IFRS Sustainability

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Exposure Draft

IFRS® Sustainability Disclosure Standard

Basis for Conclusions on [Draft] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information

Comments to be received by 29 July 2022

International Sustainability Standards Board

ED/2022/S1

Basis for Conclusions on

Exposure Draft

General Requirements for Disclosure of Sustainability-related Financial Information

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This Basis for Conclusions accompanies the ED/2022/S1 *Exposure Draft General Requirements for Disclosure of Sustainability-related Financial Information* (published March 2022; see separate booklet). It is published by the International Sustainability Standards Board (ISSB) for comment only. Comments need to be received by 29 July 2022 and should be submitted by email to commentletters@ifrs.org or online at https://www.ifrs.org/projects/open-for-comment/.

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Basis for Conclusions on [Draft] IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information*

This Basis for Conclusions accompanies, but is not part of, [draft] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information.

Background

BC1 In announcing the creation of the International Sustainability Standards Board (ISSB), the Trustees of IFRS Foundation (Trustees) emphasised that the ISSB would build on the work of investor-focused reporting initiatives to become the global standard-setter for sustainability disclosures for financial markets, which was consistent with responses to the Trustees' 2020 consultation on sustainability reporting. Acknowledging respondents' statements about the urgent need for such standard-setting, the Trustees sought to provide the ISSB with a solid foundation on which to start work. In March 2021, the Trustees recruited members of some reporting initiatives to create the Technical Readiness Working Group (TRWG), chaired by the IFRS Foundation (the Foundation), to provide recommendations to the ISSB. The TRWG comprised representatives from:

- the Climate Disclosure Standards Board (CDSB);
- the International Accounting Standards Board (IASB);
- the Task Force on Climate-related Financial Disclosures (TCFD);
- the Value Reporting Foundation, which represents:
  - the Sustainability Accounting Standards Board (SASB);
  - the International Integrated Reporting Council (IIRC); and
- the World Economic Forum and its Measuring Stakeholder Capitalism Initiative.

The International Organization of Securities Commissions (IOSCO) and the International Public Sector Accounting Standards Board participated as official observers.

BC2 The Exposure Draft builds on a prototype developed by the TRWG, which in turn evolved from work published in December 2020 by a group of five standard-setters and framework-providers focused on corporate sustainability and integrated reporting. This 'group of five' standard-setters and framework-providers—CDP (formerly the Carbon Disclosure Project), CDSB, the Global Reporting Initiative, the IIRC and the SASB—co-authored a paper illustrating how their complementary frameworks, standards and platforms could be consolidated to focus on the aspects set out by the TCFD to provide a running start for the development of a single set of global standards that could enable disclosure of how sustainability risks and opportunities create, preserve or erode an entity's enterprise value. The group of five effort was, in large part, a direct response to an increasingly fragmented approach to sustainability reporting and calls for the creation of a coherent and comprehensive system of corporate disclosure.[1]

BC3 The TRWG took up the group of five prototype as its starting point. From March to November 2021, the TRWG refined the prototype through technical collaboration which included seeking input from some preparers and investors. The TRWG also identified market feedback and technical issues that had yet to be addressed or that warranted further consideration to enable these matters to be raised with the ISSB. The TRWG's refinements also reflected input from a Technical Experts Group created by IOSCO to help ensure that a standard based on the prototype would facilitate disclosure that could meet the needs of global capital markets. A high-level overview of the latter group's assessment was published in June 2021 in IOSCO's *Report on Sustainability-related Issuer Disclosures*.

BC4 The TRWG's work on general requirements for disclosure of sustainability-related financial information resulted in publication in November 2021 of a prototype, *General Requirements for Disclosure of Sustainability-related Financial Information* (*General Requirements*), on the Foundation's website. However, the prototype was not subject to the Foundation's formal due process or that of any members of the TRWG.

BC5 Since the publication of the *General Requirements* prototype, the ISSB Chair and Vice-Chair have sought to address matters raised by the TRWG. The Exposure Draft is mainly based on the evolution of the *General Requirements* prototype; it is underpinned by the work of standard-setters and framework-providers that has been subject to extensive public consultation and redeliberation and has achieved significant market uptake. Proposals in the Exposure Draft that are substantive changes from the *General Requirements* prototype, rather than changes to improve clarity, are highlighted in the Basis for Conclusions.

Overview of the approach taken in the Exposure Draft

The need for [draft] IFRS S1

BC6 These proposals were developed in response to calls from primary users of general purpose financial reporting for more consistent, complete, comparable and verifiable sustainability-related financial information to enable them to assess an entity's enterprise value.[2] As competitive conditions change, an entity's ability to remain resilient will rely on a range of non-financial sources of value. Such sources could include its workforce, the specialised knowledge it has developed, or its relationships with local communities and natural resources. Users, therefore, seek information about the significant sustainability-related risks and opportunities facing an entity to inform their decisions about providing resources to the entity. Such

1 See 'Reporting on enterprise value: Illustrated with a prototype climate-related financial disclosure standard' (https://29kjwb3armds2g3gi4lq2sx1-wpengine.netdna-ssl.com/wp-content/uploads/Reporting-on-enterprise-value_climate-prototype_Dec20.pdf).

2 Throughout this Basis for Conclusions, the terms 'primary users' and 'users' are used with the same meaning and refer to existing and potential investors, lenders and other creditors.

information supplements and complements the information contained in the entity's financial statements.

BC7 Sustainability-related risks and opportunities arise from an entity's impacts and dependencies on resources and from the relationships the entity maintains that may be positively or negatively affected by those impacts and dependencies. When an entity's business model depends, for example, on a natural resource—such as water—it is likely to be affected by changes in the quality, availability or pricing of that resource. When an entity's activities result in adverse external impacts—for example on local communities—it is likely to be subjected to consequences such as stricter government regulation and reputational damage. Less directly, but no less importantly, when an entity's business partners face significant sustainability-related risks and opportunities, the entity could be exposed to related consequences of its own. When such impacts, dependencies and relationships create risks or opportunities for an entity's objectives, they can create or erode the entity's enterprise value and the financial returns to providers of financial capital.

BC8 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 cost of capital. The information contained in its financial statements and the information included in an entity's sustainability-related financial disclosures are essential inputs to the assessment a user of general purpose financial reporting makes of the enterprise value of an entity. If approved, the proposals would establish general requirements for an entity to disclose material information about all of the significant sustainability-related risks and opportunities to which it is exposed.

The Exposure Draft

BC9 The Exposure Draft sets out the proposed overall requirements for disclosing sustainability-related financial information to provide users of general purpose financial reporting with a complete set of sustainability-related financial disclosures. It is intended to meet the needs of users who are not in a position to require an entity to prepare reports tailored to their particular information needs.

BC10 An entity would be required to disclose material information about all of the significant sustainability-related risks and opportunities to which it is exposed. The Exposure Draft includes proposed requirements and guidance to support the disclosure of material information about significant sustainability-related risks and opportunities not specifically addressed by an existing IFRS Sustainability Disclosure Standard.

BC11 The information required would represent core aspects of the way in which an entity operates—governance, strategy, risk management and metrics and targets. This approach reflects feedback on key requirements for success in the Trustees' 2020 consultation on sustainability reporting, and builds upon the well-established work of the TCFD. The Exposure Draft uses definitions and requirements that are consistent with the IASB's *Conceptual Framework for*

Financial Reporting, IAS 1 *Presentation of Financial Statements* and IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

BC12 The Exposure Draft proposes that an entity's sustainability-related financial disclosures be made in relation to the same reporting entity as that to which its general purpose financial statements refer, and that the sustainability-related financial information be disclosed at the same time as the financial statements.

BC13 To be able to assert compliance with IFRS Sustainability Disclosure Standards, an entity must meet all the requirements of IFRS Sustainability Disclosure Standards.

Status of the proposals

BC14 The Exposure Draft would apply to sustainability-related financial information disclosed as part of an entity's general purpose financial reporting. The Exposure Draft is designed to require information that would complement that contained in an entity's financial statements, regardless of which GAAP the entity has used when preparing those financial statements. Because the Exposure Draft is being developed by the ISSB, a standard-setting body of the Foundation, it uses terminology, guidance and concepts consistent with those in IFRS Accounting Standards when applicable. The TRWG found that such an approach would not, in any way, limit the suitability of IFRS Sustainability Disclosure Standards for entities applying a GAAP and not IFRS Accounting Standards.

BC15 The Exposure Draft sets out proposals for general requirements that apply to the disclosure of sustainability-related financial information and forms the basis on which complementary standards that set out more specific disclosure requirements will be developed.

BC16 The Exposure Draft is designed to be capable of being applied in the context of various jurisdictional requirements. The proposals are intended to accommodate the laws and regulations in the various jurisdictions in which entities operate, including where those laws or regulations specify the disclosure of particular information in specific documents, formats and structures. The proposals, therefore, permit entities to report information needed to meet public policy objectives and jurisdictional regulatory requirements alongside information required by IFRS Sustainability Disclosure Standards. This approach will also allow public policy needs to be met by enabling entities using IFRS Sustainability Disclosure Standards to provide supplementary information that meets regulatory requirements and the information needs of other stakeholders, provided that any additional disclosures do not obscure the information required by IFRS Sustainability Disclosure Standards. The proposals are consistent with the objective of enabling IFRS Sustainability Disclosure Standards to be interoperable with other jurisdictional reporting requirements while meeting the needs of the capital markets.

Relationship with other IFRS Sustainability Disclosure Standards

BC17 The Exposure Draft sets out proposed general requirements that must be applied for an entity to be able to state compliance with IFRS Sustainability Disclosure Standards. It identifies the core content of a complete set of sustainability-related financial disclosures and sets out the qualitative characteristics of useful sustainability-related financial information.

BC18 The Exposure Draft establishes a basis for more robust and comparable reporting of sustainability-related financial information by proposing that some established practices from financial reporting be applied. In particular, the Exposure Draft includes a proposed requirement that an entity must disclose comparative information, identify the related financial statements and provide the sustainability-related financial information at the same time as the financial statements. The Exposure Draft also includes proposed requirements for correcting errors and updating estimates. The Exposure Draft, therefore, serves a similar role for sustainability-related financial disclosures as the IASB's *Conceptual Framework for Financial Reporting*, IAS 1 and IAS 8 serve for general purpose financial statements prepared in accordance with IFRS Accounting Standards.

Due process provisions applicable to the Exposure Draft

BC19 The urgent need for the ISSB to deliver its initial Standards has been repeatedly highlighted, including in feedback to the September 2020 consultation on sustainability reporting held by the Trustees and to the April 2021 Exposure Draft of proposed amendments to the Foundation *Constitution*. IOSCO has also emphasised the urgent need for disclosure standards on climate change. Such urgency can pose significant challenges to standard-setting, which aims to achieve effective outcomes by balancing timely responsiveness to market needs with the rigour of formal due process.

BC20 The Trustees recognised the opportunity to use and build upon existing sustainability standards and frameworks, including those developed in accordance with prior due process by the organisations that developed them and that enjoy broad user and preparer support. The main components of the Exposure Draft are based on work that has been subject to extensive public consultation and redeliberation and have since garnered significant market uptake. The Trustees viewed this as a signal these foundational standards and frameworks help to address the information needs of investors and other capital market participants.

BC21 The Trustees noted the need for prompt action and the background to the content of the Exposure Draft. However, they also noted that this does not negate the need for formal due process and exposure by the ISSB. It is important that the ISSB's stakeholders are given the opportunity to provide feedback on the proposals consistent with the Foundation's inclusive and thorough due process.

BC22 To balance the need to advance the work of the ISSB on a timely basis while obtaining input from interested parties, the Trustees decided to grant special powers to the Chair and Vice-Chair of the ISSB to enable timely publication of initial exposure drafts for stakeholder input. The Trustees agreed it would be appropriate that as the ISSB is being established (ie as a transitional measure) the ISSB Chair and Vice-Chair be provided with the ability to publish exposure drafts of a climate-related disclosure standard and/or a general requirements disclosure standard. This decision is reflected in paragraph 56 of the Foundation *Constitution* published in November 2021.

BC23 The effect of this provision in the *Constitution* is only to enable the exposure drafts to be published prior to the ISSB being quorate. The exposure drafts are subject to public consultation and will be redeliberated by a quorate ISSB. The ISSB Chair and Vice-Chair's right was made subject to oversight by the Due Process Oversight Committee of the Trustees who were consulted at a meeting convened on 21 March 2022 at which they confirmed that they did not object with the ISSB Chair and Vice-Chair publishing these exposure drafts.

Scope

BC24 If approved, the proposals would be applied when preparing and disclosing sustainability-related financial information in general purpose financial reporting. Understanding the intended scope of the proposals depends on an understanding of sustainability-related financial information and of enterprise value—concepts that are interrelated and are explained in this section.

Sustainability-related financial information

BC25 The proposal would require entities to disclose a complete set of sustainability-related financial information. Therefore, the definition of 'sustainability-related financial information' is pivotal to understanding the scope of IFRS Sustainability Disclosure Standards generally and the Exposure Draft in particular.

BC26 The definition of sustainability-related financial information is the same as that set out in the *General Requirements* prototype published on the Foundation's website in November 2021, with minor changes that are intended to enhance clarity. The definition is:

> Information that gives insight into sustainability-related risks and opportunities that affect enterprise value, providing a sufficient basis for users of general purpose financial reporting to assess the resources and relationships on which an entity's business model and strategy for sustaining and developing that model depend.

BC27 The description of sustainability-related financial information is intentionally broad to reflect that the information relevant to assessing enterprise value will change over time, for example. This definition is intended to set the overall scope of what is considered. This description does not determine the particular information that must be provided; for example, the description does not include the extent to which information is required to be industry based. Further, the information that an entity must disclose is limited to that which relates to its significant sustainability-related risks and opportunities and that affect enterprise value and is also limited to that which is material. The broad categories of information an entity must provide are set out in the Core Content section of the Exposure Draft (see paragraph BC42).

BC28 Preparing sustainability-related financial information requires an entity to consider the way in which its activities increase or mitigate sustainability risks—impacts and dependencies on resources and from the relationships it maintains that may be positively or negatively affected by those impacts and dependencies—when it is relevant to the assessment of enterprise value. What the entity should include in sustainability-related financial disclosures could, therefore, change over time. The information should take account of the interconnectedness of risks as well as interactions between the entity's resources and relationships. This includes the way in which sustainability-related risks and opportunities link and overlap and by doing so influence and amplify each other. The Exposure Draft does not propose that an entity report on all its resources and relationships. Sustainability-related financial information is required only to the extent that it is material to an assessment of enterprise value.

BC29 The Exposure Draft is focused on meeting the needs of the capital markets in assessing enterprise value which is why the focus is on sustainability-related financial information. However, it is useful to consider sustainability-related financial information in the context of definitions and interpretations of 'sustainability'.

BC30 The concept of sustainability is frequently linked to 'sustainable development', which was defined in 1987 as 'development that meets the needs of the present without compromising the ability of future generations to meet their own needs,' (World Commission on Environment and Development, The Brundtland report: *Our Common Future*, Oxford University Press, Oxford, 1987). The UN's definitions of sustainability, its sustainable development goals and international policy pronouncements, identify matters that the UN has concluded are important in considering sustainability, such as:

- climate change (the UN Framework Convention on Climate Change);
- biodiversity (the UN Convention on Biological Biodiversity);
- oceans (the UN Convention on the Law of the Sea);
- desertification (the UN Convention to Combat Desertification in those Countries Experiencing Serious Drought and/or Desertification Particularly in Africa); and
- human rights (Universal Declaration of Human Rights).

National provisions on limiting environmental and social damage can also inform how the entity evaluates the impact of its activities. The terms sustainability and sustainable development, therefore, apply widely across social and ecological communities and apply to current and future generations; the terms also cover environmental and social notions of justice, health, welfare, preservation and acknowledgement of planetary boundaries.

BC31 The focus of the Exposure Draft is on information relevant to users' understanding of enterprise value. The emphasis on sustainability-related risks and opportunities that inform an assessment of enterprise value distinguishes sustainability-related financial information from broader, multi-stakeholder reporting efforts focused on an entity's contribution to sustainable development. This separate emphasis, in turn, can be helpful:

(a) in allaying concerns that the Foundation has broadened its scope beyond investor-focused disclosure to cover the broadest possible range of sustainability issues; and

(b) in confirming that IFRS Sustainability Disclosure Standards are conceptually and practically complementary to—but not a replacement for—reporting on an entity's significant impacts on people the environment and the economy.

BC32 Nevertheless, the type of information required to meet these complementary purposes is expected to overlap significantly (see paragraph BC76).

Enterprise value

BC33 The Exposure Draft states that sustainability-related financial information provides insight into factors that affect enterprise value and is used by users of general purpose financial reporting to assess the reporting entity's enterprise value and to make decisions on whether to provide resources to the entity.

BC34 Enterprise value is generally used to describe the aggregate, real or total value of an enterprise rather than focusing only on its market capitalisation—it is the total value of a business. For the purposes of the proposals, enterprise value is defined as 'the total value of an entity' and is 'the sum of the value of the entity's equity (market capitalisation) and the value of the entity's net debt.'

BC35 Enterprise value is determined by capital market participants, based on how drivers of enterprise value affect their estimation of the amount, timing and uncertainty of future cash flows over the short, medium and long term. Therefore, enterprise value reflects users' assessments of future cash flows, including the value they attribute to those cash flows, reflecting the cost of capital. Enterprise value, therefore, reflects current market expectations about future cash flows.

BC36 The Exposure Draft assumes that assessments of enterprise value include insights that sustainability-related financial information provides about:

(a) the amount, timing and uncertainty of the entity's future cash flows over the short, medium and long term; and

(b) the entity's significant sustainability-related risks and opportunities including:

(i) their effect on (a);

(ii) whether and to what extent the entity's activities increase or mitigate those risks and opportunities (and, therefore, affect the cash flows in (a)); and

(iii) management's response to those risks and opportunities through its governance arrangements and strategy for sustaining and developing the business model in the short, medium and long term.

BC37 Users of general purpose financial reporting are already factoring sustainability-related risks and opportunities into assessments of enterprise value. The Exposure Draft aims to provide users with more useful information with which to make those assessments, by setting standards designed to ensure that the information disclosed by entities is relevant, representationally faithful, comparable, verifiable, timely and understandable.

BC38 The term 'sustainability-related risks and opportunities' refers to the uncertain, potentially wide-ranging direct, and indirect and positive and negative ways in which sustainability-related risks and opportunities drive an entity's enterprise value and affect users' assessment of enterprise value. Sustainability-related risks and opportunities are drivers of enterprise value when they result in, for example, direct or indirect changes to the market, legislation, and the relationship with the physical environment—such as caused by climate-change—in which an entity operates, such that its ability to execute its strategy and progress its business model is affected.

BC39 Sustainability-related risks and opportunities are manifested in actual or potential changes in an entity's financial position, financial performance or risk profile and, consequently, its enterprise value. Some effects of significant sustainability-related risks and opportunities are reflected in the financial statements, such as when resources at risk are recognised as assets in the entity's financial statements and those risks are reflected in the carrying amount of the asset. However, sustainability-related financial information also includes details of risks and opportunities relating to unrecognised items. They may also relate to recognised items, but the measurement consequences might not be captured in the financial statements. This is the case, for example, when the overall value expected to be created by an asset is reduced, but the carrying amount of the asset will still be recovered.

BC40 The Exposure Draft focuses on information about 'significant' sustainability-related risks and opportunities. Entities are expected to identify significant risks and opportunities by applying their risk management processes, the details of which must be disclosed. The significance of the risks and opportunities is, therefore, entity-specific and is determined according to the entity's risk management processes and informed by the entity's strategy, objectives and risk appetite. Significant risks are those that an entity prioritises for management responses. They include risks and events that in the short, medium or long term could disrupt the entity's business model or its strategy for sustaining and developing the business model that could affect the resources or relationships on which the entity depends or that threaten the viability of, or creates opportunities for, the entity. Focusing on significant sustainability-related risks and opportunities rather than all sustainability-related risks and opportunities is intended to ease application for preparers while not reducing the usefulness of information provided to users as the disclosure is already subject to materiality.

BC41 The information required to be provided must be sufficient to enable an assessment of enterprise value as at the reporting date taking into consideration information about sustainability-related risks and opportunities over the short, medium and long term. Sustainability-related financial information must, therefore, explain decisions and strategies made as at the reporting date that could reasonably be expected to affect future outcomes.

Core content

BC42 Unless another IFRS Sustainability Disclosure Standard permits or requires otherwise, the Exposure Draft would require an entity to provide disclosures about:

(a) governance—the governance processes, controls and procedures the entity uses to monitor and manage sustainability-related risks and opportunities;

(b) strategy—the approach for addressing sustainability-related risks and opportunities that could affect the entity's business model and strategy over the short, medium and long term;

(c) risk management—the processes the entity used to identify, assess and manage sustainability-related risks; and

(d) metrics and targets—information used to assess, manage and monitor the entity's performance in relation to sustainability-related risks and opportunities over time.

BC43 This core content is based on the TCFD recommendations. The feedback on key requirements for success in the Trustees' 2020 consultation on sustainability reporting agreed it was important to align with and build upon the well-established work of the TCFD, and the work of the group of five. Accordingly, the Exposure Draft proposes that the disclosure of information about significant sustainability-related risks and opportunities be built on consideration of the governance, strategy, and risk management of a business, and related metrics and targets. Information focusing on this core content is necessary for users of general purpose financial reporting to assess enterprise value. The core content provides structure for the requirements, and are not intended to indicate that information must be reported in any specific order or prescribed format.

BC44 The TCFD's recommendations are widely understood, accepted and practiced in numerous jurisdictions. Individually and collectively, disclosures about governance, strategy, risk management and metrics and targets support a comprehensive and coherent approach to disclosing sustainability-related financial information. The drafting of the proposed requirements on metrics and targets included in the *General Requirements* prototype have been revised from that included in the *General Requirements* prototype to provide additional clarity and to identify different types of metrics—those identified and defined in other applicable IFRS Sustainability Disclosure Standards; those defined in other relevant guidance; and those developed by the entity. The relationship between targets and metrics has also been clarified.

BC45 Many entities will be exposed to a range of sustainability-related risks and opportunities. The Exposure Draft allows an entity to integrate information in its disclosures relating to the core aspects of its sustainability management, rather than requiring it to repeat information in disclosures about each aspect of its sustainability management. Entities would be required to explain any adaptations that have been made to those processes to cater for the unique characteristics of those risks and opportunities when that information is material. For example, sustainability-related risks and opportunities are often assessed and managed over longer time frames than an entity's typical risk assessment time frames. Users of general purpose financial reporting would understand better how the entity's integrated risk management processes are applied to sustainability-related risks and opportunities if entities explain how and why those processes have been adapted in response to the unique characteristics of sustainability-related risks and opportunities.

General features

BC46 The general features section of the Exposure Draft sets out proposed requirements related to the reporting entity, connected information, fair presentation, materiality, comparative information, frequency of reporting, location of information, sources of estimation and outcome uncertainty, errors and statement of compliance. These sections of the proposal were adapted from IAS 1 and IAS 8.

BC47 The proposals are, therefore, based on GAAP and IFRS Accounting Standards. The reason for doing so was that these principles will be familiar to entities preparing general purpose financial statements, particularly to entities preparing them in accordance with IFRS Accounting Standards. Sustainability-related financial information is expected to be disclosed within general purpose financial reporting alongside financial statements. This approach was taken to help ensure that all of the information within the general purpose financial reporting is prepared on a consistent basis when appropriate and can be connected.

BC48 The requirements and guidance adapted from IAS 1 and IAS 8 have been changed only to refer to sustainability-related financial disclosures, with two exceptions—location of information is new, and there is special application of sources of estimation and outcome uncertainty and errors.

Reporting entity

BC49 The Exposure Draft proposes that an entity be required to disclose sustainability-related financial information for the same reporting entity for which it prepares its general purpose financial statements. For example, a parent that prepares consolidated financial statements would define the reporting entity as itself and its subsidiaries. The entity's sustainability-related financial disclosure would focus on the sustainability-related risks and opportunities that enable users of general purpose financial reporting to assess the enterprise value of the defined parent and subsidiaries. Requiring the same reporting entity for both general purpose financial statements and sustainability-related financial disclosures is designed to enable entities to link financial statements with sustainability-related financial information.

BC50 The wording about the reporting entity has been changed from that in the *General Requirements* prototype. The intention of the changes is to improve clarity rather than to change concepts. The changes are in response to feedback that the original reference to 'reporting boundaries' was confusing. To address that confusion, the proposal replaces the language of 'reporting boundary' used in the *General Requirements* prototype with the language used to describe 'the reporting entity' in IFRS Accounting Standards. This confirms that the focus of the reporting is on the same reporting entity as in the related financial statements. However, in the case of sustainability-related financial information, the focus is on the effects of sustainability-related risks and opportunities on the reporting entity's enterprise value.

BC51 The Exposure Draft also includes factors a reporting entity should consider in determining the information to disclose—explanations that were not in the *General Requirements* prototype. Specifically, the entity would be required to disclose information about sustainability-related risks and opportunities related to activities, interactions and relationships with the parties it contracts and transacts with directly and indirectly along its whole value chain. To provide clarity, a definition for value chain has been proposed within the Exposure Draft. Although the *General Requirements* prototype did not define 'value chain', it did provide a description and that description was used to develop the definition. Examples of the type of information relevant to assessments of enterprise value anticipated by the proposals are:

(a) a beverage company might need to disclose the risk of water use, especially in areas identified to be of high water stress. It might describe how its use of water affects the supply available to meet its operational needs. It might also discuss the effects on communities close to the company's operations, which could lead to risks of reputational damage and loss of customers, or the imposition of taxes or limits on the use of the resource. It could also describe how these risks have been assessed throughout the supply chain.

(b) a clothing brand company might describe the potential effects on enterprise value of its use of plastic materials in products and packaging, which might be driven by the entity's commitments to sustainable business practices, consumer preferences for more sustainable or recycled alternatives, and/or reputational and regulatory risks associated with materials sent to a landfill. They might also disclose which areas of the value chain these risks principally relate to or specific operational areas that they affect, and what processes are in place to assess and monitor those risks.

(c) an electronics manufacturer might describe the potential effects on enterprise value of human rights issues in its supply chain, including its policies, actions taken to assess and monitor risks, and how it addressed any identified abuses.

BC52 Joint ventures, associates (affiliates) and investments are not considered to be part of the reporting entity that is presenting financial statements, although they are recognised in the financial statements. However, just as financial statements recognise these investments and report aspects of the performance of associates and joint ventures, sustainability-related financial information related to those investments is relevant to the users of general purpose financial reporting in assessing the enterprise value of the reporting entity. The way in which information about sustainability-related risks and opportunities arising from joint ventures, associates (affiliates) and investments affects assessments of enterprise value may differ depending on facts and circumstances and the nature of the risks and opportunities.

BC53 The Exposure Draft does not propose specifying how to include sustainability-related financial information in these cases, but rather acknowledges that the effects arising from these investments are included, and states that specific IFRS Sustainability Disclosure Standards will provide guidance or requirements related to the disclosure of information about the sustainability-related risks and opportunities of associates, lending activities and joint ventures. For example, the [draft] IFRS S2 *Climate-Related Disclosures* ([Draft] IFRS S2) published concurrently with the Exposure Draft includes requirements for the reporting of the Scope 1 greenhouse gas emissions of associates and joint ventures as well as requirements for financed emissions. By not specifying in the Exposure Draft how this information is included in sustainability-related financial information, this approach is intended to facilitate better interaction with existing materials that may be referred to by preparers to develop their disclosures in the absence of a specific IFRS Sustainability Disclosure Standard (ie in accordance with the proposal in paragraphs 50–55 of the Exposure Draft).

Connected information

BC54 The Exposure Draft would require entities to highlight or explain connections between:

(a) separate sustainability-related risks and opportunities;

(b) the pieces of information disclosed, including between:

(i) information to respond to separate disclosure requirements about the same risk or opportunity that affects more than one core content;

(ii) disclosures about different risks and opportunities, both within and across core content; and

(iii) sustainability-related financial disclosures and information in the financial statements.

BC55 The Exposure Draft acknowledges that some sustainability-related risks and opportunities are related; for example, environmental impacts may have implications for the workforce. The requirement described in BC52 also calls for disclosures that show the relationships between sustainability-related risks and opportunities, on the one hand, and financial position and financial performance, on the other. For example, such a relationship could be demonstrated by a disclosure about the anticipated effects on financial performance of revenue related to the development of products that minimise environmental impacts. The Exposure Draft states that when an entity is asked to quantify anticipated effects, an entity could give a single estimate or a range of possible outcomes. Allowing an entity to report on a range of possible outcomes recognises that not only can ranges of possible outcomes be more useful than single estimates, but the nature of the connections between various sustainability-related risks and opportunities can make it difficult for an entity to isolate the implications of individual risks and opportunities.

BC56 The requirement in the Exposure Draft to connect information and produce a more interconnected narrative is intended to give users of general purpose financial reporting a better understanding of the relationships between various types of information in general purpose financial reporting. Entities are expected to provide information about the effects of sustainability-related risks and opportunities on their financial statements and anticipated financial performance and financial position over the short, medium and long term. Entities are also expected to explain relationships and trade-offs that arise between various sustainability-related risks and opportunities. The concept of connected information could be used to explain the actual or potential implications of connections between risks and opportunities. For example, an entity could explain how environmental risks affect its reputation or ability to operate and how developing new products to respond to those risks affects the workforce composition or financial performance.

BC57 Examples of the types of connections the proposals are designed to elicit are:

(a) a pharmaceutical company has been exposed to claims of unethical testing and the perception by its customers that its drug prices do not accurately reflect investment in research and development. The company might need to explain how its strategic response has, or has not, led to the recognition of provisions and associated operating costs in its general purpose financial statements.

(b) an electronics manufacturer has publicly announced a climate-related, net-zero target for its corporate emissions, primarily those created during the manufacturing process. The entity's strategic response includes shifting its procurement of energy to renewable sources and investing in more energy-efficient machinery. The entity might need to explain how this strategic response has led to an increase in capital expenditure and possibly an impairment review of non-energy efficient machinery.

(c) due to a supplier's treatment of workers and its record on protecting workers' rights, demand for its goods has fallen. The entity might need to explain how its strategic response has led to increases in the cost of goods sold and operating costs. The entity might also need to show performance metrics and targets related to its mitigation of the risk.

(d) an entity has a net-zero carbon plan that relies on its fleet of diesel-powered vehicles being replaced with electric vehicles. Shifting to electric vehicles will require significantly more capital investment than was necessary for the diesel vehicles. The transition plan is that each vehicle will be replaced when it reaches the end of its planned economic life to the entity. The entity concludes that the vehicles are not impaired and no changes to depreciation rates or the useful lives are required to be reflected in the financial statements. The entity may need to explain that the transition plan will have consequences for its future cash flows and that accounting, as reflected in the financial statements, is not inconsistent with its transition plan.

Fair presentation

BC58 The Exposure Draft proposes requiring that 'a complete set of sustainability-related financial disclosures shall present fairly the sustainability-related risks and opportunities to which an entity is exposed.' Fair presentation requires an entity 'to disclose information that is relevant, representationally faithful comparable, verifiable, timely and understandable' and 'to provide additional disclosures when compliance with the specific requirements in IFRS Sustainability Disclosure Standards is insufficient' for the needs of users of general purpose financial reporting. Fair presentation is a well-understood concept within GAAP and within IFRS Accounting Standards and this concept and language were derived from IAS 1 and adapted in the context of sustainability-related financial disclosure.

BC59 The Exposure Draft would require an entity to consider all relevant facts and circumstances when deciding how to aggregate information in sustainability-related financial disclosures, but the understandability of disclosures shall not be reduced 'by obscuring material information with immaterial information or by aggregating material items that are dissimilar' (see paragraph 48). This concept of aggregation and disaggregation in the Exposure Draft builds on IAS 1 with the proposal including examples of characteristics that might form the basis for aggregation or disaggregation. This concept, which is included in IAS 1 in order to ensure that users of general purpose financial reporting are provided with information at an appropriately disaggregated level is equally important for sustainability-related financial disclosures. For example, if sustainability-related risks are concentrated in a geographical region, it might be appropriate to disclose information for that region separately from information for other regions. Similarly, parts of an entity's supply or sales chain could be responsible for a greater portion of sustainability-related risks than other parts so it might be appropriate to disclose information for the riskier parts separately.

BC60 The Foundation does not have a separate conceptual framework that applies directly to sustainability-related financial information. The proposals in the Exposure Draft include guidance on the qualitative characteristics of useful sustainability-related financial information, set out in Appendix C. This guidance is an integral part of the proposals. The characteristics are adapted from the *Conceptual Framework for Financial Reporting (Conceptual Framework)*, issued by the IASB, and are intended to ensure all reporting within general purpose financial reporting, both sustainability-related financial disclosures and financial statements, are decision-useful for users. It is also included to provide information to assist entities in the preparation of sustainability-related financial information.

BC61 As with the *Conceptual Framework*, the fundamental qualitative characteristics are relevance and faithful representation. The enhancing characteristics are comparability, verifiability, timeliness and understandability. The Exposure Draft explains how those concepts relate to sustainability-related financial information. For example, because some sustainability-related financial disclosures will be in the form of explanations or forward-looking information, the proposals explain that this information can still be verifiable if it is supported by faithfully representing factually-based strategies, plans and risk analyses.

BC62 The Exposure Draft would require an entity to report material information about all significant sustainability-related risks and opportunities that affect enterprise value. The Exposure Draft includes guidance for preparers on how they can identify the sustainability-related risks and opportunities likely to be relevant to users of general purpose financial reporting in assessing the enterprise value of an entity; preparers are required to refer to IFRS Sustainability Disclosure Standards, including identified disclosure topics. Such guidance may be particularly important for entities that have not previously provided sustainability-related financial information focused on meeting the needs of users. In a change from the *General Requirements* prototype, additional guidance has been provided to facilitate identifying sustainability-related risks and opportunities. In order to provide a broad and clear range of sources to be considered when identifying sustainability-related risks and opportunities, the Exposure Draft proposes an entity would be directed to refer to 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 the sustainability-related risks and opportunities identified by entities that operate in the same industries or geographies.

BC63 To identify disclosures, including metrics, that are likely to enable users of general purpose financial reporting to assess how sustainability-related risks and opportunities to which an entity is exposed could affect its enterprise value, preparers are directed to consider the same sources. To illustrate the application of the proposals to refer to these sources in paragraph BC60, Illustrative Guidance have been added to the Exposure Draft. Such examples were not included in the *General Requirements* prototype and have been added to aid understanding.

BC64 The sources referenced in paragraph BC60 proposed to be used to identify sustainability-related risks and opportunities and related disclosures are limited to those that have been developed to meet the needs of users of general purpose financial reporting. Disclosures about sustainability-related risks and opportunities developed for other purposes (such as for public policy needs) might not be helpful in meeting the objective of the Exposure Draft which is to enable assessments of enterprise value by users. In line with the *General Requirements* prototype, entities must also ensure that the disclosures:

(a) are relevant to the decision-making needs of users;

(b) faithfully represent the entity's risks and opportunities in relation to the specific sustainability-related risk or opportunity; and

(c) are neutral.

BC65 The Exposure Draft also proposes that an entity be required to disclose the industry or industries specified for the disclosures that it has provided. That requirement was not proposed in the *General Requirements* prototype and is intended to provide greater transparency for users of general purpose financial reporting as to how disclosures have been identified and prepared. This proposed disclosure is also intended to assist users in understanding the materiality assessments that an entity has made when applying industry-based disclosure requirements required by IFRS Sustainability Disclosure Standards (such as in applying Appendix B of the proposed [Draft] IFRS S2 or when using SASB Standards to develop disclosures in the absence of specific requirements in IFRS Sustainability Disclosure Standards). The industry-based disclosure requirements are organised by industry, enabling an entity to identify the requirements that are applicable to its business model and associated activities. The disclosure topics represent those sustainability-related risks and opportunities that have been identified as being most likely to be significant to entities in that industry, and the associated metrics are those that have been identified as being most likely to result in the disclosure of information relevant to an assessment of enterprise value. The assessment of materiality is entity specific. However, the expectation is that these metrics would be material for an entity with such a business model and associated activities.

BC66 By disclosing the industry or industries that an entity has identified as being applicable, the Chair and Vice-Chair intended that greater transparency would be provided about the materiality assessments that an entity has made. In particular, it would be apparent if an entity did not disclose a metric that is required to be provided for an entity in that industry, subject only to materiality. The Exposure Draft does not propose a disclosure about how materiality assessments have been made as there was concern that such disclosures may be boiler plate.

BC67 The CDSB Framework technical guidance includes the CDSB Framework that covers the disclosure of environmental and social information, and the CDSB Framework application guidance for water- and biodiversity-related disclosures. Following consolidation of the CDSB with the Foundation these documents are now ISSB non-mandatory guidance. The work of the Value Reporting Foundation includes industry-based and activity metrics on a range of sustainability-related risks and opportunities from the SASB and the International Integrated Reporting Framework. Using these documents will assist entities in identifying sustainability-related risks and opportunities, and associated disclosures, enabling the Exposure Draft to establish a comprehensive global baseline for sustainability-related financial disclosures to meet the needs of capital markets.

BC68 The Exposure Draft proposes that entities consider the SASB Standards as a means both of identifying sustainability-related risks and opportunities and to develop disclosures in the absence of specific requirements in IFRS Sustainability Disclosure Standards. The Foundation has announced its intention to consolidate with the Value Reporting Foundation. The close link to the SASB Standards in the Exposure Draft anticipates that consolidation. Consistent with the proposals in the Exposure Draft, applying the SASB Standards and CDSB pronouncements would be considered good practice for an entity applying IFRS Sustainability Disclosure Standards, but applying those pronouncements would not be a formal requirement for an entity. For example, an entity could still assert compliance with IFRS Sustainability Disclosure Standards in accordance with paragraph 91 if it did not apply the requirements in these documents.

Materiality

BC69 The proposals in the Exposure Draft would require that a complete depiction of sustainability-related financial information include material information about all significant sustainability-related risks and opportunities.

BC70 Sustainability-related financial information is defined in the Exposure Draft as being 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.

BC71 This definition of materiality was developed based on the definitions of 'material' and 'materiality' in the *Conceptual Framework* and IAS 1. The proposed definition of materiality is aligned with the definition used in the *Conceptual Framework*, which refers to general purpose financial reports. Nevertheless, materiality judgements about sustainability-related financial information will differ from those for general purpose financial statements. Notably, information about sustainability-related risks and opportunities is unconstrained by definitions of assets and liabilities and the criteria for recognition. To prepare sustainability-related financial information, it is expected that preparers will have to consider financial implications over longer time periods than those considered in preparing general purpose financial statements; preparers will also need to consider financial implications of interactions throughout their value chain. Materiality is assessed in relation to the effect of significant sustainability-related risks and opportunities on enterprise value.

BC72 Risk severity is commonly expressed in terms of impact and likelihood and if approved, the proposals would require that when making materiality judgements, an entity should consider risks that are low likelihood but potentially high impact. The proposal would require an entity to consider:

(a) the relationship between the impacts of the entity's activities on the environment and society and the impacts of the latter on enterprise value (see paragraph BC73);

(b) changes in assumptions and conditions over time; and

(c) potentially changing information needs of users of general purpose financial reporting.

BC73 The Exposure Draft is supplemented with Illustrative Guidance. It illustrates how to think about materiality matters, but is not considered to be mandatory in applying the proposals. The Illustrative Guidance was not included in the *General Requirements* prototype and has been included to aid understanding.

BC74 As has been noted, the definition of materiality was adapted from the *Conceptual Framework* and IAS 1. The IFRS Sustainability Disclosure Standards are designed to be applied with any GAAP and the definition of materiality is not the same in every GAAP. For example, the US national standard-setter, the Financial Accounting Standards Board (FASB) has, in its Statement of Financial Accounting Concepts No. 8 defined materiality as:

> The omission or misstatement of an item in a financial report is material if, in light of surrounding circumstances, the magnitude of the item is such that it is probable that the judgment of a reasonable person relying upon the report would have been changed or influenced by the inclusion or correction of the item.[3]

BC75 There are variations in the definition of materiality as it relates to financial statements, including a definition of materiality that relates to sustainability-related risks and opportunities in the proposed Exposure Draft. The proposal in the Exposure Draft, if approved, ensures that all entities applying the proposed requirements will use the same definition of material information. How the concept of materiality is interpreted, applied and enforced is likely to vary in each jurisdiction. However, including a definition in the proposal ensures that entities applying the proposed requirements are applying and interpreting the same words.

3 See *Conceptual Framework for Financial Reporting:* Chapter 1, The Objective of General Purpose Financial Reporting, and Chapter 3, Qualitative Characteristics of Useful Financial Information, paragraph QC11.

Dynamic materiality

BC76 If approved, the Exposure Draft proposals would require an entity to reassess its materiality judgements at each reporting date to take account of changed circumstances and assumptions. The material sustainability-related financial information disclosed by a reporting entity might change from one reporting period to another as circumstances and assumptions change and as materiality judgements and the assessments of enterprise value by users of general purpose financial reporting evolve. The risks and opportunities that users reflect in their assessments of enterprise value can change from one reporting period to another. Some refer to this as 'dynamic materiality', although that term is not used in the Exposure Draft.

Global baseline

BC77 The objective of the ISSB is to develop a comprehensive global baseline of sustainability-related disclosure requirements to meet the needs of the capital markets. Some jurisdictions, including the EU, are developing proposals that reflect public policy initiatives that focus on a broader range of stakeholders than investors. The Exposure Draft was developed with this in mind.

BC78 IFRS Sustainability Disclosure Standards will provide a global baseline of requirements—a building blocks approach. Regulators will be able to meet their public policy needs by requiring the use of IFRS Sustainability Disclosure Standards and supplementing them with information that meets the information needs of other stakeholders, if necessary. The Exposure Draft would allow an entity to report information needed to meet public policy objectives in addition to the information required by IFRS Sustainability Disclosure Standards, as long as this additional information does not obscure the information required by the ISSB's Standards.

BC79 Having a global baseline of ISSB Standards enhances global comparability. It also ensures that when ISSB requirements change, they change for all entities applying the relevant Standard. The information required by IFRS Sustainability Disclosure Standards is likely to overlap substantially with the information required for public policy reasons not least because information that is relevant to society is likely to be relevant to investors in assessing enterprise value.

Location of information

BC80 The Exposure Draft proposes that sustainability-related financial disclosures be disclosed as part of a reporting entity's general purpose financial reporting. A consequence is that an entity would be required to report its sustainability-related financial disclosures at the same time it publishes its related financial statements. This requirement would be a change for entities that disclose sustainability-related financial information separately from and later than their financial statements.

BC81 While it is recognised that corporate reporting varies across jurisdictions, the term 'general purpose financial reporting' encompasses the financial statements and sustainability-related financial information. Sustainability-related financial disclosures could be included in an entity's management commentary when management commentary forms part of its general purpose financial reporting. Management commentary can be known by or incorporated in reports with various names, including management's discussion and analysis, operating and financial review, integrated report and strategic report. Management commentary (or an equivalent document) is a possible location for the required disclosures as it complements an entity's financial statements. The Exposure Draft proposes that cross-referencing between reports would be permitted under specified conditions. For example, cross-references to the financial statements or another part of the general purpose financial reporting are permitted as long as they do not reduce the clarity of the reporting.

Sources of estimation and outcome uncertainty and errors

BC82 Most accounting frameworks account for estimation uncertainty differently from the accounting for errors or for changes in accounting policy. The Exposure Draft proposes that all changes in estimate and corrections of errors in previously reported metrics and targets would be corrected by restating any comparative information presented. This proposal is designed to help provide the best information possible about trends to users of general purpose financial reporting.

BC83 It is proposed in the Exposure Draft that entities are required to disclose information about any material changes in estimates or material errors. This requirement contrasts with how changes in estimates in financial statements are addressed. Normally, changes in estimates are recognised prospectively—that is, in the period of the change. Prospective recognition means the comparatives are not changed and the change in estimate is reflected in current period profit or loss. One of the main differences that led to requiring comparatives to be changed for sustainability-related financial information is that the metrics are not part of a double-entry model that affects reported equity. The nature of some sustainability-related metrics will require significant estimation. It was considered more useful to reflect changes in estimates that relate to prior periods through comparatives, rather than knowingly misstating the current period information.

Statement of compliance

BC84 The Exposure Draft proposes requiring an entity to include an explicit and unqualified statement of compliance only if its sustainability-related financial disclosure complies with all requirements of the IFRS Sustainability Disclosure Standards. This proposed requirement reflects that it is important that users of the information understand whether the entity has been selective in its approach to reporting sustainability-related financial information or whether the entity has applied all of the requirements. Stating whether the entity has complied with all the disclosure requirements is considered particularly important to the establishment of the ISSB because its primary objective is to improve the comparability of information provided.

BC85 The Exposure Draft proposes issuing disclosure-only Standards and if an entity meets these disclosure requirements, it can assert compliance with IFRS Sustainability Disclosure Standard. A qualified statement of compliance with the IFRS Sustainability Disclosure Standards would not be permitted. The proposals in the Exposure Draft would not require an entity to implement strategic goals, but would only require it to disclose information about those strategic goals. Therefore, an entity might not be managing some of its significant risks and opportunities or established metrics and targets for them. The entity could still assert compliance with IFRS Sustainability Disclosure Standards as long as its disclosures explain that fact. The fact that an entity does not have procedures and processes in place to identify and manage sustainability-related risks and opportunities is, in and of itself, likely to be material information for the users of the sustainability-related financial disclosures. However, the entity would need to meet the specific disclosure requirements such as Scope 1 greenhouse gas emissions proposed in IFRS S2.

Effective date and transition

BC86 The proposal does not include a proposed effective date. The ISSB will determine an effective date when it issues a Standard. The ISSB will consider the comments it receives, including feedback on the period of time needed by entities to prepare to apply the proposals.

BC87 The requirements, for many entities, would be new. Entities would need time to create or adjust their internal systems and control procedures to ensure that they are able to meet the requirements of any approved Standard. The time needed will depend, among other things, on an entity’s current approach to sustainability-related risks and opportunities and reporting, as well as on an entity’s information and circumstances, such as its size and the local requirements or regulations that currently apply.

BC88 The proposal would relieve an entity from the requirement to disclose comparative information in the first period of application. This concession would allow the requirements to become effective sooner, had comparative information been required. For example, if the proposed requirements were effective for annual reporting periods beginning on or after 1 January 2024 an entity would need to collate information for the year from 1 January 2023. Rather than delaying implementation to ensure that entities are able to provide comparative information, such as setting an application date of 1 January 2025 using this example, the relief would allow the ISSB to consider a shorter transition period. Allowing entities to report on the current period only would enable them to provide users of general purpose financial reporting with the information they seek sooner.

BC89 The proposal states that the requirements can be applied before the effective date, allowing entities to meet users' information needs more quickly. Early application could be particularly relevant for entities already providing disclosures about sustainability-related risks and opportunities, and could make a transition to IFRS Sustainability Disclosure Standards more quickly.

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