The ISSB Standards – June 2023: An Incomplete Guide to the Future of Sustainability Reporting

By Alan Willis, FCPA, FCA

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Landmark News Headline and Some Key Messages

Monday, June 26, 2023, marked a rare and unforgettable milestone – a landmark in the evolution of corporate financial reporting, comparable to the adoption of International Financial Reporting Standards (IFRS) for financial statements by the International Accounting Standards Board (IASB) in 2001, and the SEC's 1980 introduction of the MD&A (Management's Discussion and Analysis).

On June 26, 2023 the International Financial Reporting Standards Foundation's International Sustainability Standards Board (ISSB) published its first two standards: "IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information" and "IFRS S2 Climate Related Disclosures – achieved after less than two years' work by the ISSB, established in November, 2021. This is unprecedented speed in the world of financial standards setting!

Context

These two standards were developed in response to increasing calls, especially by investors, for a single global baseline of standards for reliable, comparable and timely disclosures about sustainability issues, risks and opportunities that affect or may in future affect a company's prospects – its cash flows, access to or cost of financial capital.

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Over the last decade or more, large investors have increasingly sought decision-useful sustainability and climate change-related information in corporate financial reporting. Like companies as report preparers, investors as report users had been becoming increasingly frustrated by the alphabet soup of standards, guidelines and recommendations about a company's sustainability-related disclosures. The ISSB Standards are the response by the International Financial Reporting Standards Foundation (IFRS Foundation) to these calls for convergence among the leading sets of sustainability-related financial disclosure standards, guidelines and proposals,

each with distinct but sometimes overlapping objectives and features – a confusing and inefficient landscape for report users and prepares alike.[1]

Target Report Users

Unlike sustainability-related disclosures to stakeholders in general, many of whom are typically most interested in a company's current and anticipated future impacts on people and the planet, information disclosed in accordance with the requirements of IFRS S1 and S2 is specifically intended to be useful to primary users of a company's financial reporting package, along with its financial statements and other components such as the MD&A in the US and Canada. Such users are typically investors, as well as lenders and creditors, i.e., providers of financial capital (plus debt rating agencies and financial analysts).

Many well-meaning sustainability advocates appear not to realize that these standards DO NOT (and are not intended to) guide disclosures of interest to broader stakeholder categories or society in general about the current and likely future impacts on the planet and people caused by a company, its supply chain and its products or services. Since 2000, sustainability reporting of this type, already widespread among large public companies around the world, has been guided principally by the GRI Standards (originally GRI Sustainability Reporting Guidelines). These were never intended or designed to satisfy the particular decision-making information needs of investors. Indeed, typical sustainability reports – lengthy and laden with a wide range of detailed disclosures – are not investor-friendly in presenting the information most useful to primary users of financial reporting.

Mandatory, Not Voluntary

The IFRS S1 and S2 standards have not yet been officially adopted and made mandatory in any national or regional jurisdiction (e.g., by changes to company law, securities regulation or stock exchange listing rules), but they are designed to be followed by all public companies worldwide for sustainability-related financial disclosures that are expected will soon be required alongside the financial statements in a public company's annual financial reporting package. This is the package sent to shareholders and filed with capital market regulators or called for by stock exchange listing requirements.

Hitherto, any reporting by companies about sustainability and climate change has been largely voluntary (except in the EU, since the 2014 Non-Financial Reporting Directive[2]). But there has been increasing use by companies of the GRI Standards for sustainability reporting to stakeholders and society in general, and use of one or more sets of widely accepted investor-focused standards, guidelines or recommendations such as those of the SASB, the TCFD and the IIRC for the benefit of providers of financial capital. Such reporting has not been a component of periodic mandatory financial reporting; it has typically occurred separate from and at a much later date than publication of a company's financial statements. Therefore, even if subjected to some degree of external assurance, this reporting has not been subject to monitoring and enforcement by any regulatory authority (unless the reported information has been located in a company's MD&A).

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[1] The need for such convergence was foreseen in my summer 2019 article for *ThinkTWENTY20*, see https://thinktwenty20.com/docs/Enhancing_Relevance_IFAC.pdf.

[2] The NFRD is being replaced by the Corporate Sustainability Reporting Directive and accompanying disclosure standards, see https://finance.ec.europa.eu/capital-markets-union-and-financial-markets/company-reporting-and-auditing/company-reporting/corporate-sustainability-reporting_en.

Get Started Now

A key message to all companies is to "get started now" in preparing to make the sustainability-related disclosures called for by IFRS S1 and S2 an integral part of their regular annual financial reporting package. For companies that are already regular sustainability and/or climate change reporters – especially those that already use the TCFD Recommendations – application of and compliance with the ISSB standards will be less challenging than for others that, for example, may not yet have well-established data collection systems and controls.

A recent consultancy blog recommended: "Organizations should begin evaluating their internal systems and processes for collecting, aggregating, and validating sustainability-related information across the company and its value chain. The priority should initially be on climate-related data and information, in particular the calculation and reporting of greenhouse gas (GHG) emissions. Given the IFRS Sustainability Standards are intended to be auditable, it is important that organizations invest time and resources to establish robust systems and controls to gather and report their climate-related metrics and targets."[3]

No Mention of ESG!

It's important not to delay or be distracted on account of all the current "noise" and push-back in jurisdictions like the US about the widespread but ill-defined acronym "ESG." This originated in 2004 in reference to three aspects of corporate performance deemed to be of special interest to investors, namely environmental and social performance and the quality of governance related thereto. But since ESG is not mentioned anywhere in IFRS S1 or S2, or in the several guidance sources referred to in the standards, it is not mentioned again in this article!

In short, the advent of global standards for mandatory financially-relevant sustainability disclosures expressly for the benefit of investors and other capital market actors alongside financial statements in annual corporate reporting is, by any measure, a landmark event.

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About This Article

Since June 26, 2023, many summaries and commentaries on IFRS S1 and S2 have been published, especially by law firms, the major accounting firms and several consultancies and think-tanks.[4] This article does not attempt to duplicate this existing broad literature, but instead examines more closely the objectives of IFRS S1 and IFRS S2 and some key concepts and definitions in the standard, such as identification of sustainability-related risks and opportunities, materiality and material information, use of the TCFD four-pillar architecture for disclosure content requirements, how the standards are expected to become mandatory, interoperability and some other practical implementation requirements.

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[3] https://www.esgglobaladvisors.com/news-views/a-new-era-for-climate-governance-3-steps-boards-can-take-to-prepare-for-the-new-ifrs-sustainability-disclosure-standards/.

[4] The ISSB itself published a very informative and helpful Project Summary in June 2023, providing an overview of the requirements in both Standards. See https://www.ifrs.org/content/dam/ifrs/project/general-sustainability-related-disclosures/project-summary.pdf.

The article also flags two other important considerations, namely company oversight of ISSB-based disclosures in financial reporting (including audit committee review and CEO/CFO certifications), and data reliability, internal control and assurance implications.

"Get-ahead" Opportunities for a Beyond-Compliance Mindset

Finally, this article suggests that the required process for identifying sustainability-related risks and opportunities and reference to the guidance sources called for by the ISSB standards can, if executed with a creative, long-term, beyond-compliance mindset, lead to recognition of two significant opportunities to get ahead of the curve and the competition:

1. A company might identify ways to mitigate or eliminate some of its disclosable sustainability-related risks through actions to enhance its business model so as to reduce negative environmental and social impacts, and thus improve reputation, prospects and investor attractiveness - actions and innovations that might otherwise be overlooked.

2. A company might take pre-emptive actions that reduce adverse impacts on society and the environment (perhaps even lead to positive ones) in order to lessen the possibility that an environmental or social issue that today is not viewed as a material sustainability-related risk could become one tomorrow, perhaps due to new future regulation or tax measures. Such actions would no doubt also be beneficial to stakeholder relations and enhancement of "social license to operate."

These two opportunities represent a potential creative, competitive upside to what otherwise could be just a tedious, time-consuming compliance process.

Objectives of IFRS S1 and IFRS S2

At the outset, it is essential to understand the purpose of the ISSB standards – what they aim to achieve and what they do not. Yet, in the world of sustainability professionals, business executives, boards of directors and even perhaps some financial and accounting professionals, there is still some confusion about the objectives of these standards.

For example, they are not standards for measuring, assessing or reporting on a company's sustainability, whatever that might mean. They are not standards for measuring and reporting a

company's impacts on the planet and society – that is the realm of the GRI and its sustainability reporting standards. They are not standards for monetizing or quantifying and reporting a company's environmental or social externalities. They are not standards for forecasting or predicting future financial condition or the acceptability of future sustainability performance. And they are not standards applicable to financial statements – those are the IFRS issued by the IASB under the IFRS Foundation umbrella (or FASB's standards in the US).

The standards aim simply to enable a company to assess and report to stakeholders, in particular investors, on how environmental and social issues and risks, whether attributable to its own actions or to external causes, could impact future financial performance prospects and the financial condition portrayed in its financial statements – like an extension of what useful information in an MD&A aims to do.

The objectives of the first two ISSB Standards are reproduced in the box below:

"The objective of IFRS S1, General Requirements for Disclosure of Sustainability-related Financial Information, is to require an entity to disclose information about its sustainability-related risks and opportunities that is useful to primary users of general purpose financial reports in making decisions relating to providing resources to the entity."

"The objective of IFRS S2, Climate-related Disclosures, is to require an entity to disclose information about its climate-related risks and opportunities that is useful to primary users of general purpose financial reports in making decisions relating to providing resources to the entity."

IFRS S1 is basically an overarching standard that sets out broad requirements for a company's disclosures of information useful to primary users of its financial reports (investors, lenders and creditors) about the sustainability-related risks and opportunities that are specific to the company in question, other than those that, like climate change, are addressed in greater detail in a separate standard, such as IFRS S2.

The term "sustainability-related risks and opportunities" is not defined as such, but its meaning can readily be derived from the following text in Paragraph 2 of the S1 Standard, which is based on the "capitals" and "value creation" concepts found in the IIRC Integrated Reporting Framework[5]:

"Information about sustainability-related risks and opportunities is useful to primary users because an entity's ability to generate cash flows over the short, medium and long term is inextricably linked to the interactions between the entity and its stakeholders, society, the economy and the natural environment throughout the entity's value chain. Together, the entity and the resources relationships throughout its value chain form an interdependent system in which the entity operates. **The entity's dependencies on those resources and relationships and its impacts on those resources and relationships give rise to sustainability-related risks and opportunities for the entity."** (emphasis added)

This description of "sustainability-related risks and opportunities" clearly recognizes how a company interacts with the external world in which it functions and on which it depends. To the

[5] https://www.integratedreporting.org/news/integrated-reporting-concepts-are-embedded-in-the-issbs-inaugural-global-standards/.

extent that those interactions result in impacts (negative or positive) or present risks sooner or later to a company's cash flows, financial performance and prospects, investors need the information called for by IFRS S1 (and, regarding climate change, S2) to help understand those impacts and their financial implications. This is sometimes referred to as in "outside-in" reporting perspective.

Companies need to identify the sustainability aspects related to their business and its value chain that may give rise to disclosable risks and opportunities.

To the extent those interactions result in impacts by the company on its stakeholders, society, the economy and the natural environment, a company may also voluntarily choose to make disclosures about them and how they are managed. Typically, they do this in a separate sustainability report prepared and presented in accordance with the GRI Standards, or perhaps in an Integrated Report inspired by the IIRC Framework, though the latter was developed with the needs of "providers of financial capital" primarily in mind. This is sometimes referred to as an "inside-out" reporting perspective.

In other words, "sustainability-related risks and opportunities" are defined to be those "that could reasonably be expected to affect the entity's cash flows, its access to finance or cost of capital over the short, medium or long term," i.e., that could reasonably be expected to affect an entity's business and financial prospects.

IFRS S2 is a standard that specifically addresses the risks and opportunities related to the impacts on a company associated with climate change, the transition to a low carbon economy, and the greenhouse gas emissions of a company across its full value chain, that could reasonably be expected to affect its cash flows, its access to finance or cost of capital over the short, medium or long term. IFRS S2 largely embodies the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD), so will be readily familiar to companies that provide information in accordance with the TCFD Recommendations.

Readers who seek more detailed explanations and background to the ISSB's process and deliberations for creating IFRS S1 and S2 are strongly recommended to read not only the actual standards but also the Basis for Conclusions for each standard.[6]

Identification of Sustainability-related Risks and Opportunities

To make the disclosures called for in IFRS S1 about Sustainability-related Risks and Opportunities, i.e., those likely to be of interest to investors, it logically follows that companies need first to identify the sustainability aspects or topics related to their business and its value chain (both upstream suppliers and downstream users of its products and services) that may give rise to disclosable risks and opportunities.

As stated in Paragraph 11 of IFRS S1, "A complete set of sustainability-related financial disclosures shall present fairly all sustainability-related risks and opportunities that could reasonably be expected to affect an entity's prospects."

So How Is a Company to Achieve This?

For a sustainability aspect or topic for which a specific ISSB Sustainability Standard already exists, such as "Climate Change," a company would apply the specific standard, such as IFRS S2,

[6] See for example https://www.ifrs.org/content/dam/ifrs/publications/amendments/english/2023/issb-2023-c-basis-for-conclusions-on-ifrs-s1-general-requirements-for-disclosure-of-sustainability-related-financial-information-part-c.pdf.

to identify its sustainability-related risks and opportunities, step one in determining what disclosures it must make.

In the absence of such a specific standard, the company is **required** first to look to the disclosure topics in the SASB Standards and apply the metrics associated with those topics in making disclosures of material information (see below for discussion about "Materiality"). SASB disclosure standards are available for 77 industry sectors.

If this does not suffice in identifying company-relevant sustainability-related risks and opportunities, and determining appropriate disclosures relative to sustainability aspects and topics, then the company **may** look to and consider the appropriateness and applicability of other specified sources for guidance on the sustainability-related disclosures that are to be provided. Such sources include the CDSB Framework Application Guidance, the GRI Standards and the European Sustainability Reporting Standards.

IFRS S1 provides in Appendix B extensive, comprehensive practical guidance about applying the standard, including the process of identifying sustainability-related risks and opportunities and deciding what disclosures of material information about them are required.

An important practical provision in Appendix B states:

"An entity need not undertake an exhaustive search for information to identify sustainability-related risks and opportunities that could reasonably be expected to affect the entity's prospects. The assessment of what constitutes undue cost or effort depends on the entity's specific circumstances and requires a balanced consideration of the costs and efforts for the entity and the benefits of the resulting information for primary users. That assessment can change over time as circumstances change."

Therefore, companies are expected to do no more than is reasonable in their circumstances to identify the sustainability-related risks and opportunities relevant to them for which disclosures are required.

Materiality and Material Information

A key concept in financial reporting is materiality. IFRS S1 and S2 apply, with appropriate but slight modification, the same concept and definition of materiality as is used in the IASB IFRS for financial statements. The ISSB standards state: "An entity shall disclose material information about the sustainability-related risks and opportunities that could reasonably be expected to affect the entity's prospects." (paragraph 17)

And go on to state: "In the context of sustainability-related financial disclosures, information is material if omitting, misstating or obscuring that information could reasonably be expected to influence decisions that primary users of general purpose financial reports make on the basis of those reports, which include financial statements and sustainability-related financial disclosures and which provide information about a specific reporting entity." (paragraph 18)

Securities regulators in Canada and the US use a very similar concept and definition for required disclosures in financial reporting and related filings with securities regulators – familiar to all financial officers and corporate counsel who prepare financial statements and other financial filings.

This concept and definition of materiality is sometimes referred to as "financial materiality." It is of special importance for "outside-in" reporting by a company in order to decide what

information about its sustainability-related risks and opportunities could reasonably be expected to influence report users' decisions.

The financial reporting definition is in contrast to that used in "inside-out" sustainability reporting to stakeholders and the public, where, in the GRI Universal Standard, "material topics," for which disclosures are called for, are defined as topics that represent an organization's most significant impacts on the economy, environment and people, including impacts on their human rights.

It is noteworthy that, in addition to the two different materiality concepts applied in "outside-in" financial reporting and in "inside-out" sustainability reporting, the EU's CSRD and its ESRS[7] adopt an approach called "double materiality," under which a company must report both on how its business is affected by sustainability issues ("outside in") and how their activities impact society and the environment ("inside out").

TCFD-based Four Pillar Architecture

The disclosures required by both IFRS S1 and S2 (and presumably for any future ISSB standards for specific sustainability-related topics) are set out under the same four main pillars or headings as the 2017 Recommendations of the Task Force on Climate-related Financial Disclosures (TCFD), namely:

- *Governance*
- *Strategy*
- *Risk Management*
- *Metrics and Targets*

This is significant for at least two reasons. First, the TCFD comprised recognized experts from a range of relevant backgrounds, including data users (e.g., investors), data preparers (e.g., companies), "Big Four" accounting firms, debt-rating and corporate sustainability rating services, and capital market regulation. These were drawn from G20 countries and reflect the fact that the TCFD was established by the G20's Financial Stability Board, chaired by Mark Carney when he was Governor of the Bank of England. In other words, the TCFD, which was chaired by Michael Bloomberg, had very strong capital market-oriented credentials.

Second, the four-pillar framework, adopted following a public consultation and feedback process, represented a clear consensus as to the principal categories of climate-related information most sought by capital market actors, especially investors, as being material to financially-driven decision making.

The ISSB was directed from the outset by the IFRS Foundation, based on public feedback on its 2020 Consultation paper, to build its standards as much as possible off existing sets of investor-

[7] Corporate Sustainability Reporting Directive's European Sustainability Reporting Standards.

relevant disclosure standards and frameworks. The leading ones of these have since been brought under the IFRS Foundation umbrella, namely those of SASB, the CDSB, the IIRC and, most recently, the TCFD. Further, the ISSB was directed to make a climate-related financial disclosure standard its first priority.

Early on it must have become apparent that the four pillar TCFD framework for climate-related financial disclosures would be equally appropriate for standards related to any other type of sustainability topic and, indeed, for the overarching general standard for disclosure of sustainability-related information, which is now IFRS S1.

The result, as stated in paragraph 25 of IFRS S1 concerning Core Content disclosure requirements, is the following directive: "Unless another IFRS Sustainability Disclosure Standard permits or requires otherwise in specified circumstances, an entity shall provide disclosures about:

> (a) governance – the governance processes, controls and procedures the entity uses to monitor and manage sustainability-related risks and opportunities;
>
> (b) strategy – the approach the entity uses to manage sustainability-related risks and opportunities;
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> (c) risk management – the processes the entity uses to identify, assess, prioritize and monitor sustainability-related risks and opportunities; and
>
> (d) metrics and targets – the entity's performance in relation to sustainability-related risks and opportunities, including progress towards any targets the entity has set or is required to meet by law or regulation."

IFRS S1 then provides extensive detailed requirements and guidance as to what is called for under each of these four headings – modelled closely on what is called for in the TCFD Recommendations. Similarly, IFRS S2 provides clear guidance on what is expected for climate-related disclosures. Companies already applying the TCFD Recommendations in their climate-related reporting will be at a clear advantage in applying both IFRS S2 and perhaps, more broadly, IFRS S1.[8]

It is important to note that under Metrics and Targets, IFRS S2 requires disclosure of Scope 3 GHG emissions, a challenging requirement for many companies, and the use of scenario analysis in preparing disclosures about the resilience of strategy regarding climate change.

The IFRS Foundation has established a Jurisdictional Working Group to consider how best to promote and achieve uptake of the ISSB standards in their respective jurisdictions.

Business Model and Value Chain

Further, to grasp fully the intended meaning and implications of the disclosures called for in particular under Strategy and Metrics, but also under Governance and Risk Management, it is

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[8] In July 2023, the IFRS Foundation released a comparison of IFRS S2 with TCFD Recommendations: https://www.ifrs.org/news-and-events/news/2023/07/ifrs-foundation-publishes-comparison-of-ifrs-s2-with-the-tcfd-recommendations/.

helpful to keep in mind the definitions of two terms that are probably new to most financial reporting lexicons – "business model" and "value chain."

According to the definitions in Appendix A of IFRS S1, "Business Model" is "An entity's system of transforming inputs through its activities into outputs and outcomes that aims to fulfil the entity's strategic purposes and create value for the entity and hence generate cash flows over the short, medium and long term."

"Value Chain" is "the full range of interactions, resources and relationships related to a reporting entity's business model and the external environment in which it operates. A value chain encompasses the interactions, resources and relationships an entity uses and depends on to create its products or services from conception to delivery, consumption and end-of-life, including interactions, resources and relationships in the entity's operations, such as human resources; those along its supply, marketing and distribution channels, such as materials and service sourcing, and product and service sale and delivery; and the financing, geographical, geopolitical and regulatory environments in which the entity operates."

These two terms, unheard of in IFRS for financial statements, are essential for understanding the concept of sustainability and how sustainability-related risks and opportunities arise from the inputs, outputs and impacts associated with a company's business when viewed through a full life cycle lens. They are also helpful terms for understanding the IIRC Integrated Reporting Framework and a company's impacts on the six "capitals" on which business models and value creation depend.[9]

Adoption in Global Reporting Jurisdictions

Like the IFRS developed and issued by the IASB, the ISSB's sustainability-related financial disclosure standards, such as IFRS S1 and S2, will be useful to intended users only to the extent that they become mandatory for application in jurisdictions around the world. Decisions, rules, regulations, directives or legislation to achieve this are outside the powers of the ISSB and the IFRS Foundation.

IOSCO (International Organization of Securities Commissions) has since 2020 indicated its strong support for the creation of the ISSB, the development and release of its standards for disclosure of sustainability-related financial disclosures and the adoption of these as mandatory requirements in securities jurisdictions around the world – the global baseline to meet the needs of capital markets. IOSCO's endorsement of the first two ISSB standards, announced on July 25, 2023,[10] was a crucial step in promoting their uptake in reporting jurisdictions worldwide.

A key objective of the ISSB is to reduce the complexity associated with various sustainability disclosure frameworks and standards, to address the reporting burden for companies and improve the efficiency of the reporting system.

The IFRS Foundation has established a Jurisdictional Working Group (JWG) to consult with major jurisdictions in Europe, Asia and North America and consider how best to promote and achieve uptake of the ISSB standards in their respective jurisdictions.

[9] https://www.integratedreporting.org/news/integrated-reporting-concepts-are-embedded-in-the-issbs-inaugural-global-standards/.

[10] https://www.iosco.org/news/pdf/IOSCONEWS703.pdf.

In the meantime, the SEC in the US is expected to release in October 2023, or at least in the Fall of 2023, its own new rule ("The Enhancement and Standardization of Climate-Related Disclosures for Investors") regarding financial statement and other 10K disclosures of climate-related financial information, incorporating where possible the recommendations of the TCFD. In the EU, starting in 2024, the ESRS under the CSRD are expected to embody the double-materiality disclosure standards developed by EFRAG,[11] including those relating to climate change.

In Canada, the CSA appear to be playing "wait and see" regarding their proposed climate-related disclosure instrument NI 51-107, "Disclosure of Climate Related Matters," issued in October 2021, and the adoption of the ISSB Standards. On July 5, 2023, the CSA issued a statement welcoming the new ISSB standards,[12] and indicated that "CSA staff intend to conduct further consultations to adopt disclosure standards based on ISSB Standards, with modifications considered necessary and appropriate in the Canadian context." It remains to be seen what influence Canada's recently established Canadian Sustainability Standards Board will have on what Canadian regulators (CSA) eventually put in place to enforce the ISSB standards, with or without modification, to reflect Canadian circumstances.

It is not known how soon the ISSB standards, or even just IFRS S2 regarding climate change, will be adopted and become mandatory in various jurisdictions. It looks likely that, in the near future, despite calls for convergence among the leading, recognized standards for sustainability-related financial disclosures, there will continue to co-exist the ISSB standards, the EU's ESRS standards and, for climate-related disclosures, the new SEC rules. Not a perfect scenario, but at least a step in the right direction. It may not be until 2025 before ISSB-based disclosures (for the 2024 financial reporting period) appear in mandatory annual filings.

Interoperability

The ISSB seems to be very aware of the need to avoid duplication and overlap among sustainability-related disclosure standards as adopted in different jurisdictions, both to minimize confusion between them and to enhance efficiency for companies in collecting and processing data for a given sustainability issue or disclosure topic called for under multiple standards. The quest is, therefore, in progress for "interoperability," so that there can be some degree of alignment between disclosure standards and related data and presentation requirements.

As the IFRS Project Summary explains:

"A key objective of the ISSB is to reduce the complexity associated with various sustainability disclosure frameworks and standards, to address the reporting burden for companies and improve the efficiency of the reporting system.

"The ISSB is working with jurisdictional representatives through the Jurisdictional Working Group and with organizations, including the European Commission, the European Financial Reporting Advisory Group (EFRAG) and the Global Reporting Initiative (GRI) to help achieve this objective.

"An important priority has been to establish interoperability between IFRS S1 and IFRS S2 and the European Sustainability Reporting Standards (ESRS), the GRI Standards and other major

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[11] European Financial Reporting Advisory Group.

[12] https://www.newswire.ca/news-releases/canadian-securities-administrators-statement-on-proposed-climate-related-disclosure-requirements-816779906.html.

jurisdictional requirements. For example, efforts have been made to identify common disclosures in ESRS and IFRS S2, and ensure the requirements are aligned wherever possible, to prevent duplicative reporting."

It is significant that the GRI and its reporting standards are involved in this effort because, in many companies that have long-established systems for collecting sustainability-related data needed for internal management purposes and/or for disclosures in their sustainability reporting under the GRI Standards, the same or similar data and systems may well be called for under ISSB, the EU or SEC disclosure requirements.

This involvement also acknowledges the reality that the GRI Standards are an ISSB-referenced resource (in IFRS S1, Appendix C) to help companies in their identification of sustainability-related risks and opportunities.

Some Implementation Practicalities

IFRS S1 addresses several important practicalities, four of which are noted here. These considerations help to bring to sustainability-related financial reporting the rigour associated with presentation of financial statements in accordance with IFRS (or other GAAP, such as FASB standards).

1. Location of Disclosures

A company is required to present the required disclosures as a part of its normal financial reporting package, such as in its MD&A or similar report that is required to accompany the financial statements for the reporting period in question. This requirement has important implications for oversight and approval policies and processes, including, in certain jurisdictions, CEO/CFO certification of financial filings and audit committee review.

2. Timing of Reporting

IFRS S1 provides that a company's sustainability-related financial disclosures be published at the same time as its financial statements, and for the same reporting period. This may be challenging for companies that have been accustomed to issuing separate sustainability reports or climate-related reports at a much later date than issue and filing of general-purpose financial reports.

In the first year of application of the standards, Appendix E of IFRS S1 states that a company is permitted to comply only with IFRS S2, i.e., provide only climate-related disclosures to accompany financial statements and provide the full sustainability-related financial disclosures called for by IFRS S1 no later than nine months from the end of the prior financial reporting period. This helpful relief may be subject to amendment by a regulatory body in any jurisdiction that adopts the standards.

3. Comparative Information and Initial Application of the Standards

IFRS S1 states that "Unless another IFRS Sustainability Disclosure Standard permits or requires otherwise, an entity shall disclose comparative information in respect of the preceding period for all amounts disclosed in the reporting period. If such information would be useful for an understanding of the sustainability-related financial disclosures for the reporting period, the entity shall also disclose comparative information for narrative and descriptive sustainability-related financial information."

Appendix B provides detailed implementation guidance about comparatives.

Regarding initial application of the standards, Appendix E provides two reliefs: first, in the first year of applying IFRS S1 companies will only be required to address and provide disclosures related to climate related risks and opportunities; and second, companies will not be required to provide comparatives in the first annual reporting period in which they apply the standards, addressing only climate-related disclosures, nor in the second annual reporting period after which it applies IFRS S1(except for climate-related disclosures, for which in the second year comparatives will be required).

4. Statement of Compliance
This requirement is self-explanatory, but noteworthy because it provides for two allowed disclosure exemptions.

To quote from IFRS S1: "An entity whose sustainability-related financial disclosures comply with all the requirements of IFRS Sustainability Disclosure Standards shall make an explicit and unreserved statement of compliance.

"An entity shall not describe sustainability-related financial disclosures as complying with IFRS Sustainability Disclosure Standards unless they comply with all the requirements of IFRS Sustainability Disclosure Standards. This Standard relieves an entity from disclosing information otherwise required by an IFRS Sustainability Disclosure Standard if law or regulation prohibits the entity from disclosing that information….

"This Standard also relieves an entity from disclosing information about a sustainability-related opportunity otherwise required by an IFRS Sustainability Disclosure Standard if that information is commercially sensitive as described in this Standard….

"An entity using these exemptions is not prevented from asserting compliance with IFRS Sustainability Disclosure Standards."

Many believe new ways are needed to hold corporations accountable for their impacts on the well-being of the planet and society.

What is deemed to be "commercially sensitive" is an issue that may cause some controversy, however. Appendix B (34-37) provides some clarity of what may be considered "commercially sensitive" and how use of this exemption is to be disclosed.

IFRS S1 does not specify who is to sign or approve the statement of compliance. This might, therefore, be a designated officer, such as the company's CEO or CFO, or a director, such as chair of the board or the audit committee. Oversight and approval of disclosures is discussed below.

There are two further topics of importance that are not part of the ISSB standards but which are important implementation practicalities and merit some comment: oversight and approval of disclosures, and data and systems integrity, internal control and assurance.

Oversight and Approval of Disclosures
In the US and Canada, financial reporting by public companies is subject to various degrees of oversight and approval. Besides mandatory CEO and CFO certifications as to the fairness of financial reporting,[13] audit committees are required to review a company's financial statements

[13] https://www.osc.ca/en/securities-law/instruments-rules-policies/5/52-109.

and related MD&A. This raises the question as to whether, in addition to being financially literate (as required by securities regulators), audit committee members also need to be "sustainability" literate, or at least "climate change" literate.

The question also arises as to whether, in Canada and the US, CEOs and CFOs, certifying the fairness of a company's financial reporting, will in future be required to certify the fairness of sustainability-related or climate-related financial disclosures included as components of financial reporting that, like MD&As, accompany the financial statements.

Data & Systems Integrity, Internal Control and Assurance

In the US and Canada, and in other jurisdictions, financial reporting calls for integrity of the supporting data and the systems for capturing and processing it and, and its use in preparing financial statements in accordance with IFRS (or other GAAP).

There are already well-established regulatory provisions in the US and Canada to ensure and report on the adequacy of internal controls over financial reporting (ICFR) and of disclosure controls and procedures (DC&P). It must now be asked whether these concepts and regulatory provisions – including those for related CEO and CFO certifications of controls – will now also apply to the sustainability-related financial disclosures that in future are to be regarded as part of companies' annual financial reports and regulatory filings. And, in March 2023, COSO published new guidance for effective internal control over sustainability reporting.[14]

Prudence would suggest that companies should assume that such requirements will be introduced by regulators sooner or later, and therefore take the necessary steps to extend controls over reporting so as to protect officers and directors from the risk of a company providing material sustainability-related financial information that turns out to be misstated or misleading – a risk that in Canada at least, if proven, can result in liability for directors and officers under provincial securities law.

Companies need to consider and report to investors how sustainability-related issues and risks may have an impact on a company's prospects for future value creation.

Internal and external auditors, too, play important roles regarding the integrity of data and reporting systems and controls. As a reporting standard, IFRS S1 is silent as to the need for independent assurance about sustainability-related financial disclosures, but the recent issue by the IAASB of a draft standard, ISSA 5000,[15] for assurance regarding sustainability reporting suggests that, as called for by many investors and other report users, independent assurance, whether limited or reasonable, will increasingly be called for.

Further, IFRS S1 embodies the qualitative characteristic of verifiability so that it could be referred to by independent assurance providers seeking suitable criteria for auditing sustainability disclosures asserted to have been prepared and presented in compliance therewith.

[14] https://www.coso.org/Shared%20Documents/COSO-ICSR-Press-Release.pdf.

[15] "The IAASB is excited to announce that it has approved, by unanimous vote, the draft International Standard on Sustainability Assurance (ISSA) 5000, *General Requirements for Sustainability Assurance Engagements*, for public consultation. The consultation will be open from early August until early December 2023." June 28, 2023.

Preserving Our Planet for the Future

Sustainability is about preserving the planet for the benefit of future generations.[16] Taking care of the well-being and rights of people today and tomorrow is essential too.

Corporations were originally created to harness private capital to meet societal needs and desires, but were held legally accountable only to shareholders for stewardship of their invested funds and promoting the best interests of the corporation[17]. Many believe new ways are needed to hold corporations accountable for their impacts on the well-being of the planet and society. Part of the answer is to enhance the annual financial reporting by companies to those who entrust or are considering entrusting their financial capital to them, and thereby provide a wider spectrum of decision-useful information to capital markets.

Providers of financial capital need more than just financial statements to be able to satisfactorily evaluate a company's performance and prospects, the short- and long-term risks to its business model for value creation, its strategy and risk management and the adequacy of its governance processes and controls. Companies need to consider and report to investors how sustainability-related issues and risks, broadly defined, may have an impact on a company's prospects for future value creation.

Demand for reliable information for investors (not just greenwash) about the current and possible future business and financial effects of entity-relevant sustainability-related issues has been mounting for more than a decade. Twenty years ago, the advent of IFRS was a landmark in achieving worldwide comparability and reliability in financial statements. Since then, the same types of globally-recognized standards have become essential for reporting decision-useful sustainability-related information to investors alongside financial statements as an element of financial reporting. Such reporting needs to be in tandem with what the GRI Standards require for reporting to stakeholders and the public about a company's impacts on the planet and society.

The ISSB standards are not intended to guide sustainability disclosures about entity impacts on the planet and people, but they are at least a timely step in a useful direction for information needed in capital markets.

Could all this be a catalyst for new insights into value creation, planetary resources and social justice?

Companies will now be **required** to identify and think about their sustainability impacts as business risks or opportunities as the first step in deciding what disclosures to make to investors about those likely to have material financial impacts, explain what they are doing to manage them, and their implications for future financial prospects.

Could this, in turn, be a catalyst for new C-suite insights into value creation, planetary resource limits and social justice? Opening the door to new, enlightened and future-looking conversations in capital markets about the purpose of a company, its business model, its

[16] In 1987, the United Nations Brundtland Commission defined sustainable development (now shortened to sustainability) as "meeting the needs of the present without compromising the ability of future generations to meet their own needs."

[17] Section 122 (1) of the Canada Business Corporations Act now provides that when acting with a view to the best interests of the corporation the directors and officers of the corporation may, consider, but are not limited to, the following factors: (a) the interests of i) shareholders, (ii) employees, (iii) retirees and pensioners, (iv) creditors, (v) consumers, (vi) governments, and (b) the environment.

governance, the resources and relationships on which it depends for value creation, perhaps even its accountabilities?[18] In the next decade or two, capital markets will hopefully move into a new era of alignment with sustainability principles and imperatives, and allocation of capital needed for the achievement of global sustainability goals.

The ISSB standards, like IASB financial statement standards (IFRS), will of course be dynamic, not static – subject to a process of continuous refinement and expansion to reflect evolving understanding of investor needs, corporate accountability and sustainability-related risks and opportunities.

At current unprecedented rates of standard-setting progress, a two-pillar package of global sustainability reporting standards from both the inside-out (GRI) and outside-in (ISSB) perspectives should be achievable before too long, and before it's too late.

Finally, boards of directors, CEOs and CFOs can ensure that the process for complying with IFRS S1 in financial reporting can, if undertaken with a creative, innovative mindset, lead a company to fresh insights and opportunities about ways to reduce sustainability impacts and risks, adjust its business model and enhance value creation.

Isn't all this a promising new step in the right direction – not just a landmark in corporate reporting, but perhaps even another step in embedding new concepts of corporate purpose, accountability and transparency necessary to preserve our planet for the future?

[18] Delaware has recently enacted new legislation for the incorporation of Public Benefit Corporations – see https://www.mondaq.com/unitedstates/shareholders/1346894/delaware-public-benefit-corporations.