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Emmanuel Faber, ISSB Chair
Sue Lloyd, ISSB Vice-Chair
International Sustainability Standards Board
IFRS Foundation
VIA EMAIL: commentletters@ifrs.org

July 29, 2022

RESPONSE TO EXPOSURE DRAFT ON IFRS S1 GENERAL REQUIREMENTS FOR DISCLOSURE OF SUSTAINABILITY-RELATED FINANCIAL INFORMATION

Dear Chair Faber and Vice-Chair Lloyd,

On behalf of Positive Impacts (P), I welcome the opportunity to submit our consultation feedback for the ED/2022/S1 IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information.

Please do not hesitate to contact us if you want to discuss our proposals and ideas or like to learn more about the contents of our third publication from the PI paper series "Demystifying the links between sustainability/ESG and performance".

We look forward to hearing back from you and seeing an updated proposal.

With kind regards,

Martin G. Viehöver,
Founder & CEO Positive Impacts (PI)

ABOUT POSITIVE IMPACTS (PI)

Positive Impacts (PI) GmbH is a specialized strategy consulting firm for integrating sustainability/ESG into business strategies, supported by its proprietary approach and tailored digital tools. It was founded in October 2020 by Martin G. Viehöver, a sustainability expert and consultant with more than 30 years of experience in the field. More than 18.000 hours of dedicated work from a team of consultants and several decades of experience developed and tested the PI Approach for sustainability integration. This approach also received feedback and support from renowned experts, most of whom still support PI as Advisory Board members or partners. The main idea is that sustainability is an exercise of defining a strategy (and not simply reporting) and needs to go hand in hand with business strategies to be managed consistently to contribute to the company's financial goals and create societal value. That means the "right" sustainability strategy (approach) will differ between companies, depending on an organization's market environment, strategic positioning, and sustainability ambitions. The PI Approach is centered around answering four key questions. What an organization should report on then becomes the byproduct of answering these questions. Starting with the question of what to report on could lead to reporting just for the sake of complying with reporting obligations and thus, to spending more money on an exercise than necessary and without an adequate value in return – while potentially even creating new risks and most importantly: losing time.

GENERAL COMMENTS

"The biggest danger is not inaction. The real danger is when politicians and CEOs are making it look like real action is happening when in fact, almost nothing is being done, apart from clever accounting and creative PR." (G. Thunberg)

"You can print money, but you cannot print time." (M. Viehöver)

SUSTAINABILITY PERFORMANCE SHOULD BE STANDARDIZED, NOT ITS MANAGEMENT!

In essence, sustainability/ESG is about changing the way that business is done and not about reporting. However, a key component for this is reliable, comparable, and complete information. The IFRS has played an important role in standardizing what it means to report organizations' revenues and profits. On the other hand, strategies and management approaches are, to date, not standardized to ensure competition and provide organizations with a necessary level of freedom. This is also why asking PRADA and Primark to align their strategies and management approaches is nonsense. However, due to respective reporting standards, comparing their revenues and profits is possible. The same logic should be the guiding principle for any sustainability standard.

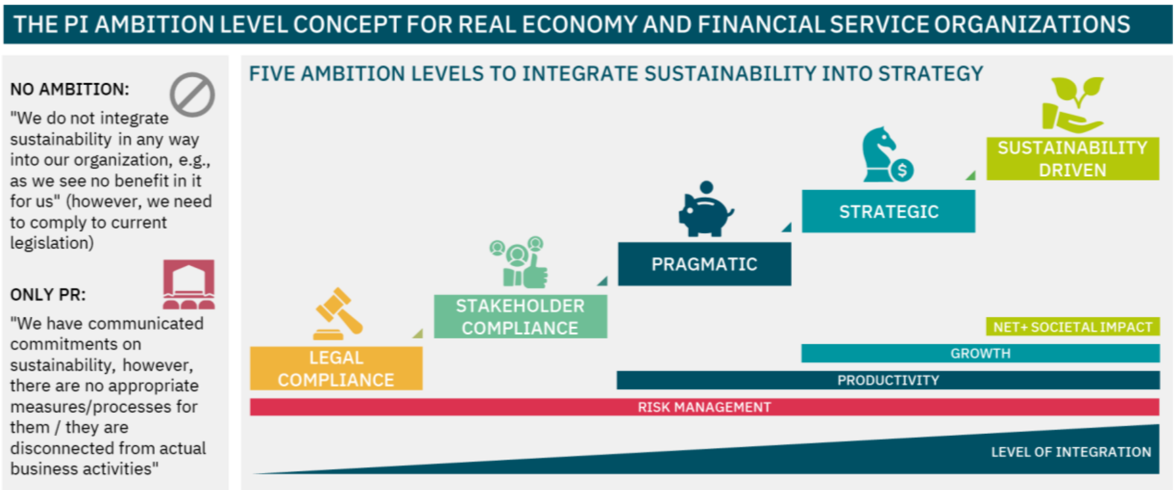
Coming from a country where one part has suffered from a state-driven economy may have shaped PI's understanding of the necessity of competition and freedom regarding strategies and management approaches. Therefore, the latter also needs to include the possibility of not doing more than complying with current legal regulations. Any required information suggesting an organization should be doing more risks producing standard-driven "Only PR" approaches. PI uses the metaphor of going on a hiking trip when it comes to the question of integrating sustainability/ESG into strategy, management, and operations. Organizations that follow "Only PR" approaches go on a weekend trip, produce a glossy report about it, and deceptively suggest that they are hiking. Such practices pose significant risks both for the organization and society. Employees that read such a report might get the impression that it seems to be ok to take integrity and compliance not too seriously, with losing trust in the management and even bribery and corruption as potential knock-on effects.

In the PI study "Strategic sustainability management pays off" (PI, 2022a) on the largest 100 stock-listed companies in Germany (N100), four of the five strategic imperatives of the PI Ambition Level Concept (see FIGURE 1) were identified. This analysis also showed how the N100 managed sustainability differed from another. Implying that every organization should aim to become Sustainability Driven compares to requiring everybody to aim for Mount Everest in their hiking trip. Putting the aim of achieving sustainable development on the shoulders of market players alone is an approach doomed to fail. Any business activity will need to be complemented with effective and efficient government interventions to change the incentives for the market environment to reach a sustainable development that maximizes Societal Value. The latter will, however, require a global standard that determines the principles and rules for accounting Societal Value KPIs, irrespective of a financial materiality judgment.

THE MATERIALITY DEFINITION IN THE REPORT SHOULD BE THE SAME AS THE ONE FOR THE ORGANIZATION'S MANAGEMENT.

The management of such indicators and KPIs, however, can either be based on a materiality judgment regarding the impact on business or the impact on society. The latter is a strategic choice, where the organization bets on having a first mover advantage and intends to proactively move the issue towards becoming financially material. The information on activities of managing currently financially immaterial topics should also be included in a sustainability report based on the ISSB framework, as this will involve investments from the firm and represents a bet of the firm that can go wrong. The key here is to give the organizations this freedom of choice and transparent communication. This logically implies a freedom for the organization to choose either single or double materiality as the basis for their management and, thus, their management reporting. Imposing one materiality definition on all organizations is state-driven management, irrespective of whether it is single or double materiality.

FIGURE 1:



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SPECIFIC COMMENTS

QUESTION 1 – OVERALL APPROACH

The Exposure Draft sets out overall requirements with the objective of disclosing sustainability-related financial information that is useful to the primary users of the entity's general purpose financial reporting when they assess the entity's enterprise value and decide whether to provide resources to it.

Proposals in the Exposure Draft would require an entity to disclose material information about all of the significant sustainability-related risks and opportunities to which it is exposed. The assessment of materiality shall be made in the context of the information necessary for users of general purpose financial reporting to assess enterprise value.

(a) Does the Exposure Draft state clearly that an entity would be required to identify and disclose material information about all of the sustainability-related risks and opportunities to which the entity is exposed, even if such risks and opportunities are not addressed by a specific IFRS Sustainability Disclosure Standard? Why or why not? If not, how could such a requirement be made clearer?
(b) Do you agree that the proposed requirements set out in the Exposure Draft meet its proposed objective (paragraph 1)? Why or why not?
(d) Do you agree that the requirements proposed in the Exposure Draft would provide a suitable basis for auditors and regulators to determine whether an entity has complied with the proposals? If not, what approach do you suggest and why?

PI RESPONSE:

> On (a), PI partially agrees; however, certain indicators should be made mandatory to report, irrespective of an organization's materiality judgment (see question 8 below). For all other information, the formulation is considered suitable.
> On (b), PI disagrees as the standard lacks the requirement to be transparent on the organization's judgment regarding their impact on society.
> On (d), PI suggests providing a choice on the materiality definition applied in the report that should be based on the organization's materiality definition in its day-to-day business management.

Reasoning:
> On (a): See below.
> On (b): Such transparency would allow the primary user to validate or challenge the organization's judgment of financial and dynamic materiality. In addition, it would allow an organization to explain why they invest in a financially immaterial topic as a bet that this will change over time (see above).
> On (d): Otherwise, this standard would only produce situations where the auditor determines the management approach of the firm, increasing the disconnect of the report to the actual management approach (see question 8 below). "When the tail wags the dog."

QUESTION 2 – OBJECTIVE

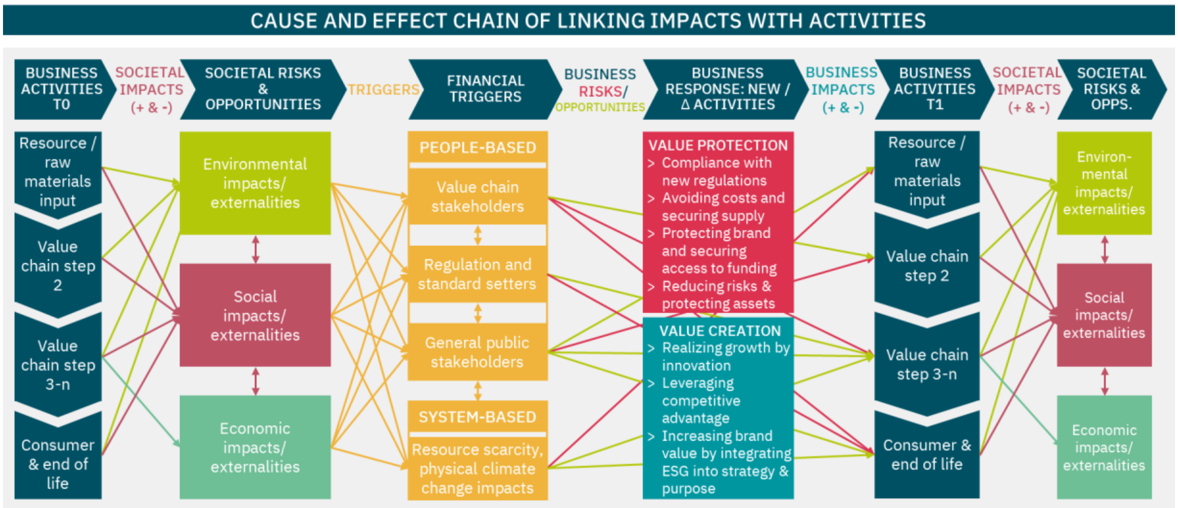
The Exposure Draft sets out proposed requirements for entities to disclose sustainability-related financial information that provides a sufficient basis for the primary users of the information to assess the implications of sustainability-related risks and opportunities on an entity's enterprise value. Enterprise value reflects expectations of the amount, timing and uncertainty of future cash flows over the short, medium and long term and the value of those cash flows in the light of the entity's risk profile, and its access to finance and cost of capital. Information that is essential for assessing the enterprise value of an entity includes information in an entity's financial statements and sustainability-related financial information. Sustainability-related financial information is broader than information reported in the financial statements that influences the assessment of enterprise value by the primary users. An entity is required to disclose material information about all of the significant sustainability-related risks and opportunities to which it is exposed. Sustainability-related financial information should, therefore, include information about the entity's governance of and strategy for addressing sustainability-related risks and opportunities and about decisions made by the entity that could result in future inflows and outflows that have not yet met the criteria for recognition in the related financial statements. Sustainability-related financial information also depicts the reputation, performance and prospects of the entity as a consequence of actions it has undertaken, such as its relationships with, and impacts and dependencies on, people, the planet and the economy, or about the entity's development of knowledge-based assets. The Exposure Draft focuses on information about significant sustainability-related risks and opportunities that can reasonably be expected to have an effect on an entity's enterprise value.

(a) Is the proposed objective of disclosing sustainability-related financial information clear? Why or why not?
(b) Is the definition of 'sustainability-related financial information' clear (see Appendix A)? Why or why not? If not, do you have any suggestions for improving the definition to make it clearer?

PI RESPONSE:

> On (b): PI broadly agrees; however, further guidance should be given for the reporting entities to understand how they could identify such links. See FIGURE 2 for a visual example that explains the interdependencies between impacts on society and impacts on business, which largely depend on the firm's response.

FIGURE 2:



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QUESTION 3 – SCOPE

Proposals in the Exposure Draft would apply to the preparation and disclosure of sustainability-related financial information in accordance with IFRS Sustainability Disclosure Standards. Sustainability-related risks and opportunities that cannot reasonably be expected to affect users' assessments of the entity's enterprise value are outside the scope of sustainability-related financial disclosures. The Exposure Draft proposals were developed to be applied by entities preparing their general purpose financial statements with any jurisdiction's GAAP (so with IFRS Accounting Standards or other GAAP).

Do you agree that the proposals in the Exposure Draft could be used by entities that prepare their general purpose financial statements in accordance with any jurisdiction's GAAP (rather than only those prepared in accordance with IFRS Accounting Standards)? If not, why not?

PI RESPONSE:

> In order to establish international comparability, PI welcomes the proposal that organizations that prepare their financial statements in accordance with any jurisdiction's GAAP may apply the proposals of this Exposure Draft.

QUESTION 4 – CORE CONTENT

The Exposure Draft includes proposals that entities disclose information that enables primary users to assess enterprise value. The information required would represent core aspects of the way in which an entity operates. This approach reflects stakeholder feedback on key requirements for success in the Trustees' 2020 consultation on sustainability reporting, and builds upon the well established work of the TCFD.

Governance

The Exposure Draft proposes that the objective of sustainability-related financial disclosures on governance would be: to enable the primary users of general purpose financial reporting to understand the governance processes, controls and procedures used to monitor and manage significant sustainability-related risks and opportunities.

Strategy

The Exposure Draft proposes that the objective of sustainability-related financial disclosures on strategy would be: to enable users of general purpose financial reporting to understand an entity's strategy for addressing significant sustainability-related risks and opportunities.

Risk management

The Exposure Draft proposes that the objective of sustainability-related financial disclosures on risk management would be: to enable the users of general purpose financial reporting to understand the process, or processes, by which sustainability-related risks and opportunities are identified, assessed and managed.

These disclosures shall also enable users to assess whether those processes are integrated into the entity's overall risk management processes and to evaluate the entity's overall risk profile and risk management processes.

Metrics and targets

The Exposure Draft proposes that the objective of sustainability-related financial disclosures on metrics and targets would be: to enable users of general purpose financial reporting to understand how an entity measures, monitors and manages its significant sustainability-related risks and opportunities. These disclosures shall enable users to understand how the entity assesses its performance, including progress towards the targets it has set.

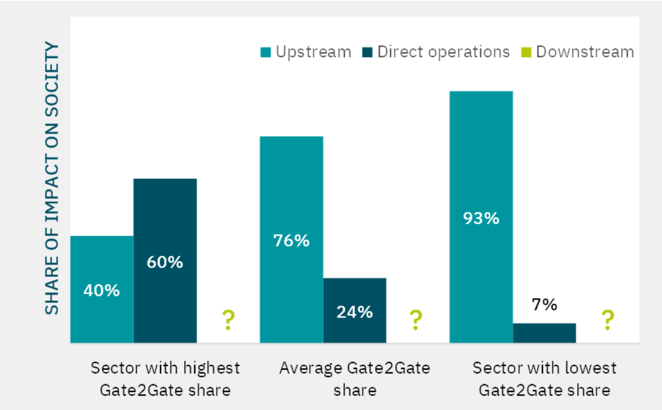
(a) Are the disclosure objectives for governance, strategy, risk management and metrics and targets clear and appropriately defined? Why or why not?
(b) Are the disclosure requirements for governance, strategy, risk management and metric appropriate to their stated disclosure objective? Why or why not?

PI RESPONSE:

- On (a): PI recommends changing "Risk management" to "Risk and innovation management".
- On (a): The organization should be obliged to state its general strategic imperative (intent) regarding sustainability (see FIGURE 1 for PI's example), with the option to have different strategic imperatives for certain markets, brands, or even topic categories. This should be the basis of the disclosure of further information on the management approach, namely, why it is or is not integrated into governance, strategy, risk, and opportunity management.
- On (b): Core metrics should be defined by the standard and shall always be required to be reported at least in absolute numbers. In addition, the ISSB should work towards monetization factors to be used to quantify the related impact on society in monetary terms.
- On (b): All metrics should be reported by at least including the relevant performance of the upstream value chain and the organization, reflecting the scope of revenues.
  Reasoning:
  - On (a): PI agrees that the risk management department may also identify a positive deviation of a plan; however, further evaluations and seizing of such opportunities will most likely be better conducted by the innovation management. In addition, several opportunities would most likely never be identified by the risk management team. Without this change, opportunities may be underrepresented in the respective reports.
  - On (b): Specific numbers alone make it hard to understand an organization's overall impact on society. In our study, 40 – 93% of the monetized impacts on society lay in the upstream value chain (see FIGURE 3). Outsourcing a certain production step may otherwise be a feasible approach to fool the primary users of a report.

FIGURE 3:

SHARE OF MONETIZED IMPACTS OF THE N100 IN 2019



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QUESTION 5 – REPORTING ENTITY

The Exposure Draft proposes that sustainability-related financial information would be required to be provided for the same reporting entity as the related general purpose financial statements.

The Exposure Draft proposals would require an entity to disclose material information about all of the significant sustainability-related risks and opportunities to which it is exposed. Such risks and opportunities relate to activities, interactions and relationships and use of resources along its value chain such as:

- its employment practices and those of its suppliers, wastage related to the packaging of the products it sells, or events that could disrupt its supply chain;
- the assets it controls (such as a production facility that relies on scarce water resources);
- investments it controls, including investments in associates and joint ventures (such as financing a greenhouse gas-emitting activity through a joint venture); and
- sources of finance.

The Exposure Draft also proposes that an entity disclose the financial statements to which sustainability-related financial disclosures relate.

(a) Do you agree that the sustainability-related financial information should be required to be provided for the same reporting entity as the related financial statements? If not, why?

(b) Do you agree with the proposed requirements to identify and explain the connections between sustainability-related risks and opportunities and information in general purpose financial reporting, including the financial statements? Why or why not? If not, what do you propose and why?

(c) Is the requirement to disclose information about sustainability-related risks and opportunities related to activities, interactions and relationships, and to the use of resources along its value chain, clear and capable of consistent application? Why or why not? If not, what further requirements or guidance would be necessary and why?

PI RESPONSE:

> On (a) PI generally agrees

> On (b) PI generally agrees

> On (c) PI generally disagrees as PI considers the basis for the inclusion of information to be reported along the value chain should be its relevance for the impact on society and not the financial relevance (see reasoning and points raised above and below, and FIGURE 3 above). However, their links to financial performance should be based on the requirements based in the ED.

QUESTION 6 – CONNECTED INFORMATION

The Exposure Draft proposes that an entity be required to provide users of general purpose financial reporting with information that enables them to assess the connections between (a) various sustainability-related risks and opportunities; (b) the governance, strategy and risk management related to those risks and opportunities, along with metrics and targets; and

(c) sustainability-related risks and opportunities and other information in general purpose financial reporting, including the financial statements.

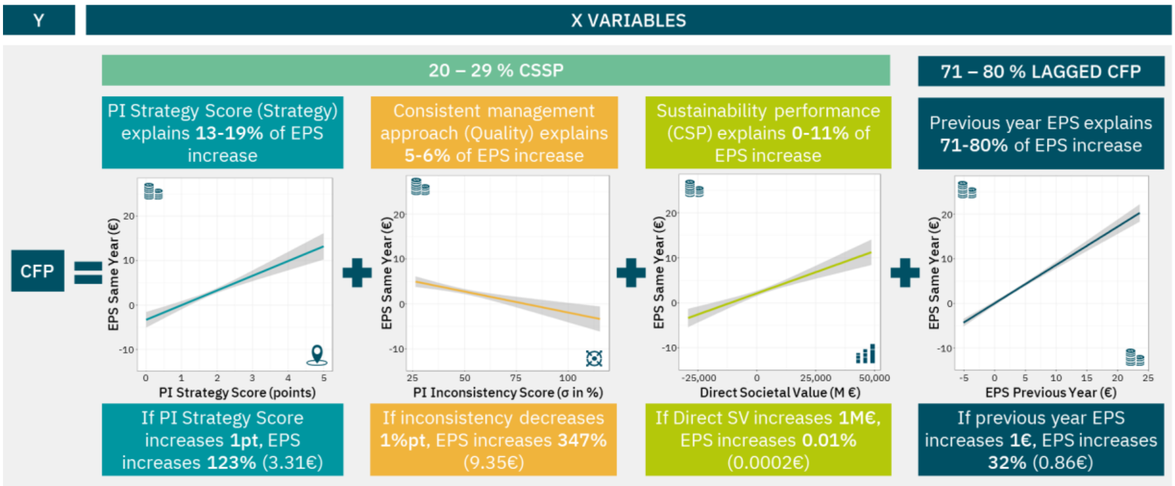
(a) Is the requirement clear on the need for connectivity between various sustainability-related risks and opportunities? Why or why not?

(b) Do you agree with the proposed requirements to identify and explain the connections between sustainability-related risks and opportunities and information in general purpose financial reporting, including the financial statements? Why or why not? If not, what do you propose and why?

PI RESPONSE:

> On (b) PI generally agrees that organizations are best positioned to understand better the inter-linkages between sustainability performance and its financial position, performance, and cash flows for the reporting period. We found a highly significant correlation between corporate sustainability strategy and performance (CSSP) and corporate financial performance (CFP) in our study on the 100 largest German companies (PI, 2022a). However, the correlation was still positive but lowest for our sustainability performance KPIs.

FIGURE 4: CSSP explained up to 29% of the CFP change in the sample of the PI study



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QUESTION 8 – MATERIALITY

The Exposure Draft defines material information in alignment with the definition in IASB's Conceptual Framework for General Purpose Financial Reporting and IAS 1. Information 'is material if omitting, misstating or obscuring that information could reasonably be expected to influence decisions that the primary users of general purpose financial reporting make on the basis of that reporting, which provides information about a specific reporting entity'.

However, the materiality judgements will vary because the nature of sustainability-related financial information is different to information included in financial statements. Whether information is material also needs to be assessed in relation to enterprise value.

Material sustainability-related financial information disclosed by an entity may change from one reporting period to another as circumstances and assumptions change, and as expectations from the primary users of reporting change. Therefore, an entity would be required to use judgement to identify what is material, and materiality judgements are reassessed at each reporting date. The Exposure Draft proposes that even if a specific IFRS Sustainability Disclosure Standard contained specific disclosure requirements, an entity would need not to provide that disclosure if the resulting information was not material. Equally, when the specific requirements would be insufficient to meet users' information needs, an entity would be required to consider whether to disclose additional information. This approach is consistent with the requirements of IAS 1.

The Exposure Draft also proposes that an entity need not disclose information otherwise required by the Exposure Draft if local laws or regulations prohibit the entity from disclosing that information. In such a case, an entity shall identify the type of information not disclosed and explain the source of the restriction.

(a) Is the definition and application of materiality clear in the context of sustainability-related financial information? Why or why not?

(b) Do you consider that the proposed definition and application of materiality will capture the breadth of sustainability-related risks and opportunities relevant to the enterprise value of a specific entity, including over time? Why or why not?
(c) Is the Exposure Draft and related Illustrative Guidance useful for identifying material sustainability-related financial information? Why or why not? If not, what additional guidance is needed and why?

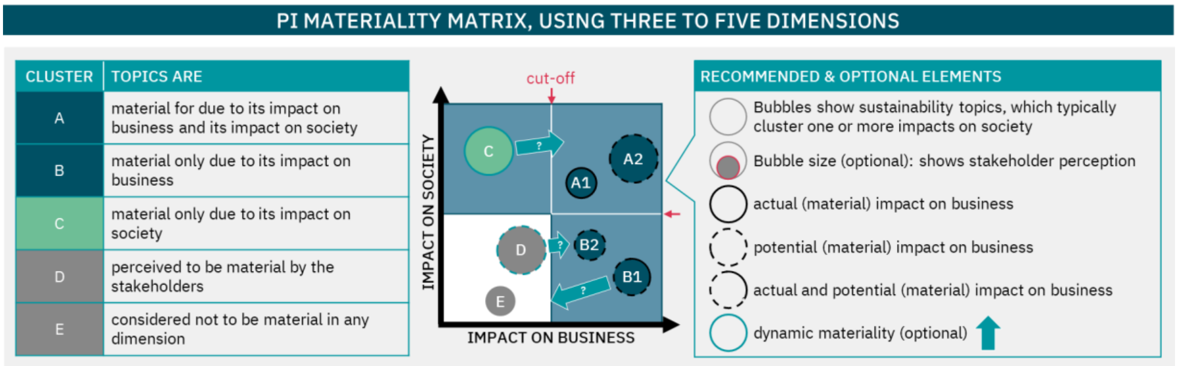
PI RESPONSE:

> On (a) PI broadly disagrees due to several reasons:
  > PI recommends a mandatory disclosure of the assessed topic categories in a materiality matrix (shown as dots or bubbles) with the two core dimensions “impact on business” (x-axis) and “impact on society” (y-axis) as long as the ISSB is a voluntary standard. It should be made clear that stakeholder perception can be added as an optional third dimension, either in the form of the bubble size or color code. Organizations should be given the freedom to choose the scale and approach for judging the relative positioning on the respective axis as well as the definition of the materiality cut-off. However, they should be obliged to elaborate on their approach, the value chain scope they applied, and what underlying drivers they have assessed, along with a disclosure of the entire matrix showing all assessed topic categories. Regarding the impact on business, two sub-dimensions should be obligatory to disclose: the actual and the potential impact on business, e.g., shown as a line format (solid/dashed) or color code (see FIGURE 5 below).
  > If the ISSB is the basis for mandatory disclosure, organizations should get the freedom to simply state that they do not consider sustainability to be material to their organization. All related management disclosures should therefore be allowed to be declared as not applicable.
  > In addition, organizations should be given the freedom to choose between single and double materiality as the basis for their ISSB reporting, based on the definition applied in their management approach.
  > The word impact should always be contextualized to be either impact on business or society (e.g., “low-probability and high-impact outcomes”). Ideally, the same is true for the terms “risks” and “opportunities”, as these concepts also apply to society (e.g., the risk of a species to get extinct or the opportunity to increase biodiversity in an area).
  > In addition, certain sustainability indicators should be required to be tracked on an activity basis (similar to the activities defined by the EU Taxonomy), reported on a product/service level to the respective customer, and reported on a group level with clear thresholds (e.g., 50 g CO_2e/1 € revenue). For each activity, the relevant pre-activities should be determined to be included in the scope of this reporting to cover the same scope as revenue (including tied impacts to COGS and not just GVA). This reporting requirement should be made mandatory, i.e., irrespective of the “financial” materiality judgment of the entity. Ideally, such indicators should be complemented by their monetized impact on society, less, e.g., the related carbon taxes paid. A lesser useful but possible approach is to define these indicators at the industry level. The rationale for choosing such indicators should be based on the impacts on society of the respective economic activities. The impact on business should not be the basis for such reporting. Such indicators can, however, be complemented with related KPIs to be used in integrated reporting that links financial and sustainability performance. However, the monetized impact on society should not be misunderstood as “sustainability related financial information” in the sense of how the ED currently defines this. (See PI, 2022b and the forthcoming third publication of PI.)
  Reasoning:

> The primary users need the information included in the proposed materiality matrix as well as the chosen materiality definition to understand and potentially challenge the basis for the entity's management and strategy.
> The primary users are not a heterogenic group of capital providers; some are short-term oriented, some mid-, some long-term, and some are purely "impact" driven investors, whose primary objective is to impact society through their investments positively. The proposed approach would provide useful information for all primary users and those with a short-term focus as they would understand that certain investments are not for them.
> The proposed approach incorporates the elements and the general idea of the building blocks approach; however, the actual and potential impact on business needs to be assessed holistically from a management point of view as the overall impact on business. Otherwise, the prioritization of topics for the management response would be misleading. In addition, it is much clearer and does not pre-define circumstances that are not necessarily true. (See PI, 2022b for further information.)
> In addition, by applying the recommended changes, a global sustainability reporting standard would produce information that is also useful for other users of sustainability information, such as employees, potential employees, customers, civil society, and governments.
> Both the quantification of impact on business and the quantification of the impact on society is in an immature state. Thus, innovation and competition should be the guiding principle until there are feasible quantitative approaches to assess these. (See PI, 2022b for further information on why a semi-quantitative scale should not be the basis for a standard.)
> "Financial materiality" is a potentially misleading wording, as some managers may not consider it to cover topics with a potential financial consequence. The ED also contains the word "impact", most likely in the sense of impact on business ("high-impact outcomes"). "Impact on business" allows the disaggregation into actual and potential impacts on business. Also, the relative importance of a topic needs to include an aggregate perspective of these sub-dimensions.
> The addition of "impact on society" would respond to the critics and would be a much clearer wording than the one proposed by EFRAG ("impact materiality").
> The term impact has been used for decades in risk management as the financial consequence if an uncertain event occurs. However, it is also used in the context of an organization's impact on society. The same is true for risks and opportunities. Having clarity on what is meant helps to reduce the confusion in this complex matter.
> One of the biggest challenges of sustainability reporting is the presence of "Only PR" approaches that are either driven by standards that require a management that either does not fit the organization's strategy or is not understood by the top management of the firm or where the management deliberately deceives the public. A standard setter cannot control the latter; an auditor can potentially check all three.
> Using "financial" materiality as the basis for choosing sustainability indicators is not only outdated but also not feasible. The financial materiality of such information will depend on several factors for a company in the same industry: The location of the operations and related legal and fiscal environments, its position in the value chain, its strategic positioning on sustainability and related commitments, and its business strategy, to name a few. PI agrees with the need for companies to assess the impact on business of sustainability

performance information and that they need support in how this should be done. For some instances, the link to financials (costs, revenues, risks, opportunities, and related capital costs) may be universal. Still, for most, it will be an individual and dynamic question with different baselines to be logically applied (see PI, 2022b for further explanations). Each ex-post and ex-ante impact on business quantification requires two scenarios. There are only two scenarios feasible for a standardized comparison: legal compliance or market average. Both are mostly region specific and therefore not feasible for a global standard. These then need to be compared to, e.g., the as-is (scenario), business as usual, or a planning scenario. Pre-defining all of these means applying a one size fits all approach and neglecting all that has been said. Thus, any KPI that shall describe the links between sustainability and financial performance should be based on the organization's materiality judgment regarding the impact on business.

FIGURE 5:



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QUESTION 13 – GLOBAL BASELINE

IFRS Sustainability Disclosure Standards are intended to meet the needs of the users of general purpose financial reporting to enable them to make assessments of enterprise value, providing a comprehensive global baseline for the assessment of enterprise value. Other stakeholders are also interested in the effects of sustainability-related risks and opportunities. Those needs may be met by requirements set by others, including regulators and jurisdictions. The ISSB intends that such requirements by others could build on the comprehensive global baseline established by the IFRS Sustainability Disclosure Standards.

Are there any particular aspects of the proposals in the Exposure Draft that you believe would limit the ability of IFRS Sustainability Disclosure Standards to be used in this manner? If so, what aspects and why? What would you suggest instead and why?

PI RESPONSE:

> For any organization, conducting a materiality assessment more than once is not feasible. Also, most providers of financial capital that have an interest in sustainability-related financial disclosures will have an interest in understanding: How did the organization assess the interdependencies of their impacts on society (see FIGURE 2) and their overall impact on business, with the sup-sets of actual and potential impacts on business (see FIGURE 5)? This missing element of the ED is one key reason why the current ED for the IFRS SDS cannot form a global baseline for sustainability reporting.

> The second factor that limits the ED from forming a global baseline for sustainability reporting is the basis for choosing indicators to be reported. The IFRS was the key global player in standardizing revenue and EBITDA; PI thinks it should be the one for quantifying the respective sister KPIs (see PI, forthcoming in 2022 for more).

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