

Sustainability Reporting

– The BIG three proposals –

BCCG Expert Group Meeting
Berlin, 15 May 2023

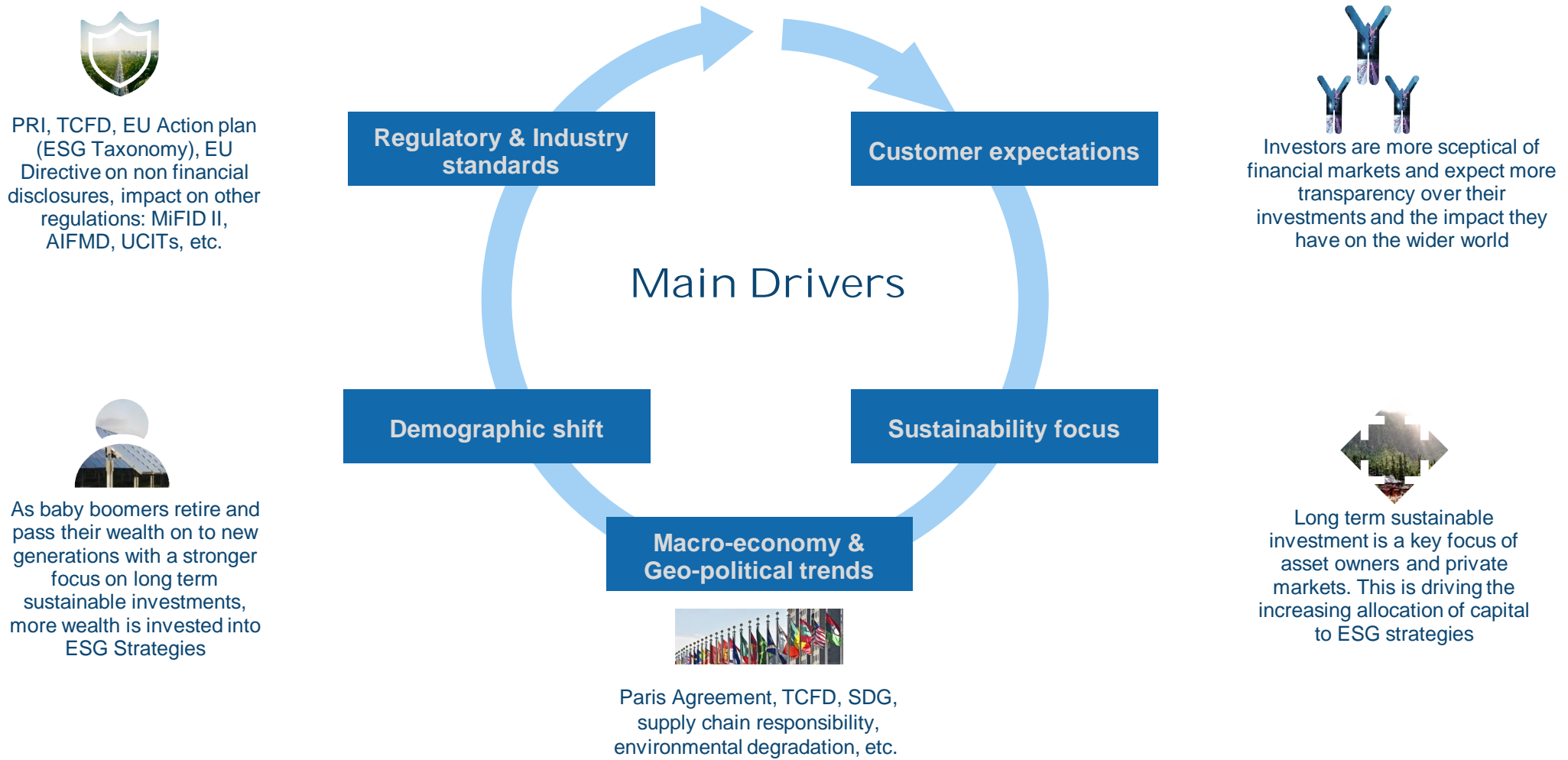
WP/ CPA Prof. Dr. Sven Hayn

Agenda

From voluntary to mandatory Sustainability Reporting

- Corporate Reporting
- The BIG three proposals for standardised sustainability disclosures
- Interoperability and Building Blocks

Beyond financial reporting ... main drivers



Corporate Reporting

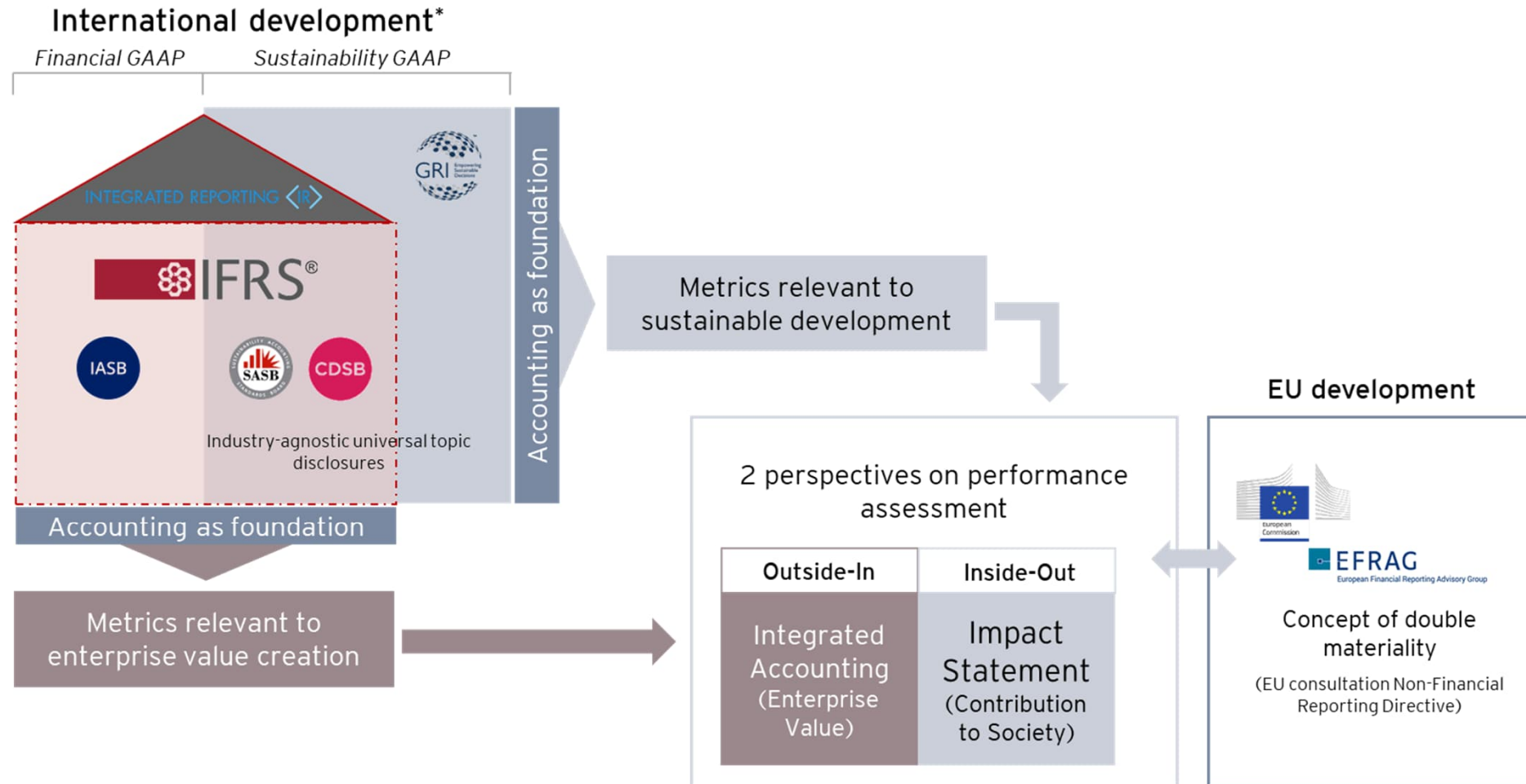
Financial Reporting + ESG Reporting =
Corporate Reporting

//
Accounting is
the language of business

//
Corporate Reporting is
the license to operate

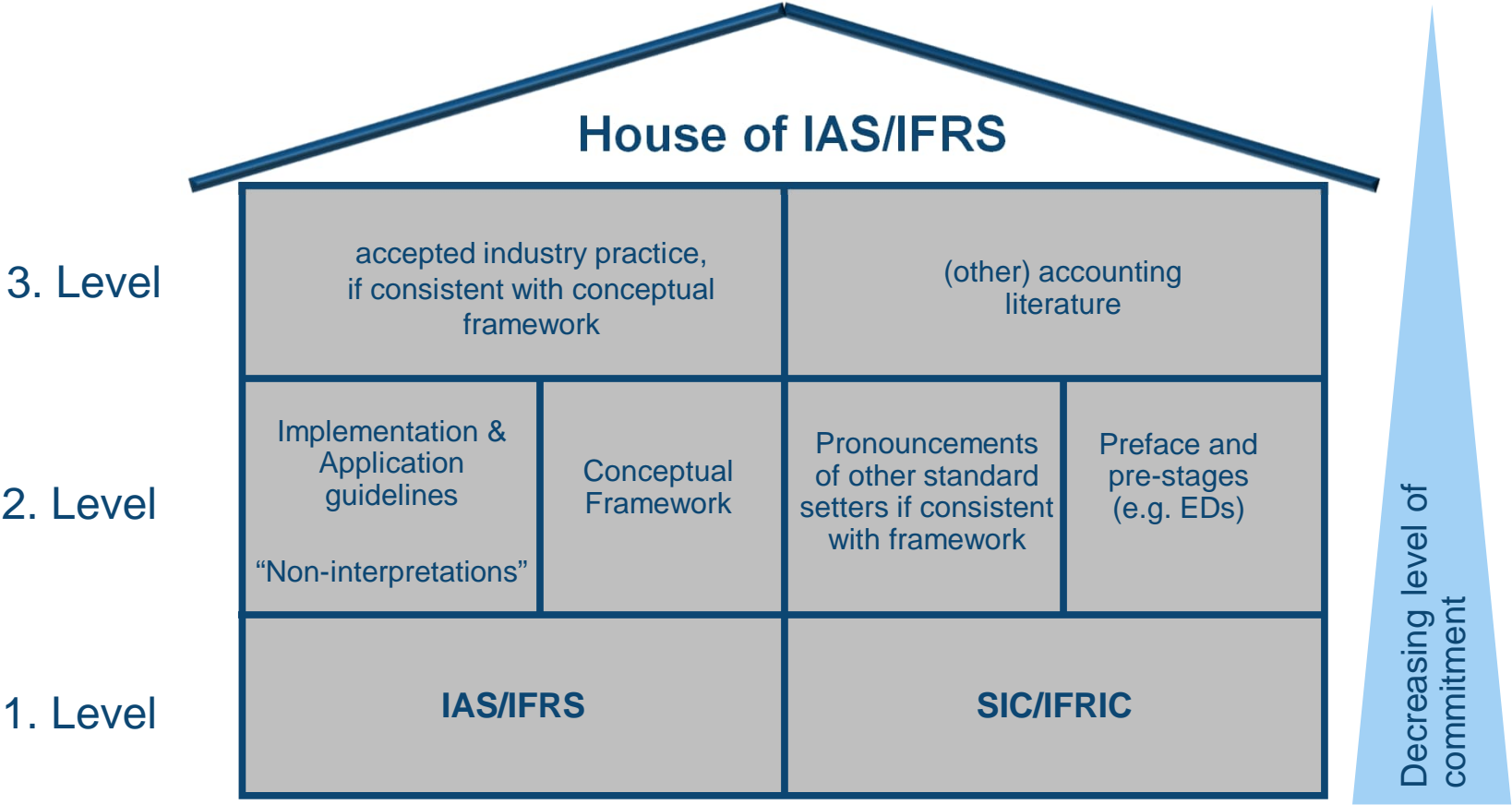


A comprehensive reporting framework ...?



Source: IFRS Foundation

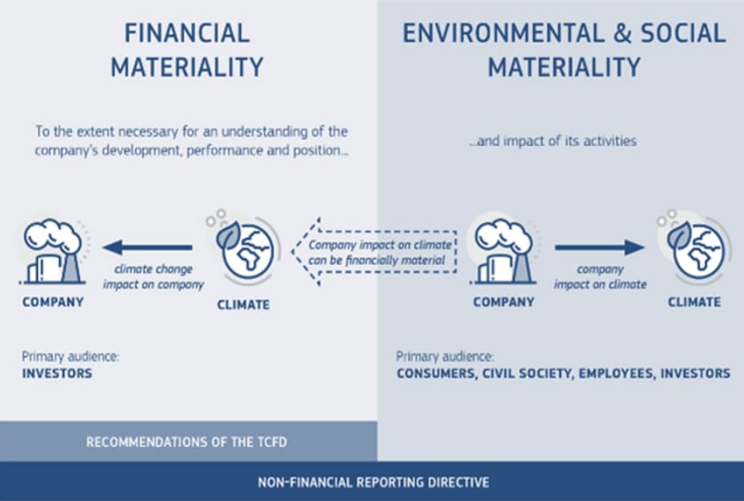
Recap: Hierarchy of IFRSs (and GAAP)



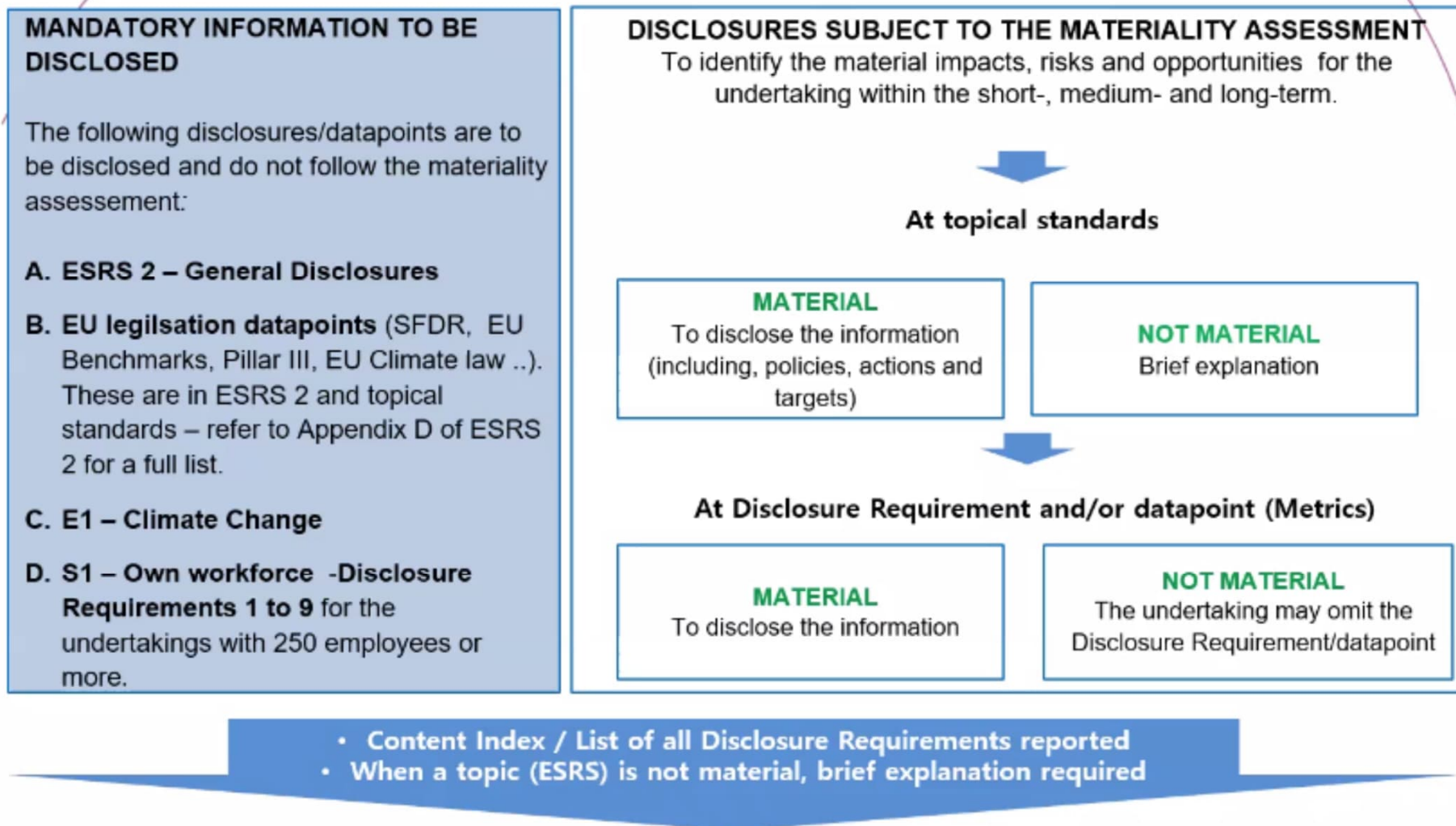
Recap: IFRS Conceptual Framework – Qualitative characteristics

Objective	To provide financial information that is useful to users in making decisions relating to providing resources to the entity			
Fundamental qualitative characteristics	Relevance	Materiality	Faithful representation	
	<ul style="list-style-type: none"> ▶ information is relevant if it is capable of making a difference to the decisions made by users ▶ financial information is capable of making a difference in decisions if it has predictive value or confirmatory value 	<ul style="list-style-type: none"> ▶ information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial reports ▶ materiality is an entity-specific aspect of relevance ▶ no uniform quantitative 	<ul style="list-style-type: none"> ▶ information must faithfully represent the substance of what it purports to represent ▶ a faithful representation is, to the maximum extent possible, complete, neutral and free from error ▶ a faithful representation is affected by level of measurement uncertainty 	
Enhancing characteristics	Comparability	Verifiability	Timeliness	Understandability
Cost benefit constraint	The benefit of providing the information needs to justify the cost of providing and using the information			

Applied materiality

EU (CSRD/ ESRS)	IFRS	SEC
<p>Double materiality</p> <ul style="list-style-type: none"> ➤ Financial materiality ➤ Impact materiality 	<p>Financial materiality</p>	<p>Financial materiality</p>
	<p>The ISSB tentatively agreed in October 2022</p> <ul style="list-style-type: none"> ➤ that the purpose of draft S1 is to require entities to meet the information needs of the primary users of general purpose financial reporting; ➤ ‘material’ in draft S1 shares the same definition as that used in IFRS Accounting Standards; ➤ the definitions of ‘value chain’ and ‘reporting entity’ as proposed in draft S1 should remain unchanged; ➤ further to amend draft S1 by removing the definition of ‘enterprise value’ and the words ‘to assess enterprise value’ from the objective and description of materiality ...; and ➤ to remove the word ‘significant’ from the proposed requirements to describe which sustainability risks and opportunities an entity would be required to disclose ... 	<p><i>“an item of information as material if there is any substantial likelihood that a reasonable investor would consider the information important in deciding how to vote or make an investment decision”</i> (U.S. Supreme Court Justice)</p> <p><i>“expected to influence an investment decision that users make on the basis of their assessment of future enterprise value”</i> (SASB definition of materiality)</p>

*subject to
current redeliberations*



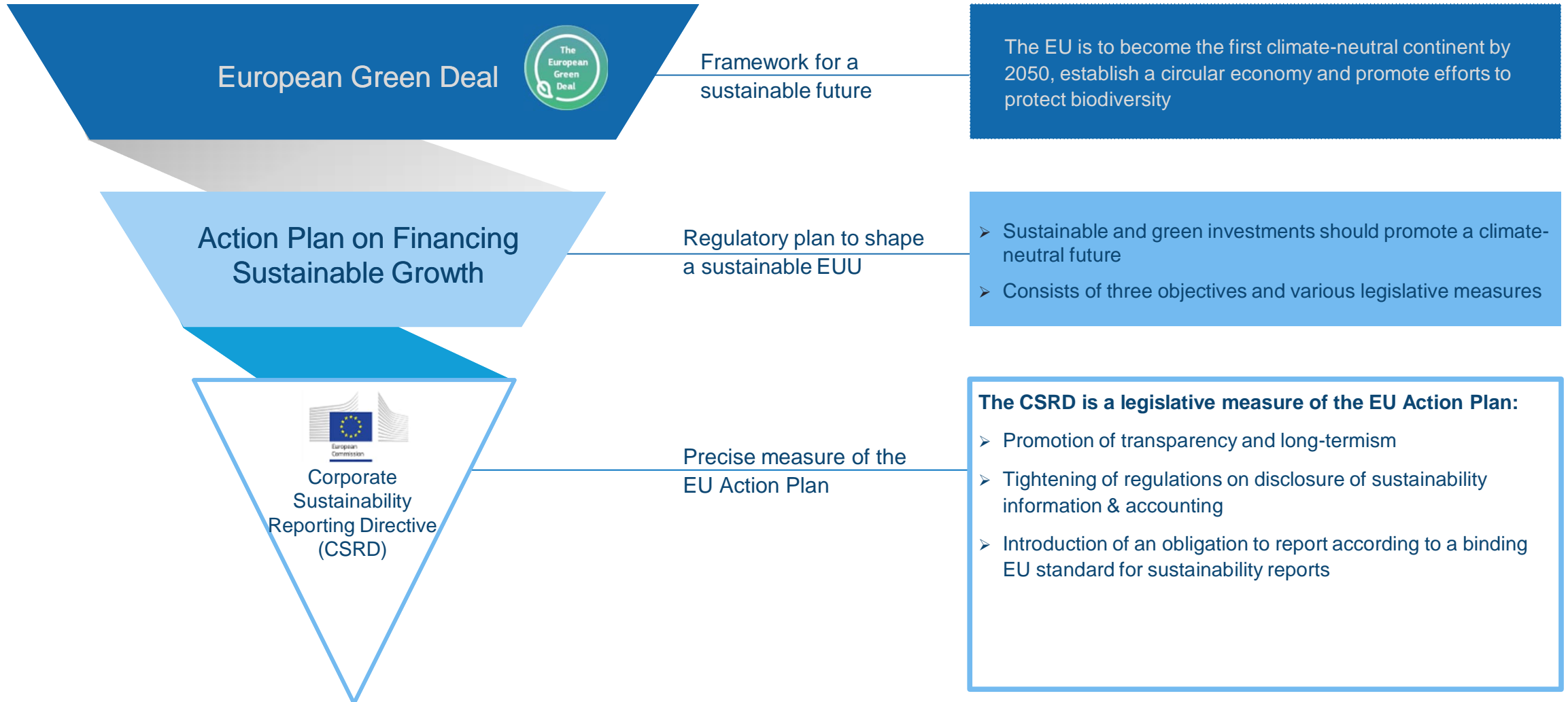
Source: EFRAG

Jurisdictions and Major Standardsetters

(simplified presentation)

Reporting	Financial Statements	Capital Markets	ESG
European Union	<ul style="list-style-type: none"> • EU-Directives • EU-Regulations • IFRS Endorsement with EU safeguards • Differentiated application for PIE and Non-PIE entities and size criteria (mixed model) 	<ul style="list-style-type: none"> • Financial and capital market as part of the European internal market (free movement of goods, services, capital and people) • equivalence approach; mutual recognition; reconciliations • European Supervisory Authorities (ESMA with CESR etc.) 	<ul style="list-style-type: none"> • EU-Directives/ delegated acts (TCFD/ Taxonomy/ CSRD) • EFRAG as de facto ESG-standard setter • Expanding the content of current sustainability reporting to full ESG • Concept of „Double Materiality“ (Impact Materiality, Financial Materiality) • Differentiated application for PIE and Non-PIE entities and size criteria (to be enhanced for sector-based disclosures) – mixed model • Extraterritoriality • Multi-Stakeholder approach • Behavioral change objective → see Green Deal
IFRS Foundation	<ul style="list-style-type: none"> • IASB Standards and IFRS IC (Standards & Interpretations) • Specific standards for SMEs 	<ul style="list-style-type: none"> • „Need“ for recognition or adoption by state authorities • IFRS IC to address requests from market supervisory authorities 	<ul style="list-style-type: none"> • ISSB Sustainability Disclosure Standards • Global Baseline • Heavily relying on existing frameworks, mandating SASB for industry-based climate disclosures principles as a starting point • Climate-first approach • Investor focus • Transparency as primary objective
United States	<ul style="list-style-type: none"> • „Generally Accepted“ Accounting Principles • Private Sector with substantial authoritative support: FASB, AICPA, etc. (Standards, Interpretationen and Sector-Guidelines) 	<ul style="list-style-type: none"> • Securities and Exchange Commission (governmental) • SEC Rules and Regulations • Acceptance of „full IFRS“ for Foreign Private Issuers only 	<ul style="list-style-type: none"> • SEC Climate Disclosure Rules <ul style="list-style-type: none"> ➢ Investor focus ➢ Climate-related disclosure requirements only ➢ Internal controls • Private Sector authoritative guidance: SASB • Support for ISSB • Transparency as primary objective

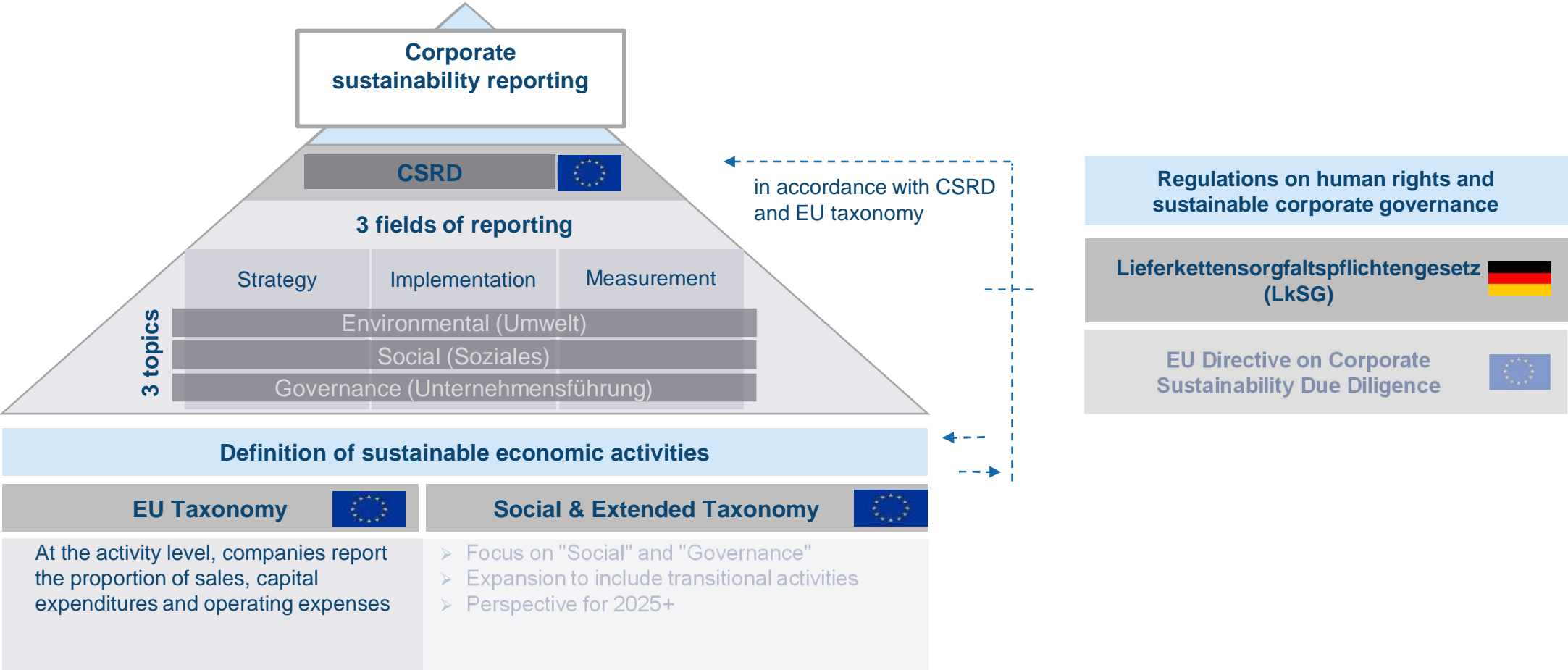
EU Sustainability Reporting Measures within the EU Green Deal



EU Sustainability Reporting

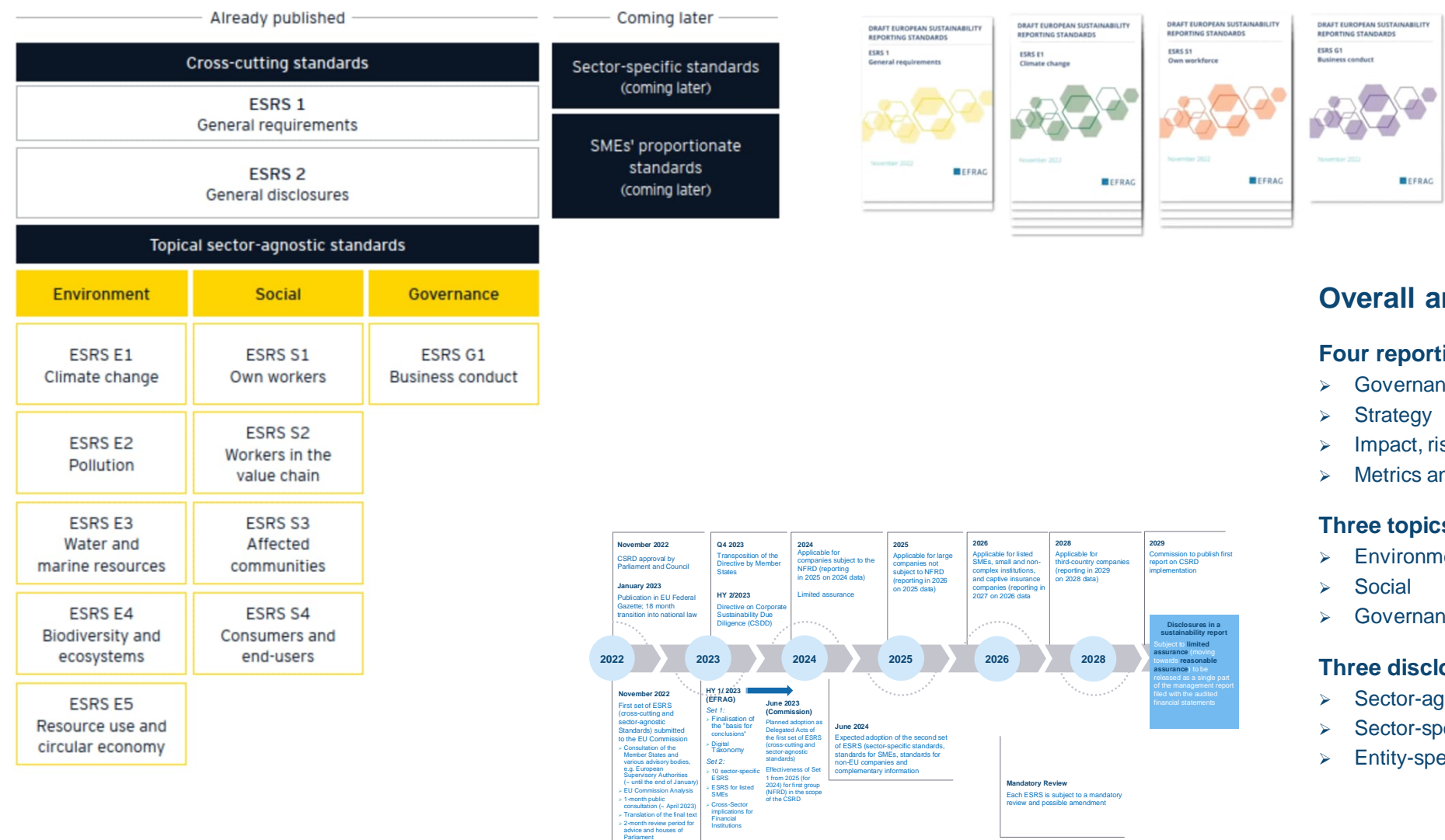
Corporate Sustainability Reporting Directive (CSRD)

The regulatory sustainability requirements are brought together under the umbrella of the CSRD



EU Sustainability Reporting

EFRAG | final draft ESRS



Overall architecture

Four reporting areas

- Governance
- Strategy
- Impact, risk and opportunity management
- Metrics and targets

Three topics

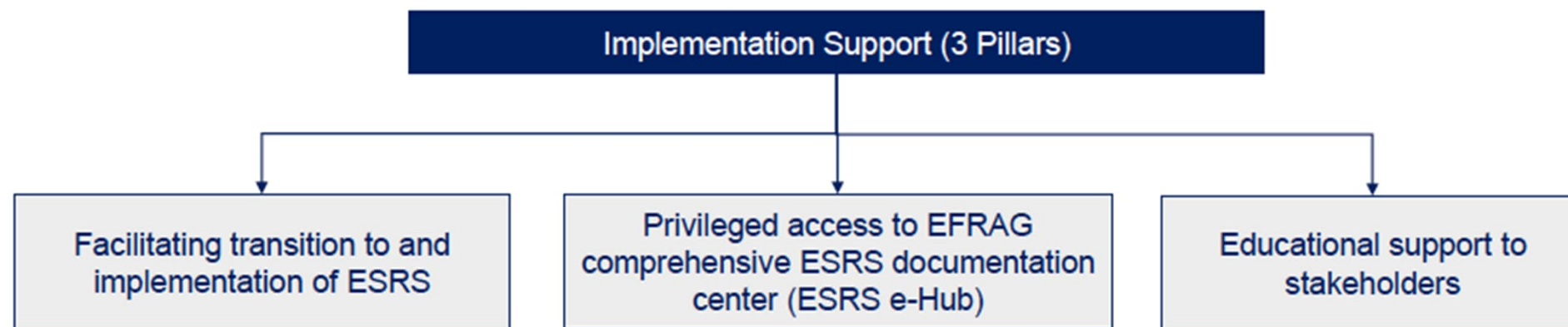
- Environmental
- Social
- Governance

Three disclosure layers

- Sector-agnostic
- Sector-specific
- Entity-specific

current status – May 2023

EU Developments – EFRAG



03/03/2023 - EFRAG RELEASES A SERIES OF EDUCATIONAL VIDEOS ON THE FIRST SET OF DRAFT ESRS

EFRAG is happy to present a series of educational videos dedicated to the First set of draft ESRS, which were released to the European Commission in November 2022. This series is composed of 20 videos:

- the "Glimpses" will give you an overview of the standards and
- the "Educational sessions" will cover the draft standards in more details.

Whether you want a brief introduction to the draft standards or a longer explanation, take a dive into this first set of draft ESRS accompanied by our experts!

10/03/2023 - EFRAG ISSUES THE SET OF BASIS FOR CONCLUSIONS FOR ITS FIRST SET OF DRAFT ESRS

EFRAG issues the set of Basis for conclusions to complement the first set of draft ESRS developed by the EFRAG SRB with the support of the EFRAG SR TEG. The first set of draft ESRS was submitted to the European Commission in November 2022. No comments are requested on the Basis for conclusions.

Each Basis for conclusions appear under the standard covers, click [here](#) to access them.

On 22 November 2022, EFRAG delivered the first set of draft ESRS to the European Commission in its role as technical adviser. This first set, approved by the EFRAG SRB, with the support of the EFRAG SR TEG, reflects the input from the public consultation on the draft ESRS EDs.

EFRAG now issues the set of Basis for conclusions ('BfC') to supplement the draft ESRS. The BfC accompanies but is not part of the draft ESRS and, as such, its content has no authoritative status.

It illustrates the objective and context of the draft standards, the process followed in their preparation, the reasons to include in the standards a disclosure requirement, when relevant the alternative considered, the references to other standard-setting initiatives or European or other relevant regulations and, where appropriate, the argument supporting the need for granular guidance.

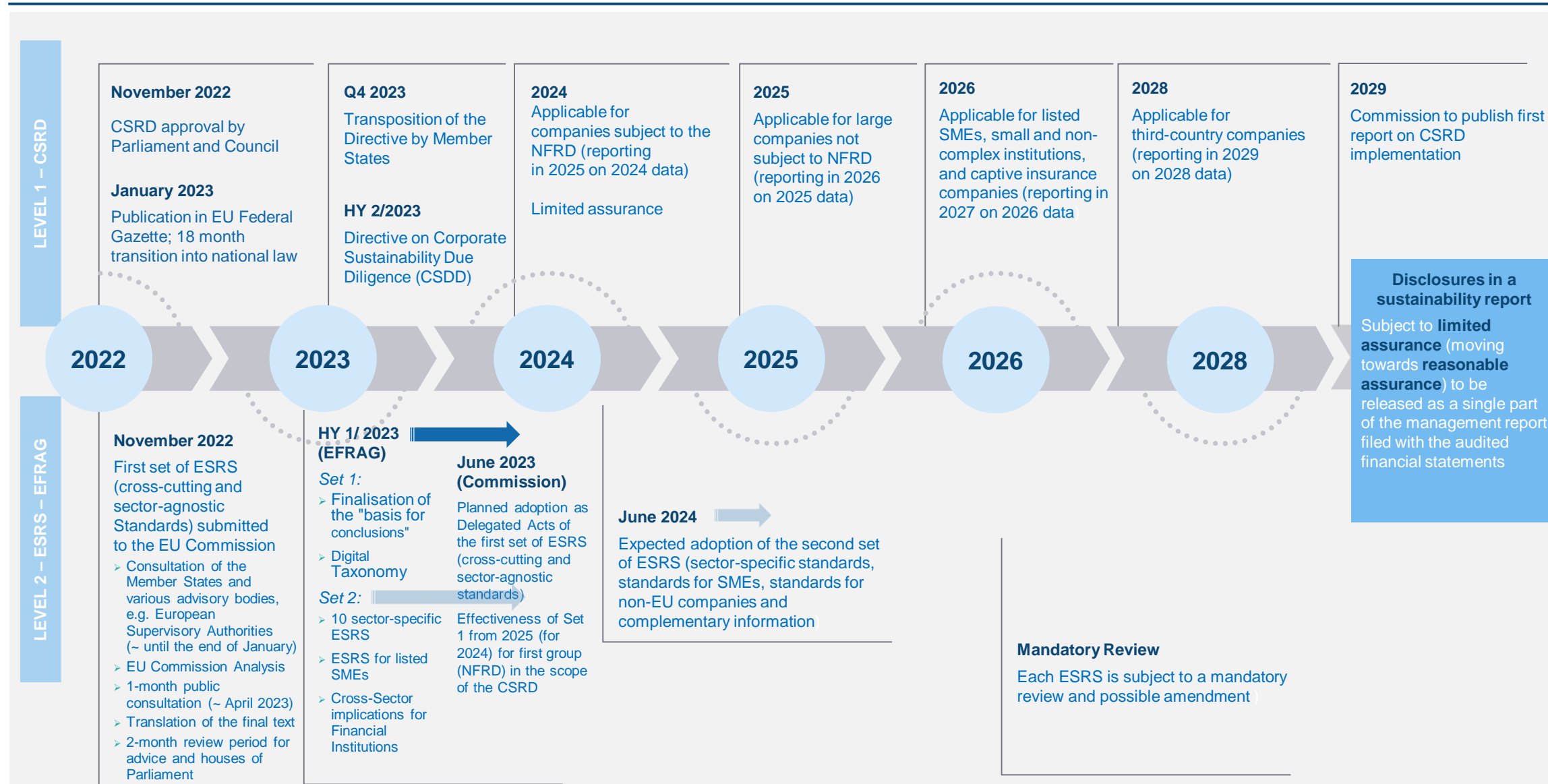
Source: EFRAG

EU Developments – EFRAG

- 15 March Ursula von der Leyen publicly advocates a 25% **reduction in reporting requirements**
- 21 March Mairead McGuinness calls for the **prioritization of application guidance** for the first set of ESRS (this consequently goes along a postponement of the work and consultation on the sector-specific standards)
- 5 April The European Commission publishes **new drafts for the delegated legal acts of the EU taxonomy** (technical assessment criteria for the environmental goals 3-6, adapted reporting forms for the reporting obligations according to Art. 8, adaptation of the climate legal act) with a comment period until 3 May 2023
- ... *Public **Commission consultation on the first set of the ESRS drafts** still pending*
- *announced for early/mid-May*
 - *"intra-services consultation" not yet started*
 - *publication by August 30 is mandatory for ESRS to apply for the 2024 reporting period*

EU Sustainability Reporting

Timeline CSRD and ESRS



ISSB current status (May 2023)

ISSB Standards will build on investor-focused standards and frameworks



Forthcoming publication:
Exposure Draft
Methodology for Enhancing the International Applicability of the SASB Standards

The International Sustainability Standards Board expects to publish Exposure Draft *Methodology for Enhancing the International Applicability of the SASB Standards* on 11 May 2023.



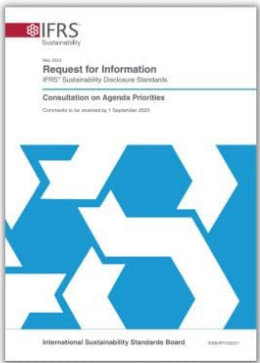
S1 General Requirements for Sustainability-related Disclosure:
Key concepts



-  Emphasises need for **consistency and connections** between financial statements and sustainability disclosures
-  Financial statements and sustainability disclosures published **at the same time**, but with transitional relief
-  Does **not specify a location** for disclosure within general purpose financial reporting and **allows for additional information**, to facilitate application in different jurisdictions

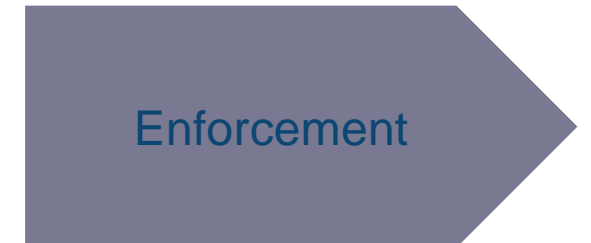
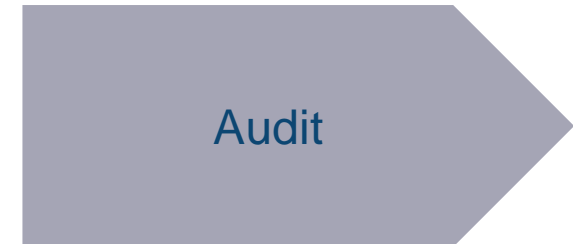
IFRS Sustainability

ISSB seeks feedback on its priorities for the next two years



Source: IFRS Foundation

Corporate Governance Building Blocks



The „BIG three“ Proposals for standardised sustainability disclosure

	EU Commission/ EFRAG	IFRS Foundation	US-SEC
Focus	Multi-Stakeholder; (two main groups: (i) affected stakeholders, ii) users)	Investor	Investor
Coverage	<ul style="list-style-type: none"> Full ESG industry-agnostic first; industry-specific to follow Enhanced by EU Taxonomy 	<ul style="list-style-type: none"> Climate – first; eventually enhanced ESG later; industry-specific 	<ul style="list-style-type: none"> Climate – only; industry-agnostic
Scope	<ul style="list-style-type: none"> Mandatory for entities in scope of CSRD (staggered approach) NFRD entities first Non-listed, SME and non-EU companies to follow 	<ul style="list-style-type: none"> Need for jurisdictional adoption Reliance on IOSCO 	<ul style="list-style-type: none"> Mandatory for SEC registrants (domestic and foreign)
Timeline	<ul style="list-style-type: none"> Staggered approach via CSRD Starting with 2024 reporting period for NFRD entities Final ESRS to be published in 06-08/ 2023 	<ul style="list-style-type: none"> Final IFRS S1 and S2 to be issued by June 2023 Transitional relief available for 2024 reporting period 	<ul style="list-style-type: none"> Final rules to be issued in first half-year 2023 Staggered approach starting w/ 2023 reporting period for large accelerated filers
Materiality	<ul style="list-style-type: none"> Double Materiality (financial and impact materiality) 	<ul style="list-style-type: none"> Financial Materiality (similar to financial reporting definition) 	<ul style="list-style-type: none"> Financial Materiality (consistent with Supreme Court's definition)
Reporting Standards	<ul style="list-style-type: none"> 12 ESRS 	<ul style="list-style-type: none"> Global baseline objective 2 IFRS Sustainability Disclosure Standards (incorporating SASB for industry-specific) 	<ul style="list-style-type: none"> 1 disclosure proposal (w/o reference to specific reporting standards)
Framework	<ul style="list-style-type: none"> (TCFD) GHG 	<ul style="list-style-type: none"> TCFD IIRC SASB GRI GHG 	<ul style="list-style-type: none"> TCFD GHG

Proposals for standardised sustainability disclosure (cont.)

	EU Commission/ EFRAG	IFRS Foundation	US-SEC
Location of disclosures	<ul style="list-style-type: none"> • Separate section in Management Report • Limited options for cross-referencing 	<ul style="list-style-type: none"> • Flexible, but as part of general-purpose financial reporting • Option to cross-reference 	<ul style="list-style-type: none"> • Non-financial statement disclosures <ul style="list-style-type: none"> • Separate section for GHG emission disclosures • Other disclosures on identify, assess, manage risks • Certain quantified climate-related risks in new Note to Financial Statement and in scope of ICFR • Incorporation by reference possible (eg risk factors)
Audit	<ul style="list-style-type: none"> • Limited assurance • Reasonable assurance (option to move-in) 	<ul style="list-style-type: none"> • n/a 	<ul style="list-style-type: none"> • Financial statement impact metrics and ICFR subject to audit (reasonable assurance) • GHG (Scope 1 & 2) emission disclosures (phased-in assurance)
Issuance	<ul style="list-style-type: none"> • Same time as financial statements • Subject to digital taxonomy 	<ul style="list-style-type: none"> • Same time as financial statements 	<ul style="list-style-type: none"> • Same time as financial statements

EFRAG | final draft ESRS

Interoperability

- Intensive dialogue between EFRAG and ISSB
- Significant progress underway
 - Structure
 - Terminologie
 - Reporting boundaries
 - Climate-related targets and transition plans
 - GHG emission coverage (Scope 1-3)
 - ...
- Ultimate goal
 - Interoperability/ alignment
 - Mapping table
 - No double reporting

Quelle: EU @ COP 27, EU ESG disclosures and ESRS

DRAFT EUROPEAN SUSTAINABILITY
REPORTING STANDARDS

Appendix V - IFRS Sustainability
Standards and ESRS reconciliation table



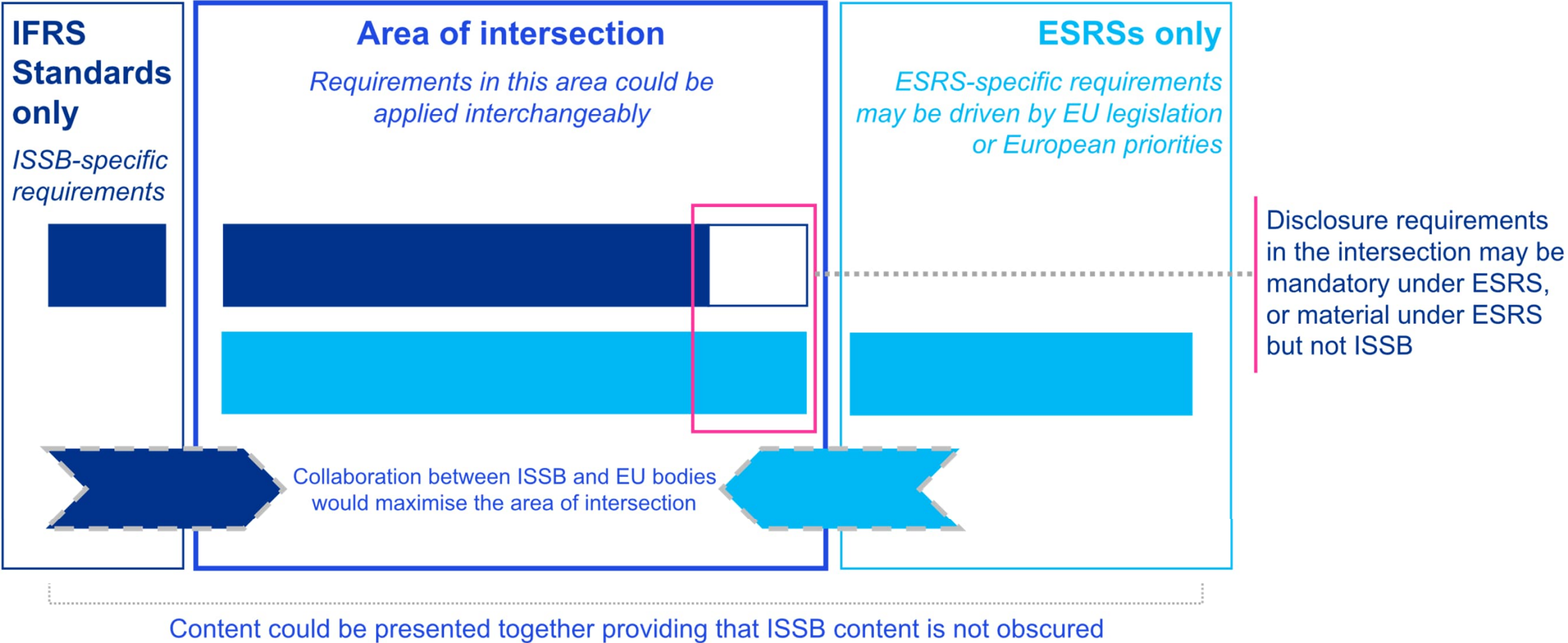
November 2022

■ EFRAG

IFRS S1	ESRS 1 / ESRS 2	Comparison IFRS S1 VS ESRS 1 and 2
Objective 1. The objective of [draft] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information is to require an entity to disclose information about its significant sustainability-related risks and opportunities that is useful to the primary users of general purpose financial reporting when they assess enterprise value and decide whether to provide resources to the entity. Note: on the basis of the ISSB tentative deliberations the final version of IFRS S1 will not refer anymore to enterprise value.	ESRS 1 § 1: The objective of this [draft] Standard is to set out the general requirements that undertakings shall comply with when preparing and presenting sustainability-related information under the Accounting Directive as amended by the Corporate Sustainability Reporting Directive (CSRD). ESRS 1 § 2.2: The information shall enable the understanding of the undertaking's impacts on those matters and how they affect the undertaking's development, performance and position. ESRS 2 § 1: This [draft] ESRS sets out the disclosure requirements that apply to all undertakings regardless of their sector of activity (i.e., sector agnostic) and apply across sustainability topics (i.e., cross-cutting). This [draft] ESRS covers the reporting areas defined in [draft] ESRS 1 General requirements section 1.2 Cross-Cutting Standards and reporting areas.	Both standards set the general principles to be followed in the preparation of sustainability reports. IFRS S1 and ESRS 1 both focus on sustainability-related risks and opportunities. In ESRS S1 and S2 the dimension of impacts is explicit, while in IFRS S1 it is implicitly considered as a source of risks and opportunities. ESRS 1 refers to a broader group of stakeholders (reflecting the principle of double materiality); the IFRS S1 primary users are included in the broader definition of stakeholders in ESRS 1.
2. A reporting entity shall disclose material information about all of the significant sustainability-related risks and opportunities to which it is exposed. The assessment of materiality shall be made in the context of the information necessary for users of general purpose financial reporting to assess enterprise value.	ESRS 1, chapter 1.1. Complying with Draft ESRS and Chapter 3 Double materiality as the basis for sustainability disclosures ESRS 1 § 1: The undertaking shall disclose, in accordance with applicable [draft] European Sustainability Reporting Standards (ESRS), all the material information regarding impacts, risks and opportunities in relation to environmental, social, and governance matters. ESRS 1 § 25: The undertaking shall report on sustainability matters based on the double materiality principle as defined and explained in this chapter.	Materiality is based on financial materiality for IFRS and double materiality for ESRS.
3. An entity's general purpose financial reporting shall include a complete, neutral and accurate depiction of its sustainability-related financial information.	ESRS 1 chapter 2 Qualitative characteristics of information ESRS 1 § 23: When preparing its sustainability statements, the undertaking shall apply: understand which Scope 3 emissions have been included in, or excluded from, those reported; (3) when the entity's measure of Scope 3 emissions includes information provided by entities in its value chain, it shall explain the basis for that measurement; (4) if the entity excludes those greenhouse gas emissions in paragraph 21(a)(vi)(3), it shall state the reason	ESRS 1 has incorporated the text of IFRS S1 on qualitative characteristics of information (plus additions to cover the impact materiality perspective).

Comparison IFRS S2 versus ESRS E1
All IFRS S2 disclosures are covered in ESRS. Temporary difference on sectoral approach: Sector-specific standards to be developed at a later stage but ESRS 1 § 133 b) allows the use of Appendix B of IFRS S2 (industry-specific) Additions in ESRS E1 are: <ul style="list-style-type: none">• Energy consumption and mix and energy intensity per revenue required by SFDR• More details on GHG emissions (share of Scope 1 emissions under EU ETS, Scope 2 emissions in market-based and location-based, distinction between removals and carbon credits)• Clarification on reporting boundaries (operational control approach required by ESRS E1)• More details and examples on potential financial effects from physical and transition risks• Taxonomy-alignment ratios (Green Turnover) and more details on opportunities (cost savings and market size for low carbon products and services)• Compatibility between internal carbon prices and those used in financial statements and financial planning; location difference between Governance (ESRS) and Metrics (IFRS S2)• Specific target on GHG emission reduction and remuneration tied to this target in ESRS• Distinction of three levels of targets: general climate-related targets, GHG emission reduction targets, and net zero targets and other neutrality claims

Interoperability



Source: KPMG

Key takeaways

- Transformation requires a clear objective, a specific time (period) reference and consistent project management
- Corporate reporting replaces traditional financial accounting – externally as well as internally (managerial)
- Key changes triggered by ESG reporting transformation include:
 - Double materiality
 - Consideration of the entire value chain
 - Link between business model & strategy
 - Transparency on methodology & assurance
 - Application of the RMS & CMS model to ESG (in a manner similar to COSO Framework)
 - Expansion of data capacity and data quality
- The responsibilities of management and the supervisory board (board of directors), auditors and regulators are not different for financial accounting/ reporting and ESG reporting
- Standardsetters need to establish interoperability
- The "language of the business" becomes a holistic "license to operate"

Thank you!

Prof. Dr. Sven Hayn

Wirtschaftsprüfer | US Certified Public Accountant (Illinois)

Mail: sven.hayn@WPHayn.com (primary) or sven.hayn@uni-hamburg.de (secondary)

[linkedin.com/in/sven-hayn](https://www.linkedin.com/in/sven-hayn)