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Sustainability reporting

Knowing your GRIs from your ISSBs

In June the International Sustainability Standards Board (ISSB) issued its first Sustainability Disclosure Standards (IFRS S1 and IFRS S2).

Since launch, there has been debate about how the new standards will be used, how they will fit with mandatory reporting requirements at the national and state jurisdictional level, and how they will align with other sustainability reporting standards, not least GRI.

The answer to these questions continues to evolve but here we offer some initial guidance on ISSB adoption and its scope.

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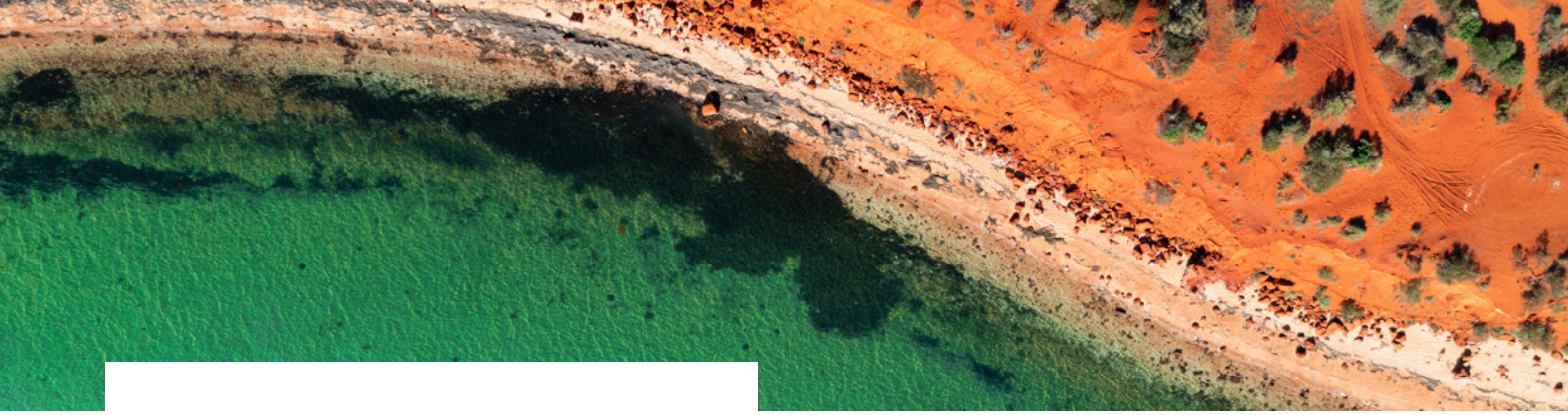


What is the aim and scope of IFRS S1 and IFRS S2?

Aim: Simplify and rationalise information exchange between entities and investors

The aim of the International Financial Reporting Standards Sustainability Disclosures Standard 1 (IFRS S1) and IFRS Sustainability Disclosures Standard 2 (IFRS S2) is to create an internationally consistent process for companies reporting sustainability-related disclosures to the capital markets.

The process should make the sustainability disclosure reporting process more manageable and structured for reporting entities, and the disclosure information generated more proportionate, accessible and 'decision-useful' to investors.

Scope: Company risk, not impacts on people and planet

An entity must disclose and report on sustainability-related (IFRS S1) or climate-related (IFRS S2) risks and opportunities that:

> "could reasonably be expected to affect the entity's cash flows, its access to finance or cost of capital over the short, medium or long term."
>
> IFRS S1, IFRS® Sustainability Disclosure Standard, General Requirements for Disclosure of Sustainability-related Financial Information

In other words, materiality under the two ISSB standards is geared solely at the risk or opportunity it poses to an entity and its value chain, not on the sustainability impact its operations may have on external stakeholders and environments.

This approach to materiality can be broadly termed '**financial materiality**.'

How are risks and opportunities identified?

How an entity identifies and gauges material risks is not dictated strictly. However, the IFRS advise that entities use the Sustainability Accounting Standards Board (SASB) materiality tools as a first port of call.

SASB (like the GRI) has developed a large list of industry groups which have been assessed against 26 material risks identified by SASB.

For example, within the Metals and Mining group SASB identified 11 of the 26 risks as being often material to entities in this industry – these range from Human Rights & Community Relations to GHG Emissions, and Air Quality.

Other reference tools cited include the Climate Disclosure Standards Board (CDSB) Framework application guidance for water-related disclosures and the CDSB Framework application guidance for biodiversity-related disclosures (collectively referred to as 'CDSB Framework Application Guidance').

Once topic materiality is established, an entity must report on four areas of action linked to these sustainability risks and opportunities.

1. **Governance** – The governance processes, controls and procedures the entity uses to monitor and manage sustainability-related risks and opportunities.
2. **Strategy** – The approach the entity uses to manage sustainability related risks and opportunities.
3. **Risk management** – The processes the entity uses to identify, assess, prioritise and monitor sustainability-related risks.
4. **Metrics and targets** – The entity's performance in relation to sustainability-related risks and opportunities.

How do the ISSB Standards impact established reporting practice?

IFRS S1 and S2 do not supersede or conflict with any broader sustainability reporting frameworks. Rather, they are aimed at simplifying and consolidating specific sustainability reporting to the capital markets.

If any entity is basing its sustainability reporting on other reporting frameworks – this can continue, and it is likely any such process can feed into any additional ISSB reporting.

What is important to remember is that IFRS S1 and S2 are solely geared towards investors, and such an approach may not be sufficient for other stakeholders, frameworks and regulators.

For example, in the European Union (EU), the new ISSB Standards only cover half the materiality reporting requirements mandated under the bloc's European Sustainability Reporting Standards (ESRS).

Under the ESRS, large companies and all listed companies in the EU must undertake a 'double materiality' approach to reporting, which is geared towards a multi-stakeholder audience including, but not limited to, capital markets.

Double materiality reporting assesses sustainability risks and opportunities that may impact on an entity's ability to operate, and thus its value (the key area of interest for investors), as well as the sustainability impact an entity could have on people (stakeholders) and planet. The latter is regardless of whether those impacts affect the entity's ability to operate.

This additional part of materiality can be termed **'impact materiality'.**

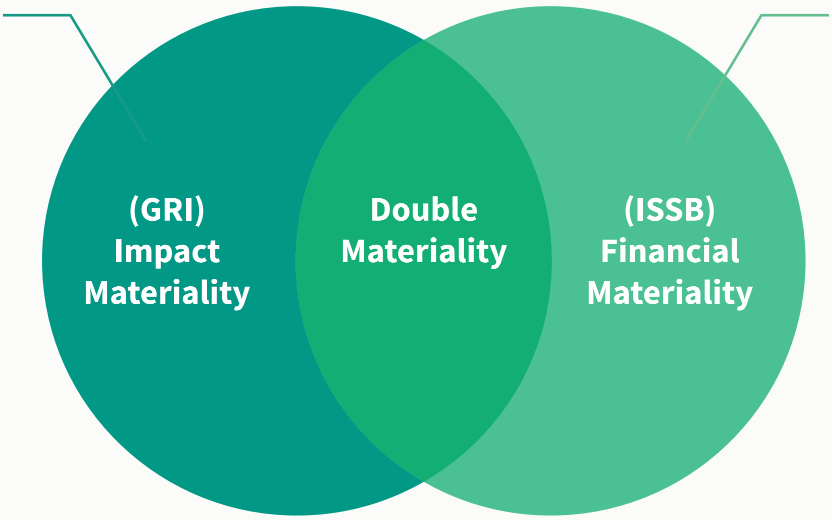
Under this approach all potential risks and opportunities are in scope, not just those that are financially material to the entity in question. This is the approach to materiality followed under GRI.

The impact materiality approach is also a common reporting requirement in industry specific due diligence and assurance frameworks.

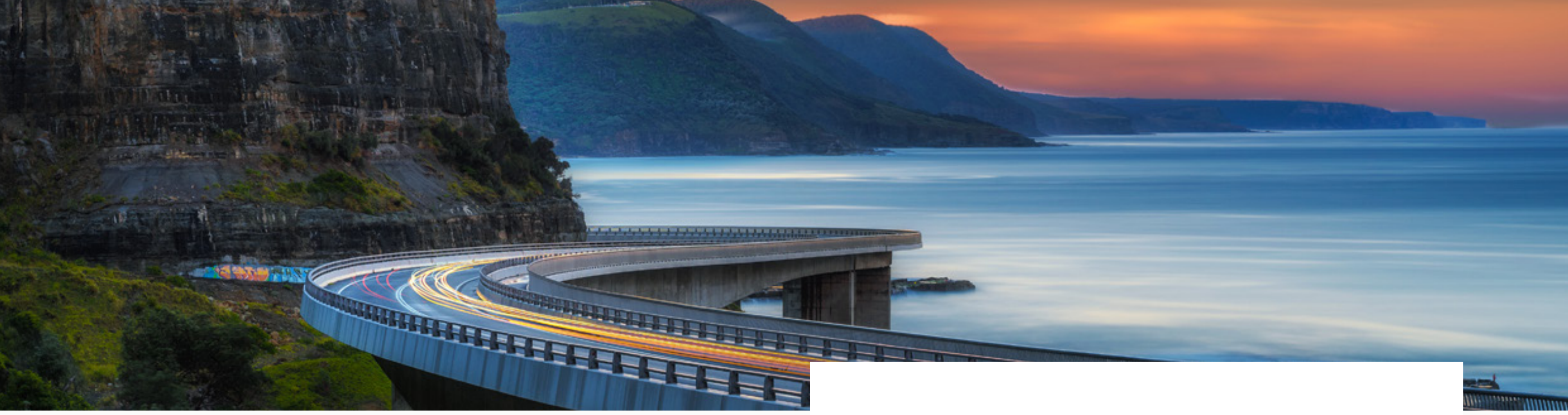
Again, to take the example of mining and metals – while earlier we noted that SASB identified 11 potential risks and opportunities for metals and mining companies, the Responsible Mineral Initiative (RMI) and the Initiative for Responsible Mining Assurance (IRMA) both go beyond financial materiality and list 32 and 30 areas of potential risk respectively.

Materiality inter-relationship

Reporting company's impact on the economy, environment and people.



Economic value creation at the level of the reporting company.



What is the right fit?

A straight financial materiality play

For companies at the start of their sustainability reporting journey, the emergence of the ISSB Standards may be a trigger to discuss how your company views sustainability.

If your company views sustainability purely in terms of the impact it may have on your company's risk profile and valuation to capital markets, then adopting a pure **financial materiality approach** to sustainability reporting based on IFRS S1 and S2 may well be optimal.

This approach will streamline the materiality assessment needed and likely reduce the number of material topics on which you will need to disclose.

It will also enable you to curate a reporting framework and set of information and metrics that is arguably less onerous and more manageable than a wider approach to reporting.

Such an approach can also be a foundation for an expanded materiality assessment and reporting at a later point.

Adopting a holistic approach

For companies already aligned with or certified under GRI, or for companies who have taken a more expansive approach to materiality generally, ISSB does not need to alter your reporting.

Equally, for companies starting to consider sustainability reporting, ISSB reporting standards may seem too restrictive.

Taking a double materiality approach can be a win-win. It can ensure your company can properly gauge all potential material topics, **including financially material topics under ISSB,** and demonstrate that your business is disclosing accurately.

Such an approach will also give your company the best opportunity to remain aligned with good practice industry expectations and emerging jurisdictional expectations, without having to bolt on further materiality reporting topics reactively in the future.

For example, once comprehensive double materiality is established, a company is empowered to solely follow GRI reporting guidance.

It could also choose to later adopt the ISSB Reporting Framework for topics identified within its established materiality matrix which fall in scope of IFRS S1 and S2.

Key takeaways

1. If viable, scope all materiality to create a solid, comprehensive baseline relevant to all stakeholders, not just capital markets.
2. Assess your stakeholders and who you want to engage.
3. Decide if you need, or want, to adopt a multistakeholder approach to reporting as defined by the GRI.
4. Decide if you need, or want, to adopt any industry or market specific reporting frameworks such as ISSB or (as mentioned earlier) IRMA in addition to or as an alternative to GRI.
5. Start disclosing and remember that unless mandated to do so by a regulator, customer, or investor, an entity does not have to conform immediately with any one or more framework. Why not begin disclosing against your general material topics, gain feedback from stakeholders, and then revisit the questions posed in point 3 and 4 above.

"The reality is that the impacts of an organization are or will become financially material over time. Without understanding these impacts, it won't be possible to get a complete overview of financially material issues affecting the company, an exercise that GRI supports. Besides, impact reporting is also highly relevant in its own right as a public interest activity for multiple stakeholders."

GRI 2022, 'The materiality madness: why definitions matter', The GRI Perspective, Issue 3, 22 Feb 2022.

Need more help?

Contact us if you'd like to talk about materiality in the context of your organisation, via sustainability@consentium.com.au or call +61 8 8431 7113.