# Sustainability Reporting Developments

July 2023 | Monthly Update
**EY Global Public Policy**

An update on sustainability reporting policy and regulatory developments

*Note: In light of summer holidays, we will not issue an August newsletter and will resume publishing in September.*

**After two years since first contemplated by the IFRS Foundation, in the final step that has the potential to usher in a new era of corporate reporting, the International Sustainability Standards Board (ISSB) has published its first global sustainability disclosure standards.**

With the launch of the inaugural International Financial Reporting Standards (IFRS) Sustainability Disclosure Standards, the ISSB now turns its focus to encouraging countries to adopt the ISSB standards at the country-level. Just weeks after the release of the standards, a growing number of countries have indicated they plan to adopt the standards within their jurisdictions.

In Europe, the European Commission completed its final public consultation on the first set of European Sustainability Reporting Standards (ESRS) ahead of their initial application beginning in January 2024.

In the United States, amidst ongoing uncertainty about the content and timing of climate and human capital disclosure rules issued by the Securities and Exchange Commission (SEC), we spoke with former SEC Chair Allison Herren Lee in an exclusive interview for her insights into the SEC rulemaking process. (See Americas section below.)

A more complete rundown of global policy developments relating to sustainability reporting is below. For quick access to regional developments, use the following links: Global; Americas, including an interview with former SEC Acting Chair and Commissioner Allison Herren Lee; Europe, Middle East, India and Africa (EMEIA); Asia-Pacific.

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## Key developments

**Global**

In late June, the **ISSB released the final version of its inaugural standards**, IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* (IFRS S1) and IFRS S2 *Climate-related Disclosures* (IFRS S2). **The release marks a significant milestone for the ISSB and has the potential to usher in a new era in corporate reporting.**

**The standards are effective for reporting periods beginning on or after 1 January 2024**, though mandatory application depends on individual country's endorsement and / or regulatory process. A "climate first" transition option is available, which allows a company to provide only climate-related disclosures in the first year pursuant to IFRS S2, notwithstanding that both IFRS S1 and IFRS S2 may be in effect.

Importantly, **the application of IFRS Sustainability Disclosure Standards is not linked to the application of IFRS Accounting Standards**. Therefore, a company applying IFRS Accounting Standards for financial reporting purposes is currently not required to also apply IFRS Sustainability Disclosure Standards, and vice versa.

**The extent to which the ISSB standards will serve as a global baseline will depend on country-level adoption.** A number of large economic jurisdictions are developing, or have already introduced, plans to consider incorporating the ISSB standards into their local frameworks, including Australia, Canada, Colombia, Hong Kong, Japan, Malaysia, New Zealand, Nigeria, Singapore, and the United Kingdom.

Shortly after the publication of IFRS S1 and IFRS S2, the ISSB announced it would take over the monitoring of the Task Force for Climate-related Financial Disclosures (TCFD) at the request of the Financial Stability Board, marking further consolidation of the long-derived "alphabet soup" of voluntary sustainability disclosure standard setters.

The ISSB still has **two open consultations** for public comment related to (i) its 2024-2026 workplan and (ii) the international applicability the Sustainability Accounting Standards Board (SASB) standards. Taking into consideration the activities outlined in its 2024-2026 workplan consultation, the ISSB will discuss in its July meeting the possible development of targeted educational material – for instance, potentially on the topic of "Just Transition" – to illustrate how the existing requirements in IFRS S2 might be applied without amending the requirements in IFRS S2.

Meanwhile, the **International Auditing and Assurance Standards Board (IAASB)** announced that it will soon release, for consultation, a draft standard for sustainability assurance (including both limited and reasonable assurance). The consultation period is expected to span from early August 2023 through December 2023.

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**Asia-Pacific**

**China** has taken a step in extending the ISSB's global footprint by opening an ISSB office in Beijing. The new office will serve as a hub for the ISSB's stakeholder engagement in Asia as well as advance the momentum for sustainability reporting in one of the world's largest economies.

In **Singapore**, the government has launched a consultation on recommendations to advance climate reporting in the country, measures of which include alignment with the ISSB standards beginning FY 2025 for all listed issuers and third-party assurance for Scope 1 and 2 emissions.

Meanwhile in **Australia**, the Treasury has launched its second consultation on mandatory climate-related financial disclosure. The standard is expected to closely align with IFRS S2 and reporting will be mandated on a phased basis beginning with the largest entities 1 July 2024.

The Financial Markets Authority of **New Zealand** had published has published a suite of guidance to support businesses as they work to meet their obligations under the new Climate Related Disclosure (CRD) reporting requirements.

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**Americas**

In the **United States**, the timing of the release of the SEC's final climate disclosure rule and proposed human capital management rule remains uncertain.

According to the SEC's regulatory agenda, both rulemakings appear slated for release sometime in the next several months.

In **California**, legislation to mandate climate-related disclosure, CA SB 253, has been amended to provide a 1-year relief from Scope 3 greenhouse gas emissions reporting. The legislation would apply to an estimated 5,400 companies (that is, any company doing business in the state and generating more than $1 billion in annual revenue). The bill must now be approved in state Assembly Committees and pass a vote on the floor.

**Interview with former SEC Acting Chair and Commissioner Allison Herren Lee**

For further insight into the SEC's rulemaking process, we recently had the chance to speak with Allison Herren Lee, former SEC Acting Chair and Commissioner, and a member of the Sustainability Advisory Board at Persefoni. Lee served as a Commissioner of the SEC from 2019 to 2022 and as Chair from January to April 2021, leading the development of the agency's draft climate-related disclosure rule. What follows are her responses to questions posed by EY:

***The SEC was scheduled to release a final climate disclosure rule in April. That deadline has obviously passed. While agencies often take longer than planned to finalize a regulation, are you at all concerned by the delay? What issues do you think the SEC is working to resolve before a final rule is brought before the Commission for a vote? How concerned do you think***

***Chair Gensler is – and how concerned are you – about the risk of a court challenge alleging that the SEC has exceeded its authority with a new climate disclosure regulation?***

*Just to level set, while the regulatory agenda appears to "set deadlines" it is really just a listing of all outstanding priorities. As a matter of form, the agendas always show either April or October as projected dates, but the work is churned out weekly and consistently over the weeks and months in each period covered by the agenda. This is just to say that, for what it's worth, I wouldn't characterize the timing as delayed. This is a complicated rulemaking that garnered significant public comment. It is not surprising, and in fact it is prudent, for the Commission to take some time to carefully deliberate over a final rule as it seeks to incorporate the public's feedback and come to a consensus internally.*

*Some of the issues that have received significant attention are the inclusion of Scope 3 GHG [greenhouse gas] reporting requirements, the proposed disclosures related to the financial impacts of climate change on a financial statement line-item basis, and the provision for assurance of Scopes 1 and 2 GHG emissions. I am confident the Commission is carefully considering these and other issues as it crafts the final rule.*

*Regarding litigation risk, I would expect that Chair Gensler, the other Commissioners, and the [SEC] staff are considering the Supreme Court's recent rulings that have invoked the major questions doctrine. In my view, the proposed rule is squarely within the SEC's established statutory authority both because it has long had rules relating to environmental risks and issues, and the proposed rule is purely about disclosure. That said, the recent judicial landscape must be on the Commission's mind.*

***With the ISSB and EU CSRD [Corporate Sustainability Reporting Directive] rules set to become effective in January, and given the delay in the release and implementation of standards in the US, is there a risk that the US could lose an ability to shape, on a global level, sustainability disclosures? How do you see the potential for greater interoperability among major standards?***

*I believe the SEC still has the ability to help shape sustainability disclosures in an important way. We have the largest and most robust capital markets in the world, so the role of the SEC is inherently significant. The recently [issued] ISSB standards closely align with the SEC's climate proposal, so I am optimistic about the potential for convergence and possible interoperability of reporting standards.*

***ESG [Environmental, Social, and Governance] issues have become increasingly politicized in the United States. What in your view is driving this politicization? Opponents of ESG say that companies need to focus solely on shareholder returns and that saddling them with ESG-related responsibilities will harm the competitiveness of US companies and US capital markets. How do you respond?***

*ESG issues present both financial risks and opportunities for companies. Therefore, companies that understand and manage the financial impacts of the specific ESG issues their businesses face are better positioned to maximize shareholder return. Focusing on the financial impacts of ESG issues is the common ground. The political wrangling tends to distract both companies and their investors from the significant issues they must address to ensure long-term corporate success, and the stability, efficiency, and prosperity of the broader economy. I believe that reason will ultimately win out over political posturing.*

***Some critics argue that an SEC climate disclosure rule may place an undue burden on companies, particularly if it is not compatible with rules in other jurisdictions where companies also operate. How can the SEC address these concerns while still ensuring transparency, accountability, and effectiveness in climate-related disclosures?***

*The [SEC] climate proposal closely aligns with the ISSB standards and leverages the same consensus-driven frameworks of the TCFD and the GHG Protocol used around the world. This was deliberate. The SEC recognized the importance of global alignment and of drawing on existing frameworks that have enjoyed significant voluntary market uptake. The proposal also provides mechanisms to ease the burden on companies by providing for phased-in compliance, safe-harbors for good faith work, and permitting the use of estimates where reported data might be difficult to obtain.*

***In 2020, the SEC released principles-based Human Capital rules. Yet, Chair Gensler has said he is working on another human capital rule. Do you agree that such a rule is needed and, if so, why?***

*The 2020 amendments to Item 101 of Regulation S-K simply added language that the topic of human capital must be addressed to the extent material to a company's business. Some would have said such a discussion was already required under Item 101. This view is bolstered by analyses since the rule was adopted showing that it has prompted little additional disclosure on the topic. However, human capital has evolved to become a central driver of enterprise value in modern business models, and thus an important topic for investors to be able to gauge and compare metrics. It makes sense for the Commission to consider how to get the specific, relevant, decision-useful information to investors they need in this area to accurately price risk and allocate capital.*

***During your tenure as an SEC Commissioner, you are credited for helping to propel ESG issues to the forefront of the agency's agenda. What made you decide that these issues should be addressed by the SEC? What do you say to those who assert that the SEC has no role in addressing ESG-related matters?***

*We were reacting directly to what we observed in the market which was an historically unprecedented shift in traditional investment analysis toward the risks and opportunities that ESG topics present. We saw massive amounts of capital being directed into ESG funds, we saw investors demanding more and better disclosures on ESG topics, and we saw a proliferation of shareholder proposals (often a harbinger of good governance trends) related to ESG. The role of the Commission is to help ensure that markets are supplied with the material information that investors need. Under the status quo, it was clear that disclosures around ESG risks and opportunities were not sufficiently consistent, comparable, or reliable to meet the demands of the market.*

*When there are no disclosure requirements, or when broad-based requirements don't result in the kind of transparency and accountability that makes our capital markets strong, it is incumbent upon securities regulators to step in and help identify the specific data, metrics and assurance needed. We saw that with, for example, executive compensation, and that's what the Commission is working toward on climate risk, and hopefully soon, on human capital. This is the quintessential work of the SEC to help ensure the stability of the capital markets and protect the millions of families whose savings are dependent on the strength of our financial system.*

**Europe, Middle East, India and Africa (EMEIA)**

In the **European Union**, the European Commission finished its final public **consultation on the first set of ESRS**. It is expected that the Commission will make some very limited revisions to the standards based on the comments received and adopt the standards by 28 July 2023. This timeline enables the standards to be finalized before the effective date of the CSRD on 1 January 2024.

In the latest draft of the standards, further updates were made – most intended to reduce the regulatory burden on companies – including:

i. All disclosure requirements within each standard will be subject to a **materiality assessment** with the exception of the disclosure requirements specified in ESRS 2 General disclosures.

ii. More **requirements will be phased-in** over time. For example, companies with less than 750 employees will receive an exemption from providing Scope 3 greenhouse gas emissions data in the first year that the ESRS take effect.

iii. **Certain disclosures will be made voluntary**, including, for example, biodiversity transition plans.

iv. **Greater flexibility will be permitted for, certain disclosures** including, for example, the methodology used for the materiality assessment process.

## On the horizon

Key dates to watch over the next 90+ days:

**TBC:** In the US, release of the SEC's final climate-related disclosure rule and draft human capital management rule.

**August 2023:** The consultation on International Auditing and Assurance Standards Board (IAASB) standard on sustainability assurance guidance is expected to open.

**September 2023:** The comment period for the ISSB's 2024-2026 workplan consultation will close.

**September 2023:** The Taskforce on Nature-related Financial Disclosures (TNFD) is expected to publish its final framework.

**Q3 2023:** IOSCO is expected to release its decision on the endorsement of the ISSB standards

**Q4 2023:** The UK Financial Conduct Authority (FCA) is expected to publish its final Sustainability Disclosure Requirements (SDR) for asset managers, and a general anti-greenwashing rule applicable to all FCA regulated firms.

## In case you missed it

**Global Sustainability Disclosure Rules Go Live.** CFOs Watch for What's Next. From the *Wall Street Journal*, companies are cautiously awaiting global sustainability disclosure rules as they plan strategies, considering potential differences in SEC and EU requirements. Link.

**The battle of sustainability assurance: audit firms "versus" other providers.** IFAC director for Sustainability, Policy & Regulatory Affairs David Madon discusses the landscape of sustainability assurance and the implications of regulation for different stakeholders, highlighting differences in scope, standards, and application between audit firms and other service providers. Link.

**Disability Hub Europe publishes updated resource that reflects latest GRI Standards.** The guide helps organizations align with the evolving sustainability reporting landscape and emphasizes the importance of inclusivity and sustainability. Link.

**FRC publishes report on ESG data use and distribution.** The Financial Reporting Council (FRC) published a new report examining how investors obtain and use environmental, social and governance (ESG) data on companies, and highlights what actions companies can take to facilitate this. Link.

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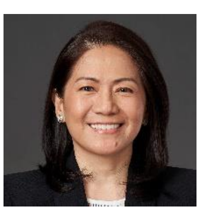

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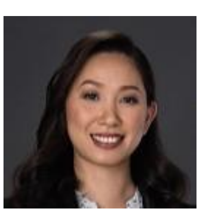

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