IFRS valokeilassa

Sustainability Reporting Newsletter #1

May 2024

Contents

Introduction

Welcome to the inaugural edition of IFRS valokeilassa Sustainability Reporting Newsletter!

We are thrilled to embark on this journey with you, aiming to keep you informed and up to date on the developments in sustainability reporting. As the landscape of corporate sustainability and reporting evolves, it is critical to stay ahead of the curve, and our newsletter is designed to provide you with valuable insights and resources to navigate this dynamic field.

What to expect

In each issue, you can look forward to a curated selection of content covering a range of topics pertinent to sustainability reporting. From standard setter news and updates to insightful analyses from PwC Global network, we aim to deliver actionable information that empowers you to enhance your reporting practices.

In this issue

In this inaugural issue, we summarise global updates from standard setters, along with specific updates from the ISSB, the EU, and the US. Additionally, PwC Sustainability Insights will explore fundamental questions such as the essence of a sustainability reporting policy, the channels for disclosing sustainability-related information, and the impact of laws and regulations on reporting practices.

Standard setter news and updates

1. Global updates

In June 2023, two inaugural standards, IFRS® Sustainability Disclosure Standards (IFRS SDS): IFRS S1 'General Requirements for Disclosure of Sustainability-related Financial Information'[1] and IFRS S2 'Climate-related Disclosures' were issued by the International Sustainability Standards Board (ISSB™). IFRS Sustainability Standards are developed to enhance investor-company dialogue so that investors receive decision-useful, globally comparable sustainability-related disclosures that meet their information needs. IFRS S1 and IFRS S2 are effective for annual reporting periods beginning on or after 1 January 2024, with early adoption permitted. This is subject to the endorsement of the standards by local jurisdictions.

In December 2023, the ISSB published amendments to the SASB® Standards[2] to enhance their international applicability and issued new educational material illustrating the nature and social aspects of climate-related risks and opportunities.

[1] IFRS is a registered trademark of the IFRS Foundation
[2] SASB Standards are a source of guidance for applying IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information.

2. EU updates

In November 2022, the Corporate Sustainability Reporting Directive (CSRD) was adopted in the European Union (EU) and became effective on 5 January 2023; EU Member States have until July 2024 to transpose CSRD into national law. The related reporting standards — the European Sustainability Reporting Standards (ESRS) — were adopted in July 2023. A two-month period of scrutiny from the European Parliament and Council of the European Union ended on October 21, 2023, and the ESRS became law on 22 December 2023 when they were published in the Official Journal of the European Union.

In December 2023, EFRAG issued materiality and value chain implementation guidance and a list of ESRS data points[3]. In February 2024, EFRAG released the first set of technical Explanations provided to assist stakeholders in the implementation of the ESRS via the EFRAG ESRS Q&A Platform[4].

3. US updates

On March 6, 2024, the SEC adopted final rules[5] designed to enhance public company disclosures related to the risks and impacts of climate-related matters. The new rules include disclosures relating to climate-related risks and risk management as well as the board and management's governance of such risks. In addition, the rules include requirements to disclose the financial effects of severe weather events and other natural conditions in the audited financial statements. Larger registrants will also be required to disclose information about greenhouse gas emissions, which will be subject to a phased-in assurance requirement.

On 4 April 2024, the SEC stayed the rules to "facilitate the orderly judicial resolution" of pending legal challenges.

In October 2023, three landmark climate disclosure bills, Senate Bill (SB) 253, SB 261, and Assembly Bill (AB) 1305, were signed into California law requiring Greenhouse gas (GHG) disclosures, Task Force on Climate-related Financial (TCFD) disclosures, and supplemental disclosures relating to emissions claims and carbon offsets.

These frameworks each describe expansive sustainability disclosures — although their scopes, effective dates, and other details vary.

[3] EFRAG has published its first three draft ESRS Implementation Guidance documents for public feedback. Draft EFRAG IG 1 deals with the requirements on the materiality assessment in ESRS and Draft EFRAG IG 2 with the value chain aspects in ESRS. Draft EFRAG IG 3 contains the detailed ESRS datapoints as a Microsoft Excel workbook with an accompanying explanatory note

[4] EFRAG launched its ESRS Q&A Platform to collect and answer technical questions, supporting preparers and other stakeholders with the implementation of the European Sustainability Reporting Standards (ESRS) issued as Delegated Ac

[5] SEC climate-related disclosure rules

The “big three” frameworks and one of the California bills incorporate the recommendations of TCFD. Leveraging this framework provides a point of continuity with voluntary reporting and unites the disclosure frameworks through the TCFD’s four pillars of governance, strategy, risk management, and metrics and targets.

Uncertainty persists regarding interoperability — There continues to be uncertainty about interoperability — that is, whether disclosures for one reporting framework can satisfy some or all of the requirements of another. Companies captured in multiple reporting regimes have a vested interest in understanding which reporting applies and where the frameworks align and diverge.

On 2 May 2024, the IFRS Foundation and EFRAG jointly published interoperability guidance[6] on climate-related disclosures for sustainability reporting. This interoperability guidance illustrates where there is a high level of alignment of the climate-related disclosures in the IFRS® Sustainability Disclosure Standards and the European Sustainability Reporting Standards (ESRS). It also notes areas with incremental disclosures and choices preparers need to make to enable interoperability. To find out more information related to the alignment in the main reporting frameworks, do not hesitate to contact us.

PwC Sustainability Insights

The three primary frameworks, ESRS, IFRS S1 and S2, and SEC climate disclosure rules, all align with the four pillars outlined in the TCFD) framework, requiring disclosure related to governance, strategy, risk management, and metrics and targets. Both the IFRS Sustainability Disclosure Standards and the ESRS adhere to this four-pillar structure for broader sustainability-related risks and opportunities, extending beyond solely climate-related considerations. However, users of sustainability reporting must understand the underlying policies driving the disclosed information.

PwC has released its initial set of FAQs on sustainability reporting In depth **INT2023-07**, ‘Navigating Sustainability reporting: Practical Application and Analysis’ to provide practical guidance to preparers. In this issue, we will explore the following fundamental questions.

Question 1. What is a sustainability reporting policy?

In contrast to financial reporting, which mandates the transparent disclosure of an entity’s accounting policies, neither the ISSB nor the SEC defines ‘sustainability reporting policies’. While ESRS 1 offers some guidance on ‘policy’, it is limited in scope.

While not explicitly mandated, preparers are encouraged to contemplate describing the policies utilised in a footnote within the sustainability report, similar to those in financial statements. This practice ensures that sustainability reporting policies are adequately recognized and documented, thereby enhancing the consistency of reporting.

This FAQ outlines that while there is no specific definition for sustainability reporting policies in major reporting frameworks, such as ESRS, IFRS SDS, and SEC climate-related disclosure rules, we would

[6] The interoperability guidance is designed to reduce complexity for entities applying both the ISSB Standards and ESRS.

expect sustainability reporting to follow financial reporting principles around reporting policies, although other approaches might be acceptable.

The FAQ emphasises that management needs to establish policies governing the compilation of sustainability data and the preparation of sustainability reporting. These policies typically include determining criteria, reporting boundaries, consolidating sustainability information, and, without a specific thematic standard, the sources of guidance considered. Consistency in applying these policies from period to period is crucial, with any deviations requiring adequate disclosure along with reasons.

Despite the absence of a formal definition of sustainability reporting policy, entities could adapt the definition provided in paragraph 5 of IAS 8 and define sustainability reporting policies as the specific principles, bases, conventions, rules, and practices applied by an entity in preparing and presenting sustainability reporting. Alternatively, the definition of 'policy' in Annex II, 'Acronyms and glossary of terms'[7], to ESRS could be applied.

Question 2. Where should sustainability-related information be disclosed?

The ESRS and SEC final rules on climate-related disclosures provide specific guidelines on where sustainability-related information should be reported. Under the ISSB standards, various factors are considered in determining the appropriate disclosure locations:

- Compliance with local regulations: Local laws or regulations may specify where sustainability-related information should be disclosed within an entity's financial reporting.
- Integration with management commentary: Sustainability-related financial information can be included in an entity's management commentary, provided it complies with local laws or regulations. Management commentary offers insights into an entity's financial position and performance, complementing financial statements, and may be titled differently within each jurisdiction.
- Cross-referencing: Information required by IFRS Sustainability Disclosure Standards can be cross-referenced, but it must be available simultaneously and must not hinder the understanding of sustainability-related financial disclosures.
- Incorporation by reference (ESRS): ESRS outlines specific conditions for incorporating information by reference from various sections, such as management reports, financial statements, and regulatory documents.

For entities reporting under ESRS, disclosure should be included within a dedicated section of the management report identified as the sustainability statements. In Finland, Toimintakertomus or Board of Directors report is the local equivalent of the management report." The sustainability statement, which is titled "kestävyysraportti" in Finnish, is part of toimintakertomus based on the Finnish Accounting Act. There are specific conditions relating to information incorporated by reference, listed in paragraph 120, ESRS 1. The incorporation of information by reference is allowed only for information found in the following locations:

[7] Annex II, 'Acronyms and glossary of terms', page 23

- another section of the management report;
- the financial statements;
- the corporate governance report (if not part of the management report);
- the remuneration report required by Directive 2007/36/EC of the European Parliament and the Council;
- the universal registration document, as referred to in Article 9 of Regulation (EU) 2017/1129;
- public disclosures under Regulation (EU) 575/2013 of the European Parliament and of the Council ('Pillar 3 disclosures'). [paragraph 119, ESRS 1].

SEC registrants will be required to disclose certain climate-related financial statement effects and related disclosures in a footnote to the audited financial statements. For disclosures required outside the financial statements, registrants should file the climate-related disclosure in their registration statements and annual reports; Include the climate-related disclosures, except for any Scopes 1 and/or 2 emissions disclosures, in a separate, appropriately captioned section of their filing or in another appropriate section of the filing, such as Risk Factors, Description of Business, or Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A"), or by incorporating such disclosure by reference from another Commission filing as long as the disclosure meets the electronic tagging requirements of the final rules.

Question 3. How do laws and regulations impact sustainability reporting?

The three main frameworks require disclosures regarding material risks and opportunities. Changes in legislation, whether new laws or amendments to existing ones, might impact an entity and the risks and opportunities outlined in its sustainability report. Presently, the main frameworks lack explicit guidance on this matter.

Entities should stay vigilant about emerging legislative and regulatory changes that may affect their operations and disclosures. Since risk and opportunity assessments are forward-looking, reliance solely on current laws and regulations is insufficient. Monitoring the legislative landscape is crucial to anticipate potential impacts on operations and the likelihood of enactment.

It might be beneficial for entities to compare how new or potential changes in laws and regulations are treated in financial reporting versus sustainability reporting.

For instance, if a law is enacted mandating responsible management of manufacturing waste, entities should evaluate potential impacts on their operations and strategies. Failure to comply could lead to penalties or necessitate changes in manufacturing processes.

Similarly, if a proposed law requires GHG emissions reductions for government suppliers, entities must assess the risk of non-compliance and its potential impact on revenue from government contracts. Such forward-looking analysis is vital for strategic decision-making and risk management.

In the next issue

Stay tuned for our next issue, where we will delve deeper into more practical reporting issues, providing you with actionable insights that enable you to navigate the complexities of sustainability reporting with confidence.

References

Navigating sustainability reporting: Practical application and analysis

Supporting materials for IFRS Sustainability Disclosure Standards

California's not waiting for the SEC's climate disclosure rules

SEC adopts climate-related disclosure rules

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