

Impact of climate change on financial statements

Background

The impact of climate change on the financial statements is a high-profile issue. Investors and regulators are increasingly looking for evidence of how the entity has incorporated environmental, social and governance (ESG) matters and in particular climate-related risk factors when making estimates and judgements in the preparation of the financial statements. Climate-related risks could include both transition impacts, for example additional costs incurred by the entity as a result of transitioning to a low-carbon economy, or physical impacts, such as damage to assets as a result of fires and flooding.

The accounting standards have an overarching requirement to disclose information that users need for them to understand the impact of particular transactions, events and conditions on the entity's financial position and financial performance. Therefore, in light of the current focus on, and impact of, climate change, entities should ensure that they have assessed the impact of climate change on measurement of assets and liabilities, and what disclosures are necessary in this context for the financial statements to comply with SFRS(I)s. SFRS(I) 1-1 (112)(c)

This appendix discusses how climate change could affect certain measurements and therefore the related disclosures in the financial statements. It also outlines some of the relevant considerations when making estimates and judgements and drafting the relevant disclosures to satisfy the current SFRS(I) requirements. We have provided signposts throughout the illustrative financial statements as reminders for readers to refer to this guidance where necessary.



For further guidance and illustrations, entities may refer to PwC's guidance: **Impact of ESG matters on IFRS financial statements**

Entities may also refer to ISCA's technical bulletin:

Addressing Climate-Related Risks in Financial Statements and Audits of such Financial Statements

IASB guidance and possible future developments

In July 2025, IASB issued a near-final staff draft of examples illustrating how an entity applies the requirements in IFRS Accounting Standards to disclose the effects of uncertainties in its financial statements. The examples illustrate the reporting of the effects of uncertainties through climate-related fact patterns, but the principles and requirements are also applicable to disclosure of other uncertainties.

There are six examples showing how to navigate the disclosure requirements related to materiality judgements, disclosure of assumptions, disclosure about credit risk, decommissioning and restoration provisions, and disaggregated information.

The IASB is making this near-final draft available to help entities start considering whether to make any changes to the information disclosed in their financial statements as a result of these illustrative examples.

The examples do not add to or change requirements in IFRS Accounting Standards and therefore there are no transition requirements. Instead, these examples will be accompanying the respective IFRS Accounting Standards they relate to.

Once the final version is issued, it will be effective immediately.



For details of the near-final draft, please refer to the following link:

[Near-final staff draft: Disclosures about Uncertainties in the Financial Statements Illustrated using Climate-related Examples](#)

Impact of climate-related risks on the financial statements**Consistency is important**

The IFRS Sustainability Disclosure Standards specifically require consistency of the disclosures and assumptions used in preparing the financial statements and sustainability disclosures. However, even before these standards become mandatory, entities should ensure their disclosures of critical estimates and other relevant information in the financial statements are consistent with the non-financial information disclosed elsewhere (for example, in the company's sustainability report) in relation to:

- (a) climate-related matters
- (b) the impact and consideration of climate-related risks, and
- (c) any material disclosure in relation to significant judgements and estimates of uncertainty arising as a result of climate-related risks.

Questions often arise about whether the assumptions in an entity's financial statements are 'Paris aligned'. This refers to whether they comply with the legally binding instrument that many nations have signed relating to limiting carbon emissions to a level designed to cap global temperature rises. Whether financial statements are 'Paris aligned' is not easy to determine because of the variety of measurement techniques required by IFRS depending on the item being considered in the statement of financial position. Therefore, it might be easier for the recognition and measurement of some items to be more closely aligned to Paris assumptions than others.

In addition to ensuring consistency of the disclosures about climate-related matters and their impact in both financial and non-financial information, entities also need to ensure consistency of the assumptions used in developing estimates for the financial statements, where possible.

For example, where an entity publicly discusses a best estimate about the impact of the Paris Agreement on the entity in a sustainability report and an SFRS(I) standard requires a best estimate approach to be used in measurement (for example, for the purpose of impairment calculations), the entity would need to consider consistency between the estimates used for financial reporting and those disclosed in the sustainability reporting.

Where there are comments in the sustainability report about estimates that haven't been reflected in financial reporting (for example, because the entity is relying on a market participant's assumptions which differ), the entity should consider explaining why such items have been reflected on a different basis in financial reporting.

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Material accounting policy information

In an effort to lower emissions and achieve carbon neutrality, many entities are entering into more complex transactions and arrangements for which the accounting continues to evolve. Examples of these include emissions trading schemes and virtual power purchase arrangements. In some cases, these transactions and arrangements are clearly within the scope of an SFRS(I) and in other cases it is less clear.

SFRS(I) 1-8
(8)
SFRS(I) 1-1
(117) - (121)

In the absence of an SFRS(I) that specifically applies to a transaction, other event or condition, management shall use its judgement in developing and applying an accounting policy that results in relevant and reliable information.

SFRS(I) 1-8
(10)

Entities shall disclose accounting policy information if it is material. Information is material if, when considered together with other information included in the financial statements, it can reasonably be expected to influence user's decisions made on the basis of the financial statements. SFRS(I) 1-1 also notes that an accounting policy may be material because of the nature of the entity's operations even if amounts for current and prior periods are not material. Accounting policies developed in accordance with SFRS(I) 1-8 are an example of policies that are expected to be material.

SFRS(I) 1-1
(117), (117B)

Entities should therefore not underestimate the importance of disclosing climate-related accounting policies in the notes to the financial statements.

Going concern

SFRS(I) 1-1 requires management to assess an entity's ability to continue as a going concern when preparing financial statements. In assessing whether the going concern basis of preparation is appropriate, management considers all available information about the future, which is at least, but is not limited to, 12 months from the end of the reporting period. If climate-related matters create material uncertainties related to events or conditions that may cast significant doubt on a company's ability to continue as a going concern, an entity should disclose these uncertainties even if the financial statements continue to be prepared on a going concern basis.

SFRS(I) 1-1
(25)

Where management has concluded that there are no material uncertainties related to the going concern assumption that require disclosure, but reaching that conclusion involved significant judgement (for example, about the feasibility and effectiveness of any planned mitigation), SFRS(I) 1-1 requires disclosure of that judgement. Entities should also consider the interrelationship with the liquidity risk disclosures discussed in Note 42(c).

SFRS(I) 1-1
(122)
SFRS(I) 7 (39)

Critical accounting estimates, assumptions and judgements

There is an overarching requirement to disclose sources of estimation uncertainty in SFRS(I) 1-1. If assumptions that an entity makes about the future have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year, the entity is required to disclose information about those assumptions and the nature and carrying amount of those assets and liabilities. The information should help users of the financial statements to understand the judgement applied by management and what might be disclosed will depend on the specific facts and circumstances. If the accounting estimate is highly sensitive to one estimated input, it might be useful to disclose the estimated input and the sensitivity of the accounting estimate to changes of this input.

SFRS(I) 1-1
(125)(a) - (b)

The entity may further need to explain the impact of various potential climate scenarios on significant estimates made in preparing the financial report. In addition, entities would typically explain changes made to past assumptions.

SFRS(I) 1-1 also has an overarching disclosure requirement to ensure that the financial statements capture all information that would be considered material and relevant to an understanding of them but is not presented elsewhere in the financial statements. This might be especially relevant for entities whose financial position or performance is particularly affected by climate-related matters.

Trade and other receivables

SFRS(I) 7 Financial Instruments: Disclosures requires information which enables the users to understand the effect of credit risk on the amount, timing and uncertainty of future cash flows.

SFRS(I) 7
(35B)

Climate change might affect a lender's exposure to credit losses for its financial assets. The expected credit loss (ECL) model in SFRS(I) 9 Financial Instruments requires the use of reasonable and supportable information that is available without undue cost or effort. Climate change might affect the assumptions that are made by lenders to estimate ECL. It could also affect the risk ratings for individual borrowers or groups of borrowers or their probability of default. In some cases, it could result in moving loans between stages.

SFRS(I) 9
(5.5.17)(c)

SFRS(I) 7 requires that entities provide qualitative and quantitative information about the changes in the amount of expected credit losses and the reason for those changes. To the extent that any changes in ECL are the result of changes made to the assumptions about the impact of climate change or other climate-related risks, that fact should be disclosed.

SFRS(I) 7
(35I)

Property, plant and equipment and intangible asset useful lives

In addition to impairment, entities may also need to reassess the useful lives and residual values of property, plant and equipment and intangible assets as a result of climate change. For example, climate impacts could result in earlier obsolescence of assets, or legal restrictions might be placed on the use of the assets or lead to inaccessibility of the assets. In the most extreme cases, if assets become inaccessible either as a result of natural climate events or government action, an entity could even lose control of assets permanently.

Entities must consider many factors in determining the useful life of assets, including obsolescence from changes in market demand and other economic factors. This estimation of the useful life of assets is a matter of judgement. Entities should consider disclosing if there are any estimation uncertainties related to the impacts of climate-related risks on the useful lives of assets. An example might be where there are multiple potential outcomes and some of them could significantly shorten the asset's life compared to the scenario with the highest probability used in determining useful life.

SFRS(I) 1-16
(56)
SFRS(I) 1-38
(90)
SFRS(I) 1-1
(125)

Entities may also have new forms of intangibles such as carbon emissions rights and should consider the appropriate disclosure of policies for such schemes (see discussion in 'Material accounting policy information' above).

Property, plant and equipment and intangible asset impairment

Climate-related risks can have a significant impact on impairment of non-financial assets. Climate change could be an indicator of impairment and trigger the need for an impairment test. For example, a decline in demand for products that emit greenhouse gases could indicate that a manufacturing plant might be impaired.

Further, the inputs and assumptions used in both a value in use or fair value less costs of disposal model could be significantly impacted by climate-related risks.

For these reasons, impairment disclosures might need to explain climate-related impacts. Where climate-related risks could have a significant impact on an entity's operations, information about how this has been factored into the recoverable amount calculations would be relevant for the users of the financial statements. In some cases, the conclusion not to adjust an impairment model for climate-related risks might be based on significant judgements or assumptions that entities should also explain in their disclosures.

SFRS(I) 1-36
(130)(f), (132),
(134)
SFRS(I) 1-1
(125)

Many companies discuss climate scenarios as part of their narrative reporting. These scenarios might stem from the Paris Agreement, from net zero targets or from the ISSB standards requirements. Such scenario analyses are likely to interact with the disclosures required by SFRS(I) 1-1 or SFRS(I) 1-36 Impairment of Assets. However, the premise of the narrative disclosures is not identical to what SFRS(I) 1-36 requires.

Property, plant and equipment and intangible asset impairment (continued)

For example, SFRS(I) 1-36 requires a sensitivity analysis if a reasonably possible change in assumptions would lead to an impairment. This might include a reasonably possible unfavourable change in an assumption relating to climate change. The ISSB Standards, on the other hand, require a scenario disclosure that is based on a 1.5°C or 2.0°C limitation on temperature rise, even though these might not be assumptions that are aligned with a company's best estimate or with market participant assumptions. Entities might consider explaining how the assumptions used for the impairment test under SFRS(I) 1-36 correspond to assumptions used in the narrative reporting on climate change scenarios to help financial statement users understand the linkage.

SFRS(I) 1-36
(134)(f)

Management should consider whether other information, such as climate reporting included in the entity's annual report, is consistent with the audited financial statements. In addition to this, regulators in a number of territories have been clear that they expect entities to explain and reconcile any discrepancies in assumptions used.

Deferred income taxes

Entities should assess the impact of climate-related matters on the estimation of future taxable profits and whether they are sufficient to recover the deferred tax assets. The assumptions used in these estimations should be consistent with those used elsewhere in the financial statements. To the extent that these assumptions are material in understanding the estimates and judgements which have been made in the recognition of the deferred tax assets, these assumptions should be disclosed.

SFRS(I) 1-12
(24), (34)
SFRS(I) 1-1
(122), (125)**Inventories**

Inventories could become impaired if their cost is not recoverable and entities must write down such inventories to their net realisable value. Some sectors might experience increased volatility in the market prices of assets as a result of changes in demand patterns for certain commodities, which could expose those inventories to greater risk of impairment.

SFRS(I) 1-2
(28)

In other cases, certain assets might be discontinued from use or production, which could result in an impairment of the parts for those assets. For example, a certain model of combustion engine might be discontinued because it no longer meets emission standards, making the parts used to produce or service that engine obsolete. If the entity has made any significant estimates or judgements in this context, it should disclose them.

SFRS(I) 1-1
(122), (125)

Entities may also have new forms of inventory such as carbon emissions rights and should consider the appropriate disclosure of policies for such schemes (see discussion in 'Material accounting policy information').

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Provisions and contingencies

SFRS(I) 1-37
(14)

Climate-related risks can have an impact on the disclosure of provisions and contingent liabilities. Actions taken or statements made by the entity could give rise to constructive obligations for which provisions must be recognised, even in the absence of legislation requiring the entity to act.

For example, an entity operates a plant that is heavily dependent on fossil fuels and for which it has recognised a decommissioning provision. The entity's sustainability strategy promises carbon neutrality by 2030. This can realistically only be achieved by substituting the plant with a newer hybrid model plant in the medium term – sooner than originally anticipated. As a result of this plan, the entity must bring forward the timing of the expected cash flows for decommissioning the plant.

In April 2024, the IFRS Interpretations Committee finalised an agenda decision on whether statements announcing committed transition plans would give rise to constructive obligation that requires a provision, and should this corresponding amount on the provision be recognised as an asset or expense. The committee has clarified that while it is not necessary to know the identity of the party the obligation is owed (i.e. may be to the public at large), whether a statement to reduce emissions creates a valid expectation that an entity will fulfill the commitment and thus result in a constructive obligation, depends on the facts and circumstances surrounding it, including any actions the entity has taken that publicly affirm its intention to fulfil the commitment. Management would have to apply judgment to reach a conclusion at each reporting date.

SFRS(I) 1-37
(10), (20)

An entity will recognise a provision on a constructive obligation that arose from the commitment only at the target date stated in the committed plan, if there are any unsettled obligations in which a reliable estimate can be made. The corresponding amount to the provision is an expense and not an asset unless it gives rise to, or forms part of the cost of an item that qualifies for recognition as an asset.

SFRS(I) 1-37
(14)

Entities must disclose an indication of the uncertainties relating to the amount or timing of any outflow as well as major assumptions made concerning future events. To the extent that climate-related risks impact the assumptions or uncertainties, entities should explain this in their notes.

SFRS(I) 1-37
(85)(b)

In addition, climate-related risks may also affect the aggregation of provisions or contingent liabilities for disclosure purposes. In determining which provisions or contingent liabilities may be aggregated to form a class, it is necessary to consider the similarities and differences of these items. Climate-related risks may be incorporated differently into provisions which were previously aggregated. Entities should therefore consider whether further disaggregation of the classes is required as the impact of climate-related risks evolve and become better understood.

SFRS(I) 1-37
(87)

Renewable power purchase agreements

As entities plan to reduce their carbon footprint, they are often seeking sources of renewable energy. An entity can demonstrate its support for renewable energy sources in several ways, for example:

- Purchase of renewable energy certificates (RECs) on a stand-alone basis in the market. RECs are created for each megawatt hour of electricity that is generated from a renewable energy resource, and they can be purchased by an entity in the market and then retired by the entity to offset energy usage from non-renewable sources.
- Physical power purchase agreements (physical PPAs) for renewable electricity. The entity takes physical delivery of renewable electricity from a particular generation facility at some point after the generation process.
- Financial settlement of renewable electricity through a virtual power purchase agreement (VPPA), where an entity obtains RECs and financially settles electricity. VPPA is sometimes called a 'financial power purchase agreement' or 'contract for differences' (CFD).

Accounting for PPAs can be complex and involve multiple accounting standards. For example, due consideration is needed on whether the arrangement gives rise to consolidation or equity accounting, contains a lease, or is in-scope as a financial instrument. This is further complicated by the fact that renewable electricity is a unique product; the timing and volume of renewable electricity production is unpredictable due to its nature-dependency and is not economically storable at scale. It is therefore important for entities to thoroughly evaluate the contractual terms of PPAs to determine the applicability of various standards.

Purchased RECs are typically accounted for as intangible assets, although they may be classified as inventory if the definition is met. Where the RECs are held for resale or consumed in the process of production of inventories (e.g., as an input cost in the manufacturing of a product), they are more likely to meet the definition of inventory. RECs are accounted for at cost on initial recognition. When retired, RECs are derecognised and the relevant costs are expensed in profit or loss as electricity costs or another appropriate line item depending on the accounting policy adopted for income statement presentation.

SFRS(I) 1-2 (6)
SFRS(I) 1-2 (9),
SFRS(I) 1-38
(24)
SFRS(I) 1-1
(85)

Management should consider whether their recognition of such agreements in the financial statements are in line with other information, such as climate reporting.



For a detailed discussion on accounting for power purchase agreements, refer to our publication:

Accounting for green/renewable power purchase agreements

Emissions trading schemes

There is no specific accounting standard that deals with accounting for emissions trading schemes. IFRIC 3 Emission Rights was intended to address the accounting in this area, but it was withdrawn in 2005.

The withdrawal of IFRIC 3 means that there are a number of accounting models that entities can use under SFRS(I) 1-8 in accounting for the participation in these schemes. Entities should disclose the accounting policies adopted for: ^{SFRS(I) 1-1 (117), (117B)}

- (a) recognition
- (b) initial measurement
- (c) subsequent measurement, and
- (d) presentation of the balances.

See the discussion about disclosure of accounting policies in 'Material accounting policy information' above.

Emissions credits granted by a government entity are generally accounted for under SFRS(I) 1-20 as the receipt of a non-monetary asset. However, SFRS(I) 1-20 allows for different accounting policy choices with respect to measurement on initial recognition and the presentation in both the balance sheet and the income statement. Disclosure of the accounting policy for these programs is key to understanding the impact of these programs on the financial statements.

To the extent that entities determine that aspects of their emissions trading schemes meet the definition of financial assets and qualify for derivative or hedge accounting, they should further consider the disclosure requirements of SFRS(I) 7 and SFRS(I) 13.

Management should consider whether their recognition of such arrangement in the financial statements are in line with other information, such as climate reporting.



For a detailed discussion on accounting for emissions trading schemes refer to our publication:

Emissions trading schemes: The opportunities ahead

Carbon offsets in the voluntary carbon market

With the increasing focus on climate change and carbon emissions, the voluntary carbon market (VCM) is growing. Consistent accounting practices for carbon offsets are relevant for entities participating in the VCM; be it corporates using carbon offsets to achieve emission reduction targets, project developers, or carbon offset traders. However, there are no accounting standards or interpretations that directly address the accounting for carbon offsets and related projects. In the absence of a clear framework, entities participating in the VCM would need to deliberate and disclose appropriate accounting policies for the generation, sale and purchase, and retirement of carbon offsets as applicable.



For a detailed discussion on accounting for carbon offsets refer to our publication:

IFRS Financial reporting considerations for entities participating in the voluntary carbon market

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Financial risk management – Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: currency risk, interest rate risk and other price risk. Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices, whether those changes are caused by:

- (a) factors specific to the individual financial statement or its issuer, or
- (b) factors affecting all similar financial instruments traded in a market.

SFRS(I) 7
Appendix A

Entities must disclose a sensitivity analysis which shows how profit or loss and equity would have been affected by changes in risk variables.

SFRS(I) 7
(40)

Climate risk could have a significant impact on market risk, for example, for investments in industries impacted both positively and negatively by climate-related risks. In some cases, it may be necessary to provide additional explanations and disclose a sensitivity analysis that reflects interdependencies between risk variables. For example, if an entity has an interest rate that is floating based on both meeting its climate initiatives and a market benchmark, the entity should consider disclosing how the impact of meeting the climate initiative was incorporated into the sensitivity analysis.

SFRS(I) 7
(40), (41)

Financial risk management – Credit risk

SFRS(I) 7 requires that entities disclose concentrations of risk including:

SFRS(I) 7
(34)(c), (B8)

- (a) how management determines such concentrations
- (b) a description of the shared characteristic that identifies each concentration, and
- (c) the amount of the risk exposure associated with all financial instruments sharing that characteristic.

Entities might have to change the way in which they are approaching their risk concentration disclosures to take into account climate-related risks. For example, more precision in determining geographic concentration might be necessary to reflect heightened risk in particular areas (such as city versus provincial/state disclosures where a particular city is particularly impacted) or more precision in the industry sector (such as a more precise disaggregation of exposure to different industrial products sectors based on carbon intensity).

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Financial risk management – Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset.

SFRS(I) 7
Appendix A

Entities are required to disclose a maturity analysis for their financial instruments as well as a description of how they manage the liquidity risk inherent in the maturities.

SFRS(I) 7
(39)

Where the impacts of climate change could accelerate the timing or alter the amount of contractual maturities of financial liabilities, for example as a result of clauses in a sustainability linked loan, entities should disclose that information.

SFRS(I) 7
(B11D)

When the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the end of the reporting period. For example, when the amount payable varies with changes in an index, the amount disclosed will be based on the index's level at the end of the period. In this case, entities should disclose the risk that the amount payable will increase depending on the index.

As an entity's climate-related risk exposures become more significant, there could also be growing pressure on an entity's debt covenants. In this context, disclosures about key covenants and facts and circumstances, if any, that indicate that the entity might have difficulty complying with the covenants and that non-current liabilities could become repayable within the next 12 months might become increasingly material. Reduced access to funding from investors in carbon-intensive industries could also be a risk that entities need to address and disclose.

SFRS(I) 1-1
(135)(a)(ii)

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Fair value measurements

SFRS(I) 13 Fair Value Measurement requires disclosure of the inputs used in fair value measurements and, for recurring fair value measurements with significant unobservable inputs, a description of the sensitivity of those measurements to changes in unobservable inputs.

SFRS(I) 13
(93)(d),
(93)(h)(i)-(ii)

Fair value is a market-based measurement which maximises the use of observable inputs and uses assumptions that market participants would use when pricing the asset or liability. These might include assumptions about climate-related risks.

Fair value measurements using observable (that is, level 1) inputs will already reflect market participant views of climate change impacts. For example, the quoted equity price of an entity in the extractives or agriculture industries will reflect market participant expectations about potential climate risk scenarios.

However, valuation models for items that are not traded in an active market should be reviewed to ensure that they adequately represent market participant assumptions for the particular item being valued.

Inputs and assumptions which might be impacted by climate-related risks include, but are not limited to:

- (a) discount rates
- (b) the timing and amount of forecasted cash flows (For example, the fair value measurement for an investment property might need to be adjusted to reflect climate impacts on rental income, occupancy rates as well as insurance cost assumptions.)
- (c) the highest and best use for certain assets measured at fair value
- (d) inflation rates, and

other assumptions that a market participant would consider in the circumstances.