INTEGRATED REPORTING
COMMITTEE OF
SOUTH AFRICA

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To the Trustees of the IFRS Foundation

Comments on the *Exposure Draft: Proposed Targeted Amendments to the IFRS Foundation Constitution to Accommodate an International Sustainability Standards Board to Set IFRS Sustainability Standards*

The Integrated Reporting Committee (IRC) of South Africa is an association not for gain founded in 2010. Its objectives are to promote and develop integrated reporting and integrated thinking in South Africa considering the international harmonization of integrated reporting and the recommendations of the King Reports on Corporate Governance.

We appreciate the opportunity to comment on the *Exposure Draft: Proposed Targeted Amendments to the IFRS Foundation Constitution to Accommodate an International Sustainability Standards Board to Set IFRS Sustainability Standards* issued by the IFRS Foundation in April 2021 and our responses to the consultation questions are in the annexure that follows.

Our comments process included initial development by the IRC of South Africa's technical Working Group and input from the IRC's organization, corporate and honorary members before going to the IRC Board for discussion and approval. The Board approval process was led by Lead Board member Ms Parmi Natesan. Professor Mervyn King (Chair of the IRC, Chair Emeritus of the Value Reporting Foundation) and Professor Suresh Kana (Deputy Chair of the IRC and a Trustee of the IFRS Foundation) recused themselves from the approval process.

Yours sincerely

Leigh Roberts CA(SA)

Chief Executive Officer

Integrated Reporting Committee of South Africa

Annexure

Question 1

Do you agree that the amendments proportionately reflect the Trustees' strategic direction, considering in particular:

(a) the proposed amendments to the objectives of the Foundation, outlined in the proposed new section 2b of the *Constitution*, as set out in Appendix A; and

(b) the proposed amendments to reflect the structure and function of the new board, outlined in the proposed new sections 43–56 of the *Constitution*, as set out in Appendix A?

(a) Objectives

We cannot give a definitive answer to question 1(a) because the broadly-stated objective in 2b is difficult to reconcile with the information in the Introductory pages of the Exposure Draft (ED), and while the *IFRS Foundation Trustees' Feedback Statement on the Consultation Paper on Sustainability Reporting* (Feedback Statement) provides additional explanatory information there are aspects that remain unclear. In particular, the IFRS Foundation has not committed to exact definitions of the fundamental terms of "sustainability", "sustainability standards" and "sustainability-related financial disclosures". Nor is there a definition of "enterprise value" which is similarly fundamental to the stated strategic direction. In particular, on this term, is whether "enterprise value" includes the impacts a company has on society and the environment over time, rather than a narrow focus on only the (inward) sustainability matters that affect the company. The lack of certainty on the underlying terms negates the standing of the objective set out in 2b.

We believe that a narrow focus is not possible, nor in the interests of investors' longer term decision-making, to separate the sustainability matters affecting a company from its impacts on the environment and society because they are inextricably linked and can pose a real source of risk and opportunity to a company over time.

We believe it will continue to be important to connect financial reporting and sustainability reporting in a holistic corporate report. The integrated report provides investors and other stakeholders with a holistic picture of how a company is affected by sustainability matters and how, in turn, the company affects the environment and society. The integrated report usefully also covers strategy, risks and opportunities, performance against strategic objectives, governance, outlook and the six capitals, which provide critical information for investors to be able to make informed investment decisions. The integrated report using the guidance of the *International <IR> Framework* is already accepted as global best practice, and indeed, in South Africa, integrated reporting is the accepted norm. By making the connections in the integrated report we believe that the general standard of international corporate reporting can be enhanced.

(b) Structure and function of the new board

We are largely in agreement with the proposed amendments to reflect the structure and function of the new board as outlined in the new sections 43-56 of the *Constitution*. We do, however, have comments pertaining to the composition of the proposed new board with regard to geographic representation. While we recognise that Africa is not as economically powerful as the Americas, Europe and Asia, it is becoming increasingly important. There are 54 countries in Africa and Africa houses 17% of the world's population. Further, some parts of Africa are disproportionately affected by sustainability issues such as climate change. Restricting Africa to one seat on the new board

(International Sustainability Standards Board), and similarly so with other IFRS bodies, makes it difficult to represent different views and perspectives.

We note that provision has been made for four members from any area to sit on the new board and respect that these members will be chosen based on their ability to contribute rather than geographic linkage.

Question 2

On the potential naming of the new board and its associated standards, do you agree that 'the International Sustainability Standards Board (ISSB)' setting 'IFRS sustainability standards' accurately describes the function of the new board and its associated standards?

Clarity is needed on the terms and scope as outlined above. If a narrow view of sustainability matters is taken with the focus only on those matters that affect enterprise value, the name "International Sustainability Standards Board" could be misleading. The term "sustainability standards" implies a broad ambit for the new board in setting standards covering enterprise value plus the impacts of a company on society and the environment. The narrow use of the term is contrary to the generally accepted and widely understood use of the term "sustainability". This potentially poses a reputation risk to the IFRS Foundation and could result in a loss of trust by stakeholders. The new board's name should reflect the exact scope of its activities and the standards being set.

We refer to the "Group of 5" paper which uses the term "sustainability-related financial disclosures" to differentiate from "sustainability reporting": "Sustainability-related financial disclosure standards would enable disclosure of how sustainability matters create or erode enterprise value. This type of reporting is distinct from sustainability reporting, which is designed to illuminate a company's most significant impacts on the environment, people and economy."[1] The term "sustainability-related" might be more appropriate depending on the extent of the new board's activities and standards.

Question 3

Do you agree with this proposed consequential amendment, outlined in proposed new sections 60 and 61 of the *Constitution*, as set out in Appendix A?

We agree with the proposed consequential amendment, however, we believe that the *Constitution* should state the experience and knowledge requirements of the executive director. We suggest that these requirements are similar to the requirements for Trustees as set out in section 6 of the *Constitution*. The requirements should include an awareness and understanding of sustainability reporting and issues.

Question 4

Are there any other matters you would like to raise in relation to the proposed targeted amendments to the *Constitution*?

In our response to the IFRS Foundation's *Discussion Paper on Sustainability Reporting* issued in September 2020, the IRC supported the need for a global set of internationally recognised sustainability reporting standards to enable more comparable and consistent reporting. We pointed out that there were benefits and risks in the IFRS Foundation undertaking the task of setting such

[1] Reporting on enterprise value: Illustrated with a prototype climate-related financial disclosure standard Progress towards a comprehensive corporate reporting system, from leading sustainability and integrated reporting organisations CDP, CDSB, GRI, IIRC and SASB. Facilitated by the Impact Management Project, World Economic Forum and Deloitte.

standards. We stated that it was important for the IFRS Foundation to set out a clear path explaining the vision and direction for global reporting standards in the years ahead.

Further to this, we believe that fundamental to the acceptance of the new standards is support from a range of stakeholders - even if the standards are designed for investors.

It is important for the IFRS Foundation to demonstrate that it has the leadership and resources to take on this broader standard-setting role. This includes that the various governing bodies are appropriately constituted with an appropriate balance of expertise. In particular, ensuring that the Trustees of the IFRS Foundation has a balance of expertise.

Sustainability scope

Paragraph 2b of the ED discusses sustainability scope in relation to the new board. It states that it would prioritise climate change: "… due to the urgent need for better information about climate-related matters, the new board would initially focus on climate-related reporting while also moving quickly to work towards meeting the information needs of investors on other environmental, social and governance (ESG) matters." We acknowledge the importance of climate-related matters, however, we are not sure that a staggered approach is possible or desirable because of the inter-connectedness of sustainability matters.

Further, and with regard to the above statement, there is no time reference or explanation addressing "moving quickly towards". And, there is no explanation of "other environmental, social and governance (ESG) matters" or linkage to the United Nations Sustainable Development Goals. In addition, the consideration of the six capitals used or affected by a company is used in corporate reporting as they cover many actual and potential matters that affect a company's ability to create and preserve value or indeed that can erode value.

Paragraph 16b of the ED states: "… its standards would help investors and other participants in the world's capital markets to understand, compare and contrast a company's sustainability performance with that of other companies, and to determine how a company's performance relates to its value creation". We believe it is crucial that the new board always use the full term of 'value creation, preservation or erosion' because these aspects are equally important for investor decision-making.

Composition of bodies

Paragraph 10 of the ED deals with areas where no substantive amendments are proposed. We believe that some of these said areas require urgent attention, as set out below:

<u>Monitoring Board</u>: The Monitoring Board has an important role in the standard-setting process. We do not think this role should change. The Monitoring Board is rightly independent of the Trustees of the IFRS Foundation. Given its role, it is critical that the Monitoring Board ensures that it has sufficient sustainability knowledge and expertise to appreciate what skills and expertise are needed within the various levels of the organisation to fulfil its role regarding financial and sustainability standards.

<u>Trustees of the IFRS Foundation</u>: We refer to the point made under Question 1b regarding geographic representation. Further, we believe the Trustees should carry out a review to determine if it has sufficient sustainability expertise and that it strive to achieve balanced, multi-stakeholder representation. Paragraph 10b of the ED suggests that the collective expertise of the Trustees can be sufficiently adjusted where necessary in the coming years as the regular rotation of its membership takes place. We respectfully suggest that the IFRS Foundation take action to achieve an appropriate balance of expertise as soon as possible.

IFRS Advisory Council: We note that the Trustees are not proposing changes to the IFRS Advisory Council. For similar reasons as discussed above, we believe that the composition of the IFRS Advisory Council be reassessed as soon as possible to ensure that there is an appropriate mix of knowledge and expertise and that it include representatives of multi-stakeholders.

Sustainability Standards Interpretations Committee: We agree that it is probably too early to establish an interpretations committee at this stage. It would be useful, however, to know when the Trustees envisage it will be appropriate to create an interpretations committee.

Conceptual framework or guiding principles

While section 2b states that the new board should "… develop, in the public interest, a single set of high quality, understandable, enforceable and globally accepted sustainability standards based upon clearly articulated principles." Currently, there are no clearly articulated principles, nor is there a conceptual framework. We note that the new board will build on the work of existing frameworks to facilitate its work, however, we believe that, as early as possible, a set of guiding principles be developed. The guiding principles would also be of value to organisations that have to deal with issues for which no standards exist, and would contribute to achieving global consistency and comparability.

Audience

We recognise that the new board will focus on information that is material to the decisions of investors and other participants in world capital markets. We believe, however, that the information resulting from the use of the standards could also be of value to a range of stakeholders. For example, the standards are likely to provide some information used in integrated reports. We suggest that acknowledgement that the standards may also be of use to stakeholders other than investors might assist in encouraging their broader acceptance.

Building on the work of the key sustainability reporting bodies

It will be important for the new board to issue a suite of standards in a reasonable amount of time, rather than an extended period. We support the principle of building on the work of the existing standards and frameworks issued by the leading sustainability reporting standard-setters. While the due process for issuing standards must be followed, we urge the Trustees to investigate ways of speeding up the process for the development and issuing of sustainability standards.

Definitions

There are a number of terms used in the proposed *Constitution* and definitions are needed. We recommend the *Constitution* include a new section dealing with the IFRS definitions; including:

- Sustainability
- Sustainability reporting
- Professional background
- Enterprise value
- Enterprise value creation, preservation or erosion

Responsibility of the proposed new board

We are pleased to note that the new board, per section 55 of the *Constitution*, will have complete responsibility for all technical matters, including the preparation and issuing of IFRS sustainability standards and exposure drafts. It is important that no other body should be able to impose its authority over the new board.

IFRS Foundation name

The Trustees are recommending the retention of the name, IFRS Foundation. An alternative name considered by the Trustees was the "International Corporate Reporting Foundation". If a narrow view of sustainability is taken by the new board we believe that it is appropriate to retain the name IFRS Foundation. However, if the Trustees decided to broaden the scope of the new board to also deal with the impacts that a company has on the environment and society, it might be appropriate to consider alternative names.

The integrated report

We believe it will continue to be important to connect financial reporting and sustainability reporting in a holistic corporate report that also covers strategy, risks and opportunities, performance against strategic objectives, governance, outlook and the six capitals. The *International <IR> Framework* is already accepted as global best practice. We believe that the general standard of corporate reporting can be enhanced by the use of the integrated report as it offers a holistic and connected view of a company and its prospects.

Governance issues

<u>The role of Trustees</u>: Section 12 states that: "Trustees may make such operational commitments and other arrangements as they deem necessary to achieve the organisation's objectives, including, but without limitation, leasing premises and agreeing contracts of employment with IASB and ISSB board members." This seems to be blurring of executive and non-executive roles and we suggest that there should be a better definition of roles between the various governance structures.

<u>Approval of resolutions</u>: Section 14 states: "Each Trustee shall have one vote, and a simple majority of those voting shall be required to take decisions on matters other than termination of the appointment of a Trustee, amendments to the *Constitution*, or minor variations made in the interest of feasibility of operations, in which cases a 75 per cent majority of all Trustees shall be required." It seems strange that a 75% majority is required for minor variations made in the interest of feasibility of operations. Conversely section 15b only requires a simple majority to appoint the Executive Director.

<u>Review of strategy</u>: Paragraph 1 states that the IFRS Foundation *Constitution* requires the Trustees to review the strategy of the IFRS Foundation every five years. In today's fast-moving world, it may be more appropriate to review the strategy more often, say on an annual basis and perform a more extensive review every two or three years.

Placing of important information in the Feedback Statement

We suggest that in future the IFRS Foundation should ensure that all important information necessary for the understanding of proposals be included in the ED, rather than being placed in, for example, a Feedback Statement. Without studying the Feedback Statement, commentators would not have a thorough understanding of the proposals put forward.

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