ISSB PROVIDES TRANSITIONAL RELIEF, PRIORITIZING CLIMATE-RELATED DISCLOSURES

This past week, the International Sustainability Standards Board (ISSB) announced that it had formally decided to prioritize climate-related disclosures (as opposed to the broader universe of sustainability-related metrics) to enable companies to focus their initial efforts on meeting strong investor demand for comprehensive, consistent and comparable decision-useful information on climate-related risks and opportunities. This means that, in the initial year of reporting under ISSB standards, reporting companies will not be required to provide full reporting on sustainability-related risks and opportunities beyond climate. That full reporting will only be required in the second year.

The ISSB disclosure regime will be effective beginning in 2024, although initial application and reporting dates could vary as ISSB standards will need to be adopted on a jurisdiction-by-jurisdiction basis.

Background

As I noted in a previous briefing note (available here), in February, the ISSB took final decisions on the technical content of its initial disclosure standards. IFRS S1 (General Requirements for Disclosure of Sustainability-related Financial Information) and IFRS S2 (Climate-related Disclosures) are expected to be issued at the end of the second quarter of this year).[1]

The ISSB is part of the International Financial Reporting Standards (IFRS) Foundation. IFRS accounting rules are followed in more than 160 countries, although not in the United States. These countries will have the option to use/not use the ISSB standards as part of their IFRS accounting frameworks (*see* ISSB FAQ).[2]

The ISSB standards are drawn in part from the existing materiality-focused standards of the Sustainability Accounting Standards Board (SASB), which now forms part of the ISSB ecosystem (*see* my previous briefing note, available here). The ISSB has stated that, where there are no clear ISSB guidelines, reporting companies, subject to certain conditions, may consider guidance from the Global Reporting Initiative (GRI) and the European Sustainability Reporting Standards (ESRSs) to be applicable in the European Union. This guidance will be set out in appendices to IFRS S1.

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1 Last March 2022, the ISSB published an Exposure Draft Snapshot of IFRS S1 and S2 that provides a useful overview of the two standards. My summary is available here.

2 According to the IFRS Foundation, "the ISSB standards are intended to provide a comprehensive global baseline of sustainability disclosure standards that can be mandated and combined with jurisdiction-specific requirements or requirements aimed at meeting the information needs of broader stakeholder groups beyond investors." As with the approach generally taken for IFRS accounting standards issued by the International Accounting Standards Board, jurisdictional authorities are free to decide whether to mandate use of ISSB standards. The backing of the G7, the G20, IOSCO, the Financial Stability Board, the African Finance Ministers and finance ministers/central bank governors from over 40 jurisdictions underscores the global nature of the baseline. Some countries are creating their own sustainability standards boards as an interface with the ISSB.

Transitional Relief

The relief provided this past week, together with prior decisions on relief, means that reporting companies *need not* for the first year they report in compliance with ISSB standards:

- provide disclosures about sustainability-related risks and opportunities beyond climate-related information (in the first year of reporting);
- provide annual sustainability-related disclosures at the same time as the related financial statements;
- provide comparative information;
- disclose Scope 3 GHG emissions (which already had a one-year grace period, decided last December)[3]; and
- use the GHG Protocol to measure emissions, if they are currently using a different approach.

Furthermore, companies that only report on climate-related risks and opportunities in the first year will be able to avail themselves of additional relief in providing comparative information, such that they will not need to provide comparative information about sustainability-related risks and opportunities beyond climate in their second year of reporting.

The ISSB April 2023 Supplementary Update notes that the one-year transition relief would not change the effective date of IFRS S1. The ISSB had tentatively decided in February to require that IFRS S1 be effective for annual reporting periods beginning on or after January 1, 2024 (with reports due the following year). However, for a company applying the transition relief in the first year it applies IFRS S1, the requirements in IFRS S1 would apply only insofar as they relate to the disclosure of climate-related financial information. The transition relief would have no effect on the application of, or requirements set out in, IFRS S2.

Other transitional relief, including as to timing of climate-related disclosure relative to release of financial statements, was agreed in February.

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[3] In October, the ISSB confirmed the inclusion of Scope 3 disclosure, when material, as set out in its draft IFRS, S2 given feedback from investors that they cannot fully understand transition risk without information about absolute gross Scope 1, 2 and 3 emissions. However, the ISSB agreed it would provide support for companies in the provision of these disclosures through guidance and relief to help them implement processes to measure Scope 3 emissions.

In December, the ISSB agreed to set out a framework in IFRS S2 for the measurement of Scope 3 GHG emissions that would require the use of reasonable and supportable information that is available without undue cost or effort and incorporates the use of estimation. Use of this framework would be accompanied by disclosures to enable investors to understand the basis for measurement of Scope 3 GHG emissions.

The ISSB also agreed in December to the one-year Scope 3 grace period following the effective date of IFRS S2, to give time for companies to implement their processes. A company will also be able to include information that is not aligned with its reporting period, when that information is obtained from companies in its value chain with a different reporting cycle.

Concluding Thoughts

The ISSB standards are separate from the EU sustainability-related disclosure requirements and the proposed SEC climate-related disclosure requirements. Some companies will be facing the prospect of complying with multiple climate-related, and potentially broader sustainability-related, disclosure regimes. According to data prepared by Refinitiv provided to the Wall Street Journal, at least 10,000 non-EU companies[4] are likely to be subject to the EU Corporate Sustainability Reporting Directive ("CSRD"), including 31% that are American. (*See* my previous briefing note on the CSRD, available here.)

The focus on disclosure is taking place against a backdrop of undeniable C-suite focus on climate change that underlies the urgency of the ISSB efforts. According to the Deloitte 2023 CxO Sustainability Report, business leaders generally ranked the threats posed by climate change as a top issue second only to the economy; 61% said climate change will have a high/very high impact on strategy and operations over the next three years and almost all respondents indicated their companies were negatively impacted by climate change in some way during 2022. The finding prompted Deloitte Global CEO Joe Ucuzoglu to conclude that, "If there was any doubt that climate change is an enduring part of the business agenda, the increased focus on sustainability by leaders over the past year should put it to rest." Pressure to act on climate change comes from multiple touchpoints: boards and management (68%), clients and consumers (68%) and regulators and governments (68%), as well as investors (66%), employees (64%) and civil society (64%). Competitors and peers (59%) and banks/lenders (50%) also are sources of pressure to act.

Interestingly, while the ISSB delay on the full sustainability framework gives companies an additional year for that more fulsome disclosure, there already are over 2,600 companies that use SASB standards in their public company communications.

All to say that the direction of travel remains clear, and companies should be well on their way to having the systems, processes and mindsets in place to manage their climate-related, and broader sustainability-related, disclosures. And, as I have noted in prior briefing notes, while the timing and scope of SEC climate-related rulemaking (not to mention the intensity of the political pushback) remains uncertain, and in terms of coverage, the contentious Scope 3 disclosure requirements in particular may well fall short of the emerging global standard, US companies may find that the bar is higher.

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[4] According to Refinitiv data, close to 10,400 non-EU companies have EU listings and more than 100 non-EU companies that are not listed in the European Union exceed the €150 million EU revenue threshold.