

Take5

for business

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IFRS Sustainability Disclosure Standards

Preparing for the new IFRS S1
and IFRS S2

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IFRS Sustainability Disclosure Standards

The International Sustainability Standards Board (ISSB) published, two exposure drafts (EDs) on International Financial Reporting Standards (IFRS) Sustainability Disclosure Standards in March 2022, namely:

- ▶ General Requirements for Disclosure of Sustainability-related Financial Information (IFRS S1)
- ▶ Climate-related Disclosures (IFRS S2)
 - ▶ Considering the ISSB's aimed issuance date by end-2022, these two standards are expected to form a baseline of sustainability disclosures designed to meet the information needs of investors and stakeholders when assessing enterprise value.

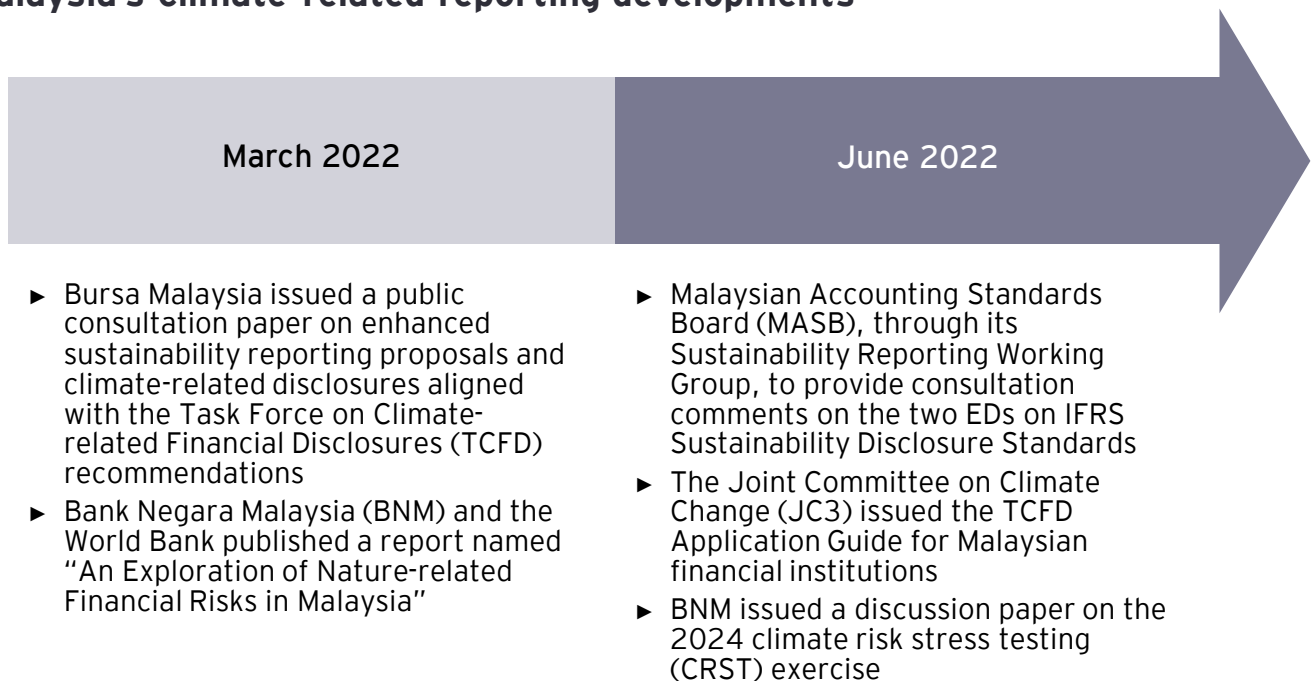
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In challenging global conditions including those related to climate risks, companies need to differentiate their value propositions with strategic transformation measures and insightful reporting to foster long-term sustainability in alignment with the goals of both the investors and stakeholders.



Dato' Abdul Rauf Rashid
Malaysia Managing Partner
Ernst & Young PLT

Malaysia's climate-related reporting developments



Sources:

- ▶ Snapshot - Exposure Drafts IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information and IFRS S2 Climate-related Disclosures, IFRS Foundation, March 2022
- ▶ IFRS Sustainability Developments Issue 1: ISSB publishes first two EDs on sustainability disclosure requirements, EY, April 2022
- ▶ EY research

Objective: To require entities to provide all material information about the entity's exposure to sustainability-related risks and opportunities that is useful to users of general-purpose financial reporting in making decisions about whether to provide economic resources to the entity.

The proposed IFRS S1 sets out the core content for a complete set of sustainability-related financial disclosures, establishing a comprehensive baseline of sustainability-related financial information.

The proposed standards require an entity:

- ▶ To disclose a complete, neutral and accurate depiction of all significant sustainability-related risks and opportunities
- ▶ To disclose information relevant to the assessment of enterprise value, including the entity's impact and dependencies on people, planet and economy
- ▶ To adopt a consistent approach for the disclosure of information about significant sustainability-related risks and opportunities based on governance, strategy, risk management, aside from metrics and targets
- ▶ To refer to relevant IFRS Sustainability Disclosure Standards to identify disclosures, including metrics, about a significant sustainability-related risk or opportunity
 - ▶ In the absence of the Sustainability Disclosure Standard that applies specifically to a sustainability matter, management is required to use judgement to identify the relevant topics included in the industry-based Sustainability Accounting Standard Board (SASB) standards and/or those announced by other standard-setting bodies, to the extent that they do not conflict with the IFRS Sustainability requirements.

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Sustainability reporting is not a compliance programme - it collects, analyses and interprets data to provide both internal and external stakeholders with useful information on sustainability performance to enable more informed decision-making, including that of an entity's strategic direction.



Ong Chee Wai
Assurance Managing Partner
Ernst & Young PLT

In brief, the S1 includes proposed requirements that an entity must disclose comparative information, identify the related financial statements and provide sustainability-related financial information at the same time as the financial statements. Consequently, the S1 serves a similar role for sustainability financial-related disclosures as the ISSB Conceptual Framework serves for general purpose financial statements prepared in accordance with the IFRS accounting standards.

Sources:

- ▶ *Snapshot – Exposure Drafts IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information and IFRS S2 Climate-related Disclosures*, IFRS Foundation, March 2022
- ▶ *IFRS Sustainability Developments Issue 1: ISSB publishes the first two EDs on sustainability disclosure requirements*, EY, April 2022

S2 IFRS S2: Climate-related Disclosures

Objective: To require entities to provide information about their exposure to climate-related risks and opportunities. The proposed standard sets out the requirements for the identification, measurement and disclosure of climate-related financial information.

The proposed IFRS 2 sets out the requirements for the identification, measurement and disclosure of climate-related physical and transition risks and opportunities, including disclosing information based on the Taskforce for Climate-related Financial Disclosures (TCFD) recommendations:

Governance

- ▶ Disclosure of governance processes, controls and procedures the entity uses to monitor and manage climate-related risks and opportunities
- ▶ Disclosure on the description of the governance body (board or committee), with oversight of the climate-related risks and opportunities, including:
 - ▶ What are the terms of reference for the company's climate-monitoring governance body?
 - ▶ What is the management's role in assessing and managing climate-related risks and opportunities?
 - ▶ How does the company ensure that it has people with the right skills and competencies available to oversee its strategies?

Strategy

- ▶ The climate-related risks and opportunities that could enhance, threaten or change the entity's business model and strategy over the short, medium and long term, include:
 - ▶ How information about climate-related risks and opportunities informs the management's strategy and decision making
 - ▶ The current and anticipated effects of climate-related risks and opportunities on its business model
 - ▶ The effects of climate-related risks and opportunities that could reasonably be expected to impact the entity's business model, strategy and cash flows including its access to finance and its cost of capital, over the short, medium or long term
 - ▶ The resilience of the entity's strategies (including its business model) to climate-related risks

Climate-related risks and opportunities

- ▶ **Physical risks:** the increased severity of extreme weather events, putting the company's assets at risk or disrupting its supply chain. Meanwhile, chronic physical risks include rising sea levels or rising mean temperatures, which may impact the company's strategy.
- ▶ **Transition risks:** associated with company's transition to a lower-carbon economy, **including policy or legal, market, technology and reputation.**

Sources:

- ▶ *Snapshot - Exposure Drafts IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information and IFRS S2 Climate-related Disclosures*, IFRS Foundation, March 2022
- ▶ *Exposure Draft - IFRS S2 Climate-related Disclosures*, IFRS Foundation, March 2022
- ▶ *IFRS Sustainability Developments Issue 1: ISSB publishes the first two EDs on sustainability disclosure requirements*, EY, April 2022



Risk management

- ▶ The processes used to identify, assess, manage and mitigate climate-related risks and opportunities (R&O), including:
 - ▶ Assessing the likelihood and effects associated with such risks (e.g., qualitative factors, quantitative thresholds)
 - ▶ Prioritizing climate-related risks relative to other types of risks, in an entity's risk management approach including its use of risk-assessment tools (e.g., science-based risk-assessment tools)
 - ▶ The input parameters used (e.g., data sources, scope of operations covered and assumption details)
 - ▶ Identifying changes in processes used compared to the prior reporting period
- ▶ The extent to which and how climate-related R&O identification, assessment and management processes are integrated into the entity's overall risk management or overall management process

Metrics and targets

- ▶ To manage and monitor the entity's performance and outcome in relation to climate-related R&O including measures that support the qualitative disclosures and targets that an entity uses to measure its performance goals
- ▶ Identify, select and disclose climate-related information on:
 - ▶ cross-industry metrics: Greenhouse gas (GHG) emissions, transition risks, physical risks, climate-related opportunities, capital deployment, internal carbon prices and remuneration
 - ▶ industry-specific metrics: disclosure of topics relevant and associated with specific business models, economic activities and other common features that characterize participation in an industry
- ▶ Consider the relationship of these amounts with the amounts recognized and disclosed in the accompanying financial statements. As an example, chemical producers would consider safe waste management as a key metric.

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When assessing the uncertainty associated with an entity's ability to continue as a going concern, climate risk impacts beyond those expected to materialize in the short term, should be considered.



Arina Kok
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Sources:

- ▶ *Snapshot - Exposure Drafts IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information and IFRS S2 Climate-related Disclosures*, IFRS Foundation, March 2022
- ▶ *Exposure Draft - IFRS S2 Climate-related Disclosures*, IFRS Foundation, March 2022
- ▶ *IFRS Sustainability Developments Issue 1: ISSB publishes the first two EDs on sustainability disclosure requirements*, EY, April 2022

What are the next steps?

To prepare for the upcoming sustainability standards requirement, companies can consider the following actions:

1 Identify the reporting metrics, targets

- ▶ Chief Financial Officers (CFOs) and finance teams must prepare for reporting across a range of environmental, social and governance (ESG) topics including the disclosure of company strategies, and risk management actions to achieve a more sustainable performance over the long-term.
- ▶ Identifying the metrics and targets most relevant to their sector, strategy and stakeholders, including developing the capacity to report on those metrics.
- ▶ Ensuring that the relevant functions within the company are well prepared to produce the necessary data outputs.

2 Put ESG and sustainability reporting on the Board's agenda

- ▶ Boards need to understand how ESG investing are impacting access to capital and relationships with investors. In attracting long-term investors, it is integral for shareholders and investors to be sufficiently informed.
- ▶ Boards need to understand the private market and regulatory initiatives, monitor developments from the major jurisdictions, including standard-setting bodies, and be aware of how ESG rating agencies and data providers perceive their company.
- ▶ Boards should supervise a materiality assessment and support the integration of ESG within the broader strategy and enterprise risk management (ERM).

3 Integrate the finance function

- ▶ CFOs and financial controllers can instill discipline into non-financial reporting processes and controls, based on their experience and knowledge of leading practices to support sustainability and ESG reporting systems.
- ▶ The finance function can assist in establishing effective governance and obtaining independent assurance over non-financial processes, controls and data outputs, which are crucial in building trust and transparency with stakeholders.

4 Contribute to the standard setting process

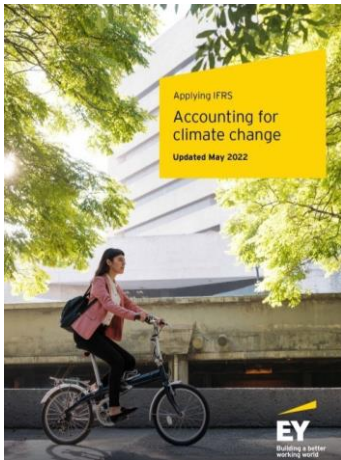
- ▶ Most leading companies have acknowledged that ESG issues are critical to the sustainable development and have embedded those issues into their strategy for long-term value creation. They see an opportunity to be part of the process, learn from experience and not wait for regulators to mandate disclosures.
- ▶ Through adequate disclosure practices, companies can increase their contribution and credibility in the standard setting discussions.

5 Seek assurance to build trust in sustainability reporting

- ▶ Companies should ensure that their sustainability reporting has robust processes and controls with a supporting audit trail, similar to its financial reporting.
- ▶ Companies can begin focusing on audit preparedness to build stakeholder confidence and comply with regulatory requirements.

Source:
The future of sustainability reporting standards, EY, June 2021

EY thought leadership



Accounting for climate change
May 2022



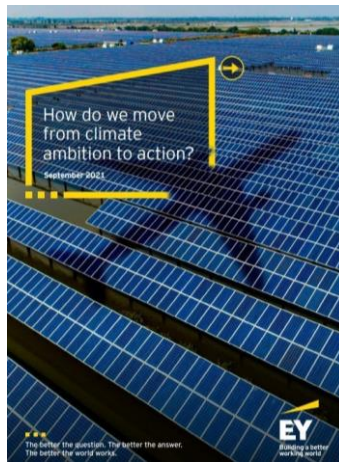
IFRS Update of standards and interpretation
March 2022



Trending: Sustainable responsible investment in Malaysia and the Region
February 2022



If climate change is everybody's business, how can all benefit from green leadership by the few?
October 2021



How do we move from climate ambition to action?
September 2021



The Evolving Non-Financial Reporting Landscape
August 2021



How can boards strengthen governance to accelerate their ESG journeys?
February 2022



The future of sustainability reporting standards
June 2021



Setting the ESG agenda to achieve sustainable long-term value
June 2021

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IFRS resource tracker

- ▶ *IFRS Sustainability Developments Issue 1: ISSB publishes first two EDs on sustainability disclosure requirements*, EY, April 2022
- ▶ [Exposure Draft] *IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information*, IFRS Foundation, March 2022
- ▶ [Exposure Draft] *Illustrative Guidance on IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information*, IFRS Foundation, March 2022
- ▶ [Exposure Draft] *IFRS S2 Climate-related Disclosures*, IFRS Foundation, March 2022
- ▶ [Exposure Draft] *Illustrative Guidance on IFRS S2 Climate-related Disclosures*, IFRS Foundation, March 2022
- ▶ [Exposure Draft] *Snapshot IFRS Sustainability Disclosure Standards*, IFRS Foundation, March 2022