July 29, 2022

Mr. Emmanuel Faber
Chair, International Sustainability Standards Board (ISSB)
Columbus Building
7 Westferry Circus
Canary Wharf, London E14 4HD
United Kingdom

INSTITUTE OF INTERNATIONAL FINANCE

RE: International Sustainability Standards Board Exposure Draft IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* and Exposure Draft IFRS S2 *Climate-related Disclosures*

Dear Mr. Faber:

The Institute of International Finance (IIF) welcomes the opportunity to comment on the International Sustainability Standards Board (ISSB) Exposure Draft (ED) IFRS S1 *"General Requirements for Disclosure of Sustainability-related Financial Information"* and ED IFRS S2 *"Climate-related Disclosures"*.

The IIF strongly supports the objective of the ISSB to develop a comprehensive global baseline of sustainability disclosures for the capital markets as well as sectors across the real economy. The IIF has previously advocated for the establishment of an internationally recognized framework for the disclosure of sustainability-related information, covering Environmental, Social, and Governance (ESG) factors, as an urgent priority.[1] While the proliferation of multiple voluntary disclosure frameworks has helped to advance the quality and technical rigor of disclosure practices, particularly with respect to climate-related risk, the resultant array of standards, definitions, metrics, and indicators is leading to fragmentation, as policymakers have begun to embed sustainability reporting expectations in mandatory disclosure requirements. At the same time, an increasing share of corporates and financial institutions are committing to climate and sustainability-related goals, such as Net Zero targets, which is inspiring innovation in technical approaches in areas such as transition planning, and relevant approaches to report on progress. The continued evolution of disclosure practices, methodologies, metrics, and expectations creates a pressing imperative for alignment. We therefore fully support the work of the IFRS Foundation and the ISSB in this field.

[1] See, for instance, the IIF Position Papers "Integrity through Alignment: A 2022 Roadmap for Global Standards and Market-led Approaches in Sustainable Finance" (February 2022) and "Building a Global ESG Disclosure Framework: A Path Forward" (June 2020).

We appreciate and encourage the ISSB to continue its close dialogue and collaboration with voluntary frameworks and standard setters, as well as jurisdictional authorities to enable as much international convergence as possible and to avoid overlaps and inconsistencies as the IFRS Sustainability Disclosure Standards and different jurisdictional frameworks evolve. **To avoid fragmentation, global consensus must be built on the IFRS Sustainability Disclosure Standards, with a clear and direct route towards global adoption and/or recognition**—not only in jurisdictions that utilize IFRS, but also in jurisdictions that follow Generally Accepted Accounting Principles (GAAP). We have advocated for the importance of alignment and interoperability of jurisdictional standards with the IFRS Sustainability Disclosure Standards in our engagement with local authorities and responses to jurisdictional consultations, including in our recent response to the U.S. Securities and Exchange Commission (SEC).

We would strongly encourage jurisdictions to adopt a substituted compliance regime with regard to IFRS Sustainability Disclosure Standards so that preparers who use those standards (or frameworks mandated in other jurisdictions) do not need to produce duplicate disclosures where the informational content is equivalent. **Such an approach would be in line with existing international precedent and would help alleviate concerns about international alignment, facilitating compliance and interoperability among different regimes.** It would also be important to not only have a common understanding of the disclosure standards but also of the litigation framework around those standards—we have provided further comments in the section on litigation and safe harbor provisions below. It would be helpful for the ISSB to encourage this type of approach to ensure the success and uptake of the final IFRS Sustainability Disclosure Standards. However, in order for this to work, an equivalent understanding of scope, terminology, etc. is needed and we therefore underscore the importance of global alignment around common definitions. We hence support the formation of a working group of jurisdictional representatives (or other similar mechanisms) to establish dialogue for increased alignment between the IFRS Sustainability Disclosure Standards and other international sustainability disclosure initiatives.

The IIF perceives that there may be aspects of the IFRS Sustainability Disclosure Standards which, as proposed, may create challenges for corporates and financial institutions. We raise a few high-level points pertaining to both Exposure Drafts (ED) in this cover letter. In the Annex to this letter, we have provided more details and additional answers to the specific questions posed in the EDs.

The IIF broadly supports the ISSB's overall goal of proposing a global baseline standard not only for climate-related disclosures but ultimately also for broader sustainability-related information. **It is important to recognize that climate-related disclosures, even though data challenges remain, have seen much more stakeholder interest and have hence developed faster than broader ESG disclosures** where a similar level of progress has yet to take place. We understand that Draft IFRS S1 is intended to work as the overarching disclosure standard upon which topical standards (such as Draft IFRS S2 for climate-related disclosures) will build and to which those topical standards will add more detail. For this reason, **the IIF believes it makes sense to publish IFRS S1 at the same time as IFRS S2. This can help promote alignment by establishing a baseline standard that jurisdictions can work with as and when they decide to look at ESG issues beyond climate.**

We acknowledge that many jurisdictions will not mandate the disclosure of non-climate-related disclosures in the foreseeable future. At the same time, certain jurisdictions are already pushing ahead on their own, hence adding to further fragmentation. **Developing a global baseline standard on sustainability information, even if not immediately adopted by all jurisdictions (at all or in its entirety), would limit the fragmentation risk.** However, we see a risk of fragmentation of the global sustainability disclosure landscape unless the term 'sustainability' used in Draft IFRS S1 is more clearly defined.

We appreciate the ISSB's focus of its proposed disclosure requirements on the concept of 'enterprise value' which would go beyond information reported in the financial statements and include information about a company's impacts and dependencies on people, the planet, and the economy when relevant to the assessment of the company's enterprise value. However, **many IIF members are concerned that the definition of 'enterprise value' might lead to myriad interpretations in different jurisdictions if such terms were applied differently in both existing and new policy frameworks and requirements**. This could lead to consistency and comparability issues in disclosures, which would ultimately impede achieving the ISSB's mission of setting global standards.

A clearer definition of 'enterprise value' and its underlying concepts (e.g. to what extent mitigating actions should be included) is therefore necessary, acknowledging that the question of what is material to investors will change over time. Of particular importance is the consideration of the underlying components of ISSB's definition of 'enterprise value' as "the sum of the value of the entity's equity (market capitalisation) and the value of the entity's net debt", as the significance of these values from an investor perspective will vary across sectors and as market conditions change. For instance, debt may not serve the same purpose for banks as it does for manufacturing companies.

The IIF supports the ISSB building on the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). Financial institutions have developed familiarity and experience with disclosure in line with the 2017 TCFD framework. However, **financial institutions have not yet gained as much experience with the disclosure of new types of climate-related information reflected in the TCFD's October 2021 revisions**, particularly in areas such as transition plans, financial impacts, and cross-industry climate-related metrics, e.g., on how the value chain should be defined for the financial sector, to provide the most useful information to investors.

In ED IFRS S1, the ISSB acknowledges that "*[w]hen metrics cannot be measured directly and can only be estimated, measurement uncertainty arises*. *The use of reasonable estimates is an essential part of preparing sustainability-related metrics*…" (paragraph 79). While the IIF agrees with this assessment, we think the same is true for certain climate-related information. In its proposed rule on *"The Enhancement and Standardization of Climate-Related Disclosures for Investors,"* the U.S. SEC, for instance, has proposed **safe harbor provisions** covering the disclosure of Scope 3 emissions, transition plans, and scenario analyses disclosures in recognition of the difficulty of calculating Scope 3 emissions (including double counting, variability in methodologies, and incomplete guidance and reporting) and the need for reliance on forward-looking information for transition planning and scenario analyses. These proposed safe harbor provisions would give preparers the ability to disclose this important information to the best of their ability with protection from liability. While jurisdictional authorities would need to decide on safe harbor provisions, we urge the ISSB to acknowledge these challenges in its EDs.

We encourage the ISSB to move expeditiously to outlining its future work program as that will be an important signal to those jurisdictions that have already outlined their plans. The more that ISSB and other jurisdictions can align their efforts the better the chance for the ISSB work to be the global baseline and thus limit additional requirements and fragmentation.

We appreciate the rapid progress the ISSB has made on this project. We understand that—given the urgency of the global climate agenda—the ISSB has not fully followed the usual due process the International Accounting Standards Board (IASB) usually applies. For that reason, we urge the ISSB to keep involving the various stakeholders—particularly other regulators and industry groups—even more closely than usual to drive convergence and ensure that the final standards can be applied and implemented in a timely and consistent manner. In that regard, we would welcome a phased/staggered implementation approach to ensure adequate time for preparers to provide the most accurate and relevant information possible.

Once again, we are grateful for the opportunity to provide feedback throughout the process of the establishment of the ISSB and the publications of its IFRS Sustainability Disclosure Standards. Close ongoing dialogue between policymakers and the global financial services industry will be important to ensure that an aligned framework is reflected in regulatory and policy instruments, supervisory expectations, and by firms' internal risk management processes. The IIF looks forward to continuing to play a role in facilitating engagement between regulators, standard setters, existing frameworks, and the financial industry to achieve this objective.

We hope that you will find our comments useful and constructive. If you have any questions, please feel free to contact the undersigned at sgibbs@iif.com or aportilla@iif.com.

Yours sincerely,

Sonja Gibbs
Managing Director and
Head of Sustainable Finance
Institute of International Finance (IIF)

Andrés Portilla
Managing Director and
Head of Regulatory Affairs
Institute of International Finance (IIF)

ANNEX: Detailed responses to questions in the Exposure Drafts

<u>ED IFRS S1: Question 4—Core content</u>

(a) Are the disclosure objectives for governance, strategy, risk management and metrics and targets clear and appropriately defined? Why or why not?

The 'core content' provision (paragraph 11-35) in ED IFRS S1 is based on the TCFD framework that was developed specifically for climate risk disclosure. A number of IIF members believe this framework may not be well-suited for the breadth of topics that ISSB may cover in future standard-setting efforts. While issuers and investors have significant experience with implementing the TCFD framework in the context of climate risk disclosure, there has been very limited experience in applying the foundations of the TCFD framework for other sustainability-related disclosures—a source of concern for some members given the heterogeneity of sustainability-related risks.

IIF members believe there are inconsistencies on objectives within the ED, for example, inconsistent incorporation of 'sustainability-related opportunities'. For example, paragraph 25 states the risk management objective is to show how "sustainability-related risks and opportunities are identified, assessed and managed." Paragraph 26 also refers to both risks and opportunities. However, paragraph 11(c) states an entity shall provide disclosures on "the processes the entity used to identify, assess and manage sustainability-related risks." It is unclear why paragraph 11(c) excludes opportunities. Further, it is unclear what is envisioned by including 'opportunities' as part of the section on risk management.

<u>ED IFRS S1: Question 5—Reporting entity</u>

(a) Do you agree that the sustainability-related financial information should be required to be provided for the same reporting entity as the related financial statements? If not, why?

IIF members believe the scope of a reporting entity should be aligned with general purpose financial reporting. While the ISSB proposal states that, in general, a reporting entity's boundary for its sustainability-related financial disclosures is the same as for its financial statements, Draft IFRS S2 is proposing additional climate-related disclosures for a broader set of entities. For instance, a consolidated group would be required to disclose GHG emissions by associates and joint ventures separately from those by the consolidated group. Access to data remains a key barrier and challenge, in particular for financial institutions that are key consumers of such information. It would be challenging for financial institutions to report for entities and investments that are not under the direct control of the consolidated group, and it would be important to have some latitude in determining organizational boundaries as long as the approach is clearly disclosed—in line with the approach permitted by the GHG Protocol.

The ISSB previously explained that the reason for separate Scope 1 & 2 GHG emissions for associates/joint ventures/unconsolidated subsidiaries is to allow investors to perform their own adjustment from the reported consolidated results among different entities due to the flexibility provided by the GHG Protocol based on an entity's controls. IIF members do not believe such disclosure will add value to the decision-usefulness for general users for the following reasons:

- Different entities have different levels of business integrations. One entity may deliver its value chain through third party supplier and another through an association. In such cases, this separate disclosure will not improve comparability. This may lead to unintended consequences and discourage a certain efficient business structure.
- Performing such adjustment can mislead the investors into believing that the entity has the ability to control its Scope 1 and 2 GHG emissions from the associates/joint ventures/unconsolidated subsidiaries. It will also distract the organizations from focusing their resources in their own controllable decarbonization pathways.
- This requirement goes beyond the current IFRS accounting disclosure requirements. The separate disclosures do not improve the connectivity between the financial results and the climate-related performance but can instead mislead if the financials of the associations/joint ventures/unconsolidated subsidiaries are not part of the consolidated financial results.

ED IFRS S1: Question 7—Fair presentation

(a) Is the proposal to present fairly the sustainability-related risks and opportunities to which the entity is exposed, including the aggregation of information, clear? Why or why not?

IIF members are concerned that the proposed language on 'fair presentation' of risk and opportunities that are not covered by IFRS Sustainability Disclosure Standards could potentially create liability risks for preparers. It is important to have more specific language on what the ISSB expects preparers to disclose in this regard, in terms of the scope of risks and opportunities considered.

ED IFRS S1: Question 7—Fair presentation

(b) Do you agree with the sources of guidance to identify sustainability-related risks and opportunities and related disclosures? If not, what sources should the entity be required to consider and why? Please explain how any alternative sources are consistent with the proposed objective of disclosing sustainability-related financial information in the Exposure Draft.

IIF members think it would be more reasonable to 'encourage' rather than 'require' looking to "most recent pronouncements of other standard-setting bodies whose requirements are designed to meet the needs of users of general-purpose financial reporting." Either way, with all these sources of guidance to identify sustainability-related risks and opportunities, the scope of disclosure could be very wide and subject to different interpretation resulting in non-comparable information between disclosing entities. Also, issues may arise as regards to audit/enforceability and necessary safeguards.

ED IFRS S1: Question 8—Materiality

(a) Is the definition and application of materiality clear in the context of sustainability-related financial information? Why or why not?

While this question is only raised in ED IFRS S1, IIF members see practical challenges of applying the materiality definition set forth in both EDs. IIF members believe that additional clarity is needed to emphasize that the S2 disclosure provisions are predicated on materiality. Focusing on non-material components of sustainability-related and climate-related information could distract from more important, bigger picture objectives and messages in disclosures. The definition of materiality should more clearly reflect the focus of the ISSB on disclosure that is decision-useful to a user of general purpose financial reporting. We recommend clarifying that the ISSB defines 'materiality' to mean information that a user of general purpose financial reporting would consider important in making an investment decision. It is unclear to what extent the materiality standard proposed in IFRS S1 departs or aligns with traditional financial materiality, where information is disclosed if it is useful for an investor in making an investment.

The ISSB's definition of materiality as the impact on enterprise value in the short, medium, and long term implies materiality determinations must be made considering a company's long-term value. This differs from the current materiality determination for financial reporting. Further guidance should be included to ensure a uniform understanding of the materiality concept.

Some members expressed concern that assessing materiality over different time frames—particularly a long time horizon—could call for speculative judgement that might not prove helpful to investors. Generally, IIF members think that concrete examples of the link between the ISSB's materiality definition with different concepts of materiality—such as financial materiality and double materiality—would help to better illustrate the interaction.

Also, the disclosure requirements are not clear for subsidiaries, particularly small subsidiaries in different sectors (e.g., a bank with an insurance or asset management subsidiary as prescribed in Appendix B). Disaggregation (e.g. by GHG or by segment/region, etc.) should follow a principles-based approach and only be required where such splits would be material in the entity-specific context.

The ISSB should clarify that materiality should be determined at the consolidated firm-level rather than the subsidiary-level. As ISSB standards are industry-based, diversified companies may have certain risks that might be considered material to specific subsidiaries, but would not be considered material to the consolidated organization, resulting in disclosure of information that is not decision-useful to investors.

Also, the Exposure Drafts use the term ‘significant’ risks and opportunities, which is inconsistent with the concept of ‘material’ risks and opportunities and will create confusion for both companies and investors. It is unclear if registrants need to disclose all effects a significant climate-related risk or opportunity might have on a business model, or only effects on the business model that are significant. Clarification and proper delineation of the two qualifiers (‘significant’ versus ‘material’) is needed since ‘materiality’ is used in financial reporting. The same is true for the use of the word ‘salient’. Similarly, further explanation of the word ‘vulnerable’ (in ED IFRS S2, paragraph 21) would be helpful.

We recommend that the ISSB consider adding materiality qualifiers throughout the standard to clarify that each recommended disclosure is predicated on the information being material to the disclosing company and its investors; this will resolve issues with the use of the term ‘significant’ throughout the standard, which inadvertently confuses the concept of materiality. In practice, this would mean that the standard includes materiality qualifiers in each individual disclosure item.

Finally, the proposed standards adapt the definition of materiality from IAS 1. Some members believe that this may make it difficult for the proposed standard to serve as an effective global baseline. Some companies do not report using International Financial Reporting Standards (IFRS), and even those that do, depending on how the inclusion of enterprise value in the proposed standard is interpreted, use a different standard of materiality for sustainability and climate reporting than they do for financial reporting and other disclosures. In practice, the ISSB proposal is creating a separate materiality standard for reporting on climate and sustainability than for other financial reporting and disclosure in jurisdictions where companies do not report using IFRS.

ED IFRS S1: Question 9—Frequency of reporting

Do you agree with the proposal that the sustainability-related financial disclosures would be required to be provided at the same time as the financial statements to which they relate? Why or why not?

We support the ISSB proposal for a company to disclose sustainability-related financial information as part of its general purpose financial reporting to ensure that financial statement information and sustainability-related financial disclosures can be considered together, highlighting interrelationships and connections between different types of risks and opportunities. As a consequence, the sustainability-related financial disclosures would be required to be published at the same time as the financial statements which would be beneficial to investors and there would be no risk of not disclosing material non-public information at the same time of financial statements.

However, IIF members perceive that there may be challenges for the feasibility of publishing sustainability-related and climate-related financial information at the same time as financial statements. Due to the complexity of delivering such analysis, it often takes longer for financial institutions to produce non-financial disclosures compared to disclosures of purely financial information. For instance, banks need to close the balance sheet position as a starting point for calculating financed emissions. The calculation of financed emissions is based on outstanding balances at year-end, and therefore requires finalized year-end financial data. Thus, it is challenging for such information to be published contemporaneously, considering the dependencies among data sources.

To address this challenge, some IIF members have suggested a staggered approach to sustainability reporting through the introduction of a reporting lag for financial institutions—which rely on third-party data—for sustainability-related and climate-related data sources from the fiscal reporting year of the reporting entity. In effect this would mean the disclosure would be done at the same time as the financial statements while the data sources used as a basis for the sustainability-related disclosure would be from previous reporting periods. Preparers should use the most recent data available to them that is both reliable and usable. Such a staggered approach to reporting of sustainability information (offset from fiscal reporting year timelines in a consistent manner) is already being taken by some jurisdictions. Preparers should have flexibility whether to align with the financial reporting cycle or to choose such a staggered approach.

ED IFRS S1: Question 11—Comparative information, sources of estimation and outcome uncertainty, and errors

a) Have these general features been adapted appropriately into the proposals? If not, what should be changed?

We support the proposal that a company would not have to provide comparative information the first time it applies the standards. However, we seek clarification on the requirement as proposed for the restatement of comparatives. For example, paragraph 84 of Draft IFRS S1 contains a requirement for entities to correct material prior period errors by restating the comparative amounts for the prior period(s) disclosed unless it is impracticable to do so, while paragraph 64 of the same draft advises that when providing sustainability-related financial disclosures the entity has to disclose comparative information that reflects updated estimates. While paragraph 84 refers to materiality, paragraph 64 refers only to updating estimates with no reference to a materiality assessment.

ED IFRS S1: Question 13—Effective date / ED IFRS S2: Question 14-Effective date

(a/b) When the ISSB sets the effective date, how long does this need to be after a final Standard is issued? Please explain the reason for your answer, including specific information about the preparation that will be required by entities applying the proposals, those using the sustainability-related financial disclosures and others.

IIF members support a phased/staggered implementation approach to ensure adequate time for preparers to provide the most accurate and relevant information possible. We recommend publishing the standards at the same time, but allow for at least two years implementation period. For jurisdictions, which are already more advanced in the disclosure of such information, there should be an early adoption option.

ED IFRS S1: Question 14—Global baseline / ED IFRS S2: Question 16—Global baseline

Are there any particular aspects of the proposals in the Exposure Draft that you believe would limit the ability of IFRS Sustainability Disclosure Standards to be used in this manner? If so, what aspects and why? What would you suggest instead and why?

We appreciate the focus of the ISSB's proposed disclosure requirements on 'enterprise value'—defined as 'the total value of an entity.' We also appreciate the ISSB's interpretation of that term as including "*information about a company's impacts and dependencies on people, the planet and the economy when relevant to the assessment of the company's enterprise value*" and hence being "*broader than information reported in the financial statements.*"

We understand that the ISSB is intending to provide a definition designed to facilitate alignment with a baseline standard by a variety of jurisdictions and markets. We further understand that the ISSB's proposed definition of 'enterprise value' would be positioned between the classical terms of 'financial materiality' and 'double materiality.' However, IIF members are concerned that this proposed definition might lead to myriad interpretations in different jurisdictions and markets and could be reflected differently in existing policy frameworks and requirements, leading to comparability issues.

If the proposed standards are meant to act as a global baseline, preparers will need a clearer definition of 'enterprise value' and its underlying concepts such as materiality and the value chain scope. Preparers would also benefit from having illustrative examples setting out methodologies and calculations for enterprise value.

ED IFRS S2: Question 1—Objective of the Exposure Draft

(a) Do you agree with the objective that has been established for the Exposure Draft? Why or why not?

Paragraph 1 of Draft IFRS 2 sets out the proposed objective of the standard according to which an entity is required to disclose information about its exposure to climate-related risks and opportunities. However, financial institutions have not yet gained as much experience with the disclosure of climate-related opportunities as they have with climate-related risks which has implications for the level of preparedness and capabilities.

Certain jurisdictions focus solely on the disclosure of climate-related risks or make the disclosure of climate-related opportunities optional at this stage—such as the U.S. Securities and Exchange Commission (SEC) in their proposed rule on *"The Enhancement and Standardization of Climate-Related Disclosures for Investors."* IIF members believe that more flexibility will be needed for the disclosure of climate-related opportunities in order not to negatively impact the organization's success with executing such related strategies, which should be considered by the ISSB when preparing further guidance as regards opportunities.

The proposal includes several components of the 2021 TCFD recommendations that were developed without broad-based input from issuers and investors and have not yet been market-tested in the same way as the 2017 TCFD recommendations.

Specifically, some IIF members have concerns about the following ISSB disclosure provisions that are based on the 2021 TCFD updated recommendations:

- Disclosure of financial impacts, and potential financial impacts tied to climate-related risks and opportunities
- Capital deployment
- Internal carbon pricing
- Executive remuneration
- Transition plans

For that reason, some IIF members recommend that the disclosure requirements outlined above should be considered voluntary, or 'recommended', until market participants have had the opportunity to implement and use the recommendations outlined in the new guidance, and the ISSB has had the opportunity to assess to what extent they are feasible for issuers to disclose.

ED IFRS S2: Question 3—Identification of climate-related risks and opportunities

(a) Are the proposed requirements to identify and to disclose a description of significant climate-related risks and opportunities sufficiently clear? Why or why not?

ED IFRS S2 requires entities to disclose "*how significant climate-related risks and opportunities have affected its most recently reported financial position, financial performance and cash flow*" (paragraph 14a). The proposal assumes that companies would be able to tie identified potentially material climate-related risks in Risk Management disclosures to the financial statements.

Some members highlighted the challenges of disaggregating climate risk from other risk drivers in historical reporting. Moreover, it might be difficult to ensure a consistent and comparable approach to the disclosure of information such as those related to weather events (e.g., heat waves, forest fires), where preparers might take different approaches (one company might attribute losses from every single heat wave and forest fire while another one might see this as part of a seasonal fluctuation). Some members think it would therefore be helpful if the ISSB could clarify how climate-related risk events—and more generally, how significant risks and opportunities—are defined to ensure consistent treatment across companies. Given a lack of clarity on the definition and scope of climate-related risk events, disclosures are likely to lack consistency. That is, one preparer may interpret flooding as a climate-related event, while another preparer may interpret it as a natural weather pattern unrelated to climate risk. Given the lack of standardization in definitions, constantly evolving climate science, and data gaps, some members believe the ISSB should provide more concrete guidance.

It is also unclear how companies would analyze expenditures or market valuation movements which might only be partially driven by climate-related risks and/or opportunities. For instance, a property enhancement may include both climate resiliency infrastructure installation and other non-climate-related functionality upgrades; a deterioration of a financial asset in the carbon sector may include both climate-related credit drivers and other credit drivers. Additional work from the ISSB is needed on how to isolate/segregate climate-related risks and opportunities from other types of risks and opportunities and how to measure and disclose these financial impacts before mandating quantitative disclosure requirements that outrun current technical capabilities.

Given the significant technical challenges and broad-based work needed to develop a better understanding of how climate risk translates into financial impacts, we strongly urge the ISSB to explore ties to the financial statements as a second phase of standard-setting where the technical challenges in this area can be given appropriate attention. IIF members thus appreciate that companies would be able to disclose current and anticipated effects on the financial statements qualitatively where they are unable to provide quantitative information.

Required disclosure of 'opportunities' is unusual within the context of financial reporting. Climate-related opportunities is not an area of disclosure that has generated significant investor interest. Some IIF members urge the ISSB to make disclosure of financial impacts of climate-related opportunities to be voluntary or 'recommended' to allow time for the ISSB to assess whether this information truly is material to investors.

<u>ED IFRS S2: Question 5–</u> <u>Transition plans and carbon offsets</u>

(c) Do you think the proposed carbon offset disclosures will enable users of general purpose financial reporting to understand an entity's approach to reducing emissions, the role played by carbon offsets and the credibility of those carbon offsets? Why or why not? If not, what do you recommend and why?

IIF members would encourage that the EDs set out clearer expectations and guidance on how firms should disclose how carbon offsets may be considered within Scope 1, 2, and 3 carbon emissions accounting; e.g., whether preparers would be expected to disclose net GHG emissions (reflecting carbon offsets) or total GHG emissions with carbon offsets being separately disclosed.

Some IIF members suggested that the ISSB should make clearer that Scope 1, 2, and 3 carbon emissions related metrics and targets should be disclosed with and without using carbon offsets, avoided emissions and carbon removals. The ISSB could include guidelines and principles in the final Standards on the use of offsets. For example, a reference to the Core Carbon Principles (CCPs) and Assessment Framework (AF) by the Integrity Council for the Voluntary Carbon Market could serve as a helpful basis once they are issued.

Transition plans could be reported outside of financial reporting to allow for the sufficient time lag that is needed between reporting by non-financial corporates and financial services firms. It is also important to emphasize that transition plan disclosure must be designed to produce decision-useful information for users. This will include information that can be easily translated into the actual reporting of impact on emissions from actions taken.

<u>ED IFRS S2: Question 6–Current and anticipated effects</u>

(a) Do you agree with the proposal that entities shall disclose quantitative information on the current and anticipated effects of climate-related risks and opportunities unless they are unable to do so, in which case qualitative information shall be provided (see paragraph 14)? Why or why not?

Access to data and data quality remain key barriers to the reliability and comparability of disclosures. We also note that the TCFD's 2021 status report found challenges associated with disclosure of anticipated financial effects of climate-related risks and opportunities. Given these limitations—such as the lack of standardized scenarios and methodologies, the lack of maturity of internal capabilities and data limitations, some IIF members suggest that ISSB include these disclosures as 'recommended' until market participants have had more experience implementing these disclosures and the ISSB is able to assess the extent to which investors find them decision-useful. If ISSB determines to include these disclosures as mandatory, IIF members welcome that qualitative disclosures can be provided and quantitative disclosures can be added over time with increased standardization and data availability.

We encourage the ISSB to consider the current challenges associated with consistent, high quality data and in particular the extreme difficulty for financial institutions to calculate Scope 3 emissions with a high degree of confidence given the reliance on corporate and counterparty data. We particularly encourage the ISSB to consider these challenges for certain sectors and asset classes for Scope 3 financed emissions and we recommend the introduction of a materiality-based approach for such disclosure. Asset class and value chain emissions that are material or influence an institution's long-term Net Zero strategy should be prioritized for disclosure. Institutions should justify their approach and retain the flexibility to determine the prioritization.

Also, IIF members asked for more guidance on when a preparer is being considered as being "unable to do so" since the phrase can be subject to different interpretations. Further guidance and examples of situations is needed where qualitative information should be provided if specific quantitative elements are unavailable to adequately disclose information on the current and anticipated effects, especially regarding social and governance (and nature-related) elements. The ISSB should further elaborate on the respective disclosure requirements and clarify what it would expect from companies to foster quantitative disclosures as much as possible in the future. Some IIF members suggested that the ISSB works with the IASB to develop appropriate accounting standards and guidance on measurement and disclosure methodologies related to climate. Also, preparers should have the possibility to use estimates and proxies as long as they are able to justify them.

ED IFRS S2: Question 6—Current and anticipated effects

(b) Do you agree with the proposed disclosure requirements for the financial effects of climate-related risks and opportunities on an entity's financial performance, financial position and cash flows for the reporting period? If not, what would you suggest and why?

Members consider that climate-related opportunities would have a positive impact on an entity's financial indicators and are therefore less important to disclose than climate-related risks, which have a negative impact on indicators and are thus critical to disclose to investors. Further, anti-competitive concerns might arise from a requirement to disclose a particular business opportunity (as, for instance, noted by the U.S. SEC in its climate-related disclosures proposal).

Members therefore propose that disclosure of climate-related opportunities be optional (or at least have a degree of flexibility). By defining 'climate-related opportunities', the proposal would promote consistency when such opportunities are disclosed, even if such disclosure is not required. In this regard, additional guidance on what constitutes a climate-related opportunity would be beneficial.

ED IFRS S2: Question 6—Current and anticipated effects

(c) Do you agree with the proposed disclosure requirements for the anticipated effects of climate-related risks and opportunities on an entity's financial position and financial performance over the short, medium and long term? If not, what would you suggest and why?

Members would like to preserve the prior period and backward-looking focus of financial statements and encourage the ISSB to clarify for those that adopt IFRS S2 that forward-looking disclosures should not be expected to be included in financial statements, but rather within the broader body of general purpose financial reporting.

ED IFRS S2: Question 7—Climate resilience

(a) Do you agree that the items listed in paragraph 15(a) reflect what users need to understand about the climate resilience of an entity's strategy? Why or why not? If not, what do you suggest instead and why?

Considering the evolving climate science and climate scenarios, and given certain limitations—such as the lack of standardized scenarios and methodologies, the lack of maturity of internal capabilities and data limitations—some IIF members suggest that quantitative disclosures should be used whenever possible. Qualitative disclosures could be used in the absence of quantitative ones.

ED IFRS S2: Question 9—Cross-industry metric categories and greenhouse gas emissions

(c) Do you agree that entities should be required to use the GHG Protocol to define and measure Scope 1, Scope 2 and Scope 3 emissions? Why or why not? Should other methodologies be allowed? Why or why not?

The GHG Protocol is the most common methodology used which would make it easier to compare disclosures and require no change in current data collection.

ED IFRS S2: Question 9—Cross-industry metric categories and greenhouse gas emissions

(d) Do you agree with the proposals that an entity be required to provide an aggregation of all seven greenhouse gases for Scope 1, Scope 2, and Scope 3— expressed in CO2 equivalent; or should the disclosures on Scope 1, Scope 2 and Scope 3 emissions be disaggregated by constituent greenhouse gas (for example, disclosing methane (CH4) separately from nitrous oxide (NO2))?

IIF members consider CO2 equivalents to be the most practical way to disclose GHG emissions and agree that aggregate emissions should be disclosed. The general disclosure of disaggregated emissions will pose an unnecessary compliance burden, but could be considered where feasible for certain sectors (e.g. oil and gas).

ED IFRS S2: Question 9—Cross-industry metric categories and greenhouse gas emissions

(e) Do you agree that entities should be required to separately disclose Scope 1 and Scope 2 emissions for:

(i) the consolidated entity; and

(ii) for any associates, joint ventures, unconsolidated subsidiaries and affiliates? Why or why not?

The inclusion of unconsolidated subsidiaries in Scope 1 and Scope 2 disclosures could lead to double counting with corporates who have the same subsidiary consolidated, cause data availability issues and require the use of different methodologies. IIF members think the disclosure requirements should be limited to consolidated subsidiaries, which would also be aligned with financial reporting.

ED IFRS S2: Question 9—Cross-industry metric categories and greenhouse gas emissions

(f) Do you agree with the proposed inclusion of absolute gross Scope 3 emissions as a cross-industry metric category for disclosure by all entities, subject to materiality? If not, what would you suggest and why?

Additional guidance and illustrative examples would be helpful to support the proposed inclusion of absolute gross Scope 3 emissions as a cross-industry metric category for disclosure by all entities, subject to materiality.

ED IFRS S2: Question 11—Industry-based requirements

(a) Do you agree with the approach taken to revising the SASB Standards to improve the international applicability, including that it will enable entities to apply the requirements regardless of jurisdiction without reducing the clarity of the guidance or substantively altering its meaning? If not, what alternative approach would you suggest and why?

(b) Do you agree with the proposed amendments that are intended to improve the international applicability of a subset of industry disclosure requirements? If not, why not?

(c) Do you agree that the proposed amendments will enable an entity that has used the relevant SASB Standards in prior periods to continue to provide information consistent with the equivalent disclosures in prior periods? If not, why not?

IIF members generally support the ISSB's proposal to leverage the industry-based standards by SASB as the most well-established industry-based investor-focused reporting initiative. However, we highly welcome that addressing international applicability of the SASB Standards is mentioned as a priority and will form part of the ISSB's initial work plan as the SASB Standards have a U.S. focus. This is particularly true for the financial sector.

In adjusting the SASB standards for global applicability, we recommend that the ISSB consider providing more flexibilities in its adoption. For example, mandating the use of Global Industry Classification Systems (GICS) to identify high carbon industry can be costly for entities that use their own local classification systems. The ISSB should permit compatible classification systems that are used in other jurisdictions.

ED IFRS S2: Question 11—Industry-based requirements

(d) Do you agree with the proposed industry-based disclosure requirements for financed and facilitated emissions, or would the cross-industry requirement to disclose Scope 3 emissions (which includes Category 15: Investments) facilitate adequate disclosure? Why or why not?

A number of IIF members believe alignment with the PCAF methodology could ensure clarity in the classification and treatment of the financial products in scope, though not all support the PCAF methodology. While methodologies for calculating Scope 3 financed or facilitated emissions continue to advance, there are many areas where development is still ongoing. We provide below several examples of areas that illustrate the need for a highly considered approach to incorporation of Scope 3 financed or facilitated emissions disclosure in S2:

- IIF members question the requirement 'Scope 3 Financed Emissions Product Scope—Derivative' which is not yet defined standards such as PCAF. Derivatives are usually executed along with a loan facility to a client. Including both products can lead to double counting. There can also be unintended consequences for different types of derivatives. For example, an interest rate swap allowing netting may produce a much smaller cash flow compared to a cross-currency swap that cannot be netted due to notional exchange in two different currencies. More generally, accounting for products where there is no methodology to date will be challenging.

- Currently, ED IFRS S2 requires all Scope 3 financed emissions to be calculated for all sectors. The ISSB defines mortgages to include Home Equity Line of Credit (HELOC), but, for example, the PCAF standard excludes HELOC from its methodology. Appendix B-19 for Mortgage Finance does not mention financed emissions disclosure. Some IIF members encourage alignment between ED IFRS S2 and the PCAF methodology.
- ED IFRS S2 currently does not have explicit language about how trading book assets are to be treated. Under PCAF for example, most of the trading book loans and investments are currently considered out-of-scope for financed emission calculations. There also have not been any standards or methodologies defined for securities financing transactions (i.e., Reverse repo) and margin loans (investor brokerage or prime brokerage) assets on balance sheets.
- There are also open questions regarding the right treatment of specialty funded securitization assets. If both the assets (Mortgage Loans) and the liabilities (Securitization Liabilities) are on the bank's balance sheet, this implies that the bank does not directly fund the asset. It would be helpful to have some general are seeking clarification as to whether this securitization asset should be included in the bank's financed emissions calculation. Moreover, if a bank issues the securitization of its own loan, would the requirement to disclose both financed (the mortgage part) and facilitated (the securitization part) emissions lead to double counting of Scope 3 emissions?
- It is difficult to calculate financed emissions for an undrawn loan considering that there Is little available guidance and there would be risk of double counting by different lenders.

Some IIF members also suggest amending the industry title and industry description of Asset Management and Custody Activities (Appendix B, Volume B15) to remove all reference to 'custody activities' or 'custody services', and to remove the metric 'Assets under Custody' from the disclosable activity metric in Appendix B, Volume B15 (Asset Management and Custody Activities). Custody services should not be grouped together with asset management activities because custody services and asset management activities represent very different businesses. Requirements adopted for asset management activities are unlikely to be appropriate for custody services, in particular in light of the very limited discretion persons providing custody services exercise over the assets they hold as custodian for investors.

ED IFRS S2: Question 11—Industry-based requirements

(e) Do you agree with the industries classified as 'carbon-related' in the proposals for commercial banks and insurance entities? Why or why not? Are there other industries you would include in this classification? If so, why?

Most IIF members from the banking and asset management sector generally agree with the industries covered. However, since different jurisdictions may have different sector definitions, we would appreciate more detailed guidance on the sectors (e.g., homebuilding vs. real estate management and development) as well as on possible sectoral granularity for climate-related disclosures.

IIF members from the insurance sector think the list with industries classified as 'carbon-related' in the proposals for insurance entities (paragraph 1.4.1) is not sufficiently discriminatory. For example, it lists utilities which could be all-renewable. Instead, we strongly recommend for the ISSB to define sectors with ISIC/NACE and clarify the framing to 'usually carbon-related' as almost any industry is related to GHG.

Also, insurers raised challenges with the proposed metrics for the Underwriting in the Insurance specific Appendix (Volume B17):

- Not one size fits all: The proposal does not reflect the different nature of (some types) re/insurance business, in terms of transparency on the underlying business or data availability. Certain information might not be relevant for the entire insurance sector, e.g. the section on 'Policies Designed to Incentivize Responsible Behavior', seems to be more relevant for direct insurers but less so for reinsurers.
- Confidential and business sensitive information: Drafts in the current form ask for information that might be commercially sensitive and/or is propriety—such as information on opportunities, transition plans or scenario analysis.
- Level of detail: Too prescriptive definition of applicable metrics will limit firms to choose the metrics/design scenarios adapted to their business model to generate meaningful information for investors. There is more flexibility needed, considering that some metrics are still being developed (as also acknowledged by TCFD) and also disclosure of the requested information is not always feasible. For example, the net premiums (premiums after reinsurance) are not always available on a policy level which is needed for FN-IN-410b.1.

More generally, alignment with other standard/framework setters would be important. For instance, the current ISSB list of carbon-related sectors is not fully aligned with the October 2021 TCFD or the NZBA classifications (e.g., TCFD specifies agriculture and capital goods as carbon-related sectors, but they were not listed in the commercial banks list).

ED IFRS S2: Question 11—Industry-based requirements

(f) Do you agree with the proposed requirement to disclose both absolute- and intensity-based financed emissions? Why or why not?

IIF members agree but some members ask that any Scope 3 disclosure requirements should be subject to a materiality qualifier.

ED IFRS S2: Question 11–Industry-based requirements

(g) Do you agree with the proposals to require disclosure of the methodology used to calculate financed emissions? If not, what would you suggest and why?

IIF members agree with this proposal as it would aid transparency.

ED IFRS S2: Question 11–Industry-based requirements

(j) Do you agree with the proposed industry-based requirements? Why or why not? If not, what do you suggest and why?

Some of the new metrics related to 'transition risk exposure' could lead to misunderstandings and possible errors in reporting. The categorization of 'transition risk exposure' in the industry-based requirements is not the most accurate description, because financed emissions are not necessarily reflective of transition risk.

Some members believe that the level of prescription in ED IFRS S2 is not proportionate to the level of maturity of this disclosure and risks creating confusion for both financial institutions preparing disclosure and investors consuming the disclosure. For example, for indicators like FN-CB-3 which relate to financed emissions, we would appreciate the focus to be on the balance sheet first and allow corporates to disclose the relevant financed emissions first, which is more mature. For instance, the FN-IN-3 states: "For each industry by asset class: (1) absolute gross (a) Scope 1 emissions, (b) Scope 2 emissions, and (c) Scope 3 emissions, and (2) gross exposure (i.e., financed emissions)." From this sentence, it seems that the gross exposure is the financed emissions, but in the explanation of the disclosure requirements the ISSB states: "The entity shall disclose its absolute gross financed emissions, disaggregated by Scope 1, Scope 2, and Scope 3 emissions for each industry by asset class." The link between the absolute gross by GHG emissions Scope 1, 2, and 3 and the financed emission is not clear from the name of the metrics itself. We recommend providing banks with flexibility to provide this disclosure in a manner that allows them to provide more meaningful information to investors. For example, banks that use the PCAF methodology may wish to disclose the data quality score for financed emissions.

ED IFRS S2: Question 14–Effective date

(a) Do you think that the effective date of the Exposure Draft should be earlier, later or the same as that of [draft] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information? Why?

As mentioned in the IIF response letter to the IFRS Foundation's Consultation Paper on Sustainability Reporting, the IIF supports the ISSB's overall goal of proposing a global baseline standard not only for climate-related disclosures but also for broader sustainability-related information. This will ensure alignment with evolving market and supervisory practices going forward. However, it is important to recognize that climate-related disclosures, even though data challenges remain, have seen increased stakeholder interest and have developed faster than broader ESG disclosures where a similar level of progress has not yet occurred. For instance, the work of the Taskforce on Nature-related Financial Disclosures (TNFD) might be crucial to have a common understanding of nature-related information. However, the TNFD is not expected to publish its final recommendations before September 2023. We therefore support the ISSB's decision to start with a climate-related specific standard (IFRS S2).

We understand Draft IFRS S1 to work as the overarching disclosure standard for sustainability-related information which topic-specific standards (such as Draft IFRS S2 for climate-related disclosures) will build upon and to which they will add more detail. If this is the intention, the IIF thinks it makes sense to publish IFRS S1 at the same time as IFRS S2 in order to establish a baseline standard. However, we see a risk of fragmentation of the global sustainability disclosure landscape unless the term 'sustainability' used in Draft IFRS S1 is more clearly scoped.

We acknowledge that many jurisdictions will not mandate the disclosure of non-climate-related information in the foreseeable future and might not decide to adopt IFRS S1. At the same time, certain jurisdictions are already pushing ahead on their own, therefore adding to further fragmentation. Developing a global baseline standard—even if not immediately adopted by all jurisdictions—would limit the fragmentation risk. In any case, some IIF members recommend that the ISSB implement an early adoption option.

We would recommend the ISSB provide further clarifications on the applicability of IFRS Standards mentioned in the EDs that are not yet effective (i.e., IFRS 17 is not yet fully effective for insurance businesses in some jurisdictions).

ED IFRS S2: Question 17—Other comments

Do you have any other comments on the proposals set out in the Exposure Draft?

Preparers would benefit from having illustrative examples setting out potential methodologies and calculations, e.g., enterprise value and the calculation of financed emissions where the allocation of the emissions data is required at the subsidiary level; however, data may only be available at the consolidated level of a counterparty and not at the legal entity level.