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August 25, 2023

International Sustainability Standards Board
IFRS Foundation
Opernplatz 14
60313 Frankfurt am Main
Germany

Re: Request for Information – Consultation on Agenda Priorities

Dear Board Members:

This letter is the response of the Canadian Accounting Standards Board (AcSB) to the International Sustainability Standards Board's (ISSB) Request for Information, "Consultation on Agenda Priorities", issued in May 2023.

Who we are

The AcSB is an independent body with the authority to establish accounting standards for use by all Canadian entities outside the public sector. We serve the public interest by establishing standards for financial reporting by all Canadian private sector entities and by contributing to the development of internationally accepted financial reporting standards.

The AcSB remains keenly interested in sustainability reporting developments due to the connectivity between information in the financial statements and sustainability-related financial disclosures. We also acknowledge that many financial statement users continue to demand high-quality information on sustainability reporting matters that can assist in making capital allocation decisions.

Our process

This response letter represents the views of AcSB members and staff based on their knowledge and experience. In developing our response, we also consulted with select board committees including our User Advisory Committee, Academic Advisory Committee, IFRS® Accounting Standards Discussion Group and Pension Plan Working Group, as well as with certain provincial regulatory bodies. The results of these discussions have been incorporated into our letter.

While the preparers and practitioners we consulted with on our committees more directly deal with financial reporting, many are also involved with the implementation of sustainability reporting initiatives.

Our views

The AcSB appreciates the opportunity to comment on the Request for Information as we support all efforts to improve the quality of information that users rely on to make capital allocation decisions. We continue to support initiatives for users to receive appropriate information on sustainability-related matters.

In line with our mandate, our response does not seek to address all the questions posed in the Request for Information. Instead, this letter primarily provides input to the ISSB on considerations and suggested areas of priority from a financial reporting perspective, including sharing our relevant insights as an experienced standard setter.

Focus on implementation of IFRS S1 and S2

We strongly encourage the ISSB to focus its time over the next two years on the implementation of its inaugural standards, IFRS S1 and S2. The implementation of new standards can be a resource-intensive process, particularly for a new board, and will involve the need to consider implementation issues, develop non-authoritative guidance or draft educational materials to support adoption among reporting entities. It is important that these matters be prioritized to ensure that the ISSB's standards have credibility and are applied in a consistent manner.

We recognize the importance for the ISSB to maintain momentum in developing sustainability reporting standards. However, many entities will need time to build their internal reporting capacity to adequately adopt the requirements in IFRS S1 and S2. Therefore, we encourage the ISSB to consider what is practically feasible to not overwhelm the market, including stakeholders' ability to provide views on any new proposals during this critical implementation period. We also recognize that in many cases, the stakeholders are the same as those dealing with the financial reporting requirements. As such, working with the International Accounting Standards Board (IASB) to balance the burden on seeking feedback and implementing of proposals is crucial.

Continue to prioritize connectivity in reporting and interoperability with other sustainability standards

Ensuring connectivity between the ISSB and IASB respective requirements is essential in providing decision-useful information to users. While the Request for Information highlights certain areas where connectivity has been achieved (e.g., use of the same reporting period and consistent financial data), there remains several gaps that need to be addressed to bridge users' expectations of reported sustainability and financial information. We strongly encourage the ISSB to continue working together with the IASB to prioritize issues related to connectivity in reporting and stay abreast of relevant IASB projects to assess for any potential impacts to ISSB's standards.

Ensuring interoperability of ISSB standards with other jurisdictional sustainability standards is also essential to facilitate the delivery of a global baseline of sustainability-related disclosures. We have heard significant concerns from many preparers of multinational corporations regarding the burden of complying with different jurisdictional sustainability reporting requirements. We believe the ISSB has an important role to play in addressing interoperability issues and, therefore, encourage carrying out this work expeditiously with other jurisdictions to minimize reporting costs and complexity.

Integration in reporting as a longer-term project

While we are not opposed to an eventual project on integration in reporting, we think that this should not be an area of priority for the ISSB during the next two years. We recommend that the ISSB allow adequate time for implementation, including connectivity with the financial statements, and build out a broader suite of sustainability reporting standards before exploring a fully integrated reporting approach.

We also recommend that any project on integration in reporting be pursued in tandem with the IASB to ensure that it is cohesive and appropriately reflects how an entity creates value, both from a financial and broader sustainability perspective.

Our responses to your questions

The Appendix to this letter responds to some of the questions posed in the Request for Information and expands on the points raised above.

We would be pleased to elaborate on our comments in more detail if you require. If so, please contact me or, alternatively, Katharine Christopoulos, Director, Accounting Standards (+1 416 204-3270 or kchristopoulos@acsbcanada.ca).

Yours truly,

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About the Canadian Accounting Standards Board
We are an independent body with the legal authority to establish accounting standards for use by all Canadian publicly accountable enterprises, private enterprises, not-for-profit organizations and pension plans in the private sector. We are comprised of a full-time Chair and volunteer members from a variety of backgrounds, including financial statement users, preparers, auditors and academics; a full-time staff complement supports our work.

Our standards
We have adopted IFRS® Accounting Standards as issued by the IASB for publicly accountable enterprises. Canadian securities legislation permits the use of U.S. GAAP in place of IFRS Accounting Standards in certain circumstances. We support a shared goal among global standard setters of high-quality accounting standards that result in comparable financial reporting outcomes regardless of the GAAP framework applied.

We developed separate sets of accounting standards for private enterprises, not-for-profit organizations and pension plans. Pension plans are required to use the applicable set of standards. Private enterprises and not-for-profit organizations can elect to apply either the set of standards developed for them, or IFRS Accounting Standards as applied by publicly accountable enterprises.

Our role vis-à-vis IFRS Accounting Standards
Our responsibility to establish Canadian GAAP necessitates an endorsement process for IFRS Accounting Standards. We evaluate and rely on the integrity of the IASB's due process as a whole, and monitor its application in practice. In addition, we perform our own due process activities for each new or amended IFRS Accounting Standard to ensure that the standard is appropriate for application in Canada. We reach out to Canadians on the IASB's proposals to understand and consider their views before deciding whether to endorse a final IFRS Accounting Standard. A final standard is available for use in Canada only after we have endorsed it as Canadian GAAP.

Appendix

Question 1 – Strategic direction and balance of the ISSB's activities
Paragraphs 18 – 22 and Table 1 provide an overview of activities within the scope of the ISSB's work. a) From highest to lowest priority, how would you rank the following activities? (i) Beginning new research and standard-setting projects. (ii) Supporting the implementation of ISSB Standards IFRS S1 and IFRS S2. (iii) Researching targeted enhancements to the ISSB Standards. (iv) Enhancing the Sustainability Accounting Standards Board (SASB) Standards. b) Please explain the reasons for your ranking order and specify the types of work the ISSB should prioritize within each activity. c) Should any other activities be included within the scope of the ISSB's work? If so, please describe these activities and explain why they are necessary.

AcSB Response

Supporting the implementation of IFRS S1 and S2

1. We strongly encourage the ISSB to focus on supporting the implementation of the ISSB's inaugural standards, IFRS S1 and S2, as its highest priority activity. This includes engaging in many of the activities outlined in the Request for Information, such as:
   - developing guidance and materials to assist with application challenges;
   - establishing a transition implementation group;
   - engaging with partners to deliver educational materials; and
   - publishing an Exposure Draft on taxonomy to facilitate digital consumption of the ISSB's standards.

2. To ensure consistent application, we think that the ISSB should itself address any interpretation issues during the early years after IFRS S1 and S2's effective date given the sustainability standards are relatively new to many jurisdictions. Thereafter, the ISSB should consider whether creating an interpretations committee, similar to the IASB's [IFRS Interpretations Committee (IFRIC)], would be worthwhile to address any ongoing implementation and application challenges with IFRS S1 and S2.

3. Ensuring that IFRS S1 and S2 are appropriately implemented will be essential for the ISSB to develop a proven track record and promote buy-in and credibility on a global stage. These actions will also help to reduce the risk of inconsistency across different jurisdictions, thereby improving the comparability of sustainability-related financial disclosures.

4. We further note that supporting the implementation of new standards is something that can take significant time for boards developing or endorsing these new requirements. For example, to support the recent implementation of IFRS 17 *Insurance Contracts*, the AcSB undertook extensive dialogue with its stakeholders to ensure it was appropriately informed and educated on key matters impacting implementation – this included staff conducting meetings with association groups, regulators and specialists, as well as hosting special board sessions to review and assess results. The implementation of IFRS 17 also required a substantial work effort from the IASB which included the development of educational materials and webinars, the establishment of a Transition Resource Group, the publication of IFRIC agenda decisions and the issuance of multiple rounds of amendments to respond to implementation-related concerns.

5. The ISSB may need to dedicate extensive resources to adequately support the implementation of IFRS S1 and S2, which should be considered as part of the ISSB's future resourcing allocations.

Connectivity in reporting and interoperability with other sustainability standards

6. Ensuring connectivity between the ISSB's and IASB's respective requirements is essential in providing decision-useful information to users. Accordingly, we are extremely supportive of the ISSB continuing to prioritize connectivity in reporting as a core activity by working together with the IASB. As outlined in the Request for Information, these activities could include:
   - collaborating with the IASB to ensure that the requirements in IFRS S2 are compatible with the output of the IASB's project on Climate-related Risks in the Financial Statements; and
   - working together with the IASB on other projects that have sustainability-related considerations (e.g., the IASB's pipeline project on pollutant pricing mechanisms).

7. While the Request for Information highlights certain areas where connectivity has been achieved throughout IFRS S1 and S2, we also note that there are several connectivity gaps that still need to be addressed. For example, there may be instances where the disclosure of sustainability-related risks and targets creates a user expectation that a provision or contingent liability exist, but neither are reflected in the financial statements (please refer to the Addendum on page 7 for further details and examples). The ISSB may want to consider whether additional qualitative disclosures are required in IFRS S1 and S2 to provide an explanation in cases where material sustainability-related risks or targets are not recognized or reflected in the financial statements.

8. Many users expressed a desire to better understand the financial costs of entities' sustainability-related commitments (e.g., net zero targets) as well as when sustainability-related risks and targets would ultimately impact the financial statements. The ISSB is encouraged to work together with the IASB to consider whether non-authoritative guidance to address these matters is required or, at a minimum, collaborate with the IASB on any relevant standard-setting initiatives. Working together with the IASB on these matters will be critical in ensuring that the financial statements and sustainability-related financial disclosures flow together as a cohesive reporting package.

9. We are also extremely supportive of the ISSB considering the interoperability of its standards with other jurisdictional sustainability standards as a core activity. Many preparers of multinational corporations expressed concerns that if jurisdictions like the U.S. and Europe require different sustainability disclosures, it would add significant costs to reporting and reduce comparability for users. To achieve comparable sustainability-related financial information on a global scale, the ISSB needs to work closely with other jurisdictions early in the process to resolve interoperability issues.

Beginning new research and standard-setting projects

10. While we are not opposed to the ISSB beginning research on potential areas of standard setting, we have concerns if the ISSB develops standards too quickly during a period when many preparers would be focused on implementation. As such, the ISSB should consider when to go to the market for feedback on any new proposals, given the focus on implementation.

11. Reporting entities need time to build their internal reporting capacity to adequately disclose the information currently required by IFRS S1 and S2. This includes adopting process changes to implement these new standards, as well as gathering information to disclose relevant data. For example, during the implementation of IFRS 17, many preparers raised concerns around their systems readiness to implement the new standard, ultimately resulting in a delay to the standard's effective date.

12. While we acknowledge that more standards on sustainability reporting topics may be required, the ISSB should ensure that entities have had a chance to fully implement and adopt IFRS S1 and S2. We are concerned that, if the ISSB starts releasing consultation documents during this critical implementation period, many stakeholders would not have the capacity to share views on new

proposals. This could affect the quality of future standards developed. Furthermore, if new sustainability reporting standards become effective too quickly, this could overwhelm preparers and set an unrealistic precedent for reporting sustainability-related information. This could also have knock-on effects in the market by sacrificing the quality and reliability of sustainability-related financial disclosures. Therefore, careful consideration is required from the ISSB in planning out future research projects.

13. Our consultations have focused more on the implications of the ISSB's work plan from a financial reporting perspective. As a result, other respondents such as the Canadian Sustainability Standards Board will provide more insights on the prioritization of sustainability research projects.

Question 2 – Criteria for assessing sustainability reporting matters that could be added to the ISSB's work plan
Paragraphs 24 – 26 discuss the criteria the ISSB proposes to use when prioritizing sustainability-related reporting issues that could be added to its work plan. a) Do you think the ISSB has identified the appropriate criteria? b) Should the ISSB consider any other criteria? If so, what criteria and why?

AcSB Response

14. Overall, we think that the ISSB has identified the appropriate criteria when prioritizing sustainability-related reporting issues and note that these are broadly consistent with those used by the IASB.

15. Particularly, going forward, we think that it will be important for the ISSB to consider the needs of users to ensure that it can effectively respond to emerging sustainability-related matters and develop relevant sustainability reporting standards. The ISSB should also carefully consider the capacity of its stakeholders to engage with the development and implementation of new standards as it considers which new projects to add to its work plan.

16. In addition to the criteria listed, we also encourage the ISSB to consider the interaction of its projects with IASB standard setting projects (and vice versa). This is important because:
    - the IASB and ISSB will need to work together to ensure that their respective requirements are connected and consistent; and
    - the IASB and ISSB will want to be cognizant of the volume of new standards being issued or consulted on by each respective board as these will require implementation and adoption or input by and from many of the same individuals at reporting entities.

Question 7 – New research and standard-setting projects that could be added to the ISSB's work plan: Integration in reporting
The research project on integration in reporting is described in paragraphs A38 – A51 of Appendix A. Please respond to the following questions: a) The integration in reporting project could be intensive on the ISSB's resources. While this means it could hinder the pace at which the topical development standards are developed, it could also help realize the full value of the IFRS Foundation's suite of materials. How would you prioritize advancing the integration in reporting project in relation to the three sustainability-related topics (proposed projects on biodiversity, ecosystems and ecosystem services; human capital; and human rights) as part of the ISSB's new two-year work plan?

b) In light of the coordination efforts required, if you think the integration in reporting project should be considered a priority, do you think it should be advanced as a formal project with the IASB, or pursued as an ISSB project (which could still draw on input from the IASB as needed without being a formal joint project)?
   (i) if you prefer a formal joint project, please explain how you think this should be conducted and why.
   (ii) if you prefer an ISSB project, please explain how you think this should be conducted and why.

c) In pursuing the project on integration in reporting, do you think the ISSB should build on and incorporate concepts from:
   (i) the IASB's Exposure Draft Management Commentary? If you agree, please describe any particular concepts that you think the ISSB should incorporate in its work. If you disagree, please explain why.
   (ii) the Integrated Reporting Framework? If you agree, please describe any particular concepts that you think the ISSB should incorporate in its work. If you disagree, please explain why.
   (iii) other sources? If you agree, please describe the source(s) and any particular concepts that you think the ISSB should incorporate in its work.

d) Do you have any other suggestions for the ISSB if it pursues this project?

AcSB Response

19. While we are not opposed to an eventual project on integration in reporting, we think that this should not be an area of priority for the ISSB during the next two years. We think that it is ambitious to develop a new integrated reporting framework while the ISSB's inaugural sustainability standards are being newly adopted and implemented by entities. It is unlikely that companies will have the ability to interpret, implement and adopt a new type of reporting framework in the near-term while building their internal reporting capacity to adequately disclose the information required in IFRS S1 and S2.

20. Instead, we recommend that the ISSB allow sufficient time for implementation, including connectivity with the financial statements, and build out a broader suite of sustainability reporting standards. This approach will set the groundwork for high-quality, connected reporting between the financial statements and sustainability-related financial disclosures, which will help to build a strong foundation for any future initiatives on integration in reporting.

21. Going forward, we also recommend that any project on integration in reporting be pursued in tandem with the IASB as opposed to being a sole project of the ISSB. This will allow the ISSB to leverage relevant concepts more effectively from the IASB's Management Commentary project and better reflect the ISSB's and IASB's assumed responsibility for the existing Integrated Reporting Framework. This approach will also help to ensure that any new reporting framework developed is cohesive and appropriately reflects how an entity creates value.

Addendum

22. The below content is a paper written by AcSB staff for the International Forum of Accounting Standard Setters (IFASS), which outlines connectivity concerns between sustainability-related information and accounting requirements in IAS 37 – *Provisions, Contingent Liabilities and Contingent Assets*. This has been included to provide additional context to ISSB staff and members.

23. Please note that this paper was written in March 2023 and includes references to draft IFRS S1 and S2 standards.

Context

IFRS Accounting Standards

1. IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* defines provisions as liabilities of uncertain timing or amount. The liabilities may be legal or constructive obligations. Constructive obligations arise from an entity's actions, through which it has indicated to others that it will accept certain responsibilities, and as a result has created a valid expectation that it will discharge those responsibilities.

2. A provision is recognized when:

   (a) an entity has a present obligation (legal or constructive) as a result of a past event;

   (b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and

   (c) a reliable estimate can be made of the amount of the obligation.

3. If these conditions are not met, such as in the case of contingent liabilities, no provision is recognised. Contingent liabilities include:

   (a) present obligations that arise from past events but that are not recognized because an outflow is not probable and/or a reliable estimate cannot be made; and

   (b) possible obligations that arise from past events and whose existence will be confirmed only by uncertain future events that are not wholly within the entity's control.

4. Contingent liabilities are disclosed, unless the probability of an outflow is remote.

5. IAS 37 also contains guidance on contingent assets. Although these are not the focus of this paper, they are relevant to the discussion of connectivity. Contingent assets are the asset-equivalent of the second type of contingent liabilities described above, i.e., they are possible *assets* rather than possible *obligations*. Similar to contingent liabilities, they are disclosed and not recognized.[1]

6. For provisions and contingent liabilities, entities would disclose their nature, an indication of uncertainties about the amount or timing of related outflows, and possible reimbursements. For provisions, entities would also disclose major assumptions about future events, and for contingent liabilities, entities would also disclose an estimate of their financial effect (where practicable). For contingent assets, entities would only need to disclose their nature and an estimate of their financial effect (where practicable).

7. IAS 37.92 exempts these disclosures "in extremely rare cases" when disclosure can be expected to prejudice seriously the entity's position in a dispute with other parties. In such cases, the entity would instead disclose the general nature of the dispute together with the fact that, and reason why, the information has not been disclosed.

[1] Contingent assets are not recognized because this may result in recognizing income that may never be realized.

<u>IFRS Sustainability Disclosure Standards</u>

Financial effects of sustainability-related risks and opportunities

8. Paragraph 22 of draft IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* requires entities to disclose the current and anticipated financial effects of sustainability-related risks and opportunities. Paragraph 14 of draft IFRS S2 *Climate-related Disclosures* contains similar requirements for climate-related risks and opportunities. Given the similarity, this paper focuses on IFRS S1 for simplicity.

9. Under draft IFRS S1.22, an entity would need to disclose:

   (a) how sustainability-related risks and opportunities have affected its most recently reported financial position, financial performance and cash flows;

   (b) information about the sustainability-related risks and opportunities identified in (a) above for which there is a significant risk that there will be a material adjustment to the carrying amounts of assets and liabilities reported in the financial statements within the next financial year;

   (c) how it expects its financial position to change over the short, medium and long term, given its strategy to address sustainability-related risks and opportunities, reflecting:

      (i) its current and committed investment plans and their anticipated effects on its financial position (e.g., capital expenditure, major acquisitions and divestments, joint ventures, business transformation, innovation, new business areas and asset retirements);

      (ii) its planned sources of funding to implement its strategy; and

   (d) how it expects its financial performance to change over the short, medium and long term, given its strategy to address sustainability-related risks and opportunities.

10. The ISSB also tentatively decided that an entity would need to explain the connections between those risks and opportunities and their current and anticipated financial effects. In addition, it would need to provide quantitative information about the financial effects unless it is unable to do so, in which case it would provide qualitative information. In determining whether it is able to provide quantitative information on a particular sustainability-related risk or opportunity, it would consider:

    (a) whether the financial effects of that risk or opportunity are separately identifiable;

    (b) whether a high level of outcome or measurement uncertainty is involved in quantifying the financial effects of that risk or opportunity; and

    (c) in case of the anticipated financial effects only, whether the entity has the skills, capabilities and resources to provide quantitative information about those effects.

Exemption for commercially sensitive information on opportunities

11. In January 2023, the ISSB introduced an exemption in IFRS S1 to permit an entity to exclude commercially sensitive information from its disclosure of sustainability-related opportunities. The ISSB also considered but rejected the idea of expanding the exemption to sustainability-related risks. Consequently, entities would have to disclose information about these risks regardless of commercial sensitivity.

12. An entity applying the exemption would instead disclose the fact that it has used the exemption. It would not be able to use commercial sensitivity as a justification for broad non-disclosure. An entity could only apply this exemption if:

(a) it has a specific reason for not disclosing information, such that keeping the information from being publicly available would provide the entity with an economic benefit that would translate to a competitive advantage;

(b) disclosing the information could be expected to prejudice seriously the economic benefits the entity is able to realise in pursuing the opportunity; and

(c) the entity determines it is not possible to disclose the information in a manner or at a level of aggregation that would resolve the entity's concerns about commercial sensitivity.

Targets and transition plans

13. Draft IFRS S1 and S2 also require entities to disclose sustainability-related targets they have set, including performance against/progress towards those targets. Under draft IFRS S2, these targets would include those set to mitigate or adapt to climate-related risks or maximize climate-related opportunities. Entities would also need to disclose their transition plans, which would include the actions they plan to take to transition towards a lower-carbon economy.

Areas of potential overlap/misalignment

User expectations

14. When users read an entity's sustainability disclosures, they would find information about both the current and anticipated financial effects of sustainability-related risks and opportunities. When users turn to the entity's financial statements, they would expect to see the current financial effects under IFRS S1.22(a) reflected in the balances. They may also expect to see the anticipated financial effects recognized as provisions or disclosed as contingent liabilities/assets. This expectation would be higher where the entity has disclosed:

    (a) information under IFRS S1.22(b) about sustainability-related risks and opportunities for which there is a significant risk that there will be a material adjustment to the carrying amounts of assets and liabilities within the next year. For example, this may indicate an outflow is probable, which is a consideration in identifying provisions and contingent liabilities under IAS 37.

    (b) the anticipated financial effects in *quantitative* terms. This would indicate that a reliable estimate can be made, which is another consideration in identifying provisions and contingent liabilities under IAS 37.

    (c) information under IFRS S1.22(c) on how the entity expects its financial position to change over time given its sustainability strategy, reflecting current and committed investment plans and planned sources of funding. If an entity discloses this information about its sustainability-related *opportunities*, that means it has not applied the exemption in IFRS S1 for commercially sensitive information to the IFRS S1.22(c) requirement. This exemption is not available for sustainability-related *risks*, so the entity would need to disclose the IFRS S1.22(c) information on those risks even if it were considered commercially sensitive. Once this information has been included in the entity's sustainability disclosures, users may expect that the entity would provide all the related IAS 37 disclosures. That is, they may expect that the entity would not use the IAS 37.92 exemption from disclosing commercially sensitive information about contingent assets, provisions or contingent liabilities in the financial statement notes.

15. Where the entity discloses sustainability-related targets (e.g., net-zero emissions) and transition plans, that may create an expectation among users that the entity will meet those targets by taking the actions disclosed. As a result, that may give rise to a constructive obligation. When users turn to the financial statements, it is not clear if they would expect to see a provision recognized or a contingent liability disclosed. In an entity's management reporting, the entity may currently disclose a variety of targets and strategic plans related to matters other than sustainability. However, not all of these translate to provisions or contingent liabilities in the entity's financial reporting. Depending on

the nature and extent of information disclosed on the entity's sustainability-related targets and transition plans, as well as how users are relying on this information, it is possible that some users may expect a provision or contingent liability to result. For example, if a customer is only doing business with an entity due to the entity's commitment to net-zero emissions, would this create a valid expectation that the entity will meet that commitment (i.e., a constructive obligation)?

Connectivity concerns

When disclosure/recognition is triggered

16. Both the draft IFRS S1/S2 disclosures (on anticipated financial effects, targets and transition plans) and the IAS 37 guidance (on provisions, contingent liabilities and contingent assets) deal with uncertainties regarding the future. However, it is not always clear when disclosure under IFRS S1/S2 triggers disclosure/recognition under IAS 37. This could reduce comparability between entities and cause confusion for users. For example:

    (a) If, for certain sustainability-related risks/opportunities, there is a significant risk of a material adjustment to the carrying amounts of assets/liabilities within the next year, IFRS S1 would require this to be disclosed. Entities may have different interpretations of whether "a significant risk of a material adjustment" under IFRS S1.22(b) would translate to a "probable outflow of resources" in the recognition guidance for provisions under IAS 37.

    (b) If an entity discloses extensive information on its sustainability-related targets and transition plans, a constructive obligation may be created. This may occur when the information creates a valid expectation among other parties that the entity will meet those targets and plans, and the parties make decisions based on that valid expectation. Judgment may be required in determining whether this would give rise to either a provision or contingent liability. Given the level of inherent uncertainty around the amounts and timing of outflows, it may be more likely for this to be treated as a contingent liability than as a provision. However, judgment would still be required in determining whether a contingent liability exists at each reporting date. Moreover, these and certain other sustainability disclosures could cover longer-term impacts that may not trigger either disclosure or recognition under IAS 37, but this may not be obvious to users without explanation.

Commercial sensitivity

17. Both IFRS S1 and IAS 37 contain exemptions from disclosing commercially sensitive information where disclosure could be expected to prejudice seriously the entity's position. However, the exemption in IFRS S1 is asymmetric (only applies to opportunities and not risks), whereas the exemption in IAS 37 is symmetric (applies to contingent assets as well as provisions and contingent liabilities).

18. While an entity may be exempt from disclosing information on provisions or contingent liabilities for sustainability-related risks in its financial statements, it would still be required to provide information on those risks in its sustainability disclosures. This could prejudice seriously the entity's position, for example, where the entity is in disputes with regulators regarding remediation for environmental damage.

Possible solutions

When disclosure/recognition is triggered

19. The IASB and ISSB would need to work together to clarify when disclosure of anticipated financial effects, targets and transition plans in IFRS S1 and S2 would trigger recognition of a provision or disclosure of a contingent liability under IAS 37.

20. In particular, the Boards could promote consistency in how entities interpret these requirements through standard-setting action at the ISSB level, such as using similar terminology to the IASB (e.g., “significant risk” in IFRS S1.22(b) vs. “probable” in IAS 37).

21. The IASB could also explore introducing illustrative guidance. For example, it could add an example to show when disclosure of sustainability-related targets and transition plans could trigger provisions or contingent liabilities. However, the IASB should consider any potential guidance in a broader context than just sustainability matters, as this may have also implications where an entity discloses other targets and transition plans in its management commentary that are not related to sustainability.

22. In addition, certain sustainability-related risks and opportunities that would be disclosed under IFRS S1 and S2 could be longer-term in nature and thus may not trigger either disclosure or recognition under IAS 37. That is, they may not appear at all in the financial statements or notes. To improve connectivity, it may be useful for entities to explain why that is the case. The ISSB recently decided that entities would need to explain the connections between sustainability-related risks and opportunities and their current and anticipated financial effects. However, understanding some of the disconnects may also be material to users’ overall understanding of the entity’s general purpose financial reporting. To support this, the IASB and ISSB could explore providing educational guidance (including examples) to help preparers identify when disclosing an explanation of such disconnects would be warranted to meet the objectives of both the Accounting and Sustainability Disclosure Standards. If the Boards determine that standard-setting action is needed to clarify when such disclosure is warranted, then one avenue to begin exploring this could be the IASB’s new project on Climate-related Risks in the Financial Statements.

Commercial sensitivity

23. Standard-setting action may be needed to deal with the misalignment in the exemptions across IFRS S1 and IAS 37 for disclosing commercially sensitive information. If entities are required to include commercially sensitive information on sustainability-related risks in their sustainability disclosures, users may question why there is no corresponding disclosure in the financial statement notes.

24. In considering whether to extend the exemption in IFRS S1 to such risks, the ISSB discussions centred on the appropriateness of asymmetry between the disclosure requirements for risks versus opportunities. For example, the ISSB staff noted that investors may be exposed to downside risk if entities do not disclose risks to their business, which is different from investors missing out on potential upside if entities do not disclose opportunities. While that may be the case, the IAS 37 exemption effectively covers both sides (contingent assets as well as provisions and contingent liabilities). One solution could be for the ISSB to revisit its decision to limit the IFRS S1 exemption to opportunities, and to expand it to include risks similar to IAS 37. Another solution could be for the IASB to revise the IAS 37 exemption to align with the asymmetrical approach taken in IFRS S1.

Illustrative examples

25. Illustrative examples outlining potential areas overlap and/or misalignment for different industries are included in the tables below. Please note that these use existing climate-related disclosures in line with the Task Force on Climate-related Disclosures (TCFD) as a proxy for the IFRS S1 and S2 requirements discussed above.

26. While some areas of linkage have been noted in the following examples, several areas of misalignment have been highlighted in accordance with the discussion above.

27. Example #1: Banking Industry

<table>
<tr><th>TCFD Disclosure</th><th>Financial Statement Disclosure</th><th>Overlap/Misalignment</th></tr>
<tr><td>Risks
Company highlights specific risks related to climate, including:
Possibility for increased credit risk (i.e., for clients most affected by physical and transition climate risks);
Increased operating or litigation costs related to environmental policies or regulations;
Damage to facilities or lack of insurability of assets.</td><td>Risks
No specific information is included on the financial impact of climate-related risks.</td><td>Risks
Unclear to users whether the climate risks identified had an impact on existing provisions in the current fiscal year.
Unclear to users whether any of the climate risks identified could lead to the recognition and/or disclosure of additional liabilities in the financial statements.</td></tr>
<tr><td>Targets
Company outlines their climate strategy and commitments. including:
Indicates the company will reduce greenhouse gas emissions by 70% by 2025 and maintain carbon neutrality in global operations;
Includes commitments to achieve $500B in sustainable financing by 2025;
Pledges to join the net-zero banking alliance (NZBA) as part of a global initiative to accelerate and support efforts to address climate change.</td><td>Targets
No specific information is included on the financial impact of climate-related commitments.</td><td>Targets
Unclear to users whether any of the climate commitments outlined would be considered a constructive obligation and lead to the recognition of a provision, or disclosure of a contingent liability, in the financial statements.</td></tr>
</table>

28. Example #2: Extractives Industry

TCFD Disclosure	Financial Statement Disclosure	Overlap/Misalignment
Risks • Company identifies risks associated with climate, including the physical impacts of climate change (e.g., increase in extreme weather events) and an increase in environmental regulations.	Risks • Details on the recognition of environmental rehabilitation provisions are discussed, including that management's "expectations [for the provision] are formed based on existing environmental and regulatory requirements."	Risks • Some linkage provided between the risk of increased environmental regulations and the recognition of environmental rehabilitation provisions. • Unclear to users whether any of the other climate risks identified could lead to the recognition and/or disclosure of additional liabilities in the financial statements.

Targets
• Company highlights several commitments and goals related to climate, including:
  ○ Decarbonization of energy sources;
  ○ Achieving net zero by 2050; and
  ○ Specific action items related to water and biodiversity.
	Targets
	• No specific information is included on the financial impact of climate-related commitments.
		Targets
		• Unclear to users whether any of the climate commitments outlined could be considered a constructive obligation and lead to the recognition of a provision, or disclosure of a contingent liability, in the financial statements.

29. Example #3: Utilities Industry

TCFD Disclosure	Financial Statement Disclosure	Overlap/Misalignment

Risks
• Company highlights specific risks related to climate, including:
  ○ Company could be subject to claims for damages from events related to its assets (e.g., forest fires) and ability to transmit electricity;
  ○ Failure to comply with government environmental regulation could subject the company to fines or penalties;
  ○ Prescence or release of harmful substances could lead to claims by third parties or require the company to take remediation action.
	Risks
	• Details on the recognition of environmental liabilities are discussed, including that these liabilities are recognized when "it is determined that future environmental remediation expenditures are probable under existing statute or regulation and the amount of future expenditures can be reasonably estimated."
	• Disclosure confirms that the outcome of existing claims and lawsuits are not expected to have a material impact on the company.
		Risks
		• Some linkage provided between climate-related risk disclosures (I.e., government regulation and need to take remediation action) and the recognition of environmental liabilities.
		• Some linkage provided between climate-related risk disclosures (I.e., being subject to claims or damages) and the disclosure of contingent liabilities.
		• Unclear to users whether any of the other climate risks identified could lead to the recognition and/or disclosure of additional liabilities in the financial statements.