Submission: IFRS Foundation Consultation Paper on Sustainability Reporting

Submission details[1]

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Response

The Guardians of New Zealand Superannuation ('Guardians') is pleased to have the opportunity to comment on the Consultation Paper on Sustainability Reporting ('Paper') published by the Trustees of the IFRS Foundation ('Foundation').

As a Crown entity, the Guardians manages the New Zealand Superannuation Fund to help pay for the increased cost of universal superannuation entitlements in the future. Information with respect to our approach to investing is available *here*.

As a long-term investor, we are committed to active ownership and the promotion of good governance for the overall health of the capital markets. In our view, good governance is an indispensable prerequisite for successful company performance over the long-term. In particular, we expect that Boards and executive teams are active in considering how to account for the changing risk profiles of the companies they are responsible for, including sustainability-related risk.

In line with the Principles of Responsible Investment, environmental, social and governance (ESG)-related disclosures made by companies are essential to the Guardians RI Framework. Such investee company disclosure helps unlock the information we need to factor ESG considerations into our investment strategies and ownership practices. Conversely, the lack of disclosure can lead to data paucity, anomalies and approximations in ESG reporting.

[1] RI > Communications > Submissions

For the purposes of this consultation, we see sustainability reporting to encompass ESG disclosure.

As an institutional investor, we are encouraged by the Paper's clear acknowledgement of the extensive body of relevant work achieved to date, the many challenges facing the proposed IFRS sustainability initiative, and some of the critical requirements for success.

Rather than reiterate the Paper's salient points, the Guardians response includes a series of observations and suggestions in relation to each of the consultation questions.

In summary, the Guardians:

1. supports the need for the integration of internationally-recognised, consistent standards for sustainability-related reporting into IFRS.
2. acknowledges the Foundation's global reach and vast experience with global reporting standards, and see the Trustees as well-placed to take a central role in the proposed endeavour.
3. proposes that the Foundation commission a time-bound, multi-stakeholder task force to establish a framework and protocols for a new IFRS sustainability standard - *rather than form a new, separate Sustainability Standards Board (SSB).*
4. suggests the Foundation's focus should be on integrating sustainability standards directly into IFRS. The task force can determine the core ESG information sets and performance metrics that are 'IFRS-ready', and establish protocols to add to these over time.
5. believes a broader range of sustainability-related standards should sit outside IFRS. Other bodies are better-placed to cover the evolution in complementary, extended ESG reporting for less well-established/evidenced ESG criteria.
6. suggests harmonising with existing sustainable reporting taxonomies and legislation to provide a degree of consistency in core terminology and protocols.
7. suggests seeking to coordinate with the Financial Accounting Standards Board (FASB) to co-develop, align or benchmark the new sustainability standards with the generally accepted accounting practices (GAAP) of the USA.
8. believes that ESG considerations, including climate change are material to long-term risk and return.
9. believes the Foundation's focus should be on integrated sustainability reporting standards - within which climate-considerations are an essential component – *rather than pursuing a "climate-first" approach.*

***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?*

We recognise the need for internationally-recognised, sustainability-related reporting standards to improve the transparency, accuracy, consistency and comparability of financial and non-financial risk disclosure across a range of sectors and jurisdictions.

We believe the IFRS Foundation is uniquely positioned to have the largest impact on improving sustainability reporting, by integrating appropriate standards directly into IFRS - and that the need for this is urgent. Setting up a sustainability standards board (SSB) that is separate to the International Accounting Standards Board (IASB) would, in our opinion, be less impactful and fall outside the Foundation's natural role.

Whilst this is an ambitious undertaking, we acknowledge the Foundation's global reach and vast experience of developing, harmonising and implementing iterations of global reporting standards, and see the Trustees as well-placed to take a central role in such an endeavour.

In terms of the scope, reach and nature of the proposed sustainability standards, we would like to raise a few points for the Foundation's consideration, as follows:

a) Given the well-reported challenges of developing robust standards across a wide range of sustainability-related criteria with varying levels of evidence/rigour, we suggest the Foundation pursue a narrow focus for this initiative.

b) To this end, the Foundation could commission a multi-stakeholder task force to establish *sustainability reporting standards* comprising 'IFRS-ready' *core ESG criteria*[2] that satisfy the IASB due process.

c) The Foundation/IASB would determine the thresholds and protocols for IFRS inclusion of new sustainability-related/ESG criteria in the IFRS standard over time.

d) This would require working with other ESG reporting bodies including the "group of five" identified in the Paper. Protocols may need to evolve to accommodate this dynamic.

e) Overall, this approach would: focus and streamline a process whereby 'IFRS-ready' ESG criteria can be included in mandatory reporting under IFRS; establish a mechanism for other ESG criteria to be subsequently considered/included; maximise coherence, quality and synergies with existing non-financial IFRS standards; deliver better, more timely information to investors and report users; and more closely align

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[2] We note that there are precedents to draw on: the WEF (2020) has consulted widely in identifying a set of *'Core metrics'*, defined as: '…more-established or critically important…primarily quantitative…metrics, for which information is already being reported by many firms (albeit often in different formats)'. Furthermore, SASB characterises robust sustainability information around metrics that are: Material; Comparable; Consistent; Reliable, and Connected (to information in financial statements).

with the current, core mission of the IFRS Foundation (a key stated requirement for success).

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?

We do not consider the proposed establishment of a new, separate Sustainability Standards Board (SSB) to be the most effective, enduring approach to elevating sustainability disclosure standards under IFRS. A separate SSB may:

- Risk compromising the current core mission of the Foundation if a disconnect emerges between the IASB and the proposed SSB.
- Lead to duplication of effort and additional bureaucracy in the elaboration and implementation of new standards.
- Risk the SSB and/or new sustainability standards – in substance or perception – being regarded as secondary or junior to the IASB/existing IFRS standards; both within the Foundation and/or with external parties.

Rather, the Guardians proposes that the Foundation considers co-commissioning a time-limited *task force*.[3] Such a task force would:

- Leverage the successful experience of the other key sustainability and standards initiatives referenced in the Paper (e.g. TCFD, VRF (formerly SASB/IIRC), GRI, Corporate Reporting Dialogue (CRD), etc.) to streamline consultation on, and implementation of the new/adapted IFRS sustainability standards.
- Retain the technical expertise, institutional knowledge and networks of current or recent representatives of related initiatives, through their inclusion in the task force.[4]
- Facilitate inclusion of members who may not otherwise be able to join a permanent SSB-like structure under the Foundation Trustees, including representatives from the Financial Accounting Standards Board (FASB), CFA, FSB, investor community, etc.
- Represent a distinct, time-bound body to engender a sense of urgency in the drive towards identification, adoption and integration of a sustainability standard.
- Be wound down once an enduring mechanism for ESG inclusion in financial and non-financial disclosure is established under IASB (and potentially GAAP).

[3] For example, the '*Task force for Integrated Sustainability-related Disclosure (TISD)'*
[4] Arguably, it was the engagement of experienced, widely respected, high profile advocates in the TCFD (an initiative of the Financial Stability Board) that helped the recommendations garner serious global support

Beyond the above comments, we defer to the Foundation in determining best fit internal governance arrangements for supporting this important initiative within the organisation's three-tier structure.

Question 3: Do you have any comment or suggested additions on the requirements for success?

We see the seven requirements for success outlined in the Paper as a sound starting point, although further elaboration of the finer details, protocols and practicalities which underpin each will be crucial. In addition, the Foundation/task force might consider the following:

- Any IFRS-adopted sustainability standards should be subject to formal standard-setting due process required for new standards/criteria under the IASB.
- The Foundation should ensure suitable sustainability skill sets are developed and employed within the IASB/Trustees.
- The perspectives of both the report preparer (companies) and user communities (including investors, lenders, etc.) should be fully engaged from the outset.

Question 4, 5 and 6: How could the IFRS Foundation best build upon and work with existing initiatives in sustainability reporting to achieve further global consistency? 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 Paper references several well-established reporting initiatives offering a range of sustainability-related standards and reporting protocols.[5] These reporting organisations are coordinating constructively with each other to build a comprehensive corporate reporting system for ESG-related data and information. The Paper further recognises the challenge in effectively collaborating and leveraging these separate initiatives, without unwittingly reinventing, undermining or duplicating their collective achievements.

We refer to our response to Question 1 here, in which we recommend an integrated sustainability reporting standard and protocols to address the challenge of finding an effective dynamic between existing IFRS standards and existing/emerging sustainability reporting standards.

See also our response to Question 2, in which we propose the Foundation considers commissioning a multi-stakeholder task force – comprising members from a range of existing initiatives – rather than a new SSB.

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[5] In particular, the work of the Climate Disclosure Project (CDP), the Climate Disclosure Standards Board (CDSB), the Global Reporting Initiative (GRI) and the International Integrated Reporting Council (IIRC) / Sustainability Accounting Standards Boards (SASB) – now amalgamated as the Value Reporting Foundation (VRF)

Furthermore, in terms of seeking to aid the adoption and consistent application of IFRS standards globally, we propose the Foundation consider:

- Seeking to co-ordinate with the FASB to co-develop, align or benchmark new sustainability standards with the USA to avoid divergence between the two bodies. However, this should not be a pre-requisite for, or unnecessarily delay, the IFRS initiative.
- Harmonising with existing sustainability reporting initiatives where feasible, to provide a degree of consistency in core terminology and protocols, whilst allowing for some flexibility for preparers/users to respect their regional/national norms.

Question 7 and 8: 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? Should an SSB have a focused definition of climate-related risks or consider broader environmental factors?

We support the Foundation focusing on the development of an integrated sustainability reporting framework/standards, within which climate-considerations are an essential component – rather than pursue an explicit climate-first approach.

As the World Economic Forum's 2020 global risks landscape study reported,[6] society faces a broad range of interrelated sustainability challenges. We recognise the critical nature and urgency of the global climate change challenge, but favour an integrated approach, recognising that:

- Climate change risk is heavily intertwined with other aspects of sustainability. Non-climatic factors are often equal or greater drivers of risk, than isolated climate-related factors.
- Some sustainability-related standards (e.g. air pollution) effectively address non-climatic criteria (e.g. human health), in addition to climate change-related indicators.
- Other (non-climate) sustainability-related criteria are equally 'IFRS-ready' in terms of their robust evidence base, verifiability, comparability, etc. These include key health and safety or human resource metrics.
- Integrated standards would support holistic, efficient transitions towards enduring sustainable business/investment strategies.
- We support IFRS incorporating and/or referencing existing climate-related risk reporting initiatives such as the TCFD which are seeing increasing rates of adoption and corresponding action.

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[6] World Economic Forum - Global Risks Report 2020

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

Significant negative ESG impacts are becoming increasingly material to companies' operations and long-term performance, at the same time as positive impacts/outcomes are being embedded into company strategies.

We see the materiality of ESG considerations as embedded in the long-term value of a company, rather than these giving rise to a 'dual materiality'. There are some issues, such as climate change and supply chain management, that are complex or require a multi-stakeholder approach to manage.

The Guardians investment belief holds that ESG considerations, including climate change, are fundamental to long-term risk and return. Investors are increasingly interested in multiple dimensions of materiality to guide investment decision-making, engagement and voting.

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?

We note the current challenges of working with new, emerging, forward-looking and/or outcome-based ESG data and suggest that any sustainability-related information to be included in financial statements would need careful consideration by IFRS in relation to the degree of objective assurance applicable/achievable.

It seems reasonable to assume that, *where it is practicable,* core ESG criteria incorporated into IFRS should be subject to formal assurance. In some cases, limited assurance may be more appropriate. We note the work of the International Auditing and Assurance Standards Board (IAASB) on their Extended External Reporting (EER) Assurance project as a key input to this discussion.

The task force will need to explore this topic further by drawing on the experience of other bodies. Given the wide range of ESG metrics, there will be those that are more material to the business and more important to be assured than others.

We are of the view that the industry will need a few years of practice – the CFA, report preparers, report assurers and report users will all need time to understand and implement any new sustainability framework, standards and criteria. This should be factored into the final recommendations of the task force.