Staff paper

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Accounting Standards Advisory Forum meeting

Date	**July 2025**
Project	**Provisions—Targeted Improvements**
Topic	**Exposure Draft feedback—Discount rates**
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Accounting Standards Advisory Forum, July 2025, Agenda Paper 1E

This paper was prepared for discussion at the International Accounting Standards Board's (IASB's) June 2025 meeting as Agenda Paper 22E. The agenda papers referred to in this paper are the other agenda papers for the IASB's June 2025 meeting.

Purpose of paper

1. The International Accounting Standards Board (IASB) published Exposure Draft *Provisions—Targeted Improvements* (Exposure Draft) in November 2024, with a comment deadline of 12 March 2025. The Exposure Draft proposes amendments to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

2. At this meeting, the IASB will discuss feedback on the Exposure Draft proposals. We are not asking the IASB to make decisions at this meeting. However, comments from IASB members will help us develop recommendations for the direction of this project.

3. Agenda Paper 22 *Provisions—Targeted Improvements—Exposure Draft feedback—Overview* provides an overview of the Exposure Draft proposals, the sources of feedback and the key messages in the feedback. It also explains the terms we have used to quantify the number of stakeholders expressing a view.

4. This paper summarises feedback on proposals relating to the rate an entity uses to discount future expenditure to its present value.

5. This paper summarises the main matters raised by respondents on these proposals. We will include feedback on more minor and drafting matters in papers we prepare for future IASB discussions.

Contents of this paper

6. The paper summarises feedback on the proposals on:

   (a) which discount rate to use (paragraphs 8–38); and

   (b) what information to disclose about the discount rate used (paragraphs 39–45).

7. A question following paragraph 45 invites IASB members to ask questions and comment on the feedback summarised in this paper.

Which discount rate to use

Exposure Draft proposals (paragraphs 47-47A)

8. IAS 37 requires an entity to measure a provision at the best estimate of the expenditure required to settle its present obligation, and to discount that expenditure to its present value if the time value of money is material. IAS 37 does not specify whether the discount rate(s) used should reflect the risk that the entity will not settle the obligation (‘own credit’ or ‘non-performance’ risk).

9. The Exposure Draft proposes to specify that the discount rate(s) used should exclude non-performance risk:

(a) paragraph 47 of the Exposure Draft proposes to require the discount rate to be a pre-tax rate (or rates) that reflect(s):

(i) current market assessments of the time value of money, represented by a risk-free rate; and

(ii) risks surrounding the amount or timing of the expenditure required to settle the obligation if those risks are not reflected in the estimates of the future cash flows.

(b) paragraph 47A of the Exposure Draft states that the rate(s) should not reflect non-performance risk.

10. The Exposure Draft proposes to add no application guidance to IAS 37 on how an entity determines an appropriate risk-free discount rate. However, paragraph BC82 of the Basis for Conclusions on the Exposure Draft states that:

> BC82 Typically, entities determine an appropriate risk-free rate by reference to an observable market proxy for a risk-free rate, such as the current yield on a low-risk government bond in a currency consistent with that of the provision. In some cases, an entity might adjust that yield—for example, to compensate for differences between the duration and liquidity of the investment and those of the provision. However, the IASB does not expect all entities to make such adjustments.

11. The proposed amendments would most affect entities with large long-term provisions—typically the asset decommissioning and environmental rehabilitation provisions of entities operating in oil and gas, mining and energy generation sectors. At present, practice among entities in these sectors varies, with some entities using risk-free discount rates and others using (higher) rates adjusted to reflect their own credit risk.

Feedback

Agreement with the proposal

12. Many respondents comment on the proposal to require entities to exclude non-performance risk, with most saying they agree with it. The respondents who agree include:

    (a) all the users of financial statements and regulators commenting;

    (b) almost all the accounting firms, national standard-setters and accountancy bodies commenting; and

    (c) almost all the preparers of financial statements commenting—other than those from Canadian oil and gas companies.

13. Almost half of these respondents do not explain their reasons for agreeing or provide any additional comments.

14. Of those respondents who do give reasons, many say a requirement to exclude non-performance risk would bring more consistency in how entities determine their discount rates. These respondents say the proposed requirement would reduce diversity in practice (described in paragraph 11) and improve comparability.

15. Some respondents say omitting non-performance risk adjustments reduces the subjectivity of the discount rates used. These respondents say that varying assumptions and methodologies can be used to calculate non-performance risk adjustments, and the required adjustments can be subject to a high degree of measurement uncertainty, creating opportunities for manipulation.

16. Some respondents say excluding non-performance risk results in better accounting outcomes. In particular:

(a) *including* non-performance risk could result in a counterintuitive outcome—an entity with a higher credit risk would recognise a lower amount of provision.

(b) *excluding* non-performance risk is consistent with IAS 37's underlying assumption that an entity will settle an obligation by fulfilling (rather than transferring) it. A national standard-setter (in Asia-Oceania) and a preparer (in the oil and gas industry in Europe) say provisions are different in nature from most other liabilities as they generally cannot be traded.

17. A group of European academics says it views as 'sound' the conceptual arguments for excluding non-performance risk set out in Appendix B to the Basis for Conclusions on the Exposure Draft.

18. A few national standard-setters say a requirement to exclude non-performance risk is consistent with the requirements in other IFRS Accounting Standards, namely:

(a) paragraph BC134 of the Basis for Conclusions on IAS 19 *Employee Benefits,* which states that '…the discount rate should not reflect the entity's own credit rating, because otherwise an entity with a lower credit rating would recognise a smaller liability'.

(b) IFRS 17 *Insurance Contracts,* which requires non-performance risk to be excluded from the measure of an insurance contract liability.

19. Some respondents comment on the practicability of the proposal:

(a) a few respondents (preparers and national standard-setters) say the proposed requirement would make determining discount rates simpler and less costly.

(b) a preparer (in the oil and gas industry in Europe) says it already uses a risk-free rate to discount provisions, and an accounting firm says a requirement to use a risk-free rate would be consistent with prevailing practice.

Disagreement with the proposal

20. Some respondents disagree with the proposal to require entities to use a risk-free discount rate. These respondents are primarily from Canada—the Canadian Accounting Standards Board (AcSB) and several Canadian preparers of financial statements, mostly in the oil and gas industry—along with a few other respondents of various types and from various jurisdictions.

Divergence from US GAAP

21. Respondents from Canada express a concern that, if Canadian entities are required to measure provisions using a risk-free discount rate, they might face a competitive disadvantage when raising capital in the US market.

22. These respondents note that a requirement to use a risk-free rate would create a divergence between the requirements for measuring asset decommissioning obligations in IAS 37 and those in US Generally Accepted Accounting Principles (US GAAP). Under US GAAP, an entity measures asset decommissioning obligations using a credit-adjusted discount rate. Therefore, entities using risk-free discount rates report larger provisions than similar entities reporting under US GAAP.

23. Respondents say that this difference could result in a misperception of the financial health of Canadian entities, reducing their attractiveness to investors, particularly when compared to similar entities reporting under US GAAP.

No need to standardise practice

24. The AcSB argues that there is no need to require all entities to use risk-free discount rates. It acknowledges diversity in practice in Canada, but adds that the information entities disclose is sufficiently robust and transparent to ensure that differences in practice are well understood by investors:

> Notably, industry practices in Canada vary, with many sectors traditionally using a risk-free discount rate. However, certain industries, such as the Canadian oil & gas sector, have developed industry-specific practices that better meet the information needs of users within that sector. While these approaches are tailored to specific industries, they reflect broader practices in Canada, where variations in discount rate usage are typically accompanied by robust and transparent disclosures. This transparency has helped ensure that differences in practice are well understood by market participants, minimizing potential disruptions. *CL30 Accounting Standards Board (AcSB) [Canada]*

Practicability and effectiveness of the proposed requirement

25. A few respondents express concern about the practicability and effectiveness of the proposed requirement:

    (a) an accounting firm says a directly observable risk-free rate is typically not available in the market, meaning entities would continue to make varying adjustments when estimating a rate.

    (b) the respondents from Canada say the proposed requirement might not achieve the comparability the IASB is seeking because entities will not all apply the same rates. Some entities will reflect risks specific to the liability in the cash flows, while others might reflect those risks in the discount rate. Furthermore, each asset decommissioning obligation typically carries unique risk factors, such as geographical, operational, regulatory, and timing differences—all of which can lead to variations in the discount rates used

Relevance of risk-free discount rates

26. The Canadian preparers and an accountancy body (in Europe) say a risk-free discount rate:

    (a) does not reflect the true economics of a provision because such a rate:

        (i) does not reflect the cost of capital to the entity; and

(ii) can be volatile depending on the benchmarks used to determine it. A preparer says economic cycles and economic policies can 'temporarily distort the risk-free rate below or above the long-term time value of money'—citing zero or negative interest rates observed in the aftermath of the global financial crisis as an example.

(b) is inconsistent with the requirements in other IFRS Accounting Standards, including IFRS 3 *Business Combinations* (as discussed in paragraphs 28–31), IFRS 9 *Financial Instruments*, IFRS 13 *Fair Value Measurement*, IFRS 16 *Leases* and IAS 36 *Impairment of Assets*.

Suggestions for alternatives to the proposed requirements

27. In the light of their views:

(a) the Canadian respondents and an accountancy body (in Europe) suggest that the desired improvements in comparability and transparency could be achieved by requiring entities to disclose more information about the discount rates they have used (as the IASB proposed), without having to require all entities to use risk-free rates.

(b) an accounting firm suggests requiring a rate similar to that required by paragraphs 83–86 of IAS 19—namely, a rate determined by reference to the market yields on high-quality corporate bond or, if no deep market exists for such bonds, the market yields on government bonds. The accounting firm expresses a view that the resulting advantages of greater consistency and comparability would outweigh the disadvantages of applying a rate that is not a precisely risk-free. It adds that entities could be required to disclose a sensitivity analysis to give users of the financial statements a full analysis of the effects of the rates used.

Other comments

Interaction between IAS 37 and IFRS 3—day-two adjustments

28. Many respondents express concern about the interaction between IAS 37 and IFRS 3, which requires an entity to measure a provision assumed in a business combination:

    (a) *on the date the business is acquired*: at the fair value of the obligation, which can be estimated by discounting the expected future cash flows using a credit-adjusted discount rate.

    (b) *subsequently*: applying the requirements in IAS 37.

29. If after the date of acquisition, a provision is re-measured using a risk-free rate, the amount of the provision will increase, requiring a ‘day 2’ adjustment. This adjustment might be debited to property, plant and equipment (PPE) if it relates to the cost of decommissioning an item of PPE. Otherwise, it might be debited to the statement of profit or loss, resulting in a ‘day 2’ loss.

30. Respondents say recognising a ‘day 2’ loss would not provide relevant information to users of financial statements and ask the IASB take action to prevent those losses:

    (a) some respondents suggest providing an exception to the *initial* measurement principle in IFRS 3—so that at the date of acquisition, a provision assumed in the business combination would be measured applying the requirements of IAS 37, not at fair value.

    (b) a few other respondents suggest the opposite—providing an exception to the *subsequent* measurement principle in IFRS 3—so that after the date of acquisition, a provision assumed in a business combination would continue to be measured at fair value, not by applying the requirements of IAS 37.

31. A few respondents say if the IASB accepts the ‘day 2’ adjustments as a consequence of the new requirements, it should acknowledge this fact in the Basis for Conclusions and provide guidance or an illustrative example. In particular, these respondents suggest clarifying whether and how the adjustments should be reflected:

(a) in profit or loss; or

(b) as an adjustment to the carrying amount of the related asset. For example, if the related asset is a revalued item of PPE, should the acquisition cost or revaluation surplus/deficit be adjusted?

Real or nominal discount rate

32. Some respondents note that an entity can measure a provision using either:

(a) cash flows estimated at current prices and discounted at a *real* (not adjusted for inflation) discount rate; or

(b) cash flows estimated at forecast future prices and discounted at a *nominal* (adjusted for inflation) discount rate.

33. Respondents note that IAS 37 does not specify that an entity must use one or other of these approaches. An accounting firm notes that, although IAS 37 does not have an explicit requirement, Example 2 in Section D of the *Guidance on implementing IAS 37* illustrates information disclosed by an entity that has measured a provision using cash flows estimated using current prices and a real discount rate.

34. A few respondents say that, although the approaches would produce the same measure of the provision at initial recognition, they could lead to different allocations of year-on-year changes in the carrying amount of a provision between:

(a) operating and financing categories in the statement of profit or loss; or

(b) financing expense and the related asset when applying IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*.

35. Respondents provide various suggestions, including:

(a) specifying whether entities should use real or nominal rates—on the grounds that consistency is important;

(b) requiring entities to disclose whether they have used real or nominal rates; or

(c) requiring entities to be consistent in their approach to inflation—to use:

   (i) real rates to discount projected cash flows estimated at current prices; and

   (ii) nominal rates to discount cash flows estimated at projected future prices.

Non-performance risk in cash flows

36. Many respondents say that, although the Exposure Draft clarifies that non-performance risk should be excluded from the rate used to discount a provision, it does not clarify whether that risk should also be excluded from the estimates of the cash flows required to settle the provision. These respondents suggest stating explicitly that the estimates of the cash flows, like the discount rate, do not reflect non-performance risk:

(a) *to reflect existing practice.*
A preparer group (in Europe) observes that, in practice, entities generally exclude non-performance risks from both expected cash flows and discount rates.

(b) *to close a potential loophole.*
A national standard-setter (in Africa) says that, without such an explicit requirement, entities could include non-performance risk in the expected cash flows to achieve a similar outcome as including the risk in the discount rate.

Requests for guidance

37. Some respondents request guidance on determining a risk-free discount rate:

(a) an accounting firm suggests stating the objective for using such a rate to help entities 'determine an appropriate approximation'; while

(b) other respondents request guidance for specific situations:

(i) when a jurisdiction experiences economic uncertainties (for example, currency volatility and hyperinflation/high inflation);

(ii) when the interest rate is zero or negative; and

(iii) when government bonds in the currency of the liability are not sufficiently low-risk—whether an entity could use other proxies, such as the current yield on a high-quality corporate bond or the overnight borrowing rate.

38. Paragraph BC82 of the Basis for Conclusions on the Exposure Draft refers to liquidity adjustments—namely, adjustments an entity might make to the current yield on an observable market proxy to compensate for differences between the duration and liquidity of the investment and those of the provision. A few respondents suggest:

(a) providing guidance on when and how an entity should make such adjustments, instead of simply stating that 'the IASB does not expect all entities to make such adjustments'; or

(b) incorporating paragraph BC82 into IAS 37 or, at least, retaining it in the Basis for Conclusions accompanying the amendments when they are issued.

Information to disclose about the discount rate

Exposure Draft proposals (paragraph 85(d))

39. The Exposure Draft proposes to require an entity to disclose:

(a) the discount rate (or rates) used in measuring a provision; and

(b) the approach used to determine that rate (or those rates).

Feedback

Agreement with the proposed disclosure requirements

40. Many respondents say they agree with the proposed disclosure requirements. These respondents include those who disagree with the proposal to specify that the discount rate excludes non-performance risk.

41. Respondents generally say the proposed disclosure requirements would:

    (a) *improve comparability and transparency of the rates used.* Respondents note that entities will use different rates, even if they all aim to use a risk-free discount rate. A user group (in North America) says the proposed disclosure requirement is particularly important given the difference between the rates required by IAS 37 and those used by entities applying US GAAP.

    (b) *provide useful information to users.* A national standard-setter (in Asia-Oceania) says the proposed information would enhance users' understanding of the impact of the discount rate (and the methods used to determine it) on the measure of a provision. Two users say the proposed information would help investors 'make informed decisions in investment analysis, risk assessment, portfolio management, stewardship and engagement.' An accountancy body (in Europe) also describes the proposed information as 'important information for users that is currently missing'.

Disagreement with the proposed disclosure requirements

42. Two preparer groups (in Canada and Europe) disagree with the proposed disclosure requirements. They say entities that operate in multiple jurisdictions would have difficulty complying. Furthermore, the Canadian preparer group points to:

    (a) the often-immaterial effect of discounting; and

(b) the existing requirement in paragraph 125 of IAS 1 *Presentation of Financial Statements*.

43. A few preparer groups disagree specifically with the proposed requirement to disclose the discount rate (or rates) used to discount provisions:

(a) a preparer group in Europe says 'disclosing the 'discount rate(s), or even a range of rates, analysed by class of provision will not contribute any useful information for users of the financial statements.'

(b) another preparer group in Europe says it might be too extensive for groups that have provisions in multiple jurisdictions.

(c) a preparer group in Asia-Oceania notes that some other IFRS Accounting Standards—such as IFRS 16—do not require the disclosure of discount rates used.

44. A few respondents specifically disagree with the proposed requirement to disclose the approach used to determine the discount rate (or rates):

(a) a few respondents say such a disclosure is unnecessary—disclosure of the rate used is sufficient to allow users of financial statements to compare rates used. Additionally, a national standard-setter (in Asia-Oceania) notes that the IASB acknowledges in paragraph BC81(a) of the Basis for Conclusions on the Exposure Draft that 'practice to determine an appropriate risk-free discount rate is already well established…'.

(b) a preparer group (in Asia-Oceania) questions whether the benefits of the proposed disclosure would outweigh its costs because measurement of provisions is 'highly individual.'

(c) a national standard-setter (in Europe) expresses concern that entities will use boilerplate language, thereby not providing useful information. That respondent suggests requiring the information only in cases where the discount rate used reflects risks concerning the amount or timing of the expenditure required to settle the obligation.

Other comments and suggestions

45. A few other respondents suggest further disclosure requirements. Suggestions include:

(a) more detailed information about the components of the discount rate used—namely the *base* rate and any adjustments made—in addition to the *actual* rate as proposed.

(b) an explanation of the assumptions used in determining the discount rate.

(c) narrative information about how a change in the discount rate between reporting dates has affected the measure of a provision.

(d) a sensitivity analysis explaining how the amount of a provision would be affected by changes in the discount rate used, if the effect of discounting is significant—one respondent suggests also highlighting both the best-case and worst-case scenarios.

Question for the IASB

Question for the IASB
Do you have any questions or comments on the feedback reported in this paper?