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Client Alert Commentary

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ISSB Issues Global Sustainability Disclosure Standards

The inaugural standards are expected to significantly influence or become mandatory sustainability reporting requirements in a wide range of jurisdictions.

Key Points:

- The ISSB standards are published by IFRS, whose accounting rules are used by over 100 countries globally.
- The inaugural disclosure standards cover general sustainability reporting and climate-specific disclosures. These standards are only the first two of a comprehensive set of standards that ISSB is planning to issue.
- Multinational companies should be aware of key differences from disclosure requirements being proposed in the United States and the European Union.

On June 26, 2023, the International Sustainability Standards Board (ISSB) released its first two standards for sustainability disclosures, which are designed to facilitate the disclosure of sustainability-related information alongside companies' financial information. The inaugural standards cover general sustainability-related information (IFRS S1) and climate-related information (IFRS S2). These standards are the first of what ISSB has indicated will be a set of standards to provide a comprehensive global baseline of sustainability disclosures for investors and other stakeholders to use when assessing the value of companies.

In this Client Alert, we discuss key takeaways from the standards and provide an overview of next steps and how companies can prepare.

What Is the ISSB?

The International Financial Reporting Standards (IFRS) Foundation created the ISSB in November 2021 at the UN Conference of the Parties to the Paris Agreement, with the mandate to develop a potential common baseline for sustainability disclosures.

Key Components of the Standards

IFRS S1 provides a general architecture for companies to communicate to investors about sustainability-related risks and opportunities (SRROs). IFRS S2, as a topic-specific standard, is designed to be used in conjunction with IFRS S1, along with additional ISSB standards to be developed in the future.

IFRS S1: General Sustainability

The objective of IFRS S1 is for companies to disclose material information about their SRROs that is decision-useful to the primary users of general financial reports (namely, investors). Unlike the standards developed in the European Union, IFRS has adopted a definition of materiality based on the IFRS accounting standards, a definition which is ultimately rooted in a concept of financial materiality.

The ISSB's disclosure requirements are structured around the same four pillars popularized by the Task Force on Climate-related Financial Disclosures (TCFD). A detailed list of the ISSB disclosure requirements is provided in Annex A. At a high level they cover:

1. Governance
   a. Board oversight
   b. Management oversight
2. Strategy
   a. The SRROs that could reasonably be expected to affect the entity's prospects
   b. Effects of those SRROs on business model, value chain, financial performance, and strategy
   c. Resilience of strategy and business model to such sustainability-related risks
3. Risk Management
   a. Processes and related policies used to identify, assess, prioritize, and monitor sustainability-related risks
   b. Processes used to identify, assess, prioritize, and monitor sustainability-related opportunities
   c. Extent to which, and how, processes used to identify, assess, prioritize, and monitor SRROs are integrated into and inform overall risk management
4. Metrics and Targets
   a. Metrics required by an applicable IFRS Sustainability Disclosure Standard or, in the absence of such a standard, information that is relevant to decision-making of users of general purpose financial reports and that faithfully represents the SRRO
   b. Metrics used to measure and monitor the SRRO and the entity's performance in relation to the SRRO, including progress toward any targets the entity has set or is required to meet by law

We anticipate that subsequent topic-based standards will provide further details on related disclosures for such topics under the above pillars. IFRS S1 also requires companies to consider the applicability of the disclosure topics in the Sustainability Accounting Standards Board (SASB) Standards, though IFRS S1 does not mandate their adoption.

IFRS S2: Climate

Similar to IFRS S1, IFRS S2 is organized around the disclosure pillars of (i) governance; (ii) strategy; (iii) risk management; and (iv) metrics and targets. A detailed list of these requirements is provided in Annex B. However, certain IFRS S2 requirements deviate from requirements currently being developed in the United States:

- **Scenario Analysis:** IFRS S2 requires an entity to use scenario analysis to assess its climate resilience. It does not mandate the analysis take a particular form, but requires the approach to be "commensurate with [the company's] circumstances" and provides a set of factors to determine the company's approach. Under the SEC Climate Proposal (see this Latham Client Alert), disclosures regarding scenario analysis would only be required to the extent a company has decided to undertake one and would not affirmatively require such analysis.

- **Scope 3 Emissions:** IFRS S2 requires an entity to disclose its Scope 3 GHG emissions and, unlike the SEC Climate Proposal, does not include a materiality qualifier. While IFRS S2 does not require all 15 categories of Scope 3 emissions to be reported on, the standard emphasizes that a reporting entity "shall consider its entire value chain…shall consider all 15 categories of Scope 3 greenhouse gas emissions…[and] shall disclose which of these categories are included in its Scope 3 greenhouse gas emissions disclosures." IFRS S2 also requires disclosure of the calculation methodology, including measurement approach, inputs, and assumptions.

With respect to the European Union and the Corporate Sustainability Reporting Directive (CSRD), there are a number of similarities between the approach under IFRS S2 and the climate-related disclosures under CSRD. The similarities reflect the objective of the European Financial Reporting Advisory Group (EFRAG) to ensure greater interoperability between the requirements under CSRD and the standards established by ISSB (including EFRAG adapting the CSRD disclosure requirements to more closely track the framework structure of TCFD). However, the granularity of climate-related disclosures required under CSRD are more detailed by comparison with the level of detail expected under IFRS S2.

Beyond this similarity, the more significant difference (which is a difference more generally between CSRD and the ISSB standards) is the application of double materiality under CSRD as compared with financial materiality under the ISSB standards. Companies that are subject to disclosure obligations under CSRD and disclosure obligations under the ISSB standards will need to carefully consider their approach to materiality, particularly in instances in which the structure, topics, and specific data points required to be disclosed under CSRD and ISSB are similar.

What Comes Next?

IFRS S1 and S2 are set to become available for annual reporting periods starting in 2024, but the standards would not be mandatory unless adopted by individual jurisdictions. As ISSB is part of the IFRS Foundation, which develops the accounting rules used in more than 100 countries, we expect that there could be large-scale adoption of the ISSB standards as sustainability disclosure regulations become more commonplace. For example, according to ISSB Chair Emmanuel Faber, Canada, Brazil, Chile, the United Kingdom, Egypt, Kenya, Nigeria, South Africa, Japan, Malaysia, and Singapore are all considering using the ISSB standards.[1]

The ISSB standards have also been welcomed by the Chair of the International Organization of Securities Commission (IOSCO), the head of the TCFD Secretariat, the World Economic Forum, and the Chair of the Financial Stability Board.

Additionally, the ISSB recently published a consultation to seek feedback on priorities for the next two-year work plan and four potential projects as the ISSB works to expand its suite of sustainability disclosure standards.

How to Prepare

While it is still too early to comment on any specific regulations regarding the adoption of the ISSB standards, companies should investigate the degree to which their home jurisdictions are likely to adopt (or at least draw from) the ISSB standards for their own sustainability disclosure requirements. If a company is likely to be subject to these standards, below are a few steps to consider:

1. **Map out what rules apply and any knock-on implications.** Companies operating across jurisdictions face an increasing risk of regulatory fragmentation. For example, foreign private issuers in the United States will need to understand how a home-jurisdiction ISSB mandate may impact their own obligations under potential forthcoming climate rules from the Securities and Exchange Commission. Similarly, companies will want to consider balancing ISSB standards reporting and obligations under the CSRD. Understanding these interactions early will be key to establishing a robust global strategy.

2. **Perform a gap analysis.** Many companies are already producing some degree of sustainability-related disclosure. These companies should understand the degree to which their effort aligns with the requirements in IFRS S1 or S2 in order to determine the degree of additional lift for compliance. This analysis should assess not only what information a company has, but also the underlying methodologies — including applicable approaches to materiality — to confirm whether the information meets any particular specifications in the ISSB requirements. Additionally, companies need to understand the interaction of their existing disclosures with these pending ISSB requirements, which may inform what a company may be expected to report in the future.

3. **Button up internal controls.** As sustainability-related reporting increasingly becomes the focus of regulation, scrutiny of all sustainability-related disclosure, regardless of whether it is in response to regulation or is voluntarily undertaken, is increasing. Importantly, companies need to know not only what they know but how they know it (and how they can demonstrate that knowledge).

4. **Continue to monitor further developments from ISSB.** As noted at the outset of this Client Alert, IFRS S1 and S2 represent just the first two sets of disclosure standards. Additional standards are anticipated, and companies should stay abreast of these developments (particularly the sector-specific standards that are developed).

Latham & Watkins will continue to monitor this space closely.

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European Commission Eases Requirements in European Sustainability Reporting Standards Consultation

ANNEX A: SUMMARY OF GENERAL IFRS S1 DISCLOSURE REQUIREMENTS

S1 Disclosure Area	Disclosure Items
Governance	How responsibilities for sustainability-related risks and opportunities (SRROs) are reflected in policies applicable to body(/ies) or individual(s) responsible for oversight of SSROs
	How the body(/ies) or individual(s) determines whether appropriate skills are available or will be developed to oversee response to SSROs
	How and how often the body(/ies) or individual(s) is informed of SRROs
	How the body(/ies) or individual(s) takes into account SSROs when overseeing the entity's business strategy, including decisions on major transactions, risk management processes, and whether the body(/ies) or individual(*s) has considered trade-offs associated with those risks and opportunities
	How the body(/ies) or individual(s) oversees the setting of targets related to SRROs and monitoring progress towards them, including whether and how related performance metrics are included in remuneration policies
	Whether management's role in governance is delegated to a specific position or committee and how oversight is exercised over that role
	Whether management uses controls to support oversight of SRROs, and how those controls are integrated with other internal functions
Strategy	The SRROs that could reasonably be expected to affect the entity's prospects
	Time horizons (short, medium, or long term) over which the effects of the SSROs could reasonably be expected to occur
	How the entity defines short, medium, and long term and how the definitions are linked to planning horizons used by the entity for strategic decision-making
	The current and anticipated effects of SRROs on the entity's business model and value chain
	Where in the entity's business model and value chain SRROs are concentrated
	How the entity has responded to, and plans to respond to, SRROs in strategy and decision-making
	Progress against plans the entity has disclosed in previous reporting periods, including quantitative and qualitative information
	Trade-offs between SRROs the entity considered

S1 Disclosure Area	Disclosure Items
	Effects of SRROs on the entity’s financial position, financial performance, and cash flows for the reporting period
	The SRROs for which there is a significant risk of a material adjustment in the next annual reporting period to the carrying amount of assets and liabilities reported in the related financial statements.
	Anticipated effects of sustainability-related risks and opportunities on the entity’s financial position, financial performance, and cash flows over the short, medium, and long term — taking into account investment and disposal plans, including plans not contractually committed to, and a company’s planned sources of funding to implement its strategy
	How the entity expects its financial performance and cash flows to change over the short, medium, and long term, given its strategy to manage SRROs.
	A qualitative and, if applicable, quantitative assessment of the resilience of its strategy in relation to its sustainability-related risks, including information about how the assessment was carried out and its time horizon.
Risk Management	The inputs and parameters the entity uses in processes to identify, assess, prioritize, and monitor SSROs
	Whether and how the entity uses scenario analysis to inform its identification of those risks
	How the entity assesses the nature, likelihood, and magnitude of the effects of those risks
	Whether and how the entity prioritizes sustainability-related risk relative to other types of risk
	How the entity monitors sustainability-related risks
	Whether and how the entity has changed the processes it uses compared with the previous reporting period
	The processes the entity uses to identify, assess, prioritize, and monitor sustainability-related opportunities
	The extent to which, and how, the processes for identifying, assessing, prioritizing, and monitoring SRROs are integrated into and inform the entity’s overall risk management process
Metrics and Targets	For each SRRO: Metrics required by an applicable IFRS Sustainability Disclosure Standard
	For each SRRO: Metrics the entity uses to measure and monitor that SRRO
	For each SRRO: The metric’s performance in relation to that SRRO, including progress towards any targets the entity has set, and any targets it is required to meet by law or regulation

S1 Disclosure Area	Disclosure Items
	(If a metric has been developed by an entity) How the metric is defined, including whether it is derived by adjusting another metric
	(If a metric has been developed by an entity) Whether the metric is absolute, relative, or qualitative
	(If a metric has been developed by an entity) Whether the metric is validated by a third party and, if so, which party
	(If a metric has been developed by an entity) The method used to calculate the metric and inputs to calculation, including limitations of the method used and significant assumptions made
	(For each target an entity has set to monitor progress towards goals) The metric used to set the target and to monitor progress towards reaching the target
	(For each target an entity has set to monitor progress towards goals) The specific quantitative or qualitative target the entity has set or is required to meet
	(For each target an entity has set to monitor progress towards goals) The period over which the target applies
	(For each target an entity has set to monitor progress towards goals) The base period from which progress is measured
	(For each target an entity has set to monitor progress towards goals) Any milestones and interim targets
	(For each target an entity has set to monitor progress towards goals) Performance against each target and an analysis of trends or changes in the entity's performance
	(For each target an entity has set to monitor progress towards goals) Any revisions to the target and an explanation for those revisions.
General Guidance	In identifying SRROs that could reasonably be expected to affect an entity's prospects, an entity shall apply IFRS Sustainability Disclosure Standards
	An entity shall refer to and consider the applicability of the *disclosure topics* in the SASB standards:The entity may conclude that the topics are not applicable
	An entity may refer to and consider the applicability of the CDSB Framework Application Guidance for Water-related Disclosures and the CDSB Framework Application Guidance for Biodiversity-related Disclosures
	An entity may refer to and consider the applicability of the most recent pronouncements of other standard-setting bodies whose requirements are designed to meet the information needs of users of general purpose financial reports

S1 Disclosure Area	Disclosure Items
	An entity may refer to and consider the applicability of the SSROs identified by entities that operate in the same industry(/ies) or geographical region(s)
	In the absence of an IFRS Sustainability Disclosure Standard that specifically applies to an SRRO, an entity shall apply judgment to information that is relevant to the decision-making of users of general purpose financial reports
	In the absence of an IFRS Sustainability Disclosure Standard that specifically applies to an SRRO, an entity shall apply judgment to information that faithfully represents the SRRO
	In making the above judgment, an entity shall refer to and consider the applicability of the metrics associated with the disclosure topics included in the SASB Standards: An entity might conclude that the metrics specified in the SASB Standards are not applicable in the entity's circumstances
	In making the above judgment, an entity may — to the extent that these sources do not conflict with IFRS Sustainability Disclosure Standards — refer to and consider the applicability of: the CDSB Framework Application Guidance, the most recent pronouncements of other standard-setting bodies whose requirements are designed to meet the information needs of users of general purpose financial reports, and the information, including metrics, disclosed by entities that operate in the same industry(/ies) or geographical region(s)
	In making the above judgment, an entity may — to the extent that these sources assist the entity in meeting the objective of this Standard and do not conflict with IFRS Sustainability Disclosure Standards — refer to and consider the applicability of the sources specified in Appendix C of S1
	An entity shall identify the specific standards, pronouncements, industry practice, and other sources of guidance that the entity has applied in preparing its sustainability-related financial disclosures, including, if applicable, identifying the disclosure topics in the SASB Standards
	An entity shall identify the industry(/ies) specified in the IFRS Sustainability Disclosure Standards, the SASB Standards or other sources of guidance relating to a particular industry(/ies) that the entity has applied in preparing its sustainability-related financial disclosures, including in identifying applicable metrics
	An entity shall report its sustainability-related financial disclosures at the same time as its related financial statements: An entity's sustainability-related financial disclosures shall cover the same reporting period as the related financial statements
	When an entity changes the end of its reporting period and provides sustainability-related financial disclosures for a period longer or shorter than 12 months, it shall disclose the period covered by the sustainability-related financial disclosures, the reason for using a longer or shorter period, and the fact that the amounts disclosed in the sustainability-related financial disclosures are not entirely comparable
	If, after the end of the reporting period but before the date on which the sustainability-related financial disclosures are authorized for issue, an entity receives information about conditions that existed at the end of the reporting period, it shall update disclosures that relate to those conditions in the light of the new information

S1 Disclosure Area	Disclosure Items
	Information about transactions, other events and conditions that occur after the end of the reporting period, but before the date on which the sustainability-related financial disclosures are authorized for issue, if non-disclosure of that information could reasonably be expected to influence decisions that primary users of general purpose financial reports make on the basis of those reports
	Unless another IFRS Sustainability Disclosure Standard permits or requires otherwise, comparative information in respect of the preceding period for all amounts disclosed in the reporting period: If such information would be useful for an understanding of the sustainability-related financial disclosures for the reporting period, the entity shall also disclose comparative information for narrative and descriptive sustainability-related financial information
	An entity whose sustainability-related financial disclosures comply with all the requirements of IFRS Sustainability Disclosure Standards shall make an explicit and unreserved statement of compliance: An entity shall not describe sustainability-related financial disclosures as complying with IFRS Sustainability Disclosure Standards unless they comply with all the requirements of IFRS Sustainability Disclosure Standards
Judgments, Uncertainties, and Errors	Information to enable users of general purpose financial reports to understand the judgements, apart from those involving estimations of amounts, that the entity has made in the process of preparing its sustainability-related financial disclosures and that have the most significant effect on the information included in those disclosures.
	Identify the amounts that it has disclosed that are subject to a high level of measurement uncertainty
	Information about the sources of measurement uncertainty
	The assumptions, approximations, and judgements the entity has made in measuring the amount
	An entity shall correct material prior period errors by restating the comparative amounts for the prior period(s) disclosed unless it is impracticable to do so

ANNEX B: SUMMARY OF GENERAL IFRS S2 DISCLOSURE REQUIREMENTS

S2 Disclosure Area	Disclosure Items
Governance	How responsibilities are reflected in policies applicable to body(/ies) or individual(s) responsible for oversight of climate-related risks and opportunities (CRROs)
	How the body(/ies) determines whether appropriate skills are available or will be developed to oversee response to CRROs
	How often the body(/ies) is informed about CRROs
	How the body(/ies) takes into account CRROs when overseeing the entity's business strategy
	How the body(/ies) oversees setting targets related to CRROs and monitors progress towards them
	Whether management's role in governance is delegated to a specific position or committee and how oversight is exercised over that role
	Whether management uses controls to support oversight of CRROs, and how those controls are integrated with other internal functions
	***In preparing governance disclosures, entities should avoid unnecessary duplication in accordance with IFRS S1.
Strategy	CRROs that could reasonably be expected to affect the entity's prospects
	(For each CRRO identified) whether the entity considers the risk to be a climate-related physical risk or climate-related transition risk
	Effects of CRROs on the entity's strategy and decision-making, including information about its climate-related transition plan
	Time horizons (short, medium, or long term) over which the effects of the CRROs could reasonably be expected to occur
	How the entity defines short, medium, and long term and how the definitions are linked to planning horizons used by the entity for strategic decision-making
	The current and anticipated effects of CRROs on the entity's business model and value chain

S2 Disclosure Area	Disclosure Items
	Where in the entity's business model and value chain CRROs are concentrated
	How the entity has responded to, and plans to respond to, CRROs in strategy and decision-making, including: (i) Current and anticipated changes to the entity's business model (ii) Current and anticipated direct mitigation and adaptation efforts (iii) Current and anticipated indirect mitigation and adaptation efforts (iv) Any climate-related transition plan the entity has (v) How the entity plans to achieve any climate-related targets
	How the entity is resourcing, and plans to resource, activities in response to CRROs
	Progress of plans disclosed in previous reporting periods for responding to CRROs
	Effects of CRROs on the entity's financial position, financial performance, and cash flows for the reporting period and over the short, medium, and long term, taking into account investment and disposal plans, including plans not contractually committed to, and the entity's planned sources of funding to implement its strategy
	The CRROs for which there is a significant risk of a material adjustment in the next annual reporting period to the carrying amount of assets and liabilities reported in the related financial statements
Climate Resilience	The entity's assessment of its climate resilience as at the reporting date to enable users of general purpose financial reports to understand: (i) The implications, if any, of the entity's assessment for its strategy and business model (ii) The significant areas of uncertainty considered in the entity's assessment of its climate resilience (iii) The entity's capacity to adjust or adapt its strategy and business model to climate change over the short, medium, and long term

S2 Disclosure Area	Disclosure Items
	How and when climate-related scenario analysis was carried out, including: (i) Information about the inputs the entity used (ii) Key assumptions the entity made in the analysis (iii) The reporting period in which the climate-related scenario was carried out
Risk Management	Inputs and parameters the entity uses
	Whether and how the entity uses scenario analysis to inform its identification of those risks
	How the entity assesses the nature, likelihood, and magnitude of the effects of those risks
	Whether and how the entity prioritizes climate-related risks relative to other types of risk
	How the entity monitors climate-related risks
	Whether and how the entity has changed the processes it uses compared with the previous reporting period
	The processes the entity uses to identify, assess, prioritize and monitor climate-related opportunities
	The extent to which, and how, the processes for identifying, assessing, prioritizing and monitoring CRROs are integrated into and inform the entity's overall risk management process
	***In preparing risk management disclosures, entities should avoid unnecessary duplication in accordance with IFRS S1.
Metrics	Information relevant to cross-industry metric categories
	Industry-based metrics that are associated with particular business models, activities, or other common features that characterize participation in an industry
	Targets set by the entity, and any targets it is required to meet by law or regulation, to mitigate or adapt to climate-related risks or take advantage of climate-related opportunities
	Absolute gross Scope 1, 2, and 3 greenhouse gas (GHG) emissions generated during the reporting period, measured in accordance with the Greenhouse Gas Protocol: A Corporate Accounting and Reporting Standard (2004)

S2 Disclosure Area	Disclosure Items
	***for Scope 1 and Scope 2, disaggregate between the consolidated accounting group and other investees
	The measurement approach, inputs, and assumptions the entity uses to measure its GHG emissions
	The reason why the entity has chosen the measurement approach, inputs, and assumptions
	Any changes the entity made to the measurement approach, inputs, and assumptions during the reporting period and the reasons for those changes
	(for Scope 2 GHG emissions) any contractual instruments necessary to inform users' understanding of the entity's Scope 2 GHG emissions
	(for Scope 3 GHG emissions) categories included within the entity's measure of scope 3 GHG emissions and, if the entity's activities include asset management, commercial banking, or insurance, disclose additional information about Category 15 GHG emissions or those associated with its investments
	Amount and percentage of assets or business activities vulnerable to climate-related transition risks
	Amount and percentage of assets or business activities vulnerable to climate-related physical risks
	Amount and percentage of assets or business activities vulnerable to climate-related opportunities
	Amount of capital expenditure, financing, or investment deployed towards DRROs
	Whether and how the entity is applying a carbon price in decision-making
	The price for each metric ton of GHG emissions the entity uses to assess the costs of its GHG emissions
	Whether and how climate-related considerations are factored into executive renumeration
	The percentage of executive management renumeration recognized in the current period that is linked to climate-related considerations
	Industry-based metrics that are associated with one or more particular business models, activities, or other common features that characterize participation in an industry
Targets	Metric used to set each target

S2 Disclosure Area	Disclosure Items
	Objective of each target
	Part of the entity to which each target applies
	Period over which each target applies
	Base period from which progress is measured for each target
	Any milestones and interim targets
	If a target is quantitative, whether it is an absolute target or an intensity target
	How the latest international agreement on climate change has informed each target
	Whether each target and the methodology for setting each target has been validated by a third party
	The entity's process for reviewing each target
	Metrics used to monitor progress towards reaching each target
	Any revisions to a target and an explanation for those revisions
	The entity's performance against each target and an analysis of trends or changes in performance
	(for each GHG emissions target) which GHGs are covered by the target
	(for each GHG emissions target) whether Scope 1, Scope 2, or Scope 3 GHG emissions are covered by the target
	(for each GHG emissions target) whether the target is a gross GHG emissions target or net GHG emissions target
	If a net GHG emissions target, the associated gross GHG emissions target
	(for each GHG emissions target) Whether the target was derived using a sectoral decarbonization approach
	The entity's planned use of carbon credits to offset GHG emissions to achieve any net GHG emissions target

Endnotes

[1] https://www.reuters.com/sustainability/new-global-rules-aim-clamp-down-corporate-greenwashing-2023-06-26/