

Chairman's Report IFRS Advisory Council November 2020

1. The Advisory Council met on 3 and 4 November 2020 by videoconference. In addition to the Advisory Council members, the meeting was attended by the Chair of the Trustees of the IFRS® Foundation, Mr. Erkki Liikanen, as well as several International Accounting Standard Board® (Board) members and IFRS Foundation staff.
2. In order to receive more detail about the topics discussed and to hear the public meeting verbatim, Trustees may also be interested in accessing web-based records of the meeting, in addition to reading this report. Both the agenda and papers for the meeting and the meeting recording are available at:
www.ifrs.org/news-and-events/calendar/2020/november/ifrs-advisory-council/
3. The Advisory Council received an update on recent Trustee activities (Agenda Paper 1). Mr. Liikanen thanked the Council members for all of their contributions to the Foundation and recognised the strong diversity of experience amongst the members. He highlighted the following three priorities since the Council had last met:
 - Covid-19 – the Foundation had continued to operate effectively, and the staff were thanked for responding to the challenges that have arisen.
 - Nominating Committee – the Committee had been very busy with a number of roles requiring succession. Of particular focus has been the succession of the IASB Chair and an announcement of the selection was expected soon. (N.B. an announcement regarding the appointment of Prof Dr Andreas Barckow as IASB Chair was published on 12 November.)
 - Sustainability – the Trustees' *Consultation Paper on Sustainability Reporting* was published on 30 September and responses to the paper can be made until 31 December 2020. Particular points that were made relating to the consultation were:
 - The consultation paper was developed based on a demand-driven process
 - Open-ended questions were included to encourage the greatest level of response
 - Trustees are listening and learning through the consultation
 - The paper notably set out proposed key requirements for success of a Sustainability Standards Board (SSB) (paragraph 31) if such a board were to be established.

Council members raised a range of questions to Mr. Liikanen. These questions covered issues related to the following:

- The expertise needed for an SSB,
- The proposed SSB's funding and financial support,
- Timelines,
- Support of supervisors and regulators, and

- Engagement with the group of five bodies currently involved with sustainability work.

Comments to these questions emphasised the open spirit of the consultation and a prudent approach.

Finally, the Council was advised that since they had last met, the updated *Due Process Handbook* had been issued and that a new website for the IFRS Foundation would be launched in first quarter of 2021.

4. Sue Lloyd, Vice Chair of the Board, provided an update of the Board's activities since the last meeting (Agenda Paper 2). She noted that the Board:
 - issued urgent amendments, as planned, on amendments to IFRS 17 *Insurance Contracts*, and IBOR Reform – phase 2.
 - continues to monitor stakeholder capacity in light of covid-19 challenges and adjusts the comment periods and publication dates as needed to assist stakeholders.
 - decided to begin the post-implementation review (PIR) of the classification and measurement requirements in IFRS 9 *Financial Instruments* and will reconsider at a later date the start dates of the PIRs on IFRS 15 *Revenue from Contracts with Customers* and the impairment and hedge accounting requirements in IFRS 9.

Ms. Lloyd also discussed updates to the *Due Process Handbook* related to:

- effects analysis – the updates reinforce the importance of effects analysis and require it throughout the entire research and standard-setting process.
- agenda decisions – the updates explain that agenda decisions:
 - cannot change existing IFRS requirements,
 - derive their authority from reference to existing requirements and
 - must be followed by companies where applicable in order to be compliant with IFRS Standards.

The updates also require a new step in which the Board is asked whether they object to the agenda decision prior to finalisation.

Ensuing discussion among AC members covered:

- location of agenda decisions – they are available in the annotated versions of the bound volumes of IFRS Standards, alongside the related requirement in the Standard, and on the IFRS Foundation website. Given the importance of agenda decisions, additional means of accessibility are being investigated.
- confirmation that past agenda decisions meet the criteria in the revised *Due Process Handbook*.
- the need for careful balance between agenda decisions supporting consistent application, which may run the risk of undermining the principles in IFRS Standards, and the use of judgment.
- the quality of disclosures on expected credit losses.
- the status of the project on the equity method of accounting.

MEETING REPORT

IFRS® Advisory Council meeting

5. Agenda Paper 3 reported how the IFRS Foundation has incorporated past Advisory Council feedback into its strategic activities related to relevance, risk, process and the IFRS Standards, since the last Council meeting.

Advisory Council feedback is reported to the Trustees, Board and staff after every meeting. In addition, the Chair of the Advisory Council attends Trustee meetings to enable further communication.

Feedback amongst Advisory Council members included:

- encouragement of continued (i) efforts on monitoring consistent adoption of IFRS Standards and (ii) coordination of stakeholder engagement activities
- requests for the status of organisational learning and skills related to technology and sustainability
- a request for more specificity on KPIs at a future meeting.

Members also requested that future reports take note of Advisory Council advice to the Trustees and the Board that has not yet been implemented along with next steps.

6. The main agenda item that was discussed and on which Advisory Council advice was provided pertained to the consultation paper on sustainability reporting.

The Advisory Council Chair thanked the Council members who were able to participate in the small group meetings in early October. He advised that those conversations would provide an excellent foundation on which to build for this meeting.

The Advisory Council Chair indicated that he would like the Council discussions to be structured along the lines of the 11 questions in the consultation paper starting with the more foundational questions (questions 1 and 2) before drilling down to the more specific questions. For ease of reference, the consultation paper questions are set out below followed by the related Advisory Council feedback.

Advisory Council members provided the following feedback on the questions:

Question 1
<p>Is there a need for a global set of internationally recognised sustainability reporting standards?</p> <p>(a) If yes, should the IFRS Foundation play a role in setting these standards and expand its standard-setting activities into this area?</p> <p>(b) If not, what approach should be adopted?</p>

There was strong support from the Council for the need for a global set of internationally recognised sustainability reporting standards. Many members were of the view that current guidance and practices in global capital markets are overly fragmented and that the demand for better disclosure is urgent. The development of

and changes in the global investor community over the past 15 years was considered as sustainability has become a crucial element in this segment's analysis.

Question 2

Is the development of a sustainability standards board (SSB) to operate under the governance structure of the IFRS Foundation an appropriate approach to achieving further consistency and global comparability in sustainability reporting?

There was general support for the creation of an SSB within the IFRS Foundation, especially in light of the Foundation's established legitimacy and credibility. In discussing the role that the Foundation could play in setting standards through an SSB the following points were covered:

- The interconnectedness between financial reporting and sustainability reporting. There was a view that 'no blind spots' should exist in corporate reporting if the SSB were created. Many provided thoughts on how the two Boards could operate together but a sense all investor needs should be covered.
- Reference was made to the parallel between financial reporting some 20+ years ago and the current state of sustainability reporting.
- The SSB should not add to the current complexity that exists with the many different groups involved in the accounting standard-setting process.
- The speed by which an SSB could be created and to then begin producing quality standards must be balanced by the urgent demand for such standards. Discussion included whether the due process activities could be shortened. The theme of 'look for some quick wins' was noted.
- The proposal of initially creating a *Council* (rather than a *Board*) similar to how the IASC/IASB evolved as some members believed that this would allow greater flexibility and promote engagement with other standard setters.
- Some members noted the desirability of developing an associated conceptual framework while others noted the impact it would have on the timing for developing standards, which in their view is urgent.

Question 3

Do you have any comment or suggested additions on the requirements for success as listed in paragraph 31 (including on the requirements for achieving a sufficient level of funding and achieving the appropriate level of technical expertise)?

There was no disagreement among members regarding the seven proposed requirements for success of an SSB, which in the view of some Advisory Council members would be more aptly named the Sustainability Reporting Standards Board (or SRSB). There were however requests for additional detail and elaboration.

Paragraph 31(a) - *achieving a sufficient level of global support from public authorities, global regulators and market stakeholders, including investors and preparers, in key markets*: The importance of regulatory support was emphasised. It was also noted that appropriate public support could create momentum for existing

regional and global initiatives to cooperate and/or consolidate. Some also questioned whether buy-in was required from all stakeholders from the start, suggesting careful stakeholder analysis could identify those who could provide critical input. Others noted that a sound conceptual framework for sustainability reporting could help achieve support for the standards.

Paragraph 31(b) - *working with regional initiatives to achieve global consistency and reduce complexity in sustainability reporting*: There was strong emphasis on the importance of achieving buy-in from existing global organisations and initiatives working in the sustainability reporting field (eg the Financial Stability Board's Task Force on Climate-related Financial Disclosures). This, it was argued, is essential in helping to ensure a new SSB would consolidate, rather than add to, the complexity. The importance of clarity of scope and mission was highlighted to determine whether the objective is cooperation or consolidation. Some members expressed the view that achievement of paragraph 31(a) might lessen the urgency of achieving this requirement.

Paragraph 31(c) - *ensuring the adequacy of the governance structure*: Some noted the political sensitivity around environmental, social and governance (ESG) themes and therefore good governance is key to maintaining a SSB's independence. A clear mission statement and reviewing the role and structure of the Monitoring Board were emphasised as important to achieving this independence.

Paragraph 31(d) - *achieving appropriate technical expertise for the Trustees, SSB members and staff*: It was highlighted that an SSB would require a broad range of skills that are different to those of the IASB, including how to measure, not just report on sustainability. The ability to secure these skills was highlighted as a risk. Furthermore, SSB members should not only have relevant technical expertise but represent a diversity of industries and geographical regions and be major participants in capital markets.

Paragraph 31 (e) - *achieving the level of separate funding required and the capacity to obtain financial support*: It was suggested that a part-time SSB could reduce financial pressures. The importance of appropriate funding was also highlighted, noting if those that are seen to contribute to climate change are funding the standards, it could undermine independence and integrity.

Paragraph 31 (f) - *developing a structure and culture that seeks to build effective synergies with financial reporting*: The importance of achieving a synergy between financial and non-financial information was emphasised, noting that, if non-financial information is not quantifiable and did not relate to cash flows, it will not create value for users. The Foundation's ability to make this connection was considered a strong argument in favour of its possible role in establishing a SSB. There was also discussion about how the two Boards would work together, noting that Management Commentary might look very different if a SSB were to be established.

Paragraph 31 (g) - *ensuring the current mission and resources of the IFRS Foundation are not compromised*: The importance of not diverting IASB financial and human resources to a new SSB were emphasised.

Members were of the view that the following areas were missing or required further definition as ‘requirements for success’:

- **Timeliness** - A number of participants emphasised that timeliness of delivery should be a requirement for success, particularly considering the urgency posed by climate risk. Some noted the rigour of the Foundation’s Due Process may limit the ability to develop sustainability reporting standards in a sufficiently timely manner and questioned whether the SSB should have its own processes. However, it was also highlighted that the Foundation’s reputation for developing quality standards could be jeopardised if complex areas are not given the adequate time required to develop related standards properly. Using knowledge and skills of other organisations, creating an ‘acting Board’ to develop a prototype and narrowing the initial scope of target organisations required to apply the standards, were some of the suggestions made to improve timeliness.
- **Scope** - The importance of a well-defined scope as a requirement for success was also highlighted. It was suggested that the scope should clearly define key themes, including what is meant by ‘sustainability’ and ‘climate-related’ and clarify how the SSB intended to work with other initiatives (cooperation or consolidation); whether its focus was single or double materiality; and whether it would focus on climate-related disclosures only or would expand into *Social* and *Governance*.

Question 4

Could the IFRS Foundation use its relationships with stakeholders to aid the adoption and consistent application of SSB standards globally? If so, under what conditions?

Question 5

How could the IFRS Foundation best build upon and work with the existing initiatives in sustainability reporting to achieve further global consistency?

Question 6

How could the IFRS Foundation best build upon and work with the existing jurisdictional initiatives to find a global solution for consistent sustainability reporting?

Questions 4, 5 and 6 were addressed collectively. During the discussion the following themes arose:

- **Key factors underpinning consistent application** - The importance of clear definitions and measurements, supported by education, was highlighted as key to achieving consistency. Members noted, however, that political sensitivities could hamper the ability to reach globally-agreed definitions. Members also asked for clarification on whether application of sustainability standards would be mandatory to claim compliance with IFRS Standards, and who would be the appropriate regulatory body to oversee application.

- Working with existing initiatives to achieve global consistency - Identifying where the Foundation can add value to the process and promote the interests of stakeholders was noted as key to addressing these three questions. It was also suggested that distinguishing between different scopes of certain initiatives could assist clarity. For example, the Foundation focuses on those standards relevant for investors while the European Union focuses on standards for the broader public interest.
- Working with existing initiatives to achieve globally consistent standards - The importance of integrating key features of existing standards was discussed. These standards should be comprehensively researched, aggregated, tied to concepts of reporting, rationalised and ratified. It was noted that cooperation with existing initiatives was key to this. There was also discussion about whether a global framework could allow flexibility for additional requirements at a regional or jurisdictional level.
- Need for a balanced scorecard - The conflict between an environmental focus and the need to reduce poverty was discussed. For example, providing people access to electricity may entail sub-optimal approaches from a 'green' perspective. As a result, a balanced scorecard could be developed to avoid restricting economies that are growing their society. This would acknowledge a higher social score, even if the environmental score is low.

Question 7

If the IFRS Foundation were to establish an SSB, should it initially develop climate-related financial disclosures before potentially broadening its remit into other areas of sustainability reporting?

Question 8

Should an SSB have a focused definition of climate-related risks or consider broader environmental factors?

Question 9

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

Questions 7, 8 and 9 were addressed collectively. During the discussion the following themes arose:

- Climate-first approach - The discussion highlighted that a climate-first approach would provide early proof of concept that the SSB functions, and the sense of urgency around climate change was important to gain momentum and quickly achieve quantifiable information that can be assured. These members cautioned that expanding beyond climate could be overly ambitious (ie a 'baby steps' approach is the right way to start). However, some members questioned whether climate was indeed the priority for sustainability reporting or whether the pandemic and business practices of off-shoring employees and sourcing products from overseas were currently more relevant. Some also raised the risk that, if the

SSB did not expand into *Social* and *Governance*, other initiatives would develop in this space.

- Materiality - The importance of providing decision-useful information for investors and other market participants was emphasised, highlighting this was most easily achieved by focusing on single materiality. However, it was also noted that the interests of a wider range of stakeholders may promote a broader scope that includes double materiality. Some suggested that a double materiality approach would increase the complexity of standards. Others suggested that a single materiality approach is insufficiently ambitious and that, if the proposed SSB did not take the lead and address the hard questions relating to double materiality, it would simply cover ground already addressed by other initiatives. Views were also expressed that “relevance” is the better metric as “materiality” is too subjective.
 - Developing a conceptual framework - A number of members supported the development of a conceptual framework for ESG reporting. It was suggested that, if a framework was developed that encompassed all relevant ESG factors, the SSB could then determine the areas on which it wished to focus.
 - Developing a vision and timeline - Although there was overall support for an initial focus on single materiality and climate-related disclosures, several members called for a clear timeline that would provide for the short, medium and long term, setting out how the scope might be broadened as the SSB becomes more established.
7. This was the last meeting for a number of Advisory Council members, most of whom had served for 5 years. Appreciation was shown for their significant contribution over their term of office.
 8. Appreciation was also shown for all of those who participated in the Council meeting for their preparation and contribution to the lively, constructive discussions.