Comment Letter in response to the Consultation Paper on Sustainability Reporting

Thank you for the opportunity to comment on the Consultation Paper. The views expressed herein are personal views; they do not represent official positions of the respective universities, or other institutions, with which we are affiliated. For the purposes of transparency, we disclose below our most relevant institutional associations, none of which we consider raises any conflict of interest with respect to this comment letter.

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Summary of main messages

For greater clarity, we preface our specific answers to the Consultation Paper (CP) questions with a summary of our main messages.

The mission of the IFRS Foundation is to provide material information to providers of financial capital ('investors' and other creditors, or 'capital providers'). We refer to such information as 'financial reporting'. The scope of financial reporting is therefore defined by 'financial materiality' to capital providers.

The objective of general-purpose financial reporting, as stated in the Conceptual Framework, is "to provide financial information about the entity that is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity." Yet the IFRS Foundation has to-date focused almost exclusively on providing financially-material information via the financial statements (including notes). Yet reporting standards that provide additional disclosures outside the financial statements should also be considered within the IFRS Foundation's mission, much in the same way that related-party or risk disclosures can provide relevant information to capital providers. Such complementary disclosures are currently provided by companies in a variety of different ways, albeit partially and mostly voluntarily. These disclosures are 'financial' in that they are material to providers of financial capital. They can be quantitative ('metrics') or qualitative ('narrative') and, if the former, either monetary or non-monetary.

One way to interpret the strong capital market demand for sustainability reporting, cited in the CP, is that capital providers do not think they get sufficiently comparable, timely and reliable financially-material information on sustainability-related matters, such as climate change (Amel-Zadeh and Serafeim, 2018). In this regard, there is no conceptual distinction between financially-material information that arises directly from a firm's normal business activities and that which arises indirectly from environmental and social impacts on the firm. Either way, in order to estimate future cash flows and value a firm, all financially-material information is by construction and definition decision-relevant.

In our view, this unmet demand for financially-material disclosure should be satisfied or addressed by the IFRS Foundation. This follows directly from the Conceptual Framework's stated objective for general-purpose financial reporting. To the extent that current IFRS financial statements do not provide obvious ways to provide such information, the disclosure requirements should be expanded accordingly. In this way, financial reporting under the auspices of the IFRS Foundation would comprise both financial statements and other

financially-material disclosure, which (for consistency with emerging terminology) we refer to as ‘sustainability-related financial disclosure’.

One reason why reporting entities do not currently provide sufficient sustainability-related financial disclosure is that the issues involved are both complex and in some respects different from traditional areas of financial reporting. Another reason is that voluntary reporting frameworks ‘lack teeth’ – they do not lend themselves to complete, comparable disclosures, in part because of the public-good nature of information provision. Mandatory reporting standards would address both of these concerns, while also establishing an agreed foundation for the development of both audit practice and regulatory enforcement. Such standards would provide guidance on what sustainability-related information is likely to be considered financially material, along with specific requirements for the disclosure of that information.

In this regard, we note the global credibility, authority and legitimacy of the IFRS Foundation in setting international reporting standards for participants in capital markets. Our expectation is that this platform will greatly facilitate standards for sustainability-related financial disclosure becoming mandatory, and enforced, in all jurisdictions that currently require IFRS reporting. The aim here is to achieve IFRS disclosure requirements for sustainability-related financial disclosure that are comparable with those already in place for financial statements.

We urge caution, however in recognizing the limits of what the IFRS Foundation can, and should, be called upon to do. To be clear about this, we make an important distinction between two distinct types of sustainability reporting, which we refer to as ‘Type A’ and ‘Type B’. A comprehensive system of sustainability reporting includes both types.

- Type A is sustainability-related financial disclosure, as described above. This targets capital providers’ information needs and adopts an ‘outside-in’ perspective, whereby sustainability information is financially material because it relates to the economic value creation of the reporting entity. The question here for disclosure is one of financial impact *on* the reporting entity itself (sometimes termed ‘dependency’): Is the reporting entity itself affected by sustainability matters in its value creation over the long-term?
- Type B comprises corporate sustainability disclosure that is material to one or more stakeholders in society at large, but which concerns corporate impacts that are currently external effects with respect to enterprise value and are therefore not financially material. This type of disclosure targets stakeholders other than capital providers (or the non-financial preferences of capital providers) and it adopts an ‘inside-out’ perspective. The question here for disclosure is one of impact *by* the reporting entity: Does the reporting entity itself affect the sustainability of the systems within which the firm operates and that it affects (‘the planet’s life support systems’, ‘society’, ‘communities’,

etc.)? Type B information allows anyone to assess the ability of these systems to continue to sustain human society, given the firm's impact.

We recognize that the two types of sustainability reporting are connected. Type B impacts could become financially material, and therefore reclassified as Type A, because of stakeholder responses; this is 'dynamic materiality'. The more society forces firms to internalize what are currently external effects, the greater is Type A in relation to Type B.

In our view, the IFRS Foundation should focus on Type A standards. Regarding Type B sustainability reporting, we see the IFRS Foundation's role as more of an enabler that could wield its international reach and reputation to support and bring to fruition other organizations' standard-setting activities. Not only would Type B reporting divert the IFRS Foundation from its mission to inform capital markets. It would also involve inappropriate, direct engagement in public policy. Type B reporting carries implications for steering corporate behaviour (Christensen et al., 2019), similar to taxation or regulation, and it therefore requires a democratic legitimization that a private standard-setting body should not presume to hold.

Type A issues are those where there is sufficient consensus among capital providers on the materiality of those issues to them, which provides the mandate for the IFRS Foundation to determine standardized reporting requirements. Such consensus is more likely for sustainability issues on which there is inter-governmental agreement, because this implies the expected future internalization of corporate environmental or social impacts. Such consensus is perhaps most evident in the cases of climate change and human rights, and it is likely to expand as (for example) the UN's Sustainable Development Goals (SDGs) become increasingly crystalized. In contrast, individual jurisdictions retain responsibility for the setting of reporting standards on sustainability issues material to them, but on which consensus is lacking. Standard-setting on these issues raises the question of democratic legitimacy, whereby the determination of materiality for society at large is the role of government, and not of a private standard-setting body. According to this reasoning, IFRS sustainability-related financial disclosures (Type A) form an international baseline, to which individual jurisdictions can add Type B requirements according to their specific determinations of the public interest.

Critically, Type A includes information that simultaneously serves the needs of both capital providers and of other stakeholders. For example, the reporting of an entity's carbon emissions provides important Type A information, because it defines the scale of the challenge faced by that entity in transitioning its business model to net zero. But simultaneously it provides important Type B information, because it reports on the entity's environmental impact. Two things follow. First, by acting within its mission of providing information to capital providers, the IFRS Foundation's standards on sustainability-related financial disclosure would also serve a

broader public interest. While such disclosure might therefore have 'real effects' – changing corporate environmental and social impact as a result of increased transparency – these are incidental to the defining purpose of IFRS standards, which is to inform capital markets. Second, the need for Type B regulation and standards is defined to be over and above the sustainability-related financial disclosure provided by the IFRS Foundation standards. If this distinction is accepted, then the logical order of priority is that Type B builds on Type A, and not the other way around.

How the IFRS Foundation sets internationally recognised standards for sustainability-related financial disclosure is a matter of internal organization, within the IFRS Foundation: whether it creates a Sustainability Standards Board (SSB), or whether the IASB is itself reconfigured to set standards for sustainability-related financial disclosure. We discuss these alternatives below.

While the IFRS Foundation should set standards across all areas of sustainability-related financial disclosure, ranging from the consumption of natural resources to impacts on social capital, we acknowledge that an initial focus on climate issues is a pragmatic and sensible starting point. This should not, however, be taken to imply any narrowing of scope in ultimately providing financially-material disclosure across all sustainability issues.

Question 1: Is there a need for a global set of internationally recognised sustainability reporting standards?

In our view there is a need for Type A reporting standards – sustainability-related financial disclosures – to the extent that capital providers do not receive financially material information when it comes to sustainability matters. And we would add that, in that case, there is a need for standards that are mandatory as well as enforced. We reach this conclusion by (1) considering the meaning and purpose of a 'global set of internationally recognised sustainability reporting standards', and then (2) addressing whether the purpose is currently being met, and whether a need therefore arises that the IFRS Foundation could address.

We take 'sustainability reporting standards' to mean an agreed framework (and associated principles, rules or guidance) for the faithful representation, by companies, of metrics and other disclosures relating to environmental and social impact. Such impact is Type A if it is material to enterprise value, and Type B otherwise. Disclosures required by such standards include (perhaps primarily) 'non-financial' disclosures, which are neither represented in monetary terms, nor directly related to amounts currently recognized in the financial statements; the obvious example is carbon emissions. We understand the importance of 'internationally recognised' to be that consensus is a precondition for any standard to be adopted and used.

The broad context is that the sustainability crisis raises issues that are simultaneously economic, environmental and social (Arrow et al., 1995; Heal, 2016; Helm, 2015; Ruggie, 2013). Such issues are therefore important to all corporate stakeholders as well as to society at large, implying a need for sustainability reporting. Extreme weather events, for example, cause economic disruption and cost, they arise increasingly frequently as a result of global warming, and they dislocate communities, typically having greatest impact on those already most disadvantaged. The need for information relating to these issues is increasingly 'global', in the sense of not being confined within national or regional boundaries. The impact of carbon emissions on global warming is independent of its geographic source; major corporations have global supply chains; and capital providers manage portfolios on a global basis. Sustainability scientists agree that urgent steps are needed for sustainability targets (including the Paris Agreement's 1.5 to 2.0° C goal) to be reached as committed.

While these issues could be addressed in practice by 'sharp' regulatory tools of direct command-and-control regulation (e.g., outright bans of fossil fuels) and financial incentives (e.g., a carbon tax), transparent corporate reporting requirements can also help 'nudge' firms towards adapting their business activities (e.g., Weil et al. 2013; Leuz and Wysocki, 2016; Christensen et al, 2019; Hombach and Sellhorn 2019). An illustration is that understanding of and consensus on the economic, environmental and social impacts of biodiversity loss currently

lags behind that of climate change, in spite of those impacts being of a comparable scale (IPBES, 2019); this lag can be explained in part by a relative absence of effective information disclosure about this issue.

A need for sustainability information from companies does not necessarily imply a need for reporting standards. It is, however, economically efficient for companies to follow common guidance on reporting, rather than for each to attempt to invent the wheel. Such an approach is efficient also for users of corporate reporting, in comparing companies against one another. While these efficiencies can in principle be realized by a voluntary process of developing and adhering to standards, such an approach can be subject to market failure in the provision of information, for which mandatory standards offer a response (Bromwich, 1985). There is, for example, a public good component to corporate reporting, whereby information provision is costly, yet its benefits are both non-excludable and non-rival, making the direct recovery of that cost infeasible. Legislation and regulation was accordingly critical to IFRS as agreed global standards for financial reporting (Camfferman and Zeff, 2015). Mandatory standards also better enable strict enforcement, which itself is required to 'translate' high quality standards into to high quality information (e.g., Christensen et al., 2013).

Within the broad context of the sustainability crisis, an important distinction can be made between two different audiences for corporate reporting (Barker et al. 2020). The first comprises those investing in the corporate sector to achieve a financial return, which calls for a 'capital provider' approach to sustainability reporting (Type A). The second audience comprises those affected by corporate environmental and social impact. To some extent, the information needs of this second, all-inclusive audience are in part met by Type A reporting. For example, Type A might include the reporting of an entity's carbon footprint. Yet, to the extent that the information demands are not fully met, additional, 'public interest' reporting could be also called for (Type B).

There is not, at present, a global set of internationally recognised, mandatory sustainability reporting standards. This holds for both Type A and Type B reporting. While there is extensive sustainability reporting in practice (KPMG, 2020), supported by several standardising initiatives with global reach and growing acceptance (such as GRI and TCFD), current practice falls short of anything comparable with mandatory IFRS reporting, supported by jurisdiction-specific auditing and enforcement regimes. In the case of Type A, there is a disconnect here between the general principle that firms should provide financially material information and investor opinion that in practice they do not, at least not in a way that can be compared favourably with IFRS-based reporting. This can be understood as sustainability reporting being subject to 'non-compliance' and an absence of 'harmonisation' – and therefore as failure to meet the information needs of capital providers. Current sustainability reporting practice is also

insufficiently clear, and to a degree inconsistent on its intended ‘real effects’, on whether its purpose is simply to inform or instead to be an agent of social change (Buijink et al., 2019).

Some of the leading proponents of sustainability reporting themselves acknowledge that the landscape is both complex and incomplete. The Global Reporting Initiative (GRI), the International Integrated Reporting Council (IIRC), the Sustainability Accounting Standards Board (SASB) the Climate Disclosure Standards Board (CDSB) and CDP are agreed (citing stakeholder outreach) that “… a consistent message … (is that preparers and users alike) are, to varying degrees, confused and frustrated by the current state of the reporting landscape. Many … expressed their perception that the relationships, interconnections and alignment between the Participants’ frameworks and standards are not well articulated to the market” (CRD, 2019, p.9). This is in sharp contrast with financial reporting, where IFRS is mandated and supported by more than 140 countries worldwide.

Question 1 (a): If yes, should the IFRS Foundation play a role in setting these standards and expand its standard-setting activities into this area?

Yes, in our view the IFRS Foundation should play a role in setting Type A global sustainability reporting standards (Barker and Eccles, 2018). However:

- There could also be a need for ‘Type B’ sustainability reporting standards, which would not be set by the IFRS Foundation, but where the Foundation could play the role as an enabler and facilitator. That role would include explicit recognition, in engaging with governments, regulators and others, that Type A is a partial ‘solution’ to sustainability reporting, and that jurisdictions may set additional standards/requirements for Type B reporting. In addition, there would be a need to coordinate directly with institutions setting Type B standards, in order to ensure that they build effectively on Type A reporting, and that the reporting system as a whole is coherent.
- While we accept the wording ‘expand its standard-setting activities into this area,’ we also note a sense in which the IFRS Foundation is actually proposing to follow through on its existing mission, which is “to develop standards that bring transparency, accountability and efficiency to financial markets around the world.” The IFRS Foundation has mostly limited its interpretation of this mission to information provided through the financial statements (i.e., the primary financial statements and the accompanying notes; CF 1.6), albeit that the Practice Statement on Management Commentary adopts a broader approach (BC7). For this reason, the Conceptual Framework is effectively silent on information that is material to capital providers but that fails to meet the definition of financial statement elements and the criteria for recognition (Barker and Teixeira, 2018). While it is possible that some sustainability-

related disclosure can be required by current IFRS (Anderson 2019), such information is marginal at best in relation to the range of sustainability matters that are financially material yet not related directly to amounts recognized in the financial statements. Sustainability-related financial disclosure arguably therefore fills an important gap in the IFRS Foundation's delivery of its mission, albeit that this would indeed imply considerable expansion of standard-setting activity.

Our reasons for supporting a role for the IFRS Foundation are the following, which are based not least upon the track record of IFRS (Camfferman and Zeff, 2015).

- *Alignment with existing IFRS*. The IFRS Foundation is well placed to align the reporting of IFRS financial statements with Type A sustainability-related financial disclosure, thereby providing overall coherence in financial reporting to capital providers.
- *Global standards*. Meeting the information needs of capital providers across the world requires a standard-setting body that is international in composition and outlook, and that has the recognized ability and network to carry on a truly global dialogue. The IFRS Foundation's distinctive strength in this regard is evidenced in its unique track record of obtaining international buy-in to IFRS, and in its relationships with capital providers, preparers, governments, regulators and other capital market authorities globally.
- *Robust governance*. The IFRS Foundation has proven credibility and accountability, based upon effective governance, oversight and due process.
- *Expertise in standard-setting*. The IFRS Foundation is unique in its institutional experience in drafting mandatory international corporate reporting standards, which includes its capacity to translate those standards into multiple global languages.
- *Legitimacy*. The IFRS Foundation is the recognised authority with respect to setting international financial reporting standards. These are currently used "for all or most domestic publicly accountable entities (listed companies and financial institutions) in 144 jurisdictions around the world" (CP, para 19).

We support the IFRS Foundation's involvement, subject to the following conditions:

- *Building on existing achievements*. The IFRS Foundation would be in a position to select the 'best of the best' from the extensive knowledge, experience, published materials and stakeholder engagement that has been achieved already by organisations such as IIRC, CDP, GRI, SASB, CDSB and TCFD. The IFRS Foundation must proceed by building on existing achievements in this way. (An alternative approach, whereby these bodies jointly develop a single set of standards, has not yet been achieved, with experience suggesting that the aspiration is unrealistic; CRD, 2019.)

- *Urgency of response*. The climate emergency, in particular, calls for a standard setter to close existing information gaps quickly and comprehensively. The IFRS Foundation is the institution that is likely best placed to set global Type A standards that will most quickly achieve global acceptance and implementation, given the objective for financial reporting that exists already in the conceptual framework, coupled with the extensive disclosure regimes that exist already around the world that are grounded in financial materiality. Yet, to realise its potential role, the IFRS Foundation must plan and act with the utmost expediency.

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?

The answer to Q2 is secondary (though closely related) to the answers to Q1 and Q1a, because it is concerned primarily with the internal organization of the IFRS Foundation, rather than with the more important question of what role the Foundation should play in setting global sustainability standards. In this regard, we urge that the Foundation considers three organizational design questions in structuring its involvement:

- First, which approach would best enable coherence between existing IFRS and Type A standards for sustainability-related financial disclosure?
- Second, which approach would most quickly achieve internationally recognized legitimacy in setting Type A sustainability-related financial disclosure standards?
- Third, which approach would best enable expeditious setting of high-quality sustainability-related financial disclosure standards?

We offer two different approaches, which might be considered. We identify the respective strengths of each, implicitly also identifying the respective weaknesses. We note that either approach could in principle be consistent with maintaining the existing IFRS distinction between the financial statements and 'other financial reporting' (Management Commentary, Preface para 7). This distinction parallels those maintained elsewhere, for example in the U.S. MD&A, German Management Report and UK Strategic Report.

1. *Expanded International Accounting Standards Board,* perhaps renamed and relaunched as the International Financial Reporting Standards Board. This approach would:
    a. Minimize change in organizational structure
    b. Be viewed as a 'natural' extension of the IFRS Foundation's existing mandate
    c. Signal and reinforce that the IFRS Foundation has a single mission to generate financial reporting standards for the benefit of capital providers, including

    standards relating to both financial statements and sustainability-related financial disclosure
    d. Be viewed as consistent with or in the tradition of other IAS or IFRS that pertain primarily to disclosures, such as IAS 24 on Related Party Disclosure.
    e. Maintain direct oversight, by a single body, of alignment and consistency between financial statements and sustainability-related financial disclosures
    f. Rely for sustainability matter expertise upon specially-constituted bodies, constructed either as sub-committees of the IASB or as project working groups, the purpose of which would be similar in concept and function to (for example) the Insurance Working Group in the IASB's development of IFRS 17
2. *Sustainability Standards Board*. This is the IFRS Foundation's proposed approach. This approach would:
    a. Enable the construction of a separate board with appropriate experience and expertise in sustainability reporting
    b. Allow the IASB to continue to set accounting standards, without detracting from its agenda time and focus
    c. Allow an organizational distinction between standard-setting for financial statements and for sustainability-related financial disclosures, enabling such things as earmarked funding, and distinctive stakeholder relationships
    d. Allow the SSB to progress as its own pace, in particular to adopt a working practice of proceeding with great urgency over the next few years
    e. Recognize and signal that sustainability-related financial disclosure, while sharing financial materiality with financial statement information, requires specific expertise
    f. Recognize and signal that sustainability-related financial disclosure is a major project in its own right, requiring substantial board time and focus
    g. Maintain consistency with IFRS by means of a shared conceptual framework

Question 3: Do you have any comment or suggested additions on the requirements for success as listed in paragraph 31 (including on the requirement for achieving a sufficient level of funding and achieving the appropriate level of technical expertise)?

We agree broadly on the seven 'essential' requirements for success listed in paragraph 31. We would also add two further requirements. The first is to have a widely understood, realistic, and concretely itemized plan for how and when jurisdictions and companies can transition from their current, diverse situations. It is important not to understate the progress that has already been made towards the development of global sustainability reporting standards, even though progress in adoption has been very uneven across companies and jurisdictions. The second and

related requirement is to ‘do no harm’ to complementary initiatives to provide Type B reporting standards.

While it would, of course, be necessary to ‘achieve a sufficient level of global support,’ we would add that the Trustees should not require anything like consensus. As was the case with IFRS, it would be sufficient in the first instance to move ahead with a reasonable assumption that the standards would be adopted in at least some key markets (Camfferman and Zeff, 2015).

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?

Yes, the IFRS Foundation’s relationships with its stakeholders are critically important, not least because capital provider-oriented sustainability reporting standards would be a natural extension of its existing relationships with governments, regulators, capital providers, preparers and others. The strength of the IFRS Foundation’s relationship with IOSCO is a critically important case in point.

A new stakeholder group, which is likely to be important, is that which is concerned with the environmental and social impacts of corporate activity. Members of this group range from sustainability NGOs to the World Bank, and across United Nations bodies from the International Labour Organization to the Global Compact. These institutions are likely to be valuable sources of expertise on how and why sustainability impacts are material to capital providers.

Question 5: How could the IFRS Foundation best build upon and work with the existing initiatives in sustainability reporting to achieve further global consistency?

Several of the leading initiatives in sustainability reporting have committed to ‘work together towards comprehensive corporate reporting’ (IMP et al., 2020a). This includes an explicit public commitment to work together to harmonize frameworks and standards (Eccles, 2020). The recent merger of IIRC and SASB illustrates progress. While there is much here that remains to be determined and decided, the ‘open door’ is that the IFRS Foundation should build on the work of these initiatives in order that:

- first, there is effective transition from current practice; and
- second, and subsequently, best practice can be drawn from the expertise of each initiative, such that future standards represent the ‘best of the best’

We are encouraged by the recent statement from CDP, CDSB, GRI, IIRC, SASB and others, which provides the clearest statement to-date on both a commitment to work together and on a pathway to make this possible (IMP et al., 2020b).

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 most important work being done here is within the EU, including the NFRD and the EU Taxonomy. Just as the EU played a critical role in ensuring global endorsement of IFRS, so too it is essential for the IFRS Foundation and the EU to work together in the area of sustainability reporting. The EU's support would be invaluable in establishing the IFRS Foundation as the international standard-setter for (Type A) sustainability-related financial disclosure. And, given the IFRS Foundation's good working relations with the EU, alongside the EU's considerations on moving into non-financial reporting standard setting, a dovetailed division of labour between the IFRS Foundation (Type A) and the EU (Type B) would lead to an efficient and mutually beneficial outcome, in which both parties play to their respective mandates and areas of expertise.

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?

Yes. We support an initial focus on climate-related reporting, though we stress the importance of being clear on the rationale for this approach. Specifically, we identify three issues.

- *Priority*. Within the remit of the IFRS Foundation's role in providing material information to capital providers, climate-related reporting is a priority issue. Note the logical flow here. There is a priority information demand from capital providers, and therefore it is a priority issue for the IFRS Foundation. It is *not* instead the case that climate change has been imposed by the IFRS Foundation as the highest priority issue for society and, therefore, the priority for the IFRS standard-setting agenda. These different logical flows are very closely related, of course. Climate change is arguably the greatest issue of our time and, because the corporate sector is a major contributor to global warming, corporate transition to net zero is a major imperative for public policy. Associated with this, the corporate sector itself is greatly exposed to the effects of climate change, and its expected transition path to net zero affects capital providers' evaluation of financial risk and return. While sustainability reporting under standards issued by the IFRS Foundation would therefore align considerably with the public interest, the role of the Foundation in issuing those standards concerns capital provider materiality. This would

not preclude the IFRS Foundation's standards from usefully complementing Type B standards that focus on additional environmental and social impacts.

- *Practicality*. Climate-related reporting is among the most developed areas of sustainability reporting practice (e.g. GHG Protocol, CDP, CDSB, TCFD), making it an obvious foundation for an expeditious launch of sustainability-related financial disclosure standards.
- *Legitimacy*. Climate-related impacts have become increasingly relevant to enterprise value, and there is a high level of capital provider and intergovernmental agreement (e.g. via the 2015 Paris Agreement) on issues ranging from the presence of climate-related corporate risk and opportunity, to the transition to net-zero business model. On these grounds of consensus on financial materiality, reporting standard-setting on climate-related financial disclosure can legitimately be located within the IFRS Foundation We also note, however, that issues of climate change are not unique in this regard, and that (for example) other elements within the UN Sustainable Development Goals (SDGs) are also the basis of consensus on issues within a much broader set of sustainability goals, including for example longstanding international legal agreement on human rights. Therefore, expanding the scope of Type A sustainability reporting standards to also encompass those other areas that are financially material should not be put on the back burner for too long.

We stress that starting with climate-related issues does not downplay the urgency for the SSB of setting standards on other aspects of Type A environmental and social sustainability; it is instead simply a practical recognition that something must come first.

Question 8: Should an SSB have a focused definition of climate-related risk or consider broader environmental factors?

We are not persuaded of the need for 'a focused definition of climate-related risk.' One reason is that clarity over materiality is itself sufficient to determine the scope of Type A reporting standards. A second reason is that 'climate-related' is not easily defined, and attempts to 'pin it down' are unlikely to be productive. The same is true for 'sustainability'. Yet setting standards on specific issues that are 'climate-related' or 'sustainability-related' is not conditional upon tight definitions of those broad terms, in much the same way that 'financially material' disclosures can in general be determined on a case-by-case basis.

Question 9: Do you agree with the proposed approach to materiality in paragraph 50 that could be taken by the SSB?

The application of materiality in the IFRS Conceptual Framework focuses on the provision of information to capital providers. Jurisdiction-specific capital-market regimes generally see it this way too. The U.S. Supreme Court, for example, considers information material "if there is a substantial likelihood that the disclosure of the omitted fact would have been viewed by a reasonable investor as having significantly altered the total mix of information made available" (TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 1976).

Material information can be provided by means of general-purpose financial statements and disclosure standards, including for sustainability-related disclosures that are relevant to the 'performance and long-term health of the reporting entity' and that could therefore 'influence the decisions of investors' (CP, para. 46). These sustainability disclosures are increasingly important to investors in understanding a reporting entity's ongoing capacity to sustain financial performance, and so to generate enterprise value, especially over the long term (Eccles et al., 2014). In this regard, they are relevant to financial risk and return, even though they typically concern externalities arising from the reporting entity's current business activities, because they affect expectations that current impacts will by some means be internalized in the future (Unerman et al., 2018; Christensen et al., 2019).

The notion of 'double materiality' recognises that the interests of capital providers could differ from those of society at large. With respect to the latter, material information from the reporting entity, if omitted, misstated or obscured, could affect the decision-making of *any* stakeholder. Instead of financial risk and return being the evaluative criterion here, it is instead broadened, for example to the impact of the company on the achievement of the Sustainable Development Goals (Adams et al., 2020).

In our view, the IFRS Foundation should declare itself responsible for sustainability reporting that adopts a single materiality focus (Type A).) In so doing, the IFRS Foundation should continuously engage with any future standard-setters for Type B reporting, since information that falls at one time under Type B can quickly move to Type A, as when societal impacts become material to investors.

Single (capital provider) materiality is consistent with, and therefore arguably a fulfilment of, the existing mission of the IFRS Foundation. The same is not true for double materiality, which would represent a significant extension of, and departure from, the IFRS Foundation's current remit. Moreover, extension to double materiality would face the following challenges.

- *Legitimacy:* The appropriate mandate for public policy is held by democratically legitimized governments, and not by a private standard-setting body. It is not for the IFRS Foundation to determine what is in the public interest. While the IFRS Foundation is recognised globally as a standard setter for capital market information, it is not currently recognised as a legitimate authority for public policy.
- *Heterogeneous information demand:* Capital providers' information needs can be regarded as relatively homogeneous across global capital markets, while there is likely to be heterogeneity in national sustainability policy and legislation. Such heterogeneity implies geographic variation in public-interest sustainability standards, which would make it inherently problematic for the IFRS Foundation to set global standards. Instead, the IFRS Foundation can provide 'baseline' global financial reporting, onto which individual jurisdictions can add reporting requirements to meet their specific needs.
- *Focus.* A single set of standards, set with the dual purpose of informing both capital providers and broader society, could fall short of the specific information demands of either of those constituencies. Viewed from a capital providers' perspective, information is best provided by a coherent system of financial reporting, in which both financial statements and sustainability-related financial disclosure are designed with a single audience in mind, and based upon a single lens of financial materiality.
- *Efficiency and expediency:* There is a specific, capital provider-oriented demand for coherent corporate reporting, comprising both financial standards and sustainability-related financial disclosure standards. The IASB already provides the former, and it is well placed to complement this with the latter. Capital provider-oriented standards (Type A) are therefore the obvious organizational priority for the IFRS Foundation in terms of agenda and workflow. Yet the time and effort required to develop sustainability reporting standards should not be underestimated For this reason, it would be much better for the IFRS Foundation to focus on providing material information to capital providers, and for governments and others to focus on providing material information in the public interest (Mohin and Eccles, 2020).

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?

Issues of audit and enforcement are critical in practice for the effectiveness of mandatory standards, making consideration of these issues very important in guiding the work of the IFRS Foundation. While the question of whether or not information should be audited is not itself a matter for the IFRS Foundation to decide, it is reasonable to presume essentially the same distinction as holds for IFRS, where information included in the financial statements and notes

are relatively straightforward to audit under well-established procedures, but additional disclosures of a more subjective and/or forward-looking nature are more challenging. To illustrate, the reporting of carbon emissions is amenable to the same degree of audit rigour as amounts recognised in the financial statements, given the long-established greenhouse gas protocol (GHG, 2004), while more general disclosures regarding governance and risk management are not yet auditable in the same way. Moreover, if sustainability disclosures are going to reach the intended purpose, audit approaches and requirements as well as enforcement mechanisms will have to evolve (quickly) along with the related reporting requirements. It will not be acceptable to judge auditability solely based on what audit firms are currently willing and able to do, although it might be expedient to initially maintain a degree of separation between auditing the financial statement and auditing sustainability-related financial disclosure standards, which would avoid that progress in expanding sustainability disclosures is retarded by auditability restrictions applicable in an IFRS context.

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