

PRI RESPONSE

AASB'S CONSULTATION ON DRAFT IFRS S1 – GENERAL REQUIREMENTS FOR DISCLOSURE OF SUSTAINABILITY- RELATED FINANCIAL INFORMATION & IFRS S2 – CLIMATE- RELATED DISCLOSURES

July 2022

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INTRODUCTION

The Principles for Responsible Investment (PRI) works with its international network of signatories to put the six Principles for Responsible Investment into practice. Its goals are to understand the investment implications of environmental, social and governance (ESG) issues and to support signatories in integrating these issues into investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society as a whole.

The six Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a range of possible actions for incorporating ESG issues into investment practice. The Principles were developed by investors, for investors. In implementing them, signatories contribute to developing a more sustainable global financial system.

The PRI has published [consultation responses](#) on the International Sustainability Standards Board (ISSB) Exposure Drafts and previously provided [views and recommendations](#) on the Technical Readiness Working Group prototypes on climate and general disclosure requirement, as well as on international sustainability reporting standard setting through [consultation responses](#) and [public statements](#). In addition, the PRI has submitted views and recommendations on corporate reporting developments in other major regional jurisdictions, including the [US](#), [UK](#), [EU](#), and [China](#).

The PRI welcomes the opportunity to respond to the Australian Accounting Standards Board's (AASB) call for feedback on the draft IFRS S1 general requirements for disclosure of sustainability-related and S2 climate-related disclosure standards.

ABOUT THIS CONSULTATION

The AASB is [consulting on the International Sustainability Standards Board's Exposure Drafts on IFRS S1 and IFRS S2](#). It aims to gather feedback to provide input into the ongoing work of the ISSB and inform the AASB as to the appropriateness of and support for its proposed approach to sustainability-related financial reporting in Australia.

For more information, contact:

Daniel Wiseman

Head of APAC Policy

daniel.wiseman@unpri.org

Mayleah House

Senior Policy Analyst, Australia

mayleah.house@unpri.org

KEY RECOMMENDATIONS

The PRI welcomes the AASB's engagement with the International Sustainability Standards Board (ISSB) to enhance compatibility between a global baseline of sustainability reporting set by the ISSB and Australia.

The PRI strongly supports the ISSB's mission to deliver a high-quality global baseline of sustainability disclosures and encourages the AASB alongside Treasury, ASIC, APRA and the RBA to engage closely with the ISSB with the goal to develop a global baseline for corporate sustainability reporting.

The PRI's key recommendations are:

- The Government should develop and introduce legislation that requires all listed and large proprietary entities to disclose sustainability-related information in their annual reports on a mandatory basis, in accordance with sustainability reporting standards to be developed by the AASB, from 2024 onwards.
- The standards for mandatory sustainability reporting, to be developed by the AASB, should be based on the final IFRS standards as a minimum baseline, with modifications made as necessary to enable companies to report information reflecting Australian specific market dynamics and investor needs, which should not be limited by the concept of enterprise value (including any potential taxonomy-related disclosures that are required).
- The Government should develop and introduce legislation authorising the AASB (or a subsidiary body) to develop and issue such standards and ensure that the AASB is appropriately governed and resourced to do so.
- All Australian entities subject to such sustainability reporting requirements should be required to disclose Scope 3 emissions where they are a significant portion of an entity's overall emissions.
- All Australian entities should be required to calculate GHG emissions in line with the GHG Protocol methodology (including the Corporate Standard).
- All mandatory sustainability reports should be assured and included in the auditor's overall opinion on an entity's annual reports.

DETAILED RESPONSE

MATTERS CONCERNING PROPOSALS IN DRAFT IFRS 1

A1: 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 strongly support the ISSB's mission to deliver a high-quality global baseline of sustainability-related financial disclosures and welcome the standard's recognition that sustainability-related financial information captures all information that can result in changes to the entity's enterprise value in the short, medium, and long term; including from the entity's actions that result in impacts and dependencies on people, planet and the economy. With this, the standard will enable disclosure of information that captures elements of an entity's sustainability performance and its positive and negative contributions to sustainability outcomes.

However, disclosure focused on enterprise value alone will not serve the needs of all investors, particularly those that are looking for a broader understanding of an entity's sustainability performance and outcomes, and feedback from several signatories has indicated the need for impact-related information.

Therefore, the PRI supports the 'building blocks' approach to enable companies to report information that goes beyond the ISSB's focus on enterprise value. IFRS Sustainability Disclosure Standards should be used as a baseline, with flexibility for Australian-specific initiatives (including any potential taxonomy-related disclosures that may soon become standard practice) and/or the Global Reporting Initiative (GRI)¹ to implement reporting requirements that meets the information needs of all investors.

To implement this approach in practice, we suggest the ASSB and the Council for Financial Regulators work closely with the ISSB and the GRI to:

- Ensure their standards are consistent on: (i) reporting design/structure, such that investors are still able to extract comparable data (whether across issues or on specific issues) on governance, strategy, risk management and metrics/targets, even if not under the same headings; (ii) terminology and definitions, including common taxonomies; and (iii) reporting concepts underpinning the standards, such as the qualitative characteristics (relevance, faithful representation etc.).
- Ensure alignment in disclosures that can serve both reporting of information that is relevant to an entity's enterprise value and its sustainability performance and outcomes. This would include disclosure on relevant aspects of the entity's governance, strategy and risk management processes across issues and common indicators for metrics/targets on specific issues.

¹ See slide 6: <https://www.ifrs.org/content/dam/ifrs/meetings/2022/june/cmac-gpf/ap6-issb-update-and-issb-exposure-drafts.pdf>

MATTERS CONCERNING PROPOSALS IN DRAFT IFRS S2

B1: 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?

Yes – the PRI supports the disclosure of Scope 3 emissions where they are a significant portion of an entity's overall emissions profile.

While Scope 3 emissions are often more difficult to report, these are [the most impactful kind of emissions for some industries](#) such as Australia's thermal coal, oil and gas producers. Leaving them out could mean that a large share of actual emissions, where material, are not reported.

In our view, disclosures on Scope 3 emissions should be accompanied by an indication of what portion of an entity's total Scope 3 emissions have been captured in the figure provided. Note we are not recommending that entities disclose a precise percentage figure, but rather an approximative range that would provide investors with a better understanding of potential exposure to transition risk.

In addition, Scope 3 disclosures should be accompanied by robust methodological explanations of the underlying inputs, assumptions and calculation methodologies used – including organisational scope, emissions factors used and other information on the calculation approach

This would help investors verify reported GHG emissions, particularly if these have not been subject to third-party verification. Furthermore, it would allow for better global alignment as such reporting has also been suggested in both the [US Securities and Exchange Commission's Proposed Rule on climate-related disclosures](#) [page 471] and [EFRAG Exposure Draft ESRS E1 on Climate change](#) [page 31].

Finally, we recommend that reporting captures aggregated Scope 3 emissions as well as Scope 3 emissions from relevant categories where these are significant.

B2: Do you agree that Australian entities should be required to apply the Greenhouse Gas Corporate Standard given existing GHG emissions legislation and guidance in place for Australian entities?

Yes – Australian entities should be required to calculate GHG emissions in line with the GHG Protocol methodology (including the Corporate Standard) in line with the PRI's recommendation that IFRS S2 should likewise require GHG emissions to be calculated according to this methodology. The GHG Protocol methodology is the most widely used and recognised international standard for calculating GHG emissions. While we recognise outstanding methodological issues, this would allow for a standardisation of emissions data across jurisdictions, increasing comparability and facilitating aggregation for investors.

MATTERS CONCERNING BOTH DRAFT IFRS S1 AND S2

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

Initially, Australian entities that should be required to apply IFRS S1 and IFRS S2, as implemented by the AASB, include all listed and large proprietary entities.² Over time, this could be extended to all entities that have existing obligations to produce a financial report compliant with the IFRS accounting standards.³

Financial reporting obligations are imposed on these entities, in part, to provide relevant financial information to meet shareholders and members needs. Requiring the same entities to apply the final IFRS standards ensures that investors' data needs on relevant sustainability matters are met.

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 IFRS S1 and IFRS S2?

In order to ensure that the final IFRS S1 and S2 standards are appropriately implemented in Australia, legislative and regulatory action will be required.

AASB's current powers and functions are largely constrained to developing and implementing accounting standards.⁴ The PRI notes that the AASB has broad powers to advance the main objectives of the *ASIC Act 2001 (Cth)*.⁵ These objectives could be read broadly to include a distinct goal of maintaining investor confidence in the Australian economy and its capital markets.⁶ In this case, the PRI considers the AASB could have the authority to develop standards in line with the final IFRS standards.⁷ However, if a narrow interpretation of the *ASIC Act 2001 (Cth)* s 224 is applied, the AASB's powers would be limited to maintaining investor confidence in Australia *only* by facilitating accounting standards. This could likely undermine AASB's ability to develop sustainability reporting standards aligned with IFRS S1 and S2.

Regardless, legislation will be required to ensure that Australian entities disclose information according to any sustainability reporting standards introduced by the AASB. There is currently no existing legislation or regulation in Australia that requires corporate sustainability reporting.⁸ A voluntary approach to corporate sustainability reporting is not sufficient to ensure the consistent, high quality and comparable sustainability information that investors require for their decision-making.

² See Corporations Act 2001 (Cth) s 45A.

³ *Corporations Act 2001 (Cth)* ss 292; 296.

⁴ *ASIC Act 2001 (Cth)* s 227; *Corporations Act 2001 (Cth)* s 334.

⁵ *ASIC Act 2001 (Cth)* s 227(1)(e).

⁶ *ASIC Act 2001 (Cth)* s 224(c).

⁷ Noting that the purpose of the IFRS introducing the standards is to provide a comprehensive global baseline of sustainability related disclosure standards that provide investors with information about companies' sustainability-related risks and opportunities to help them make informed decisions.

⁸ The *Corporations Act 2001 (Cth)* requires certain entities to disclose financial reports prepared in accordance with accounting standards. Yet that act does not explicitly compel Australian entities to disclose any form of sustainability information, let alone specific reports prepared in accordance with regulated sustainability reporting standards. Likewise, the ASX's Listing Rules does not require listed companies to publish sustainability reports to the market.

To avoid any doubt about AASB's authority and ensure the effective implementation of Australian standards that are consistent with the final IFRS standards, the PRI therefore recommends that:

- The Australian Government develop and introduce legislative amendments to the *Corporations Act 2001* (Cth) to explicitly require all listed and large proprietary entities to disclose sustainability-related information in their annual reports, prepared in accordance with sustainability reporting standards to be developed by AASB (or a subsidiary body).
- The Australian Government develop and introduce legislative amendments to the *ASIC Act 2001* (Cth) to explicitly authorise the AASB (or a subsidiary body) to develop and formulate sustainability reporting, for the purposes of meeting any new sustainability reporting requirement under the Corporations Act.
- The Australian Government ensure that the AASB is appropriately governed and resourced to enable it to implement sustainability reporting standards. Appropriate governance would require the AASB board to include directors with practical experience in environmental and social organisations and balance this sustainability experience alongside the extensive accounting, auditing, tax, financial, legal and governance experience that the board already holds. Alternatively, the AASB could set up a subsidiary board that is directly responsible for its work on sustainability reporting standards that is overseen by directors with relevant environmental, social, governance, and reporting experience.

C3: Do the proposals in Exposure Drafts IFRS S1 and IFRS S2 align with existing or anticipated requirements, guidance or practice in Australia?

Yes – existing and anticipated requirements, guidance and practice in Australia complements rather than conflicts with Exposure Drafts IFRS S1 and S2.

Currently certain Australian entities are required to disclose their greenhouse gas emissions.⁹ These obligations have a distinctive purpose and their primary user (i.e., the Clean Energy Regulator) correlates reported data rather than disclosing individual entity reports. Reporting under Exposure Draft IFRS S1 and S2 is appropriately additive as it provides separate, decision-useful climate and sustainability information to investors.

The PRI also acknowledges that the current development of an [Australian sustainable finance taxonomy](#) could eventually lead to a requirement on or practice by certain Australian entities to disclose sustainability information at an activity level.¹⁰ However, we consider that any anticipated taxonomy disclosures would not detract or conflict with disclosures under the IFRS S1 and S2.

Exposure Drafts IFRS S1 and S2 therefore provide an appropriate baseline for company-level sustainability reporting that the AASB could build upon as requirements for additional sustainability disclosures develop.

⁹ National Greenhouse and Energy Reporting Act 2007 (Cth).

¹⁰ For example, the EU Taxonomy regulation requires large, non-financial companies to disclose their capital and operating expenditure that is associated with environmentally sustainable economic activities.

C4: Would the proposals in Exposure Drafts IFRS S1 and IFRS S2 result in useful information for primary users of general purpose financial reports.

Yes - Exposure Drafts IFRS S1 and S2 would result in information about companies' significant sustainability-related risks and opportunities that is useful to primary users of general purpose financial reporting when they assess enterprise value and decide whether to provide resources to an entity.

The exposure drafts consistently focus on requirements in the Core content (i.e. on governance, strategy, risk management and metrics/targets) on sustainability-related risks and opportunities. They also focus on sustainability-related financial information that may directly/indirectly influence investors' assessment of enterprise value with:

- their focus on information that is material to primary users;
- their requirements to provide an integrated view on key elements of the business through insights on governance, strategy and risk management – core elements of sustainability-related disclosure widely recognised by investors, following the Taskforce on Climate-related Disclosure (TCFD) recommendations' four pillars; and
- connectivity with the financial performance through strategy, which signatories have identified as key to their investment process.

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

All mandatory sustainability reports should be assured and included in the auditor's overall opinion on an entity's financial reports.

Climate and sustainability information that is used for investment decision-making need to be accurate and reliable. They merit the same level of assurance and accountability currently provided to similarly considered financial information.

External auditing and assurance can play an important role in upholding the quality of reporting, providing comfort to users that the standards used have been satisfied. Lack of external audit and assurance allows firms with negative climate and sustainability impacts to conceal or convolute negative information, leading to incomplete or inaccurate disclosures from issuers and can "increase information processing costs of the recipient."¹¹

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

The final IFRS standards should be made effective in Australia as soon as practical and feasible.

It is important that reporting according to these standards is made mandatory to provide investors with consistent and reliable information that enables them to fully understand related risks and opportunities and take investment and stewardship decisions aligned with their long-term investment

¹¹ Fabrizio, Kira R., and Eun-Hee Kim (2019), "Reluctant Disclosure and Transparency: Evidence from Environmental Disclosures", available at *Organization Science* 30 (6): 1207–31.

goals. It is important, therefore, that these disclosure requirements are introduced urgently to enable investors to act in their beneficiaries best financial interests.

The PRI suggests that mandatory IFRS S1 and S2 disclosures could be introduced on a staggered basis starting from 2024. Consistent with phase-in approaches in other jurisdictions, this staggered approach should be based on size and capacity of the company, allowing for gradual learning and competence building over time.

The PRI has experience of contributing to public policy on sustainable finance and responsible investment across multiple markets and stands ready to support the work of AASB further to implement global sustainability disclosures in Australia.

Please send any questions or comments to policy@unpri.org.

More information on www.unpri.org