To: IFRS Foundation

From: Professor Carol Adams CA PhD FAICD, Durham University Business School, UK and Swinburne Business School, Australia. Founding Editor and Editor-in-Chief, *Sustainability Accounting Management and Policy Journal*.

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Response to the Consultation Paper on Sustainability Reporting

I write to you as a Professor of Accounting with around 30 years' experience in financial, non-financial, integrated and sustainability reporting research. I founded in the *Sustainability Accounting, Management and Policy Journal* in 2010 in order to develop a field of research to inform practice and policy in accounting and reporting on the impact of organisations on society and sustainable development. I have led the integration of sustainability into strategy, developed sustainability reports and advised organisations on integrated reporting and SDG impact reporting. In the interests of transparency I disclose that I have been involved in the development of the AA1000 Standards, the work of the International Integrated Reporting Council (IIRC) and the Global Reporting Initiative (GRI) and that I am currently technical expert to the UNDP's SDG Impact Team and a member of the Climate Disclosure Standards Board's (CDSB) Technical Working Group. The views expressed here are my own.

My key concerns are:

- As formulated, this proposal is not in the public interest;
- The proposal is not cognisant of current investor and corporate best practice and findings of evidence-based research;
- A focus on the financial materiality of sustainable development issues is not in the long-term interests of investors, companies, society and governments that have committed to the UN SDGs;
- By focussing on narrow interests of a sub-set of stakeholders, the proposal will not achieve a stated goal of IFRS Foundation Trustees to reduce the number of frameworks/standards.

Question 1

Is there a need for a global set of internationally recognised sustainability reporting standards?

(a) If yes, should the IFRS Foundation play a role in setting these standards and expand its standard-setting activities into this area?

(b) If not, what approach should be adopted?

The question is puzzling. There is already a global set of internationally recognised sustainability reporting standards. There is no need for another one. The GRI Standards are internationally recognised and used by companies around the world. The IFRS Foundation could use its relationships to assist in making those Standards mandatory along with concepts and content elements in the International <IR> Framework. The latter's broad view of value creation and multiple capitals approach is more appropriate in the context of sustainability disclosures than the IFRS Foundation's narrow focus on 'financial materiality'. The TCFD recommendations have broad support for additional climate related disclosures.

The consultation paper does not make a robust or convincing case for the IFRS Foundation setting additional sustainability reporting standards. For example, in para 17, the Consultation Paper refers to "the IFRS Foundation's track record in and expertise in standard-setting, and its relationships with global regulators and governments around the world, could be useful for setting sustainability reporting standards" and paragraph 18 highlights the IFRS Foundation's due process. But the Consultation Paper does not explain how this compares with the track record on these matters of other global bodies. GRI, for example, was founded in 1997, has a due process for setting sustainability standards informed by those of accounting standard setters and involving multi-stakeholder input. It also has relationships with global regulators and national governments.

I would expect to see some evidence-based analysis of what the criteria are for successful sustainability reporting standard setting or what the IFRS Foundation could add relative to existing global offerings.

Paragraphs 18 and 21 appear to assume that national governments will chose to delegate sustainability reporting standard setting to the national body responsible for financial reporting. Has this been tested?

National governments have signed up to achieving the UN SDGs and are recognising the role that corporate reporting plays in this. For example, Recommendation 15 of the report of Australian Senate Inquiry on the SDGs recommends "that the Australian Government partners with private and tertiary sector stakeholders to develop and disseminate Australian guidance on reporting against the Sustainable Development Goals in order to ensure consistent and transparent reporting…" (Australian Department of Senate, 2019). The IFRS Foundation proposals are not aligned with this need.

No evidence is provided regarding "the increasing interconnectedness between financial reporting and sustainability reporting" (para 27) nor of benefits from it. I do believe that longer-term financial *performance* is dependent on the achievement of the United Nations Sustainable Development Goals. However, this measuring this longer-term impact in financial terms is problematic. Further, reporting that measures an organisation's impact on sustainable development (and achievement of the SDGs) mostly cannot be expressed in financial terms nor linked to financial reporting. The implications for value creation as defined in the International <IR> Framework (IIRC, 2013) are easier to identify and more relevant to investors than financial materiality. Sustainable development issues do of course have implications for asset valuations and financial liabilities, and this is where the IFRS Foundation should focus.

The Consultation Paper has not been informed by independent analysis of the desirable features of a sustainability standard setting body or independent assessment of the relative merits of the various standard setting bodies. Such an analysis should be conducted before proceeding.

Overall, I have concerns about proposals and assertions made that are not supported by independent evidence. The IFRS Foundation should act in the public interest and, as such, this is a matter that must be addressed. The IFRS Foundation has referred to a number of reports that inform its proposals that are also not based on evidence of how reporting drives change (or doesn't)[1].

Question 2

Is the development of a sustainability standards board (SSB) to operate under the governance structure of the IFRS Foundation an appropriate approach to achieving further consistency and global comparability in sustainability reporting?

I cannot answer this question with the information provided. No information has been provided on how this would be achieved. The IFRS Foundation needs to consider what is meant by "consistency and global comparability" in the context of their being global framework/standard setting bodies as opposed to different national practice as was the case with financial reporting pre-establishment of the International Accounting Standards Committee (IASC). I urge the IFRS Foundation to articulate what it considers to be inconsistent and lacking in comparability, why that matters, to whom it matters and, most importantly, what information or corporate thinking might be lost in the process of increasing consistency. Sustainability issues are complex and interdependent - organisations and investors need to be able to handle this. Research that I am currently writing up with Subhash Abhayawansa indicates that even large multinationals considered to be leaders in sustainability have inadequate management systems and governance processes to incorporate sustainable development risks and opportunities into their decision making. Focussing on consistency and comparability in reporting will likely inhibit the further development of such processes. The *SDGD Recommendations*[2] are designed to increase internal capacity to deal with complexity by requiring reporting on management approach, strategy, governance oversight and performance and targets and are aligned to the TCFD recommendations, International <IR> Framework and GRI Standards.

The situation with sustainability reporting is very different from the circumstances that led to the harmonisation of national financial reporting practices described in Weetman et al (1998)[3]. The IASC was established in 1973. It took until 1998 to complete a set of 'core standards' that satisfied the International Organization of Securities Commissions (IOSCO) for the purposes of multiple Stock Exchange listings. (The International Accounting Standards Board (IASB) was formed in 2001.) Such a lengthy timeline is inappropriate in the context of climate change and consideration needs to be given to how the IFRS Foundation can best focus and prioritise its efforts to speed up corporate responses to *physical* climate change risks.

Current research I am undertaking with my colleague Subhash Abhayawansa shows that only a small proportion of high impact companies are demonstrating that they are considering the *physical* risks of climate change. This will have longer term financial consequences.

If the IASB Trustees decide to go ahead with the establishment of another global Sustainability Standards Board they would need to consider a pathway and timescale to delivering sustainability

[1] I have written critiques of the WEF and Big 4, Accountancy Europe and the Statement of Intent of current standard setters.

[2] Adams, C A, with Druckman, P B, Picot, R C, (2020) *Sustainable Development Goal Disclosure (SDGD) Recommendations*, published by ACCA, Chartered Accountants ANZ, ICAS, IFAC, IIRC and WBA. ISBN: 978-1-909883-62-8 [link]

[3] Weetman P, Jones E, Adams C A and Gray S J (1998). Profit measurement in UK accounting standards: a case of increasing disharmony in relation to US GAAP and IASs, *Accounting and Business Research* 28(3): 189–208.

standards. National governments have agreed to deliver on the United Nations Sustainable Development Goals by 2030 and that the sustainable development issues addressed by the SDGs mean that a business-as-usual (financial materiality/investor oriented) approach is not viable in that context.

The IFRS Foundation should be explicit about the implications for existing standards and global standard-setters and consider what reducing the number of standard setters (the apparent goal in this exercise that follows calls to make reporting easier for investors and reporting companies) will mean for companies that seek to provide information for a broader stakeholder audience than the IFRS Foundation seeks to cater for. This proposal does not fill that need.

Question 3

Do you have any comment or suggested additions on the requirements for success as listed in paragraph 31 (including on the requirements for achieving a sufficient level of funding and achieving the appropriate level of technical expertise)?

Before proceeding consideration should be given to the relationship with existing standard setters, the work done by them over more than 20 years (in the case of GRI) on developing sustainability reporting standards. It is unclear whether the intention is to incorporate the extant body of work, how that process would occur and what it means for the urgent further development and funding of *that* work.

Whilst the consultation paper notes the need to "build effective synergies with financial reporting", mention of the need to build effective synergies with work on sustainable development is absent. Standards that purport to be 'sustainability reporting' standards must do so. Such work includes the UNDP's SDG Impact Standards[4] and initiatives with the corporate sector by UNCTAD-ISAR and the UN Global Compact. The UNDP's SDG Impact Standards[5] fill a gap that is consistent with the findings of research by accounting academics that the transition to sustainable development requires changes in management approach, approaches to developing strategy and targets and governance oversight (see, for example, Adams 2017a,b). The *UNDP's SDG Impact Standards for Enterprises* is open for consultation until 31st December and is relevant to companies and their investors.

Question 4

Could the IFRS Foundation use its relationships with stakeholders to aid the adoption and consistent application of SSB standards globally? If so, under what conditions?

The IFRS Foundation would make a valuable contribution if it used its relationships to assist in making concepts and content elements on the International <IR> Framework and the GRI Standards mandatory.

The IFRS Foundation has not set out a convincing case to establish an additional Sustainability Standards Board. See also my response to questions 1 and 2. The IFRS Foundation probably could leverage its relationships, but whether it could do this better than current standard setters is not clear

[4] UNDP's SDG Impact Standards. [link]
[5] UNDP's SDG Impact Standards. [link]

and has not been analysed. There are also doubts as to whether the IASB can work in a timely manner - see my answer to Question 2 regarding the slow progress of the IASB and its predecessor IASC.

Question 5

How could the IFRS Foundation best build upon and work with the existing initiatives in sustainability reporting to achieve further global consistency?

The intention/plan is unclear from the information provided. However, the appropriateness of current IFRS Standards in light of climate change and other sustainable development issues requires urgent consideration and should be the first priority of the IFRS Foundation. No other body can do this –this is the job of IFRS. The IFRS Foundation should focus on revisions required to current IFRS Standards and leave 'sustainability reporting' to those bodies with a long history of developing standards that address multiple stakeholder concerns.

Question 6

How could the IFRS Foundation best build upon and work with the existing jurisdictional initiatives to find a global solution for consistent sustainability reporting?

The IFRS Foundation could seek to use its relationships to ensure that national/jurisdictional developments are consistent with the International <IR> Framework, GRI Standards and the TCFD recommendations and seek to add weight to make those standards mandatory.

Question 7

If the IFRS Foundation were to establish an SSB, should it initially develop climate-related financial disclosures before potentially broadening its remit into other areas of sustainability reporting?

The IFRS Foundation's first priority should be to review existing IFRS Standards in light of climate change issues. A second priority could be to assist in making the TCFD recommendations, the International <IR> Framework and the GRI Standards mandatory. Disclosure on climate change should not be limited to a subjective view of what is financially relevant now and what might be financially relevant in the future and when. This mindset results in poor disclosures of the physical risks of climate change.

Question 8

Should an SSB have a focused definition of climate-related risks or consider broader environmental factors?

While climate change does impact on the achievement of most other SDGs, the other SDGs represent global consensus on the key sustainable development issues facing organisations, people and planet. These are urgent.

The *TCFD recommendations* already consider climate-related risks and the IFRS Foundation could use its relationships to make them mandatory.

The focus should not just be on risk. Organisations should disclose their management approach to identifying opportunities, how they are incorporated into strategy to create value for organisations and society and governance oversight of that process as required in the *SDGD Recommendations*.

Question 9

Do you agree with the proposed approach to materiality in paragraph 50 that could be taken by the SSB?

No. I strongly disagree with this approach. I disagree with a focus on financial materiality for investors. This is a backward step given the influence the IIRC has had in broadening thinking on value creation (see Adams et al, 2016 and Adams 2017a). Further, it is inappropriate to start with one conceptual framework and then switch to another. (I am surprised the IFRS Foundation is suggesting this.) Views on what is ultimately financially material for investors varies widely. Organisations cannot continue to create value for themselves, their shareholders or society more widely unless sustainable development issues are addressed. Your proposed approach increases complexity, rather than reducing it and a later switch would require revision of earlier standards.

'Double materiality' as defined by the EU is also inappropriate because it has a narrow focus on financial materiality rather than a broader approach to value creation as adopted by the International Integrated Reporting Council (IIRC, 2013).

The Fundamental Concepts of the *SDGD Recommendations*[6], with a definition of materiality that is informed by the IIRC's *International <IR> Framework* and the GRI Standards but with an additional focus on sustainable development and impact on achievement of the SDGs is a more appropriate starting point and aligns the work of the GRI, IIRC and TCFD (Adams 2017b, 2020). The stated focus of SASB and CDSB on financial materiality is a small subset of what is expected of organisations and falls within this broader definition of materiality.

The IFRS Foundation's decisions should be informed by best practice. Substantial evidence was given to the Australian Senate Inquiry from a range of stakeholders on the current state of investor and corporate practice and thinking with respect to the relevance of sustainable development issues to investors and companies[7]. The UK Parliament's Environmental Audit Committee collected substantial evidence concerning the used of the TCFD recommendations[8]. These matters have also been the focus of academic research[9].

Question 10

Should the sustainability information to be disclosed be auditable or subject to external assurance? If not, what different types of assurance would be acceptable for the information disclosed to be reliable and decision-useful?

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[6] *SDGD Recommendations* [link]

[7] The Senate Inquiry report is available here

[8] The UK Parliament's Environmental Audit Committee report is available here

[9] See letter to the Chair of the IFRS Foundation Trustees from journal editors and professors of accounting summarising research relevant to this consultation [link]

Disclosure of management approach, strategy and governance oversight[10] (as in the *SDGD Recommendations*) is important information, and its disclosure is critical to changing the way organisations make decisions. Assurance providers need to find ways of assuring such information. Research has shown that assurance scopes are limited due to cost and assurance provider conservatism. It is *not* appropriate to limit disclosure requirements to what assurance providers are prepared to include in scope.

Question 11

Stakeholders are welcome to raise any other comment or relevant matters for our consideration.

I am concerned about the lack of evidence supporting the proposals and assertions made in this document and that they are not cognisant of the body of research by accounting academics in this field[11]. Some of the proposals give the impression that they are made to serve a sub-group of legitimate stakeholders with respect to corporate sustainability reporting. I expect the IFRS Foundation to act in the Public Interest.

I am a signatory to a separate letter summarising the key findings of this research which may be helpful in developing your approach. Particularly important are research findings that reporting that is not both mandated *and* enforced is often misleading and of poor quality[12].

I agree with para 52 that sustainability information should be subject to external assurance but am concerned that might lead to reported information being limited to that which the Big 4 is prepared to assure. This would be inappropriate as disclosures on management approach, strategy and governance oversight that have been found to drive changes in decision making processes (Adams, 2017a; 2017b; 2020; Adams et al, 2020). These disclosures are rarely within the scope of external assurance. This must change.

On a matter of governance, cross connections with governing bodies other sustainability standard setting bodies by the IFRS Foundation trustees should be made transparent and noted in any further publications on this matter.

References

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[10] See the *SDGD Recommendations* [link]
[11] I am a signatory to a letter to the Chair of the IFRS Foundation Trustees summarising this research [link]
[12] See letter to the Chair of the IFRS Foundation Trustees summarising this research [link]

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