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Mr Andreas Barckow, Chair
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only submitted electronically via: https://www.ifrs.org/projects/open-for-comment/

Re.: IASB Exposure Draft (ED)/2024/6 – Climate-related and Other Uncertainties in the Financial Statements – Proposed illustrative examples

Dear Mr Barckow

The IDW (Institut der Wirtschaftsprüfer in Deutschland e.V.)[1] is pleased to comment on the International Accounting Standards Board's IFRS Accounting Standard Exposure Draft (ED)/2024/6 *"Climate-related and Other Uncertainties in the Financial Statements – Proposed illustrative examples".*

We welcome the IASB's decision to act on the feedback from respondents to its Third Agenda Consultation and launch a project focused on the presentation of Climate-related and Other Uncertainties in IFRS financial statements. In its comment letter to the IASB's Third Agenda Consultation dated September 27, 2021, the IDW generally pointed out the importance of the issue of considering sustainability-related aspects in IFRS financial statements in view of current environmental and socio-economic developments, especially with regard to the increased investor demand for information in this regard.

Furthermore, we remain firmly convinced that in the coming years the IASB will increasingly have to address questions of interconnectivity between financial and non-financial/sustainability reporting in its standard-setting projects and

[1] The IDW is a voluntary membership organisation representing the interests of the profession of public auditors in Germany and counts over 79 % of this profession as members.

that, against this background, cooperation between members and technical staff of the IASB and the ISSB will be the norm rather than the exception.

Therefore, we see the current project and the present ED as a first step in the right direction. However, we would have liked the IASB to have been more courageous in addressing this issue, given its importance. In our view, the proposed examples may be helpful and understandable for preparers of financial statements who are dealing with the potential impact of sustainability-related issues on their IFRS financial statements for the first time. However, for preparers who have already come part of the way and, for example, have already dealt with the IASB's educational material 'Effects of climate-related matters on financial statements' (2020/2023), we think the examples are too simple, too clear-cut, and, in some cases, inconsistent and consequently of little practical use.

In our view, additional examples combined with the call for more disclosures of climate-related and other uncertainties based on the general principles of IAS 1 are not enough to bring about a real change in practice. In our view, more than such minimally invasive means are needed to achieve appropriate consideration of sustainability-related issues in IFRS financial statements, while still ensuring consistency of such information in financial statements and sustainability reports (without simply duplicating sustainability-related information in both reports). The issue is too significant and too multifaceted for that.

Rather, we believe that several fundamental questions need to be answered first. These include, among others:

- Clarifying the objective and content of IFRS financial statements:
  - What should future IFRS financial statements look like?
  - How can relevance and decision-usefulness of IFRS financial statements be ensured in the long term in view of current developments related to sustainability issues and sustainability reporting?
  - What information should IFRS financial statements contain and what role should sustainability-related information (qualitative and/or quantitative) play in them?
- Connectivity between financial and sustainability reporting:
  - How can or should both standard-setting bodies (IASB, ISSB) distinguish between information to be included in IFRS financial statements and that to be included in sustainability reports with regard to future standard-setting projects?

- Can financial and sustainability-related information be separated on a principles-based approach and, if so, how?
- How can the duplication of information in the IFRS financial statements and the sustainability reports be avoided?

In our view, current questions facing the practice (e.g. whether and, if so, how climate-related transition plans or value chains should be reflected in IFRS financial statements) cannot be answered until these fundamental questions have been clarified by the IASB.

The educational material already published by the Board and the examples proposed in this ED may initially help to raise awareness of the issue of considering sustainability-related information in IFRS financial statements. From our point of view, however, a clear objective and strategy for handling sustainability-related information is now required. After that, the current set of IAS/IFRS would have to be reviewed to determine whether, in addition to the above general non-binding guidance and recommendations for additional disclosures based on IAS 1/IFRS 18, standard-setting activities are also required, i.e. the amendment or supplementation of both the recognition and measurement requirements and the disclosure requirements of individual standards (e.g. IAS 36, IAS 37).

In our perception, analysts and enforcement authorities, particularly in Europe, have high expectations regarding an appropriate consideration of relevant and decision-useful sustainability-related information in IFRS financial statements and the consistency of financial reports with the information provided in sustainability reports.[2] We doubt that the examples proposed in this ED will be sufficient to fulfil their expectations.

In our view, clear, balanced and enforceable requirements are needed to ensure that analysts and investors receive the information they actually need to make meaningful decisions. On the other hand, preparers should not be burdened with undue cost of gathering information and should not be exposed to the de facto pressure to bloat their IFRS financial statements with “recommended” information or information that individual stakeholders consider to be essential/material (“information overload”).

We are aware of the challenges faced by the Board when determining how to deal with non-financial/sustainability information in IFRS financial statements.

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2 See, e.g., ESMA’s report, The Heat is On: Disclosures of Climate-Related Matters in the Financial Statements (25 October 2023) and ESMA’s Public Statements, European common enforcement priorities for 2023/2024 annual financial reports.

Nevertheless, we hope that the IASB will continue to pursue the issue and take all necessary steps to ensure that it can continue to provide its stakeholders with high-quality, understandable, enforceable and globally accepted IFRS accounting and sustainability disclosure standards.

Notwithstanding the concerns and other suggestions set out in the previous sections and the following comments made on the specific questions of the ED below, the IDW is in favour of the examples proposed in the ED being finalised and published as illustrative examples of the respective IFRS Accounting Standard.

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.*

(a): We believe that examples can only strengthen the link between the presentation of climate-related and other information related to uncertainties in IFRS financial statements and in sustainability reports/other general-purpose financial reports to a certain extent. Furthermore, this presupposes that the examples ultimately chosen are relevant to practice and clearly formulated.

As already described in the General Remarks above, we hope that the final examples – in addition to the IASB's already published educational material – will help to raise awareness of the issue of considering effects of climate-related and other uncertainties in the financial statements among those preparers who have not yet addressed it. However, it cannot be ruled out that further examples only lead to good preparers improving their climate-related disclosures, while the impact on other preparers could be minimal.

In general, we have serious doubts that simply providing examples will lead to a significant improvement in the reporting of the effects of climate-related and other uncertainties in the financial statements. Notably, we doubt that examples will suffice to meet the expectations for uniform, consistent and comprehensive reporting of climate-related information within and outside of financial reports, which we perceive particularly among analysts and enforcement authorities.

As already stated in the General Remarks above, we believe that fundamental conceptual questions regarding the handling of sustainability-related information in IFRS financial statements must first be clarified before it can be determined whether, in addition to non-binding guidance and recommendations for additional disclosures based on IAS 1/IFRS 18, standard-setting bodies may need to take specific measures, i.e. amend or supplement recognition and measurement requirements and/or disclosure requirements in individual standards, in order to achieve the stated goal of improving the financial reporting.

(b): In general, the IDW agrees to include the examples proposed in the ED as illustrative examples of the respective IFRS accounting standards. However, this procedure only makes sense if the examples, as suggested, are kept relatively simple and if they refer exclusively to the principles contained in the respective IAS/IFRS (i.e. no new principles or requirements are introduced by them).

Furthermore, this procedure also means that the proposed examples are less helpful in practice. However, sustainability-related matters (e.g., an entity's plans for transition or policies regarding greenhouse gas emissions) regularly have potential effects not only on assets, liabilities, expenses and income that are covered by one specific IAS/IFRS. In our view, such issues need to be assessed more comprehensively, i.e. across all standards. The assessment of such complex examples could be presented in a new IFRS Practice Statement, for instance. However, as soon as new principles and/or new disclosure requirements are applied in the assessment of such comprehensive sustainability-related issues, a new project should be put on the IASB’s agenda.

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 BC1O-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 agree with the Board that examples should focus on specific requirements in in IFRS Accounting Standards that

a) are among the most relevant for reporting the effects of climate-related and other uncertainties in the financial statements; and

b) are likely to address concerns that information about the effects of climate-related risks is insufficient or appears inconsistent with information outside financial statements.

We also agree with the IASB's view that individual examples can never fully represent the application of all requirements in the IFRS Accounting Standards that may be applicable to a specific case. Similarly, not all facts and circumstances that an entity would consider in assessing materiality in a particular case or all material information required to be disclosed by an entity in a particular case can be illustrated by examples.

By deciding to develop only so-called stand-alone examples, i.e. examples with narrow fact patterns illustrating particular requirements in an IFRS Accounting Standard, the IASB may be able to achieve faster project progress. However, the comparatively rapid project progress achieved by developing simple examples is at the expense of the usefulness of the examples. We strongly recommend that the IASB develop additional examples with broad fact patterns illustrating several requirements in a selection of IFRS Accounting Standards (so-called walk-through examples), either as part of this project or as a separate project. The walk-through examples could be included in a new IFRS Practice Statement, for instance.

Furthermore, we would appreciate if the IASB could also offer examples that address uncertainties not only related to environmental risks, Currently, only one of the eight examples (Example 5) is not directly related to environmental risks. New examples could address, among other things, macroeconomic risks, social risks, etc.

Moreover, we have the following comments and questions on selected examples of the ED:

Example 1

Specific examples of judgements made in the context of qualitative materiality assessments may appear helpful at first glance. However, the assessment of materiality always depends to a large extent on the facts and circumstances of the individual case. Such examples always carry the risk of generalisation or drawing analogies. From the preparer's point of view, such an approach is of course easy to follow, but it may be inappropriate in the respective individual case.

In general, several examples provided in the ED (including Example 1) result in disclosures based solely on the requirements of paragraph 31 of IAS 1. Accordingly, an entity shall also consider whether to provide additional disclosures when compliance with specific requirements in IFRS is insufficient to enable users of financial statements to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance. In our view, the examples provided in the ED may go beyond what could reasonably be expected in relation to disclosures based on this requirement. We do not believe that the intended outcome in the relevant examples could be achieved without standard-setting activities to introduce more specific requirements. From a conceptual perspective, it is at least worth discussing why preparers should explain why they have not provided further information (even if users would expect it).

If the determination to include additional disclosures in the notes to IFRS financial statements, as set out in several examples in the ED, is applied to other matters, we assume that significantly more information will be included in the notes in future, but that the usefulness of this information will often be limited. Instead, we see a significant risk of information overload, which can lead to truly material information being obscured.

Example 2

As in Example 1, the IDW questions whether the preparation and, if so, the extent of a general purpose financial report outside the financial statements should determine the extent of disclosures in IFRS financial statements in relation to climate-related matters (we refer to paragraphs 1.8(a) and 2.8(a) of the ED). We would be grateful for further clarification.

Example 3

We think that the example would have been more useful if it had illustrated the thought process behind determining that the entity's assumptions about the future cost of emission allowances are key assumptions (i.e. among the assumptions to which the recoverable amount of the cash-generating unit is most sensitive), as set out in paragraph 3.3 of the ED.

In addition, we question whether the level of emissions could also represent a key assumption of the entity within the meaning of IAS 36. A corresponding addition to the example might be helpful.

Example 5

The IDW considers the idea underlying Example 5 to be useful, i.e. to illustrate the interaction between the specific requirements of IAS 12 and the general requirements of IAS 1 (i.e. paragraphs 31 and 125). Ultimately, the disclosure requirement arises from paragraph 31 of IAS 1, i.e. in the example, the effects of the timing of the regulation on the carrying amount of the deferred tax asset were assessed as material information for the users. In this context we refer to our comments on Example 1.

Furthermore, we believe that the example would be more realistic and therefore more helpful if it related not only to the utilisation of tax losses, but also to the utilisation of deductible temporary differences, because the recoverability of carried-forward tax losses should not be assessed separately from the recoverability of other sources of deferred tax assets.

Finally, paragraph 5.2 of the ED states that *„the regulation could significantly affect the entity's profitability … "*. In addition to the entity's ability to recover the carrying amount of its deferred tax asset for the carryforward of unused tax losses, this also raises questions about the recoverability of other assets. Therefore, it would be welcome if it were clarified that this example only refers to the uncertainty relating the entity's deferred tax asset.

Example 7

In general, we do not consider this example to be realistic, as our experience in the petrochemical industry shows that decommissioning and restoration obligations are regularly material, even over a long period of time.

Moreover, from a conceptual point of view, we question why an existing risk that triggers disclosure requirements is not reflected in the measurement of the provision. Further clarification would be helpful.

Example 8

In general, the IDW supports this example. However, we recommend that the example includes a reference to the explanation provided in the IFRS financial statements as to why an aggregation or disaggregation of the figures has been made.

In addition, we propose to clarify how the disaggregation within this example interacts with the disaggregation at class level in accordance with IAS 16, paragraph 73. Example 8 implies that both "low emission" and "high emission" PP&E belong to one class of PP&E (we refer paragraph 8.6 of the ED *"the entity disaggregates the information it provides in the notes **about the related class of PP&E between the two types of PP&E**"*). According to the definition of a "class" in paragraph 37 of IAS 16 (i.e. *"a grouping of assets of a **similar nature** or use"*), it could also be argued that the two PP&Es (i.e. one with lower, the other with higher greenhouse gas emissions) each constitute separate "classes" within the meaning of IAS 16.

Irrespective of this, we think that an example concerning the disaggregation of information with reference to paragraph 114 of IFRS 15 ("Disaggregation of revenue") might even be more suitable. In this paragraph the term "uncertainty" is even explicitly mentioned as a factor to be taken into account.

Question 3: Other comments

Do you have any other comments on the Exposure Draft?

Finally, we would like to draw your attention to another accounting issue related to the presentation of sustainability-related aspects in IFRS financial statements, which, in our opinion, needs to be addressed with increasing urgency: pollutant pricing mechanisms.

We were pleased to see that, as a result of the Third Agenda Consultation in 2022, the IASB has at least put the development of specific accounting requirements for pollutant pricing mechanisms on a reserve list of projects that could be added to the work plan if additional capacity becomes available. Being aware that developing specific accounting requirements for pollutant pricing mechanisms would be complex and therefore likely to tie up a significant amount of the IASB's and, presumably, the ISSB's capacity for some time. This is nevertheless necessary, as clear, uniform and consistent accounting requirements are becoming increasingly important, particularly in view of the constantly evolving emissions trading market. We therefore suggest adding the project to the IASB's active agenda as soon as possible.

We would be pleased to answer any questions that you may have or discuss any aspect of this letter.

Yours sincerely,

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