ACRA
ACCOUNTING AND CORPORATE REGULATORY AUTHORITY

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(By online submission)

Dear Andreas

RESPONSE TO EXPOSURE DRAFT ON CLIMATE-RELATED AND OTHER UNCERTAINTIES IN THE FINANCIAL STATEMENTS—PROPOSED ILLUSTRATIVE EXAMPLES

The Singapore Accounting Standards Committee (ASC), under the Accounting and Corporate Regulatory Authority (ACRA), welcomes the opportunity to comment on the Exposure Draft on *Climate-related and Other Uncertainties in the Financial Statements—Proposed illustrative examples* (the ED) issued by the International Accounting Standards Board (the IASB) in July 2024.

We support the IASB's objective to provide illustrative examples that demonstrate how entities should apply the requirements in IFRS Accounting Standards to report the effects of climate-related and other uncertainties in their financial statements. Given the increasing significance of these uncertainties, guidance on reflecting these uncertainties in financial reporting is increasingly necessary. The proposed illustrative examples are a positive first step towards addressing stakeholder concerns about the adequate disclosures related to climate risks and their financial impact. This guidance should help entities better apply the requirements in IFRS Accounting Standards and navigate the complexities of communicating climate-related and other uncertainties together with their impact on financial position and performance.

We are generally supportive of the proposals set out in the ED but have specific comments on certain aspects. Our comments are as follows:

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.

Based on the IASB's research, IFRS Accounting Standards are generally sufficient in requiring disclosures about the effects of climate-related risks in the financial statements but entities face challenges in applying those Standards to situations arising from climate-related and other uncertainties. Climate-related risk reporting is not a totally new area, but the significant focus on it over the recent past few years made it crucial now for entities to ensure that they are able to apply judgement in IFRS Accounting Standards to derive the relevant disclosures important to users of financial statements. However, we are cognisant that it is not easy and entities should be given time to deepen their knowledge on the application.

We have obtained some feedback from our stakeholder outreach that better reporting of climate-related and other uncertainties goes beyond simply issuing these examples as the exercise of judgement using the overarching requirement in paragraph 31 of IAS 1 *Presentation of Financial Statements* would likely fall short, resulting in the existing reporting issue continuing in practice. These stakeholders believed that standard setting that requires mandatory disclosure requirements would better drive appropriate behavioural changes and better climate-related risks reporting in financial statements.

That said, in striking an appropriate balance between mandatory standard-setting requirements, which could take a longer period of time, and issuing these examples in a more timely manner, the latter approach would, in our view, represent a well-balanced approach. It is a positive first step to quickly issue guidance to help improve the reporting in the financial statements for these areas. Issuing these examples could guide entities in applying existing principles to report on these uncertainties, as well as raise awareness and promote greater consistency in reporting practices. While we acknowledge that examples alone may not achieve the full desired behavioural changes compared to mandatory disclosure requirements, they represent a pragmatic approach in the interim, especially given the rapidly evolving nature of climate and sustainability reporting.

We suggest further that the IASB continues to monitor whether the lack of reporting on climate-related risks in financial statements continues to be an issue, even after the issuance of these examples. If entities are still not disclosing sufficient information, this could lend further credence that paragraph 31 of IAS 1 is not working as intended and hence, the IASB should consider standard-setting to address the underlying issue.

We agree with the ED proposal to include the examples as illustrative examples accompanying the IFRS Accounting Standards based on the rationale in paragraph BC43 of the ED. Reflecting on past IASB materials on climate-related topics which were published separately as educational material, there exists the risk that these examples might be overlooked by entities, especially if they are in a different location to the suite of IFRS Accounting Standards and their accompanying documents. In addition, we suggest that the IASB provides more and/or updated examples on a periodic basis to reflect new emerging scenarios as climate-related risk reporting and sustainability reporting standards evolve. This ensures that the examples remain relevant with the latest requirements.

In addition, we support the IASB’s suggestion in paragraph BC45 of the ED to group examples pertaining to climate-related and other uncertainties into a single document, which would facilitate easier access for entities to refer to all climate-related examples in one package.

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.

We generally agree with the IASB's approach to developing the examples and the selection of requirements and fact patterns illustrated. However, we have several observations below.

<u>Clarification on implementing the examples</u>

To avoid the concern about possible unintended consequences arising from the examples, including leading to increased disclosures in a manner that obscures other material information already disclosed, we suggest that the IASB considers including explanations, in the Basis for Conclusions, to clarify that the examples are intended to illustrate the application of certain disclosures required under IFRS Accounting Standards based on the specific fact patterns and are not meant to cover all possible other situations, nor serve as a comprehensive checklist. It would also be beneficial for the IASB to emphasise the importance of entities tailoring climate-related risk disclosures and the assumptions to their specific circumstances and avoid using boilerplate language.

<u>Connectivity between sustainability and financial reporting</u>

We view that the examples demonstrate an improvement in the connectivity between financial reporting and sustainability reporting. However, we suggest that the IASB continues to collaborate closely with the ISSB to further strengthen the connectivity between the information an entity provides in its financial statements and the information it provides in its sustainability-related financial disclosures by specifically demonstrating the linkage between sustainability reports and financial statements in the examples. For instance, the examples could demonstrate how disclosures in sustainability reporting, such as those related to climate scenario analysis or transition plans, connect to and impact information in financial reporting. This could be illustrated further by reconciling or explaining differences between sustainability commitments (such as net-zero targets) and their financial implications in the financial statements or illustrating how transition plans (such as strategies for replacing machinery with sustainable alternatives or adopting sustainable fuel options) disclosed in sustainability reports might influence financial statement disclosures and estimates. The examples could possibly include some form of reconciliation from financial statements to sustainability reports to demonstrate the connectivity, a concept not dissimilar to MPMs in IFRS 18 *Presentation and Disclosure in Financial Statements*. Such an approach would help entities provide a more coherent and integrated view of their climate-related risks and strategies.

Expanding the scope of examples

We do not think that the IASB should be restricted to only either stand-alone examples or walk-through examples as they provide illustrations based on different purposes. As explained in paragraph BC17 of the ED, stand-alone examples would be good for illustrations with narrow fact patterns illustrating particular requirements in an IFRS Accounting Standard. Conversely, walk-through examples would be better for illustrations with broad fact patterns illustrating several requirements in a selection of IFRS Accounting Standards. If more time is needed to develop walk-through examples, the IASB could proceed to issue these eight examples first, and work on some walk-through examples when they publish their next set of periodic examples, if the IASB takes up our earlier suggestion to provide continuous periodic update of examples.

Further, we suggest that IASB include examples that involve a higher degree of judgement, particularly in determining certain accounting treatments. These examples should explain when disclosures are necessary if sustainability commitments are not required to be provided for under IFRS Accounting Standards. This would help entities better understand how to apply judgement in complex scenarios.

We note that in the exposure draft on *Provisions—Targeted Improvements*, the IASB proposes to add a new illustrative example based on the fact patterns of the agenda decision on *Climate related Commitments*. We view that this agenda decision is also relevant to this ED and its inclusion, based on the existing requirements of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, in the package of climate-related examples, should the IASB proceed with paragraph BC45 of the ED, would be warranted to ensure that the illustrative examples reflect recent guidance on climate-related financial reporting. When the IASB issues amendments to IAS 37 after finalising the proposals of this ED, the IASB should update this illustrative example accordingly.

Our stakeholders have also suggested the inclusion of the following examples in its next update, should the IASB agree with our earlier suggestion to provide more and/or updated examples on a periodic basis to reflect new emerging scenarios:

(a) An example on how an entity applies the requirements of IFRS 13 *Fair Value Measurements*, to consider information to disclose about the effects of climate-related risks on the fair value of its investment properties that are exposed to climate-related physical risks could be provided;

(b) An example on how an entity applies the requirements IFRS 16 *Leases*, particularly how climate-related risks impact operating and finance leases; and

(c) Transition plans, including examples on replacing sustainable machinery, using sustainable fuel alternatives, and purchasing carbon credits to offset residual emissions.

<u>More examples on other Uncertainties</u>

While we understand that the focus of this ED is on climate-related risks reporting, we suggest that the IASB considers providing more examples relating to non-climate-related uncertainties as there is only one such example out of the eight examples in the ED. Entities face a wide variety of non-climate-related uncertainties, and a single example may not sufficiently cover the diverse range of risks and uncertainties they encounter. Additional examples would also help ensure consistent application across these various types of risks and uncertainties.

Our specific comments on the individual examples are as follows:

<u>Example 1</u>

Example 1 relates to how an entity considers qualitative factors in making materiality judgements and we are glad that the IASB utilised and built on the examples in IFRS Practice Statement 2 *Making Materiality Judgements* (PS2), for example on Example K, which illustrates how external qualitative factors impact materiality judgements. That said, we view that the IASB should highlight that materiality assessments should encompass both qualitative and quantitative factors, even though example 1 illustrates a scenario with a focus on the qualitative aspects. As it is currently drafted, we observe that there can be potential unintended consequences that may arise from this example and its implications for financial reporting practices. The example presents a scenario where it is evident in the financial statements of the entity that there is a low asset base and an absence of asset retirement obligations. Thus, this raises the question about the necessity and value of additional climate-related disclosures in such an instance. Further, the example appears to rely on the expectation that decisions of users of financial statements could be reasonably influenced by a lack of understanding of how the entity's transition plan has affected the entity's financial position and financial performance. Such an expectation could happen on factors beyond climate-related risks and impact what boundaries should be set to meet users' expectations. Therefore, we suggest that the IASB clarifies that disclosures are only required when they provide meaningful information about financial impacts, in line with the requirements in IAS 1.

We also note that while Example K is located in PS2, example 1 (and 2) is proposed to be located in IAS 1 (or IFRS 18). We suggest that the IASB considers including a reference of example 1 (and 2) to PS2 Example K to facilitate entities comparing and drawing references between these examples, or alternatively, considers whether locating example 1 (and 2) in PS2 would be better. To strengthen the usefulness of this example, we suggest that the IASB considers including a broader range of factors that may indicate qualitative materiality, such as referring to or contextualising user-specific aspects. For example, climate-related inputs used in financial analysis or investor calls, user information requests to the entity or information published by stakeholders or data analysts, instead of only referring to an entity’s own disclosures and the industry in which the entity operates in.

<u>Example 3</u>

We observe that this example could be interpreted as applicable only to an entity with high greenhouse gas emissions, and could therefore, potentially lead entities with lower greenhouse gas emissions to conclude that the example is not applicable to their circumstances. To address this potential issue, we suggest that the IASB considers using more precise wording, for example in the Basis for Conclusions, to ensure broader applicability of the example.

We also note that the example does not mention whether climate-related risks are incorporated into the discount rate or cash flow projections and suggest that the IASB provides clarification to mitigate any risk of potentially double-counting these risks in both cash flows and discount rates. This observation is also applicable for Example 4.

<u>Example 4</u>

We observe that the example omits mention of intangible assets not yet available for use. Hence, we suggest that the IASB considers not including technical explanations, such as those included in paragraph 4.4, to mitigate the risk of incomplete guidance. A more effective approach might be to simply state that "a mandatory annual impairment test is not required" without further elaboration.

<u>Example 5</u>

While we note that it is not uncommon for governments to announce plans to implement regulations in advance without providing specific details, we observe that there could be a risk of interpreting the example as requiring disclosure of financial effects of such future regulations. This could be onerous for group entities operating in multiple jurisdictions, given the varying stages and uncertainty of regulatory developments across different jurisdictions. If the IASB intends for example 5 to only illustrate disclosures on uncertainties surrounding the recognition of deferred tax assets, we suggest that the IASB clarifies this specifically in the background.

Further, the IASB should also clarify that there is no going concern issue for this entity, given that implications related to going concern could be raised if the regulation could affect the entity’s profitability significantly. One other suggestion is clarifying certain terms used in the example, such as 'announced', 'enacted', and 'effective', which appear to be broad and could be interpreted differently.

<u>Example 6</u>

We note that paragraph 6.4(c) of the example suggests an entity considers what information to provide about properties held as collateral that are subject to flood risk and whether that risk is insured. Having insurance protection is one of various risk mitigation techniques that an entity can deploy to mitigate climate risk, and therefore, we suggest that the IASB considers rewording this part of the example to consider the various risk mitigation approaches, instead of specifying a requirement for explicit disclosure about insurance.

Example 7

We note that this is a good example to illustrate that even if the carrying amount of the plant decommissioning and site restoration obligations is immaterial, an entity would have to determine whether it needs to disclose information about that associated provision. However, we suggest that the IASB considers adding more clarity on how the entity makes a materiality judgement using the information provided in the fact pattern, including whether entities should consider qualitative factors for all other information (including references to IAS 1, where applicable) even when the carrying amount of assets and liabilities is quantitatively immaterial. Other clarifications include whether the entity has a transition plan to a low greenhouse gas emission plant or if such a plan is disclosed in other reports. This ambiguity could lead users of financial statements to form expectations about the entity's operations that may not be aligned with the entity's actual assumptions, such as anticipating an earlier cessation of petrochemical facility operations.

Example 8

This example illustrates the requirements in paragraphs 41–42 and B110 of IFRS 18. However, IFRS 18 has an effective date of 1 January 2027, unless entities choose to early apply the Standard. Therefore, there could be potential confusion in practice whether the example should be based on the principles in IFRS 18 or IAS 1 and we suggest that the IASB clarifies this point.

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

We have the additional following comments on the ED:

Materiality considerations

Feedback received from our stakeholders indicates that application guidance is sought when (and whether) material sustainability disclosures, applying IFRS S1 and S2, may become material for financial statements disclosures. We note that the latest version of PS2 was issued before the issuance of IFRS S1 and S2, and suggest that the IASB considers reviewing PS2 with the ISSB on whether a revision would be necessary or to demonstrate greater connectivity between the information an entity provides in its financial statements and in its sustainability-related financial disclosures.

Incorporating the examples into IFRS for SMEs Accounting Standard

Climate-related risks affect all businesses, regardless of size. The IASB's intention of issuing these examples to provide clarity and guidance on applying existing requirements in IFRS Accounting Standards, would therefore apply similarly to entities applying IFRS for SMEs Accounting Standard. While we acknowledge the concerns about increased reporting burden and complexity, particularly for smaller entities, the IASB could balance the disclosures required with the undue cost or effort consideration in IFRS for SMEs Accounting Standard, especially since those entities do not have public accountability. Therefore, we suggest that the IASB considers introducing these examples into the IFRS for SMEs Accounting Standard and modify them if necessary to factor in the above considerations.

We hope that our comments will contribute to the IASB's deliberation on the ED. Should you require any further clarification, please contact our project managers Yat Hwa Guan at Guan_Yat_Hwa@acra.gov.sg and Chuan Jian Lo at Lo_Chuan_Jian@acra.gov.sg.

Yours sincerely

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