Invitation to Comment:

Draft Comment Letter - Exposure Drafts S1: *General Requirements for disclosure of Sustainability-related Financial Information* and S2: *Climate-related Disclosures*

Deadline for completion of this Invitation to Comment:
Close of business Monday, 27 June 2022
Please submit to:
UKEndorsementBoard@endorsement-board.uk

UK Endorsement Board

The UK Endorsement Board (UKEB) is responsible for endorsement and adoption of IFRS for use in the UK and therefore is the UK's National Standard Setter for IFRS. The UKEB also leads the UK's engagement with the IFRS Foundation (Foundation) on the development of new accounting standards, amendments and interpretations. This letter is intended to contribute to the IASB's due process. The views expressed by the UKEB in this letter are separate from, and will not necessarily affect the conclusions in, any endorsement and adoption assessment on new or amended International Accounting Standards undertaken by the UKEB.

Introduction

The Department for Business, Energy, and Industrial Strategy (BEIS) have asked the UKEB to assist with the UK response to these proposals, specifically the overlap/impact between these standards and IFRS accounting standards. The objective of this Invitation to Comment is to obtain input from stakeholders on the UKEB's draft comment letter on the ISSB's Exposure Drafts S1: *General Requirements for Disclosure of Sustainability-related Financial Information* and S2: *Climate-related Disclosures*.

Who should respond to this Invitation to Comment?

Stakeholders with an interest in the quality of accounts that apply IFRS accounting standards and how they overlap with IFRS sustainability disclosure standards.

How to respond to this Invitation to Comment

Please download this document, answer any questions on which you would like to provide views, and return to UKEndorsementBoard@endorsement-board.uk by close of business on **Monday, 27 June** 2022.

Please note:

The UKEB welcomes your responses to any or all of the questions in this document. As an alternative to submitting this form you can also provide feedback on this consultation by emailing your comments directly to the above email address.

For information on UKEB privacy and other policies please refer to the final page of the document.

This document is set out in three sections:

UKEB UK Endorsement Board

Part A

Questions: [Draft] IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information*.

1. Do you foresee any conflicts or overlaps with requirements in IASB issued standards on application of the ED? Please provide your rationale and include any illustrative examples to help explain the potential implications for users of general-purpose financial statements.

Response:

Not in addition to those you highlight already in paragraphs B5, B7, B15 and B27.

We agree that there should be no 'overlaps' or 'conflicts' between the ED and IASB issued standards. CFA UK agrees that the two frameworks have to be consistent with one another, however, it must be recognised that they serve different purposes and so inherently will lead to different disclosures.

Financial reporting covers short time-frames, matters of very little uncertainty which can be ultimately quantified in one number. Sustainability disclosures will be more long-term and uncertain in nature and require more qualitative disclosures. There is value for investors from seeing the differences between these disclosures, provided that companies clearly explain the reasons for why these differences arise.

With this in mind, CFA UK disagree with some of your observations in paragraph B15 of your letter:

a) Liabilities: where future expenditure has been proposed and is planned for this should become a liability. Where it is likely but not yet sufficiently quantified or known it still should be discussed or noted and the scale or range of the potential cost discussed. Where the expenditure is likely but still sufficiently uncertain to become a balance-sheet item it should not be left ignored.
b) Funding sources: it will be useful for investors to know the proportion of the planned and likely expenditures under a) above for which external funding will or might need to be sought, respectively.
c) Confidentiality/Commercially sensitive information: we agree that the protections to companies available under IFRS companies should also apply to sustainability disclosures under IFRS.
d) Outcomes under previously disclosed plans: we anticipate that the parameters around sustainable disclosures could be highly dynamic in coming years. It is highly important for investors to be able to monitor companies' progress in this area by being able to reconcile the most recent progress with previously disclosed plans. We note your paragraph B15d) refers to your paragraph A15a but A15a does not exist.
e) Restatement of comparatives: same as for d) above. We note your paragraph B15e) refers to your paragraph A15a but A15a does not exist.

2. The term "sustainability" is not defined in the proposals. Do you think that a definition of the term "sustainability" would create a shared understanding of the boundaries of this term? *Please explain your rationale.*

Response:

We would hope a definition can be agreed on quickly and would suggest adoption of the UN's definition of sustainability (https://www.un.org/en/academic-impact/sustainability).

We would not want this question to delay determination and implementation of these important accounting standards; we do not regard it is an essential requirement for the standards to be effective.

3. To identify sustainability-related risks and opportunities paragraph 51 of the ED states that an entity "shall consider" external documents such as SASB standards, ISSB non-mandatory guidance, pronouncements of other standard setting bodies and risks and opportunities disclosed by other entities? *Do you agree with the alternative approaches suggested in the draft comment letter? Please explain your rationale and any alternative approaches would you suggest?*

   Response:

We assume this is a reference to your proposals in paragraph B31 of your draft letter which we support. We are as much concerned with companies greenwashing their disclosures by over-reporting 'positive' information as under-reporting 'negative' information. As you observe in your Appendix, neutrality is a qualitative characteristic of sustainability reporting as well as financial reporting.

It would be preferable for the standard to allow for the 'consideration' of other standards and frameworks without actually specifying any, similar to the approach taken in IAS8. Any specification of particular standards or frameworks (e.g. SASB) could be provided within accompanying guidance. This would better accommodate the fast-moving developments likely in this area over the coming years and would remove the risk that particular standards or frameworks become enshrined in practice and therefore difficult to change or deviate from as new IFRS Sustainability Standards are developed.

4. In relation to comparatives:

   a) Do you support the requirement, unless impracticable, to update comparative information with updated assumptions, and explain any difference between that and the number published in the prior year?

   b) Can you think of examples where under the proposed requirements you would choose to restate or not restate a comparative?

   c) How would you balance restatement that is useful to users versus the burden on preparers?

   Please explain your rationale.

Responses:

a) *Yes. Please see our response to question 1.*

b) *We think all comparatives should be restated. If they do not merit restatement then they probably should not have been disclosed in the first place. The requirement to restate increases the accountability on company directors to endeavour to make accurate disclosures. Where a company is requirement to make perennial restatements this is a useful red flag for investors particularly if sector peer companies are not needing to make the same restatements. It can be seen as a good indicator of a company's risk management processes. If there is no requirement to restate companies can continually make false or unrealistic disclosures and there would be no official record of this fact.*

c) *See our response to question 4b. above. If balance is required, it applies to the original disclosure not the requirement to restate it.*

5. When considering the proposals on materiality:

   a. Do you consider it necessary to use both the terms "significant" and "material" in the proposals? Could "material" be used in place of "significant"?

   b. Could the IASB definition of materiality for IFRS Accounting Standards be used instead of creating a new definition for ISSB purposes?

Please explain your rationale and include any illustrative examples to support your position.

Response:

a) *These terms should not be used inter-changeably. To provide the least room for confusion, we would recommend that the ISSB drop the 'significant' term completely and simply require all 'material' sustainability data to be disclosed. We note that the IASB's current narrow-scope amendment on disclosure of accounting policies is dropping the use of the term 'significant' and instead using the term 'material', because of the greater clarity around this term.*

b) *Yes, if it can be modified to reflect the qualitative nature of sustainability matters. The very long-term timescales and reduced certainty of many sustainability-related decisions mean that they require a different treatment than 'material' issues under traditional IFRS, which is usually judged in the context of, for example, a percentage of profits, revenues or assets. The definition of material in IAS 1 could be adapted for sustainability information as follows: Information is material if omitting, misstating or obscuring it could reasonably be expected to influence the decisions that the primary users of general purpose financial statements sustainability-related financial information make on the basis of those financial statements that information, which supplements and complements the provide financial information contained in about a specific reporting entity's financial statements in assessing the entity's enterprise value.*

6. The ED requires disclosures related to significant sustainability-related risks and opportunities in the value chain. *Is it clear what information is required from entities in*

the value chain, and how far this chain should be considered? Are there any practical difficulties that arise in relation to the value chain?

Response:

The disruption to supply chains that has and is being caused by covid is ample evidence of the importance of sustainability reporting in this area. *This is undoubtedly a complex area due to a wide range of issues – systems, data availability and quality, processes and consistency etc. As such, we believe it will be too difficult and counter-productive at this stage to seek to proscribe this with greater specification than the ISSB has done. We considered the merits of a temporary safe harbour for companies but ultimately decided against this as we were unsure how long the safe harbour might be for and fundamentally we believe companies should be incentivised to make the necessary investments in systems to consistently measure and monitor relevant data.* *We note the definition of 'business model' is provided by the ISSB on p40 in Appendix A of the ED and we have no comments on it.*

7. The Exposure Draft requires disclosures related to significant sustainability-related risks and opportunities in the business model. As users have emphasised the most useful disclosures are those directly linked to the entities business model, do you think the concept of business model should be given greater prominence in the proposals. *Please explain your rationale.*

Response:

We are content with the level of prominence given to the term 'business model' in the ED. We agree it is important: the business model drives the risks and opportunities and actions and strategies and plans and our experience as investors is that company disclosures are most useful and relevant when driven from a clear understanding of the business model and strategy. We note that for certain companies the clock is ticking on their need to transition for climate, so information about their business model, and any changes that may come to it, is critical.

8. The ED suggests in paragraph 66 that the sustainability-related financial proposals should be presented at the same time as the related financial statements? *Do you believe this is practical for your organisation? Do you believe this would delay your reporting timetable?*

Response:

We believe this requirement is of critical importance for investors. The two are much more decision-useful if they can be cross-referenced in the same time-period. *There is also greater management accountability for the sustainable disclosures if they are made in the same place as the financial disclosures. Also, if they are produced at the same time it also allows for the company's financial auditors to apply a consistency check to the sustainability disclosures which is valuable for investors as sustainability disclosures are otherwise unaudited information.*

If they are completed as a separate exercise then there is a risk that the sustainability disclosures are seen as a 'side-hobby' and not treated with the same rigour.

9. Overall, do you believe the proposals in the ED are successful in establishing a suitable "*global baseline for the assessment of enterprise value*"? Please explain your rationale.

Response:

It is important that a global baseline is established - both for multinational companies to ensure consistency within their sustainability disclosures and for investors to allow for international comparability across different companies and sectors. As the reporting infrastructure is at different stages of development in different countries, this means that we agree that the baseline cannot be set at the level of the most developed economies. That said, the global baseline should not be regarded as 'the lowest common denominator' and we would expect sustainability reporting from companies within the advanced economies to go beyond the global baseline. As investors we will find it interesting to compare the degree to which companies within the same sector choose to do this. We see this as an indicator of the quality of a company's risk management systems and potential vulnerability to climate and other risks versus its peers.

10. Overall, do you believe the proposals in the ED will successfully meet their objective to create "*more consistent, complete, comparable and verifiable sustainability-related financial information*"? Please explain your rationale.

Response:

We would have serious concerns that these goals will not be reached if:

- *Sustainability reporting is mot integrated into the financial reporting timetable;*
- *If there is permitted to be too much divergence between jurisdictions and/or insufficient acknowledgement of the challenges that some jurisdictions will face introducing sustainability reporting;*
- *Historic disclosures do not have to be restated;*
- *Companies are not forced to have to make uncomfortable disclosures as well as positive disclosures around opportunities.*

11. Are there any other comments you would like to make on Exposure Draft IFRS S1?

Response:

We believe that the ISSB has on the whole struck the right balance between investor requirements and costs on preparers. We would underline that we would expect the quality of disclosures to improve significantly over the first few reporting cycles as reporting infrastructure is built-out, best practice is cascaded through companies and sectors, auditors and systems investment starts to bear fruit and ultimately investors start to distinguish between companies with good disclosures and poor disclosures and factor this into their decisions. In recognition of this there should not be a quick jump for judgement after the first set of disclosures are produced.

Part B

[Draft] IFRS S2 *Climate-related Disclosures*.

Considering the requirements in IASB issued standards, do you foresee any conflicts or overlaps on application of the exposure draft? *Please provide your rationale and any illustrative examples to explain the potential implications for users of general-purpose financial statements.*

Response:

We refer to our answer to question 1 on the First Exposure Draft.

This question implies that matters of non-alignment are 'conflicts' or 'overlaps'. Owing to the inherently higher degree of subjectivity relating to sustainability disclosures, however, they will necessarily be more descriptive, uncertain and qualitative in nature than financial disclosures under IASB issued standards. We expect the information provided in company sustainability disclosures to complement the information provided in company financial reporting.

1. Do you foresee any conflicts or overlaps with other jurisdictions' climate-related standards which may cause issues for UK users of general-purpose financial statements? *Please provide your rationale and potential implications for users.*

Response:

Because much of the information to be disclosed under S2 is derived from TCFD recommendations, we would not expect a significant difference as many jurisdictions, including the UK, use or plan to use the TCFD framework as the basis of their climate disclosures.

To be clear we are supportive of TCFD and of the ISSB basing its standard upon it. Because the standard has already been adopted by many and has been applied in practice it has been tested and its value as a disclosures framework proven.

2. Should the term "climate-related risks and opportunities" be defined to create a shared understanding of the boundaries of this term? *Please explain your rationale. Can you suggest any suitable alternative definitions or guidance the ISSB should consider?*

Response:

CFA UK believe a definition might be helpful and we would fully support reference to the definitions of 'climate-related risk and opportunities' as set out in the TCFD framework. TCFD is the most widely applied framework globally with respect to climate and starting with their definitions would promote consistency.

A principle-based definition that can adapt to changing circumstances would allow a neutral assessment of both risks and opportunities by boards and management teams. This could help them to more easily navigate their corporate future, to choose the correct investment opportunities and product markets to target and to avoid or reduce activities in areas that could put the company's long-term viability at risk.

3. Do you have any comments on the likely benefits of implementing the proposals and the likely costs that the ISSB should consider in analysing the likely effects of these proposals?

Response:

We have no doubt that the costs of fully complying with the spirit and letter of these new disclosure requirements will be significant. However, provided these disclosure requirements are well targeted and focus only on what is needed – and applied with intelligence and judgement - we regard these costs rather as an investment which will allow companies to ultimately make better risk management decisions on those issues which not only affect them directly but also the world and its resources which they in turn rely on.

If the goals are realised the benefits will be significant. Ultimately capital will be better allocated and as a result more effectively put to work to facilitate the 'just transition' rather than become lost/wasted/stranded on or in unsustainable activities. We believe the benefits of having better (more complete, comparable, transparent and reliable) information should outweigh the costs of providing it. We believe these benefits extend to both users and preparers in providing information that is useful in making decisions, both initially and on an ongoing basis.

4. Do you have any comments on the costs of ongoing application of the proposals that the ISSB should consider?

Response:

See our response to question 4.

5. Are there any disclosure requirements included in the Exposure Draft for which the benefits would not outweigh the costs associated with preparing that information? Why or why not?

Response:

We believe the ED strikes an appropriate balance between the needs of both issuers and users. Ultimately, we believe that the disclosures sought will benefit both issuers to manage their long-term viability and risk and investors to allocate their capital towards more sustainable companies.

6. Are there any other comments you would like to make on Exposure Draft IFRS S2?

Response:

CFA UK strongly supports the establishment of the ISSB; its success will have a decisive and positive influence on the capital allocation process within markets and facilitate business transformation to a more sustainable future. The global relevance and penetration of its mission will accelerate the requirement of many companies to make difficult decisions concerning their long-term business models. These decisions will inevitably produce resistance around the globe to different aspects of these reforms and so it is critical that ISSB is able to demonstrate that its own governance is robust and that appropriate due process is followed.

As the EDs were issued only by the Chair and Vice-Chair of the ISSB before a full board had been appointed, they have not had the benefit of a public board debate process which would be expected as part of the ISSB's robust governance processes, which are in turn expected from the IFRS Foundation. CFA UK therefore believes it is essential to delay the issuance of the final standards until a fully quorate board is able to deliberate upon them, even if this means a delay and even potentially the re-issuance of the draft standards. We believe this is preferable to a potential situation in which certain aspects of any final standards come to attract significant criticism and the ISSB's reputation is attacked as a consequence for having rushed due process on such an important reporting regime.

UKEB UK Endorsement Board

Part C

General Questions regarding both [Draft] IFRS S1 and S2

1. Following finalisation of these exposure drafts,

   a) how much lead time would your organisation require to be able to implement them?

   b) Do you believe phased effective dates for either the standards or particular elements of the proposed standards would be helpful? If so, for which elements and how would you phase the timing?

   Response:

   This question is not relevant to CFA UK.

2. Do you have any other comments on the ISSB's proposed due process for issue of the final standards?

   Response:

   No further comment.

Thank you for completing this Invitation to Comment

Please submit this document

by close of business on Monday 27 June to:

UKEndorsementBoard@endorsement-board.uk

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