



<b>Project:</b>	<b>Climate-related Financial Disclosures</b>	<b>Meeting:</b>	AASB 26 August 2024 (M207)
<b>Topic:</b>	Introduction to Agenda Paper 3.2.4 (working draft AASB S2)	<b>Agenda Item:</b>	3.2.3
		<b>Date:</b>	16 August 2024
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		<b>Decision-Making:</b>	High
		<b>Project Status:</b>	Finalising Standard

## Objective

- 1 The objectives of this paper and Agenda Paper 3.2.4 are for the Board to consider a working draft version of AASB S2 *Climate-related Disclosures* (as outlined in Agenda Paper 3.2.4) and decide on any changes required for the purposes of finalising AASB S2.
- 2 This paper highlights some aspects of the working draft AASB S2 that may require further discussion by Board members at the meeting on 26 August 2024.

## Adding Appendix D to AASB S2

- 3 The Board formed a subcommittee to identify which paragraphs of IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* need to be incorporated in an appendix to AASB S2 to enable it to function as intended. The subcommittee met on 25 June and 5 August 2024. Agenda Paper 3.2.6 (in supplementary folder) provides a summary of subcommittee meeting outcomes for Board members' information.
- 4 Staff have prepared Appendix D based on the decisions of the subcommittee. In addition to recommending which IFRS S1 paragraphs should be added to AASB S2, the subcommittee also recommends:
  - (a) using the IFRS S1 paragraph numbering in Appendix D so that readers would be able to easily make reference to AASB S1 or IFRS S1 and help demonstrate alignment with the 'baseline';
  - (b) the title of Appendix D should mimic the title of IFRS S1 to the extent feasible. Accordingly, staff have titled Appendix D as "General Requirements for Disclosure of Climate-related Financial Information"; and
  - (c) adding an introduction to the start of Appendix D explaining how Appendix D functions together with the body of AASB S2, and how it interacts with voluntary AASB S1.
- 5 In preparing the working draft AASB S2, relevant references to IFRS S1 paragraphs have been replaced with references to Appendix D paragraphs except for the paragraphs described in paragraph 6.

- 6 The requirements set out in IFRS S1 paragraphs B6(b) and B11 are consistent with IFRS S2 paragraphs B34 and B36; therefore, the subcommittee decided that those IFRS S1 paragraphs need not be included in Appendix D of AASB S2. When incorporating IFRS S2 paragraphs B34–B36 in AASB S2, staff have omitted the cross-references to IFRS S1 paragraphs B6(b) and B11. Changes made to IFRS S2 paragraphs B34–B36 are shown in marked-up text below, with deleted text struckthrough and new text underlined.

B34	<del>In accordance with paragraph B11 in IFRS S1, on</del> On the occurrence of a significant event or a significant change in circumstances, an entity shall reassess the scope of all affected climate-related risks and opportunities throughout its value chain, including reassessing which Scope 3 categories and entities throughout its value chain to include in the measurement of its Scope 3 greenhouse gas emissions. ...
B35	An entity is permitted, but not required, to reassess the scope of any climate-related risk or opportunity throughout its value chain more frequently than required by <del>paragraph B11 in IFRS S1</del> <u>paragraph B34</u> .
B36	<del>In accordance with paragraph B6(b) in IFRS S1, to</del> To determine the scope of the value chain, which includes its breadth and composition, an entity shall use all reasonable and supportable information that is available to the entity at the reporting date without undue cost or effort.

#### Questions for Board members

- Q1: Do Board members agree with using the IFRS S1 paragraph numbering in Appendix D?
- Q2: Do Board members agree with titling Appendix D as “General Requirements for Disclosure of Climate-related Financial Information”? If not, what alternative title do Board members suggest?
- Q3: Do Board members agree with not including IFRS S1 paragraphs B6(b) and B11 in Appendix D and removing cross-references to those paragraphs in AASB S2 paragraphs B34–B36?

#### Optionality in the Bill regarding consolidated reporting (changes to Appendix D)

- 7 To comply with IFRS S2, in accordance with IFRS S1 paragraphs 20 and B38, an entity would be required to prepare climate-related financial disclosures for its consolidated group if the related financial statements are prepared for that consolidated group.
- 8 Because the “reporting entity” concept is explained in IFRS S1 and not in IFRS S2, the subcommittee recommended that the requirements in IFRS S1 paragraphs 20 and B38 be incorporated in AASB S2 Appendix D, as follows.
- 20 An entity’s climate-related financial disclosures shall be for the same reporting entity as the related financial statements (see paragraph B38).
- B38 Paragraph 20 requires that climate-related financial disclosures shall be for the same reporting entity as the related financial statements. For example, consolidated financial statements prepared in accordance with Australian Accounting Standards provide information about the parent and its subsidiaries as a single reporting entity. Consequently, that entity’s climate-related financial disclosures shall enable users of general purpose financial reports to understand the effects of the climate-related risks and opportunities on the cash flows, access to finance and cost of capital over the short, medium and long term for the parent and its subsidiaries.
- 9 ASIC identified that the requirement established in IFRS S1 paragraph 20 may not be consistent with section 292A of the proposed legislation to establish the sustainability reporting regime in Schedule 4 of the *Treasury Laws Amendment (Financial Market Infrastructure and Other Measures) Bill 2024* (the Bill) in some circumstances. This is because under the Bill, a parent entity of a consolidated group has a choice, but is not required to, prepare a sustainability report for the consolidated entity.

- 10 Section 292A (1) and (2) of the Bill are reproduced below (emphasis shown in blue shaded text).

### **292A Who has to prepare annual sustainability reports**

- (1) Subject to subsection (2), an entity must prepare a sustainability report for a financial year if:
- (a) the entity must prepare a financial report for the financial year under this Chapter; and
  - (b) subsection (3), (5) or (6) of this section applies to the entity for the financial year.

Note: For financial years commencing before 1 July 2027, only certain entities are required to prepare a sustainability report: see Part 10.77.

- (2) Despite subsection (1), if:
- (a) the accounting standards require an entity (the *parent*) to prepare financial statements in relation to a consolidated entity for the financial year; and
  - (b) the parent elects to prepare a sustainability report for the consolidated entity for the financial year;
- then:
- (c) the parent is the only entity in the consolidated entity that must prepare a sustainability report for the financial year; and
  - (d) the sustainability report must be prepared as if the consolidated entity is a single entity.

- 11 Paragraph 4.54 and 4.55 of the Explanatory Memorandum to the Bill are reproduced below (emphasis shown in blue shaded text).

- 4.54 Whether an entity may choose to prepare a sustainability report on a consolidated basis is generally dependent on whether the entity prepares a financial statement on a consolidated basis.
- 4.55 If the entity is required to prepare financial statements on a consolidated basis, it may choose to prepare a sustainability report for the group on a consolidated basis (as the parent entity). This provision is intended to streamline general reporting requirements and treat the two reporting requirements (sustainability and financial) in a consistent manner. Where this occurs, each individual entity that is otherwise required to prepare a sustainability report would not need to, if the parent's sustainability report covers those individual entities in the consolidated sustainability report.

- 12 Staff note that subsections 292A(1) and (2) of the Bill expressly deal with which entities must prepare the sustainability report and those provisions provide optionality for the parent entity of a consolidated group. Specifically, subsection 292A(2) makes it optional (but not mandatory) for an entity that is required by accounting standards to prepare consolidated financial statements to prepare a consolidated sustainability report. Similarly, paragraphs 4.54 and 4.55 of the Explanatory Memorandum to the Bill identify that in circumstances where the parent entity is required to prepare consolidated financial statements, the parent entity has a choice as to whether or not it will prepare the sustainability report on a consolidated basis.
- 13 Given that the Bill provides a parent entity the choice of preparing a sustainability report for either the consolidated group or for the parent entity, staff consider that the requirements set out in IFRS S1 paragraphs 20 and B38 appear inconsistent with subsection 292A(2) of the Bill. To ensure that AASB S2 is not inconsistent with the Bill, staff recommend modifying the requirements set out in those IFRS S1 paragraphs when incorporating them in AASB S2 Appendix D.
- 14 In the working draft Standard, staff omitted paragraphs 20 and B38 and instead added paragraphs Aus20.1 and AusB38.1 to Appendix D, as follows (changes made to the text approved by the subcommittee are marked up):

- |          |   |
|----------|---|
| Aus20.1  | An entity's climate-related financial disclosures shall be for the same reporting entity as the related financial statements, <u>unless otherwise permitted by law</u> (see paragraph <u>AusB38.1</u> ).                    |
| AusB38.1 | <u>Unless otherwise permitted by law, paragraph</u> <del>Paragraph</del> <u>Aus20.1</u> requires that climate-related financial disclosures shall be for the same reporting entity as the related financial statements. For |

example, consolidated financial statements prepared in accordance with Australian Accounting Standards provide information about the parent and its subsidiaries as a single reporting entity. Consequently, that entity's climate-related financial disclosures shall enable users of general purpose financial reports to understand the effects of the climate-related risks and opportunities on the cash flows, access to finance and cost of capital over the short, medium and long term for the parent and its subsidiaries.

#### Question for Board members

Q4: Do Board members agree with the proposed paragraphs Aus20.1 and AusB38.1 in Appendix D?

### Amending IFRS S2 paragraphs 7 and 26 about avoiding unnecessary duplication of disclosures

- 15 To avoid unnecessary duplication of disclosures of common items of information required by IFRS Sustainability Disclosure Standards, IFRS S2 paragraphs 7 and 26 require an entity to provide integrated disclosures instead of separate disclosures for each sustainability-related risk and opportunity, if oversight of sustainability-related risks and opportunities is managed on an integrated basis. Staff consider that the requirements set out in those IFRS 2 paragraphs would be relevant only if an entity elects to voluntarily apply AASB S1 concurrently to disclose other sustainability-related risks and opportunities.
- 16 Accordingly, staff have deleted paragraphs 7 and 26 and added paragraphs Aus7.1 and Aus26.1 in the working draft Standard for the Board's consideration, as quoted below (changes made to IFRS S2 paragraphs 7 and 26 are shown in marked-up text).

Aus7.1	<p><u>If an entity elects to voluntarily apply AASB S1 <i>General Requirements for Disclosure of Sustainability-related Financial Information</i> (AASB S1) ([Month] 2024) to disclose information about other sustainability-related risks and opportunities, in</u> <del>In</del> preparing disclosures to fulfil the requirements in paragraph 6, <u>it</u> <del>an entity</del> shall avoid unnecessary duplication in accordance with <u>AASB S1</u> <del>IFRS S1</del> (see paragraph B42(b) of <u>AASB S1</u> <del>IFRS S1</del> – which is included in this Standard as paragraph B42(b) in Appendix D). For example, although an entity shall provide the information required by paragraph 6, if oversight of sustainability-related risks and opportunities is managed on an integrated basis, the entity would avoid duplication by providing integrated governance disclosures instead of separate disclosures for each sustainability-related risk and opportunity.</p>
Aus26.1	<p><u>If an entity elects to voluntarily apply AASB S1 to disclose information about other sustainability-related risks and opportunities, in</u> <del>In</del> preparing disclosures to fulfil the requirements in paragraph 25, <u>it</u> <del>an entity</del> shall avoid unnecessary duplication in accordance with <u>AASB S1</u> <del>IFRS S1</del> (see paragraph B42(b) of <u>AASB S1</u> <del>IFRS S1</del> – which is included in this Standard as paragraph B42(b) in Appendix D). For example, although an entity shall provide the information required by paragraph 25, if oversight of sustainability-related risks and opportunities is managed on an integrated basis, the entity would avoid duplication by providing integrated risk management disclosures instead of separate disclosures for each sustainability-related risk and opportunity.</p>

#### Question for Board members

Q5: Do Board members agree with the proposed paragraphs Aus7.1 and Aus26.1?

### Consideration and disclosure of industry-based information

- 17 At its 19 July 2024 meeting, the Board confirmed its decision to not require an entity to provide industry-based disclosures and to refer to and consider the applicability of the industry-based disclosure topics (and the industry-based metrics associated with those disclosure topics) defined in the *Industry-based Guidance on Implementing IFRS S2* issued by the ISSB.

18 Accordingly, the working draft Standard:

- (a) shows IFRS S2 paragraphs 12, 23, 28(b), 32, 37, B65(d) and B67 as deleted by the AASB;
- (b) shows the definition of “disclosure topic” in Appendix A as deleted by the AASB; and
- (c) includes paragraphs Aus23.1, Aus37.1 and AusB67.1 to retain the requirement for an entity to consider cross-industry metrics.

#### Question for Board members

Q6: Do Board members agree with the proposed changes described in paragraph 18?

#### Users of a not-for-profit entity’s general purpose financial report

- 19 At its 19 July 2024 meeting, the Board decided to require not-for-profit (NFP) entities to refer to the meanings of “general purpose financial reports” and “primary users of general purpose financial reports” specified in the *Framework for the Preparation and Presentation of Financial Statements* (the NFP Conceptual Framework) when applying ASRS 2.
- 20 Accordingly, staff added a subheading and paragraph AusA1 in Appendix A, as follows:

#### Australian-specific definitions

AusA1 The following terms are defined in the *Framework for the Preparation and Presentation of Financial Statements* (as amended to March 2020) for not-for-profit entities and are used in this Standard with the definition specified in that conceptual framework:

- (a) general purpose financial reports; and
- (b) primary users of general purpose financial reports (primary users, users of general purpose financial reports, users).

- 21 IFRS S1 paragraphs B14 and B15 (incorporated in Appendix D of AASB S2) provide guidance on a user’s resource allocation considerations. Consistent with the Board’s decision to require an NFP entity to refer to the NFP Conceptual Framework when applying AASB S2, staff are of the view that modifications to that guidance should be made for NFP entities to be consistent with that Framework.
- 22 Accordingly, with the support of the subcommittee, staff added in AASB S2 Appendix D paragraphs AusB14.1 and AusB15.1, which were proposed in ED SR1.<sup>1</sup> Stakeholders did not comment on those paragraphs. Those paragraphs and IFRS S1 paragraphs B14 and B15 are reproduced below for the Board’s consideration.

B14 The decisions of primary users relate to providing resources to the entity and involve decisions about:

- (a) buying, selling or holding equity and debt instruments;
- (b) providing or selling loans and other forms of credit; or
- (c) exercising rights to vote on, or otherwise influence, the entity’s management’s actions that affect the use of the entity’s economic resources.

AusB14.1 In respect of not-for-profit entities, the following are examples of decisions of primary users relating to providing resources to an entity:

- (a) parliaments deciding on behalf of constituents whether to fund particular programmes for delivery by an entity;

1 Exposure Draft ED SR1 *Australian Sustainability Reporting Standards – Disclosure of Climate-related Financial Information* (October 2023)

	(b) taxpayers deciding who should represent them in government;
	(c) donors deciding whether to donate resources to an entity; and
	(d) recipients of goods and services deciding whether they can continue to rely on the provision of goods and services from the entity or whether to seek alternative suppliers.
B15	The decisions described in paragraph B14 depend on primary users' expectations about returns, for example, dividends, principal and interest payments or market price increases. Those expectations depend on primary users' assessment of the amount, timing and uncertainty of future net cash inflows to the entity and on their assessment of stewardship of the entity's economic resources by the entity's management and its governing body(s) or individual(s).
AusB15.1	In respect of not-for-profit entities, the decisions described in paragraph AusB14.1 depend on primary users' expectations about returns and a not-for-profit entity's ability to continue providing goods or services. Those expectations depend on primary users' assessment of the amount, timing and uncertainty of future net cash inflows to the entity and on their assessment of stewardship of the entity's economic resources by the entity's management and its governing body(s) or individual(s).

### Questions for Board members

Q7: Do Board members agree with the proposed addition of paragraph AusA1 in Appendix A described in paragraph 20?

Q8: Do Board members agree with adding paragraphs AusB14.1 and AusB15.1 to Appendix D?

### Global warming potential (GWP) values

- 23 IFRS S2 paragraphs B21 and B22 require an entity to convert greenhouse gas (GHG) emissions into a CO<sub>2</sub> equivalent value using GWP values based on a 100-year time horizon from the latest IPCC assessment available at the reporting date (the latest is IPCC 6<sup>th</sup> assessment), unless emission factors applied by the entity have already converted the constituent gases into CO<sub>2</sub> equivalent values.
- 24 Reporting under NGER Scheme legislation, which is consistent with the Paris Agreement, requires converting GHG emissions using the GWP values in IPCC 5<sup>th</sup> assessment (IPCC AR5). At its 6-7 June 2024 meeting, Board members requested that the Basis for Conclusions include explanations that NGER reporters would be able to apply the GWP values consistent with the requirements set out in NGER scheme legislation in complying with AASB S2.
- 25 Accordingly, staff added paragraph BC39, as follows:

BC39	To align with the reporting requirements related to the Paris Agreement and NGER Scheme legislation, ED SR1 proposed to require an entity to convert greenhouse gases into a CO <sub>2</sub> equivalent value using the global warming potential (GWP) values from the Intergovernmental Panel on Climate Change (IPCC) 5 <sup>th</sup> Assessment Report (AR5), instead of the GWP values from the latest IPCC assessment available at the reporting date (the 6 <sup>th</sup> Assessment Report is the latest report available at the time of issuing this Standard). Upon considering feedback received on this topic, the AASB decided that such a mandate is unnecessary. This is because:
	(a) in accordance with paragraph B22 of the Standard, if an entity uses appropriate emission factors that have already converted the constituent gases into CO <sub>2</sub> equivalent values (e.g. the Australian National Greenhouse Accounts Factors), the entity would not be required to recalculate the emission factors using GWP values from the latest IPCC assessment available at the reporting date;
	(b) the AASB observed that an entity required by an Australian government authority or legislation to use direct measurement to measure GHG emissions is permitted under paragraphs 29(a)(ii) and B24 of the Standard to use measurement methods, including the GWP values, prescribed by that authority or legislation. Therefore, if a relevant authority or legislation (e.g. NGER Scheme legislation) requires an Australian entity to use GWP values from an IPCC assessment report that is not the latest IPCC assessment report available at the reporting date to convert GHG emissions into CO <sub>2</sub> equivalent values, doing so would not be a departure from IFRS S2; and

- (c) the AASB observed that the *Methods and Measurement Criteria Guideline* (July 2023) published by the Clean Energy Regulator states that “emissions are rarely measured through direct observation”. Therefore, there may not be many Australian entities voluntarily electing to measure GHG emissions using the direct measurement method that would be required under paragraph B21 to use the GWP values from the latest IPCC assessment report and be inconsistent with the Paris Agreement. That is, the AASB considered that the issue of which GWP values should be applied by those entities voluntarily electing to measure GHG emissions using direct measurement is unlikely to be a pervasive matter that would justify modification from the baseline of IFRS S2.

#### Question for Board members

Q9: Do Board members agree with the draft paragraph BC39? If not, what changes do Board members suggest?

### Scope 3 GHG emission categories

- 26 At its 6–7 June 2024 meeting, the Board observed that some stakeholders supported having flexibility for entities to categorise their sources of Scope 3 GHG emissions using categories most relevant to their circumstances and operations. The Board was of the view that IFRS S2 does not prevent an entity from using categories outside of the 15 categories in the GHG Protocol Standard and instructed staff to clarify this matter in the Basis for Conclusions.
- 27 Accordingly, staff added paragraph BC45, as follows:

- BC45 Some stakeholders commented that the Standard should provide flexibility for entities to disclose the categories most relevant to their operations. The AASB observed that to meet the objective of IFRS S2 paragraph B32—to disclose information about its Scope 3 GHG emissions to enable users of GPFR to understand the source of these emissions—an entity would:
- (a) consider all 15 categories of Scope 3 GHG emissions described in the GHG Protocol and disclose which of these categories are included in its Scope 3 GHG emissions disclosures; and
  - (b) in accordance with IFRS S1 paragraphs 15(b) and B26 (incorporated in Appendix D of AASB S2), disclose other material sources of emissions using other categories if after undertaking the step described in point (a) it determines that none of the categories described in the GHG Protocol adequately describes some of its material sources of emissions.

#### Question for Board members

Q10: Do Board members agree with the draft paragraph BC45? If not, what changes do Board members suggest?

### Greenhouse gas removals

- 28 At its 6–7 June 2024 meeting, Board members requested that the Basis for Conclusions provide explanations of the requirements relating to greenhouse gas removals, which is different to carbon credits. Accordingly, staff added paragraphs BC65 and BC66, as follows:

#### Greenhouse gas removals

- BC65 Some stakeholders commented that IFRS S2 is unclear about the reporting requirements relating to GHG removals. The AASB noted that, when reporting net GHG emission targets, IFRS S2 paragraph B68 establishes the principle that an entity may include offsetting effort beyond the carbon credits defined in the baseline (e.g. GHG removals).
- BC66 The AASB is of the view that, to meet the disclosure objective related to metrics and targets, where information about offsetting efforts is material, an entity would be required to disclose sufficient information about these offsetting efforts to enable users of GPFR to understand progress towards any climate-related targets.

**Question for Board members**

Q11: Do Board members agree with the draft paragraphs BC65 and BC66? If not, what changes do Board members suggest?

**Comparing AASB S2 with IFRS S2**

29 At the June and July 2024 AASB meetings, Board members requested that the Standard be prepared in a manner that would allow a reader to understand the differences between AASB S2 and IFRS S2. Accordingly, in addition to the explanations in the draft Basis for Conclusions, staff have added:

- (a) a “Comparison with IFRS S2” page (see page 5 of Agenda Paper 3.2.4) to explain the Board’s approach in preparing AASB S2 and the differences in the requirements relating to matters described in paragraphs 3–22 above; and
- (b) a “Deleted IFRS S2 text” page (see page 45 of Agenda Paper 3.2.4) to list out all IFRS S2 text not incorporated in the working draft Standard.

**Question for Board members**

Q12: For the purposes of finalising AASB S2, subject to the Board’s decisions on the matters discussed in this paper, do Board members propose any further changes to the working draft Standard as set out in Agenda Paper 3.2.4, including:

- (a) Appendix D;
- (b) the additional pages mentioned in paragraph 29; and
- (c) the draft Basis for Conclusions?