INSTITUT DER WIRTSCHAFTSPRÜFER

29 July 2022

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Re.: IFRS Sustainability Disclosure Standard, Exposure Draft: ED/2022/S1: [Draft] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information

Dear Mr. Faber,

We would like to thank you for the opportunity to provide the ISSB with our comments on the IFRS Sustainability Disclosure Standard ED/2022/S1: [Draft] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information, hereinafter referred to as “the Exposure Draft”.

The Institut der Wirtschaftsprüfer would also like to take this chance to welcome the ISSB and acknowledge its presence in Frankfurt and also to wish the new Board every success in establishing a suite of sustainability-related reporting standards to serve as a global solution or global baseline for jurisdictional sustainability reporting initiatives.

We acknowledge that assurance of sustainability disclosures does not fall within the remit of the ISSB. However, we are pleased that the ISSB has included questions that will also illicit responses as to the potential assurability of proposed disclosures, as this is a significant issue for many stakeholders too.

As the ISSB will be aware, with agreement now having been reached on the Corporate Sustainability Reporting Directive (CSRD), the European Commission has recognized the essential role of assurance of sustainability reporting.

As an organization representing professional audit and assurance practitioners, the IDW would like to emphasize the role of our members and the suitability of our profession to perform assurance engagements. Besides practical experience in this field gained through voluntary assurance of so-called non-financial information in Germany, this includes the application of high-quality assurance standards, adherence to quality management standards within firms and the required aspects of ethical behavior required of the profession.

Before addressing the individual questions raised in the Exposure Draft, we will provide some general comments.

General Comments

Achieving a global baseline and the related imperative for comparability with other standard setting initiatives

We fully support the intended speedy establishment of a global baseline that is suitable to facilitate a building blocks approach, such as that envisaged for in the European Union.

In this regard, we particularly support the recent establishment of the Jurisdictional Working Group in order to foster this intention such that the proposals of various standard setting initiatives can be as closely aligned as possible. This is in line with provisions of the EU's Corporate Sustainability Reporting Directive. From a German perspective, we encourage both EFRAG and the ISSB to pursue this further at a bilateral level.

We appreciate the fact that the ISSB has drawn upon the established work of others already active in the field of sustainability-related reporting and acknowledge that the core content (governance, strategy etc.) is consistent with the TCFD, thus lending a degree of familiarity for many potential reporting entities. The structure will be familiar to users and preparers and supports companies in reporting material information, without imposing a change on many companies already reporting in this area.

In our response to q. 1 we do, however, suggest the ISSB clarify the authority of the material promulgated by other Standard Setters and current reporting practices of others referred to in paras. 51 and 54. As noted below, the ISSB has not outlined what the term "sustainability-related" may mean in the context of IFRS S1, instead opting to require an entity to consider specified standards setters' work as well as the reporting practices of others that operate in the same industries or geographies both to identify its own entity-specific disclosure topics and when management makes a judgement as to the entity's disclosures. We note that the IG refers to such information potentially being helpful. We therefore suggest the ISSB clarify the authority of this material vis a vis IFRS S1 and whether any form of hierarchy is intended. Requiring all entities to study all available material and practices of others operating in the same industries or geographies would be overly burdensome. In commenting on the lack of clarity as to the boundary of sustainability-related matters below we also question the difference in approach to this material between paras. 51 and 54 is warranted.

We also note the recent collaboration agreement reached between the ISSB and the GRI and would support further development of the ISSB's standards towards achieving a common goal, not least because GRI has been used by a number of companies in Germany and would reduce further the gap between the ISSB's notion of enterprise value and the double materiality lens used by CSRD/EFRAG. We, therefore, suggest the ISSB be transparent as to the future intended impact of this collaboration on the ISSB's work and its interpretation of materiality. In particular, stakeholders will wish to know whether it can be expected that the ISSB's standards may become more closely aligned to the concept of double materiality as to be applied in the European Union, notwithstanding the desire for the ISSB's suite of standards to provide a global baseline for sustainability reporting.

Finally, we support the intention for the ISSB's Standards to be GAAP-agnostic and suggest that – to the extent possible – common terminology, key concepts and reported metrics be pursued. A principles-based approach to clarify when a reporting entity would refer to the intended meaning of terms and concepts embedded in local GAAP and where there is potential for the standard setters to adopt common terms etc. would minimize regulatory fragmentation and duplication of effort for many reporting entities, which would in turn likely enhance the acceptance of the Standards from a political perspective. Currently, there appears to be a relatively high alignment with IFRS.

<u>Anticipated application challenges in practice</u>

We acknowledge the ISSB's recognition of potential practical implementation challenges and also support the ISSB specifically consulting on the question of whether the effective dates of IFRS S1 and S2 should be aligned and specifically requesting feedback on staggered application.

As explained in more detail in our response to q. 13, from an assurance perspective, we are concerned that – without sufficient time – many potential reporting entities will struggle to reach the level of data collection and internal control systems' maturity sufficient to enable them to fully prepare sustainability-related reporting of the desired quality (which, in turn, is a prerequisite for a meaningful assurance engagement). Besides clear criteria to govern the content of sustainability-related reporting, sufficient time for preparers to establish data collection and internal control systems will be key to the success of sustainability-related reporting. We expect that entities already familiar with some form of sustainability-related reporting may require less "preparation time" than those new to this form of reporting.

We therefore urge the ISSB to raise awareness to policy makers ultimately responsible for any adoption decisions in regard to sustainability reporting.

<u>Lack of clarity as to the boundary of sustainability-related matters</u>

We are concerned that the ISSB has chosen not to clarify which matters are considered "sustainability-related" in the context of its proposed reporting requirements – instead placing reliance on standard setting work and non-mandatory guidance of others (ED IFRS S1. 51 (a)- (c)) and – even more concerning – the reporting practices of other entities (ED IFRS S1. 52 (d)). This essentially denies control to the ISSB until it develops an own standard on a particular matter and may be an impediment to the take up of IFRS S1.

In this context, we also suggest the ISSB further consider and clarify more fully the relationship between IFRS S1 and IFRS Sustainability Disclosure Standards – currently only ED IFRS S2. Specifically, para. 51 requires an entity refer to IFRS Sustainability Disclosure Standards (first sentence) and then, <u>in addition</u> to the items listed in (a) – (d) (second sentence) to identify sustainability-related risks and opportunities about which information could reasonably be expected to influence decisions that the users of general purpose financial reporting make on the basis of that information, i.e., a "double check approach". In contrast, para. 52 requires an entity refer to the relevant IFRS Sustainability Disclosure Standard to identify disclosures, including metrics, about a significant sustainability-related risk or opportunity and para. 53 is only applicable in the absence of an IFRS Sustainability Disclosure Standard, i.e., only then requiring the entity to use its own judgement (and consider the same items as required in para. 54), i.e., an "either or approach". We question whether this difference in approach is warranted.

We therefore suggest the ISSB clarify what it currently means by the term "sustainability-related" and use its future standard setting as an opportunity to add relevant developments as and when new matters emerge that warrant addressing in a global baseline. We also suggest the ISSB be transparent as to whether going forward there is an intention that as further the IFRS

Sustainability Disclosure Standards are developed these shall obviate the requirement to consider the items listed in para. 51 (a) –(d) and in para. 54 and in finalizing IFRS S1 and S2 this aspect in regard to climate.

German companies and their auditors are familiar with the terms “risks” and “opportunities” as defined and required to be reported under the German accounting standard governing the management report (GAS 20). Without a definition from the ISSB, it may be unclear whether these terms are intended to have the same or different meanings. We suggest clarification be given that the disclosure of gross risks is intended and that risk mitigation measures shall be disclosed separately, as this would also be helpful to other entities globally who may not already be familiar with such reporting.

<u>Enterprise value and entity specific value drivers</u>

We support the ISSB’s proposed approach to using enterprise value. This supports the management approach featured in GAS 20, as mentioned above, which has a proven track record in Germany. We thus suggest that IFRS S1 similarly use a management approach to the identification of risks and opportunities. However, the proposed approach to materiality determinations would benefit from further clarification or guidance pertaining to the entity-specific value drivers to be taken into account in complying with para. 61, which requires an entity to consider whether to disclose additional information in the case that compliance with an IFRS sustainability disclosure standard is insufficient to enable the users to assess the effect on enterprise value of the sustainability-related risks and opportunities to which the entity is exposed.

<u>Connectivity with the financial statements</u>

Clear connectivity with the financial statements is essential, but with reliability as an important qualitative characteristic. In our comment letter regarding ED IFRS S2, we discuss the need for further clarification of how an entity shall determine whether estimates of financial impacts can be sufficiently reliable and complete related disclosure of the nature of reported information, including inherent limitations uncertainties so to be useful to the primary users or considered connected with information in the financial statements.

In our response to question 9, we also express the view that the concurrent provision of financial statements and sustainability-related information is essential to achieve the aims of sustainability reporting, including the role this plays in providing the entity itself with information to drive integrated thinking and sustainable business behaviour.

Materiality relates to the reporting entity and beyond

The proposed approach to materiality as outlined in para. 57 is an area of difference to the financial statements since actions of associates, investments and joint ventures as well as others within the supply chain are also issues potentially requiring disclosure. We note that IFRS S2 includes some guidance relating to information pertaining to associates, investments and joint ventures and suggest the ISSB include a general principle in IFRS S1 to address the treatment of information pertaining to associates, investments and joint ventures. Preparers will find it challenging to determine what a primary user really cares about (e.g., investors do not necessarily know themselves what they require as to interactions within supply chains and so this is changing rapidly). Additional clarification of the interaction between qualitative characteristics would be helpful for reporting entities when they need to decide whether to use estimates or even whether to omit required disclosures.

We refer to our response to q. 8 where we comment on the proposed approach to materiality.

Interaction with others

We suggest the ISSB consider the need for an interpretations mechanism (committee).

We also support the intentioned coordination with the IASB.

As far as assurability of reported information is concerned, we suggest the ISSB also liaise with the IAASB in finalizing IFRS S1 and S2 as well as future standards. The IAASB has commenced its own work in this field and so adequate liaison between the two Boards will be essential. We also refer to our comment letter regarding ED IFRS S2, and specifically to our responses to question 13 in this context.

Preparers need firm criteria, including robust definitions, as do all assurance service providers, as they need to compare management’s assertions against such criteria. Challenges from an assurance perspective will include determinations associated with the terms “sustainability-related”, “significant” and “material” but also scenario analyses and forward-looking information that is by nature inherently uncertain. Solutions may have to include management and auditors clearly describing and highlighting the inherent limitations of specific disclosures, so we suggest the ISSB develop more specific guidance on these issues. Definitions of terms such as “direct and indirect mitigation”, “adaptation efforts”, “vulnerable”, “resilience”, “reasonably expects” used throughout the suite of IFRS Sustainability Disclosure Standards would also be helpful.

The role of strong internal governance within the reporting entity and its internal control mechanisms are crucial to ensure maximum quality of sustainability-related information reported.

Differentiation between the terms “significant” and “material”

The terms “significant” and “material” are not sufficiently clear.

A reporting entity needs firm guidance as to the criteria to determine when sustainability-related risks and opportunities are significant and – once these are determined – when information relating to them is material. The last sentence in para. 57: *“it can include information about sustainability-related risks and opportunities with low probabilities and high-impact outcomes”* would be expected to be relevant to both determinations.

We would welcome a clearer explanation of the authority attaching to this material.

We would be pleased to provide you with further information if you have any additional questions about our response, and would be pleased to be able to discuss our views with you.

Yours truly,

Klaus-Peter Naumann	Bernd Stibi
Chief Executive Officer	Technical Director Reporting

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APPENDIX

Questions for respondents

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 (para. 1)? Why or why not?

(c) Is it clear how the proposed requirements in the Exposure Draft would be applied together with other IFRS Sustainability Disclosure Standards, including the [draft] IFRS S2 Climate-related Disclosures? Why or why not? If not, what aspects of the proposals are unclear?

(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?

Whilst we do not disagree with the ISSB's desire not to constrain reporting entities and thus not to define the term "sustainability-related risk and opportunity" since this can change over time and vary between cultures, we believe that a boundary to explain the intended meaning of "sustainability-related" in the context of the IFRS Sustainability Disclosure Standards is needed.

Consideration of all the sources listed in para. 51 – and subsection (d) in particular – potentially leaves the individual interpretations of entities but also their stakeholders too open ended, especially as individual entities may voluntarily report on matters not necessarily widely understood as constituting sustainability-related matters. Beside this requiring consideration of all such material may impose undue costs on reporting entities. We would therefore welcome the ISSB providing firmer guidance as to the topics that "sustainability-related" encompasses for the purposes of reporting at this point in time. We note for example the "list" set forth in the Proposal for the CSRD serves this purpose.

In this context, we also agree with the ISSB that the focus in identification should be on <u>significant</u> sustainability-related risks and opportunities affecting the entity and that IFRS S1 should be very clear that it does not require preparers (and their auditors) to undertake an exhaustive search for all possibly imaginable risks and opportunities. The note in para. 9 would benefit from further explanation and we therefore suggest IFRS S1 be clear that the entity's process of determining significant issues will be a reflection of the way in which the entity operates and is managed but not go beyond this.

We also have a concern as to the authority of material not developed by the ISSB. Requiring a list of specific material promulgated by a diverse range of unspecified others be considered (paras. 51 and 54 of ED IFRS S1) implies this material assumes an authoritativeness it does not have and also means that IFRS S1 is not self-contained.

IG12 clarifies that

"The [draft] Standard includes requirements for an entity to consider the applicability of other sources of guidance that are designed to meet the needs of users of general-purpose financial reporting (see paras. 50 – 54). These materials <u>can</u> inform the: (a) identification of significant sustainability-related risks and opportunities; and (b) selection of metrics or other information for disclosure."

IG 120 states "…*Appropriate non-mandatory standards and guidance, such as the SASB Standards, <u>can help</u> the entity to apply the requirements of the [draft] Standard in a way that meets users' needs for information that is relevant, faithfully representational, comparable, verifiable, timely and understandable."*

IG 120 explains the relationship in a more appropriate way *("The [draft] Standard requires that a complete set of sustainability-related financial disclosures present fairly the sustainability-related risks and opportunities to* *which an entity is exposed (para. 45). Appropriate non-mandatory standards and guidance, such as the SASB Standards, can help the entity to apply the requirements of the [draft] Standard in a way that meets users' needs for information that is relevant, faithfully representational, comparable, verifiable, timely and understandable.")* This language implies such material shall have a supporting rather than mandatory role and so this aspect should be better articulated in the standard itself. In this context clarification of whether this listing is intended to be applied as a hierarchy would also be helpful. The use of "and" means that all entities have to look at all material listed in para. 51 to identify sustainability-related risks and opportunities but – subject to better clarification as suggested above – will be able to pick and choose the exact disclosure rather than have to apply e.g., either SASB or CDSB standards. The granularity of SASB standards may be an issue (especially for entities involved in various industries) and the volume of associated material a cost and resource factor.

Whilst the approach taken means that some preparers can just continue to report as before, it will be challenging for others and especially first-time preparers.

It is also an issue that is relevant to any legal adoption process (i.e., material outside the control of the ISSB can change over time at the discretion of others).

Question 2 — Objective (paras. 1–7)

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?

It is clear that the aim is to disclose material information pertaining to significant-sustainability-related risks and opportunities facing an entity.

However, as we note in responding to questions below, the terms "sustainability-related", "material" and "significant" require better clarification or guidance.

What is "sustainability": There is a need to explain what sustainability is intended to mean for the purpose of the ISSB's standards. The notion of "what matters to investors" to determine what a sustainability-related matter constitutes is likely to be difficult in practice given the relatively "late" recognition of sustainability-related matters in society in general (and by e.g., rating agencies) and the fact that the term "sustainability" is to some extent subjective and liable to change from time to time and is impacted by cultural factors between jurisdictions. For example, the EU Commission has outlined key sustainability-related matters for the purpose of its current initiatives relating to the development of sustainability reporting requirements. The ISSB has not done so, instead relying on entities being required to consider selected work and practices by others in their identification of what are potential sustainability-related risks and opportunities, before determining which are significant to the entity and what material information to disclose about them.

What is "significant": Para. 9 states*: "Sustainability-related risks and opportunities that cannot reasonably be expected to affect assessments of an entity's enterprise value by primary users of general purpose financial reporting* *are outside the scope of this [draft] Standard."* It would be helpful for the ISSB to be clear as to what criteria are used to determine whether or not a sustainability-related risk and opportunity is significant. For example – and as noted elsewhere – there is a difference between a sustainability-related risk or opportunity that could be expected to affect users' assessments as their assessment will also depending on the probability of occurrence and the expected magnitude of its impact should the risk or opportunity materialize. However, this consideration seems to be "reserved" as an issue to consider only in regard to materiality as per para. 57. Arguably, it should be seen as relevant for determining the relative significance of risks and opportunities (in financial reporting context this would be relevant in determining recognition), so it would make sense to include this in both the determination of which risks and opportunities need to be disclosed and in determining material information relevant to them.

Question 3 — Scope (paras. 8–10)

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?

From our perspective it makes sense for *IFRS Sustainability Disclosure Standards* to be developed on a jurisdiction and GAAP neutral basis.

Question 4 — Core content (paras. 11–35)

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 metrics and targets appropriate to their stated disclosure objective? Why or why not?

We generally agree with and support the disclosure objectives. We suggest that further clarification of certain specific requirements might be helpful:

- 13(e) trade-offs and sensitivity analysis – when would these be disclosed?
- Would disclosure of mitigative actions in para. 26 (d) be helpful? Or is this intended to be included under "manage"?
- Short, medium and long term perspectives in para. 22 (these are subject to reliability and assurability issues – as it is unclear what this should mean in practice). We agree the ISSB should not seek to define time periods, we agree that they should vary according to the entity's circumstances and so suggest clarification.
- Clarification of authority, hierarchy or not, onerous volume of material issues etc. re paras. 51 - 54 (see our response to q. 1).
- Reliability vs the assumed reliability of quantitative information in particular is also an issue to be addressed clearly.
- Possible overlap/duplication of information in the financial statements where para. 22(a) and (c) – cross referencing could be permitted and ISSB and IASB should collaborate fully.

Question 5 — Reporting entity (paras. 37–41)

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) 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?

(c) Do you agree with the proposed requirement for identifying the related financial statements? Why or why not?

We agree that the same reporting entity should be required to report.

We accept that the actions of associates, investments and joint ventures as well as others within the supply chain also potentially require disclosure. Without firmer criteria and a definition of what "sustainability-related" means preparers will find it challenging to determine what an investor really cares about in assessing enterprise value (investors do not necessarily know themselves and so this is changing rapidly – thus there are assurance issues in this area too exacerbated by the fact that this is less cut and dried than in the case of financial materiality). For this reason, firm criteria, including appropriate definitions will be needed to determine risks and opportunities along the value chain are essential for further standards. Para. 40 merely provides a few examples, whereas para. 53 relies on the work of others being appropriate until the ISSB has developed further standards.

Practicalities associated with obtaining reliable information (or in the absence using estimations based on industry norms etc.) need to be acknowledged in

IFRS S1 as do how to report on them (period of grace? Should the entity report on measures to obtain such data?). The issue of when is it not appropriate to disclose (i.e., not meeting the qualitative characteristics) also needs clarification in this context.

Question 6 — Connected information (paras. 42–44)

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?

Connected information e.g., impact of a specific activity affects several areas, so it is key that consistent assumptions are used.

We agree that connectivity between the financial statements and sustainability-related financial information is essential.

Connectivity has often been an issue brought up by the investor community some of whose members assert that the two separate reports (financial statements and the directors report that includes non-financial information) should present a cohesive view of the entity and supplement one another. We also note, for example, that the current SEC Proposals focus heavily on the impacts of sustainability-related matters on individual line items in the financial statements and that the draft EFRAG Standard ESRS 1 “General principles” respects the principle of connectivity to the financial statements.

Whilst we support entities providing an indication of how the entity’s strategy could be expected to impact the entity in general, we believe that quantitative disclosures of estimated financial impacts on financial statement items or financial metrics and targets could be misleading especially if viewed in an isolated context. To that end we challenge the example given in the second sentence as well as the penultimate sentences of para. 43 as we are not convinced that such disclosure would be sufficiently reliable as to be helpful to users.

We encourage a robust dialogue between the ISSB and IASB to ensure an appropriate degree of connectivity is achieved.

Question 7 — Fair presentation (paras. 45–55)

The Exposure Draft proposes that a complete set of sustainability-related financial disclosures would be required to present fairly the sustainability-related risks and opportunities to which an entity is exposed. Fair presentation would require the faithful representation of sustainability-related risks and opportunities in accordance with the proposed principles set out in the Exposure Draft. Applying IFRS Sustainability Disclosure Standards, with additional disclosure when necessary, is presumed to result in sustainability-related financial disclosures that achieve a fair presentation.

To identify significant sustainability-related risks and opportunities, an entity would apply IFRS Sustainability Disclosure Standards. In addition to IFRS Sustainability Disclosure Standards to identify sustainability-related risks and opportunities, the entity shall consider the disclosure topics in the industry-based SASB Standards, the ISSB's non-mandatory guidance (such as the CDSB Framework application guidance for water- and biodiversity-related disclosures), the most recent pronouncements of other standard-setting bodies whose requirements are designed to meet the needs of users of general purpose financial reporting, and sustainability-related risks and opportunities identified by entities that operate in the same industries or geographies.

To identify disclosures, including metrics, that are likely to be helpful in assessing how sustainability-related risks and opportunities to which it is exposed could affect its enterprise value, an entity would apply the relevant IFRS Sustainability Disclosure Standards. In the absence of an IFRS Sustainability Disclosure Standard that applies specifically to a sustainability-related risk and opportunity, an entity shall use its judgement in identifying disclosures that (a) are relevant to the decision-making needs of users of general purpose financial reporting; (b) faithfully represent the entity's risks and opportunities in relation to the specific sustainability-related risk or opportunity; and (c) are neutral. In making that judgement, entities would consider the same sources identified in the preceding paragraph, to the extent that they do not conflict with an IFRS Sustainability Disclosure Standard.

(a) Is the proposal to present fairly the sustainability-related risks and opportunities to which the entity is exposed, including the aggregation of information, clear? Why or why not?

(b) Do you agree with the sources of guidance to identify sustainability-related risks and opportunities and related disclosures? If not, what sources should the entity be required to consider and why? Please explain how any alternative sources are consistent with the proposed objective of disclosing sustainability-related financial information in the Exposure Draft.

We firmly support the explanation in para. 45 as to what a complete set of sustainability-related financial disclosure shall fairly present.

However, as explained elsewhere, we suggest the ISSB clarify the term "sustainability-related" in the context of its reporting standards.

Question 8 — Materiality (paras. 56–62)

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?

(d) Do you agree with the proposal to relieve an entity from disclosing information otherwise required by the Exposure Draft if local laws or regulations prohibit the entity from disclosing that information? Why or why not? If not, why?

We acknowledge that leveraging material on the “how to” in determining materiality from the IFRS practice note is likely helpful, but given the fact that the ISSB’s standards are designed to be GAAP neutral it would be preferable to move some of the illustrative guidance material into the Standards (e.g., the part on materiality and how to decide).

We note that the differences in the ISSB’s approach and the EFRAG’s approach to so-called double materiality issue have been widely discussed, and it is generally acknowledged that the (not immediately financially relevant) risks and opportunities arising from the entity’s impact on the planet, people and the economy will often be seen as material in terms of requiring disclosures under ISSB standards, given their (longer-term) ability to impact the entity’s reputation, customer base and regulatory actions. It would be helpful for the ISSB to outline this aspect in particular in regard to how the entity selects the disclosures, as we anticipate that this is likely to be a contentious area in terms of practical application.

Whilst we find the approach to materiality relatively straightforward, we suggest a few areas requiring better clarification:

<u>Criteria for determining significance of a sustainability-related risk or opportunity</u>

The proposal is for entities to disclose material information about all of the <u>significant</u> sustainability-related risks and opportunities to which it is exposed.

Para. 9 of the ED explains that sustainability-related risks and opportunities that cannot reasonably be expected to affect assessments of an entity's enterprise value by primary users of general-purpose financial reporting are outside the scope: implicitly all others are inside the scope.

The difference between a sustainability-related risk or opportunity and a <u>significant</u> sustainability-related risk or opportunity is unclear.

It is confusing that some parts of the standard e.g., para. 12 on governance, refer to sustainability-related risks and opportunities (implying this means <u>all</u> such risks and opportunities in scope and not solely the significant ones), whereas other parts refer specifically to significant sustainability-related risks and opportunities e.g., para. 14 on strategy and para. 16 and elsewhere.

It is also confusing that para. 19 refers to the role of para. 51 identifying significant sustainability-related risks and opportunities, whereas para. 51 itself requires consideration of different specified sources to identify sustainability-related risks and opportunities but is silent as to how the "significance test" should apply. Para. 40 lists possible sources of <u>significant</u> sustainability-related risks and opportunities to which the entity is exposed, some of which are outside the boundary of the reporting entity, whereas it seems implicit that not all such sources will involve or give rise to significant sustainability-related risks and opportunities for a particular entity. We suggest the ISSB clarify the criteria an entity shall apply in determining which sustainability-related risks and opportunities it has identified in applying para. 51 are <u>significant</u> and thus require the entity to report material information thereon.

It is implicit that what poses a sustainability-related risk or opportunity has to be determined in consideration of the individual circumstances of the entity and equally that the relative significance must also depend on the individual circumstances of the entity, i.e., the estimated potential (likelihood) to impact enterprise value in the short, medium or longer term and the estimated magnitude of such impact (see last sentence of para. 57). Thus, it appears that there are parallels to recognition criteria known in financial statements. Significance criteria equally need to be addressed for reasons of comparability.

It would be helpful to clarify the difference between the determination of significance and materiality. I.e., so as to clearly explain that the "significance test" is made in consideration of the individual circumstances of the entity, whereas the materiality test determining the information to be disclosed is made taking account of the perspective of the entity-specific primary users' assessments of enterprise value (as has been well explained in paras. 56 - 62). Arguably the weight attached to factors such as likelihood and impact play a role in determining significance - further clarification of the relationship between these factors and firmer criteria as to disclosure of the assumptions made would be helpful.

See para. 22 of ED IFRS S1. Would (b) not be expected to be reflected in the financial statements? Companies do not generally plan specific sources of funding in advance – and this may not be assurable. Would it be preferable to be transparent about such uncertainties rather than lending disclosures (e.g., 22c and d) a sense of quantifiability that does not exist? The time horizon is also an issue (what is reasonable as to be useful – this needs to vary according to the business model – it will preclude comparability even within the same industry).

Question 9 — Frequency of reporting (paras. 66–71)

The Exposure Draft proposes that an entity be required to report its sustainability-related financial disclosures at the same time as its related financial statements, and the sustainability-related financial disclosures shall be for the same reporting period as the financial statements.

Do you agree with the proposal that the sustainability-related financial disclosures would be required to be provided at the same time as the financial statements to which they relate? Why or why not?

Yes. In our view, the concurrent provision of financial statements and sustainability-related information is essential to achieve the aims of sustainability reporting, not least the role this plays in providing the entity itself with information to drive integrated thinking and sustainable business behaviour.

Some form of staggered approach to sustainability reporting may be helpful to alleviate the concerns as to preparer readiness we have outlined in responding to q. 13.

Question 10 — Location of information (paras. 72–78)

The Exposure Draft proposes that an entity be required to disclose information required by the IFRS Sustainability Disclosure Standards as part of its general *purpose financial reporting—i.e., as part of the same package of reporting that is targeted at investors and other providers of financial capital.*

However, the Exposure Draft deliberately avoids requiring the information to be provided in a particular location within the general purpose financial reporting so as not to limit an entity's ability to communicate information in an effective and coherent manner, and to prevent conflicts with specific jurisdictional regulatory requirements on general purpose financial reporting.

The proposal permits an entity to disclose information required by an IFRS Sustainability Disclosure Standard in the same location as information disclosed to meet other requirements, such as information required by regulators. However, the entity would be required to ensure that the sustainability-related financial disclosures are clearly identifiable and not obscured by that additional information.

Information required by an IFRS Sustainability Disclosure Standard could also be included by cross-reference, provided that the information is available to users of general purpose financial reporting on the same terms and at the same time as the information to which it is cross-referenced. For example, information required by an IFRS Sustainability Disclosure Standard could be disclosed in the related financial statements.

The Exposure Draft also proposes that when IFRS Sustainability Disclosure Standards require a disclosure of common items of information, an entity shall avoid unnecessary duplication.

(a) Do you agree with the proposals about the location of sustainability-related financial disclosures? Why or why not?

(b) Are you aware of any jurisdiction-specific requirements that would make it difficult for an entity to provide the information required by the Exposure Draft despite the proposals on location?

(c) Do you agree with the proposal that information required by IFRS Sustainability Disclosure Standards can be included by cross-reference provided that the information is available to users of general purpose financial reporting on the same terms and at the same time as the information to which it is cross-referenced? Why or why not?

(d) Is it clear that entities are not required to make separate disclosures on each aspect of governance, strategy and risk management for individual sustainability-related risks and opportunities, but are encouraged to make integrated disclosures, especially where the relevant sustainability issues

are managed through the same approach and/or in an integrated way? Why or why not?

From a German perspective, we support sustainability-related information being located within the management report. Comparability, integration and usefulness to users are all impacted by the location of disclosures on sustainability-related issues as they also seek to understand connectivity with the entity's financial statements. We would support the ISSB being clearer as to the relative benefits in terms of connectivity associated with the location of information to be disclosed as a way to foster comparability globally.

The use of cross referencing would need careful consideration in terms of availability to users and how to ensure that the source of any information included by cross-reference has been subject to the same level of assurance as any required in respect of sustainability-related financial information.

Question 11 — Comparative information, sources of estimation and outcome uncertainty, and errors (paras. 63–65, 79–83 and 84–90)

The Exposure Draft sets out proposed requirements for comparative information, sources of estimation and outcome uncertainty, and errors. These proposals are based on corresponding concepts for financial statements contained in IAS 1 and IAS 8. However, rather than requiring a change in estimate to be reported as part of the current period disclosures, the Exposure Draft proposes that comparative information which reflects updated estimates be disclosed, except when this would be impracticable —i.e., the comparatives would be restated to reflect the better estimate.

The Exposure Draft also includes a proposed requirement that financial data and assumptions within sustainability-related financial disclosures be consistent with corresponding financial data and assumptions used in the entity's financial statements, to the extent possible.

(a) Have these general features been adapted appropriately into the proposals? If not, what should be changed?

(b) Do you agree that if an entity has a better measure of a metric reported in the prior year that it should disclose the revised metric in its comparatives?

(c) Do you agree with the proposal that financial data and assumptions within sustainability-related financial disclosures be consistent with corresponding financial data and assumptions used in the entity's financial

statements to the extent possible? Are you aware of any circumstances for which this requirement will not be able to be applied?

We agree with the proposals. Whilst not specifically addressed in the question on this section, we believe that the requirement proposed in para. 83 regarding disclosure of significant outcome uncertainty is essential such that it is clear that the entity is reporting on various potential scenarios not probabilities.

Question 12 — Statement of compliance (paras. 91-92)

The Exposure Draft proposes that for an entity to claim compliance with IFRS Sustainability Disclosure Standards, it would be required to comply with the proposals in the Exposure Draft and all of the requirements of applicable IFRS Sustainability Disclosure Standards. Furthermore, the entity would be required to include an explicit and unqualified statement that it has complied with all of these requirements.

The Exposure Draft proposes a relief for an entity. It would not be required to disclose information otherwise required by an IFRS Sustainability Disclosure Standard if local laws or regulations prohibit the entity from disclosing that information. An entity using that relief is not prevented from asserting compliance with IFRS Sustainability Disclosure Standards.

Do you agree with this proposal? Why or why not? If not, what would you suggest and why?

We agree in principle, as we would hope that this consultation and further development of the ED would serve to ensure that the final standards would seek to avoid requiring disclosure of legally prohibited information. Transparency as proposed in para. 62 within the statement of compliance will be key to ensuring readers understand the “validity” of any departures from the standards which ought to occur only in extremely rare circumstances. We do not believe unclear or partial statements of compliance are helpful.

However, as noted elsewhere we suggest users would benefit from a better clarification of the term “sustainability-related” or failing this, at least the role of material promulgated by others (see our response to q. 1 above) accompanied by a disclosure outlining the specific external sources the entity has considered in complying with the requirements of paras. 50 - 55, especially when it has considered (additional) risks and opportunities identified by entities that operate in the same industries or geographies (see para. 51(d)) or metrics used by such entities (see para. 54). Para. 55 requires only disclosure of the relevant industry or industries considered.

Question 13 — Effective date (Appendix B)

The Exposure Draft proposes allowing entities to apply the Standard before the effective date to be set by the ISSB. It also proposes relief from the requirement to present comparative information in the first year the requirements would be applied to facilitate timely application of the Standard.

(a) When the ISSB sets the effective date, how long does this need to be after a final Standard is issued? Please explain the reason for your answer, including specific information about the preparation that will be required by entities applying the proposals, those using the sustainability-related financial disclosures and others.

(b) Do you agree with the ISSB providing the proposed relief from disclosing comparatives in the first year of application? If not, why not?

We acknowledge the ISSBs recognition of this issue, and are concerned as to the potential tension between the different levels of entity preparedness and the impact on market needs and enforcement issues and the desire not to delay action on reporting relating to key sustainability matters. In this context, we note that even though financial statement reporting is relatively mature, the statistics on deficient financial reporting depicted in reports on oversight findings issued by national oversight authorities or others such as ESMA and IFIAR in respect of financial statements are of concern to financial statement users.

Sustainability reporting will be a “new” area for many companies. There will need to be appropriate “lead-in” time for preparers to establish robust information collection and control systems for this type of reporting for clarification of practical challenges relating to interpretation of standards and potentially for meaningful assurance to be feasible.

A big bang approach (whereby all reporting entities are required to report on a comprehensive basis on all aspects of sustainability from the outset) carries the risk that many entities may not be ideally prepared to comply with the standards and – if forced to do so whilst lacking the necessary degree of maturity of internal systems and controls over data collection and presentation – will not provide the market with the quality of information it needs.

In this regard we would support the ISSB considering any potential for scalability as its work progresses. We refer to our letter regarding ED IFRS S2 in which we expand upon this in the context of climate-related reporting.

Question 14 — 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?

In our view, and subject to our comments made elsewhere on the need for clarification of terms and guidance and further alignment with other initiatives via its Jurisdictional Working Group, we believe that the proposed IFRS Sustainability Disclosure Standards can provide a suitable global baseline.

We would also urge the ISSB to align terminology used with other major sustainability standard setters and in particular EFRAG, especially for reasons of compatibility that many users are demanding.

Question 15 — Digital reporting

The ISSB plans to prioritise enabling digital consumption of sustainability-related financial information prepared in accordance with IFRS Sustainability Disclosure Standards from the outset of its work. The primary benefit of digital consumption as compared to paper-based consumption is improved accessibility, enabling easier extraction and comparison of information. To facilitate digital consumption of information provided in accordance with IFRS Sustainability Disclosure Standards, an IFRS Sustainability Disclosures Taxonomy is being developed by the IFRS Foundation. The Exposure Draft and [draft] IFRS S2 Climate-related Disclosures Standards are the sources for the Taxonomy.

It is intended that a staff draft of the Taxonomy will be published shortly after the release of the Exposure Draft, accompanied by a staff paper which will include an overview of the essential proposals for the Taxonomy. At a later date, an Exposure Draft of Taxonomy proposals is planned to be published by the ISSB for public consultation.

Do you have any comments or suggestions relating to the drafting of the Exposure Draft that would facilitate the development of a Taxonomy and digital reporting (for example, any particular disclosure requirements that could be difficult to tag digitally)?

We support the ISSB's stated intention to prioritise enabling digital consumption of sustainability-related financial information prepared in accordance with IFRS Sustainability Disclosure Standards.

Question 16 — Costs, benefits and likely effects

The ISSB is committed to ensuring that implementing the Exposure Draft proposals appropriately balances costs and benefits.

(a) Do you have any comments on the likely benefits of implementing the proposals and the likely costs of implementing them that the ISSB should consider in analysing the likely effects of these proposals?

(b) Do you have any comments on the costs of ongoing application of the proposals that the ISSB should consider.

We anticipate that certain aspects of ED IFRS S1 will introduce significant costs. In particular as explained in our cover letter the lack of clarification of the term "sustainability-related" instead relying on individual preparers considering the work of others to identify potential matters to be reported (paras. 51 and 54) will likely be (unnecessarily) costly.

From a German perspective, we also encourage the ISSB to work closely with EFRAG to ensure differences between the respective reporting requirements are minimised, such that any preparers who may have to apply both sets of standards do not incur undue costs.

We also refer to our response to ED IFRS S2 in this regard.

Question 17 — Other comments

Do you have any other comments on the proposals set out in the Exposure Draft?

<u>Information used in managing the business vs required to be reported</u>

Information used in managing the business will be available and “known” by management, the financial statement auditor and often to key investors. Where the reporting requirements may potentially go beyond this to include metrics and targets that are either not used in the day-to-day management or are not required under sustainability reporting standards used so far, disclosure can be problematical. There is a practical concern that management (and auditors) may not always be able to identify and “quantify” all the issues that can affect enterprise value in as timely a manner as would be needed. Thus, it is sensible to ensure the information required does reflect the way in which an entity operates covering governance strategy risk management and metrics and targets (as per the introduction on page 6 “*The information required reflects the way in which an entity operates … building on well-established work of the TCFD”*) and not imply a requirement to go beyond this.

We refer to comments above and in our comment letter regarding ED IFRS S2 in regard for the need for the ISSB to consider scalability more thoroughly as it finalizes these standards and progresses its work further.