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Presentation to the NFSA
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The Heat is On

Report

Disclosures of climate-related matters in the financial statements

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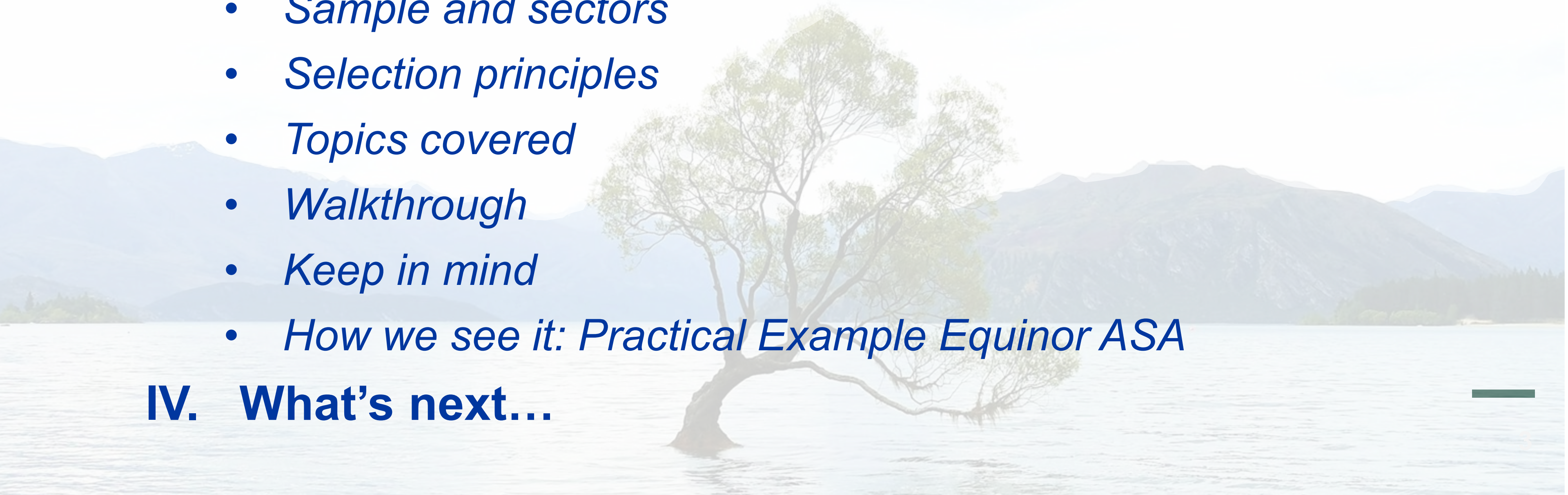

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Background

- ESMA's strategic priorities for 2023-2028;
- IASB publications on climate related matters in IFRS (Nick Anderson Article and the education material);
- Discussions at ESMA's groups (EECS and CFI TF);
- 2021, 2022 and 2023 European Common Enforcement priorities;
- Assessment of 2021 ECEP – 2022 Activity report;
- Publication of Decisions related to climate matters in EECS extract of Decisions (27 and 28th Extracts).

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2023 ECEP Statement

General considerations & reminders	Financial Reporting

General considerations & reminders

Financial Reporting

- Insurance Contracts (IFRS 17)
- Amendments to IAS 12: International Tax Reform Pillar Two Model Rules

Sustainability Reporting

- Preparations in view of the entry into force of the Corporate Sustainability Reporting Directive
- European Commission's recommendation on Transition finance

Financial Reporting

Impact of **Climate Matters** in IFRS Financial Statements, focus on:

- ✓ Consistency & Connectivity btw Financial and non-financial information;
- ✓ Accounting for emission trading schemes and renewable energy certificates;
- ✓ Impairment of non-financial assets;
- ✓ Power Purchase Agreements (PPAs)
- ✓ Specific considerations for financial institutions

Macroeconomic Environment

- Refinancing and Other Financial Risks
- Fair-Value Measurement and Disclosures
  - ✓ Climate matters in investment properties

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2023 ECEP Statement

Sustainability Reporting	Alternative Performance Measures
Disclosures relating to **Article 8 Taxonomy Regulation** Disclosures of **Climate-related Targets, Actions and Progress** **Scope 3** Emissions	**Reminders** on • Application of APM Guidelines • Reconciliations • Neutral Presentation **Digital Reporting** **Reminders** on • Selection / use of core taxonomy elements • Block-tagging legibility

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The Heat is On: Scope and disclaimers

What the Report Is...

- an educational illustration using selected European disclosures examples related to climate-related matters in IFRS financial statements
- a non-exhaustive reflection of IFRS requirements that can be relevant for climate-related matters
- a collection of examples of climate-related disclosures demonstrating certain ECEP recommendations
- Enforcers' views on how issuers may provide more relevant and transparent information to the market in relation to climate-related matters in IFRS financial statements

What the Report Is Not...

- a 'template' to use for disclosures or 'checklist' of areas to look into.
- an assessment of the quality of financial reporting, notably, measurement, recognition and presentation of the selected examples
- a rating of 'best in class' to any of the selected issuers or providing a quality stamp regarding the financial statements as a whole
- an exhaustive sample coverage -i.e., it cannot be extrapolated to any given European issuer population (country, sector, industry)
- a view on issuers' ability to comply with disclosed climate-related targets, commitments or to any climate-related requirements
- an assessment of the quality, completeness or relevance of issuers' sustainability disclosures.

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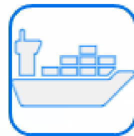
The Heat is On: Sample and sectors

22 examples across nine EU/EEA countries from issuers in nine sectors:

Electricity

Automotives


Industrial Transportation

Industrial Metals & Mining

Gas, Water & Multi-utilities

Oil, Gas and Coal

Chemicals

Construction & Materials

Telecommunications

No representation from financial institutions or insurance companies.

One example per issuer.

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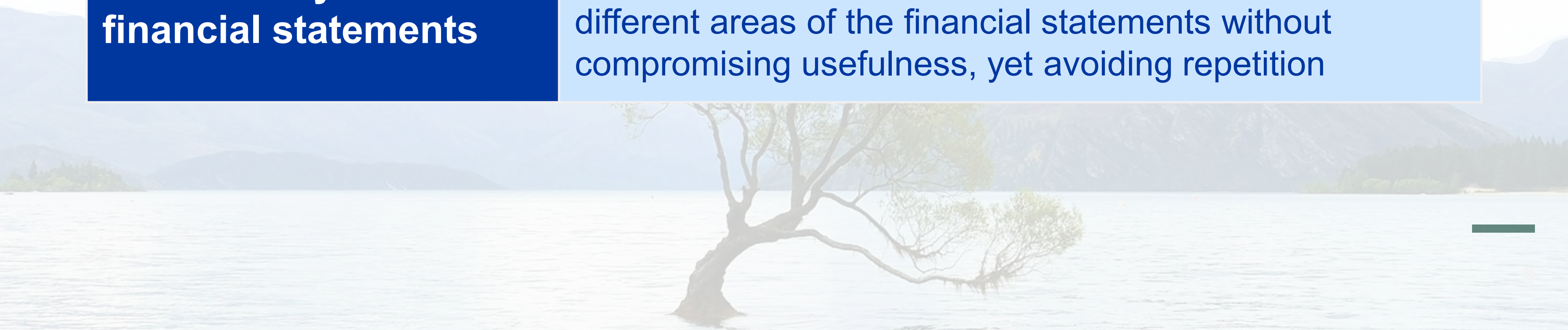
The Heat is On: Selection principles – General

Entity-specific	The disclosure appears to be tailored to the issuer's specificities
Simple and clear	Relevant information is put forward in a clear and simple manner that is easy to follow
Organised and well-formatted	The information is organised in clear paragraphs and appears to be presented in a suitable format (narrative, tabular, etc.)
Quantifications	Assumptions and impacts are quantified to allow investors to understand their effect
Consistency within the financial statements	The information seems to be consistent across the different areas of the financial statements without compromising usefulness, yet avoiding repetition



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The Heat is On: Selection principles – Connectivity

Question	Principle
Do assumptions appear consistent within and across the different components of the AFR?	*Consistency & Coherence*
Is there complementarity between the information included in the non-financial section of the AFR and the financial statements?	*Complementarity*
Are there links within and across the different components of the AFR?	*Cross-referencing*
Is the information specific and useful to the understanding of the financial statements or is it merely repeating the contents of the non-financial section of the AFR?	*Avoidance of repetition*

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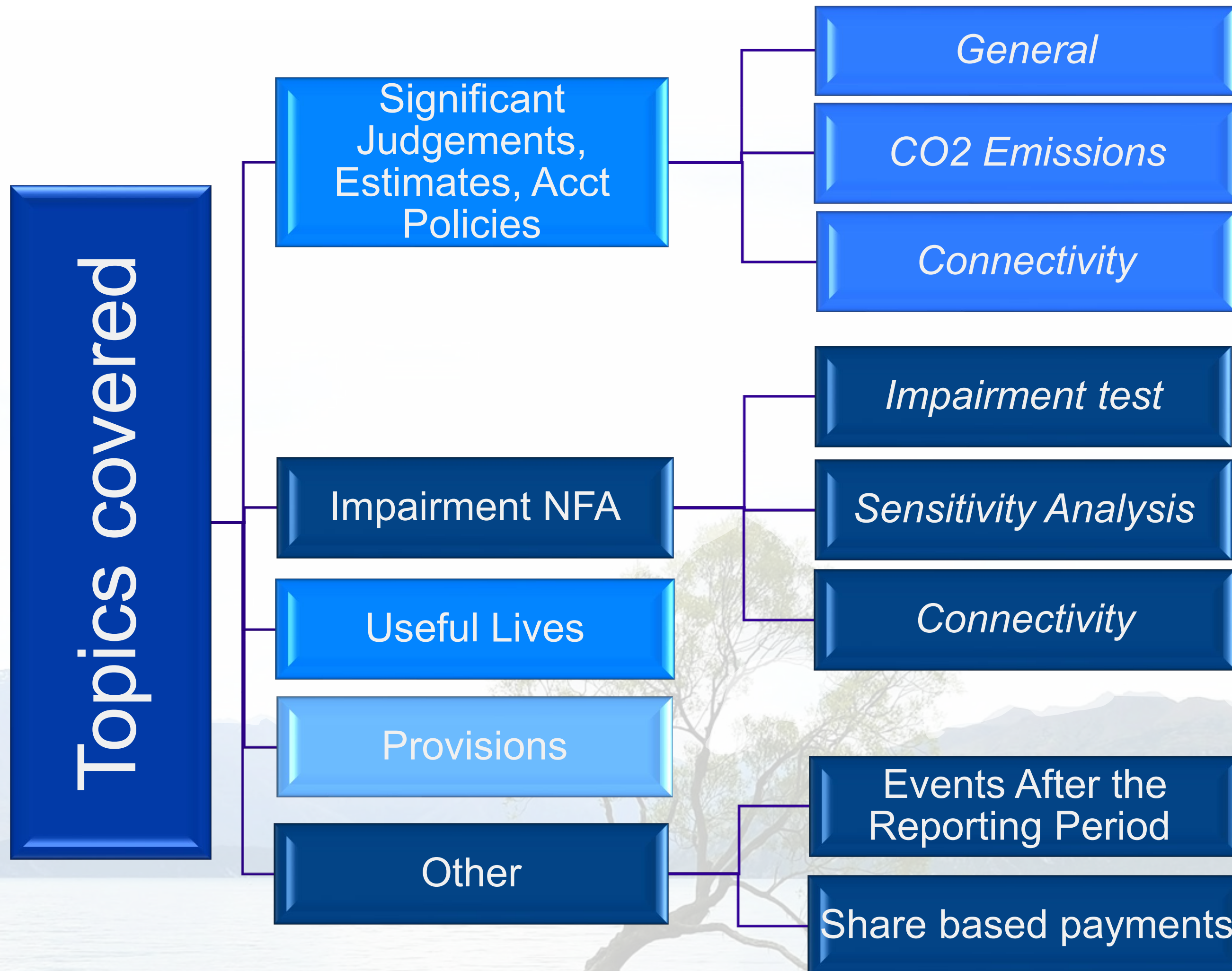
The Heat is On: Topics covered



The Heat is On: Walkthrough

Emphasis using text highlights…

…and comment boxes to pinpoint useful aspects

Exposure to climate risks.
Given their geographic location, the Group's entities may potentially be exposed to physical risks related to climate change, such as flooding, heat waves, wildfires and droughts. At December 31, 2022, the carrying amount of these sites represented 10.2% of the Group's consolidated assets (2.5% at December 31, 2021). Criteria for the identification of these sites are described in Note 19.
(…)

Note 19 Impairment Tests
(…)

Furthermore, Imerys calculated its sensitivity to risks arising from climate change with respect to the global warming scenario of +2° C by 2050, as projected by the International Energy Agency (IEA) in its Stated Policies Scenarios published in the World Energy Outlook in 2019. Executive Management selected this scenario, which represents one of the three trajectories modeled by the IEA, for the sensitivity tests as it is deemed to be reasonably possible. Risks accounted for in this model are heat waves as identified by the S&P Global Trucost Assessment, wildfires as identified by the FM Global Assessment and the Angström index and drought as identified by the Water Risk Filter of the World Wild Fund for Nature and the Deutsche Investitions- und Entwicklungsgesellschaft. Sites included in the sensitivity exercise are those where risks are recognized as uninsurable in the long term, based on the most recent information available at December 31, 2022 as well as those which are usually insurable, but are specifically recognized as uninsurable due to specific climate conditions. On this basis, Executive Management has estimated the frequency of planned closure for each site, as well as the corresponding cash flow losses.

As summarized in the table below, the sensitivity calculated in the mid case scenario indicates, n Performance Minerals, Asia Pacific (PMAPAC) excluding G&C, an impairment of -€12.5 million in the event of a 1.00% increase in the discount rate and an impairment of -€4.5 million in the event of a 1.00% decline in terminal growth rates. However, the sensitivity calculated on risks and opportunities arising from climate change did not indicate any impairment.

Quantitative information regarding tangible assets' exposure to climate risks.

Details of sensitivity analysis performed to risks arising from climate change with respect to 2°C by 2050.

Disclosure of the external sources used and rationale for selecting this source.

Example 8 – Imerys SA

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The Heat is On: Keep in mind

The examples should be read together with the key areas for continued focus.

These are to be considered additional 'food for thought'!

To keep in mind	
a)	Issuers might consider whether **regulations** related to climate matters give rise to **constructive or present obligations** and thus, to **recognition of provisions or disclosure of contingent liabilities**. Please also refer to IFRS Interpretation Committee (IFRS IC) discussions on negative low emissions vehicle credits.
b)	Where provisions related to climate matters are recognised, issuers should provide information on the **measurement of such provisions** (including information on sources of such assumptions – **external vs internal**, different geographies), especially when such provisions require estimations of future prices (such as CO_2 emissions).
c)	Issuers are reminded that an **obligation** stemming from possible new laws or regulations introduced in relation to climate change (for example, new environmental and decommissioning obligations) can arise **only when the legislation is enacted**. As such, issuers are encouraged to continue **monitoring government actions and introductions of or changes to regulations relating to climate** and consider whether these may give rise to specific conditions where a provision must be recognised.
d)	Issuers should consider **disclosing sensitivity analyses** regarding key assumptions related to climate matters used on the recognition or measurement of provisions or contingent liabilities.
e)	Issuers should also consider **disclosing the maturities expected and timing** related to unwinding provisions recognised related to climate matters (in particular, when such provisions may affect long term periods – such as decommissioning provisions).

See also…

2021 ECEP

2022 ECEP

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Example: Equinor ASA

Equinor ASA, an energy company, described its accounting policies related to EU Emissions Trading System (EU ETS) allowances and disclosed the assessment underpinning how it had considered the impact of the allowances on its 2022 financial statements.

EXAMPLE 5 – EQUINOR ASA

Pages 140-143

ESMA emphasis added in *Orange*

Note 3. Consequences of initiatives to limit climate changes
Accounting policies - cost of CO_2 quotas
Purchased CO_2 quotas under the EU Emissions Trading System (EU ETS) are reflected at cost in Operating expenses as incurred in line with emissions. Accruals for CO_2 quotas required to cover emissions to date are valued at market price and reflected as a current liability within Trade, other payables and provisions. Quotas owned, but exceeding the emissions incurred to date, are carried in the balance sheet at cost price, classified as Other current receivables, as long as such purchased quotas are acquired in order to cover own emissions and may be kept to cover subsequent years' emissions. Quotas purchased and held for trading purposes are carried in the balance sheet at fair value, and the changes in fair value are reflected in the Consolidated statement of income on the line-item Other income.
(…)
Impact on Equinor's financial statements
CO_2-cost and EU ETS carbon credits
Our oil & gas operations in Europe are part of the EU Emission Trading Scheme (EU ETS). Equinor buys EU ETS allowances (quotas or carbon credits) for the emissions related to our oil & gas production and processing. Currently we receive a share of free quotas according to the EU ETS regulation. The share of free quotas is expected to be significantly reduced in the future.

Information regarding which line items in the balance sheet and statement of profit or loss (P&L) are affected by the accounting of CO_2 costs.

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Example: Equinor ASA (cont)

Total expensed CO_2 cost related to emissions and purchase of CO_2 quotas in Equinor related to activities resulting in GHG emissions (Equinor's share of the operating licences in addition to our land-based facilities) amounts to USD 510 million in 2022, USD 428 million in 2021, and USD 268 million in 2020. A large portion of the cost of CO_2 in Equinor is related to the purchase of EU ETS quotas. The table below shows an analysis of number of quotas utilised by Equinor's operated licences and land-based facilities subject to the requirements under EU ETS:

Number of EU ETS quotas	2022	2021
Opening balance at 1 January	11,026,286	11,027,242
Allocated free quotas	3,697,089	3,560,286
Purchased quotas on the ETS market	5,985,000	7,605,265
Sold quotas on the ETS market	0	(135,177)
Settled quotas (offset against emissions)	(9,925,999)	(11,031,330)
Closing balance at 31 December	10,782,376	11,026,286

Description of the accounting policies applied in the treatment of CO_2 quotas, mention of consumption, acquisition and

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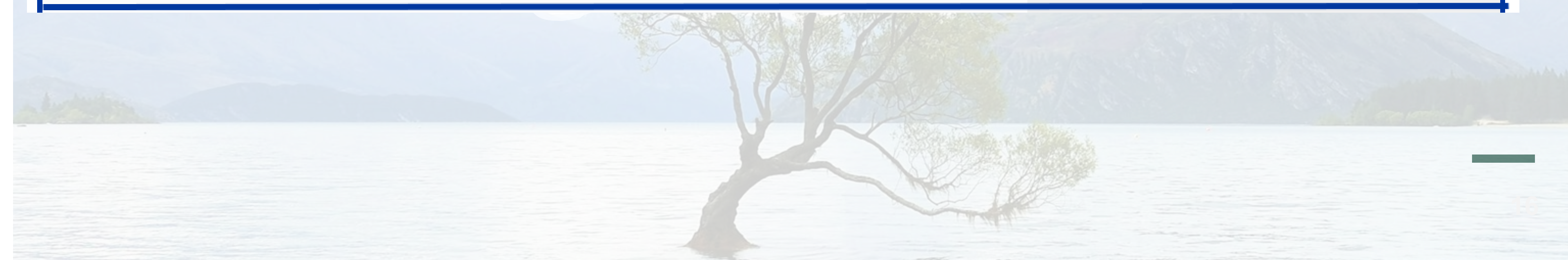
Example: Equinor ASA (cont)

Effects on estimation uncertainty
(…)
Commodity prices
Equinor's **commodity price assumptions applied in value-in-use impairment testing, are set in accordance with requirements in IFRS and based on management's best estimate of the development of relevant current circumstances** and the likely future development of such circumstances. **This price-set is currently not equal to a price-set required to achieve the goals in the Net Zero Emissions (NZE) by 2050 Scenario, nor a price-set in accordance with the Announced Pledges Scenario as defined by the International Energy Agency (IEA)**. A future change in the trajectory of how the world acts with regards to implementing actions in accordance with the goals in the Paris agreement could, depending on the detailed characteristics of such a trajectory, **have a negative impact on the valuation of Equinor's property, plant and equipment in total.** A calculation of a possible effect of using the assumed commodity prices and **CO_2 prices in a 1.5°C compatible NZE by 2050 Scenario as estimated by IEA could result in an impairment of upstream production assets and intangible assets around USD 4 billion before tax**, see the sensitivity table below.
Similarly, we have calculated the possible effect of using prices according to the Announced Pledges Scenario, a scenario which is based on all of the climate-related commitments announced by governments around the Globe. **Using this scenario, the world is expected to reach a 1.8°C increase in the year 2100, and this could result in an impairment of less than USD 0.5 billion before tax using the same simplified model, see the sensitivity table below.**
(…)

Potential impacts of +1.5°C by 2050, and +1.8°C by 2100 on assets valuations and sensitivities for different external climate scenarios.



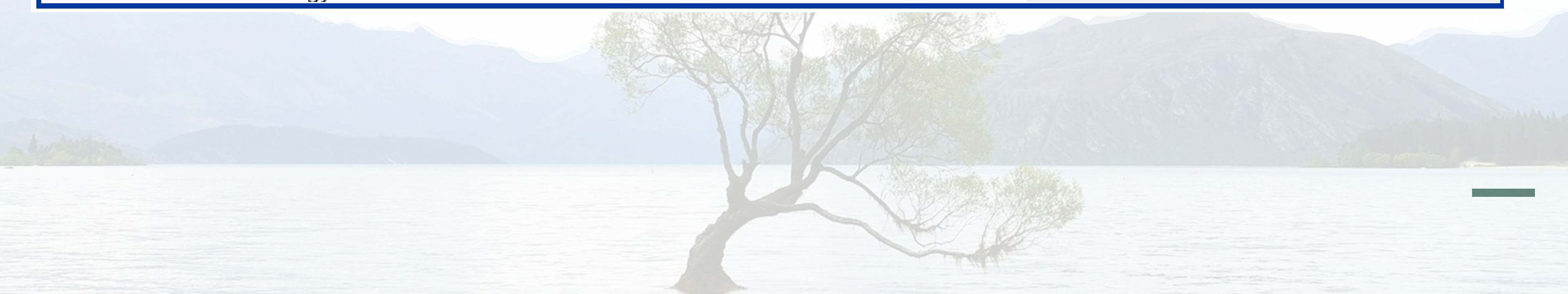
Example: Equinor ASA (cont)

Cost of CO_2

The EU ETS price has increased significantly from 25 EUR/tonne in 2020. The average cost of EU ETS allowances was 81 EUR/tonne in 2022 (54 EUR/tonne in 2021). The price is expected to remain high, in the region of **80 EUR/tonne for the next couple of years. Then the price is expected to be 105 EUR/tonne in 2040 and thereafter increasing to 130 EUR/tonne in 2050.** As such, Equinor expects greenhouse gas emission costs to increase from current levels and to have a wider geographical range than today, and a global tax on CO_2 emissions **will have a negative impact on the valuation of Equinor's oil and gas assets.** Currently, Equinor pays CO_2 fees in Norway, the UK, Germany and Nigeria. Norway's Climate Action Plan for the period 2021-2030 (Meld. St 13 (2020-2021)) which assumes a gradually increased CO_2 tax (the total of EU ETS + Norwegian CO_2 tax) **in Norway to 2,000 NOK/tonne in 2030 is used for impairment calculations of Norwegian upstream assets**.

Equinor's response to this risk is evaluation of carbon intensity on both project and portfolio level in our investment and divestment decisions. **We have also introduced an internal carbon price, currently set at 58 USD/tonne and increasing towards 100 USD/ tonne by the year 2030** and staying flat thereafter (in countries with higher carbon costs, we use the country specific cost expectations), to be used in our investment decisions. This cost-scenario is uncertain, but this extra cost serves as a placeholder for possible future CO_2 pricing systems, making sure our assets are financially robust in such a scenario. As such, climate considerations are a part of the investment decisions following Equinor's strategy and commitments to the energy transition.

Assumptions regarding CO_2 emission costs by geographies in impairment tests and sensitivity analysis.



Example: Equinor ASA (cont)

Climate considerations are also included in the impairment calculations directly by estimating the CO_2 taxes in the cash flows. Indirectly, the expected effect of climate change is included in the estimated commodity prices where supply and demand are considered. **The CO_2 prices also have effect on the estimated production profiles and economic cut-off of the projects. Impairment calculations are based on best estimate assumptions.** To reflect that carbon will have a cost for all our assets, the current best estimate is considered to be EU ETS for countries outside EU where carbon is not already subject to taxation or where Equinor has not established specific estimates.
(…)

	Management's price assumptions[1]		NZE by 2050 scenario		Announced Pledged Scenario	
Brent blend, 2030	75	USD/bbl	40	USD/bbl	71	USD/bbl
Brent blend, 2040	70	USD/bbl	34	USD/bbl	69	USD/bbl
Brent blend, 2050	65	USD/bbl	28	USD/bbl	67	USD/bbl
TTF, 2030	9.5	USD/MMBtu	5.0	USD/MMBtu	8.5	USD/MMBtu
TTF, 2040	9.0	USD/MMBtu	4.5	USD/MMBtu	7.7	USD/MMBtu
TTF, 2050	9.0	USD/MMBtu	4.1	USD/MMBtu	6.8	USD/MMBtu
EU ETS [2), 3)], 2030	94	USD/tCO_2	152	USD/tCO_2	146	USD/tCO_2
EU ETS [2), 3)], 2040	124	USD/tCO_2	222	USD/tCO_2	189	USD/tCO_2
EU ETS [2), 3)], 2050	153	USD/tCO_2	271	USD/tCO_2	216	USD/tCO_2
Illustrative potential impairment (USD)			~ 4.0	billion	< 0.5	billion

1) Management's future commodity price assumptions applied when estimating value in use, see note 14 Impairments
2) Scenarios: Price of CO_2 quotas in advanced economies with net zero pledges, not including any other CO_2 taxes
3) EU ETS price assumptions have been translated from EUR to USD using Equinor's assumptions for currency rates, EUR/USD = 1,176

Consideration of CO_2 prices as a key assumption in value in use calculations. Steady decrease of Brent prices.

Example on Connectivity: Uniper SE

EXAMPLE 14 – UNIPER SE

Pages 132; 220; 224

ESMA emphasis added in *Orange*

Financial Statements	Non-financial Information
(17) Impairment Testing in Accordance with IAS 36 (…) **Non-current assets:** Intangible assets, property, plant and equipment, including right-of-use assets, and groups of these assets, as well as companies accounted for under the equity method, are tested for impairment as indicated at the level of the individual asset or the CGU. Impairment testing of the aforementioned assets or CGUs is performed whenever there are indications of impairment. In the European Generation segment, ***for example, the tests are based on remaining useful life, which can be shorter than the technical useful life specifically in coal-fired power plants, due to measures taken in specific countries to mitigate climate change, and on other plant-specific valuation parameters***. Uncertainties relating to a variable regulatory environment are generally accounted for by means of scenario evaluations. Recoverable amounts were usually determined using the value in use. (…) Some of the **coal phase-out pathways already adopted in specific countries have been considered accordingly in the impairment tests performed.** In cases where Uniper sees the use of fossil energy sources ending early, this has been reflected accordingly. **No fossil-fuel power plants were modeled Group-wide from 2050 forward** **Full-Year Presentation for 2022** (…) **The most substantial individual impairment in the European Generation segment in the 2022 fiscal year in terms of amount related to the Datteln 4 hard-coal power plant and amounted to €87 million**. Aside from the price-driven adjustments made in the context of regular medium-term corporate planning that reflected the impact of the **increased cost of carbon and the costs incurred for climate neutrality**, among other factors, revised regulatory and legal as well as political assessments resulted in these impairment losses at year-end.	**Decarbonizing the Coal and Gas Business** In 2022, Uniper's coal-based power production in Europe amounted to 17.3 TWh, which is a decrease of 1.3 TWh from 2021. The temporary security of supply measures has impacted Uniper's original coal exit path. Nonetheless, Uniper remains committed to its decarbonization pledge: ***Aligned with its coal phase-out strategy and relevant national legislations, Uniper will end coal-fired power generation in the United Kingdom by 2024, in the Netherlands by 2029, and in Germany by 2026 with the divestment of the Datteln 4 hard-coal-fired power plant.*** (…)

Disclosure highlights the link between the abandonment of coal-fired power plants and the recognition of impairment.

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What's next:

- Monitor the developments in this area notably, the work carried out by the IASB and EFRAG;
- Discuss cases regarding the application of IFRS to climate related matters;
- Contribute to standard setting activities (i.e. comment letters);
- Assess the adherence of issuers with 2022 ECEP and 2023 ECEP;
- Where necessary, publish further guidance to the market (e.g. EECS Extract of decisions, connectivity with ESRS).

Questions?

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