Responsible Investment Association Australasia

Submission
AASB ED 321: Comment on ISSB Draft Standards – S1 *General Requirements for Disclosure of Sustainability-related and Financial Information* and S2 *Climate-related Disclosures*

15 July 2022

Overview

The Responsible Investment Association Australasia (RIAA) thanks the Australian Accounting Standards Board (AASB) for the opportunity to comment on AASB Exposure Draft ED321, on the Australian implementation of the ISSB's [Draft] IFRS S1 *General Requirements for Disclosure of Sustainability-related and Financial Information* and [Draft] IFRS S2 *Climate-related Disclosures* (draft ISSB Standards).

RIAA strongly supports prompt, mandatory implementation of the ISSB Standards in Australia. The Standards are a natural and welcome progression from Australia's existing legal obligations for companies to manage and disclose climate risk, and the Standards build on the well-established TCFD reporting framework. Implementation of the Standards is an important opportunity for Australia to embed a world-leading regulatory environment for sustainability disclosures.

Full and effective implementation of the ISSB Standards in Australia will significantly improve the extent and accuracy of climate-related information in our markets. It will enable investors and others to more accurately gauge the risks and value of companies, and to make better-informed decisions. It will ultimately boost efforts towards improving sustainability outcomes in Australia and align reporting in Australia with international reporting frameworks. This is critical to ensuring that Australian markets remain attractive to investors and internationally viable.

While RIAA's detailed comments on the ISSB Standards will be contained in our submissions to the ISSB, we highlight the following issues for the AASB's consideration:

- In relation to both [Draft] IFRS S1 and IFRS S2, we support clarification by the ISSB of a comprehensive definition of 'materiality' that is focused on long term view and a consideration of a company's impacts and dependencies on people, the planet and the economy as an important element of both proposed Standards.
- In relation to [Draft] IFRS S2, we strongly support mandatory disclosure of scope 3 greenhouse gas (GHG) emissions. We support the specified industry-based disclosure requirements, acknowledging these may require further work to identify and address any gaps or lack of clarity.
- We will strongly support the Australian Government and regulators to do all that is required to promptly and effectively implement the ISSB Standards as baseline standards for reporting in Australia.

- The Australian Government and regulators should take a ‘building blocks’ approach to the ISSB baseline, to ensure Australia’s disclosure requirements are comprehensive, effective and represent global leadership.
- All for-profit entities should be required to report against the ISSB Standards. We refer to the Australian Sustainable Finance Institute (ASFI) Roadmap recommendations 11 and 12 in relation to the types of entities that should first report against the Standards.
- We broadly support the AASB’s proposal that the ISSB Standards be adopted as standalone in Australia, while leaving open the option for integrated sustainability and financial reporting.

Response to questions

Part A: Matters for comment relating to specific proposals in Exposure Draft on [Draft] IFRS S1

A1. Exposure Draft on [Draft] IFRS S1 is proposing that entities be required to disclose information that is material and gives insight into an entity’s sustainability-related risks and opportunities that affect enterprise value. Is focusing on an entity’s enterprise value the most appropriate approach when considering sustainability-related financial reporting? If not, what approach do you suggest and why?

We detail our view on ‘materiality’ under [Draft] IFRS S1 and IFRS S2 in our submission to the ISSB. Our following comments apply to both proposed Standards.

The definition of materiality encompasses a broad view of the risks and opportunities that may affect enterprise value. This includes ‘information about a company’s impacts and dependencies on people, the planet and the economy when relevant to the assessment of the company's enterprise value’.[1]

From an investor perspective, enterprise value encompasses the external impacts a company has on people, planet and the economy that will financially impact the company in the medium to long term. These would include external impacts that lead to consumer backlash, stranded assets, action by regulators, litigation, law reform or other potential consequences which will affect enterprise value. A long-term view of enterprise value is critical to investors as primary users of the disclosures under the proposed standards. This comprehensive interpretation of materiality on enterprise value – sometimes referred to as double materiality – is an important element of the standards that we are recommending be further clarified by the ISSB. We also commend this approach to the AASB, consistent with global leading practices.

Part B: Matters for comment relating to specific proposals in Exposure Draft on [Draft] IFRS S2

B1. To comply with the proposals in Exposure Draft on [Draft] IFRS S2 an entity would be required to disclose its Scope 3 greenhouse gas (GHG) emissions in addition to its Scope 1 and 2 GHG emissions. Do you agree that Australian entities should be required to disclose their Scope 3 GHG emissions in addition to their Scope 1 and Scope 2 GHG emissions? If not, what changes do you suggest and why?

B2. To comply with the proposals related to GHG emissions disclosures in Exposure Draft on [Draft] IFRS S2 an entity would be required to apply the Greenhouse Gas Corporate (GHGC) Standard. Do you agree that Australian entities should be required to apply the GHGC Standard given existing GHG emissions legislation and guidance in

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[1] ISSB, *Snapshot of Exposure Draft IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information and Exposure Draft S2 Climate-related Disclosures*, page 3.

place for Australian entities (for example, the NGER Act, NGER (Measurement) Determination 2008 and related guidance)?

B3. Are the proposed industry-based disclosure requirements in Appendix B to Exposure Draft on [Draft] IFRS S2 relevant for Australian industries and sectors? If not, what changes do you suggest and why?

B4. Are there any Australian-specific climate-related matters that the AASB should consider incorporating into the requirements proposed in Exposure Draft on [Draft] IFRS S2? For example, given the Exposure Draft on [Draft] IFRS S2 is the starting point for the AASB's work on climate-related financial disclosure, should there be additional reporting requirements for Australian entities? If so, what additional reporting requirements should be required and why?

Emissions disclosure

RIAA strongly agrees that entities should disclose scope 3 GHG emissions, in line with Draft IFRS S2 and the October 2021 Annex to the TCFD Recommendations.

The ISSB Standard will become a global baseline, which will elevate the consistency, comprehensiveness and comparability of disclosures. Derogation from the global baseline, particularly on such a significant aspect, would not be in line with the intent and direction of global standards setting and would be detrimental to Australia's attractiveness to international investors and integration into international markets.

For investors, scope 3 emissions disclosures are critical in assessing the risks in a company's value chain, for example, the company's financed emissions. Scope 3 emissions can highlight where a company is vulnerable, particularly to physical risk and transition risk, and provide a clearer and more comprehensive picture of enterprise value. The requirement to disclose scope 3 emissions will align the market with the expectations of investors and their beneficiaries to be transparent about climate risks and opportunities, and, more broadly, the company's impact on people and planet.

For companies already disclosing scope 3 emissions, this requirement under [S2] will better equalise markets by bringing competitors up to leading practices. For companies not already disclosing scope 3 emissions, it will prompt better understanding of climate risks and opportunities, and their ability to manage a range of physical, transitional, regulatory, reputational and other risks.

For Australia, it will ensure our regulatory environment better aligns with international regulatory environments and places us as an attractive market for investment, including overseas investment.

We also broadly agree with the proposal to require entities to use the international standard. International consistency should be a key objective of implementing the ISSB Standards in Australia. We are not aware of any lack of alignment between the international standard and Australian requirements. Any inconsistencies should be resolved in line with the aim of global consistency.

Industry-based disclosure requirements

RIAA supports the inclusion of specified industry-based requirements in IFRS Draft S2 Appendix B, based on the SASB Standards.

The SASB Standards are increasingly used in Australia. Adopting the industry-based requirements from the international standard in Australia will improve the comparability of disclosures. However, to ensure the industry-specific standards are comprehensive and practical, the ISSB will have further work to do in field testing the standards globally, including identifying and addressing any gaps or lack of clarity.

Part C: Matters for comment relating to both Exposure Drafts on [Draft] IFRS S1 and [Draft] IFRS S2

C1. Which Australian entities should be expected to apply the proposals in Exposure Drafts on [Draft] IFRS S1 and [Draft] IFRS S2 and why? Specifically:

(a) should the proposals be intended for all for-profit entities in Australia or only to a subset of for-profit entities? And

(b) should relief from specific aspects of the proposals be permitted for some entities for which the proposals are deemed burdensome (for example, Scope 3 GHG emissions and scientific and scenario analyses)? If so, which entities and why?

C2. Are there any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals in Exposure Drafts on [Draft] IFRS S1 and [Draft] IFRS S2?

C3. Do the proposals in Exposure Drafts on [Draft] IFRS S1 and [Draft] IFRS S2 align with existing or anticipated requirements, guidance or practice in Australia? If not:

(a) please explain the key differences that may arise from applying the proposals in Exposure Drafts on [Draft] IFRS S1 and [Draft] IFRS S2 and the impact of any such differences; and

(b) do you suggest any changes to the proposals in Exposure Drafts on [Draft] IFRS S1 and [Draft] IFRS S2?

C4. Would the proposals in Exposure Drafts on [Draft] IFRS S1 and [Draft] IFRS S2 result in useful information for primary users of general purpose financial reports?

C5. Do the proposals in Exposure Drafts on [Draft] IFRS S1 and [Draft] IFRS S2 create any auditing or assurance challenges?

C6. When should the proposals in Exposure Drafts on [Draft] IFRS S1 and [Draft] IFRS S2 be made effective in Australia and why?

C7. Should the effective date of the proposals in Exposure Draft on [Draft] IFRS S1 be consistent with, or set for a date after, the effective date of the proposals in Exposure Draft on [Draft] IFRS S2? If so, why?

C8. Would any wording or terminology introduced in Exposure Drafts on [Draft] IFRS S1 and [Draft] IFRS S2 be difficult to understand? If yes, what changes do you suggest and why?

C9. Unless already provided in response to specific matters for comment A1 to C8 above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative. In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental cost.

Implementation in Australia

The standards should apply to all Australian for-profit entities. As a starting point, the ASFI Roadmap recommends that all ASX 300 companies and all financial institutions with annual consolidated revenue of over $100 million should report against the TCFD on an 'if not why not' basis by 2023 (recommendations 11 and 12). As a leading participant in the ASFI Roadmap, RIAA supports, as a minimum starting point, immediate implementation of IFRS S2 for those entities.

We understand that, if the standards are implemented in Australia on a standalone basis as proposed (that is, not within the Australian Accounting Standards) legislative change will be required to mandate compliance with the standards. We strongly support the Australian Government promptly consulting on and implementing the law reform required.

RIAA will submit to the ISSB that the standards should be effective as soon as possible after they are finalised. This will enable Australia and other countries to make the legislative and regulatory changes required at the national level to mandate the standards.

The implementation of these standards is a natural progression from the current regulatory position of regulators encouraging listed companies to report against the TCFD framework. It is also in the context of existing legal requirements to manage climate change risk and disclose climate risk which is material to a company's financial performance. RIAA will strongly support Australian regulators to promptly enact any regulatory changes additional to legislative reform that are required to fully and effectively implement the standards. The implementation of these standards is an opportunity for Australia to shift from a less-developed regulatory environment to one which represents global leadership.

Many companies, particularly larger listed companies, are currently well-placed to start complying with the standards, having committed to reporting under the TCFD framework. ASX 200 companies are rapidly committing to TCFD reporting. The Australian Council of Superannuation Investors found that in 2020, 80 companies had adopted the TCFD framework, versus just 11 companies in 2017. It is likely that majority of ASX 200 companies are now using the TCFD framework.[2] Transitional arrangements may be required for some entities, depending on entity size and industry sector.

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[2] Australian Council of Superannuation Investors, *Promises, pathways & performance: Climate change disclosure in the ASX200*, August 2021, p 5.

‘Building blocks’ approach
Given the ISSB Standards are not yet finalised, if there is any change which detracts from the comprehensiveness of the current proposals (for example, the final S2 does not mandate reporting on Scope 3 GHG emissions) we will urge the Australian Government and regulators to mandate the higher standard, in addition to the ISSB framework. This would be in line with the ‘building blocks’ approach to national implementation of the ISSB baseline. Australia can mandate more practical and effective requirements which are consistent with, but go over and above, the baseline.

We also encourage the Australian Government and regulators to keep pace with future international developments in disclosure standards, and similarly use the building blocks approach to ensure Australia leads on the regulation of sustainability disclosures.

Usefulness to investors and cost benefit

The ISSB Standards, as a comprehensive global baseline for sustainability-related disclosures, should significantly improve the consistency, reliability and comparability of sustainability related disclosures.

While many companies are already reporting comprehensive sustainability-related information to markets, including in Australia, the global baseline will enable investors to better understand, compare and analyse disclosures. This will boost their understanding of investment risks and opportunities, shape investment strategies and enable investors to make more efficient and well-informed decisions. It will also enable investors to meet their beneficiaries’ increasing expectations of transparency and sustainable and net zero-aligned investment approaches.

From the perspective of reporting entities, a comprehensive global baseline would, over time, streamline reporting costs, lower transaction costs, facilitate smoother cross-border capital flows, reduce market segmentation and increase market confidence, and has the potential to improve internal understanding of risks and opportunities. It could inform more sustainable business opportunities and ventures. ‘Good’ reporting against the ISSB Standards will signal to investors that an entity is committed to improving the sustainability of its business, and is capably managing its related risks and opportunities.
There is clear value in the ISSB’s global baseline in a range of jurisdictions. For example, Aotearoa New Zealand is forging ahead on mandating climate-related disclosures, with its own standard now in development and due to commence in 2023. That process is happening in parallel with, and informed by, the ISSB Standards. Conversely, the swift implementation of the ISSB’s comprehensive global baseline in Australia will enable us, and other countries at a similar stage, to swiftly move forward with disclosures regulation and be on par with other nations. It will enable Australian regulators and companies to prepare for higher standards of disclosures going forward as standards lift internationally.

Part D: Matters for comment relating to the AASB’s proposed approach

D1. Do you agree with the AASB’s proposed approach to developing sustainability-related financial reporting requirements as a separate suite of standards? As an alternative model, the AASB would value comments as to whether sustainability-related financial reporting requirements should be developed as part of existing Australian Accounting Standards. The alternative model would result in sustainability-related financial disclosures forming part of an entity’s general purpose financial statements.
D2 Are the proposals in Exposure Drafts on [Draft] IFRS S1 and [Draft] IFRS S2 in the best interests of the Australian economy?

Separate versus integrated reporting

We broadly support the AASB’s proposed approach, as separate sustainability disclosures reported at the same time as an entity’s general purpose financial statements, with connected information (as proposed under the ISSB Standards), can be clear and practical for users.

However, integrated sustainability and financial reporting is increasingly common in corporate reporting. Given Australia is likely to follow global trends in future, we support a model which leaves open the option for companies to prepare integrated sustainability and financial reports.

Best interests of the Australian economy

In our view, while there are issues to clarify in S1, the proposals in the draft ISSB Standards are clearly in the best interests of the Australian economy.

Investors need high-quality, comprehensive, comparable information about companies to make decisions about where to direct capital to align with both financial and sustainability objectives.

Implementation of the ISSB Standards will be critical to Australian markets remaining attractive to investors. Our global trade and investment partners are bedding down climate and sustainability disclosures regimes. Those regimes will support sustainable investment and ultimately boost the power of capital to support national and global sustainability and climate change goals. Australia must engage with international regulatory efforts to remain a globally viable market.

Investment can play a key role in supporting a prosperous and sustainable future for our nation, from building infrastructure and supporting affordable housing to investing in new technologies and financing the transition to net zero emissions. A strong and effective sustainability disclosure regime is a critical element in building confident and robust markets, which will ensure Australia has a strong, stable and resilient financial system that continues to attract capital.

About RIAA and our members

RIAA champions responsible investing and a sustainable financial system in New Zealand and Australia and is dedicated to ensuring capital is aligned with achieving a healthy society, environment, and economy.

With approximately 500 members managing more than US$29 trillion in assets globally, RIAA is the largest and most active network of people and organisations engaged in responsible, ethical and impact investing across New Zealand and Australia. RIAA's membership includes superannuation funds, KiwiSaver default providers, fund managers, banks, consultants, researchers, brokers, property managers, community trusts, foundations, faith-based groups, financial advisers, financial advisory groups, and others involved in the finance industry, across the full value chain of institutional to retail investors.