Climate-related issues in IFRS financial statements

Skopje, North Macedonia

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Aims

» develop a more cohesive understanding of how climate-related risks are accounted for and reported in IFRS financial statements

» enhance capacity to make/audit/regulate the judgements in applying IFRS Accounting Standards with regard to climate-related matters

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Outline

- IFRS financial statements: pre-existing climate reporting
- IASB's climate-related projects
- Emissions trading schemes case study
- IFRS connectivity issues
- IAG climate connectivity case study
- Useful sources of information

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IFRS financial statements: pre-existing climate-related reporting

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Regulatory observations Example: FRC (UK) 2023

- **Considerable variation** in the quality of companies' disclosures of how climate change targets have been taken into account in the preparation of their financial statements disclosures.
- Mixed practice in our routine correspondence with companies in respect of connectivity between climate-related information included in narrative reporting and financial statements disclosures.
- **Written to 16 companies** during 2022-23, either to:
  - **seek more information** about how climate change has been considered in their financial statements; or
  - to **highlight areas** where we believe that disclosures could be improved.

Source: FRC (UK) CRR Thematic review of climate-related metrics and targets (July 2023), p8 (**emphasis** added)

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IFRS Accounting Standards

Overarching disclosures climate reporting considerations include…

» Although IFRS does not refer explicitly to climate-related matters, IAS 1's overarching disclosure requirements could be relevant when considering climate-related matters. For example, must disclose climate-related information when:

- » climate-related matters cast significant doubt on the entity's ability to continue as a **going concern** or significant judgement is required in reaching the conclusion climate-related matters do not cast **significant doubt** on the entity's ability to continue as a going concern. (IAS 1.25 and 26)
- » climate-related information is **relevant to an understanding** of any of the financial statements. (IAS 1.112)
- » compliance with the **specific requirements in IFRS Accounting Standards is insufficient** to enable investors to **understand** the impact of particular transactions, other events and conditions on the company's financial position and financial performance. (IAS 1.31)
- » information about how management has considered climate-related matters in preparing a company's financial statements may be material with respect to the **most significant judgements and estimates** that management has made. (IAS 1.122 and 125)

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IFRS Accounting Standards

Non-financial items climate reporting considerations include…

» Relevant climate-related matters must be considered when:

- » determining when an **environmental obligation** is incurred (ie **liability existence**)
- » determining when an environmental obligation first satisfies the **recognition** criteria
- » **measuring** an environmental obligation (eg, environmental restoration liability)
- » **measuring depreciation** (for example, estimating useful life and residual values)
- » **impairment testing** inventory, PPE, intangibles, goodwill etc
- » identifying model inputs for **measuring fair value** (particularly at Level 3)
- » identifying **onerous executory contracts** and measuring their **onerousness**
- » determining and applying an accounting policy for **emissions trading schemes.**

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IFRS Accounting Standards
Financial instruments climate reporting considerations include…

- **Classification and measurement:** climate-related contractual cash flows (eg, when affected by attaining climate targets could be relevant to:
  - **Lender's** SPPI test (IFRS 9); and
  - **Borrower's** determination of whether to bifurcate a climate derivative (IAS 32 and IFRS 9).
- **Impairment:** climate-related matters could be relevant to measuring expected credit losses (for example, modelling for the effects of environmental disasters, regulatory changes etc) (IFRS 9)
- **Disclosure:** climate-related matters could be relevant to financial instrument risk disclosures including ECL effects and concentrations of credit risk. (IFRS 7)

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IFRS Accounting Standards
Insurance contracts climate reporting considerations include…

- Relevant climate-related matters affect the **measurement** of insurance contract liabilities.
- **Disclosures** about climate-related assumptions (and judgements) and changes in assumptions in measuring insurance liabilities and the associated risk disclosures (including **exposure, risk management** and **sensitivity analysis**).

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Connectivity between IFRS Accounting Standards and IFRS Sustainability Disclosure Standards

- The ISSB and the IASB **function under the IFRS Foundation** to achieve connectivity between IFRS Accounting Standards and IFRS Sustainability Disclosure Standards.
- How best to reflect connectivity linkages?
  - **December 2022:** ISSB tentatively propose joint ISSB-IASB project on IASB's Management Discussion material and ISSB's Integrated Reporting Framework.
  - **September 2023:** comment deadline ISSB's Request for Information *Consultation on Agenda Priorities*
  - **January 2024:** IASB-ISSB joint meeting

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IASB's climate-related risk project/s

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IASB project climate-related and other uncertainties in financial statements

- **Objective** = targeted improvements to reporting of climate-related and other uncertainties in financial statements.
- IASB project team includes ISSB staff (**connectivity**)
- **Actions** taking include:
  - ED IFRS Accounting Standards *Climate-related and Other Uncertainties in the Financial Statements Proposed illustrative examples (issued 07/2024)*
  - Refer to IFRIC the question on applying IAS 37 to climate commitments
  - Extending examples, for example, in Practice Statement 2 *Making Materiality Judgements* to include climate-related examples and education materials on IAS 1's overarching disclosure requirements.
  - Clarifying or amending estimation uncertainty disclosures.

Sources include: Agenda reference 14 IASB meeting December 2023 www.ifrs.org/content/dam/ifrs/meetings/2023/december/iasb/ap14-project-update.pdf (accessed on 19/12/2023)

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IASB project climate-related and other uncertainties in financial statements

- **Actions/potential actions** continued:
  - Consult with IFRIC implications for IAS 36 *Impairment of Assets*
  - IFRS 18 strengthens aggregation/disaggregation requirements
  - Amendments to IAS 32 for ESG linked features
  - Power purchase agreements for renewable energy
  - Article on the role of financial statements (and connectivity with sustainability disclosures)
  - Improved accessibility of education materials

Sources include: Agenda reference 14 IASB meeting December 2023 www.ifrs.org/content/dam/ifrs/meetings/2023/december/iasb/ap14-project-update.pdf (accessed on 19/12/2023)

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Emissions trading schemes case study

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European Union Emissions Trading Scheme (EU ETS)

» The EU ETS works on the ‘cap and trade’ principle.

» A cap is set on the total amount of certain GHGs that can be emitted by installations covered by the system. The cap is reduced over time so that total emissions fall.

» Within the cap, companies receive or buy emission allowances which they can trade with one another as needed. They can also buy limited amounts of international credits from emission-saving projects around the world. The limit on the total number of allowances available ensures that they have a value.

» After each year a company must surrender enough allowances to cover all its emissions, otherwise heavy fines are imposed. If a company reduces its emissions, it can keep the spare allowances to cover its future needs or else sell them to another company that is short of allowances.

» Trading brings flexibility that ensures emissions are cut where it costs least to do so. A robust carbon price also promotes investment in clean, low-carbon technologies.

Sources include: http://ec.europa.eu/clima/policies/ets/index_en.htm search performed on 27/09/ 2016)

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IFRIC 3 *Emission Rights* withrdawn! IFRIC 3 specified that…

- allowances are an intangible asset.
- the issue of allowances free of charge by government is a government grant; accordingly, the allowances are initially recognised as an **intangible asset at fair value** and the corresponding entry is a deferred credit.
  - (The IFRIC decided to preclude entities from using the option in IAS 20 that would have allowed them to recognise the allowances issued at nominal amounts)
- during the year, as the entity emits CO_2, a liability is recognised for the obligation to deliver allowances at the end of the year to cover those emissions. This **liability is measured at the end of each reporting period by reference to the current market value of the allowances**.
- during the year, the entity **amortises the government grant** (deferred credit) to profit or loss.
- allowances are derecognised on their sale (if sold into the market) or on their delivery to the government in settlement of the entity's obligation to deliver allowances to cover emissions. **If the allowances are traded in an active market they are not amortised**.

Sources include: IASB (June 2010) www.ifrs.org/Current-Projects/IASB-Projects/Emission-Trading-Schemes/Documents/Background_historyETS.pdf; IASplus www.iasplus.com/en/binary/pressrel/0507withdrawifric3.pdf

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Post IFRIC 3 IASB project/s

- Since 2012 the IASB has discussed their on/off research project on emissions trading schemes.
- In the meantime, those applying IFRS Accounting Standards must use their judgement in developing and applying an accounting policy that results in relevant information that is, among other things, represent faithfully the financial position of the entity.
- To the extent necessary, applying paragraph 10 to 12 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors.*

Sources include: www.ifrs.org/projects/pipeline-projects/

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Post IFRIC 3
IFRS Practice

- » 5% of the respondents apply the **IFRIC 3 approach**, as described above.
- » 15% measure the **granted allowances initially at fair value** (**some subsequently** remeasured those rights, others did not), with any **obligation for emissions:**
  - » measured with reference to the **carrying amount of allowances on hand**.
  - » Any additional obligation is then valued at **market prices** and or **contracted prices**.
- » 5% measure the **granted allowances at nil value** with the **full obligation recognised at market value.**
- » 60% recognise **granted allowances at nil value.** The most common approach for valuing the obligation is to value it based on the carrying value of allowances on hand. Any additional obligation is then valued at market prices and or contracted prices.
- » 15% use **other approaches**.

Sources include: *Trouble-Entry Accounting – Revisited: Uncertainty in accounting for the EU Emissions Trading Scheme and Certified Emission Reductions* (see www.ieta.org/resources/Resources/Reports/trouble_entry_accounting.pdf) 19

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Mini-case study 1: zero-emission vehicle manufacturer (ZEVM)

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Emissions trading schemes case study
Mini-case study 1: zero-emission vehicle manufacturer (ZEVM)

Californian ZEV credits

» Californian law provides that a manufacturer of zero-emission vehicles may earn regulatory credits ("ZEV credits") and may sell excess credits to other manufacturers who apply such credits to comply with these regulatory requirements.

» Manufacturers of solely zero-emission vehicles, earn ZEV emission credits that they do not need to surrender to the authorities because they do not produce and sell internal combustion engine cars. Consequently, from time to time, they sell their ZEV credits to third-parties.

Mini-case study 1: zero-emission vehicle manufacturer (ZEVM)

Timeline

» **31/12/2020:** ZEVM's market capitalization increases from $50 billion to $55 billion, in response to Country (in which ZEVM manufactures its zero emission vehicles) unexpectedly introducing a ZEV credit scheme like that Tesla is subject to in California.

» **01/01/2021:**

- » Government of Country grants ZEVM 100,000 ZEV credits; and
- » ZEVM sells 50,000 ZEV credits at $10,000 each.

» **31/12/2021:** ZEVM observes that ZEV credits are actively trading at $15,000 each.

Mini-case study 1: zero-emission vehicle manufacturer (ZEVM)
Assumptions for answering questions 1-4 (the economics)

zero-emission vehicle manufacturer (ZEVM)

» ZEVM accounts for all of its assets **using the fair value model** (sometimes called 'mark to market' accounting); and

» Immediately before the introduction of the ZEV credit scheme:

  » ZEVM has no liabilities; and

  » ZEVM's market capitalization = $50 billion = the carrying amount (sometimes called 'book value') of its equity = the carrying amount of its assets.

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Mini-case study 1: zero-emission vehicle manufacturer
The economics
What do you think?

1) On 31/12/2020 what is the economic effect on ZEVM of the event: Country introducing the ZEV credit scheme? Choose one of:

	Financial Position				Financial Performance for 2020	
	Assets	**=**	**Liabilities**	**Equity**	**Income**	**Expense**
(a)	No effect		No effect	No effect	No effect	No effect
(b)	↓$5 billion			↓$5 billion		↑$5 billion
(c)	↑$5 billion			↑$5 billion		
(d)	↑$5 billion		↑$5 billion			
(e)	↑$5 billion			↑$5 billion	↑$5 billion	

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Mini-case study 1: zero-emission vehicle manufacturer
The economics
What do you think?

2) On 01/01/2021 what is the economic effect on ZEVM of the transaction: receiving 100,000 ZEV credits from Government of Country? Choose one of:

	Financial Position				Financial Performance for 2021	
	Assets	**=**	**Liabilities**	**Equity**	**Income**	**Expense**
(a)	No effect		No effect	No effect	No effect	No effect
(b)	↓$1 billion			↓$1 billion		↑$1 billion
(c)	↑$1 billion			↑$1 billion		
(d)	↑$1 billion		↑$1 billion			
(e)	↑$1 billion			↑$1 billion	↑$1 billion	

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Mini-case study 1: zero-emission vehicle manufacturer
The economics
What do you think?

3) On 01/01/2021 what is the economic effect on ZEVM of the transaction: ZEVM sells 50,000 of its ZEV credits? Choose one of:

	Financial Position				Financial Performance for 2021	
	Assets	**=**	**Liabilities**	**Equity**	**Income**	**Expense**
(a)	No effect		No effect	No effect	No effect	No effect
(b)	↑$0.5 billion ↓$0.5 billion					
(c)	↑$0.5 billion			↑$0.5 billion		
(d)	↑$0.5 billion		↑$0.5 billion			
(e)	↑$0.5 billion			↑$0.5 billion	↑$0.5 billion	

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Mini-case study 1: zero-emission vehicle manufacturer The economics What do you think?

4) On 31/12/2021 what is the economic effect on ZEVM of the event: observing ZEV credits actively trading at $15,000 each? Choose one of:

	Financial Position				Financial Performance 2021	
	Assets	**=**	**Liabilities**	**Equity**	**Income**	**Expense**
(a)	No effect		No effect	No effect	No effect	No effect
(b)	↑$0.25 billion ↓$0.25 billion					
(c)	↑$0.25 billion			↑$0.25 billion		
(d)	↑$0.25 billion		↑$0.25 billion			
(e)	↑$0.25 billion			↑$0.25 billion	↑$0.25 billion	

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Mini-case study 1: zero-emission vehicle manufacturer (ZEVM)

Assumptions for answering questions 5-9 (the accounting)

zero-emission vehicle manufacturer (ZEVM)

» immediately before the introduction of the ZEV scheme, the carrying amount (sometimes called ‘book value’) of ZEVM’s equity = assets = $5 billion (and ZEVM has no liabilities).

» ZEVM accounts for its ZEV certificates at their **historical cost** (ie nil from when granted until derecognized when sold).

» ZEVM accounts for its other assets (for example, its intangible assets and factories) using the **cost model** (ie historical cost less depreciation and impairment, if any).

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Mini-case study 1: zero-emission vehicle manufacturer
The cost model accounting
What do you think?

5) What would ZEVM's accounting, if any, be on 31/12/2020 for the event: Country introducing the ZEV credit scheme? Choose one of:

	Financial Position				Financial Performance 2020	
	Assets	**=**	**Liabilities**	**Equity**	**Income**	**Expense**
(a)	No effect		No effect	No effect	No effect	No effect
(b)	↓$5 billion			↓$5 billion		↑$5 billion
(c)	↑$5 billion			↑$5 billion		
(d)	↑$5 billion		↑$5 billion			
(e)	↑$5 billion			↑$5 billion	↑$5 billion	

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Mini-case study 1: zero-emission vehicle manufacturer
The cost model accounting
What do you think?

6) What would ZEVM's accounting, if any, be on 01/01/2021 for the transaction: receiving 100,000 ZEV credits from Government of

	Financial Position				Financial Performance 2021	
	Assets	**=**	**Liabilities**	**Equity**	**Income**	**Expense**
(a)	No effect		No effect	No effect	No effect	No effect
(b)	↓$1 billion			↓$1 billion		↑$1 billion
(c)	↑$1 billion			↑$1 billion		
(d)	↑$1 billion		↑$1 billion			
(e)	↑$1 billion			↑$1 billion	↑$1 billion	

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Mini-case study 1: zero-emission vehicle manufacturer
The cost model accounting
What do you think?

7) What would ZEVM's accounting, if any, be on 01/01/2021 for the transaction: ZEVM sells 50,000 of its ZEV credits? Country? Choose one of:

	Financial Position				Financial Performance 2021	
	Assets	**=**	**Liabilities**	**Equity**	**Income**	**Expense**
(a)	No effect		No effect	No effect	No effect	No effect
(b)	↑$0.5 billion ↓$0.5 billion					
(c)	↑$0.5 billion			↑$0.5 billion		
(d)	↑$0.5 billion		↑$0.5 billion			
(e)	↑$0.5 billion			↑$0.5 billion	↑$0.5 billion	

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Mini-case study 1: zero-emission vehicle manufacturer
The cost model accounting
What do you think?

8) What would ZEVM's accounting, if any, be on 31/12/2021 for the event: observing ZEV credits actively trading at $15,000 each? Choose one of:

	Financial Position				Financial Performance 2021	
	Assets	**=**	**Liabilities**	**Equity**	**Income**	**Expense**
(a)	No effect		No effect	No effect	No effect	No effect
(b)	↑$0.25 billion ↓$0.25 billion					
(c)	↑$0.25 billion			↑$0.25 billion		
(d)	↑$0.25 billion		↑$0.25 billion			
(e)	↑$0.25 billion			↑$0.25 billion	↑$0.25 billion	

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Mini-case study 1: zero-emission vehicle manufacturer The cost model accounting What do you think?

9) ZEVM's accounting for which of the following, if any, is consistent with the economics ? Choose one of:

(a) on 31/12/2020 the event: Country introducing the ZEV credit scheme;

(b) on 01/01/2021 the transaction: receiving 100,000 ZEV credits from Government of Country;

(c) on 01/01/2021 the transaction: ZEVM sells 50,000 of its ZEV credits;

(d) on 31/12/2021 the event: observing ZEV credits actively trading at $15,000 each;

(e) all of (a) - (d) above;

(f) (b) - (d) above; or

(g) none of (a) - (d) above.

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Mini-case study 1: zero-emission vehicle manufacturer (ZEVM) Assumptions for answering questions 10-14 (the accounting)

zero-emission vehicle manufacturer (ZEVM)

» immediately before the introduction of the ZEV scheme, the carrying amount (sometimes called 'book value') of ZEVM's equity = assets = $5 billion (and ZEVM has no liabilities).

» ZEVM accounts for its **ZEV certificates using the fair value model** (sometimes called 'mark to market' accounting).

» ZEVM accounts for its **other assets** (for example, its intangible assets and factories) using the **cost model** (ie historical cost less depreciation and impairment, if any).

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Mini-case study 1: zero-emission vehicle manufacturer Mixed measurement model accounting What do you think?

10) What would ZEVM's accounting, if any, be on 31/12/2020 for the event: Country introducing the ZEV credit scheme? Choose one of:

	Financial Position				Financial Performance for 2020	
	Assets	**=**	**Liabilities**	**Equity**	**Income**	**Expense**
(a)	No effect		No effect	No effect	No effect	No effect
(b)	↓$5 billion			↓$5 billion		↑$5 billion
(c)	↑$5 billion			↑$5 billion		
(d)	↑$5 billion		↑$5 billion			
(e)	↑$5 billion			↑$5 billion	↑$5 billion	

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Mini-case study 1: zero-emission vehicle manufacturer Mixed measurement model accounting What do you think?

11) What would ZEVM's accounting, if any, be on 01/01/2021 for the transaction: receiving 100,000 ZEV credits from Government of Country? Choose one of:

	Financial Position				Financial Performance for 2021	
	Assets	**=**	**Liabilities**	**Equity**	**Income**	**Expense**
(a)	No effect		No effect	No effect	No effect	No effect
(b)	↓$1 billion			↓$1 billion		↑$1 billion
(c)	↑$1 billion			↑$1 billion		
(d)	↑$1 billion		↑$1 billion			
(e)	↑$1 billion			↑$1 billion	↑$1 billion	

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Mini-case study 1: zero-emission vehicle manufacturer
Mixed measurement model accounting
What do you think?

12) What would ZEVM's accounting, if any, be on 01/01/2021 for the transaction: ZEVM sells 50,000 of its ZEV credits? Choose one of:

	Financial Position				Financial Performance for 2021	
	Assets	**=**	**Liabilities**	**Equity**	**Income**	**Expense**
(a)	No effect		No effect	No effect	No effect	No effect
(b)	↑$0.5 billion ↓$0.5 billion					
(c)	↑$0.5 billion			↑$0.5 billion		
(d)	↑$0.5 billion		↑$0.5 billion			
(e)	↑$0.5 billion			↑$0.5 billion	↑$0.5 billion	

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Mini-case study 1: zero-emission vehicle manufacturer
Mixed measurement model accounting
What do you think?

13) What would ZEVM's accounting, if any, be on 31/12/2021 for the event: observing ZEV credits actively trading at $15,000 each? Choose one of:

	Financial Position				Financial Performance 2021	
	Assets	**=**	**Liabilities**	**Equity**	**Income**	**Expense**
(a)	No effect		No effect	No effect	No effect	No effect
(b)	↑$0.25 billion ↓$0.25 billion					
(c)	↑$0.25 billion			↑$0.25 billion		
(d)	↑$0.25 billion		↑$0.25 billion			
(e)	↑$0.25 billion			↑$0.25 billion	↑$0.25 billion	

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Mini-case study 1: zero-emission vehicle manufacturer
Mixed measurement model accounting
What do you think?

14) ZEVM's accounting for which of the following, if any, is consistent with the economics? Choose one of:

(a)on 31/12/2020 the event: Country introducing the ZEV credit scheme;

(b)on 01/01/2021 the transaction: receiving 100,000 ZEV credits from Government of Country;

(c)on 01/01/2021 the transaction: ZEVM sells 50,000 of its ZEV credits;

(d)on 31/12/2021 the event: observing ZEV credits actively trading at $15,000 each;

(e)all of (a) - (d) above;

(f) (b) - (d) above; or

(g)none of (a) - (d) above.

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Mini-case study 2: Heavy GHG emitter

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Mini-case study 2: Heavy GHG emitter
Summary of emissions trading scheme, and transactions & events

» **Event 1:** Government imposes a cap and trade emissions trading scheme (similar schemes are not imposed on the entity's competitors whose operations are located other jurisdictions). Entity's market capitalisation falls from $40 million to $35 million. Any entity emitting more carbon than it has certificates for will incur harsh penalties.

» **Transaction 1:** Entity pays $4 million to buy 1,000 tradable emissions certificates to cover its expected carbon emissions.

» **Event 2:** Government issues Entity 1,000 certificates to emit a specified quantity of carbon over 3 years.

» **Event 3:** Entity's pollution Y1 = 500 certificates.

» **Event 4:** Fair value of certificates doubles.

Mini-case study 2: Heavy GHG emitter
Event 1: Government imposes restrictions on emissions
What do you think?

Economics: competitiveness of entity relative to its peers in other jurisdictions declines (as its operating costs increase). Consequently, the entity's market capitalisation falls

- » before: net assets $40 million = equity $40 million
- » restrictions: asset ↓$5 million and equity (market cap) ↓$5 million
- » after: net assets $35 million = equity $35 million

Accounting: before: net assets $20 million = equity $20 million

How much are net assets/equity after? Choose one of: 1) $35 million; 2) $20 million; or 3) $15 million.

Mini-case study 2: Heavy GHG emitter
Transaction: entity pays $4 million to buy 1,000 tradable emissions certificates

Economics: exchange of assets (pay cash receive ETS certificates)

» before purchase: net assets $35 million = equity $35 million

» purchase: asset cash ↓$4 million and asset ETS certificates ↑$4 million

» after purchase: net assets $35 million = equity $35 million

Accounting: before purchase: net assets $20 million = equity $20 million.

» **How much are net assets/equity after?** Choose one of: 1) $35 million; 2) $20 million; 3) $16 million; or 4) $15 million.

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IFRS connectivity issues

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Connectivity
regulatory expectations example (1)

» FRC (UK) expects preparers to consider the connectivity between TCFD disclosures and the financial statements, and explain where necessary, including whether:

- » the **emphasis placed on climate change risks and uncertainties in narrative reporting**, including TCFD disclosures**,** **is consistent with the disclosure of this impact of those uncertainties on judgements and estimates in the financial statements**;
- » the **relationships between assumptions and sensitivities** considered in TCFD scenarios, and those in the financial statements, is clear;

Source: FRC (UK), Appendix 2–Detailed FRC expectations–Key expectations for good reporting of climate in the financial statements, CRR Thematic review of TCFD disclosures and climate in the financial statements, 2022 (p128) (**emphasis** added)

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Connectivity
regulatory expectations example (2)

» FRC (UK) expects (continued):

- » **emissions reduction commitments and strategies** are appropriately reflected in the financial statements;
- » the scale of growth of businesses and climate-related opportunities is consistent between narrative and segmental disclosures;
- » the time periods disclosed for TCFD reporting are consistent with the going concern [and viability statements]; and
- » **discussion of matters** that may have an adverse effect on asset values or useful lives in the narrative reporting is consistent with judgements in the financial statements, for example, that there are no indicators of impairment.

Source: FRC (UK), Appendix 2–Detailed FRC expectations–Key expectations for good reporting of climate in the financial statements, CRR Thematic review of TCFD disclosures and climate in the financial statements, 2022 (p128) (**emphasis** added)

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Connectivity between IFRS-S and IFRS-A
Accessibility

Time	Reporting period	Location
At the same time as annual report **Transition relief** on timing of 1st annual report	For the same reporting period as annual report	Can be separate Clearly identifiable not obscured X-referenced to a specified place Identify related financial statements

Sources: paragraphs 60-69 and E4 of IFRS S1

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Connectivity between IFRS-S and IFRS-A
Specific required disclosures

Same
- Reporting entity
- Materiality
- Primary users

To extent possible:
- Use **data and assumptions in SrFD** that are **consistent with** data, assumptions and units of measure used for **financial statements**
- Use **entity's financial statements presentation currency** in making its **currency metric sustainability disclosures**

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Connectivity between IFRS-S and IFRS-A

» **Avoid cluttering** financial information with unnecessary duplication and immaterial information

» Must **disclose information about significant disconnects** in its financial information

  » For example, when significant differences exist between data and assumptions used in preparing its sustainability-related financial disclosures and its related financial statements

Source: paragraph B42 of IFRS S1

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Connectivity between IFRS-S and IFRS-A
Example 1 development and manufacture of new product
What do you think?

» From Entity's sustainability-related financial disclosures you observe that Entity has developed, and in Q3 2024 began the commercial production of, a new more climate-sensitive product which it has identified as a major sustainability-related opportunity (SrO) that it has pursued.

» **In light of the information above, what accounting (recognition and measurement) and disclosures, (if any), do you expect to see in Entity's 31/12/2024 annual financial statements?** Choose **one or more** of: 1) research expense; 2) capitalization of development costs; 3) capital commitment disclosures; 4) amortisation of development costs; 5) revenue from the sale of goods; 5) cost of sales expense.

Sources: paragraphs B40 and B41 of IFRS S1

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Connectivity between IFRS-S and IFRS-A
Example 2 transition risk—decreasing demand for products

- From Entity's 2024 sustainability-related financial disclosures you observe:
  - Entity is facing **decreasing demand for its products because of consumer preferences are shifting to lower-carbon alternatives.**
  - Entity's strategic response deciding to close a major factory.

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Connectivity between IFRS-S and IFRS-A
Example 2 transition risk—decreasing demand for products
What do you think?

What accounting (recognition and measurement) and disclosures, (if any), do you expect to see in Entity's 31/12/2024 annual financial statements?

Choose **one or more** of:

1) reclassification of affected assets to non-current assets held for sale (if IFRS 5 criteria met);
2) termination benefits employee benefits liability (if criteria met);
3) change in depreciation estimates—useful life, depreciation method, residual value (if IFRS 5 criteria not met);
4) impairment of factory assets expense and disclosures (if IFRS 5 criteria not met);
5) profit or loss on sale of factory (if factory sold).

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Connectivity between IFRS-S and IFRS-A
Example 3: Associate's GHG emissions

» From Entity's 2024 sustainability-related financial disclosures you observe:
  » Entity has a **30% equity interest in Associate;**
  » Associate's main asset is its **owner-operated factory;**
  » **Entity's Scope 2 GHG emissions** includes 30% of Associate's GHG emissions (ie using the equity share approach);

Source: IFRS S2.B27 and BC101 and BC102

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Connectivity between IFRS-S and IFRS-A
Example 3: Associate's GHG emissions
What do you think?

How would Entity account for its associate in its 2024 consolidated balance sheet? Choose one of:

1) Equity method accounting for the investment asset (external to consolidated Entity);
2) Proportionate consolidation, ie 30% of Associate's factory asset;
3) Consolidation, ie 100% of Associate's factory asset and non-controlling interest equity.

Source: IFRS S2.B27 and BC101 and BC102

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Connectivity between IFRS-S and IFRS-A
ED Example 6: Disclosure about climate-related credit risk (1)

» Bank's **credit risk management practices** include **considering climate-related risk effects**.

» Bank **identifies two portfolios** of loans that require it to monitor and take action to mitigate credit risk arising from its customers' exposure to climate-related risks:

   » loans to **agricultural customers** for which climate-related events such as droughts could affect the borrowers' ability to repay their loans; and

   » loans to **corporate real estate** customers that are secured by properties located in low-lying areas subject to flood risk.

Source: ED IFRS Accounting Standards *Climate-related and Other Uncertainties in the Financial Statements Proposed illustrative examples (07/2024)* 78

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Connectivity between IFRS-S and IFRS-A
ED Example 6: Disclosure about climate-related credit risk (2)

» Bank determines that information about the effects of climate-related risks on its **exposure to credit risk** on those two portfolios **is material** on the basis of the following factors:

   » the size of the portfolios affected by climate-related risks relative to bank's overall lending portfolio.

   » the significance of the effects of climate-related risks on bank's exposure to credit risk compared to other factors affecting that exposure. The effects depend on factors such as loan maturities and the nature, likelihood and magnitude of the climate-related risks.

   » external climate-related qualitative factors—such as climate-related market, economic, regulatory and legal developments—that make the information more likely to influence decisions primary users of the entity's financial statements make on the basis of the financial statements.

Source: ED IFRS Accounting Standards *Climate-related and Other Uncertainties in the Financial Statements Proposed illustrative examples (07/2024)* 79

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Connectivity between IFRS-S and IFRS-A
ED Example 6: Disclosure about climate-related credit risk (3)
What do you think?

» How, in accordance with IFRS 7.35A–38, might Bank disclose:

1. information about the effects of particular risks on its credit risk exposures and credit risk management practices? and
2. information about how these practices relate to the recognition and measurement of expected credit losses?

Source: ED IFRS Accounting Standards *Climate-related and Other Uncertainties in the Financial Statements Proposed illustrative examples (07/2024)*

IFRS connectivity mini-case study 1
sustainability disclosures

“We are introducing **10 fuel bulk carriers, … to our roster of vessels, with the first vessel delivered in December 2022 – the remaining vessels are expected to be delivered by mid-2024.** They offer significant environmental benefits, having the potential to cut CO_2 emissions by up to 35% compared with vessels fuelled by conventional marine oil alone, while adoption of new technologies will eliminate the release of unburnt methane, as well as removing sulphur oxides, and reducing the volume of nitrogen oxides and particulate matter.”

*What aspects of its **financial statements** do you expect could be materiality impacted by the sustainability matter disclosed (and why)?*

Source: UKEB A Study in Connectivity: Analysis of 2022 UK Company Annual Reports, September 2023 (p15)

IFRS connectivity mini-case study 2
GHG emissions reduction commitments (1)

» In December 20X0 Entity, a manufacturer of household products, publicly states a commitment:
  » to reduce its GHG emissions by at least 60% by 20X9;
  » To offset its remaining emissions **in 20X9 and thereafter**, by buying carbon credits and retiring them from the carbon market.

Source: November 2023 IFRIC meeting Agenda reference 2 (see www.ifrs.org/content/dam/ifrs/meetings/2023/november/ifric/ap02-climate-related-commitments-initial-consideration-ias-37.pdf

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IFRS connectivity mini-case study 2
GHG emissions reduction commitments (2)

» With its statement, the entity publishes a detailed plan setting out how it will gradually modify its manufacturing methods between 20X1 and 20X9 to achieve the 60% reduction in its GHG emissions by 20X9. The modifications will involve:
  » investing in more energy-efficient processes;
  » buying energy from renewable sources; and
  » replacing existing petroleum-based product ingredients and packaging materials with lower-carbon alternatives.

» Management is confident that the entity can make all these modifications and continue to sell its products at a profit.

Source: November 2023 IFRIC meeting Agenda reference 2 (see www.ifrs.org/content/dam/ifrs/meetings/2023/november/ifric/ap02-climate-related-commitments-initial-consideration-ias-37.pdf

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IFRS connectivity mini-case study 2
GHG emissions reduction commitments (3)
What do you think?

- At 31/12/20X0 does Entity have a provision liability? Choose one of: 1) Yes; or 2) No.
- At 31/12/20X0 what aspects of its financial statements do you expect could be materiality impacted by the manufacturer's GHG emissions reduction commitments (and why)?

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IFRS connectivity mini-case study 2
GHG emissions reduction commitments (4)
What do you think?

- At 31/12/20X9 does Entity likely have a provision liability? Choose one of: 1) Yes; or 2) No.
- What aspects of its financial statements do you expect could be materiality impacted by the manufacturer's GHG emissions reduction commitments (and why)?

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IAG climate connectivity case study

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IAG climate connectivity case study
Generic/foundational connectivity questions
What do you think?

1) **Is the reporting entity the same for IFRS financial statements and IFRS sustainability disclosures?** Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study
Generic/foundational connectivity questions
What do you think?

2) **Are IFRS financial statements and the IFRS sustainability disclosures focussed on the same users' needs?** Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study
Generic/foundational connectivity questions
What do you think?

3) **Is the same materiality concept used for IFRS financial statements and IFRS sustainability disclosures?** Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study
Generic/foundational connectivity questions
What do you think?

4) **Must a reporting entity's IFRS financial statements and its IFRS sustainability disclosures cover the same reporting period (ie coterminous reporting period)?** Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study
Generic/foundational connectivity questions
What do you think?

5) **Must a reporting entity's IFRS financial statements and its IFRS sustainability disclosures be published at the same time (ie the same publication date)?** Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study
Generic/foundational connectivity questions
What do you think?

6) **Must a reporting entity's IFRS financial statements and its IFRS sustainability disclosures be prepared using the same data, assumptions and units of measure?** Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study
Generic/foundational connectivity questions
What do you think?

7) **Whose eyes must IAG's management look through when making the relevance judgements in preparing IAG's IFRS financial statements?**
   a) Management's eyes;
   b) Auditor's eyes;
   c) Regulators' eyes;
   d) General public's eyes;
   e) Competitors' eyes; or
   f) Existing and potential investors', lenders' and creditors' eyes.

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IAG climate connectivity case study
Generic/foundational connectivity questions
What do you think?

8) Whose eyes must management look through when making the relevance judgements in preparing IFRS climate-related financial disclosures? Choose one of:

a) Management's eyes;
b) Auditor's eyes;
c) Regulators' eyes;
d) General public's eyes;
e) Competitors' eyes; or
f) Existing and potential investors', lenders' and creditors' eyes.

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IAG climate connectivity case study
Generic/foundational connectivity questions
What do you think?

9) Whose eyes must a regulator look through when assessing the relevance judgements management made in preparing IFRS financial statements? Choose one of:

a) Management's eyes;
b) Auditor's eyes;
c) Regulators' eyes;
d) General public's eyes;
e) Competitors' eyes; or
f) Existing and potential investors', lenders' and creditors' eyes.

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IAG climate connectivity case study
Generic/foundational connectivity questions
What do you think?

10)Whose eyes must a regulator look through when assessing the relevance judgements management made in preparing IFRS climate-related financial disclosures?

a) Management's eyes;
b) Auditor's eyes;
c) Regulators' eyes;
d) General public's eyes;
e) Competitors' eyes; or
f) Existing and potential investors', lenders' and creditors' eyes.

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IAG climate and connectivity case study
connectivity expectation-related questions
What do you think?

On the basis of IAG's climate-related disclosures, what aspects of its consolidated financial statements do you expect to be materiality impacted by climate-related matters (and why)?

11)Which assets and liabilities? Choose one or more of: 1) IAS 16; 2) IAS 19; 3) IAS 20; 4) IAS 36; 5) IAS 37; 6) IAS 38; 7) IFRS 5.

12)Which aspects of financial performance?

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IAG climate and connectivity case study connectivity expectation-related questions What do you think?

On the basis of IAG's climate-related disclosures, what aspects of its consolidated financial statements do you expect to be materiality impacted by climate-related matters (and why)?

13) Any unrecognised contractual commitments (for example, paragraph 114(c)(iv) of IAS 1; paragraph 74(c) of IAS 16; and paragraph 122(e) of IAS 38)? Choose one of 1) Yes; or 2) No.

14) Any contingent liabilities (IAS 37)? Choose one of 1) Yes; or 2) No.

18) **Any other overarching disclosures (for example, paragraphs 31 and 112 of IAS 1)?** Choose one of 1) Yes; or 2) No.

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IAG climate and connectivity case study connectivity expectation-related questions What do you think?

13)Any unrecognised contractual commitments (for example, paragraph 114(c)(iv) of IAS 1; paragraph 74(c) of IAS 16; and paragraph 122(e) of IAS 38)? Choose one of: 1) Yes; or 2) No.

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IAG climate and connectivity case study connectivity expectation-related questions What do you think?

14) **Any contingent liabilities (IAS 37)?** Choose one of: 1) Yes; or 2) No.

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IAG climate and connectivity case study connectivity expectation-related questions What do you think?

18) **Any other overarching disclosures (for example, paragraphs 31 and 112 of IAS 1)?** Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study connectivity expectation-related questions What do you think?

On the basis of IAG's climate-related disclosures, what aspects of its consolidated financial statements do you expect to be materiality impacted by climate-related matters (and why)?

15)Any key sources of estimation uncertainty (paragraphs 122-124 of IAS 1)? Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study connectivity expectation-related questions What do you think?

On the basis of IAG's climate-related disclosures, what aspects of its consolidated financial statements do you expect to be materiality impacted by climate-related matters (and why)?

16)Any change in an accounting estimate (paragraph 39 of IAS 8)? Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study connectivity expectation-related questions What do you think?

On the basis of IAG's climate-related disclosures, what aspects of its consolidated financial statements do you expect to be materiality impacted by climate-related matters (and why)?

17)Any other significant judgements (paragraphs 122-124 of IAS 1)? Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study connectivity questions What do you think?

24)Is the reporting entity the same for IAG's 2022 sustainability disclosures in the front end of its 2022 Annual Report and its 2022 consolidated IFRS financial statements? Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study connectivity questions What do you think?

25) Do IAG's TCFD disclosures identify the financial statements to which the climate-related financial disclosures relate? Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study connectivity questions What do you think?

26) Are IAG's 2022 consolidated IFRS financial statements and the sustainability disclosures in the front end of its 2022 Annual Report focussed on the same users' needs? Choose one of: 1) Yes; or 2) No

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IAG climate connectivity case study connectivity questions What do you think?

27)Does IAG use the same materiality concept in its 2022 consolidated IFRS financial statements and climate-related financial disclosures in the front end of its 2022 Annual Report? Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study connectivity questions What do you think?

28)Do IAG's 2022 consolidated IFRS financial statements and its climate-related financial disclosures in the front end of its 2022 Annual Report cover the same reporting period (ie coterminous reporting period)? Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study
connectivity questions
What do you think?

29) Were IAG's 2022 consolidated IFRS financial statements and the sustainability disclosures in the front end of its 2022 Annual Report made publicly available at the same time? Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study
connectivity questions
What do you think?

30) To the extent possible, are IAG's 2022 consolidated IFRS financial statements and its climate-related financial disclosures prepared using the same data, assumptions and units of measure? Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study connectivity questions What do you think?

31) Does IAG disclose information about significant disconnects, if any, in its climate-related financial information (for example, TCFD and financial statements)? Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study connectivity questions What do you think?

32) Are clear and concise linkages that enable primary users to understand the connections between IAG's financial statements and its climate-related financial disclosures? Choose one of: 1) Yes; or 2) No.

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IAG climate connectivity case study connectivity questions What do you think?

33)**Does IAG use its consolidated financial statement presentation currency in making its currency metric climate-related disclosures?** Choose one of: 1) Yes; or 2) No.

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Useful sources of information

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Questions?

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