ISSB Sustainability Disclosure Standards

By Amy Kennedy, Harry Keegan, Ezra Zahabi, George O'Malley and Simrhan Khetani

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Introduction

The International Sustainability Standards Board (ISSB) published its first sustainability disclosure standards, IFRS S1 and IFRS S2 (Standards), on 26 June 2023 with the aim of improving the disclosure and transparency of ESG information reported by companies. The Standards were published after feedback was received on the ISSB's consultation on its exposure drafts (see our previous client alert on the **ISSB Sustainability Disclosure Proposals**) and incorporate the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD).

Together, the Standards have the objective of requiring an entity to disclose information about its **"sustainability-related risks and opportunities"** (IFRS S1) and its **"climate-related risks and opportunities"** (IFRS S2) which 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". The Standards aim to improve trust and confidence in company disclosures about sustainability to inform investment decisions and create a common language for disclosing the effect of climate-related risks and opportunities on a company's prospects.

The Standards have been developed to be used in conjunction with any accounting requirements and are built on the concepts that underpin the IFRS Accounting Standards. They must be reported at the same time as its related financial statements and must cover the same reporting period. Further, the Standards may be applied by an entity irrespective of whether the entity's financial statements are prepared using IFRS or other generally accepted accounting principles.

Endorsement of the Standards is at the discretion of individual jurisdictions, however, as further discussed below, the United Kingdom Government has indicated its intention for UK companies to adopt the Standards and is in the process of setting up an appropriate endorsement mechanism. As such, it is expected that UK companies will be required to adhere to these standards in future reporting.

Required Disclosure

1. Governance

   - Details on the governance processes, controls and procedures the entity uses to monitor and manage sustainability and climate-related risks and opportunities.
   - Information about the governance body's responsibility in overseeing these risks and opportunities and how informed the body is on these issues, as well as management's role in the governance process and if there are any controls and procedures in place to support this role.

2. Strategy
   - How sustainability and climate-related risks and opportunities might impact planning horizons for strategic decision-making by explaining how the entity defines short, long and medium term in light of how these risks and opportunities might occur.
   - The current and anticipated effects of these issues on the business model and value chain, and where these issues are concentrated in the entity.
   - How the entity responds, and plans to respond, to these risks and opportunities in strategy and decision-making, and any progress made since the last reporting period.
   - The effect of these risks and opportunities on the entity's financial position, performance and cash flow and any anticipated effects in these areas, including how funding in this area is sourced and if there are any investment and disposal plans.
3. Risk management
   - Processes and related policies the entity uses to identify, assess, prioritise and monitor sustainability and climate-related risks.
   - For instance, information on the inputs and parameters used, if the entity uses scenario analysis, how the entity assesses the nature and magnitude of the risks, and how risks are monitored.
   - Specifically for climate-related risks within IFRS S2, the entity must explain whether the risk is a physical risk or transition risk, and explain any mitigation and adaptation efforts along with any transition plan that the entity has.
4. Metrics and Targets
   - Metrics the entity uses to measure and monitor the sustainability and climate-related risks and opportunities, and any performance measures such as progress towards targets or adherence to law or regulation.
   - Targets it has set to monitor progress and metrics used to set the target.
   - For climate-related risks within IFRS S2, the entity must disclose its gross greenhouse gas emissions generated during the reporting period, the internal carbon prices, and whether executive remuneration is linked to climate-related considerations.

Adoption and UK Implementation

Individual jurisdictions will decide whether companies are required to comply with the above Standards. The ISSB will be working with jurisdictions and companies to support adoption, initially through creating a Transition Implementation Group to support companies that apply the Standards and launching capacity-building initiatives to support effective implementation.

The UK government has signalled support for the ISSB and is in the process of setting up an appropriate mechanism for formal UK endorsement and adoption of the ISSB Standards. The government is establishing two advisory committees: one to recommend which standards should be endorsed by the UK, and one to advise on how the Standards fit alongside existing reporting requirements for UK companies. In its Mobilising Green Investment: 2023 Green Finance Strategy, the UK Government has stated its commitment to introducing mandatory reporting against UK endorsed ISSB standards. Decisions on incorporating UK endorsed ISSB standards into UK company law will be taken alongside future reforms to the UK's non-financial reporting framework, as they are developed within the UK's Non-Financial Reporting Review[1].

While premium-listed UK companies must already include TCFD-related disclosures in their annual reports under LR 9.8.6(8) of the UK Listing Rules, the Standards would apply to a broader range of UK companies, listed and non-listed.

The Financial Conduct Authority has stated it remains "committed to playing an active role in supporting implementation of the ISSB standards and helping to build capacity to adopt these around the world". Its intention is to update the reporting requirements for UK companies in line with the ISSB's standards once they are endorsed for use in the UK. The UK is expected to make an endorsement decision on the Standards within the next 12 months.

IFRS S1 and S2 are effective for annual reporting periods beginning on or after 1 January 2024, with transitional period provisions in respect of an entity's first annual reporting period.

If you have questions about this client alert, please contact any Akin lawyer or advisor below:

Amy Kennedy
amy.kennedy@akingump.com
+44 20.7012.9868

Harry Keegan
hkeegan@akingump.com
+44 20.7012.9658

Ezra Zahabi
ezra.zahabi@akingump.com
+44 20.7661.5367

George O'Malley
george.omalley@akingump.com
+44 20.7661.5388

Simrhan Khetani
simrhan.khetani@akingump.com
+44 20.7661.5546

[1] The Department for Business and Trade is working with the UK Financial Reporting Council to conduct a review of the non-financial reporting requirements UK companies need to comply with in their annual report. Through this review, the UK Government is looking at what opportunities exist to refresh and rationalise current reporting requirements to build on the UK's non-financial reporting framework. The review is currently in the first stage of the process, which is a call for evidence.