NSW GOVERNMENT | Treasury

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Dear Keith

AASB ED 321 Request for Comment on [Draft] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information and [Draft] IFRS S2 Climate-related Disclosures

The Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) welcomes the opportunity to respond to ED 321 on the draft IFRS Sustainability Standards S1 and S2.

HoTARAC is aware that the AASB has decided that it does not intend to apply these standards to the not-for-profit public sector at this time.

Implementation of sustainability reporting by any or all public sector entities is a government policy decision to be taken by each government jurisdiction. Policy decisions about sustainability reporting have been taken to different extents by individual jurisdictions, and HoTARAC is making no comment on jurisdictional policy decisions.

HOTARAC's view is that the experience of its members in reporting matters allows us to make a contribution to the deliberations of the AASB and the International Sustainability Standards Board (ISSB) on S1 and S2. Our view is that S1 and S2 seek to expand on and more formally incorporate into public reporting systems the existing aspirational reporting models used in current voluntary reporting, which is becoming increasingly widespread among private sector entities internationally.

We note that S2 focusses on climate-related reporting, with a heavy emphasis on emissions. We regard sustainability as being broader in scope than this, and we note that the ISSB will consider further standards after S1 and S2 are completed.

The public sector

We support exclusion of the not-for-profit public sector at present because we consider more thought is warranted before application. The public sector (and some other not-for-profits) may genuinely have different objectives to be achieved from sustainability reporting, to those presented in the Exposure Drafts:

- Central to the proposal in the Exposure Drafts is the concept of impacts on 'enterprise value'. This concept is defined as an entity's total value, being the sum of market values of an entity's equity, and its net debt. The concept of a market value for equity in not-for-profit-entities is not relevant.

- A significant factor for public sector entities, particularly at Commonwealth and State/Territory level, is achievement of government policy, rather than maximising 'enterprise value'. For example, this is recognised in the report of the World Bank[1] which, while proposing a similar model to the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD), nevertheless proposes a nuanced alternative reporting solution to address sovereign sustainability risks and opportunities.
- The previous two points indicate that the specific disclosures required under S1 and S2 will need to be modified for public sector use.
- The Exposure Drafts raise issues that are unique to the public sector, or have a proportionately greater impact on the public sector. HoTARAC has identified the most significant of these in the attachment to this submission.

You will be aware of the sustainability-reporting-related activities of the International Public Sector Accounting Standards Board (IPSASB), including its discussion paper on accounting for natural resources, and its consultation paper *Advancing Public Sector Sustainability Reporting*. These acknowledge that there is a public-sector-specific lens to sustainability issues, and they should inform sustainability reporting proposals for the public sector.

Broader considerations

For application beyond the public sector, we note the expressed urgency to introduce consistent global standards for sustainability applicable to for profit entities and for use in capital markets. This has received widespread support from expected user groups. The proposals in the Exposure Drafts are primarily drawn from the recommendations of the TCFD, but have some differing reporting requirements.

We understand that reporting under underlying models such as TCFD and the Global Reporting Initiative is currently well established among some private sector entities. However, it will be new to many preparers and assurance providers, so will require considerable work for widespread implementation across sectors. We expect that if these Exposure Drafts are issued as standards, revisions will be necessary to address emerging issues and to ensure appropriate links with any additional sustainability standards that may be issued.

Our view is that implementation and ongoing compliance should balance the costs of preparation with the benefits to users. We accept that, similar to accounting standards, many of the benefits will be intangible or difficult to measure, but are nevertheless present. Our members have expressed concern about implementation and ongoing costs, and we think opportunities should be taken to further develop generic models, tools and guidance to simplify application and reduce costs through minimising the need for external assistance.

Consequently, while immediate implementation may be a priority for some stakeholders, we consider these two standards to be work in progress. In addition to the current consultation and regular monitoring there should be both a formal post implementation review, and support for further study - such as academic study - to provide supporting and clarifying evidence about the usefulness of the current or any future revised model.

[1] *(Sovereign Climate and Nature Reporting – Proposal for a Risks and Opportunities Disclosure Framework, Washington, 2022)*

Assurance

We appreciate that the current consultation is about proposed sustainability reporting standards. However, as preparers we also have an interest in assurance requirements over reports we prepare, and we view assurance as a critical issue:

- In principle we agree with the view that providing assurance over sustainability reports would enhance the trust of users in the report contents.
- Mandatory requirements for assurance will be determined by regulators who manage the reporting framework in each jurisdiction. HoTARAC does not currently express a view on this matter.
- Assurance requirements for a sustainability report fully compliant with S1 and S2 may be difficult to apply in the early years because preparers will need time to fully implement up to the evidential standard required. This will be even more so if a level of audit ('reasonable assurance') is required.
- Further, some of our members have noticed comments from stakeholders identifying the need for a sufficiently knowledgeable and skilled base among assurance providers.
- We note the work undertaken by the IAASB (and AuASB) to address assurance issues but we do not view this work as yet completed, so we support both ongoing work in this field and further liaison between sustainability standard-setters and assurance standard-setters.

Our view is that there will be issues in applying assurance standards, rather than deficiencies in the standards/guidance themselves. Assurance guidance[2] identifies the high degree to which judgement is required in collecting and assessing evidence, primarily due to the inherently uncertain nature of the information being assured. Until there is more experience with the subject matter, there may be inconsistent assurance judgements between assurance practitioners, and frequent judgement differences between preparers and assurance practitioners.

Format of this submission

Our submission identifies in the attachment some of the issues that will be relevant to public sector application of S1 and S2. It is not an exhaustive list, and there are other issues of less significance that we have identified. While many of the issues are common to private sector application, we have focussed on the impact for the public sector and have not comprehensively analysed private sector issues. Accordingly we have not directly answered the questions included in the exposure drafts, since they are asked primarily in a private sector context.

As the issues are summarised in "dot point" form, HoTARAC members will welcome separate meetings, to expand on or clarify the issues raised.

If you require any further information or explanations, please in the first instance contact Peter Gibson of the Australian Government Department of Finance on peter.gibson@finance.gov.au.

[2] *International Audit and Assurance Standards Board, Non-Authoritative Guidance on Applying ISAE 3000 (Revised) to Sustainability and Other Extended External Reporting (EER) Assurance Engagements, and related AuASB guidance.*

Yours sincerely

Stewart Walters
Chair
Heads of Treasuries Accounting and Reporting Advisory Committee

ATTACHMENT

Issues in application of Proposed IFRS Sustainability Standards S1 and S2

Our assumption when identifying these issues is that sustainability reports will be subject to assurance. If assurance is not required, some issues may be less significant.

a) **Issues specific to the (not for profit) Public Sector**

- The concept of enterprise value is less relevant.
- There are additional issues of aggregation about the scope of a public sector reporting entity, over and above general reporting entity issues.
- Ability to report future monetary impacts is potentially more problematic in the public sector than in other sectors.
- It may be necessary to undertake extensive analysis of the underlying sources of taxation and grant revenue, and certain types of expenses such as grants, subsidies and social benefits, to be able to comply with GHG Scope 3 reporting requirements, unless these items are scoped out.
- The relationship between sustainability reporting and other non-financial reporting such as service performance reporting needs to be determined. HoTARAC's view is that this should not delay further work on either sustainability reporting or performance reporting in the AASB work program.
- S2 does not presently include industry-specific requirements for core governments a.k.a. the 'public administration' industry. This does not prevent reporting, but if there are not common national and international protocols, there would be inconsistency if different government jurisdictions arrive at different judgements about what industry-specific information and measures are relevant.
- The language used in S1 refers to contracts and transactions, terminology that does not always apply to the activities of public sector entities.
- Government policy-setting may not encompass the setting of whole-of-government targets across all time periods (short/medium/long). Similarly, whole-of-government policy-setting may not include actions such as setting of sufficiently-specific transition plans. This would make compliant sustainability reporting for government more difficult or complex.
- Compliance with (or modification to) the *AASB Not-for-Profit Entity Standard-Setting Framework*.
- Governments currently have existing sustainability reporting requirements, some set jurisdiction-by-jurisdiction. If these are not to be adopted or integrated into a public sector reporting model under S2, they will need time to be "unpicked", affecting implementation time and complexity. Alternatively they may be continued, resulting in duplicated reporting.

b) Issues that apply to the Public Sector that may apply to other sectors

- Issues of definition and measurement of GHG Scope 3 emissions unless there are models and tools to simplify this aspect.
- Quantitative 'value chain' reporting more generally, for the same reasons.
- Reporting GHG Scope 1 and 2 emissions for those associates, joint ventures and unconsolidated subsidiaries that cannot be compelled to supply relevant information.
- Difficulty in accurately determining climate-related financial (i.e. monetary) impacts, both in the current period and forward-looking.
- Cost of implementation and ongoing compliance. Matters of specific concern include scenario analysis; expert reports that need to be obtained; data collection systems for large corporate groups; costs of negotiating differences in judgement between stakeholders; costs of preparing financial statements and sustainability reports to the same reporting deadline; and the costs of complying and the volume of reporting where an entity or group is engaged in multiple industries or sub-industries. While we expect tools and models will become

available over time to mitigate cost issues, cost should be taken into account in considering the implementation plan.

- Scope of reporting, particularly options for differential reporting.
- Issues in meeting the qualitative characteristics of understandability and verifiability.
- Materiality judgements will differ between stakeholders, such as between management and assurers. Application of the accounting concept of materiality will be difficult in practice. e.g. assessing cumulative materiality for the entity as a whole based on aggregating different non-financial measures.
- Overlaps in the reporting requirements, across the three contextual pillars of governance, strategy and risk management. We expect this will be effectively mitigated through removing duplication of information as discussed in the Exposure Drafts and the bases of conclusions. However, this concession may be partially offset by an increase in complexity for some uses.
- S1 contains a requirement that sustainability reports should include information on all material sustainability-related risks and opportunities, not solely those covered in issued topic-specific standards. This may be impractical since the term ‘sustainability’ is neither defined, nor subject to a boundary.
- S1 proposes that the reporting entity be the same as that for financial reporting purposes. We expect this will be workable for those entities currently targeted such as publicly listed entities, but may work less well for other entities.
- Disclosure of complex connections between items may be difficult to do in a clear and concise way.
- Reporting information by one entity across multiple industries, multiple geographic regions and multiple time horizons may be difficult to do concisely.
- Industry definitions are based on the Sustainable Industry Classification System. We recommend that there be further discussions with international statistical bodies internationally about classification. Having an industry classification system for sustainability-reporting that is consistent with the classification system for other statistical reporting purposes will enhance the ability to collect global level statistics, which in turn could provide publicly-available information that will simplify management and measurement of sustainability risks and opportunities.
- Any mandatory effective date needs to be set to allow sufficient implementation time for relevant stakeholders. Implementation will require capacity building and systems development, as well as understanding of the reporting requirements.
- Phased implementation and/or transitional provisions will make compliance easier.
- The illustrative guidance provided with the proposed standards is brief. While we have not assessed what additional matters, if any, should be included in illustrative guidance, we would expect more guidance material is justified given the high level of judgement required in applying the standards.
- There would be benefits if the ISSB supported development of, or references to, illustrative examples.[3]
- The term “sustainability-related financial information” may be confusing to some stakeholders, since sustainability is not defined (as noted above) and most of the required information is not monetary but qualitative and text-based. The term “significant” is used, without further clarification or reconciling with the term “material”.
- Reporting implications for risks and opportunities that are unique to, or more pronounced for, Australia.
- While S1 purports to be the framework, in reality it is a mixture of framework matters and specific disclosures.
- Practical matters, such as gaming exemptions from reporting because it is legally prohibited.
- There are mixed views on the costs and benefits of scenario analysis.

[3] *Note the TCFD provides examples of how entities have reported under its framework.*