ISDA

International Accounting Standards Board,
Columbus Building,
7 Westferry Circus,
Canary Wharf,
London E14 4HD

17 December 2020

Dear Trustees,

Ref.: IFRS Foundation Consultation paper on Sustainability Reporting

The International Swaps and Derivatives Association ("ISDA")[1] welcomes the opportunity to provide input on the above referenced Consultation Paper ('CP') issued by the IFRS Foundation in September 2020.

Representing the global derivatives market, ISDA's mission is to foster safe and efficient derivatives markets to facilitate effective risk management for all users of derivative products. ISDA members represent leading participants in the derivatives industry. Collectively, the membership of ISDA has substantial professional expertise and practical experience addressing accounting policy issues with respect to financial instruments. ISDA has also put in place a Sustainable Finance Working Group, which deals with relevant Environmental, Social and Governance (ESG) issues affecting the derivatives industry. While derivatives are widely used to manage or hedge risk in financial markets, they can also play a very important role in raising and allocating trillions of capital to green finance, helping firms manage financial risks related to ESG issues.

With respect to the CP, the key points we would like to emphasise are as follows:

- Given the increasing interest in and importance of ESG matters globally, there is a clear need for global transparency and consistency in sustainability reporting while building as much as possible on existing practices and taking into consideration firms' specific regional or sectoral characteristics. This can only be achieved through the development of global sustainability standards.
- The IFRS Foundation is appropriately qualified and can leverage its expertise to take on the challenge of setting global standards for sustainability reporting.

[1] Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has over 925 member institutions from 75 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org. Follow us on Twitter, LinkedIn, Facebook and YouTube.

- It is crucial that the IFRS Foundation builds on the established work and accumulated knowledge of those organisations and regional authorities[2] that have already developed and established ESG related reporting standards and works in co-operation with them.
- We encourage the IFRS Foundation to establish the SSB, define its governance based on a strong cooperation with international organisations and regional competent authorities around the globe, secure its mandate, and start by conducting a scoping exercise to properly assess the current sustainability reporting landscape in order to identify the areas in which it can most effectively add value. This will enable the SSB to adopt a realistic approach and avoid further fragmentation in sustainability reporting and the proliferation of reporting standards.

Our detailed responses to the questions raised in the CP are included in the appendix to this letter.

We look forward to further supporting the IASB as its work progresses in this area.

Should you have any questions or would like clarification on any of the matters raised in this letter please do not hesitate to contact the undersigned.

Yours sincerely,

Fiona Thomson
Managing Director
Goldman Sachs International
ISDA European Accounting WG Chair

Antonio Corbi
Director
Risk and Capital
ISDA

Appendix attached

[2] For example, the European Commission, European Financial Reporting Group (EFRAG), European Banking Authority and ESMA in Europe along with the International Platform on Sustainable Finance, the World Economic Forum and International Organisation of Securities Commissions.

Appendix – Responses to questions

Question 1
Is there a need for a global set of internationally recognised sustainability reporting standards? (a) If yes, should the IFRS Foundation play a role in setting these standards and expand its standard-setting activities into this area? (b) If not, what approach should be adopted?

ISDA very much welcomes the proposed establishment of a Sustainability Standards Board (SSB) by the IFRS Foundation to help prevent market fragmentation that would undermine efforts taken by the public and private sector.

Environmental, social and governance (ESG) risks and metrics are increasingly considered part of the credit-rating process, where material ESG risks have the potential to negatively impact the creditworthiness of a counterparty. As a result, ESG metrics are becoming integrated into the corporate/sovereign bond market with companies/sovereigns incorporating ESG into their business practices. By enabling the use of financial markets to hedge and manage ESG related risks, derivatives offer an effective tool to hedge climate risks for example (either direct physical risks or those related to required financial indicators). For a market such as this to develop, it is essential that there are commonly understood measures of ESG risk quantification that can be used for the purpose of pricing risk transfer tools.

There is also a growing demand from stakeholders for information on entities' progress in achieving ESG objectives and sustainable performance indicators. Entities, including public companies need to be able to report their performance on sustainability matters in a way that users of the information are confident of its relevance, completeness, and accuracy. It is therefore essential that there is global transparency and consistency to sustainability reporting practices while building as much as possible on existing practices and respecting firms' regional and sectoral specificities.

As financial products related to ESG develop, the accounting treatment for these instruments will also need to be considered. This could relate to features within financial instruments which impact their classification and measurement for accounting purposes or could affect the application of hedge accounting for ESG linked derivatives. The accounting treatment for ESG features would continue to be subject to the framework provided by International Financial Reporting Standards (IFRS), which should remain wholly separate from and not be directly affected by the development of global sustainability reporting standards. However, the development and application of global sustainability reporting standards and consequential increase in transparency, has the potential to improve the information available to determine the accounting of ESG features under IFRS. Additionally, whilst responsibility for setting sustainability standards and accounting standards related to ESG products would sit with different Boards within the IFRS Foundation, a close relationship between the two allowing the interaction of financial reporting and sustainability reporting implications, would bring a further benefit from the IFRS Foundation establishing a Sustainability Standards Board (SSB).

The IFRS Foundation is ideally placed to play a pivotal role in setting sustainability standards in great cooperation with those regional authorities and international organisations that have already developed and established ESG related reporting standards. Particular qualities that the IFRS Foundation has demonstrated in this respect are as follows:

- Establishing and running an appropriate governance structure to oversee the process of global standard setting. The IFRS Foundation provides overall oversight and is accountable, with responsibilities and decision delegated as appropriate, for example for accounting standards to the International Accounting Standards Board.
- Engaging effectively with stakeholders, to gather their feedback and respond to it in a transparent process. IFRS is globally supported and has therefore been adopted in large part because stakeholders are able to participate in the standard setting process and are therefore inclined to support the final standards having contributed to their development.
- Thought leadership, through the use of highly skilled technical experts to develop the proposals for new standards. A strength of IFRS is the intellectual rigour applied in their development, which lends credibility to the final standards produced.

These activities ensure that the standards produced by the IFRS Foundation are of high quality and are supported by stakeholders. These characteristics are essential for the development of global sustainable accounting and reporting standards.

Question 2
Is the development of a sustainability standards board (SSB) to operate under the governance structure of the IFRS Foundation an appropriate approach to achieving further consistency and global comparability in sustainability reporting?

Yes, we agree that the development of the SSB is appropriate. We note that the IFRS Foundation is well positioned to take on this role. A prerequisite for the SSB's success in achieving a harmonised approach towards ESG global standards is to initially focus on understanding the current landscape of sustainability reporting. This will enable the IFRS Foundation to work in cooperation with those regional organisations that have already developed and established ESG related reporting standards and add value towards the consolidation of reporting requirements while guarding against the proliferation of frameworks. We support the IFRS Foundation in this measure.

Question 3
Do you have any comment or suggested additions on the requirements for success as listed in paragraph 31 (including on the requirements for achieving a sufficient level of funding and achieving the appropriate level of technical expertise)?

With respect to paragraph 31(e) we encourage the IFRS Foundation to obtain diverse sources of funding. This will provide it with the long-term financial stability it needs to develop ESG accounting standards, which are to be required without delay and that will continue to evolve once they are set. Having a diverse source of funding will mean that the SSB will not be affected by a change in the ability or willingness of individual funders to continue their support.

Furthermore, the SSB may initiate its work by conducting a scoping exercise to evaluate the current sustainability reporting landscape in order to develop a clear view for its mandate and future funding requirements.

Question 4
Could the IFRS Foundation use its relationships with stakeholders to aid the adoption and consistent application of SSB standards globally? If so, under what conditions?

The IFRS Foundation should use its existing relationships with stakeholders to aid in the adoption of SSB standards. An important condition must be that securing the agreement of SSB standards is on the merit of the standards considered separately without any link or conditions attached to the other work on the IFRS Foundation in setting IFRS. The work of the SSB must have full independence and integrity from the other activities of the IFRS Foundation.

Question 5
How could the IFRS Foundation best build upon and work with the existing initiatives in sustainability reporting to achieve further global consistency?

The first priority for the IFRS Foundation should be to work closely with all stakeholders and to leverage the expertise and experience reflected in existing initiatives with a view to understanding how existing frameworks fit together, identifying overlaps and potential gaps so as to focus efforts. After evaluating the current sustainability reporting landscape and understanding existing challenges from current market participants, the SSB can identify where and how it can add value.

We are of the view that this undertaking will be most successful if the SSB can work closely with other organisations who have previously been involved in sustainability reporting standard setting and have developed expertise that will be relevant to the work of the SSB. To this end, it is important to consider work by organisations such as the Carbon Disclosure Project (CDP), Climate Disclosure Standards Board (CDSB), Global Reporting Initiative (GRI) the International Integrated Reporting Council (IIRC) and Sustainability Accounting Standards Board (SASB) who recently issued a statement of intent to work together towards a comprehensive corporate reporting system. The Task Force on Climate-related Financial Disclosures (TCFD) has proven to be a workable and widely accepted global framework to report on climate related risks and opportunities and should be considered for incorporation in any global standard setting effort on broader sustainability issues. Additionally, it is important to work with national, regional and international authorities who have established, or are in the process of developing, legislative, regulatory and prudential frameworks on sustainability reporting (for example, the European Commission, European Financial Reporting Group (EFRAG), European Banking Authority and ESMA in Europe along with the International Platform on Sustainable Finance, the World Economic Forum and International Organisation of Securities Commissions). Given the experience of the IFRS Foundation in working successfully with predecessor national accounting standard setters during the development of IFRS, we are confident that the experience of groups already active in developing ESG reporting can be included in the work of the SSB.

Question 6
How could the IFRS Foundation best build upon and work with the existing jurisdictional initiatives to find a global solution for consistent sustainability reporting?

One of the significant achievements of the IFRS Foundation in setting IFRS has been to engage and work with individual jurisdictions that have different accounting standards. In setting standards for sustainability reporting, it will be important for the IFRS Foundation to identify those jurisdictional initiatives which are already well established and have support and consider how it could assist in improving accuracy, comparability and credibility of existing initiatives. Please also refer to our response to Question 2.

Question 7
If the IFRS Foundation were to establish an SSB, should it initially develop climate-related financial disclosures before potentially broadening its remit into other areas of sustainability reporting?

There appears to be an immediate need for global standard for sustainability reporting. We agree that the SSB could in the first instance focus on climate-related disclosures and seek to consolidate the progress already made in this field by existing organisations, such as the TCFD. Since the development of climate related disclosures is already well progressed, we believe the SSB should bring together existing guidance rather than proliferate new standards. The SSB could in due course consider whether to establish a remit in other areas of ESG reporting where the standards are not presently so well progressed. By having a broader remit, the SSB will have the flexibility to identify best practice and in parallel refine climate-related disclosures. We maintain that for the IFRS Foundation's initiative to be successful it will need to properly engage in a scoping exercise to fully comprehend existing frameworks and future needs.

Question 8
Should an SSB have a focused definition of climate-related risks or consider broader environmental factors?

Our views in this area are nuanced. Whilst we believe there is merit in the SSB initially focusing on climate related risk, we would advise not preclude the SSB from also considering broader ESG topics either now or in future. Also, we encourage the SSB to work closely wherever possible with those organisations and regional authorities[3] that have already established climate disclosure standards, rather than for the SSB to develop new ones. Lastly, we are supportive of the SSB adopting existing definitions, including on climate risk.

Some of our members suggest the standards should include both qualitative and quantitative disclosure requirements and that these elements in combination are necessary to meet the objectives of providing transparency and encouraging the emergence of best practice. Other members believe these objectives can be best met by focusing only on quantitative disclosure.

Question 9
Do you agree with the proposed approach to materiality in paragraph 50 that could be taken by the SSB?

We understand that the SSB may propose not to initially commence with a double-materiality approach to setting sustainability standards given the potential increase in the complexity of the standards that this may bring. However, we also note that the financial community will at some point be asking for companies' information on their impacts on the environment and society in complementarity with information on how the environment and society can impact their financial health.

As such, we agree that the starting point for determining materiality should be by reference to the potential financial impact of the particular sustainability measure while also anticipating an increasing demand from the financial community which may necessitate the development of a double-materiality approach.

We acknowledge that there are mixed views in this area, and we suggest the IFRS Foundation should actively monitor developments in this area with a view to giving the question of double-materiality further consideration as early as appropriate.

Question 10
Should the sustainability information to be disclosed be auditable or subject to external assurance? If not, what different types of assurance would be acceptable for the information disclosed to be reliable and decision-useful?

Yes, we consider that the process by which third party assurance would be provided on sustainability measures is consistent with ensuring that users of ESG reporting have confidence in the completeness and accuracy of information disclosed in the financial statements.

The current model by which financial statements are subject to external audit provides a well understood and highly effective process which can be applied to provide confidence in sustainability reporting measures. However, we suggest that whilst the global sustainability standards are being developed and becoming established, we should start with a phased approach and limited assurance by third parties. This is because subjecting the sustainability

---

[3] For example, the European Commission, European Financial Reporting Group (EFRAG), European Banking Authority and ESMA in Europe along with the International Platform on Sustainable Finance, the World Economic Forum and International Organisation of Securities Commissions).

information to mandatory assurance too soon could be counterproductive and result in a narrow compliance-based approach to reporting which could stifle development in this area.

Lastly it remains crucial that disclosures are made at the parent entity level to avoid duplication of efforts by subsidiaries and, more importantly, to enable investors to take informative decisions related to their consolidated financial exposure.

Question 11
Stakeholders are welcome to raise any other comment or relevant matters for our consideration.

As noted above, we support the suggestion for the IFRS Foundation to take on the role of setting global standards for ESG accounting and reporting while leveraging the progress that regional authorities and international organisations have already made in this area. A key reason for our support is the success the IFRS Foundation has demonstrated in setting IFRS. However, our support presupposes that the IFRS Foundation's work in setting IFRS will continue at the same high standard as it does presently. We would not want the IFRS Foundation's work on IFRS to be compromised in any way by it taking on this new responsibility. IFRS is a body of guidance for which it is essential that it continues to evolve in response to changes in the economic and business environment in which it is applied, so the existing work of the IFRS Foundation in this area must be unaffected.

The IFRS Foundation has significant experience in developing IFRS and working with multiple national authorities around the world to secure the endorsement of its standards and make their use mandatory. This experience will be invaluable as an essential part of the SSB's role will be to ensure that its standards become part of the mandatory framework of external reporting that organisations must comply with. To help achieve this, the IFRS Foundation must provide a very high level of transparency for its progress in developing standards and securing support for them in the many jurisdictions in which it will operate.

In addition, we encourage the IFRS Foundation to act quickly to establish the SSB, define its governance involving co-operation with international organisations and regional competent authorities, secure its mandate and start the important work towards harmonisation of developing global sustainability standards in a way that is articulated with the current initiatives undertaken in certain jurisdiction, notably via the international platform on sustainable finance. We are concerned that unless there is a strong sense of urgency attached to this initiative, it could be many years before sustainability reporting standards are finalised and available for use. This would be a great shame as there is already a need for clarity in the field of ESG reporting, which needs to be addressed as a priority.

In June 2020, ISDA in conjunction with AFME responded to the European Commission's consultation on the revision of the EU Non-Financial Reporting Directive[4] where we provided further insights that we trust could be helpful to the IFRS Foundation in deciding a way forward on taking a role in the establishment of global sustainability reporting standards.

---

[4] https://www.afme.eu/Portals/0/DispatchFeaturedImages/AFME%20ISDA%20NFRD%20revision%20consultation%20response_Final_11062020.pdf