASB's aim to generalise the entities in the fact patterns for applicability across various industries, members have indicated that examples incorporating industries such as insurance, agriculture, healthcare and the energy sector would be useful. We propose that any additional examples focus on common ambiguous scenarios, starting with key sectors that will be most impacted and progressively expanding to other sectors.

Inclusion of illustrative disclosures

Members have expressed that the term "illustrative examples" created an expectation sample wording to support preparers in drafting clear disclosures for climate-related and other uncertainties. While we appreciate the balance between principle-based and rule-based guidance—and the risk of encouraging boilerplate disclosures—feedback indicates that specific example wording would be very helpful. The IASB has provided such guidance in the illustrative examples accompanying IFRS 9 *Financial Instruments* and IFRS 16 *Leases*, which have been well-received by our members.

Fact patterns and technical content

We have obtained the below specific feedback for each example:

- **Examples 1 and 2** are broadly accepted and concluded to be most valuable when considered together. Both examples effectively illustrate the considerations behind making additional disclosures under paragraph 31 of IAS 1, with contrasting results based on their respective fact patterns. We understand that in current practice this requirement is used in relatively rare situations as the focus on the disclosure requirements in subject matter specific IFRS Accounting Standards. However, some members are apprehensive that its application to the conclusion in Example 1 is somewhat stretched. There is doubt regarding the usefulness of disclosing items that do not have a material effect on an entity's financial statements. In addition, it raises concerns that such disclosures may lead to excessive disclosures, obscuring other material information already disclosed. These examples could be improved by incorporating the four-step process outlined in IFRS Practice Statement 2: Making Materiality Judgements. Applying these key principles to assess the materiality of climate-related uncertainties would provide more robust reasoning for disclosing items that do not have a material effect on the financial statements.

- **Example 3** could be improved by including guidance on how the future emission allowance costs were determined as a key assumption. Although Example 3 provides the reasoning of it being among the most sensitive assumptions impacting the Cash Generating Unit (CGU)'s recoverable amount, it does not illustrate consideration of other factors warranting the disclosure. The facts state that significant goodwill is allocated to the CGU, and therefore paragraph 134(d)(i) of IAS 36 requires it be disclosed. In its current form, the example does not appear to add more substance than reading IAS 36 in isolation. Feedback from members indicates that including numbers and calculations in this example would make it more useful. It would also be beneficial to illustrate how to determine the extent of a "reasonably possible change" in the key assumptions. We also note current challenges in practice with connectivity between climate-related scenarios and impairment assumptions, the effects on expected cash flows beyond a five-year period and subsequent impact on asset terminal value. Based on the consensus that additional considerations should be incorporated into this example, we believe it would be more beneficial in a "walk-through" format that comprehensively illustrates determination of the key assumptions and the consequential impact when calculating the recoverable amount.

- **Example 4**, like Example 3, primarily reiterates requirements already included in IAS 1 and offers minimal guidance on the application of the related principles. However, Example 4 is much more comprehensive in stepping through the considerations for several relevant factors in reaching its conclusion. Other examples would benefit from a similar approach of how matters of judgement were approached and analysed. Several members expected these examples to include illustrative disclosures, and we believe this example is an optimal opportunity to include an illustrative disclosure that demonstrates application of paragraph 129 of IAS 1 to *"[disclose]* ***in a manner*** *for users to understand the judgements that management makes"*. We recognise the IASB's intention for this example to address stakeholder misinterpretation that uncertainties that will not be resolved until after the next financial year may not be in the scope of paragraph 125 of IAS 1, which is also sometimes overlooked. Overall, we believe that this example alongside illustrative

disclosures assists prepares in dealing with measurement of assets and liabilities where significant estimation uncertainty exists.

- **Example 5** is the only example that is not explicitly climate related. This is perceived as unbalanced, and our members are largely indifferent about its inclusion. Further, the scenario is rare and therefore is likely to have limited application in practice. It does not offer sufficient detail when considering the extent to which it is probable that taxable profit will be available against which unused tax losses can be utilised. This example could be improved by reconstructing it into a "walk-through" format that applies the considerations in paragraph 36 of IAS 12 in more detail prior to evaluating the facts against the general disclosure requirements in IAS 1. Due to the pervasive impact of potential restrictive jurisdictional legislation, several requirements in a selection of IFRS Accounting Standards are relevant.

- **Example 6** helpfully outlines key considerations when determining whether the effect of climate-related risks on exposure to credit risk is material. However, the example also outlines the potential information to be disclosed under IFRS 7, which is less valuable, as it merely repeats the content of paragraphs 35(e)-(g) and 38. We have received feedback from members in the financial industry that this example is not relevant in practice as it neglects to address non-credit risks, including but not limited to liquidity or market risk. In addition, the fact pattern does not include the term of the loans, which may have material influence, not least owing to the time value of money. This is another example where inclusion of an illustrative disclosure may be beneficial, as we have been advised that it can be particularly challenging to determine the nature and extent of information to disclose on this matter.

- **Example 7** is viewed by several of our members as a missed opportunity to provide more comprehensive guidance around the recognition of a climate-related provision. Using a legal obligation instead of a constructive obligation in this example is less beneficial. There is a demand for guidance to assist with determining whether the facts of an entity's commitment, and the circumstances surrounding it, meets the definition of a constructive obligation. In addition, it may be beneficial to include in the example a reference to the aggregation requirements in paragraph 87 of IAS 37. Some facilities may be subject to more uncertainty than others, and therefore not sufficiently similar for a single statement about their timing uncertainties to be a fair representation under paragraph 85(b) of IAS 37.

- **Example 8** is supported and a useful illustration of the IFRS 18 principle of disaggregating information related toa class of property, plant and equipment based on risk characteristics. However, it would be helpful to clarify how the materiality was assessed and how the disaggregation resulted in material information. The example could be further improved by providing clearer guidance on when an entity would be required to disaggregate, as opposed to when they may choose to disaggregate based on professional judgment. This could be achieved by expanding the example to a "walk-through" format. Finally, it would be useful to address in the example whether the same conclusion applies under the requirements of IAS 1 as under IFRS 18.

3. Do you have any other comments on the Exposure Draft?

We have no other comments further to those provided above.

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