

# CLIMATE-RELATED AND OTHER UNCERTAINTIES IN THE FINANCIAL STATEMENTS

*IASB PROJECT UPDATE*

EFRAG FRB AND SRB MEETING – AGENDA PAPER 06-01



## DISCLAIMER

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## WHAT WE WILL COVER

- Overview of the IASB project

Appendix : EFRAG Secretariat Briefing findings (*for background purposes only*)



# OVERVIEW OF THE IASB PROJECT

# IASB PROJECT- TIMELINE



## IASB SEPTEMBER 2023- INITIAL AGREED NEXT STEPS

Following its outreach, in September the IASB conveyed **overall IFRS are sufficient**. That said, in light of outreach feedback agreed to:

- refer to the IFRS Interpretations Committee (**Discussed at the November 2023 ASAF meeting**)
  - **a question about the circumstances in which an entity recognises a liability when applying IAS 37 Provisions, Contingent Liabilities and Contingent Assets to climate-related commitments**
  - **questions related to the application of IAS 36 Impairment of Assets**
- **explore whether to create examples to illustrate how to apply requirements** in IFRS Accounting Standards to reporting the effects of climate-related and other uncertainties (**Discussed at the December 2023 ASAF meeting**)
- **explore clarifying or enhancing IFRS requirements** related to disclosure of uncertainty in estimates (**IAS 1.125**) (i.e., **related to interpretation that such disclosure is only required for a 12-month horizon**) (Expected standard setting actions would be by 2025)

The IASB reframed the scope of the project **to include other matters (besides climate-related matters)** and to **encompass uncertainties and not only risks**

## SEPTEMBER 2023 MEETING- *WHAT WILL NOT BE DONE*

The IASB decided not to explore clarifying or enhancing requirements in IFRS Accounting Standards in relation to:

- **connections between** items of information in the financial statements and between the **financial statements and other general purpose financial reports**;
- **assessing** whether information is **material**; and
- the **'catch-all' disclosure requirement** in paragraph 31 of **IAS 1** *Presentation of Financial Statements*.

# NOVEMBER 2023 IFRIC INTERPRETATION- NET ZERO COMMITMENTS

In a tentative agenda decision (TAD), IFRIC clarified that:

- A Net Zero transition commitment **does not necessarily create a constructive obligation** → Entity's management needs to judge whether such a commitment has created a valid expectation in the public at large;
- the entity, at the announcement date, **has not a present obligation (meaning no provision/liability is recognised)** for the following reasons:
  - all the costs of modifying its manufacturing methods and of purchasing carbon credits need to be incurred to operate in the future and, therefore, when an entity publishes its net zero transition commitment in 20X0 they do not exist independently of the entity's future actions;
  - The entity will at some point incur a present obligation to pay for resources it purchases to modifying its manufacturing methods (e.g., new plant or equipment) but only when it receives those resources; and
  - The entity will have a present obligation to purchase carbon credits only if and when it emits greenhouse gases in 20X9 and later year.
- The IFRS IC will discuss the feedback received on the TAD at the forthcoming meeting in March 2024.



## IASB FOLLOW-UP ACTIONS- EXAMPLE DEVELOPMENT

- **Tailoring materiality examples included in the IFRS Materiality Practice Statement for climate-risk**
  - **Applying catch-all requirements-** Example C, which shows how the materiality judgment could lead to the disclosure of information in addition to that specifically required by IFRS Accounting Standard
  - **Qualitative materiality assessment-** Example K, which shows how an entity should consider qualitative factors when assessing whether information is material, even when there is no quantitative impact on the financial statements (e.g., impairment tests applying IAS 36 *Impairment of Assets* and expected credit losses applying IFRS 9 *Financial Instruments*)
- **Examples that apply for IFRS Accounting Standards** related to climate-related matters.
- ASAF members views:
  - **Supported examples** would help entities apply IFRS Accounting Standards in reporting the effects of climate-related and other uncertainties in the financial statements;
  - **Preferred examples that illustrate the application of specific IFRS Accounting requirements**
  - **Preferred examples in IFRS Accounting Standards** rather than as educational materials

## QUESTIONS

**Q1:** Do EFRAG FR and SR Board members have any comments on the IASB project overview?

# APPENDIX - OVERVIEW OF FINDINGS IN EFRAG SECRETARIAT BRIEFING ([Accessible through this link](#))



## CLIMATE-RELATED RISKS IN THE FINANCIAL STATEMENTS



### EFRAG SECRETARIAT BRIEFING

*SUMMARY: EFRAG OUTREACH, LEARNINGS FROM REVIEWS OF EUROPEAN REPORTING TRENDS*

**SEPTEMBER 2023**

## NATURE OF CONCERNS

Lack of connection between the information inside and outside the financial statements

- Companies disclose climate-related risks in the front part **without any quantitative disclosures** in the financial statements
- **Commitments and investments disclosed** outside the financial statements **are often non reflected in the financial statements**
- **Lack of linkage between the entity's transition plans and disclosed information** in terms of carrying value, remaining useful life, impairment of assets and segment reporting
- **Difficult to reconcile information** in the Sustainability Reporting to the financial statements
- **Lack of consistency in terms of terminology used** (e.g., commitments, target)

The climate-related information is too high-level and inadequate

- **Failure to apply qualitative thresholds of materiality**
- **Disclosure are mostly qualitative than quantitative**
- **Lack of disclosure relating assumptions and estimates** underpinning the future cash-flow projections and valuation of assets and absence of sensitivity analysis

## CAUSES OF CONCERNS

### Remediable causes of concerns

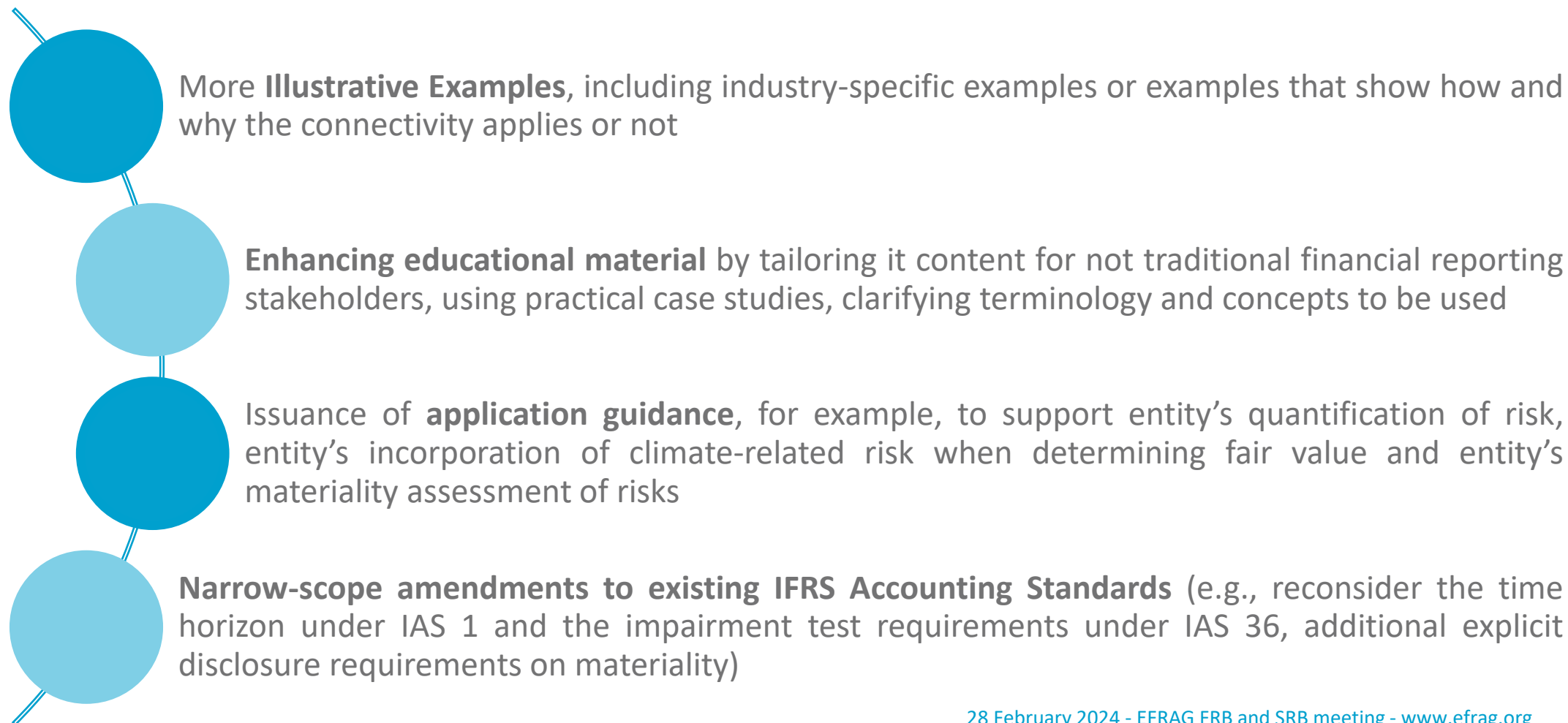
- **Lack of compliance with existing IFRS requirements**
- **Lack of transparency on the entity's assessment of materiality**
- **Limitations of existing requirements of IFRS Accounting Standards** in respect of the applicable time horizon, impairment test requirements under IAS 36 and lack of connection requirement in current IFRS Accounting Standards
- **High-level nature, non-authoritative stature, and limited awareness about the IASB educational material**
- **Difficulties and constraints in assessing and measuring climate-related risks**, due to the limited data availability, complexity of the calculation, inadequate risk management systems and the prevalence of siloed organisations
- **Lack of practical application guidance** on how to assess and measure climate-related risks
- **Expectation gap** on what information can be reflected in the financial statements

# WHY INFORMATION MAY NOT BE REFLECTED IN THE FINANCIAL STATEMENTS

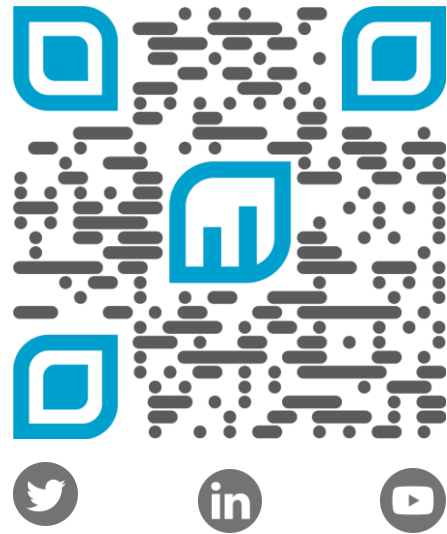
Justifiable causes for information not being reflected in financial statements

- **Differing materiality thresholds** (i.e., impact materiality and financial materiality under ESRS requirements versus material item as defined in IAS 1)
- **Constraints in reporting climate-related economic opportunities** (e.g., potential assets) which are not allowed under current IFRS Accounting Standards.
- **Differing reporting boundaries**
- **Differences in the time horizons** typically applied to sustainability disclosures and financial statements information (e.g., different interpretation of the applicable time horizon under IAS 1 or for impairment testing under IAS 36)
- **Climate-related risks may not meet the criteria for recognition of provisions and liabilities**
- **Climate-related risk may be implicit and embedded within reported line items** (e.g., climate risk would be part of the risk adjustment under IFRS 17 or IFRS 9)

## SUGGESTED COURSES OF ACTION



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THANK YOU