November 25, 2024

Andreas Barckow
Chair
International Accounting Standards Board (IASB)

Exposure Draft Climate-related and Other Uncertainties in the Financial Statements Proposed Illustrative examples

Dear Andreas,

This submission is being made by the ESG and Sustainability Committee of the Financial Executives International Canada (FEI Canada). FEI Canada has the following purpose:
"As an organization of professionals, FEI Canada's mission is to be the leading voice and informed choice for senior financial executives across the country by providing professional development, networking opportunities and thought leadership in delivering valuable "Canadian-centric" knowledge to our members." Our members serve as financial leaders in various industries and across a wide spectrum of entities in a global business environment. Consequently, our comments are neither industry-specific nor entity-specific, with an intent to provide an objective and informed opinion on aspects that will maximize value to all stakeholders.

We appreciate the overall objective of improving entities' disclosures about the effects of climate-related risks and other uncertainties in the financial statements. The Exposure Draft seeks to provide illustrative examples, purportedly to help entities in reporting such effects and strengthen the connection between information reported outside the financial statements and the financial statements themselves.

However, we have significant concerns about indirectly setting accounting standards through illustrative examples, which pose significant risks, as such examples are often seen as expressions of how the Board believes IFRS Accounting Standards should be interpreted and applied. These examples signal the intended application of the standards and are frequently used by analogy to guide the development of accounting policies for transactions and events beyond those explicitly covered in the examples. In this case, we anticipate that the examples will be applied to other types of transactions, events, and risks, potentially leading to broader interpretations than intended initially and well beyond climate-related risks.

While the technical argument is made that such illustrative examples are not authoritative, as they are not formally part of IAS 1 or IFRS 18, in practice, they carry significant weight. Preparers, auditors, securities regulators, litigators and others often rely on these examples to ensure compliance with IFRS as intended by the IASB or to support other objectives, e.g. litigation.

The ED concludes that while certain climate-related matters are not subject to specific disclosure requirements under specific IFRSs, they should still be disclosed based on the general provisions found in IAS 1 and IFRS 8 listed below (emphasis added):

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IAS 1 paragraphs 17, and 31 – Virtually in all circumstance, an entity achieves a fair presentation by compliance with applicable IFRSs, but in certain instances additional disclosures may be required when IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on an entity's financial position and financial performance.

IAS 1 paragraph 125 – Source of estimation uncertainty - An entity shall disclose information about the assumptions it makes about the future and other significant sources of estimation uncertainty at the end of the reporting period that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

We are concerned that the ED's approach could significantly alter the intent and application of these provisions, extending beyond climate-related risks. This shift creates the perception that entities may not be able to achieve fair presentation in virtually all circumstances through compliance with applicable IFRSs.

We recommend the Board make targeted amendments to specific standards if it believes the current guidance is insufficient. This approach would help preserve the clarity and quality of IFRS Accounting Standards while minimizing the unintended consequences outlined above. Including illustrative examples accompanying IFRSs that suggest fair presentation cannot be achieved, in virtually all instances, by complying with applicable IFRSs would undermine the quality of the standards and would not serve the best interests of investors, other users of financial statements or the entities themselves.

Examples 1 and 2 - Materiality judgements leading to additional disclosures and not leading to additional disclosures (IAS 1/IFRS 18)

We are specifically concerned that Examples 1 and 2 of the ED alter the original intent and current application of IFRS in the following areas:

1. Expands the concept of materiality beyond the current boundaries of an entity's own financial statements[1] and performance by suggesting that an entity should:

    a. Benchmark its business model/operation against other entities in the "industry" and disclose "material" difference based on the hypothetical users of that "industry's" financial statements that they "might expect" assume there should be disclosures. We have application questions regarding what "industry" that an entity should consider when preparing disclosures under this new disclosure requirement. There are a number of approaches that can be taken to determine "industry" that a hypothetical user would consider, and clarification by the Board would be helpful if the Board continues to support these illustrative examples. For example, should we look at Standard Industrial Classification, stock exchange classifications, or rely on professional judgment.

[1] Extends the concept of "material" beyond the financial statement, as concept defined in IAS 1 which is *"Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions that users make on **the basis of the** financial statements"*

Also, the term "might" requires further clarification as to what threshold the Board is intending. We recommend that the Board use terms such as remote, probable, highly probable or virtually certain, that are more commonly used and understood terminology in IFRS Accounting Standards.

b. Disclose matters that have no effect on the recognition and measurement of its assets and liabilities and related incomes and expenses, otherwise referred to as "negative confirmation". We would also like to understand how this is considered with other disclosures in IFRS Accounting Standards, and whether this would also broaden the application of other disclosure requirements. Currently, preparers do not disclose information where there is no material impact on the current financial statements. If there is no disclosure, there is a presumption that the information is not material. This now appears to be a new interpretation of materiality requirements.

c. Disregard the required assumption about the characteristic of financial statements users, which requires preparers to assume that users "have a reasonable knowledge of business and economic activities and who review and analyze the information diligently. At times, even well-informed and diligent users may need to seek the aid of an adviser to understand information about complex economic phenomena."[2]

2. Broadens the concept of fair presentation, implying that to achieve fair presentation under IFRS, an entity should also consider matters that do not affect the faithful representation of the effects of transactions, other events and conditions in accordance with the definition and recognition criteria for assets, liabilities, income and expenses set out in the IFRS Conceptual Framework for Financial Reporting for the period presented.

In our view, Examples 1 and 2, unlike the other examples, introduce new materiality principles and concepts. We recommend that the Board remove Examples 1 and 2. It is not an action that we recommend but the Board might then consider amending the formal standard. Contrary to simply releasing the illustrative examples, consideration of an amendment to the formal standard provides additional due processes, including in-depth consultation and a transitional period, for adopting any new disclosure requirements.

Example 7 – Disclosure about decommissioning and restoration provisions (IAS 37)

In paragraph 7.2, the term "increasing" is used to describe the risk, but in our view, the risk should be described as significant, not merely increasing, as an increasing risk may still represent a relatively low level of risk. The core issue in this example seems to be whether the assumption around the very long discount rate leading to an immaterial provision is appropriate, rather than relying on disclosure to address this.

[2] Conceptual Framework for Financial Reporting 2.36

The disclosures appear to be extending the disclosure requirements of IAS 37 including requiring the undiscounted cash flows and the specific timing of the entity's expectation of when it expects to close the manufacturing facility which may differ from the expected timing of cash outflows. These requirements are better addressed in explicit standard setting and narrow scope amendments to IAS 37 than through an illustrative example.

We also recommend changing the language in the example of "assumes that it will continue to maintain and operate the facilities *for an extremely long time*". Instead, we recommend using language more consistent with IFRS Accounting Standards such as "for the foreseeable future".

Effective Date

We understand that materials accompanying IFRS Accounting Standards, including Illustrative Examples, are not an integral part of the IFRS Accounting Standards and as such, do not have an effective date or transition requirements. We suggest that the Board clarify that if an entity provides additional disclosures, that this would not be considered as a result of an error, similar to IFRS Interpretation Committee agenda decisions.

Thank you for considering our comments and recommendations.

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Chair, ESG and Sustainability Committee
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