

AGENDA PAPER

Item Number: 6
Date of Meeting: 7 December 2022
Subject: Update on Sustainability

Action required For discussion For noting For information

Purpose

To provide the Board with an update on international and Australian developments in Sustainability.

Background

The sustainability regulatory environment is rapidly evolving, driven by the increased demand from investors, those charged with governance, the public and other stakeholders for sustainability and ESG reporting and assurance. However, the current frameworks for this type of reporting are voluntary and are not standardised across industries and jurisdictions. This complexity of multiple frameworks increases the risk of greenwashing and means the information reported lacks reliability and comparability. Standard-setters globally and across various jurisdictions are working to develop sustainability reporting and assurance standards to address these concerns.

An update on sustainability and ESG reporting was provided at the November 2021 Board meeting ([Agenda Item 5](#)), which reported on the launch of the International Sustainability Standards Board (ISSB) at the November 2021 COP 26 UN Climate Change Conference in Glasgow by the International Financial Reporting Standards (IFRS) Foundation.

A further update was provided at the June 2022 meeting ([Agenda Item 6](#)), which noted the following:

- the ISSB's first two proposed standards on general sustainability-related and climate-related disclosure requirements were issued in March 2022 ([The Exposure Draft IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information \(draft IFRS S1\)](#) and [Exposure Draft IFRS S2 Climate-related Disclosures \(draft IFRS S2\)](#)); and
- the establishment of the International Ethics Standards Board for Accountants (IESBA) Sustainability Working Group in March 2022, chaired by IESBA Board Member, Mark Babington (UK FRC).

In the September 2022 meeting update ([Agenda Item 12](#)), it was reported that over 1,300 submissions were made to the ISSB on its two proposed standards from accounting bodies, audit firms, investors, preparers, public interest bodies, regulators and standard setters from various jurisdictions spanning six continents.

Recent Developments

APESB Technical Staff have continued monitoring international and Australian developments in sustainability and ESG reporting outlined below.

1. International Developments

The IFRS Foundation and ISSB

The ISSB have been considering the feedback received in response to their two exposure drafts and have noted the following matters/issues and themes:

Draft IFRS S1

Respondents strongly supported a consolidated standard and emphasised the need to issue the final standards rapidly. Key issues raised related to:

- Scalability - the concern that compliance will require substantial resources and capabilities, likely to impact SMPs significantly.
- Need for greater clarity for some requirements and definitions used.
- Consistency across jurisdictions and with other standard setters.

Further details are here: [Summary of Comments General Sustainability-related Disclosure](#)

Draft IFRS S2

The draft IFRS S2 was well received, but respondents again emphasised the urgency for a global baseline on climate-related disclosures. Most respondents supported utilising the Task Force on Climate-related Financial Disclosures (TCFD) recommendations and agreed with the proposal on governance, strategy, risk management, the cross-industry metrics categories and targets; however, views were mixed relating to disclosure requirements for Scope 3 Greenhouse gas (GHG) emissions, the use of scenario analysis and industry-based requirements.

Key issues raised related to:

- Scope 3 GHG emissions – mixed views on the disclosure requirements and the ability for entities to be able to determine scope 3 emissions.
- Further guidance is needed on the term ‘significant’ to describe risks and opportunities, the terms ‘anticipated effects’ and ‘reasonably expected’, and what is considered short, medium and long term.
- Relevancy of disclosures if entities are already reporting climate-related disclosures based on ESG reporting, the TCFD recommendations and IFRS Accounting Standards.

- Additional guidance or illustrative examples to assist with determining significant climate-related risks and opportunities and how this is isolated from other risks, determining risk concentration and assessing current and anticipated effects.
- The significant resources to implement the requirements include investment in new systems and human resources.

Further details are here: [Summary of comments Climate-related Disclosures](#).

At their September 2022 Board meeting, the ISSB developed a list of items to be redeliberated, set out below (further details available at [ISSB September 2022 update](#)):

The ISSB tentatively decided on topics for redeliberation		
Both drafts of IFRS S1 and IFRS S2:	Draft IFRS S1:	Draft IFRS S2:
<ul style="list-style-type: none"> • Scalability. • Current and anticipated effects of sustainability-related and climate-related risks and opportunities on an entity's financial performance, financial position and cash flows. 	<ul style="list-style-type: none"> • Enterprise value. • The breadth of reporting required. • Significant sustainability-related risk or opportunity. • Identifying significant sustainability-related risks and opportunities and disclosures (including using the materials of other standard-setters). • Application of the materiality assessment. • Connected information. • Frequency of reporting. 	<ul style="list-style-type: none"> • Strategy and decision-making, including transition planning. • Climate resilience. • GHG emissions. • Industry-based requirements, including financed and facilitated emissions.

The ISSB met twice during November 2022 with the following key matters deliberated:

- Companies will be required to use climate-related scenario analysis to report on climate resilience and to identify the risks and opportunities to support their disclosures. This will be incorporated into IFRS S2. (Decided at 1 November 2022 meeting);
- Changes will be made to the requirement to revise comparative information to limit the application to estimates for the previously disclosed reporting period and exclude forward-looking estimates disclosed in the previous reporting period. Additional guidance will also be developed (tentatively decided at the 15-16 November meeting);
- Companies should present their sustainability-related financial disclosures simultaneously with the related financial statements. Some transitional relief may be provided, but the form and extent of the relief is to be reconsidered at a future meeting (tentatively decided at the 15-16 November meeting); and
- Further clarification will be provided on disclosures relating to climate-related risks and opportunities and the impact on the entity's financial strategy and decision-making, its plans to transition to a lower-carbon economy and its climate-related decisions meeting (tentatively decided at the 15-16 November meeting).

Further details are available in the updates from the [1-3 November](#) and [15-16 November](#) meetings.

The ISSB is planning to release IFRS S1 and S2 in early 2023. The next meeting of the ISSB will be held on 12-16 December 2022.

International Auditing and Assurance Standards Board (IAASB)

During the September Board meeting, the IAASB approved a project proposal to develop an overarching standard for assurance on sustainability reporting for all assurance practitioners.

The approach is to develop a new suite of standards relating to assurance on sustainability, expected to be called International Standards on Sustainability Assurance (ISSA) within a new 5000-number range. The overarching assurance standard for sustainability reporting will be standalone, but will be consistent with ISAE 3000 (Revised) and ISAE 3410. The standard will enhance the global consistency and reliability of sustainability reporting.

At the upcoming December 2022 IAASB board meeting, the Board will consider the proposed drafting for some of the parts of the proposed ISSA 5000.

The IAASB's project timeline would see an exposure draft approved for issue by September 2023 with a comment period of 120 days (Feb 2024 comment period close). The final pronouncement is expected to be released between December 2024 to March 2025.

International Ethics Standards Board for Accountants (IESBA)

During their September 2022 meeting, the IESBA discussed the potential approach to develop a fit-for-purpose, globally applicable ethics and independence standard for sustainability reporting and assurance by professional accountants. The priority will be developing revisions to the Code for professional accountants and with a view to making it also accessible for non-accountants.

Two approaches were presented during the IESBA September Board meeting:

- A. Amend Part 4A over the independence requirements that apply to sustainability-related engagements.
- B. Retain Part 4A and 4B and develop a new Part 4C to deal with sustainability-related information expressly.

The discussion at the September meeting indicated a preference for Part 4A to be amended rather than developing a new Part 4C.

On 1 November 2022, the IESBA considered four options, set out in the table below, for developing profession-agnostic ethics and independence standards for sustainability assurance engagements:

Revisions to Part 4 A			Establish separate Part
Option 1	Option 2	Option 3	Option 4
<ul style="list-style-type: none"> Involves the use of “sustainability assurance engagements” without amending the definition of “audit” as used in Part 4A 	<ul style="list-style-type: none"> Based on the current extant model – the term “audit” is extended to include “sustainability assurance engagements” in addition to as well as “review” engagements. 	<ul style="list-style-type: none"> The approach uses more general terms (e.g., “practitioner” and “engagement”). Proposed ET-GA revisions not yet considered; Will need to adapt/ revise new definitions arising from ET-GA work. 	<ul style="list-style-type: none"> Involves revisions to extant Part 4A to address independence only for “sustainability assurance engagements.” Will be positioned between extant Part 4A and Part 4B Similar to Option 1, but without any references to “audit.”
<ul style="list-style-type: none"> Retain provisions that apply to audit and review engagements Adapt definitions and key concepts, especially those arising from the ET-GA project. Establish/ Tweak definitions for sustainability Add sustainability-specific examples and guidance Align to IAASB ‘s proposed ISSA 5000 			<ul style="list-style-type: none"> Delete provisions that apply to audit and review engagements Establish/ adapt definitions for sustainability assurance Add sustainability-specific examples and guidance Align to IAASB’s ISSA 5000

Key considerations by the Board included:

- Most options would not be user-friendly for non-professional accountants. This is because they need to navigate the Code (designed for accountants) to find the relevant sections.
- The Code's title may need to change regardless of which option is chosen.
- There is a need to retain flexibility when developing sustainability-related materials in a dynamic and fast-moving market.
- A standalone Code for sustainability assurance engagements will provide greater flexibility and will not scope non-professional accountants into the rest of the Code.
- A new Standalone Code or Part would create duplication and conflicts across the extant Code.
- A new standalone Code would lose the ability to leverage off or be anchored to an already well-established extant Code.

No decision was made at this meeting on the option that the IESBA would pursue.

At the upcoming November/ December 2022 IESBA meeting, the Board will consider project proposals on sustainability for two distinct working streams:

- (a) the development of ethics and independence standards for sustainability reporting and assurance; and
- (b) the use of experts.

In relation to the development of ethics and independence for sustainability reporting, the IESBA will consider which of the four options set out in the table above should be adopted. The draft project proposal also notes that Parts 1 to 3 of the Code will also be revised for specific ethics requirements and guidance for sustainability reporting.

There is expected to be an increase in demand for the use of experts when reporting sustainability/ESG information. However, the IESBA also considers that there is a need to clarify and enhance independence when professional accountants use experts who are not part of the audit team.

Subject to IESBA's approval, these projects will commence immediately.

Global roundtables are planned for April/ May 2023 to engage with targeted stakeholders, such as sustainability assurance providers who are not PAs. The proposed project timeline indicates an exposure draft will be released after September 2023, with the Final Standard likely to be approved by September 2024 and effective from December 2024.

A verbal update of the IESBA meeting outcomes will be provided to the APESB on the 7th of December 2022.

IESBA Technical Staff publication on Greenwashing

On 21 October 2022, the IESBA released [*Ethics Considerations in Sustainability Reporting, Including Guidance to Address Concerns about Greenwashing*](#). The Questions & Answers (Q&A) guidance aims to assist professional accountants and professionals who are involved in preparing sustainability reports to navigate ethics challenges that may arise from sustainability reporting with misleading or false sustainability information (greenwashing).

The ethical issues relating to greenwashing in the publication include:

- Pressure to breach Fundamental Principle of Ethics
- Misleading or inaccurate claims on sustainability-related performance of an investment.
- Inadvertent errors.
- The complexity of, and lack of reliable and comparable, ESG data.

U.S Securities and Exchange Commission

The [*U.S. SEC has proposed enhanced climate disclosures*](#) on climate-related risk and relevant risk management processes to support a global system for delivering consistent, comparable and assurable sustainability information.

European Commission

The European Commission have developed a proposed [Directive on Corporate Sustainability Due Diligence](#), closely interlinked with the [Corporate Sustainability Reporting Directive \(CSRD\)](#) adopted in April 2021. Provisional political agreement was reached by the European Parliament on the CSRD on [21 June 2022](#) and the three stages of the application of the regulation.

On 10 November 2022, the European Parliament approved the final political agreement on the CSRD. The CSRD introduces more reporting requirements on sustainability reporting that align with the [EU's climate goals](#), which will mitigate the risk of greenwashing. The Council is expected to adopt the proposal on 28 November 2022.

In addition, the European Reporting Advisory Group have approved the first set of European Sustainability Reporting Standards (ESRSs), which were submitted to the European Commission. The Commission will undertake its due diligence to ensure complete alignment with the CSRD and plans to adopt the final ESRS in June 2023.

IOSCO

On [9 November 2022](#), at COP 27, the International Organization for Securities Commissions (IOSCO) outlined actions to mitigate greenwashing for sustainability disclosures and promote transparency and integrity in the carbon market.

The IOSCO set out their expectations that the disclosure and assurance sustainability standards will be effective for the 2024-year end. In addition, IOSCO published a [call for action](#) for all voluntary standard-setting bodies and industry associations operating in financial markets to promote good practices to mitigate the risk of greenwashing related to asset managers and ESG rating and data providers.

IFAC

On 9 November 2022, IFAC released a new report [Getting to Net Zero: A Global Review Corporate Disclosures](#), which focuses on corporate emissions reduction reporting. The report analyses disclosure trends in emission targets for 600 companies, including 40 of the largest listed companies across 15 jurisdictions.

The report findings suggest a lack of consistency and comparability in climate reporting, particularly target disclosures. The report highlighted the following key considerations:

- The need for consistent terminology;
- The inclusion of scope 3 emissions in reduction targets and transition plans;
- Standardise transition plan disclosures; and
- Transparency of financial implications of decarbonisation.

NZ XRB

The comment period for the Exposure Drafts for Climate-related disclosures issued by the External Reporting Board (XRB) closed in September 2022. The XRB has received 133 submissions and is in the process of finalising the standard, which will be published in December 2022. Further details on the Exposure Drafts and the submissions can be found on the XRB [website](#).

2. Australian Developments

APESB

On 24 October 2022, the APESB and the External Reporting Board (XRB) sent a joint letter to the IESBA on the proposed approach for the IESBA Code to develop ethics and independence standards for sustainability reporting and assurance.

APESB and XRB both support the IESBA prioritising the sustainability project and their ongoing work with IAASB on the assurance and ethical consideration of sustainability-related corporate reporting.

The APESB and XRB raised concerns concerning the proposed approach of expanding Part 4A of the IESBA Code to address the independence requirements of sustainability assurance engagements. APESB and XRB recommend the IESBA engage with a broader range of sustainability practitioners to develop independence requirements for sustainability assurance.

Refer to Agenda Item 6(a) for the APESB and XRB joint letter.

Chartered Accountants and Australia and New Zealand (CA ANZ)

CA ANZ, in conjunction with ACCA, have released a new insight series built on the popular “How SMEs can create a more sustainable world” playbook. The series focuses on five key areas SMEs can incorporate sustainable practices in their business operations. These areas are the role of SMEs; developing a sustainability strategy; climate and the environment; waste and the circular economy and social sustainability.

The latest guide, ‘How SMEs can create a more sustainable world,’ provides a range of resources and insights and sets out the business case for SMEs. This includes how embedding sustainability can strengthen the supply chain, drives down costs, create value, attract talent, and improve access to finance. Further details can be found in CA ANZ’s [media release](#).

Way Forward

Technical Staff will continue to update the Board on key Australian and international developments from an ethical perspective. Where appropriate, APESB will participate and influence global and local developments in sustainability reporting and assurance when it impacts or interrelates with professional & ethical standards.

Recommendation

That the Board note the update on the developments in sustainability globally and in Australia.

Material Presented

Agenda Item 6 (a) Joint APESB NZ XRB Letter on the IESBA's Sustainability Project

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