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RESPONSE TO THE EXPOSURE DRAFT (ED) ON IFRS S2 *CLIMATE-RELATED DISCLOSURES*

The Institute of Singapore Chartered Accountants (ISCA) appreciates the opportunity to comment on the ED above published by the International Sustainability Standards Board (ISSB) in March 2022.

To solicit meaningful feedback from key stakeholders on the ED, ISCA undertook the following initiatives:

- Conducted a one-month public consultation to seek feedback from its members;

- Solicited feedback on the ED from the ISCA Sustainability and Climate Change Committee and its Sustainability Reporting Quality Sub-Committee, which comprise experienced individuals with subject matter knowledge in sustainability-related matters, including practitioners from accounting firms, C-suite executives from large corporations and regulators; and

- Organised two focus group sessions to engage preparers of sustainability reports and assurance practitioners to obtain their views on the ED.

On the whole, ISCA supports the ISSB's aim for the IFRS Sustainability Disclosure Standards (the Standards) to serve as a comprehensive global baseline of sustainability disclosures. As highlighted in our earlier comment letter in response to the IFRS Foundation Trustees' Consultation Paper on Sustainability Reporting, there is an urgent need for consistency and comparability in sustainability reporting.

The ISSB's decision to focus on climate-related disclosures is apt given the exigencies arising from climate change. This is consistent with ISCA's priorities as we issued in April 2022 the ISCA Climate Disclosure Guide – Taking First Steps Towards Climate-related Disclosures, a guide which aims to help companies, including Singapore-listed companies that have to meet the Singapore Exchange's requirements for climate reporting, adopt the recommendations by the Task Force on Climate-Related Financial Disclosures (TCFD Recommendations).

We recognise that setting a comprehensive global baseline is not an easy task given the varying levels of maturity amongst preparers and users of such information as well as the need to **avoid the perception of the Standards being 'yet another standard'** which could then lead to further fragmentation in the market.

Hence, we commend the ISSB for its efforts and the speed at which actions are being taken. The ISSB's diligence in carrying out numerous outreach activities to raise awareness of the EDs, including in the ASEAN region, is much appreciated as well.

We agree that there is an urgent need globally for high-quality and reliable reporting of environmental, social and governance (ESG) matters. We also firmly believe that all entities, regardless of size, should eventually adhere to a common set of sustainability reporting requirements. Having said that, we recognise that time and patience are needed given the challenges in achieving this common objective, which we detail further below. We hope that standard-setters and regulators globally can work together and commit to an acceptable timeline for adoption of the Standards.

We have submitted a separate letter in response to ED IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information*. In that letter, we shared several overall comments and suggestions which are applicable to both ED IFRS S1 and ED IFRS S2, which we have reproduced here for easy reference.

1. Balancing aspiration and reality

We appreciate and understand the rationale behind the current design of the EDs, which aspires to provide comprehensive baseline information useful for the assessment of enterprise value and capital allocation decisions. In attempting to achieve that objective, the EDs appear to be all-encompassing (for example, the need to disclose material information about all significant sustainability-related risks or opportunities). We believe that **due consideration needs to be given to the current state of sustainability reporting as well as the readiness of preparers**.

Although sustainability reporting has gained significant traction globally in recent years and maturity of preparers are improving, issues such as 'cherrypicking' (e.g. preparers only reporting on those areas which they are ready), lack of reliable data and inadequate talent pool are still commonplace. Coupled with the complexities of sustainability reporting requirements and limited resources available, these have led to relatively low levels of reporting by small-and-medium enterprises (SMEs).

It is difficult to expect the landscape to immediately progress from the current state to one where many preparers could fully comply with the Standards. Based on the current form of the EDs, even large corporates may find it challenging to comply with the Standards' requirements. Through our outreach, we hear views that the requirements in the EDs are being **set too high as a baseline**, for example the requirements to disclose information about the effects of significant sustainability risks and opportunities on its value chain, particularly considering the gap in today's practices.

In addition, given the need to rely on information from third parties, such as along the value chain as required by ED IFRS S1 and Scope 3 greenhouse gas emissions as required by ED IFRS S2, the ability of an entity to comply with the Standards is, to a certain extent, linked to how widely adopted the Standards are.

Hence, we believe that more emphasis should be placed on increasing the rate of adoption by **easing the path toward adoption of the Standards**, while progressing to the desired aspiration as the landscape matures further.

A more supportive approach to facilitate easier adoption of the Standards may then be more encouraging, particularly for the SMEs which typically play critical roles along the value chain.

A few suggestions are included under point no. 2 below.

2. Recognition of sustainability as a journey

We believe that the Standards could be more adoption-friendly if there are elements or provisions which recognise that sustainability is a journey. In this regard, the following are some suggestions for the ISSB's consideration:

a. Introduction of **transitional provisions and practical expedients** or a **phased approach** to provide some leeway towards certain requirements (such as Scope 3 emissions) in the early years of adoption or in specific circumstances (please see our response to Question 9 below).

b. **Different tiers of compliance** – It is unlikely that companies can go from zero to being able to prepare sustainability disclosures in full compliance with the Standards in a short span of time if the bar is set too high from the outset. This may deter a company from even starting as it will need to invest years of efforts before seeing any meaningful returns.

Given that there are many different stages of maturity and readiness amongst preparers, having different tiers of compliance with the Standards could be helpful in encouraging companies to embark on sustainability reporting using the Standards.

c. **Starting with a more prescriptive and narrow set of requirements** – Bearing in mind the state of sustainability reporting today as mentioned in point no. 1 above, there could be merits to starting with a set of more prescriptive and narrow requirements. This could also include having a set of core ESG metrics to serve as a starting point.

   Although this approach may not be ideal vis-à-vis the objective of a comprehensive global baseline, this approach could get more companies, including SMEs, started on this journey. There can also be quick wins in terms of higher level of consistency and comparability in reported information. The Standards can then progress to be more principles-based , like ED IFRS S1, as preparers (and users) mature.

3. Clarity, comparability and verifiability

We hope that more examples or application guidance materials can be included in the Standards to provide more clarity to key terms and concepts, such as materiality, significant risks or opportunities, the evaluation of enterprise value as well as the extent to which a company's value chain has to be determined (i.e. how far up and/or down the line of value chain do companies have to consider). This will help in driving consistency and comparability in reported information.

Assurance over sustainability-related financial information remains challenging (please see our response to Question 13 below), and we hope that the ISSB will work closely with the International Auditing and Assurance Standards Board (IAASB) on the bespoke sustainability assurance standards, which the IAASB is expecting to issue for public consultation in 2023.

4. Interoperability with other major sustainability reporting standards/frameworks, particularly Global Reporting Initiative (GRI)

We laud the ongoing collaborative efforts between the ISSB and the GRI. We believe that the results of these efforts, particularly in ensuring the interoperability of the Standards with the GRI Standards, are critical in driving global adoption of the Standards. This is because there are currently many GRI reporters in the market, given the GRI framework's popularity. We have heard feedback from some GRI reporters that they are not likely to take any action towards adopting the Standards until there is clarity on the interoperability front.

It appears that there is impetus for the ISSB to expedite the progress of its collaborative work with the GRI.

5. **Self-contained standards**

We support the approach which the ISSB has taken by building on existing established standards/frameworks such as SASB Standards and CDSB Framework.

However, some confusion arises when navigating the Standards, particularly where there are requirements which refer to those other standards/frameworks (please see our response to Question 7 of ED IFRS S1).

It becomes unclear the extent to which adopters of the Standards will also need to understand and comply with the requirements of those other standards/frameworks.

Hence, it may be preferable for the Standards to be more self-contained and for all mandatory requirements and considerations to be included within the Standards themselves. We propose that references to other sustainability reporting standards/frameworks be considered only as non-mandatory guidance materials.

6. **Emphasis on ethics**

With the rising significance of sustainability information, the importance of ethical behaviour by those preparing such information cannot be understated.

While we note that the IFRS Accounting Standards similarly are silent on ethics, our view is that a different approach may be required for the Standards. Financial reporting is typically performed by professional accountants who are subject to the ethical code of conduct promulgated by professional accountancy bodies or by national regulators.

The same cannot be said about sustainability reporting. The sustainability reporting process may involve individuals of varying backgrounds, who may or may not be professional accountants or belong to another profession, where its professionals are subject to ethical codes of similar rigour as the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants (IESBA).

Given the nature of sustainability-related financial information and the risk of greenwashing, we hope that the ISSB and IESBA could work together in developing a framework or standard of ethical conduct for the purpose of sustainability reporting which will be adhered to by all preparers of sustainability reporting, not just professional accountants.

Our responses to selected questions in the ED are as follows:

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? (b) Does the objective focus on the information that would enable users of general purpose financial reporting to assess the effects of climate-related risks and opportunities on enterprise value? (c) Do the disclosure requirements set out in the Exposure Draft meet the objectives described in paragraph 1? Why or why not? If not, what do you propose instead and why?

(a) & (b)
Yes, we agree with the objective stated in the ED as it supports disclosures which will be relevant for users of general purpose financial reporting to assess the effects of climate-related risks and opportunities on enterprise value.

(c) The proposed requirements would generally meet the proposed objective of the ED if preparers are able to fully comply with them. However, as mentioned under point no. 1 earlier in this letter, it appears unlikely in the current state that most preparers will be able to fully comply with all the requirements of the ED.

Question 2 – Governance
Do you agree with the proposed disclosure requirements for governance processes, controls and procedures used to monitor and manage climate-related risks and opportunities? Why or why not?

We agree with the proposed disclosure requirements for governance processes, controls and procedures in this ED.

However, as highlighted in our response to Question 1 (c) of ED IFRS S1, it would be helpful if more examples/guidance can be provided to illustrate how the proposed requirements of the ED on governance and those required under ED IFRS S1 can be applied together in an understandable and integrated manner.

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?

While the proposed requirements are clear, preparers may face difficulties in determining which climate-related risks and opportunities are considered as significant since this involves a considerable level of judgement.

Paragraph 9 of the ED requires an entity to disclose the significant climate-related risks and opportunities and the time horizon over which each could reasonably be expected to affect its business model, strategy and cash flows, its access to finance and its cost of capital, over the short, medium or long term. The entity is also required to disclose how it defines short, medium and long term. Given the relative unpredictability of the impact of climate-related risks and opportunities, preparers may also face difficulties in assessing the time horizon (i.e. short, medium and long term) in which these risks and opportunities could affect the entity's business model, strategy, cash flows, access to finance and cost of capital.

Additional illustrative guidance would certainly be helpful in driving consistency and comparability.

Question 4 – Concentrations of climate-related risks and opportunities in an entity's value chain
(a) Do you agree with the proposed disclosure requirements about the effects of significant climate-related risks and opportunities on an entity's business model and value chain? Why or why not?

We appreciate the importance of extending the requirements for disclosures to the value chain as this can serve to compel other entities in the ecosystem to scale up disclosure capabilities.

However, we believe that clarity of this extension is necessary to ensure consistency and comparability. It is not clear from the ED how far up or down the value chain a reporting entity needs to consider.

Naturally, there are limitations to accessing information from suppliers or other third parties due to fears of divulging sensitive information which could affect competitive advantages as well as concerns over potential litigation risks. There is also no obligation for the suppliers or third parties to share any information in the first place.

For the reporting entity, there could also be a risk of undue reliance on the information obtained from these external parties, particularly as it would be difficult to assess the reliability of such information.

In this regard, we hope the ISSB can provide more application guidance and illustrative examples.

Question 6 – Current and anticipated effects
(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?
(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?
(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?

(a) We agree with the approach of requiring quantitative disclosures and where that is not possible, allowing qualitative disclosures.

(b) In principle, the proposed disclosures 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 is useful for the users of general purpose financial reporting.

However, more clarity should be provided on the extent to which such financial effects should be disclosed. Specifically, it is not clear if this is limited to financial effects which are assessed in accordance with the financial reporting standards, hence had an effect on the current reporting period's financial position, financial performance and cash flows.

For instance, if a retail business is affected by flood, would disclosure of financial effects be limited to those which are more certain or quantifiable such as inventory write-off or costs incurred (or estimated to be incurred) to repair damages to the premises? Or would the disclosure of financial effects extend to those which are more judgemental and involve significant assumptions to be made such as the opportunity cost of closure of business?

(c) There are concerns over the proposed requirements in paragraphs 14 (c) and (d) which require disclosure over how the entity expects its financial position and financial performance to change over time, given its strategy to address significant climate-related risks and opportunities.

Such forward-looking disclosures involve significant judgement and estimation. Preparers are concerned of the potential repercussions (both reputational and legal) if such expectations disclosed do not materialise. This is especially since there can be other factors (such as competition and market conditions) which affect future financial position and financial performance.

Some guidance, which takes into consideration such risks associated with forward-looking disclosures, on how an entity can meet these proposed requirements would be helpful.

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? (b) The Exposure Draft proposes that if an entity is unable to perform climate-related scenario analysis, that it can use alternative methods or techniques (for example, qualitative analysis, single-point forecasts, sensitivity analysis and stress tests) instead of scenario analysis to assess the climate resilience of its strategy. (i) Do you agree with this proposal? Why or why not? (ii) Do you agree with the proposal that an entity that is unable to use climate-related scenario analysis to assess the climate resilience of its strategy be required to disclose the reason why? Why or why not? (iii) Alternatively, should all entities be required to undertake climate-related scenario analysis to assess climate resilience? If mandatory application were required, would this affect your response to Question 14(c) and if so, why? (c) Do you agree with the proposed disclosures about an entity's climate-related scenario analysis? Why or why not? (d) Do you agree with the proposed disclosure about alternative techniques (for example, qualitative analysis, single-point forecasts, sensitivity analysis and stress tests) used for the assessment of the climate resilience of an entity's strategy? Why or why not? (e) Do the proposed disclosure requirements appropriately balance the costs of applying the requirements with the benefits of information on an entity's strategic resilience to climate change? Why or why not? If not, what do you recommend and why?

We agree with the ISSB's approach of requiring the use of climate-related scenario analysis and allowing alternative methods or techniques where an entity is unable to perform climate-related scenario analysis. However, it would be helpful if there is further guidance on what are considered acceptable reasons (or unacceptable reasons) for not being able to perform climate-related scenario analysis. This would promote consistency in application of the requirements of the standard.

In addition, the ED requires the climate-related scenario analyses to utilise assumptions based on the different scenarios determined by the entity, for example those aligned with the latest international agreements, and not actual forecasted outcomes that could be sensitive. Having said that, we have received feedback that entities remain hesitant to disclose the results of their analyses due to concerns over the repercussions if the results do not eventualise.

In view of the potential sensitivity and subjectivity over why the entity considers its chosen scenarios to be more relevant than others, the ISSB can consider specifying certain baseline scenarios to be used which are aligned with the latest international agreement on climate change.

Moreover, the ISSB can consider requiring disclosures arising from jurisdictional regulations, for example those relating to carbon taxes or building standards.

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? (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?

While we agree that the inclusion of Scope 3 emissions is important to achieving the objective of the ED, we have heard significant concerns over the practicability of this requirement considering the state of sustainability reporting today, as discussed earlier in point no. 1 of this letter.

The calculation of Scope 3 emissions is still an area where entities face significant practical challenges in view of difficulties in obtaining reliable data, particularly since Scope 3 emissions are generally not within an entity's direct control.

It will be helpful if the ISSB could allow some time for the sustainability reporting landscape to progress on this front. In the meantime, we propose the introduction of transitional provisions and practical expedients or different tiers of compliance (as suggested under point no. 2 earlier in this letter) with the Standards to encourage more adoption of sustainability reporting (and the Standards) at the current juncture.

Furthermore, in paragraph 21 (a)(iii)(1), the ED states that the entity shall disclose Scope 1 and Scope 2 emissions separately for the consolidated accounting group (the parent and its subsidiaries). It should be noted that the criterion to determine operational control under the GHG Protocol is not consistent with the criteria to determine control under IFRS 10 *Consolidated Financial Statements*.

While uncommon, an entity might determine that it does not have operational control over a subsidiary, and hence had excluded that subsidiary's Scope 1 and 2 emissions in its current reporting of GHG emissions. The ED's requirement to include the Scope 1 and 2 emissions of all subsidiaries could lead to issues for such entities which have been adopting the operational control approach under the GHG Protocol for the purpose of reporting on approved science-based targets or as part of targets under green/sustainable finance bonds/loans. In this respect, it would be useful if the ISSB could provide some guidance on how such issues can be addressed or explained.

Additionally, paragraph 21 (a)(iii)(2) requires Scope 1 and 2 emissions to be disclosed for associates, joint ventures, unconsolidated subsidiaries or affiliates. The equity share or operational control method under the GHG Protocol should be used. It would be useful to obtain more clarity if the Scope 1 and 2 emissions of these investees should be classified under category 15 (investments) of Scope 3 emissions and/or under this proposed disclosure.

Lastly, internal carbon prices and remuneration, which the ISSB proposes to require disclosure in paragraphs 21 (f) and 21 (g), may not be levers that all entities use to meet their emissions targets. The ISSB can consider including the phrase "where these are applicable" and/or require disclosures to highlight any other areas that entities use as tools to reduce their emissions.

Question 13 – Verifiability and enforceability
Are there any disclosure requirements proposed in the Exposure Draft that would present particular challenges to verify or to enforce (or that cannot be verified or enforced) by auditors and regulators? If you have identified any disclosure requirements that present challenges, please provide your reasoning.

We believe that auditors and regulators will face difficulties given the nature of sustainability-related financial information required by the ED. While certain information could be verifiable, such as historical quantitative and qualitative information which are factual in nature, sustainability-related financial information prepared in compliance with the ED will include forward-looking statements and qualitative disclosures which are highly subjective in nature.

The IAASB's Non-authoritative Guidance on Applying ISAE 3000 (Revised) to Sustainability and Other Extended External Reporting Assurance Engagements (EER Guide) highlights some of the challenges faced in assurance engagements over sustainability information, such as qualitative information which are inherently subjective. The challenges raised in the EER Guide are generally applicable to sustainability-related financial information as required by the ED as well.

To reduce the risk of greenwashing and undue reliance on assurance engagements over sustainability-related financial information, the inherent limitations of such assurance engagements need to be clearly articulated. There needs to be further clarity and consensus (and subsequently education) over which types of information can be assured and which cannot be.

We would like to reiterate our earlier point no. 3 of this letter on the importance of the ISSB working closely with the IAASB on the bespoke sustainability assurance standards.

Question 14 – Effective date
(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 in the Exposure Draft.

We wish to draw reference to points no. 1 and no. 2 of this letter in which we have highlighted the need to balance the aspiration of the ED and the current state of sustainability reporting as well as the recognition of sustainability as a journey.

It is difficult to suggest a reasonable effective date based on the current form of the ED as it may be too challenging for immediate adoption by many companies. Public-listed and multi-national corporations aside, there are many SMEs which have not embarked on sustainability reporting and are staying on the sidelines until reporting requirements and practices are more matured and certain. This is expected given the practical need to make the most out of the limited resources which they have.

To encourage sustainability reporting and wider adoption of the Standards, we wish to reiterate our earlier suggestions in point no. 2 in this letter, which include:

a. Introduction of **transitional provisions and practical expedients** or a **phased approach**
b. **Providing for different tiers of compliance**
c. **Starting with a more prescriptive and narrow set of requirements**

Should you require any further clarification, please feel free to contact Mr Terence Lam at terence.lam@isca.org.sg or Mr Donaphan Boey at donaphan.boey@isca.org.sg.

Yours faithfully,

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