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Comment letter on the IFRS S1 Exposure Draft (ED)

Thank you for the opportunity to comment on the IFRS S1 Exposure Draft (ED).

I provide my comments as a leading accounting academic and Chartered Accountant with substantial research, practice and policy experience in sustainability and other forms of non-financial reporting. This experience is detailed here.

I provide an overall critique, key suggestions for addressing the problematic issues and responses to the most pertinent consultation questions.

Overall critique

Overall, the conceptual framing is muddled and flawed. This is perhaps inevitable given the Exposure Draft is the outcome of a recent amalgamation of bodies with reporting frameworks that have either an indirect or unclear relationship to sustainable development (sustainability) or financial statements. But it also stems from a confused and changing picture of what the IFRS Foundation is seeking to achieve beyond that amalgamation.

Problems with the proposed conceptual framing were highlighted by academic responses to the Trustees' initial *Consultation Paper on Sustainability Reporting* most of which objected (strongly) to the proposals, providing evidence to support those objections (see Adams and Mueller, 2022 for an analysis of academic responses). Issues have also subsequently been discussed in recently published work (see, for example, Abelo, 2022; Adams and Abhaywansa, 2022; Giñer and Luque Vílchez, 2022).

The conceptual framing in the ED is: a) inconsistent with the stated objective of the proposed standard; b) a poor fit with the examples of information to be disclosed; and, of most concern, c) requires a high level of judgement on matters that mean different things to different investors. These issues will not be resolved by using the SASB Standards as encouraged by the IFRS Foundation.

Key definitions are imprecise and problematic to apply. They appear to be an attempt to align the IFRS desire to serve capital markets with an intention to include selective impact indicators in GRI Standards. At the same time the IFRS Foundation is *not* encouraging the use of GRI Standards but *is* encouraging the use of SASB and CDSB Standards, which are not concerned with impact of the organisation.

Key suggestions

There is much to be done to develop reporting requirements concerned with facilitating decisions on enterprise value for the purpose of allocating financial resources. I (again) recommend that the IFRS Foundation urges the mandatory use of GRI Standards as the starting point or *baseline* for sustainability reporting. This will allow the ISSB to focus on identifying matters that are directly related to the assessment of enterprise value and provide a coherent baseline for that purpose.

An organisation cannot identify all material sustainability-related financial matters unless it has first identified its material impacts through use of the GRI Standards. GRI is best placed to develop Standards concerning the impact of organisations on economies, society and the environment. GRI Standards are clearly drafted (including relative to these Exposure Drafts) as one might expect having been developed over more than two decades. GRI has a robust governance structure which is fit for this purpose[1].

Investors can and do make assessments regarding how these corporate impacts on economies, society and the environment influence enterprise value. They should not have to rely on solely on reporters to make this determination. They need comprehensive impact information.

I urge the IFRS Foundation to move on from the amalgamation and associated frameworks and look to what is needed from this single body in the future regarding financially relevant information.

I believe the conceptual framework and the relationship with GRI and GRI Standards needs to be addressed and another Exposure Draft issued by a full Board on base-line *financial disclosures* resulting from sustainable development mega trends and corporate impacts on economies, society and the environment (reported using GRI Standards, which companies use to report to a wide range of stakeholders including investors).

Question 1 (relating to overall approach)

The key issue with the requirements is the considerable amount of judgement involved on matters that are not well understood and with respect to terms and matters that are understood differently by the intended users of the standards. As such, they will *not* lead to harmonisation (a stated aim of the IFRS Foundation Trustees), green washing will flourish and disclosures will be challenging to audit. Green washing will be facilitated because reporters lack knowledge about how risks might influence enterprise value and because reporting on impact is not the focus of the ISSB (and the IFRS Foundation has no experience in this). Some will also use the looseness in the wording to avoid disclosing matters they prefer not to. The most efficient way to reduce green washing would be for GRI Standards to be mandated alongside standards that focus on financial statement implications of sustainable development trends and corporate impacts.

According to the ED the decision regarding whether to disclose requires consideration of a range of matters that involve considerable judgement:

[1] See https://www.icas.com/landing/sustainability/non-financial-reporting/explainer-the-global-reporting-initiative-and-the-gssbs-sustainability-reporting-standards-what-you-need-to-know for a description.

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a) Whether information is useful to providers of finance when they assess 'enterprise value' and decide whether to provide resources (para 1)

b) What constitutes 'enterprise value' and what influences it across different time horizons (paras 2, 5)

c) The risk appetite of providers of finance (para 2)

d) The boundaries around relevant information (for example, the information relevant to para 6b and 6d is broader than what I would consider to be 'sustainability-related financial information')

e) The link between potential disclosures and enterprise value (this is unclear, for example with respect to the information required in para 6a (governance oversight) and 6c ("relationships with people, planet and the economy, and its impacts and dependencies on them")

At this point there is only one other ED, so this proposed Standard would apply to all sustainability matters other than climate change. This is concerning.

Given the significant amount of judgement involved in all the above determinations my answer to questions 1 a) to d) is 'no'. With regard to the requirements of sustainability reporting standards to facilitate the assurance of sustainability reporting (your question 1 d), I recommend to you reports published by the Institute of Chartered Accountants of Scotland (ICAS, 2022a,b).

Question 2 (relating to paras 1-7, Objective)

No, to a) and b) – The objective of disclosing sustainability-related financial information and its connection with impact reporting covered in GRI Standards, needs clearer articulation. This also applies to what comprises 'sustainability-related financial disclosures'. See my answer to Q1 above re the amount of judgement involved and the matters requiring judgement.

Question 3 (relating to paras 8-10, Scope)

The nature of GAAP is irrelevant. Financial risks and opportunities are difficult to assess. The proposals need to be narrowed down to and go deeper into the financial statement implications with GRI Standards being the *baseline* regarding impact reporting.

Question 4 (relating to paras 11-35, Core content)

No, to a) and b) regarding clarity and appropriateness of proposed disclosures.

The content elements include matters that are more clearly and appropriately expressed in GRI 2 on governance and strategy. The ISSB should not seek to rewrite these (given they are widely used in their current form) but rather include only additional matters relevant to the organisation's approach to sustainability risks and opportunities.

Governance. The governance disclosure requirements in GRI 2-9 to GRI 2-21 are excellent. I suggest IFRS S1 focusses on additional matters relevant to oversight of sustainability-related risks and opportunities from the organisation's perspective.

Strategy. Strategy disclosures should include, but not be limited to, allowing an investor "to understand the effects of significant sustainability-related risks and opportunities on its strategy and decision making" (ED, p 12). The strategy itself should be disclosed. This could be clearer in the text. For example, does the reporting entity plan to change its product/service mix? What you refer to here is management approach to risk and opportunity, rather strategy. The required strategy disclosures in GRI 2 are clearer and more appropriate (as would be expected given their relatively advanced stage of development) (see GRI2-22 to G2-25).

Sustainability related risks and opportunities. Paras 16-20 are clear and appropriate for an organisation that has already considered its material impacts following GRI 3, GRI Topic Standards and GRI Sector Standards. The requirement to disclose how sustainable development risks and opportunities are incorporated into board-agreed strategy is critical to ensuring it is given appropriate consideration.

Financial position, financial performance and cash flows and resilience. I suggest that effort is expended on enhancing this section rather than rewriting the disclosures required in G2.

Risk management. This section should be retitled so as not to preference a focus on risks. Identifying opportunities is critical to improving the performance of companies (enterprise value) and hence should be disclosed according to the conceptualisation in the ED.

Metrics and targets. The IFRS Foundation should focus its requirements on a) how organisations identify which of the matters that it reports using GRI Standards that affect future cash flows; b) any matters additional to the organisation's impacts on economies, society and the environment that affect future cash flows.

[See the *Sustainable Development Goals Disclosure Recommendations* (Adams et al, 2020) for changes to the TCFD categories to address these points and the explanation in Adams (2020)].

Question 5 (relating to paras 37-41, Reporting entity)

a) The language regarding reporting entities is confusing. The examples ask reporters to report information in its value chain i.e. relating to organisations that are not the reporting entity. A starting point to considering financial implications of value chain activities should be reporting on value chain impacts. The link to the reporting organisation's financial position of these impacts should the focus of the ISSB – not the impacts themselves.

b) No, an organisation needs to first report the impacts of its value chain on economies, society and the environment before it can identify sustainability-related risks. See answer to a).

c) Yes. The sustainability related financial reporting requirements and their relationship with GRI impact reporting need further development first, but it would seem logical.

Question 6 (relating to paras 42-44, Connected information)

Yes, to a) and b). The requirement to report on connectivity is clear. However, I suggest that examples and guidance are extended and provided separately, not in the requirements themselves. I commend to you the way the GRI Standards do this.

Question 7 (relating to paras 45-55, Fair presentation)

The amount of judgement involved (as discussed above) will make 'fair presentation' and assurance of it, challenging.

Question 8 (relating to paras 56-62, Materiality)

The definition of materiality assumes that the only sustainability information investors use to make investment decisions is sustainability-related financial information. Many investors use the impact reporting provided by companies complying with GRI Standards to make their own assessments concerning its relevance to their investment decisions and some will not trust reporting organisations to do this for them. I reiterate the need for a double materiality approach, recognising that investors need information on corporate impacts on economies, society and the environment (provided through GRI Standards) and information on the financial implications of sustainable development issues. The ISSB must focus on the latter if either are to be done well.

Any definition of materiality will be difficult to apply unless the amount of judgement required (see answer to question 1) is first addressed and guidance given. Considerably more guidance would need to be provided to reporting entities. (See Adams et al, 2021 for a summary of research on the application of materiality.)

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