Accelerating pace of mandatory ESG reporting

Financial Reporting Webinar Series

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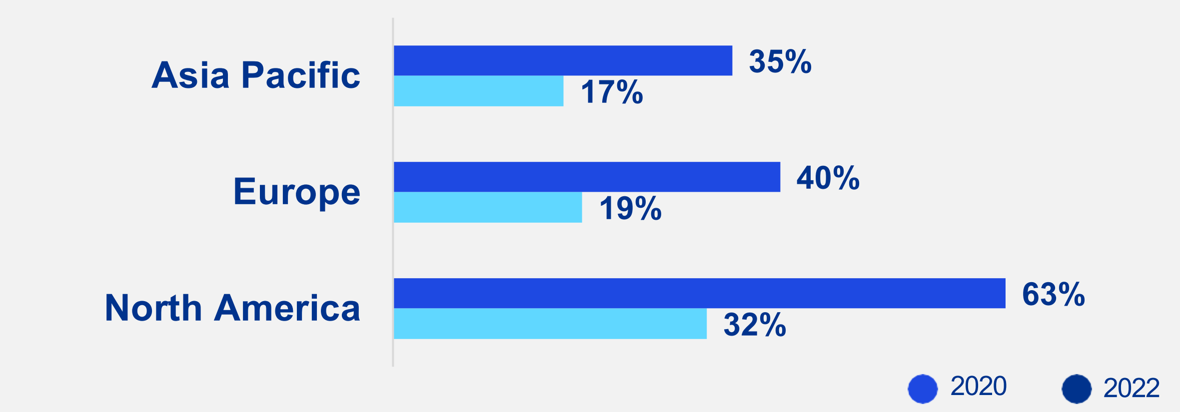
Thursday 17 November 2022

Marked increase in TCFD adoption

TCFD adoption:

	2020	2022
G250	37%	61%
China	8%	20%

TCFD adoption by N100 companies in selected regions (2020 – 2022)



Significant growth seen in:

	2020	2022
Japan	47%	94%
South Korea	3%	54%
UK	34%	86%
US	28%	64%

Remark: N100 refers to the worldwide sample of the top 100 companies by revenue in each of the 58 countries, territories and jurisdictions reviewed in the survey. G250 refers to the world's 250 largest companies by revenue based on the 2021 Fortune 500 ranking

Base: 4,100 N100 companies and 250 G250 companies

Source: KPMG Survey of Sustainability Reporting 2022, KPMG International, September 2022

ISSB Comment letter feedback summary

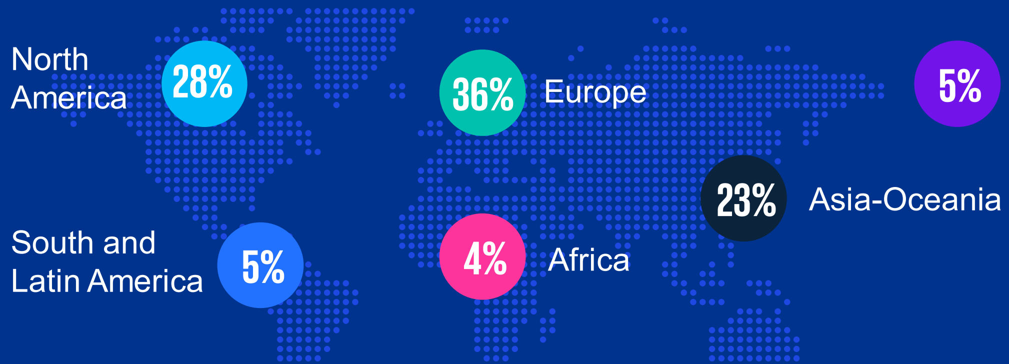
1,435

Comment letters and survey responses

Almost all Respondents supported:[1]

- Building on the TCFD framework
- Creating a global baseline
- Achieving interoperability with US and EU requirements

Engagement from across the globe



42% from preparers

13% From users

45% From others[2]

1. This slide summarises the ISSB's own analysis of feedback received. 'Almost all' is defined as 'all except a very small minority'. Interoperability with EFRAG and SEC proposals was highlighted as important by almost all European and US respondents respectively.
2. Including public interest groups, accountants and academics, standard sellers, regulators and policy-makers.
3. The ISSB added this topic to its plan in the October 2022 meeting.

Action list

Key areas chosen for redeliberation

GENERAL REQUIREMENTS

- ✓ **Scope and breadth of reporting** - Five topics including application of materiality, value chain reporting, and the meaning of terms including 'enterprise value' and 'significant'
- ✓ **Connected information** between topics and with the financial statements, plus IASB collaboration
- ✓ **Frequency of reporting** including location requirements
- ✓ **Updating estimates** in comparative information[3]

CLIMATE

- ✓ Disclosures on **strategy, decision making, and transition plans and targets**
- ✓ **Climate resilience and scenario analysis**
- ✓ **GHG emissions**, particularly Scope 3 and measurement methods
- ✓ **Industry-based topics**, including financed and facilitated emissions

CROSS CUTTING

- ✓ **Interoperability** of the standards for all types of global company
- ✓ **Financial effects** of sustainability- and climate-related risks and opportunities

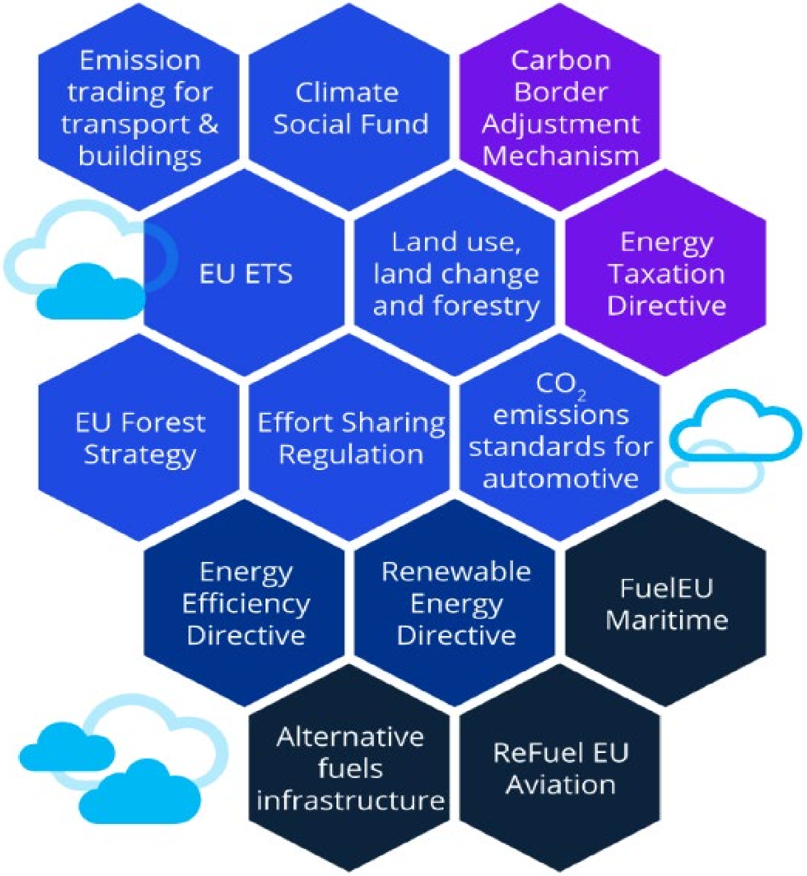
EU Green Deal – Fit for 55

General action plan to fight climate change.

Preparatory path to meet the targets of the EU Green Deal.

Milestone target: Reduce greenhouse gas emissions by **55% by 2030.**

Fit-for-55 package



Fit for 55 objectives include:

- Tightening and expansion of ETS and prevention of carbon leakage
- Alignment of taxation policies with European Green Deal
- Increased use of renewable energy
- Faster rollout of low emission transport modes
- Decarbonization with a social dimension

How does CBAM work?

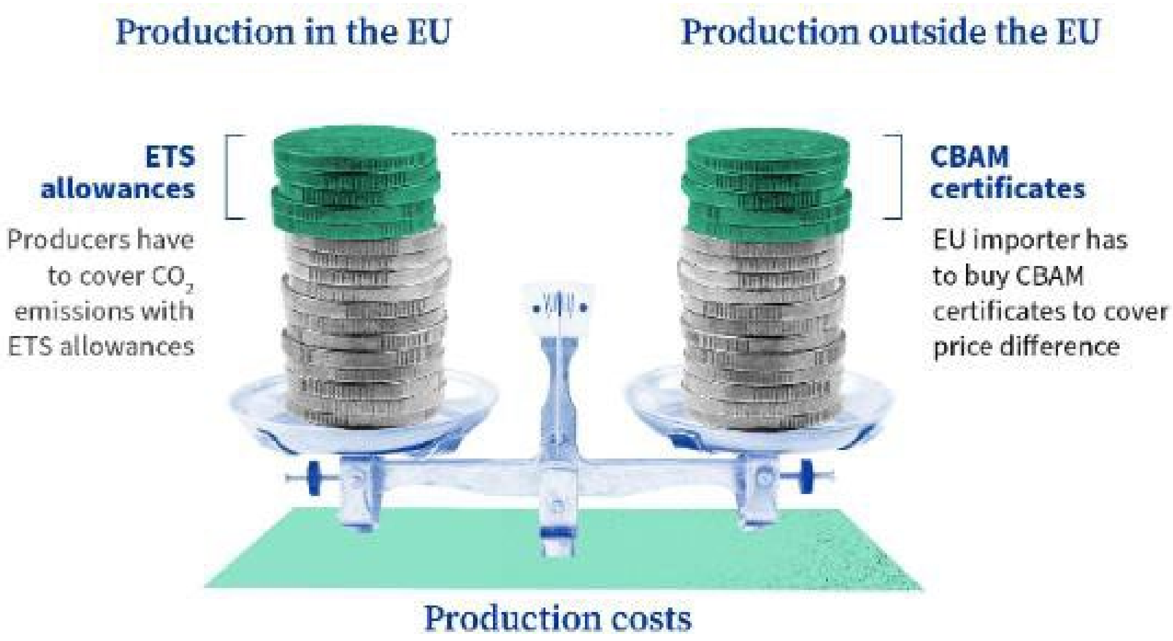
Establishes a Carbon Border Adjustment Mechanism for regulating greenhouse gas emissions embedded in certain goods*:

Electricity | **Iron and steel** | **Cement** | **Aluminium** | **Fertilisers**

upon their importation into the customs territory of the European Union, with the purpose of preventing the risk of carbon leakage.

***possible** inclusion of polymers, organic chemicals, hydrogen, ammonia in the first phase.*

- CBAM operates by imposing a charge on the embedded carbon content of certain imports into the EU that is equal to the charge imposed on domestic goods under the EU ETS.
- Adjustments are made to this charge to take into account any mandatory carbon prices paid in the exporting country recognised by the EU
- Equivalent carbon price on imports creates level playing field for EU producers and EU importers.



Source: https://www.consilium.europa.eu/en/infographics/fit-for-55-cbam-carbon-border-adjustment-mechanism/

Trends and Value Proposition

EU CBAM signals the trends…

Once the EU introduces CBAM, the other jurisdictions would try to or have to do the same.

CBAM may become a globally universal compliance carbon pricing (tax) system.

Carbon will become assets and liabilities of any business.

MRV, i.e., Monitoring (“book keeping”), Reporting, and Verification (“audit”), will become a fundamental system for businesses.

The value proposition of decarbonisation

Carbon emission reduction is not just for branding but also **price advantage and market share**.

Baseline assessment and MRV set-up is key. This is not just strategy, but also day-to-day operation.

It may be best time ever to **introduce low-carbon projects** – green technology, green investments, green finance, etc.

Need for Actions – Baseline Assessment and Decarbonisation

What are the products potentially subject to CBAM? Reviewing the CN/HS/customs codes (customs) and the supply chain is key.

Assess the financial impacts and the business impacts (such as how much carbon tax can be passed on to customers), and consider them a potential carbon liability or even asset of the organization.

1. **Identify In-scope Products and Vendors**
2. **Analyse Product Carbon Footprint**
3. **Assess the CBAM Financial Impacts**
4. **Provide Impact Mitigation Suggestions**

Is MRV (Monitoring, Reporting and Verification) a well-established system readily there for CBAM? How will you company assess Product Carbon Footprint?

Identify and analyse the existing emissions reduction opportunities of the organisation as well as the value chain.

A new regulatory wave is coming

TODAY

EU-Taxonomy[1]

- Disclosure of **3 financial KPIs** (Sales, CapEx and OpEx) **classified based on sustainability criteria** e.g. for Climate Change Mitigation with respective narratives
- **Part of non-financial statement**
- (Voluntary) Limited/Reasonable Assurance

2024

CSRD

Corporate Sustainability Reporting Directive[2]

- Expecting **>100 non-financial KPIs** and additional qualitative disclosures based on new binding Sustainability Reporting standards
- Reporting as **part of the management report**
- **Mandatory Limited Assurance** required from the beginning with intent to move to reasonable assurance.

[1]EU Taxonomy Regulation (EU) 2020/852
[2]Proposal of the Corporate Sustainability Reporting Directive as of 21st June 2022

The “topical” and two cross-cutting standards released

Topical standards

Environmental[1]

- Climate change
- Pollution
- Water and marine resources
- Biodiversity
- Resource use and circular economy

Social

- Own workforce
- Workers in the value chain
- Affected communities
- Consumers/end-users

Governance[2]

- Business conduct

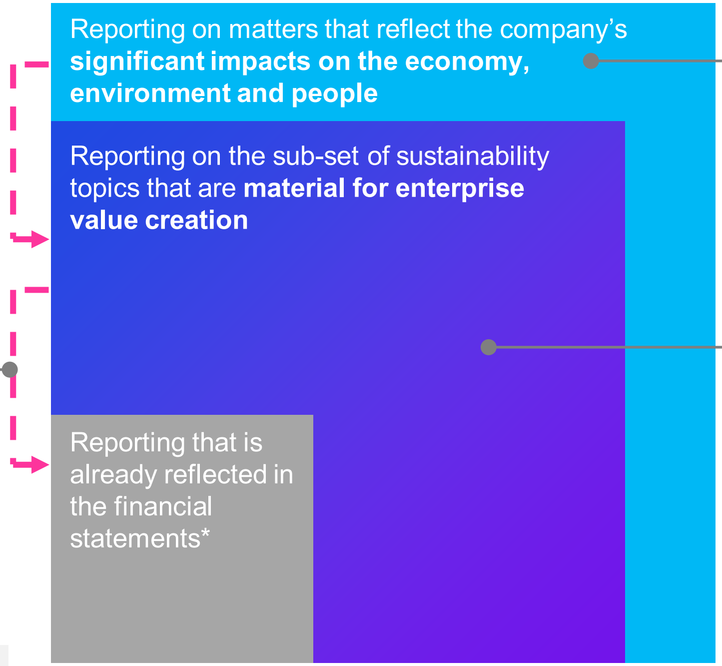
2 Cross cutting standards – general requirements and general disclosures

Sector specific standards expected to be issued 2023-2025 by batches

1 Environmental sub topics follow the 6 objectives of the EU taxonomy
2. This differs from the reporting of the governance of a specific sustainability topic

Materiality

The needs of users of sustainability reporting information may differ. Materiality provides the filter that helps companies focus on what matters to users.



*Including assumptions and cash flow projections

Dynamic materiality

Sustainability topics can move – either gradually or very quickly

Wider stakeholder lens (EFRAG only)

To various users with various objectives who want to understand the company's positive and negative contributions to sustainable development

Investor lens (all three proposals)

Specifically to the sub-set of those users whose primary objective is to improve economic decisions

Adapted from: Statement of Intent to Work Together Towards Comprehensive Corporate Reporting, Summary of alignment discussions among leading sustainability and integrated reporting organisations CDP, CDSB, GRI, IIRC and SASB, Sept 2020; Figure 1, Dynamic materiality

Double materiality

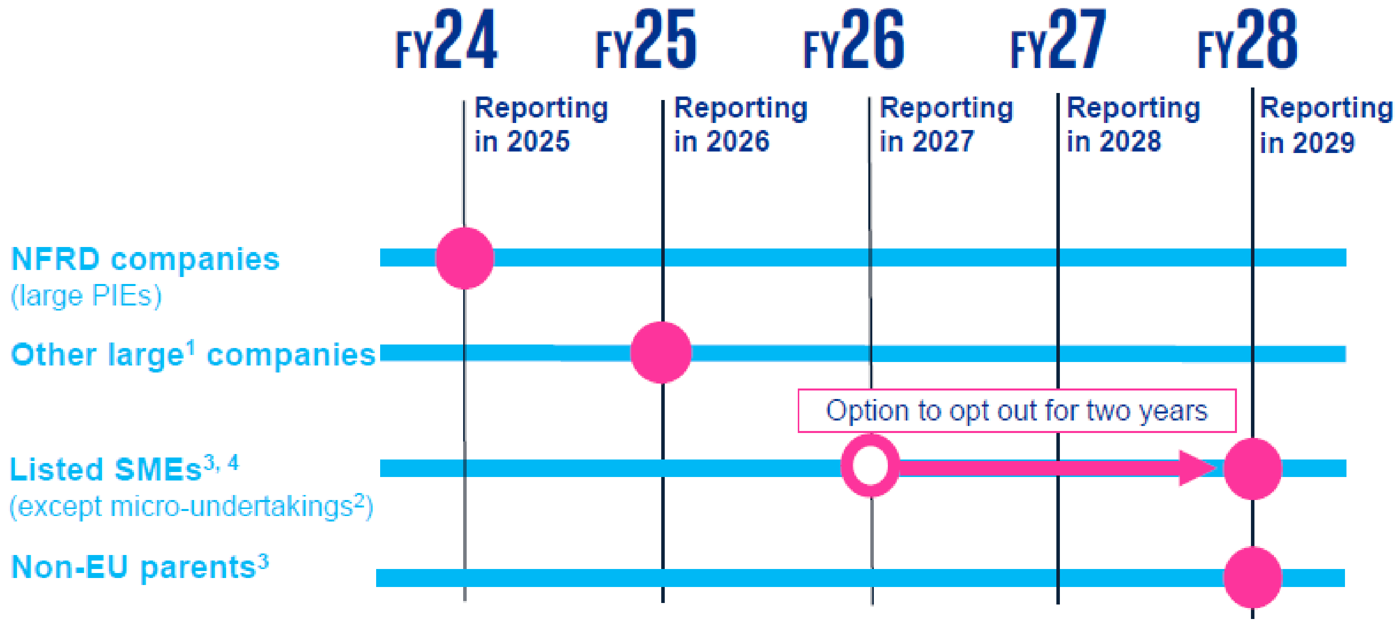
EFRAG adopts 'double materiality' principles – aiming to report on all significant impacts by considering both the investor and wider stakeholder lenses.

When, and to whom, would the ESRSs apply?

When: The ESRSs would apply for years beginning on/after 1 January 2024 (reporting in 2025). Phased introduction would start with companies already subject to reporting requirements under the NFRD (i.e. large PIEs).

Who: Ultimately, ESRSs would be applied by (group exemptions apply):

- large EU companies[1];
- listed EU companies (except micro-undertakings[2]); and
- Ultimate non-EU parent companies[3] with a combined group turnover in the EU of more than EUR 150 million.



[1] Large companies are those that exceed on the balance sheet date two of the following three criteria (including subsidiaries): 250 employees, net revenue of EUR 40m or total assets of EUR 20m.

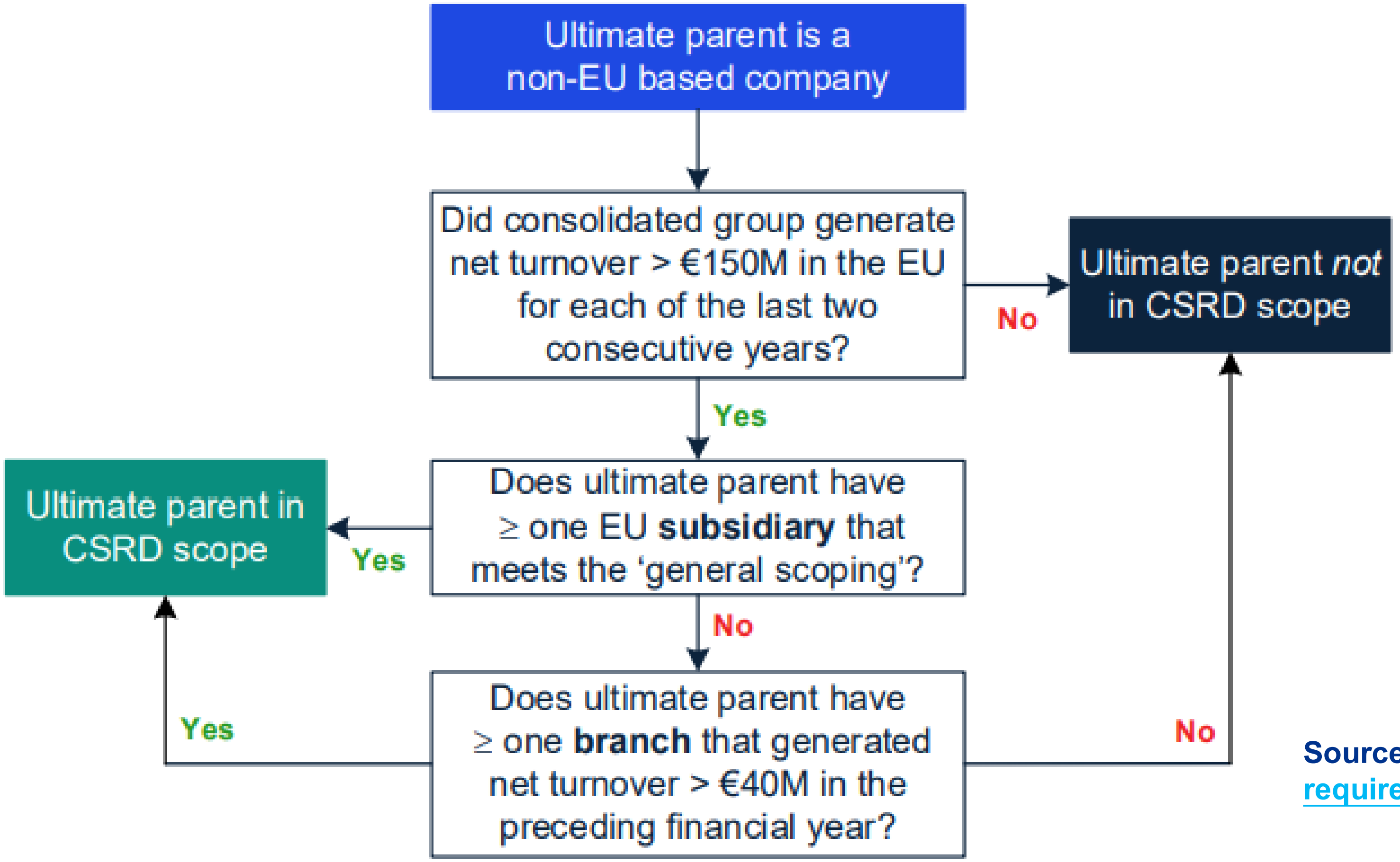
[2] Micro-undertakings are companies that do not exceed two of the following three criteria (including subsidiaries): 10 employees, net revenue of EUR 700,000 or total assets of EUR 350,000.

[3] Separate standards will be developed for SMEs and non-EU parent companies (to be adopted by 30 June 2024).

[4] Small and non-complex institutions and captive insurers are treated like listed SMEs (opt-out option until 2028 does not apply unless they also meet the definition of SME).

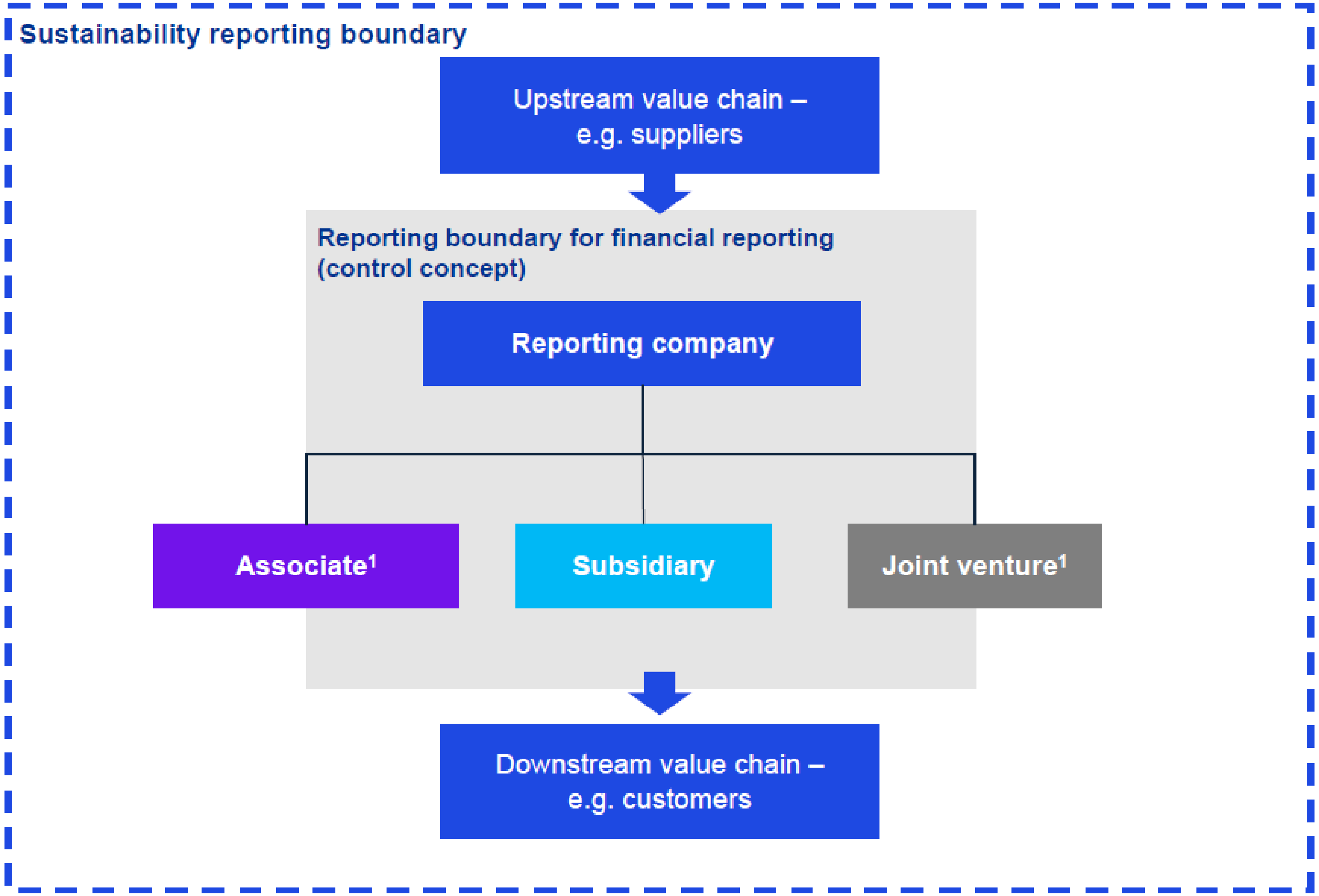
The ESRSs are due for finalisation by June 2023. They would apply for certain companies in years beginning on or after 1 January 2024.

ESRS Scoping decision tree of non-EU parent scoping



Source: [US company impact of EU ESG reporting requirements (kpmg.us)]

What reporting boundaries would you consider?



Reporting boundary for sustainability reporting

The reporting boundaries would be based on the financial statements but expanded for the upstream and downstream value chain.

The reporting boundary would be expanded to cover material sustainability matters that are connected to the company by its direct or indirect business relationships regardless of its level of control over them.

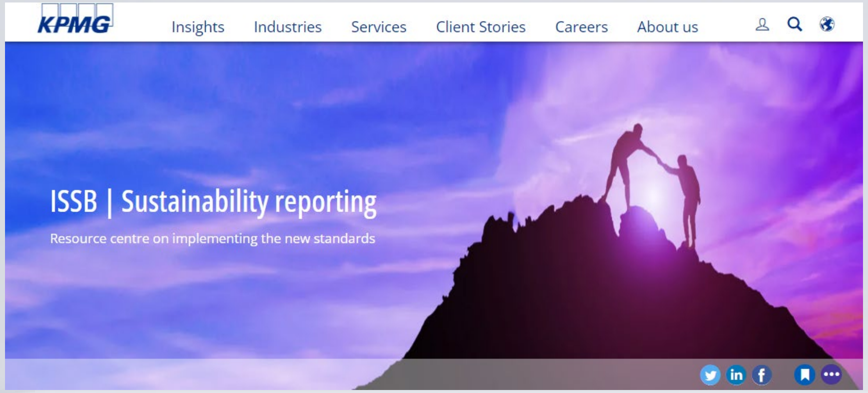
If collecting data is impracticable, then a company would use approximate data using all reasonable and supportable information.

A company would revise the reporting boundary regularly to ensure its appropriateness over time.

[1] Equity investments and joint ventures form part of the upstream or downstream value chain. For financial reporting, they are only partially included under the equity method and are based on the investor's share of control.

Resources

Website:
[ISSB | Sustainability reporting - KPMG Global (home.kpmg)]



Big shifts, small steps
Survey of Sustainability Reporting 2022

Webinar dates and topics for 2022

- 26 January – HKEX Listing Rules Update
- 18 March – IFRS Sustainability Standards – The climate-related and general disclosure prototypes
- 20 May – Get ready for 2022 Interim Reporting season
- 10 June – Closing the gap between climate risk and climate strategy
- 15 July – Crypto-assets – tax and financial reporting considerations
- 7 October – Valuation challenges in the current environment
- **18 November – Accelerating pace of mandatory ESG reporting**
- **14 December – Year-end reporting reminders**

For more details and access to our webinar series:

https://home.kpmg/cn/en/home/services/audit/ifrs-news/financial-reporting-webinar-series.html

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