

5 February 2024

Bruce Mackenzie  
Chair  
IFRS Interpretations Committee

Columbus Building  
7 Westferry Circus  
Canary Wharf  
London, E14 4HD  
United Kingdom

Dear Mr Mackenzie

## **Tentative agenda decision – Climate-related Commitments (IAS 37)**

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretations Committee's publication in the November 2023 *IFRIC Update* of the tentative agenda decision not to take onto the Committee's agenda the request about an entity's commitment to reduce or offset its greenhouse gas emissions.

We agree with the analysis of the issue presented in the tentative agenda decision and with the Committee's decision not to add this item onto its agenda for the reasons set out in the tentative agenda decision.

We support the efforts of the Committee to set out the analysis required to assess whether an entity's "net zero" commitment gives rise to a provision that should be recognised in the entity's financial statements, noting that this is an area that has caught the attention of a broad group of stakeholders, beyond traditional users of financial statements. We believe that this heightens the need for a clear and comprehensive explanation of the relevant principles and specific guidance of IAS 37 and, to that end, have suggested amendments to the agenda decision in the Appendix to this letter.

This issue highlights the need for connectivity between broader corporate reporting (including sustainability reporting) and information in the financial statements to, in this case, provide clarity for the broad range of interested stakeholders on whether statements made as part of a sustainability report do, or validly do not, affect the recognition and measurement of items in the financial statements. We urge the International Accounting Standards Board (the IASB) to accelerate its project on climate-related and other uncertainties in financial statements and, in collaboration with the International Sustainability Standards Board, to focus on the interaction between those disclosures and the information provided by sustainability reporting.

We also take this opportunity to reiterate the view expressed in our response to response to the IASB's request for information *Third Agenda Consultation* that a project should be undertaken to address issues related to pollutant pricing mechanisms together with cryptocurrencies and commodity transactions. We regret that the IASB's project on pollutant pricing mechanisms has been relegated to the reserve list and observe that a lack of clarity on how to account for carbon credits and similar instruments has resulted in diversity in practice. This diversity is likely to increase as more and more entities participate in carbon

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credit programs as part of their net zero commitments. We strongly believe that the IASB should reconsider the level of priority afforded to this project.

If you have any questions concerning our response, please contact Veronica Poole in London at +44 (0)20 7007 0884.

Yours sincerely

A handwritten signature in black ink, appearing to read 'V. Poole', with a stylized flourish at the end.

**Veronica Poole**  
Global IFRS and Corporate Reporting Leader

## Appendix – Suggested amendments to the technical analysis provided in the TAD

We have organised our suggestions by reference to the headers used in the TAD.

### Does the entity have a constructive obligation?

The Committee observed that whether an entity's statement of its commitment to reduce or offset its emissions creates a constructive obligation depends on facts and circumstances, and management needs to apply judgement to reach a conclusion. We believe there is further guidance in IAS 37 that should be referred to in the agenda decision to explain the factors management may consider in making this judgement.

*Paragraph 20 of IAS 37 notes that in order for a commitment to give rise to a constructive obligation, the commitment should be communicated in a sufficiently specific manner to raise a valid expectation in the party to whom the obligation is owed that the entity will discharge its responsibilities. The Committee further observed that whether an entity's statement of its commitment to reduce or offset its emissions creates a valid expectation that it will fulfil its commitment—and hence creates a constructive obligation—depends on the facts of the commitment and the circumstances surrounding it. Management would apply judgement to reach a conclusion considering those facts and circumstances.*

We also propose a further clarification to support the conclusion that the fact that the obligation extends to the public at large does not prevent a constructive obligation existing based on paragraph 20 of IAS 37.

*The Committee observed that a constructive obligation to reduce or offset greenhouse gas emissions, if one exists, would be owed to all people adversely affected by the emissions so would extend to the public at large. In accordance with paragraph 20 of IAS 37, it is not necessary to know the identity of the party to whom the obligation is owed in order for a constructive obligation to exist and as such the obligation may be to the public at large.*

### Does the constructive obligation satisfy the criteria for recognising a provision?

We note that the agenda decision correctly indicates that an entity recognises a provision only if all three of the criteria in paragraph 14 of IAS 37 are met. We also note that the analysis that follows considers all three criteria despite the fact that this is not strictly required as the first criteria (present obligation as a result of a past event) is not met. Hence, it may be appropriate to highlight this fact.

#### Present obligation as a result of a past event

A clearer context to the discussion in this section would be provided by including a reminder of the requirements in paragraph 17 of IAS 37.

*The Committee observed that, just as an entity has a present legal obligation only when it has taken the action to which a law applies, it has a present constructive obligation only when it has taken the action to which its published policy or statement applies. For example, as illustrated in Illustrative Example 2B accompanying IAS 37, an entity with a widely published policy of cleaning up land it contaminates incurs a present obligation only when it contaminates land—publishing the policy is necessary but not sufficient.*

*As noted in paragraphs 17 and 19 of IAS 37, a past event gives rise to an obligation when that entity has no realistic alternative but to settle the obligation. In explaining the requirement for a present obligation, paragraph 18 of IAS 37 states that 'no provision is recognised for costs that need to be incurred to operate in the future' and 'it is only those obligations arising from past events existing independently of the entity's future actions (ie the future conduct of its business) that are*

recognised as provisions'. Accordingly, as stated in paragraph 18 of IAS 37, 'no provision is recognised for costs that need to be incurred to operate in the future'.

The value of the tentative agenda decision would also be enhanced by an explanation of the circumstances in which a provision *would* arise in respect of commitments to change an entity's operations, namely being party to onerous contracts or having committed to a detailed formal restructuring plan including the costs of exiting current operations (rather than of developing new, lower carbon, alternatives).

In addition, we note that the fact pattern presented in the tentative agenda decision contemplates a narrow range of actions that the entity expects to undertake as part of its net zero commitment. In practice, such commitments may encompass a wider range of activities requiring the entity to consider other aspects of IAS 37. For these reasons, we suggest the following amendments to the text of the agenda decision.

*(b) the entity ~~will never~~ does not have a present obligation for future modifications to its manufacturing methods as described in the fact pattern because the costs of those modifications ~~will always be~~ are costs incurred to operate in the future. The entity will at some point have to pay for resources it purchases to modify its manufacturing methods—for example, to pay for new plant or equipment—but only when it receives those resources. Prior to that, a purchase commitment gives rise to a provision only if the contract is onerous applying paragraphs of 68A of IAS 37.*

*In addition, the Committee observed that the modification of the manufacturing methods may involve a restructuring of the entity's existing operations. An entity would apply the requirements in paragraphs 70-83 of IAS 37 to determine if a provision for restructuring costs should be recognised.*

#### Probable outflow of resources

The Committee concluded that settling the obligation to reduce the entity's greenhouse gas emissions will not require an outflow of resources embodying economic benefits because although the entity will incur expenditure to modify its manufacturing methods, it will receive other resources in exchange for that expenditure. We believe the analysis should be drafted in a manner that highlights how to apply the principle rather than firmly conclude on whether the criteria are met.

*(a) settling the obligation to reduce the entity's greenhouse gas emissions will not require an outflow of resources embodying economic benefits. ~~Although the entity will~~ to the extent that when the entity incurs the expenditure to modify its manufacturing methods, it ~~will~~ receives other resources—in for example, property, plant, equipment, energy, product ingredients or packaging materials—in exchange for that expenditure, and ~~will be~~ is able to use these resources to manufacture products it can sell at a profit*

#### Reliable estimate

The Committee concluded that in the fact pattern described, it is likely that the entity would be able to make a reliable estimate of the amount of a constructive obligation that satisfies the other recognition criteria. It is not necessarily clear how the Committee arrived at this conclusion given the limited description of the fact pattern. In addition, we believe the wording of the tentative agenda decision should be amended to avoid any confusion as to whether the threshold in paragraph 25 of IAS 37 is "likely" vs "extremely rare".

*Therefore, the entity assesses whether it is able to make a reliable estimate of the amount of a constructive obligation that satisfied the other two recognition criteria. In this regard, the Committee notes ~~p~~Paragraph 25 of IAS 37 that states that 'except in extremely rare cases, an entity*

*will be able to determine a range of possible outcomes and can therefore make an estimate of the obligation that is sufficiently reliable to use in recognising a provision’.*

*The Committee concluded that in the fact pattern described, it is likely that the entity would be able to make a reliable estimate of the amount of a constructive obligation that satisfies the other recognition criteria.*