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First Notes

The International Sustainability Standards Board

7 December 2021

First Notes on

Financial reporting

Corporate law updates

Regulatory and other information

Disclosures

Sector

All

Banking and insurance

Information, communication, entertainment

Consumer and industrial markets

Infrastructure and government

Relevant to

All

Audit committee

CFO

Others

Transition

Immediately

Within the next three months

Post three months but within six months

Post six months

Forthcoming requirement

Introduction

On 3 November 2021, the International Financial Reporting Standards (IFRS) Foundation announced the formation of the new International Sustainability Standards Board (ISSB). The ISSB will develop a comprehensive global baseline of high – quality sustainability disclosure standards which are focussed on enterprise value. The ISSB will focus on meeting the sustainability information needs of investors for assessing enterprise value and making investment decisions. The standards will help investors understand how companies are responding to ESG issues, like climate, diversity etc. to inform capital allocation decisions.

The establishment of the ISSB marks a significant milestone in the journey towards a holistic corporate reporting by global corporates, given the growing significance of Environment, Social and Governance (ESG) disclosures to investors in the global markets today.

Global organisations contributing to the ISSB

Several leading investor-focussed sustainability disclosure organisations will participate and consolidate in the ISSB. The IFRS Foundation will complete consolidation of the Climate Disclosure Standards Board (CDSB—an initiative of CDP[1]) and the Value Reporting Foundation (VRF—which houses the Integrated Reporting Framework and the SASB[2] Standards) by June 2022[3]. The ISSB will also be supported by IOSCO[4], TCFD[5] and WEF[6]. Together, these organisations share the aim of enterprise value-focussed sustainability standards.

Bringing different perspectives together – Shaping the ISSB and IFRS Sustainability Disclosure Standards

--Resources consolidated into the IFRS Foundation
(Source: KPMG US, Defining Issues, November 2021)

[1] Formerly known as the Carbon Disclosure Project
[2] SASB – Sustainability Accounting Standards Board
[3] Source: IFRS dated 3 November 2021, https://www.ifrs.org/news-and-events/news/2021/11/ifrs-foundation-announces-issb-consolidation-with-cdsb-vrf-publication-of-prototypes/
[4] IOSCO – International Organisation of Securities Commissions
[5] TCFD – Task Force on Climate-related Financial Disclosures
[6] WEF – World Economic Forum

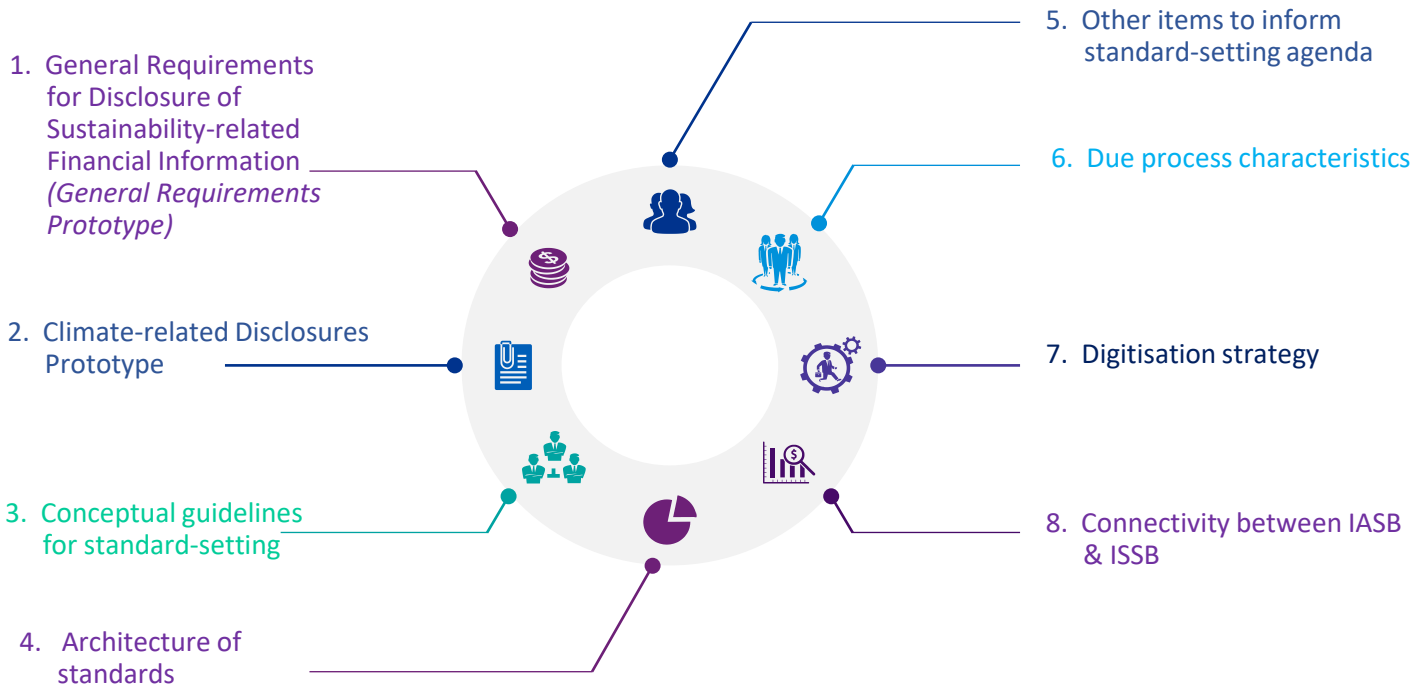
Global organisations contributing to the ISSB (contd.)

The ISSB will work in close cooperation with the IASB[7] Board to ensure compatibility and connectivity between the IFRS Accounting Standards and the IFRS Sustainability Standards issued by the ISSB. Both the ISSB and the IASB will be independent and their respective standards are aimed to complement each other such that comprehensive information can be provided to investors and other stakeholders.

Immediate priorities

As a stepping stone, the IFRS Foundation created the Technical Readiness Working Group (TRWG) to provide recommendations to the ISSB. The TRWG work plan includes creating prototypes containing technical recommendations for consideration by the newly constituted ISSB. The prototypes are built on the past work done by the TRWG's individual member organisations, the market-informed and market-tested tools and resources and the individual and collective expertise established through the development and implementation of these widely used resources and tools.

The work plan for the TRWG consists of providing eight deliverables to ISSB for discussion, these are included in the picture below:



(Source: Summary of the Technical Readiness Working Group's Programme of Work, dated November 2021)

On 3 November 2021, the TRWG published the first two deliverables for ISSB's considerations (more details are provided in the next section) namely:

- General Requirements for Disclosure of Sustainability-related Financial Information (General Requirements Prototype)
- Climate-related Disclosures Prototype.

Additionally, the TRWG also published an overview of its work programme and provides a summary of the proposals from the third and fourth deliverables regarding Conceptual Guidelines and the Architecture of Standards. The remaining deliverables 5-8 as (depicted in the picture) above concern recommendations for operational and technical factors required for:

- The functioning of the ISSB
- Their interplay with IFRS Accounting Standards, and
- Connection between financial statements and sustainability-related financial disclosures (including those in the management commentary)

The ISSB in due course will consider these prototypes in its work programme and determine the next steps.

[7] IASB- International Accounting Standards Board

General Requirements Prototype

IAS 1, *Presentation of Financial Statements* issued by the IASB sets out the overall requirements for, and standardises the presentation of, financial statements. The general requirements prototype are similar in approach to IAS 1 and sets out the overall requirements for disclosing significant sustainability-related risks and opportunities to which the reporting entity is exposed that is useful to primary users of general purpose financial reporting in deciding whether to provide resources to the entity. Those decisions involve decisions about:

a) Buying, selling or holding equity and debt instruments

b) Providing or settling loans and other forms of credit, or

c) Exercising rights to vote on, or otherwise influence, management's actions that affect the use of the entity's economic resources.

Scope

An entity should apply this standard in preparing and disclosing sustainability-related financial information in accordance with IFRS Sustainability Disclosure Standards. An entity is permitted to apply IFRS Sustainability Disclosure Standards when the entity's related financial statements are prepared in accordance with IFRS Accounting Standards or other GAAP.

Definition of 'Sustainability'

As per Appendix B of the standard, the term sustainability can refer:

(a) To activities and relationships that make impacts on people, the environment, and the economy, and

(b) To activities that erode, maintain, or enhance its ability to create enterprise value over the short, medium and long term.

An entity is required to provide information about sustainability-related information as defined. That definition focusses on drivers of enterprise value and may include information about matters such as climate change, water use and discharge, biodiversity, human rights, etc.

Applying materiality

The concept of materiality is aligned to that used in the IFRS Accounting Standards. General purpose financial reporting includes financial statements of and sustainability-related financial information about a specific reporting entity. Sustainability-related financial information is material if omitting, misstating or obscuring that information could reasonably be expected to influence decisions that the primary users (such as existing and potential investors, lenders and other creditors) of general purpose financial reports make on the basis of those reports. Materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates. The prototype does not specify a uniform quantitative threshold for materiality or predetermine what would be material in a particular situation.

- **Sustainability-related financial information** influences those decisions if it influences users' assessments of the entity's enterprise value. This information could include but is not limited to information about an entity's impacts on society and the environment that could reasonably be expected to affect enterprise value.
- **Enterprise value** is determined by capital market participants, based on their estimation of the amount, timing and certainty of future cash flows spanning the short, medium, and long term, and the value they attribute to those cash flows.
- **Materiality judgements** are reassessed at each reporting date in the light of those changed circumstance, since an entity's circumstances change over time.

Entity's reporting boundary and connectivity

The reporting entity for sustainability-related financial disclosures is the same as for financial statements. An entity shall disclose material information about significant sustainability-related risks and opportunities arising from activities, interactions and relationships with parties outside the reporting entity's boundary that affect users' assessment of enterprise value.

A complete set of sustainability-related financial disclosures is provided so that users can understand the connections, dependencies and trade-offs that may apply between sustainability-related financial disclosures and other information in general purpose financial reporting. An entity shall connect sustainability-related financial disclosure with other information, for example but not limited to, where:

(a) It highlights relationships between different pieces of information and present it clearly and concisely.

(b) It explains trade-offs when sustainability-related risks and opportunities give rise to other sustainability-related risks and opportunities.

General Requirements Prototype (contd.)

General disclosure requirements

The disclosure requirements for each sustainability matter focus on matters critical to the way an entity operates. Providing information on all four aspects listed below will enhance consistency and comparability across entities.

- **Governance:** The governance processes, controls and procedures a reporting entity uses to monitor sustainability-related risks and opportunities
- **Strategy:** The sustainability-related risks and opportunities that could enhance the entity's business model and strategy over the short, medium and long term
- **Risk management:** How sustainability-related risks are identified, assessed, managed and mitigated and
- **Metrics and targets:** Information used to manage and monitor the entity's performance in relation to sustainability-related risks and opportunities over time.

The general requirements prototype provides the objectives and disclosure requirements of the above listed aspects to achieve stated outcomes.

Comparative information and reporting frequency

An entity shall present comparative information regarding the previous period for all amounts including metrics and key performance indicators reported in the current period. When relevant to understanding the current period's sustainability-related financial disclosures an entity shall also disclose comparative information for narrative and descriptive information.

An entity shall identify the reporting period for sustainability-related financial disclosures. An entity shall disclose sustainability-related financial disclosures for the same reporting period on which the entity's financial statements are based, and therefore report at least every 12 months and at the same time as those financial statements.

Reporting channel

An entity is required to disclose information required by IFRS Sustainability Disclosure Standards as a part of the entity's general purpose financial reporting. Subject to any regulation or other requirements that apply to an entity, there are various possible locations in its general purpose financial reporting in which it can disclose sustainability-related financial information such as included as part of the management commentary, incorporated as a cross reference from another report, etc.

Fair presentation, sources of estimation and outcome uncertainty

The standard requires an entity to present fairly the sustainability-related risks and opportunities to which the entity is exposed. A fair presentation also requires an entity:

(a) To disclose information that is relevant, reliable, comparable and understandable, and

(b) To provide additional disclosures when compliance with the specific requirements in IFRS Sustainability Disclosure Standards is insufficient to enable users to understand the impact or potential impact of significant sustainability-related risks and opportunities on the entity's enterprise value.

In the absence of an IFRS Sustainability Disclosure Standard that applies specifically to a sustainability matter, management shall use its judgement in disclosing information that will meet the objective set out in this section.

When metrics cannot be quantified directly and can only be estimated, measurement uncertainty arises. The use of reasonable estimates is an essential part of preparing sustainability-related metrics and does not undermine the usefulness of the information if the estimates are clearly and accurately described and explained. Even a high level of measurement uncertainty does not necessarily prevent such an estimate from providing useful information. An entity shall identify metrics it has disclosed that have significant estimation uncertainty, disclosing the sources and nature of the estimation uncertainties and the factors affecting the uncertainties.

Use of other standards

The ISSB will require time to develop thematic standards on sustainability-related matters in addition to the standard on climate, and industry-specific standards. In the absence of an ISSB Standard that applies to a specific sustainability matter, preparers are required to use their judgement to provide disclosures that are relevant, neutral and faithfully represent the entity's significant sustainability-related risks and opportunities. In applying such judgement, an entity is required to consider the requirements of the General Requirements Prototype and other IFRS Sustainability Disclosure Standards that address similar and related issues. They may also use the most recent pronouncements of other standard-setting bodies whose requirements are designed to meet the needs of users of general purpose financial reporting and accepted industry practices. This is similar to the approach the IASB takes in IAS 8 '*Accounting Policies, Changes in Accounting Estimates and Errors*'.

Climate-related Disclosures Prototype (Climate Prototype)

This is the first thematic standard published by the TRWG for consideration by the ISSB. It encapsulates the recommendations by the Task Force on Climate-Related Financial Disclosures (TCFD). The climate prototype sets out the requirements for the identification, measurement, and disclosure of climate-related financial information.

Scope

This standard applies to climate-related risks that an entity is exposed to which includes physical risks from climate change (physical risks) and risks associated with the transition to a lower-carbon economy (transition risks). It also applies to climate-related opportunities available to and considered by the entity.

Objective

Entities are required to provide information about their exposure to climate-related risks and opportunities. This information, along with other information provided as part of an entity's general purpose financial reporting, assists users of the information provided:

- In assessing the entity's future cash flows, their amounts, timing and certainty, over the short, medium and long term. This information, together with the value attributed by users to those cash flows, supports their assessment of the entity's enterprise value.
- Understand how management's use of resources, and corresponding inputs, activities, outputs and outcomes support the entity's response to and strategy for managing its climate-related risks and opportunities and
- To evaluate the ability of the entity to adapt its planning, business model and operations in response to climate-related risks and opportunities.

Governance

An entity is required to disclose information regarding the governance processes, controls and procedures used to monitor and manage climate-related risks and opportunities. To achieve this objective, the entity should disclose a description of the governance body or bodies (which can include a board, committee or equivalent body charged with governance) with oversight of climate-related risks and opportunities, and of management's role with respect to climate-related risks and opportunities.

Strategy

An entity should disclose 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, including:

- Whether and how information about climate-related risks and opportunities inform management's strategy and decision making
- The current and the anticipated effects of climate-related risks and opportunities on its business model
- The impact of climate-related risks and opportunities on the entity's financial position, performance and cash flows, both at the end of the reporting period and the anticipated effects over the short, medium and long term, and
- The resilience of the entity's strategy to climate-related risks.

Risk management

An entity should disclose information on how climate-related risks are identified, assessed, managed and mitigated. Specifically, an entity should describe the process by which climate-related risks are identified, the process, or processes, by which the entity assesses the significance of climate related risks, for each significant climate-related risk how the risk is being monitored, managed, and mitigated, including related policies and for each significant climate-related risk, information that enables an understanding of how the risk is being monitored, managed, and mitigated, including related policies, etc.

Metrics and targets:

An entity should disclose information regarding the entity's performance in managing significant climate-related risks and opportunities. To achieve this objective, an entity should disclose:

(a) Cross-industry metrics (for example; greenhouse gas emissions—in terms of absolute gross Scope 1, Scope 2 and Scope 3, expressed as metric tonnes of CO2 equivalent, in accordance with the Greenhouse Gas Protocol, and emissions intensity, transition risks—the amount and percentage of assets or business activities vulnerable to transition risks, etc.)

(b) Industry-based metrics (for example; for an apparel, accessories and footwear industry, on the topic of 'raw material sourcing,' an entity should provide a description of environmental and social risks associated with sourcing priority raw materials and the percentage of raw materials third-party certified to an environmental and/or social sustainability standard, by standard[8])

[8] Source: The Climate Prototype Appendix B – Industry disclosure requirements

Climate-related Disclosures Prototype (Climate Prototype) (Contd.)

(c) **Targets set by management** to mitigate or adapt to climate-related risks or maximise climate-related opportunities, and

(d) **Other key performance indicators** used by the board or management to measure progress towards the targets identified in point (c) above.

Our comments

The formation of the ISSB by the IFRS Foundation marks a significant milestone in the evolution of sustainability reporting across the globe. One set of globally accepted standards on sustainability by the ISSB will address the challenge of fragmented corporate reporting by companies due to multiple standards and frameworks being issued by various regulatory bodies and standard setters. Investors and other stakeholders in the capital ecosystem can now look forward to a more global baseline sustainability reporting which will allow enhanced comparability and consistency in the way companies will report on sustainability.

Comprehensive framework: The ISSB will build on the well-established frameworks laid out by the TCFD, IIRC, SASB, CDSB and will be supported by the IOSCO and the WEF. The ISSB has released a project plan of the consultation process and timeline for issuance of final standards. The setting up of the TRWG will help to accelerate the work and development of the sustainability standards by the ISSB since it has been provided a running start.

Connectivity within an entity's general purpose financial statements: The general requirements standard set out the overall requirements for disclosing sustainability-related financial information relevant to the sustainability-related risks and opportunities of the entity. The objective of the ISSB standards is to require entities to provide 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. Under the governance of the IFRS Foundation, the IASB Board and the ISSB are set to work in collaboration emphasising the importance of connectivity within the entity's general purpose financial reporting, including between the entity's general purpose financial statements and sustainability-related financial information.

Building block approach by ISSB: The ISSB has adopted a building block approach and would be working with standard-setters from key jurisdictions. The standards that would be issued by the ISSB would provide a globally consistent and comparable sustainability reporting baseline, while also providing flexibility to various jurisdictions for coordination on reporting requirements that capture wider sustainability impacts that are relevant from the perspective of each jurisdiction.

Preparedness by companies: The climate-related disclosures standard is expected to be the first of the proposed suite of sustainability disclosure standards to be issued by ISSB. Companies should watch out this space for further developments as standards are expected to be released at a fast pace. Using the climate- related disclosure prototype, companies should start planning ahead and revamp processes and IT controls within their organisation in order to report on the metrics and targets that would be set out in the climate standard and wider set of areas as they are released by ISSB.

Assurance on sustainability reporting: With the foundation towards a global system for sustainability-related reporting having been laid; investors, regulators, policymakers, employees and providers of finance are turning their attention to the importance of role of assurance on non-financial information. As reporting evolves, auditors are increasingly asked to provide assurance on sustainability or ESG reporting. Currently this type of reporting, and assurance thereon, is often undertaken on a voluntary basis by entities, there is an increasing focus on this being mandated by law or regulation. With the growing importance of—and reliance on—sustainability information, low-quality assurance is an emerging investor protection and financial stability risk. Significant differences in practices exist across different jurisdictions. IAASB[9] is making a significant step forward in supporting assurance for non-financial reporting and companies should watch this space. Additionally, accountants and other professionals should enhance their own technical skill sets to provide independent assurance on sustainability reporting.

[9] International Auditing and Assurance Standards Board

Our comments (contd.)

Applicability to India: The Securities and Exchange Board of India (SEBI) in May 2021 prescribed a new reporting requirement by the top 1,000 listed companies in India. As per this, companies would be required to submit a new report on Environment, Social and Governance (ESG) parameters namely the Business Responsibility and Sustainability Reporting (BRSR)[10]. The BRSR is based on the nine principles of the National Guidelines for Responsible Business Conduct (NGRBC). The guidance note on BRSR provides that in case a listed company is preparing and disclosing sustainability reports under any other framework, such as the SASB, TCFD, IR, etc. then such disclosures can be cross referenced under the disclosures sought by the BRSR format.

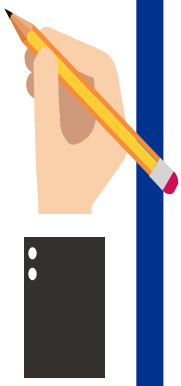
As provided in the general requirements of the prototype issued by the TRWG, an entity's general purpose financial report shall comply with the requirements in IFRS Sustainability Disclosure Standards, including requirements related to materiality (materiality requirements), for the entity to state its compliance with those Standards. Hence, an entity that wishes to state compliance with IFRS Sustainability Disclosure Standards cannot provide less information than the information required by the Standards, even if local laws and regulations permit it to do so.

Since the forthcoming ISSB standards are based on building block approach, SEBI and other regulators in India should watch this space for more developments and assess whether they need to build on these global standards to serve the local jurisdictional needs in India and also make the local standards comparable with the best practices around the world to serve investor needs.

[10] BRSR reporting is mandatory for top 1,000 listed companies by market capitalization from financial year 2022-23 and voluntary from financial year 2021-22.

The bottom line

A global set of standards for corporate reporting is critical for users and preparers of financial and non-financial disclosures. The IFRS Foundation is set to pave the way for putting sustainability reporting under the same lens as financial reporting by setting up the ISSB. The new sustainability disclosure standards will help drive a globally consistent, comparable and reliant sustainability reporting. This will in turn assist in improving the efficiency and effectiveness of capital markets and help investors make sound investment decisions. Additionally, a comprehensive framework by the IFRS Foundation on both financial and sustainability-related financial disclosures will enable a single global approach to assurance. Enhanced connectivity within an entity's general purpose financial reporting will be important for companies and users of financial statements to place trust and reliance on the integrated general purpose financial statements.



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KPMG in India's IFRS institute

Visit KPMG in India's IFRS institute - a web-based platform, which seeks to act as a wide-ranging site for information and updates on IFRS implementation in India.

The website provides information and resources to help board and audit committee members, executives, management, stakeholders and government representatives gain insight and access to thought leadership publications that are based on the evolving global financial reporting framework.

Missed an issue of Accounting and Auditing Update or First Notes?

Issue no. 63 – October 2021

The topics covered in this issue are:

- SPAC: India tax and regulatory conundrum
- Accounting of financial instruments under Ind AS
- Regulatory updates.

SEBI mandates additional compliance for issuer of non-convertible securities

10 November 2021

With a view to improve transparency and enhance the robustness of the corporate bond market, on 7 September 2021, the SEBI issued amendments to the Listing regulations through the SEBI (Listing Obligations and Disclosure Requirements) Fifth Amendment Regulations, 2021 (amendments). The amendments mainly pertain to the following areas: Those relate to the following:

I. Corporate governance regulations applicable to High Value Debt Listed Entities (HVDLE)

II. Financial reporting

III. Additional disclosures to stock exchanges, debenture trustees and on websites

IV. Other amendments

Voices on Reporting

VOR quarterly publication for the quarter ended 30 September 2021

Quarterly updates publication (for the quarter ended 30 September 2021) provides a summary of key updates from the Securities and Exchange Board of India (SEBI), the Ministry of Corporate Affairs (MCA), the Institute of Chartered Accountants of India (ICAI) and the Reserve Bank of India (RBI).To access the publication, please click here.

Feedback/queries can be sent to aaupdate@kpmg.com

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