The New IFRS S2 Climate -related Disclosures 11/05/2023

CCH Learning:

Hello, everybody, and welcome to today's webinar: The new IFRS S2 Climate-related Disclosures. My name is Susannah Gynther from Wolters Kluwer CCH Learning and I will be your moderator for today. A few quick pointers before we get started. In the handout section, you'll find the PowerPoint slides for today's presentation. If you're having sound problems, please check your audio settings, try and toggle between audio and phone, and just a reminder that within 24 to 48 hours you will receive an email notification of the e-learning recording. You can ask questions at any point during the presentation by sending them through the Questions Box. I will collect those questions and ask them at the Q&A towards the end of today's presentation.

CCH Learning also offers a subscription service which many people have termed Netflix for professionals. It provides members with access to our entire library of recordings as well as live webinars for a competitive flat fee. That's for over 500 hours of content. For CPD purposes, your viewing is logged automatically. Your presenters today... Oh, hold on. I went through a slide. I apologize. Your presenters today are Aletta Boshoff, partner and national leader IFRS and Corporate Reporting, ESG, and Sustainability, and Dean Ardern Director of BDO Australia.

Aletta is an IFRS advisory specialist with over 25 years experience in financial reporting and accounting, including IFRS. Aletta's, involvement in sustainability and environmental, social, and governance, ESG reporting, is a consequence of her focus on an organization's ability to create and sustain long-term value in a rapidly changing world and managing the risks and opportunities associated with these changes. Aletta also puts heavy emphasis on risk management because monitoring and mitigating risks across all three dimensions is an important priority for any company that is serious about sustainability and ESG.

Dean has been advising on IFRS and other financial reporting matters for over 15 years. Having worked with a range of clients in both for-profit and not-for-profit sectors, Dean understands the challenges in the para space. Dean's primary role is to identify practical and compliant reporting solutions for clients and assurance staff. To achieve this, Dean works at building constructive relationships with clients with the view to providing responsive, accurate, and outcome-focused technical advice and guidance. I will now hand you over to Aletta and Dean to commence today's presentation.

Aletta Boshoff:

Thank you very much, Susannah, and good afternoon to everybody. If we look at today's agenda, we'll be looking at some of the latest developments around sustainability, we will touch on connectivity and what it is and what does it deliver, we'll do an overview of the proposed IFRS 2 and then we will go into a little bit of depth of IFRS 2. So we look at the pillar governance, then the pillar strategy, the pillar risk management, and finally the pillar around targets and metrics.

We'll then also talk about how do we get ready for IFRS S2 and next steps. I should start off by saying we are in May, as you all know, and we are expecting IFRS S2 to be issued before the end of June by the International Sustainability Standards Board. We've seen the ED, I think a lot of us commented on the ED, but really exciting that we're going to see the final standard very soon.

In April, a few weeks ago, the ISSB announced that there will be transitional relief in relation to IFRS S1. So in the first year when sustainability reporting included in financial or annual reports is mandatory, it will be a focus initially on IFRS S2 that we're talking about today and a year later, IFRS S1 and as we discussed last time, IFRS S1 is the general requirements but they don't want entities to be distracted. They want everybody to focus on climate-related disclosures and focus on IFRS S2 and therefore, a year later bringing the other things in IFRS S1.

So mandatory implementation of IFRS S1 has been delayed by a year or deferred by a year, initial focus on IFRS S2. They now also have a number of transitional relief available and I think it might be interesting to have a look at them briefly. So initially, it's climate-related information. Secondly, the idea is to provide sustainability-related disclosures at the same time as the disclosures in normal financial statements. However, there's transitional relief for that. So in the initial year, it could be at a different time and I think that is acknowledging the staff pressures and constraints that a number of clients have flagged.

Also in the first year which in Australia it's expected to be 30 June 2025, no need to provide comparative information in the very first year. So it'll be for the Period 1 July 2024 to 30 June 2025 and no comparatives in that particular year. Also, in the first year of IFRS S2, we'll only have to disclose Scope 1 and Scope 2 Greenhouse Gas Emissions and the final one is it's always been a recommendation or actually, it has always been intended to have a mandated requirement to use the Greenhouse Gas Protocol. But if an entity is using a different approach currently to measure their carbon footprint, that they could continue to do that at least in the first year. So there's still a move to the Greenhouse Gas Protocol but not on Day 1. So these are some of the latest developments and definitely a focus on IFRS S2.

So we want to... Before we look at IFRS S2, Dean and I would like to touch on connectivity. Now, what happened a few weeks ago is the chair of the International Accounting Standards Board and the chair of the International Sustainability Standards Board made a joint statement and issued an article where they talked about connectivity and where they talk about linking traditional financial statements with the sustainability disclosures with additional information that ultimately go to other shareholders.

What they've indicated is that both standard setting bodies, the International Accounting Standards Board as well as the International Sustainability Standards Board, are actively trying to work together in order to maintain and achieve this connectivity and ultimately to try and achieve integrated reporting. Now, I particularly like this diagram because they're trying to put all the frameworks and all the reporting for us together and I think this is quite clear.

If you start on the left-hand side at the bottom, we are talking about traditional financial statements that are prepared in accordance with IFRS quite often and they are subject to audit so nothing changed with them. However, they want to add to that in the operating and financial review. In the broader financial report, they want to add sustainability-related financial disclosures as issued by the International Sustainability Standards Board and obviously, it is subject to jurisdictional initiatives and mandated reporting.

But those sustainability-related financial disclosures would initially be IFRS S2 and then it will be IFRS S1 and a raft of other S-series standards. The financial statements as we know it and these new sustainability-related financial disclosures would form general purpose financial reports which have an investor focus. Then, in the gray bits you see additional information that are provided to a broader stakeholder group. So not just investors, a broader group and a lot of additional information and that can be financial and non-financial.

Now, that gray area is covered by a lot of other frameworks. It could be GRI. It could be World Economic Forum. What we expect to see... That gray area could be covered in a separate sustainability report or an impact report or a corporate social stability report. What we expect to see over time is that the aqua part or the light blue part will become more extensive because we will have IFRS S3 on biodiversity, we'll have IFRS S4 on workforce, we'll have an IFRS 5 or 6 around supply chain, and ultimately, the gray bit will become very small and potentially completely be removed because all of the sustainability-related information will end up in the general purpose financial report. That will take a bit of time.

So I think this is a nice diagram to put all of this in perspective and linking all the different types of report because it can be confusing. So if we look at connectivity, what it is and what does it deliver, I think what the standard setters are articulating is that they are aiming to get to realistic, comprehensive, and coherent general purpose financial reports. That is ultimately the goal and there's therefore connectivity between the reports and therefore, we've got connectivity between the boards, we've got connectivity in the processes they follow and the staff working together, and ultimately also the products but the big aim here is we want to list the comprehensive and general purpose financial reports. It will take a bit of time but that's the goal.

If we look at these connectivity in reports, we know investors are the primary audience for general purpose financial reports and they're asking for these additional disclosures and initially, we'll start with climate change, then it will go to biodiversity and nature-related disclosures but, very important, people-related disclosures will come next.

So this is just an illustration around how we connect. On the left-hand side are financial statements prepared in accordance with Australian and international accounting standards. It's subject to audit but we are now connecting it on the right-hand side, at the moment, voluntarily prepared sustainability reports. But from 30 June 2025, we're connecting it with mandatory reporting around climate risk but also some voluntary additional disclosures that over time will also become mandatory.

The connectivity in product, if we want to achieve reports that speak to each other, it is important that the two standard setting bodies work together. It's also important that the concepts they use, definition of materiality, are similar. It's important that there are no gaps and also no unintended overlaps between their standards and also the digital taxonomies. So the standard setting bodies are saying, "We are aware of the absolute great opportunity but we're also aware of the potential stumbling blocks and we're actively working to overcome those with the ultimate goal of integrated reporting."

This is just trying to illustrate how they've already done this, how they're already working together, how they already have very similar concepts and terms in accounting standards and the first two standards, S1 and S2. Dean, I don't think we need to elaborate much more. It's just really important that everybody in your team understand that connectivity is really important and there's an active project to achieve that.

What are we seeing in practice? How does this play out in practice? Previously, sustainability professionals were looking after sustainability matters and sustainability reporting. However now, that sustainability is so linked to financial statements and now that sustainability information is becoming part of the broader financial report, general purpose financial report, and annual report, we know that CFOs and finance teams are sitting up and taking attention and there's active collaboration at an entity level, at our clients' level, between finance teams and sustainability professionals which is amazing to see and they're following the example of what we see here by the standard setters.

So if we look at a bit of an overview of the proposed IFRS S2, we know first of all with these new standards as we have with accounting standards, there's always a lot of literature. So if you look at the published documents, there's currently the exposure draft on IFRS S2 which will become standard. There's been some changes.

There's illustrative guidance on the exposure draft, there's basis for conclusions, and a very important document is the fourth document and that is Appendix B which is industry-based disclosure requirements. It is basically an incorporation of the SASB standards which has always been heavily focused on various industries and we will show some examples towards the end of this webinar. There's more than 600 pages in that Appendix B but not all of that will apply to each and every entity. So you'll look at how have they categorized different entities or which of them would be relevant to your business.

If you've got a big group, it might be more than one. And then, there are very good indications or recommendations of what good industry-based disclosures would look like. So IFRS 2 is providing a framework around the general disclosures that one would expect across all entities where Appendix B is talking about additional disclosure requirements in addition to what already or what will already be mandated within the body of IFRS S2.

So the proposed IFRS S2 is requiring a company to disclose information that would enable an investor to assess the effect of climate-related risk but also opportunities on its enterprise value so a big focus on investors. If we provide this information that we think investors would like to see, it will obviously also provide useful information to other stakeholders. But when designing the standard, it was around what investors would like to see and investors have been quite vocal on what they would like to see around climate-related risks and opportunities in broader annual reports.

So the objective of IFRS 2, require an entity to disclose information about exposure to significant climate-related risk and opportunities and we want to enhance the users of general purpose financial reporting's understanding so we want them to be able to do three things. We want them to be able to assess the effect of these climate-related risk and opportunities on enterprise value, we want them to understand how the entity is planning to respond to these risks and opportunities and how that will impact their strategy for managing these risk and opportunities, and finally, also, we would like these users to be able to evaluate to what extent the entity is adapting its planning, its business model, its risk management, its operations to respond to significant climate-related risks and opportunities.

If you look at the scope of IFRS S2, it's looking at climate-related risks and climate-related opportunities. Even if you look at recent ASIC media releases, it's saying in the operating financial review, there's a requirement that entities should disclose their business risks which could include climate-related risk but also a requirement to disclose business opportunities including climate-related opportunities so it's not just from the standard setters but also from the regulators.

If you look at climate-related risks, they consist of two parts or two big categories but one is around physical risks so physical risks from climate change. So that could be floods or bush fires, extreme weather events for example. And then, transition risks. So transition risk is all about the risks associated with transitioning to a lower carbon economy. So if we currently use manufacturing processes or activities that are burning fossil fuels, high carbon economy, how do we transition to a lower carbon economy?

In our previous webinar, we provided an overview of the proposed IFRS S1 and that overview and the syncing around the structure of the sustainability standards remain consistent here and that is that we start with governance and then we move to strategy and then we move to risk management and right at the end, we consider metrics and potentially, targets in the same year. So it's governance strategy, risk management, metrics, and targets and I would expect each and every sustainability standard issued by the ISSB to follow this structure and this approach.

So let's start with governance. So we looked at governance, what are the requirements here? They would like us to disclose our governance processes, controls, procedures that the company uses to monitor and manage climate-related risks and opportunities. They specifically want us to disclose the description of the governance body. Maybe it's the board, maybe it's a committee who have oversight over these opportunities. So what are the terms of reference of whoever is monitoring climate-related risks and opportunities? So what's their terms of reference but that's around the board and their terms of reference.

But also, what about management? What is management's role in assessing and managing these risks? Finally, and I think this is interesting, how does the company ensure that it has people with the right skills and competencies to oversee the strategies and the risk management activities around climate-related risks and opportunities? So it is about the body, it is about the terms of reference, it is about management, but it's also about skills. So it's a skills matrix for the board but at a management level, do we have somebody in the finance team or the broader executive that has the skills to address climate-related risks and opportunities?

Again, it's important that there's an emphasis on connections between various sustainability related risks and opportunities. So IFRS S1 articulated it and they also do it here, that sustainability risks and opportunities don't sit in isolation but there's a linkage and also, that a company should integrate its oversight of all sustainability-related risks and opportunities. Actually, it's all... I think sustainability is all about collaboration. It's collaboration between most parts of the business because sustainability, in particular climate-related risk, could sit anywhere in the organization so it's how do we get collaboration around risks and opportunities?

If we move to the second pillar which is strategy, what are they recommending or will be requiring around strategy? So they would like organizations to disclose information on how climate change could reasonably be expected to affect their business model, their strategy and cash flows over the short-term, medium-term, or long-term and access to finance and cost of capital. So three parts there. How does climate change impact business model, strategy, cash flows, and how does it impact strategy, cash flow, business model over the short, medium, and long-term? Also, ultimately, how does it impact access to finance which could be debt financing or impact their cost of capital and potentially equity investments? So a real clear articulation of the impact.

So if we look at climate risks, earlier, we said climate-related risks consists of physical risk and transitional risks. So if we unpack physical risks a bit, physical risk could be acute risks so that could be an earthquake but it could also be a chronic risk so certain areas where we've got quite a regular flooding or prone to bushfires so it's a chronic physical risk. An acute physical risk would be an extreme weather event or an extreme event.

If you look at transitional risk, there could be risks around policy and other legal matters and if you think of over the last six months we've seen the new climate change bull, we've seen the safeguard mechanism being introduced, and we know we're expecting treasury to announce mandatory sustainability reporting. All of that is sitting within the policy and legal transitional risk. There's also technology risk around do we have appropriate technology in order to lower our carbon intensity? So what innovation is required? We also have market risk in that the market expectations change on what products they're willing to buy. And then, brand and reputation, incredibly important. If we ignore carbon and climate-related risk, what would that do to our brand and our reputation? So this is more our acute and our chronic physical risks which we've already discussed on. So Dean, happy to go on with that one. If you look at transition risk, we've discussed this as well. It's more the words around the diagrams that we've discussed earlier.

The disclosures, so a company would be required to disclose a description of its plans for responding to climate-related transition risks and opportunities. So examples, how do they plan to achieve any climate-related targets? How will these plans be resourced? How will they review their targets? How do they expect to adapt or mitigate climate-related risks? How do the entity expect to adapt or mitigate indirect climate-related risk in its value chain? So how do they intend to work with their customers and supply chains to address climate-related risks?

Also, do they have a carbon offsetting plan? If that's part of their initiatives, they have to disclose specific information to allow investors to understand these offset schemes.

As we know, buying carbon offsets is a last resort. It costs you money so it's expensive but that doesn't really fix the problem. So it is can we reduce our emissions in the first instance? And then, some companies use carbon prices to internalize the cost of emissions when they make capital expenditure decisions. So they would say, "When we look at alternative, let's bake into the budget the carbon cost and the emissions," so important that we explain how we apply that carbon pricing and also if we have offsets, how do we bake that into our modelling?

Important and I think this is something that now that sustainability is well and truly on the radar of CFOs and boards, a very important consideration is around financial position, financial performance, and cash flows. I'll give you an example here. One of the key items we've identified at BDO Australia when we calculated our own carbon footprint is we realized that business travel is our biggest contributor to our carbon footprint. So we could just go and buy carbon offsets which is a last resort and would be expensive.

Now, instead, an organization should be thinking, "Do we need all the business travel? Do we need all the overseas strips? Do we need all the face-to-face events training within our business in Australia?" Now, there will be some level of travel required. Absolutely. We are not saying, "No travel. No face-to-face events," but let's think about is there a way that we can critically evaluate when global travel, national travel is essential and when it could be avoided.

If we do that, we achieve two things. One, we reduce our carbon footprint but also it has a positive impact on our bottom line because we are not paying airfares, hotel accommodation, etc. So that linkage with financial performance is incredibly important. So the one disclosure year is around that link with financial position, financial performance, and cash flow, the company might disclose a material asset impairment as a consequence of a strategy or for managing a transition risk and maybe we are moving out of a certain building because it's in a flood zone or the company would be investing a lot of money in new technologies and innovation to use the advantage of a climate-related opportunity so that would explain a significant investment on our balance sheet.

Some additional examples. These financial accounting consequences could be increased revenue, it could be additional costs of products to have lower carbon products, it could be physical damage to assets as a result of weather events, it could be cost to do climate adaptation. So it's important when providing quantitative information, companies are permitted to disclose single amounts or ranges of amounts.

Another part of the disclosures is climate resilience. So if we've identified climate risks, how does the organization intend to respond and how resilient is the organization to these risks? So disclose information such as whether it can continue to use assets and investments in a way they've done before because if there's increased flooding risk, can we still use it or should we relocate, decommission, or upgrade the asset? We should also disclose whether the organization has sufficient finance available to withstand these climate-related risks or maybe take advantage of opportunities.

Also, a requirement to use climate-related scenario analysis to assess risks and opportunities and finally, there's a proposal for companies to disclose how its climate-related analysis aligns with the latest international agreement on climate change. So our climate analysis linking to, for example, the Paris Agreement which is the latest international agreement at the moment. Dean, I think this is where I hand over to you to pick up on risk management as well as metrics and targets.

Dean Ardern:

Thanks, Aletta. I just thought too, it is interesting when you're talking, I was just thinking about... We've talked about in the last couple of seminars about the ways that regulators have been putting pressure on entities to make these disclosures and the interesting thing I'd thought about that is that in the context of this framework, the regulators haven't certainly been talking about the opportunities. They talk about the risks, they want to hear about the risks but not necessarily the opportunities.

But also, they don't talk about the strategies either which is, I think, is an interesting thing because it's a one-sided... Maybe you could look at it maybe a little bit suspiciously and think, "It's a bit of a one-sided approach to try and get entities into ESG reporting," but what it does is it makes you really think as a, say if you're a CFO or a CEO, think about your disclosures more holistically and saying, "Well, actually, if I'm putting in risks, can I put my strategies as well? Can I put in my opportunities?" These are all part of the story. It's not a one-sided story but it can be a very one-sided discussion if it's only really focused on the risks. So, to me, it's an interesting conversation to see how people are moving towards a more holistic disclosure regime, maybe not even thinking about it while they're doing it.

Aletta Boshoff:

Correct.

Dean Ardern:

So I'll move on to risk management. The risk management in terms of the pillar, the risk management disclosures follow effectively the same structure as the proposed IFRS S1, the proposed IFRS S2 requires information about the processes that companies are using to manage climate-related risk and opportunities. Now, I think the interesting thing for this is that, again, we've talked about this in the last couple of presentations but when you read the standards, S1 is the same and S2 is the same, as accountants you read them and they sound a lot like accounting standards. They read like accounting standards. They have similar approaches and this particularly, these disclosures remind me a lot of the more recent disclosures that the IASB have put out. The way that they're written, not necessarily the content but the way that they're written. So they're focusing on principle based and they're focusing on tell us about so facilitate my understanding or facilitate the user's understanding.

So it's about giving the framework or giving information which gives the investors a framework to understand the information. So explaining, "Okay. I've got certain risks but what am I doing around those things?" So when you think about those disclosures, if you were sort of thinking, "What would they look like?" I think if you think about the disclosures that we're required to give around expected credit loss under SSB 7 and IFRS 7, I think it's that type of disclosure where they're saying, "Tell me what you do. Tell me about your processes. Tell me about what your inputs are. Tell me about what your objectives are, what your strategies, how you're mitigating those things." So IFRS 7 is a really good example of a standard that has a similar sort of feel to it that it's not necessarily about disclose this, that, and the other thing. It's not about specific things. It's about we all know you've got this but what do you do about it and how do you measure it and how do you manage it?

And so, from that perspective, that's why it's when you read IFRS S2 as well as S1, as an accountant, you get a feel of exactly... It's very natural language so you get a very, very good or should get a very good understanding immediately when you read it what exactly they're looking for or the kinds of disclosures, what the disclosure should look like. It's interesting too that S2 is looking at disclosing how entities prioritize the climate-related risks relative to other types of risks, including the use of the risk assessment tools such as the science-based risk assessment tool.

So again, it's saying to you, "How are you doing this? Tell us exactly how you're doing it." It's no different to when you think about an ECL disclosure too where they say, "How do you measure credit risk?" and you say, "Well, I do it on the basis of days outstanding." So I haven't been paid for 30 days, 60 days, 90 days outstanding. It might not be the perfect model. You know might find when you look at banks' financial statements there, they're much more sophisticated but you might say, "Well, actually, it works for me and it does grade my risk relatively well given my circumstances."

The other pillar, the last pillar, targets and metrics. This is where it ends in many respects. I suppose when we think about those pillars, those pillars are really interconnected. So you think about starting at governance, how do you manage this? Then you're working your way down to strategy or when thinking about governance, you're thinking about, "Who manages this?" When you move down to strategies, "How you manage this?" When you're moving further down to risk, you're thinking about, "What are my fundamentals? What are the things I'm exposed to and what are my opportunities?" When you get down to targets and metrics, it's looking at actually, "How do you implement all those things above it and how do they all integrate it to a point where you've identified the things that you need to know and how do they then turn feedback into your governance and your strategy and your risk management?"

So the targets and metrics are a critical part of it if only to be able to demonstrate to, perhaps users, "Yes, we are actually measuring it." Like, "We're managing this but by virtue of the fact that we're measuring it, we can manage it because we can actually then adjust our governance, strategy, risk management to reflect any changes that we might be experiencing." Now, if you're not measuring it's very hard to tell whether things are changing and therefore whether or not you need to implement any changes.

But if you are measuring it, you may or may not be measuring the right thing but there is also an issue about well, you need to disclose exactly what you are measuring to give people an understanding about how you're going about it. The interesting thing to me too is that I remember many years ago when I was in standard setting and talking to quite a senior standard setter about operating segment disclosures and I remember him saying to me, "I like operating segment disclosures because if an entity doesn't disclose that information, it tells me something about the entity as well. If they do disclose operating segment information, good. That tells me something. But if they actually fail to disclose operating segment disclosure, that also tells me something. So that tells me something about the way the board manages the business presuming that they're simply not disclosing because they don't want to. Presuming that by virtue of them not disclosing, it means they don't have anything to disclose."

So I think targets and metrics are in that same areas that if you got through all the disclosures right down to targets and metrics and you waxed lyrical about all of your governance and risk management and strategies around ESG but you came down and said, "Well, actually, we don't have any targets and metrics," I think your discloses would look really hollow and I think your message would be really not a strong message about your ESG credibility.

So targets and metrics are almost like the... It's the cream on the cake but it also is the thing that ties everything together. So in the absence of those things, I think your disclosures would be quite limited. It is required to disclose your metrics and targets and I think the whole point of it is it's not so much what metrics and targets you're using, although I'm sure users would be interested in knowing how you're doing it but the very fact that you do have metrics and targets is probably a critical part of it because unless you are actually measuring it, it's very hard to manage it.

Greenhouse gas emissions, I think we mentioned those before, Aletta sort of in passing. So when you get down to the metrics, the greenhouse gas emissions is probably a critical part of it. I think Aletta mentioned previously is that as a transition relief that the ISSB have actually said that they wouldn't expect it in the first year of applying IFRS S1 and S2, that entities would've to measure Scope 3. Scope 3's probably the more complicated one. Well, the most complicated one. Scope 1 and 2 are probably a lot more easier and again, just, again, it's unsurprising that the standard setters have done this. It's trying to get entities into a framework in the quickest and probably least difficult way and one way of doing that is relieving them of providing Scope 3 disclosures.

It was mentioned there of the intensity of those emissions. Intensity of emissions is actually a measure of carbon dioxide and other greenhouse gases per unit of activity. So to understand that, just think about it as that well, how much greenhouse gas emissions are created by the production of one unit? It gives you an idea about the... It's not just the volume but it's also how much per unit. It's easy to misunderstand a volume if you don't understand exactly... You can't make it relative to something.

So using that intensity aspect is way of actually helping people to understand, "Okay. Your volume might be very low but your intensity's very high in the sense that you don't produce many units," or vice versa, "Your intensity's very low but your volume's very high because it requires you a lot lower per unit production."

At this point in time, the ISSB have permitted the use of the Greenhouse Gas Protocol. I think eventually, they'll move to it. The expectation, I think, is that most entities will move to it and the reason for that is it's relatively widely accepted and relatively recognized as an appropriate framework to measure greenhouse gases and greenhouse gas emissions. In terms of group reporting, obviously, consolidated group would be required to disclose their emissions by associates and joint ventures separately from the consolidated group and I mentioned it before about the scope exemption for and the relief provided for Scope 3.

This diagram provides just a little bit of a, I suppose, context to the Scope 1, 2, and 3 emissions to understand them. So your Scope 1's are obviously your direct emissions, talking about your company facilities, your company vehicles. So company facilities, keeping in mind that they could be your leased properties as well so they don't have to be physically owned assets, it's what assets that you are responsible for or control.

Your Scope 2, your indirect, includes your transportation and distribution and I think Aletta mentioned before transportation at BDO, when we did our carbon footprint, we discovered that effectively transport and travel was one of our largest greenhouse gas producers. You're looking also at processing of solid products, use of solid products, and various other ways down the supply chain.

Your Scope 3 are lots of other aspects to it. So looking at the things that actually feed into your supply chain so looking at things like purchased goods and services, your capital goods, and things like fuel and related activities. Now, there on the right-hand side of the screen is the BDO Global's publication on the Greenhouse Gas Protocol. BDO global produced some really good at a glance publication so they're relatively short, concise, and they've got lots of good information on them. Also, it'll help you in terms of being able to identify where to look elsewhere for further information so I'd recommend if you are interested. Certainly, it's a good publication to look at.

Aletta mentioned industry-based disclosures before when she was talking about the Appendix B, these industry-based disclosures, they're really carved up in terms of looking at various different types of industries and trying to identify the types of disclosures we'd expect to see for that industry relative to what our expectations are around their ESG obligations, requirements, and perhaps also their carbon footprint.

The disclosure topics included there... The requirements relate to the climate-related risks or opportunities of each of the industry group and they actually provide a set of metrics along with it too to provide you with some guidance as to the kinds of things you might expect to see disclosed around those particular risks and opportunities. They are really most likely to be significant to companies that are in particular industries. And so, the disclosures are really curated for industries rather than particular entities. So as much as they're a good starting point, you'd also need to think about, "Look, in my particular circumstances, what do I do that may be different to the industry that I work in or that I'm a part of and the effect that might have on my, for example, my greenhouse footprint?"

Now, bit of a bit spill of information here but it's probably worthwhile just to understand it. So the proposed IFRS S2 includes 77 industry classifications across 11 sectors. So it's quite a broad classification so it's very, very likely that you can find a category in which your entity falls within. The related disclosure requirements are derived from the SASB standards and I'll mention it later but when you look at the actual Appendix B, there are codes that take you back to the SASB standards. And so, it gives you an idea about where do I need to look in the SASB standards. So this is the way that, effectively, the ISSB is incorporating SASB disclosures in... Was one of the ways. It is incorporating disclosures into the ISSB standards.

Now, this information being identified as relevant to an assessment of the enterprise value of companies in that industry, like I said, it's been identified as relevant, you'd need to consider your own circumstances because your situation may very well be a little bit different to the rest of the industry you're operating in. Maybe you've entered that industry more recently, maybe you have different equipment, maybe you have different plant, maybe you have different arrangements, you might already be on green energy, those sort of things that you need to think about.

The industry classifications are intended to be useful for companies and investors in identifying relevant disclosures. Again, facts and circumstances, it's a good starting place and need to think about exactly how you might actually amend those or adjust your disclosures for your own particular circumstances. Industry-based topics and associated metrics have been included in Appendix B, like I mentioned. Those metrics then run across to the SASB standards as well so they give you some reference in there. So identifying those and given you'd be able to follow those through to be able to identify some guidance around what and how.

A company can view all the topics and metrics or just those of the specific industry. Obviously, there's nothing stopping any entity applying all of them or some of them. It's really just guidance to be able to understand what would we normally expect to see and it would help you also structure your thinking about what I should be doing. There's 68 industry-based sets of disclosure requirements in separate volumes. The remaining 9 industry classifications don't have climate-related disclosures so you might find that there's some industries that don't quite have any climate impacts for various reasons. As a consequence, they've been identified separately.

Now, this is just... What I provided there is effectively just a summary of those tables that explain the various industries and also referencing them to where they're found in the actual Appendix B. So you can see there for example, consumer goods, apparel, accessories, footwear that's found in Appendix B-1 so it's just a cross reference, I think. But as you can see, there's actually quite a lot and there's another slide as well so there's quite a broad range of industries covered so I would fully imagine that you'd be able to find an industry that suits or even is very, very close to what your entities would fall into.

Now, if we just use one example, software and IT services. Now, I was thinking about this two days ago in fact when I was listening to the federal budget because again, I wasn't maybe thinking about it that deeply, but I was thinking about software and IT services and it was announced in the federal budget just recently about the... I don't remember what it was called again. The Clean Building Fund.

So the Clean Building fund is a fund that grants money to companies to encourage them to move towards green energy and one of the things that they've done is changed the scope of that fund to include data warehouses and data centres and the reason for that is I hadn't... Maybe I was away with the birds when I was thinking about it but I thought that's an interesting thing. And then, someone mentioned, "You know they're very big energy users." I could just imagine data centres and data warehouses, a lot of computers, a lot of energy supplies so it would make sense that they should be encouraged to be using buildings which are more environmentally sympathetic on the basis that obviously, they are potentially large producers of greenhouse gas emissions. So I thought it was an interesting one to look at. It wasn't chosen specifically for that but it just was a interesting conflation of thoughts.

So if you're in that software industry services, you'd move your way through to the sustainability disclosure topics and metrics and as you can see there on the left-hand side of the table, the topic is describing environmental footprint so it breaks down the various areas broadly and then breaks it further down into accounting metrics. So if I think about environmental footprint of hardware infrastructure, "Oh okay. So total energy consumed," that could be an accounting metric that I could disclose. Percentage grid electricity, so how much am I pulling off the grid? Percentage of renewable, how much am I actually using, generating myself, or perhaps purchasing through the grid as renewable energy and so on and so forth?

So you can see what they're trying to do is they're taking a broad area that is relatively easy to identify within your business and trying to break it down a little bit within the different disclosures. Pardon me. Yeah. I mean, it's very similar approach but activity metrics as well. Now, in terms of getting ready for IFRS S2, I think we've mentioned it before that a really good place to start is the recommendations of the task force for climate-related financial disclosures and the reason for that is a couple of things.

One, is that, clearly, the ISSB have based some of their standards and their disclosures on these recommendations so they've used the framework and we mentioned before, the idea of the four pillars. They've used those frameworks to disclose those things and they're using those, and as Aletta mentioned previously too, that we would expect the ISSB to be continuing to use those pillars going forward through all the standards.

So once you've started on that journey and you've identified the pillars and you're working your way down through them, that information doesn't become irrelevant in the change in the accounting standard. We'd expect it to continue to be relevant. It may be need to be enhanced but at least, the framework is there, you have something to base it on.

The TCFD Disclosure requirements are really a good place to start because they can apply to all entities. They're very generic, they're very high level, but they also provide good framework to think about your disclosures. They do cover off and as the diagram on the right-hand side of that slide describes, they do cover off all of those other aspects of your climate-related risk opportunities and financial impact. So for me, I mentioned before the idea that you need to be very careful about knee-jerk disclosures and reactions to disclosure requirements and thinking about, "I'm needing to be giving a balanced view here. Now, if I don't have any opportunities or I don't have any risk management, well, obviously, that's what the disclosure's going to be. I'm going to be quiet on it. But if I do, then it would be helpful to investors, obviously, to know that if I'm also telling them about my risks because it also explains to them what I'm doing. It informs their decision making."

Now the interesting thing too, and I've heard this sometime ago, that when we started researching into climate-related disclosure and the effect of that on investors, I'm going back a bit now, often it didn't have... The effect wasn't necessarily always obvious that it necessarily helped investors. Now, the interesting thing is that I think investors were always looking for the information but not quite sure how to use it, not quite sure how to understand it, and not sure how it fitted into their proprietary models about valuation.

So in the past, you tended to find that people didn't maybe react to that information as probably as in such an informed way as perhaps they are now. So it's something that you need to consider too is that the idea that well, notwithstanding people might not have wanted, desired, or need this information in the past, they're clearly looking for it now and you might expect that their proprietary valuation models will start to build that kind of information in as well. So as Aletta mentioned in a previous slide too, entities themselves building things like greenhouse gas footprints into their capital investment decisions.

I mentioned the four pillars, the TCFD is based on them as are IFRS S1 and S2, they're good structures in which to understand your disclosures. I think the key thing to probably highlight here is just that the 11 recommendations, they're very easy to get into your financial statements compared to say if you went to IFRS S2. So IFRS S2 is obviously a lot more deeper. If you are trying to find a way to get into IFRS S2, the TCFD Disclosures are a good place to start because they're not as deep and they're much more aligned with your financial reporting processes.

So looking at things, for example, the governance, the board's oversight of climate-related risks and opportunities, I can see that completely being built into things like your operating financial reporting disclosures but also things like other disclosures within your financial statements like risk management in terms of, for example, IFRS 7 or other financial disclosures. Describe management's role in assessing and managing client risk in OFR but it could also be built into other aspects of your financial statements.

Just a reminder. As a transition relief, Scope 3 emissions, entities are relieved of having to disclose those in the first time but there is an expectation that they will have to going forward. It's after the first year of transition in the second year and going on and obviously, there would be an expectation you'd be moving towards the Greenhouse Gas Protocol as opposed to using another framework. I mentioned before, the GHG Protocol, the BDO Global at a glance publication, it's a good place to start. It is a continuous improvement journey. I'm not a big fan of that phrase journey but I'll have to admit it is actually a journey. It is not a one-step process and it's not something that you necessarily can see the end of like it's something that you have to build into your processes and it just becomes like what you do with your financial reporting. Every year, you're closing up your books, you're putting together your financial statements, and at the same time, you'd expect to be putting together some notes around your ESG position.

So effectively, in terms of that journey, it starts out with that calculator report baseline and we mentioned it before, you have to start somewhere. You disclosures help you to move towards there but you need that baseline to start with. You need to measure everything first. You develop your carbon reduction strategy so that pillar of the TCFD, so what are your strategies? You implement that carbon reduction strategy and then you monitor it. What you're monitoring is obviously your metrics and your other information that you detail quantitative and qualitative information around it. So as much as I don't like the phrase journey, it is actually a journey. It's a process that is continuous, it doesn't stop, it keeps going because there's always and I think... Yeah. I think the key part of it is to understand that obviously, there's a lot of estimations, a lot of movement and there's changes in strategies too. It's a shifting area so we can't imagine that once we've done it, we're finished. Things are going to keep moving and we have to just keep working that process through.

Next steps. Interestingly, we spoke to a client the other day about their efforts in terms of developing ESG report and the interesting thing to come out of it was that they really did emphasize, I don't think they were trying to, but they kept coming back to the fact that they had to keep revisiting what they were doing. So there was a constant approach that they had to keep coming back to the measures that they were making around some of their environmental and social aspects and questioning them and thinking about different ways to measure them. Part of that process was really around understanding how do my proxies, that I can see, relate to the things that I'm trying to measure that I can't see?

And so, by virtue of picking them, sometimes they picked some good proxies which helped them but then sometimes they're picking some maybe not so good proxies because they were probably more obvious but not the best measures of what they were trying to achieve. So there was this sort of on... And they were realizing in that process that it is this circular process whereby you build your decarbonization strategy, you start implementing, and then you find when you're measuring your carbon footprint, you might actually have to go back to your strategy and think, "Actually, it's the metrics or maybe it's our processes but we have to go back and have a look at it again and reframe and then you go back and measure again and consider how it's actually changed." So it is a process but often, the starting point really does involve looking at your baseline and thinking about what exactly you do and understanding that in the context of your wider activities.

We'll just provide there just probably a quick guide. Maybe the best way to use that, I think, is to probably look at it as a way to frame your thinking around if you are moving into ESG reporting frame, you're thinking about what are the things I have to do and in what order do I necessarily have to do them? The clear part of it is probably... There's a couple of clear bits obviously. One, it's a board priority and often, a case with these kinds of things, it requires a champion on the board. So one of those things is about governments.

The next one is about strategy and going, "Where does this fit in with what we do? How do we integrate it in such a way as that, notwithstanding it's going to be a bit of work, it actually flows out in a way that produces things that we can use so it produces information we can use and that we can support?" And then looking at it from the perspective saying, "Okay. Once we understand our strategy, we understand our risks, what's the best way to measure it?" So hopefully, that kind of thing will give you a bit of a headstart and I think, Susannah, that takes us to, I think the end of the presentation.

CCH Learning:

Thank you very much for that, Dean and Aletta. That was a lot of information in an hour but that's okay. I'll just take that back and show my screen. So yes, we will be spending the next few minutes taking questions. So please put them into the questions pane. To give you some time to type those up, I will mention our upcoming webinars.

Next week, we're looking at how to increase your fees and keep your clients. We've also got our tax technical update for May coming up. We're looking at working with difficult people and the accidental counsellor. We're also looking at officer duties of due diligence under WHS legislation and we're also looking at the year-end conversations for all your SMSF clients. If you're interested in any of those, please head to our website at wolterskluwer.cchlearning.com.au. All right. So let's have a little look at our questions. I have a question from Jane. Jane is asking, "Are the proposed IFRS S1 and IFRS S2 the only ISSB standards we should expect or is the ISSB intending to issue more standards and if so, what would they cover?"

Dean Ardern:

Okay. The answer would be yes. They are intending to issue more standards. I think I've mentioned in previous presentations so IFSR S1 is a bit like... No, it's a bit like SSB 101 and SSB 108 together. It's a bit of a framework standard. S2 is a bit more detailed disclosures. I think Aletta mentioned before that the ISSB are currently in the process of actually looking to develop quite a few other standards. So they're looking to develop one on biodiversity. I think they're looking at human rights and workforce. I think another one they're looking for, I think supply chain, I think Aletta had mentioned as well.

If you're interested, I think it's pretty easy to just in your internet browser, just basically type in ISSB work plan or something like that and you'll get to the ISSB website which isn't linked to the IFRS website and I think you'll find pretty quickly that they've got quite a few projects on the board. They probably haven't identified everything they're going to do like I suspect when you think about ESG... Well, okay. We've got IFRS, if we've got nearly, I don't know, 30 IFRS standards. I don't think the ISSB is probably necessarily as bold to announce that they're going to issue 30 more standards but I imagine that there'll be more after that.

I'm sure that they've got a whole list of ones that they want to address but you might find that they're not necessarily identifying them at this point as a priority or necessarily thinking that's what they're going to do because they might find in the process that rather than having that topic in this standard, they might decide to do it as another standard. But yeah, the answer is yes, there'll be more and I don't know how many but yeah, expect more.

CCH Learning:

Thank you for that. Thank you for that, Dean. So I hope that helps you there, Jane. Might need to go do some investigation. I also had a question from Michael. Michael was asking, "There seems to be a lot of discussion around Greenhouse Gas Protocol. How does it relate to standard S1 and S2 and do entities have to apply it?"

Dean Ardern:

Yeah. So maybe if I answered the last question first, do they have to apply it? No, not at this stage. It's one of the frameworks that they could apply and keep in mind, the Greenhouse Gas Protocol is probably best used for measuring your Scope 3 emissions which are the hardest ones to measure. But at this stage, those are also for the first year of ESG reporting, effectively those Scope 3 emissions, you've got some transition relief around them so you don't have to do them. So you don't have to use necessarily, at this point, the Greenhouse Gas Protocol or necessarily use all of it.

To give you context of what it is, it's effectively like accounting standards for measuring greenhouse gas emissions. So imagine when we think about accounting standards, if I say to you, "I've prepared these financial statements in accordance with IFRS," we all know, "Oh, okay. I understand." So your property plant equipment's measured at cost or fair value, your inventory is measured at cost of replacement, those sort of rules we already know. So if you think about the same scenario with greenhouse gas emissions, if I was to say tomorrow, "Measure your greenhouse gas emissions." You couldn't and wouldn't probably physically measure them. I'm not going to put an equipment on the back of my car to capture how much is being produced by my car. I don't even know how to do that.

But so like with accounting, what we do in accounting, we estimate things based on proxies and assumptions and other information. So when we think about, if I'm trying to work out depreciation on an asset, I might say, "Okay. Well, it's this type of asset. I generally know that it lasts for about physically last for five years but maybe I'll turn it over in three because technology-wise, it's become redundant at that stage." So my useful life is estimated at three years, I divide the carrying them out by three years and I work at my depreciation expense.

So think of a similar thing where I've got a fleet of cars and I'm trying to work out how much that fleet of cars produces in greenhouse gas. I could put a plastic bag on each one of the exhausts and catch it that way or there might be some rules that I could apply like what the ATO does and says to you, "If you use your car, this is what your deduction is per kilometre," so you could do the same thing and I suppose when you think about that you go, "Oh okay." This is probably where the protocol then comes in which says, you might say, "Well, I've got a big fleet of cars. I assume I've got a big greenhouse gas emissions."

But you might say, "Well, yeah, but all of them are electric." "Okay. Well, okay. Well now, how do I adjust for that?" or half of them are electric and half of them are petrol, "Okay. So how much... Is it the fact that I've got all of these cars or is it the fact that I use them?" So then I have to counter in, "Well, is it distance travelled or is it how they're used? Is it short trips or is it long trips?" So you can see what... These are the kind of things that you need about rules because it's hard to be able to quantify these things so we're trying to estimate these things but we all need to apply the same assumptions and I suppose processes and rules to get us to a point where our results are comparable to everyone else and that's what the Greenhouse Gas Protocol can help do.

CCH Learning:

Thank you very much for that, Dean. I hope that helps you there, Michael. A little bit of information there in that answer. Well, that does bring us to the end of our questions for today. So in terms of next steps, I would like to remind you all to please take a moment to provide your feedback when exiting. We have asked you a couple of questions about today's webinar so it's really important for us to hear your opinions. It's also a reminder that within 24 to 48 hours you will be enrolled into the e-learning recording which can be watched multiple times and have access to the PowerPoint, transcript, any other supporting documentation, and of course, your CPD certificate. I would very much like to thank Aletta and Dean for the session today and to you, the audience, for joining us. We hope to see you back online for another CCH learning webinar very soon. Enjoy the rest of your day. Thank you very much.