28 November 2024

International Accounting Standards Board
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United Kingdom
Email: commentletters@ifrs.org

Dear Sir/Madam

SAICA SUBMISSION ON ED/2024/6 – *CLIMATE-RELATED AND OTHER UNCERTAINTIES IN THE FINANCIAL STATEMENTS - PROPOSED ILLUSTRATIVE EXAMPLES*

In response to your request for comments on ED/2024/6 – *Climate-Related and Other Uncertainties in the Financial Statements –Proposed Illustrative Examples*, attached is the comment letter prepared by the South African Institute of Chartered Accountants (SAICA). This comment letter results from deliberations of SAICA's Accounting Practices Committee (APC), which comprises members from reporting organisations, regulators, auditors, IFRS specialists, investment analysts and academics.

We thank you for the opportunity to provide comments on this Exposure Draft.

Please do not hesitate to contact us should you wish to discuss any of our comments.

Prof Ahmed Mohammadali-Haji
Chairperson: APC

Mulala Ratshitanga
Project Director: Financial Reporting

Cc: Bongeka Nodada
Executive: Corporate Reporting

OVERALL COMMENT

We agree for the inclusion of illustrative examples to accompany IFRS Accounting Standards. We do however believe that there are areas of enhancement that the International Accounting Standards Board (IASB/Board) should consider in finalising the examples. These consist of clarifying information included within the examples by including wording incorporated within the Basis for Conclusions into the body of the examples and considering introducing a decision tree or framework that may be applied by a user in determining the appropriate disclosure that may be required from a climate related risk or uncertainty.

SPECIFIC COMMENTS

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.

We agree that providing examples would help improve the reporting of the effects of climate-related and other uncertainties in the financial statements. We acknowledge that the examples in the exposure draft focus on climate-related uncertainties based on stakeholder feedback and that the principles can be applied to other uncertainties (BC 15). However, we are concerned that the illustrative examples are coming across as restrictive because of the focus on climate-related matters and that it is not clear how it will apply to other uncertainties (ESG and non-ESG related) even though in principle the examples would apply.

We have noted that the Basis for Conclusions (BCs) does not provide more clarity on other uncertainties, and we are concerned that preparers or users of this material might not be able to identify other uncertainties from the information provided or apply the examples to other uncertainties. We note that climate is an interrelated issue with other aspects of environmental, social, and governance (ESG) and we recommend that, in future, as the Board develops other standards on sustainability the Board consider incorporating the integration of climate with other ESG elements in the illustrative examples by expanding the scope of the illustrative examples to also include other areas of uncertainties, for example impacts of social and governance related uncertainties, and not limiting only to climate-related uncertainties. In addition, we recommend that the concepts and further explanations that are provided through the BCs should be incorporated in the examples as it would provide additional clarity as the BCs are often not published together with the examples on final issuance.

With regards to the examples provided we would appreciate the Board to consider the following highlighted concerns:

- The examples provided only describe eight situations and this might result in these examples being looked at as an exhaustive list for consideration whether the examples apply or don't apply to the entity's situation. This might result in inadequate completeness of disclosures. We acknowledge that paragraph BC 12 aims to clarify that the examples are not an exhaustive list however, as noted above the BCs are published with the examples and preparers could potentially interpret the examples as being an exhaustive list. We recommend that such key principles that are included in the BCs are moved to, and included with the examples.

- The examples provided are driven by the current needs of stakeholders and are specifically linked to climate-related uncertainties. We are concerned that in the long-term this may not be sustainable or broad enough to be fit for purpose based on the introduction of new risks and uncertainties. For example, with the introduction of generative artificial intelligence, there is a risk of structural changes within an organisation that may affect future operating models and sustainability which in turn may affect financial related outcomes. We recommend that the Board considers future-proofing the illustrative examples with a framework as noted above, or to consider introducing additional examples by taking other risks into consideration, such as data privacy and social relations etc.

- Some constituents might misinterpret the eight examples provided as guidance only whilst others may see it as interpretations of the standards to be used to conclude on the appropriate disclosure to be provided in that limited instance. We would strongly recommend that the Board consider introducing an overarching decision tree or a disclosure framework to be used by preparers in developing these qualitative disclosures that relate to climate and other related uncertainties, we would recommend for such a decision tree/ framework to be included in IAS 1 and IFRS 18. The examples provided in the Exposure Draft will be the outcome of such decision tree and framework of how to disclose these concepts, while the decision tree/framework would provide guidance on when a matter would require disclosure. In developing such decision tree or framework, certain constituents are of the view that the risks and any related uncertainties should be linked to any outcomes from the application of the International Sustainability Standards Board (ISSB) standards. These standards would be an appropriate base in determining any resultant qualitative financial statement disclosures. This will also assist with improving connectivity between financial information (IASB) and sustainability information (ISSB).

  "For example, for a financial services entity, many climate related risks are identified in their sustainability report. Consideration is then given to how these identified climate related risks impact the financial statements. The financial services entity identifies that the climate related risks have an impact on the credit risk of their debtors. The materiality decision tree/framework would then be applied to determine whether disclosures should be provided in the financial statements to highlight the impact of the related climate uncertainties on the financial statements."

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.

Example 1—Materiality judgements leading to additional disclosures (IAS 1/IFRS 18)

We support example 1 and we believe that the example provided is useful in illustrating the principle of materiality and we also believe that it would link to a decision tree, suggested in question 1 above, in assisting to illustrate and decide whether or not it is material.

However, we would like to bring the following points to the attention of the Board for further consideration:

- We note that the background provided in paragraph 1.2 does not only refer to '*energy-efficient technology like equipment, but it also includes changes in its raw materials and manufacturing and methods'*. We have however noted that the application of the background does not refer to the other standards such as IAS 2 – *Inventories* (IAS 2) as a potential IFRS Accounting standard to be considered even though inventories are clearly referred to in the background. We understand that the BCs (BC 12) state that the intention is not to capture all possible scenarios and all the principles of IFRS Accounting Standards, however for this example, our suggestion is that on paragraph 1.4 where other standards could be applicable, the Board should consider incorporating other standards including IAS 2 or to narrow the background information provided so that the focus remains on the impact of IAS 16 – *Property, Plant and Equipment* (IAS 16). An example would be to focus on the change in technology and the equipment that is being used.

  We are concerned that the example noted in paragraph 1.8 which considers " the disclosures in the general purpose financial report outside the financial statements" could have a wider implication on the audit report by requiring auditors to consider assuring a broader range of information outside the financial statements.

- We recommend that the Board considers introducing an analysis of other resultant risks that may arise because of the introduction of energy-efficient technology with a narrative of how management has considered these risks in determining the outcome and disclosure that was determined to be provided. Certain constituents are of the view that this would provide more useful information to a user in determining how disclosure should be provided.

- We recommend that the Board reconsiders the wording noted in paragraph 1.9 which states that "*the entity discloses that its transition plan has no effect on its financial position and financial performance*". The statement reads as a negative statement with no impact on the entity which would not entirely be true as any resultant effect of the transition plan may be immaterial rather than Nil. We recommend the Board include the following wording "the entity discloses that its transition plan has no material effect on its financial position and financial performance…".

Example 2—Materiality judgements not leading to additional disclosures (IAS 1/IFRS 18)

We support this example, however as this follows from example 1, we recommend that the Board considers the comments provided in example 1 as it will indirectly affect the outcome in example 2.

Example 3—Disclosure of assumptions: specific requirements (IAS 36)

We support this example and believe it is useful to assist users in considering the disclosure requirements of IAS 36 – *Impairment of Assets* (IAS 36).

We note that the example only refers to the requirements of IAS 36, and although not directly required due to IAS 36's requirements, the example does not illustrate how these disclosure requirements are supported by the principles in IAS 1 – *Presentation of Financial Statements* (IAS 1) paragraph 125 which underpins the basis for the disclosure. We recommend that the Board considers adding a link into the example to illustrate how paragraph 125 of IAS 1 supports the disclosure requirements in IAS 36.

Example 4—Disclosure of assumptions: general requirements (IAS 1/IAS 8)

We support example 4 and appreciate the link to IAS 1 disclosure requirements that the example illustrates.

However, we would like to bring the following to the attention of the Board:

- In our view we believe that the current wording in the example could potentially create an expectation of users that disclosure would always be required, even when no disclosure is required under a specific accounting standard (IAS 36 in the case of this example) and the assumptions do not reflect major sources of uncertainty.

- We note that example 5 illustrates a scenario where disclosure is not required in terms of IAS 1 paragraph 125, this however relates to an income tax scenario and we do not believe that it clearly illustrates when IAS 1 paragraph 125 requires additional disclosure and when it does not, especially if the examples are not included within a single suite of examples to a specific IFRS Accounting Standard.

- We request the Board to consider clarifying the link between examples 4 and 5 to illustrate the above-mentioned point. Alternatively, the converse within example 4 could be created to illustrate that if the assumptions in an impairment assessment of a CGU that does not contain any goodwill, or intangible assets with indefinite useful lives, are not considered a major source of estimation uncertainty, then the additional disclosure in accordance with IAS 1 is not required.

Further we believe it may be beneficial if the example was supported by a framework or decision tree to illustrate the principles in IAS 1 paragraph 125.

Example 5—Disclosure of assumptions: additional disclosures (IAS 1/IFRS 18)

We support example 5, and as noted in example 4 we appreciate the link that is made to the disclosure requirements in IAS 1.

However, we would like to bring the following to the attention of the Board:

- In our view the current wording in the example does not illustrate why the announced regulations in the example are material to the users of the financial statements, and without this clarity we believe preparers could potentially interpret the example to mean that any matter, even one where the likelihood of it materialising is remote, could require disclosure in terms of IAS 1. We do not believe this is the intention of the disclosure requirements in IAS 1 paragraph 31. We suggest that the Board consider clarifying why the announced regulations are considered material and how the fact that a scenario being a possibility, even in the event that the likelihood of the outcome is remote, is material.

Example 6—Disclosure about credit risk (IFRS 7)

We are supportive of the example.

However, we would like to bring the following to attention of the Board:

- We note that in example 6 the background in paragraph 6.2 is broad and can be construed as to include all financial institutions, even if the financial institution holds a portfolio that may be quantitatively material but is not necessarily significant in relation to the overall loans and advances made by the entity. If so construed, this may result in entities interpreting the example such that onerous disclosure is required to illustrate their risk in relation to climate related matters for a portfolio that is not significant. We note that in paragraph 6.3 the examples aim to narrow the scope to which it would apply, specifically in indicating that the size of the portfolio in relation to the overall lending portfolio should be considered, however, we do not believe that this sufficiently narrows the scope. A commercial bank for example may have a significant mortgage portfolio that is affected by climate risk, but to a limited extent. In relation to such a portfolio, the climate related risks are unlikely to be significant enough to warrant disclosure.

- We recommend that the Board consider narrowing the scope of the example in the background section, so that it applies specifically to financial institutions which predominantly service the agricultural sector, for example. As we do not believe the example currently provide sufficient guidance on how granular the disaggregation of portfolios should be, or how an entity would assess the disclosure requirements if a portfolio is quantitatively material and climate related risks does not have a material impact on the portfolio.

Further, some of our constituents have noted that although the example refers to the specific disclosure requirements in accordance with IFRS 7 – *Financial instruments: Disclosures* (IFRS 7), there may be scenarios where the assumptions relating to climate related risks in an entity's ECL model are not themselves significant but there is a major estimation uncertainty in relation to climate related risks which may require disclosure in accordance with IAS 1 paragraph 125. We recommend that the Board considers including a link to IAS 1 paragraph 125 in this example to illustrate that there may be scenarios where such disclosure is required.

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

We are supportive of an example in relation to how provisions may be impacted by climate related uncertainties, however we do not agree that example 7 clearly illustrates these principles.

We request the Board to provide clarity on this example, specifically on how disclosure requirements are within the scope of IAS 37 – *Provisions, Contingent liabilities, and Contingent Assets (IAS 37)*. Our view is that the fact pattern in this example does not result in the recognition of a provision, and we are concerned that a matter which does not result in an item being recognised in the financial statements or represent a contingent liability would necessitate further disclosure under IAS 37.

Paragraph 7.3 indicates that the information is material and therefore disclosure is required under IAS 37, in our view such disclosure would be required in accordance with IAS 1 paragraph 31. However, a concern was raised that if by applying the measurement and recognition requirements of IAS 37 only an immaterial amount is recognised, would the information truly be material to the users. In our view preparers applying the requirements of IAS 37 would result in sufficient disclosure. We recommend that the Board considers clarifying in the example under which standard the required disclosure would be necessitated and to clearly illustrate why the information is considered material.

Example 8—Disclosure of disaggregated information (IFRS 18)

We are supportive of the example however we recommend the Board to consider the following points:

- We request the Board to include a link to references in IAS 1 paragraph 30A as was done in the other examples and provide a clear link back to example 1 and 2;

- We request the Board to link the example to IAS 16 paragraph 73 as per its requirement to disaggregate per class of assets; and

- We request the Board to reconsider whether the bases included in this example are appropriate in the context of IAS 16's definition of classes of property, plant and equipment (PPE) as we are concerned with the disaggregation noted in the example. IAS 16 defines classes of PPE as groupings of assets of a similar nature and use in an entity's operations, whereas this example would infer that additional bases of aggregation and disaggregation are required even where the grouping of items is clearly defined within a specific accounting standard.

Question 3—Other comments

Do you have any other comments on the Exposure Draft?

We do not have any additional comments.