



# Counting Carbon Molecules

The New IFRS Sustainability Disclosure Standard and Why Canadian Hydrocarbon Companies Must Respond to Consultations Now

## EXECUTIVE SUMMARY

- At every level of government, the Canadian bureaucracy is deeply committed to meeting its 2030 Net-Zero goals at all costs and as such is set to adopt the forthcoming IFRS Sustainability Disclosure Standard which is currently in draft format and open for feedback.
- The IFRS Sustainability Disclosure Standard consists of the following draft documents: *IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information*, *IFRS S2 Climate-related Disclosures*, and *S2 Appendix B Industry-based Disclosure Requirements*.
- The stated purpose of creating a new global baseline for sustainability and climate-related disclosure is to fight “greenwashing” by bringing sustainability into all accounting, thus the whole economy.
- Underwritten by the principles of stakeholder capitalism, and championed by the Big Four accounting firms, the proposed standards are purported to be: simple, applicable to every entity, in line with the UN’s Sustainable Development Goals, and legally enforceable. The goal is accuracy, verifiability, and comparability, creating a single gauge by which consumers, investors, insurers, bond holders, lenders, and others can compare entities and hold them accountable for their carbon-behaviour.
- There are four areas that comprise the core content of this new disclosure standard: governance, strategy, risk management, and metrics and targets. There are several issues within each of these areas, especially for hydrocarbon companies, for example:
  1. They demand that duplication be avoided yet insist, at times, that other standards and requirements be considered.
  2. There are contradictory statements, mixed messages, and vague terms.
  3. There are serious problems with mandating scenario analysis such as its evolving applicability to climate as well as cost.
  4. By insisting on the disclosure of **all gross** Scope 1, Scope 2, and Scope 3 emissions any industries that manufacture any kind of product, or produce, handle, or utilize hydrocarbons in any way are targeted and likely penalized. Scope 3 emissions reporting is not only notoriously difficult to quantify it also leads to a duplication in accounting such that emissions are counted several times over and are not an accurate representation of climate-risk.

5. Entities could be made financially liable for any perceived misstatement on emissions, future scenarios, future global developments and future weather events, the behaviours and actions of those who use an entity's products, and reputational damage from "controversies."
  6. By focusing on gross carbon emissions and emissions intensity, and offering no place to quantitatively account for net emissions, the standards preclude the possibility that a company employs technology that actually reduces its carbon emissions, and discriminate against companies that have more emissions than others.
  7. Under risk assessment, hydrocarbon companies must estimate and account for the cost of early asset retirement under varying policy scenarios. There is no specific provision for asset end-of-life/retirement/disposal calculations for solar, wind, or battery technology manufacturers or project developers.
  8. Given recent geopolitical developments with respect to the Russian invasion of Ukraine and the subsequent sanctions against Russian oil and natural gas, energy security is a stunning omission within the draft disclosures.
- The deadline for submitting feedback on drafts of the IFRS Sustainability Disclosure Standard is July 29, 2022 and all feedback is being published on the IFRS website for public viewing.
  - Once the IFRS Sustainability Disclosure Standard is enforceable, the finances and operations of hydrocarbon companies, and any industry that utilizes hydrocarbons, will be seriously compromised to the point of extinction.
  - Every Canadian hydrocarbon company should respond to and provide feedback on the drafts by the deadline.

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# THE NEW IFRS SUSTAINABILITY DISCLOSURE STANDARD

AND WHY CANADIAN HYDROCARBON COMPANIES MUST RESPOND NOW

## INTRODUCTION

*[The IFRS global baseline] is one of the most important innovations in accounting since almost the 14<sup>th</sup> century.*

Ramya Krishnaswamy, WEF Annual Meeting 2022

Canada has committed to adopting the International Financial Reporting Standards (IFRS) new Sustainability Disclosure Standard for sustainability-related disclosures (IFRS S1) and climate-related disclosures (IFRS S2). It has begun by mandating Task Force on Climate-Related Financial Disclosures (TCFD) requirements for banks, and with the granting of an International Sustainability Standards Board (ISSB) office in Montreal, it is expected that the IFRS Sustainability Disclosure Standard will become mandatory in the very near future. As currently written, since the standards demonize greenhouse gas emissions through the accounting standards' metrics, the finances and operations of hydrocarbon companies, and any industry that utilizes hydrocarbons, will be compromised. Canada's Accountability Standards Board is encouraging Canadian entities to participate in the ISSB commentary period, especially financial institutions, insurers, and investors. The window for feedback, an opportunity for individuals and companies to comment on the draft documents, is open now and closes on 29 July 2022. This is the moment to evince real change in how the entire Canadian industry is measured and ranked.

## I. BACKGROUND

The IFRS was created in 2001 to help develop global reporting standards to enable transparent and comparable information across jurisdictions. The International Accounting Standards Board (IASB) develops the accounting standards for the IFRS, and these are used in 140 jurisdictions around the world including Canada. The IFRS has now been tasked with developing a set of accounting-based metrics for sustainability and climate-related financial disclosures that will become a global baseline and essentially replace the many varied current Environmental, Social, Governance (ESG) reporting.

At the G7 meeting in June 2021, Canada and the rest of the G7 supported the movement towards a mandatory global baseline for climate-related disclosures based on the TCFD standards through the creation of the ISSB at the IFRS.<sup>1</sup> In November 2021, at COP 26 in Glasgow, the new organization called the [International Sustainability Standards Board](https://www.g7uk.org/g7-finance-ministers-and-central-bank-governors-communique/) was indeed established within the IFRS by merging the Sustainability Accounting Standards Board, the Climate

<sup>1</sup> G7 Finance Ministers, *G7 Finance Ministers and Central Bank Governors' Communiqué* - G7 UK Presidency 2021, 5 June 2021, <https://www.g7uk.org/g7-finance-ministers-and-central-bank-governors-communique/>, [accessed 29 May 2020]

Disclosure Standards Board and the International Integrated Reporting Council.<sup>2</sup> When this new standards board issues its final requirements, “they will form a comprehensive global baseline of sustainability disclosures.”<sup>3</sup> What sets these standards apart from current ESG iterations is that they will be taken into account for financial accounting purposes and be held to a legally accountable status under terms of financial compliance. The intent is ostensibly to prevent “greenwashing,” misleading ESG claims, or fraud by holding companies to account for misstatements or material gaps in their detailed sustainability and climate-related disclosures.

In early 2022, two prototype global standards were put forward, developed by the Climate Disclosure Standards Board, the International Financial Reporting Standards Foundation, TCFD, Value Reporting Foundation, and the World Economic Forum: [Climate-related Disclosures Prototype](#); and [General Requirements for Disclosure of Sustainability-related Financial Information Prototype](#).<sup>4</sup> As Brian Moynihan, CEO of Bank of America, explained at the World Economic Forum annual meeting in Davos in May 2022, “We started this because of the proliferation of metrics, and disparities, with no real regulation on who could be a standard setter. Got the Big Four [accounting firms] to get together and align standards to the SDGs [UN Sustainable Development Goals].”<sup>5</sup> Thus, with the assistance of the Big Four accounting firms, these have now been refined and were released for comment at the end of March 2022 as the IFRS Sustainability Disclosure Standard in three documents: Exposure Draft IFRS S1 [General Requirements for Disclosure of Sustainability-related Financial Information](#), and the Exposure Draft IFRS S2 [Climate-related Disclosures](#), and [Appendix B Industry-based Disclosure Requirements](#).<sup>6</sup>

Although each country and jurisdiction may set its own standards<sup>7</sup> or modify certain elements of the IFRS proposed standards, some observers suggest that in the very near future, the Canadian

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<sup>2</sup>International Financial Reporting Standards Foundation, IFRS – ISSB, Frequently Asked Questions, <https://www.ifrs.org/groups/international-sustainability-standards-board/issb-frequently-asked-questions/>, [last accessed, 27 May 2022].

<sup>3</sup>International Financial Reporting Standards Foundation, “ISSB Delivers Proposals that Create Comprehensive Global Baseline of Sustainability Disclosures”, 31 March 2022, <https://www.ifrs.org/news-and-events/news/2022/03/issb-delivers-proposals-that-create-comprehensive-global-baseline-of-sustainability-disclosures/>, [accessed, 27 May 2022].

<sup>4</sup>IFRS, *Climate-related Disclosures Prototype*, November 2021, <https://www.ifrs.org/content/dam/ifrs/groups/trwg/trwg-climate-related-disclosures-prototype.pdf>, [accessed, 24 May 2022]; *General Requirements for Disclosure of Sustainability-related Financial Information Prototype*, November 2021, <https://www.ifrs.org/content/dam/ifrs/groups/trwg/trwg-general-requirements-prototype.pdf>, [accessed, 24 May 2022].

<sup>5</sup>World Economic Forum, Annual Meeting 2022, 25 May 2022, Global ESG Standards: Are We There Yet?, Ramya Krishnaswamy, (Moderator), Brian T. Moynihan (CEO, Bank of America), Emmanuel Faber (Chair, IFRS), Gillian R. Tett (Financial Times), <https://www.weforum.org/events/world-economic-forum-annual-meeting-2022/sessions/global-esg-standards-are-we-there-yet>, [accessed 31 May 2022].

<sup>6</sup>IFRS, *S1 Exposure Draft, General Requirements for Disclosure of Sustainability-related Financial Information*, March 2022, <https://www.ifrs.org/content/dam/ifrs/project/general-sustainability-related-disclosures/exposure-draft-ifrs-s1-general-requirements-for-disclosure-of-sustainability-related-financial-information.pdf>, [accessed, 27 May 2022]; *S2 Exposure Draft Climate-related Disclosures*, March 2022, <https://www.ifrs.org/content/dam/ifrs/project/climate-related-disclosures/issb-exposure-draft-2022-2-climate-related-disclosures.pdf>, [accessed, 27 May 2022]; *Appendix B Industry-based Disclosure Requirements*, March 2022, <https://www.ifrs.org/content/dam/ifrs/project/climate-related-disclosures/issb-exposure-draft-2022-2-appendix-b.pdf>, [accessed, 27 May 2022].

<sup>7</sup>The United States Security Exchange Commission (SEC) issued in parallel a similar set of draft standards for ESG specific funds – “We are proposing to require a fund engaging in ESG investing to provide additional information about the fund’s implementation of ESG factors in the fund’s principal investment strategies.” See, United States Security Exchange Commission, Proposed Rule, *Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices*, <https://www.sec.gov/rules/proposed/2022/ia-6034.pdf>. Of concern is that these standards will eventually be applied to all investments. The SEC is also developing initiatives “to proactively identify ESG-related misconduct...[and] any material gaps or misstatements in issuers’ disclosure of climate risks under existing rules.” SEC, <https://www.sec.gov/news/press-release/2021-42>. In an interview on the launch of the IFRS draft disclosures, ISSB chair Emmanuel Faber told a Bloomberg Live interviewer that even though it was unlikely the US would adopt them, the proposed global baseline standards were designed to be “supplemental, complementary, and compatible with [SEC] rulings.” Bloomberg Live, “ISSB Chair on New Sustainability Disclosure Standards,” 31 March 2022, <https://m.youtube.com/watch?v=Klw1LWRz1IU>. Although the SEC rules are of grave concern for ESG funds, it is beyond the scope of this report which is focused on the broader changes being proposed by the ISSB.



Standards Agency (CSA) “will impose for the first-time mandatory climate related disclosure and sustainability financial reporting requirements on all of Canada’s public reporting companies in their core disclosure documents.”<sup>8</sup> In addition, Canada recently held a consultation period on the concept of establishing a Canadian Sustainability Standards Board that will liaise with the ISSB to ensure alignment with the new global baseline.<sup>9</sup>

The G7 recently reiterated its support and endorsement of the ISSB global baseline: “We encourage countries to prepare or continue to prepare the ground for usage of the baseline.”<sup>10</sup> It is highly likely that the IFRS standards will be adopted by Canada as part of a new global standard intended to be the basis of proposed global mandatory sustainability reporting for all sizes of businesses—small, medium, and large—from mom-and-pop operations to multinational corporations.<sup>11</sup> As the G7 communiqué stated, “The baseline should be practical, flexible and proportionate and ultimately suitable for small and medium-size enterprises and enable jurisdictions to implement the baseline and a more extensive approach to supplement the baseline.”<sup>12</sup> Brian Moynihan, at the WEF 2022, was very clear on the intent of these standards:

*It’s got to apply to the WHOLE economy, otherwise the issue will be the activities can migrate away. ...Once you bring it into accounting, all companies have to do it, there’s no debate. One, simplicity; two, all companies; three, SDGs; four, compliance—so nobody could hide from it. It becomes the thing. That gives investors, consumers, bond holders a consistent way to see across companies. The bar, if which you’re below, people shouldn’t invest in, they shouldn’t be lent to.*<sup>13</sup>

The current draft Sustainability Disclosure Standard is open for comment until 29 July 2022. The S1, S2, and Appendix B draft standards, covering 68 different industries, need further analysis to understand the implications not only for the Canadian hydrocarbon industry but for the Canadian economy as a whole.

## II. DRAFT DISCLOSURES

### A. EXPOSURE DRAFT IFRS S1 GENERAL REQUIREMENTS FOR SUSTAINABILITY-RELATED FINANCIAL DISCLOSURES (IFRS S1)

<sup>8</sup> “The ISSB: a game changer for ESG reporting?” *Financier Worldwide*, May 2022, <https://www.financierworldwide.com/the-issb-a-game-changer-for-esg-reporting>, [accessed 27 May 2022].

<sup>9</sup> Independent Review Committee on Standard Setting in Canada, “Consultation Paper – Independent Review Committee on Standard Setting in Canada,” <https://www.ircsscanada.ca/en/consultation-paper>, [accessed 20 May 2022].

<sup>10</sup> US Department of the Treasury, Group of Seven (G7), *G7 Finance Ministers and Central Bank Governors Meeting Communiqué*, Petersberg, Germany, 20 May 2022, <https://home.treasury.gov/news/press-releases/jy0797>, [accessed 23 May 2022].

<sup>11</sup> Michael Cohn, “G7 prods ISSB to tackle more than climate standards,” *Accounting Today*, 20 May 2022, <https://www.accountingtoday.com/news/g7-prods-issb-to-tackle-more-than-climate-standards>, [accessed 21 May 2022].

<sup>12</sup> US Department of the Treasury, Group of Seven (G7), *G7 Finance Ministers and Central Bank Governors Meeting Communiqué*, Petersberg, Germany, 20 May 2022, <https://home.treasury.gov/news/press-releases/jy0797>, [accessed 23 May 2022].

<sup>13</sup> World Economic Forum, Annual Meeting 2022, 25 May 2022, Global ESG Standards: Are We There Yet?, Ramya Krishnaswamy, (Moderator), Brian T. Moynihan (CEO, Bank of America), Emmanuel Faber (Chair, IFRS), Gillian R. Tett (Financial Times), <https://www.weforum.org/events/world-economic-forum-annual-meeting-2022/sessions/global-esg-standards-are-we-there-yet>, [accessed 31 May 2022]. This point, that it is a whole economy transformation, was also made by John Graham, President of the Canada Pension Plan Investment Board, “this is not just about transitioning from fossil fuels to renewables it’s about transitioning the entire global economy even in hard to abate sectors.” World Economic Forum, Annual Meeting, 2022, 24 May 2022, Shaping the Future of Investing, Alessandra Galloni. (Editor-in-Chief, Thomson Reuters), Nikhil Kamath (Zerodha Broking), John Graham (President, CEO, Canada Pension Plan Investment Board), Lynn Martin (President, NYSE Group Inc.), Kai-Fu Lee (Chairman and CEO, Sinovation Management Limited), <https://www.youtube.com/watch?v=s33c5in9HQU>, [accessed 2 June 2022].

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## a) OBJECTIVE AND SCOPE

IFRS S1 opens with sections on the objective and scope of the disclosure standard. The stated objective is to require useful information about significant “sustainability-related risks and opportunities” that can assist in assessing enterprise value for those seeking to provide resources (lenders, insurers, investors) to an entity. The information must be complete, “neutral,” and accurate. It clarifies that even though the information must be disclosed along with its general purpose financial reporting, it will be broader than information normally reported in financial statements.<sup>14</sup> Examples of broader information include, governance and strategy for addressing sustainability-risks and opportunities; decisions that could result in “future inflows and outflows that have not yet met the criteria for recognition in its related financial statements”; actions taken that have affected its reputation and impacts on relationships “with people, the planet, and the economy”; and development of knowledge-based assets.<sup>15</sup>

The scope of the Standard covers entities that use IFRS Accounting Standards or other Generally Accepted Accounting Principles (GAAP). Although the accompanying questions for comment state that the intent is to ensure all information is disclosed, a subjective qualifier stipulates that “sustainability-related risks and opportunities that cannot reasonably be expected to affect assessments of an entity’s enterprise value by primary users of general purpose financial reporting are outside the scope of this [draft] Standard.” What that means precisely, and how that will be decided, is unclear.

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## b) CORE CONTENT

There are four areas that comprise the core content: governance, strategy, risk management, and metrics and targets.

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### i. GOVERNANCE

The main purpose of this section is to identify which individuals or body within a company are responsible for the oversight of sustainability and climate-related risks and opportunities. Details on the responsibilities, skills, competencies, frequency of audit or risk advice, how the individuals or bodies oversee strategy and risk management and monitor progress, and whether or not salaries are tied to progress. The role of management in assessing and managing these issues is expected to be explained in detail.<sup>16</sup>

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### ii. STRATEGY

The objective of this reporting area is to require detailed information—quantitative and qualitative—on an entity’s comprehensive strategy for dealing with sustainability-related risks and opportunities. Most of the information requested, however, deals with risks rather than opportunities. Required disclosure ranges from risks to: business models and value chains; strategy and decision-making; cash flows, access to finance, and costs of capital and how the financial position will change over the short, medium or long-term; and an explanation of the

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<sup>14</sup> IFRS, S1 *Sustainability-related Disclosures*, 36, para. 72.

<sup>15</sup> IFRS, S1 *Sustainability-related Disclosures*, 22-23, para.6.

<sup>16</sup> IFRS, S1 *Sustainability-related Disclosures*, 24, para.12-13.



resilience of its strategy to “significant sustainability-related risks.”<sup>17</sup> Progress on plans identified in previous reporting periods shall be disclosed. Despite being touted as the global standard, the one-stop shop for reporting, in identifying risks and opportunities entities are told to consider not only the IFRS Sustainability Disclosure Standard but also disclosure topics in the SASB standards, the CDSB framework, “the most recent pronouncements of other standard-setting bodies,” and other standards identified by those operating “in the same industries or geographies.”<sup>18</sup> This is a vague and sweeping qualifier that leaves companies vulnerable to accusations that the correct standards were not applied. A company is also required to explain how resilient its strategy and cash flow will be so as to demonstrate its capacity to adjust to uncertainties. The type of information required to explain resilience was not provided in this draft. Instead, it was stated other IFRS Sustainability Disclosure Standards will specify what is required at some point in the future.<sup>19</sup> As Alan Jope said at the WEF 2022, “We are in danger of letting perfect get in the way of good, of letting complex get in [the] way of simple and of letting local get in the way of global.”<sup>20</sup> The draft Standard does indeed seem rushed and far from good, not just far from perfect.

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### iii. RISK MANAGEMENT

This section requires information on the processes a company uses to identify, assess, and manage sustainability risks and opportunities, and how those processes are integrated into overall risk management. The stated objective is to obtain information “to evaluate the entity’s overall risk profile and risk management processes.”<sup>21</sup> To that end, a company is required to disclose in detail how it assesses risks and opportunities, how it prioritizes sustainability-related risks relative to other risks, the input parameters it uses, if processes have changed from prior reports, and the extent to which these approaches are integrated into the overall management process.

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### iv. METRICS AND TARGETS

The objective of this section is to quantify sustainability-related risks and opportunities—how these are measured, monitored, and managed—so that users can understand how performance is measured and if progress towards set targets is being made. The metrics are specified as those contained in the IFRS S2 *Climate-related Disclosures*, Appendix B *Industry Specific Standards*, and other relevant or applicable standards including metrics developed internally by an entity. To be specified, and consistent over time, are: the definition and calculation of the metrics used, the applicable target period, the base period for progress to be measured, any interim targets or milestones, analysis of trends or significant changes in its performance towards the disclosed targets, and revisions to targets and explanation for those revisions.<sup>22</sup>

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## c) GENERAL FEATURES

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<sup>17</sup> IFRS, S1 *Sustainability-related Disclosures*, 25, para.15.

<sup>18</sup> IFRS, S1 *Sustainability-related Disclosures*, 32-33, para.51.

<sup>19</sup> IFRS, S1 *Sustainability-related Disclosures*, 27, para. 23-24. It is unclear if this is in reference to IFRS S2 *Climate-related Disclosures*, “Climate resilience” 37-39, para. 15.

<sup>20</sup> World Economic Forum, Annual Meeting 2022, 24 May 2022, “ESG for Global Resilience,” Shereen Bhan, (Moderator), Brian T. Moynihan (CEO, Bank of America), Alan Jope (CEO, Unilever), Emmanuel Faber (Chair, IFRS), Laura M. Chan (Chairman, HKEX), <https://www.weforum.org/events/world-economic-forum-annual-meeting-2022/sessions/global-esg-for-global-resilience>, [accessed 9 June 2022].

<sup>21</sup> IFRS, S1 *Sustainability-related Disclosures*, 28.

<sup>22</sup> IFRS, S1 *Sustainability-related Disclosures*, 29-30, para. 27-35.

The remaining bulk of the Standard in IFRS S1 deals with general features such as details of the reporting entity, connected information, fair presentation, materiality, comparative information, frequency of reporting, location of information, sources of estimation and outcome uncertainty, errors, and lastly, statement of compliance. While this section intends to provide some clarification of expectations and requirements, there are areas of concern. For example, under *materiality* it states “an entity shall apply judgement to identify material sustainability-related financial information. ... An entity need not provide a specific disclosure that would otherwise be required by an IFRS Sustainability Disclosure Standard if the information resulting from that disclosure is not material.” This is vague and open for dispute.<sup>23</sup> Also, it requires considerable assumptions and predictions about possible future events with the demand that “all relevant facts and circumstances” about possible outcomes must be considered, including potential effects of events on value, timing, and certainty of future cash flows in the long-term.<sup>24</sup> Lastly, an explicit and unqualified statement of compliance, with all of the related legal implications, must be made declaring compliance with “all of the relevant requirements.”<sup>25</sup>

## B. EXPOSURE DRAFT IFRS S2 CLIMATE-RELATED DISCLOSURES (IFRS S2)

### a) OBJECTIVE AND SCOPE

This second layer of the IFRS Sustainability Disclosure Standard complements the IFRS S1 Sustainability-related Disclosures as outlined above. It follows a similar order and format. The declared objective is to “facilitate the provision of comparable information for global markets...to [be able to] assess entities' exposure to and management of climate-related risks and opportunities, across markets, to facilitate capital allocation and stewardship decisions.” This means “more consistent, complete, comparable, verifiable information, including consistent metrics and standardised qualitative disclosures.”<sup>26</sup> Entities must disclose how resources are used and correspond with stated strategies and goals so that lenders, investors, and insurers can assess an entity's adaptive capabilities to climate risks and opportunities. Identifiable risks included in the standards are physical risks of climate change and risks of the transition to a low carbon economy.

### b) CORE CONTENT

There are four areas that comprise the core content: governance, strategy, risk management, and metrics and targets.

#### i. GOVERNANCE

This section is identical to the governance requirements in IFRS S1 except for an added paragraph at the end stipulating that unnecessary duplication shall be avoided. To reiterate, the

<sup>23</sup> IFRS, S1 *Sustainability-related Disclosures*, 34, para. 59-60.

<sup>24</sup> IFRS, S1 *Sustainability-related Disclosures*, 37-38, para. 81-83. An entity must also disclose all information about the assumptions it makes.

<sup>25</sup> IFRS, S1 *Sustainability-related Disclosures*, 39, para. 91.

<sup>26</sup> IFRS S2, *Climate-related Disclosures*, 5.

purpose of this section is to identify which individuals or body within a company are responsible for the oversight of climate-related risks and opportunities. Details on the responsibilities, skills, competencies, frequency of audit or risk advice, how the individuals or bodies oversee strategy and risk management and monitor progress, and whether or not salaries are tied to progress. The role of management in assessing and managing these issues is expected to be explained in detail.<sup>27</sup>

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## ii. STRATEGY

This section is very similar to the strategy requirements in IFRS S1, with two small insertions to include transition plans and identify significant transition risks, and the significant addition for scenario analysis. To reiterate, the objective of this reporting area is to require detailed information—quantitative and qualitative—on an entity's comprehensive strategy for dealing with climate-related risks and opportunities. Most of the information requested, however, deals with risks rather than opportunities. Information disclosures required range from risks to: business models and value chains; strategy and decision-making including how targets are to be achieved and transition plans; cash flows, access to finance, and costs of capital and how the financial position will change over the short, medium or long-term; and an explanation of the climate resilience of its strategy and business model to physical and transition risks.<sup>28</sup>

Specific information required for identifying “significant climate-related risks and opportunities” is found in the disclosure topics in the industry specific requirements in Appendix B.<sup>29</sup> As part of the qualitative climate-related targets, entities are asked to explain if carbon offsets will be used to achieve emission targets and whether they will be nature or technologically based. It must also be declared if the offsets have been verified by an accredited third party. To be clear, there is nowhere in the reporting to include offsets quantitatively within the overall emissions. Only *gross* emissions are tabulated.

A significant addition to this area is the requirement for some type of scenario analysis to assess an entity's “climate resilience.” A company must identify its financial resources available to and investment in “climate-related mitigation, adaptation, or opportunities for climate resilience.”<sup>30</sup> A company must explain which scenario analysis it used and various details associated with it. If a company decides not to use a scenario analysis it must use “an alternative method or technique to assess its climate resilience,” and it must explain why it did not use a scenario analysis. In whatever scenario analysis it undertakes, it must utilize assumptions “about the way the transition to a lower-carbon economy will affect the entity, including policy assumptions for the jurisdictions in which the entity operates; assumptions about macroeconomic trends; energy usage and mix; and technology.”<sup>31</sup> Compelling the use of some type of costly and cumbersome scenario analysis that “aligns with the latest international agreement on climate change,” forces the use of predictions that are predicated on the assumption that hydrocarbons must be or will be left in the ground regardless of advances in carbon technology.

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<sup>27</sup> IFRS, S2 *Climate-related Disclosures*, 32-33.

<sup>28</sup> IFRS, S2 *Climate-related Disclosures*, 33-34, para. 8(c), 8(e).

<sup>29</sup> IFRS, S2 *Climate-related Disclosures*, 34, para. 10.

<sup>30</sup> IFRS, S2 *Climate-related Disclosures*, 38, para. 15(a)(iii)(3).

<sup>31</sup> IFRS, S2 *Climate-related Disclosures*, 38, para. 15 (b)(i)(8).

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### iii. RISK MANAGEMENT

This section is identical to the risk management requirements in IFRS S1 except for an added paragraph at the end that stipulates unnecessary duplication shall be avoided and suggests integrated rather than separate reporting. To reiterate, it requires information on the process (or processes) a company uses to identify, assess, and manage climate-related risks and opportunities, and how those processes are integrated into the overall risk management processes using science-based risk assessment tools. A company is required to disclose in detail how it assesses risks and opportunities, how it prioritizes climate-related risks relative to other risks, the input parameters it uses, if processes have changed from prior reports, and the extent to which these approaches are integrated into the overall management process.<sup>32</sup>

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### iv. METRICS AND TARGETS

Next to strategy and the inclusion of scenario analysis, this is the largest and most important section because of the overall importance emissions have for this entire exercise. The objective of this section is to quantify climate-related risks and opportunities—how these are measured, monitored, and managed—so that users can understand how performance is measured and if progress towards set targets is being made. All scopes of emissions generated during the designated reporting period are to be calculated and reported by an entity with the *Greenhouse Gas Protocol* being the preferred standard.<sup>33</sup> Scope 1 covers “direct greenhouse gas emissions that occur from sources that are owned or controlled by an entity”; Scope 2 includes “indirect greenhouse gas emissions that occur from the generation of purchased electricity, heat or steam consumed by an entity,” and, controversially, entities must disclose all upstream and downstream Scope 3 emissions, which are “indirect emissions outside of Scope 2 emissions that occur in the value chain of the reporting entity, including **both upstream and downstream emissions**.”<sup>34</sup> [emphasis added] The fifteen categories included in Scope 3 emission calculations must be specified and the basis for the measurement must be explained if the information is provided by parties in the value chain.<sup>35</sup> If some Scope 3 emissions are excluded an entity must explain why, such as “it is unable to obtain a faithful measure.”<sup>36</sup> Absolute **gross** greenhouse gas emissions are to be reported and expressed as CO<sub>2</sub> equivalent. There is no place for incorporating carbon removal such as carbon capture and storage or offsets in a clear and demonstrable way as part of an entity’s overall net emissions.

An entity must also quantify its asset or business activity that is vulnerable to transition and physical risks and “what amount and percentage of assets or business activities are aligned with climate-related opportunities.”<sup>37</sup> Additionally, an entity must disclose its internal carbon price and

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<sup>32</sup> IFRS, *S2 Climate-related Disclosures*, 40, para. 17-18.

<sup>33</sup> However, standards and accounting practices continue to evolve and by making one protocol mandatory precludes the opportunity for evolution and improvement in GHG accounting and reporting.

<sup>34</sup> IFRS, *S2 Climate-related Disclosures, Appendix A: Defined Terms*, 46-47.

<sup>35</sup> The fifteen categories are purchased goods and services; capital goods; fuel- and energy-related activities not included in Scope 1 or Scope 2 emissions; upstream transportation and distribution; waste generated in operations; business travel; employee commuting; upstream leased assets; downstream transportation and distribution; processing of sold products; use of sold products; end-of-life treatment of sold products; downstream leased assets; franchises; and investments. The definition also suggests accounting for “the extraction and production of purchased materials and fuels; transport-related activities in vehicles not owned or controlled by the reporting entity; electricity-related activity (for example, transmission and distribution losses), outsourced activities, and waste disposal.” IFRS, *S2 Climate-related Disclosures, Appendix A: Defined Terms*, 47.

<sup>36</sup> IFRS, *S2 Climate-related Disclosures*, 42, para. 21(a)(vi)(4)

<sup>37</sup> IFRS, *S2 Climate-related Disclosures*, 42, para. 21(d).

how this price is applied in its decision-making. The metrics are further specified as those contained in the IFRS S2 *Climate-related Disclosures*, Appendix B *Industry Specific Standards*, and other relevant or applicable standards including metrics developed internally by an entity.

To be specified, and consistent over time, are: the definition and calculation of the metrics used, if the target is an absolute or intensity target, “how the target compares with those created in the latest international agreement on climate change and whether it has been validated by a third party,” the applicable target period, the base period for progress to be measured, any interim targets or milestones, analysis of trends or significant changes in its performance towards the disclosed targets, and revisions to targets and explanation for those revisions.<sup>38</sup> These paragraphs on targets are intended to force companies to commit to the arbitrary Paris Agreement targets, and therefore make them liable for not meeting them. This removes responsibility from governments that set the impossible targets. The assumption here is that any amount of emissions control will actually control Earth’s temperature; an unprovable theory at this point.

### C. EXPOSURE DRAFT IFRS S2 CLIMATE-RELATED DISCLOSURES APPENDIX B INDUSTRY-BASED DISCLOSURE REQUIREMENTS

An integral part of the IFRS S2 *Climate-related Disclosures* are the industry specific disclosure requirements to acquire additional information “associated with specific business models, economic activities and other common features characterized by participation in an industry.”<sup>39</sup> The requirements are derived from existing SASB Standards including the industry classifications, disclosure topics, metrics and technical protocols, and activity metrics.<sup>40</sup> The disclosures require an entity to identify the significant climate-related risks and opportunities, with “the industry-based requirements to be a useful starting point.”<sup>41</sup> Entities must disclose and explain in detail what and how they are doing their part “to support the transition.”<sup>42</sup> There are 11 designated sectors covering 68 industries from consumer goods to oil and gas operations, health care to consumer services. These global standards are intended to apply to every business aspect of society.

It is beyond the scope of this report to analyze in detail all 68 industries. However, to understand the implications of the IFRS Standard to Canada's economy and its agriculture and hydrocarbon industries in particular, it is useful to explore some of the industry-based requirements. There is considerable emphasis on water management throughout the industry specific requirements that has the potential to discriminate against certain North American regions, particularly western Canada. Water management disclosure standards are based on the World Resources Institute (WRI), Water Risk Atlas tool, Aqueduct, and require an accounting of activities that take place in areas of High or Extremely High baseline water stress. According to the WRI, as shown in Figure 1 on the following page, the main agricultural and oil and gas producing areas of southern Manitoba, Saskatchewan, and Alberta are located in High and Extremely High baseline water stress regions. This means that activities in those areas will be highlighted, quantified, and potentially counted against entities by lenders, investors, and insurers.

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<sup>38</sup> IFRS, S2 *Climate-related Disclosures*, 43, para. 23-24.

<sup>39</sup> IFRS, S2 *Climate-related Disclosures*, Appendix B, 49, para. B1.

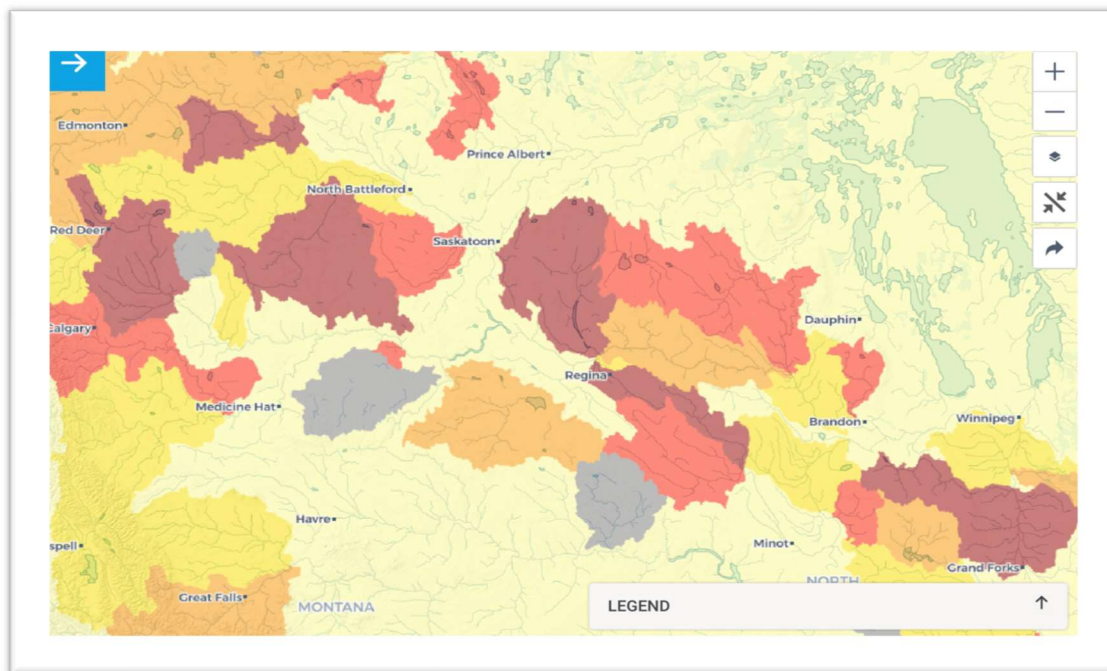
<sup>40</sup> IFRS, S2 *Climate-related Disclosures*, Appendix B, 51, para. B10.

<sup>41</sup> IFRS, S2 *Climate-related Disclosures*, Appendix B, 51, para. B13.

<sup>42</sup> IFRS, S2 *Climate-related Disclosures*, Appendix B, 52, para. B14, example.



Figure 1 Water Stress Areas Parts of Alberta, Saskatchewan, Manitoba



Source: World Resources Institute, Aqueduct. <https://www.wri.org/aqueduct>

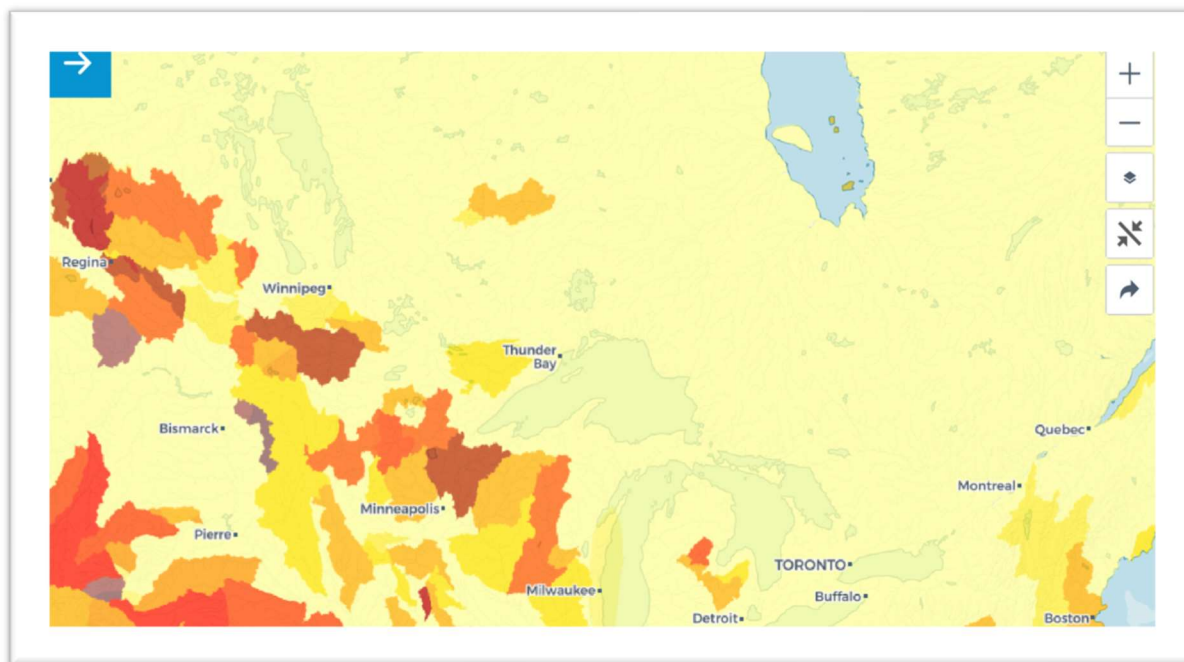
For example, a company identified as an Agricultural Product producer must disclose the “percentage of agricultural products sourced from regions with High or Extremely High Baseline Water Stress.” As shown in Figure 2 on the following page, this would mean grain from southern Saskatchewan would fall into the High/Extremely High Baseline Water Stress region, but grain from southern Ontario or Quebec would not. In addition, although farming per se is not one of the industries included in Appendix B, independent farmers will be compelled to account for their activities and emissions as an ingredient source for the Agricultural Products industry, and as part of the Scope 2 and Scope 3 emissions accounting in the previous two sets of standards.<sup>43</sup>

Most troubling is that the level of information required, and applicable metrics are not equitable across all industries. For example, there is no provision for asset end-of-life/retirement/disposal calculations for solar, wind, or battery technology manufacturers or project developers. This is particularly concerning given that there is currently no way to recycle or dispose of retired solar panels, wind turbines, or large-scale batteries. In addition, solar and wind projects need only provide their nameplate energy produced rather than actual energy produced—which can often be less than one-third of the nameplate rating, whereas other electrical utility generators must

<sup>43</sup> IFRS, *S2 Climate-related Disclosures* Appendix B Industry-based disclosure requirements, B20 Agricultural Products, 139.



Figure 2 Water Stress Area Parts of Saskatchewan, Manitoba, Ontario, Quebec



Source: World Resources Institute, Aqueduct. <https://www.wri.org/aqueduct>

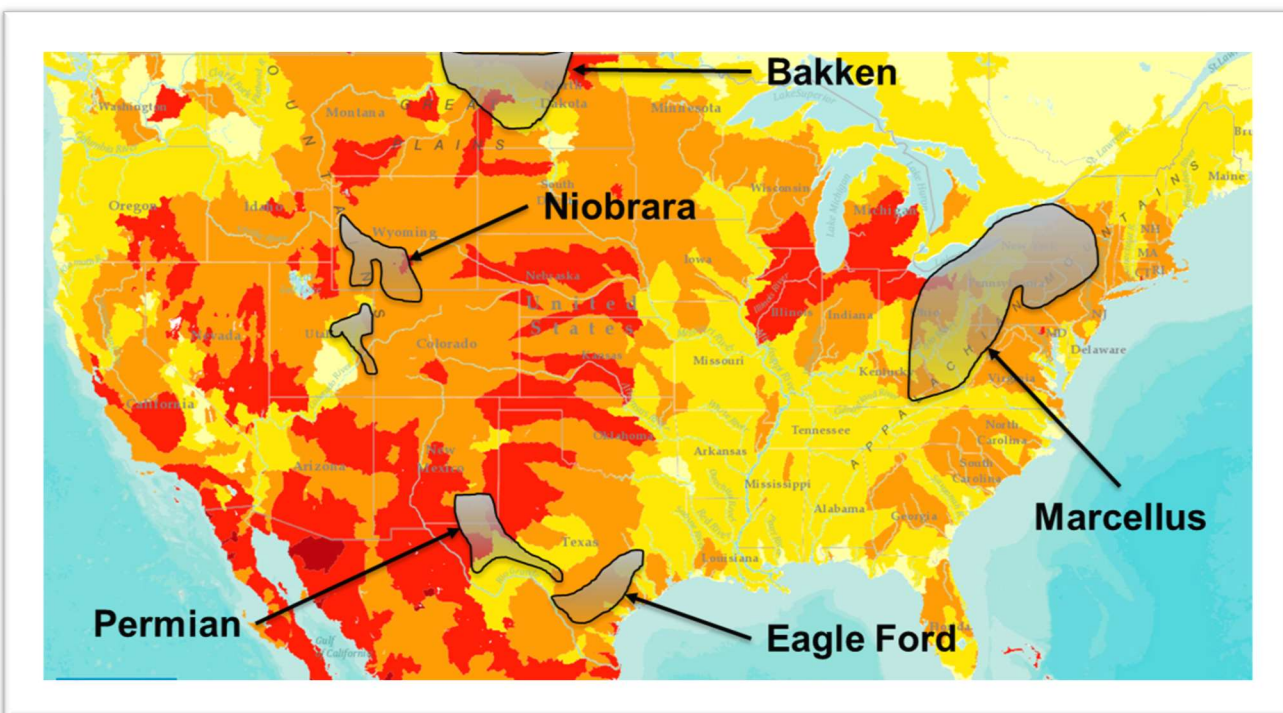
disclose precisely how much total electricity was delivered to the various consumers.<sup>44</sup> Energy policy within an operating region is to be taken into account but not geopolitical issues that may have an impact on the availability of the materials for the manufacturing of solar panels or wind turbines, or the manufactured equipment itself.

This is in stark contrast to *IFRS S2 B11 Oil & Gas—Exploration and Production*, for example, which will see companies that employ hydraulic fracturing techniques in Alberta, Saskatchewan, and across the border in the United States be discriminated against because they utilize water. As illustrated in Figure 3 on the following page, it just so happens that the most prolific formations such as the Bakken Field and the Permian Basin, are located mostly within the High to Extremely High Risk water stress areas as designated by the World Resource Institute.<sup>45</sup>

<sup>44</sup> IFRS, *S2 Climate-related Disclosures* Appendix B Industry-based disclosure requirements, B44 Solar Technology & Project Developers, 471-482; B45 Wind Technology & Project Developers; B32 Electric Utilities & Power Generators, 298-299.

<sup>45</sup> David Parham, "Why water scarcity is a major risk for oil producers," Greenbiz, 9 March 2017, <https://www.greenbiz.com/article/why-water-scarcity-major-risk-oil-producers>, [accessed 1 June 2022].

**Figure 3 Water Stress Areas and Major Shale Formations**



Source: Greenbiz, <https://www.greenbiz.com/article/why-water-scarcity-major-risk-oil-producers>

In addition, companies are penalized for having large reserves and must take into account, using various scenario and sensitivity analyses, potential policy shifts that may render reserves uneconomic to extract. Potential emissions embedded in reserves must be calculated and counted against a company, thereby discouraging the expansion of reserves.<sup>46</sup> A company like Suncor, with incredible reserve numbers in the oilsands (4.7 Billion barrels) will likely be compared unfavourably to a company like Spain's Repsol that has much lower reserve numbers (2.1 Billion barrels). There will be little incentive for a company to invest in exploring for more oil and gas and adding to the reserve base if it will mean lenders, insurers and investors will count that against the company and make funding or backing less likely. The location of the reserves or assets or if they are secure are not taken into account in the proposed Standard.

There is no place to include an assessment of energy security and geopolitical issues that could affect asset valuation, nor the benefits that an industry provides to the well-being of the society in which it operates. Since geopolitical risks and considerations are not taken into account in these standards, one could interpret this to mean that if a company is operating in a country or region with less stringent regulations they will be at less risk than operating in a country or region with a more stringent regulatory environment. Investment could very well shift away from nations with strong regulations to regions with weak regulations and poor environmental, social, and governance records. Furthermore, there is no place to include carbon capture utilization and storage or carbon tech that could enable net-zero production of oil and gas. Lastly, Scope 1

<sup>46</sup> IFRS, S2 Appendix B11, 90-91.

emissions must be calculated “in accordance with a 100-year time horizon of global warming potential (GWP) values. ...the preferred source for GWP values is the IPCC Fifth Assessment Report (2014).”<sup>47</sup>

There are a total of twenty-two industries that are obligated to use a 100-year GWP in assessing their Scope 1 emissions. These industries include coal; metals and mining; oil and gas exploration, development, refining, marketing, and midstream; agricultural products; meat, poultry, and dairy; chemicals (including fertilizer); electrical utilities; containers and packaging; and all forms of transportation. Some critics suggest that the entire purpose of the GWP calculation is to provide a numerical indictment of CO<sub>2</sub> because “every one of the GWPs calculated is enormously inflated due to division by the extremely small denominator associated with the slope of the CO<sub>2</sub> absorption curve.”<sup>48</sup> The inclusion of this incredibly problematic and pernicious calculation suggests these standards are designed to make any industry that produces or utilizes hydrocarbons or greenhouse gases appear in a highly negative way, and therefore a risky financial proposition. As Brian Moynihan stated, “companies that deliver on the metrics will get more capital, the ones that don’t will get less...the metrics will be applied to everyone everywhere...It’s a business system, it’s a setting of metrics across the whole economy.”<sup>49</sup>

### III. DISCUSSION

The ostensible goal of the three layers of disclosures outlined above—*IFRS S1 Sustainability-related*, *IFRS S2 Climate-related Financial Disclosures*, and *IFRS S2 Climate-related Financial Disclosures Appendix B Industry-based Disclosure Requirements*—is to prevent “greenwashing” by mandating a global baseline of stringent quantitative reporting on emissions reduction net-zero actions compared to targets within and across industries that are legally binding. The claim is for accuracy, verifiability, and comparability. While that may be the idealized intention, the devil is in the details.

The *IFRS S1 Sustainability-related Standards* and the *IFRS S2 Climate-related Standards* have a great deal of overlap and duplication, are unclear in the level of detail required in many of the sections and offer contradictory statements concerning the overall approach. There are considerable problems with certain elements that are included such as the requirement for scenario analysis, Scope 3 emissions, gross emissions, and unforeseen outcomes relating to liability, reputation, and overall expense and complexity. There are also glaring omissions relating to carbon emission removals, capture, utilization, and storage, asset retirements, energy security, and geopolitical considerations.

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<sup>47</sup> IFRS, S2 Appendix B11, 109.

<sup>48</sup> Thomas P. Sheahan, “Climatic Distortions Due to Diminutive Denominators,” Watts Up With That, 25 May 2018, <https://wattsupwiththat.com/2018/05/25/climatic-distortions-due-to-diminutive-denominators/>, [accessed on 31 May 2022]. See also, Myles R. Allen, et al., “A solution to the misrepresentations of CO<sub>2</sub>-equivalent emissions of short-lived climate pollutants under ambitious mitigation,” *Nature*, 4 June 2018, <https://www.nature.com/articles/s41612-018-0026-8#Abs1>, [accessed on 31 May 2022].

<sup>49</sup> World Economic Forum, Annual Meeting 2022, 24 May 2022, Global ESG for Global Resilience, Laura Cha (Chairman, Hong Kong Exchanges and Clearing), Emmanuel Faber (Chair, ISSB), Alan Jope (CEO, Unilever), Brian Moynihan (CEO, Bank of America), <https://www.weforum.org/events/world-economic-forum-annual-meeting-2022/sessions/global-esg-for-global-resilience>, [accessed 31 May 2022].

## A. DUPLICATION AND CONTRADICTIONS

The IFRS Standard demands that duplication be avoided, yet there is not only duplication across the Exposure Drafts, there are also parts which insist outside standards and requirements be considered. For example, in the *Illustrative Guidance on S1*, it is suggested that “in the absence” of specific standards on “water- and biodiversity-related risks and opportunities” other standards can be considered.<sup>50</sup> It is unclear how an entity would know when it is supposed to take into account other standards if it has not been included in the S1, S2, and Appendix B standards, and the penalty for not doing so. The IFRS Standard also makes clear that these are a **baseline**, meaning other jurisdictions and regulators could build upon it as they see fit.<sup>51</sup> This does not seem to be a true global baseline when there are other standards that must also be taken into account, nor does it seem to streamline and simplify the process when several elements are duplicated.

An example of duplication can be found in the Governance sections which require the same information, as does the sections on risks and opportunities in the Strategy and Risk Management sections. It is unclear how “climate-related risks” are different from the criteria used for “sustainability-related risks.” It is also unclear if the IFRS Standard, if made mandatory by various nations, including Canada, will be in addition to existing ESG reporting or if it is intended to replace it. Avoiding duplication is difficult because the IFRS Standard also requires incorporating reference to and application of other standards and requirements that request similar information.

Contradictory statements and mixed messaging are also evident. For example, in question 1 of the *IFRS S1 Exposure Draft* under “overall approach” it first states that only significant sustainability-related risks and opportunities information will be required, but then in the next sentence declares that “**all** of the sustainability-related risks and opportunities to which the entity is exposed, even if such risks and opportunities are not addressed by a specific IFRS Sustainability Disclosure Standard,” are what is required. There is a large gap between “significant” and “all” and contradicts what ISSB Chair Emmanuel Faber told the World Economic Forum at Davos in May 2022, “First we must be pragmatic. You only report what matters to your company. You’re not reporting everything. You pick and you choose for right reasons what matters and what doesn’t.”<sup>52</sup> Who will determine what those right reasons are and what matters? Will this be left to the courts to determine when seemingly inevitable legal action is taken? In any event, as demonstrated in the previous section, that is not what is actually written in the disclosure drafts. So, what should one believe?

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<sup>50</sup> *IFRS Illustrative Guidance on [Draft] IFRS, S1 General Requirements for Disclosure of Sustainability-related Financial Information*, 8-10. See also, *IFRS, S1 Sustainability-related Disclosures*, 15 -- a caveat is inserted here that entities will also need to take into account topics included in at least four other types of standards.

<sup>51</sup> *IFRS, S1 Sustainability-related Disclosures*, 20.

<sup>52</sup> World Economic Forum, Annual Meeting 2022, 25 May 2022, Global ESG Standards: Are We There Yet?, Ramya Krishnaswamy, (Moderator), Brian T. Moynihan (CEO, Bank of America), Emmanuel Faber (Chair, IFRS), Gillian R. Tett (Financial Times), <https://www.weforum.org/events/world-economic-forum-annual-meeting-2022/sessions/global-esg-standards-are-we-there-yet>, [accessed 31 May 2022].

## B. SCENARIO ANALYSIS

Comments on the IFRS Standard Draft Exposures are to be framed around questions provided on each section by the ISSB. Question 7 acknowledges serious problems with scenario analysis such as its evolving applicability to climate, and great expense and resource intensiveness for most businesses. The ISSB also admits that the preparers of the Draft Exposures raised concerns regarding “the speculative nature of the information that scenario analysis generates, potential legal liability associated with disclosure (or miscommunication) of such information, data availability and disclosure of confidential information about an entity’s strategy.”<sup>53</sup> Despite those concerns, the requirement for scenario analysis was included. As described in the previous section, entities are highly encouraged to conduct one “unless it is unable to do so.” If a company decides not to use a scenario analysis to outline its “climate resilience” it must explain in excruciating detail what methods, assumptions, time horizons, inputs it did use and offer “an explanation of why the entity was unable to use climate-related scenario analysis to assess the climate resilience of its strategy.”<sup>54</sup> Dr. Peter Wells, an expert on financial reporting regulation and financial statement analysis, wrote in his letter of comment that it was inappropriate to include scenario analyses in a *reporting standard* because they were subject to value judgements and not quantifiable.<sup>55</sup> He expressed similar reservations about anything beyond Scope 1 reporting as Scope 2 and Scope 3 were impossibly unverifiable.

## C. SCOPE 3 EMISSIONS

The disclosures require the accounting of Scope 3 emissions: all indirect emissions that can be linked to an entity. The GHG Protocol lists 15 different categories for Scope 3 emissions, as

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<sup>53</sup> IFRS, *S2 Climate-related Disclosures*, 18.

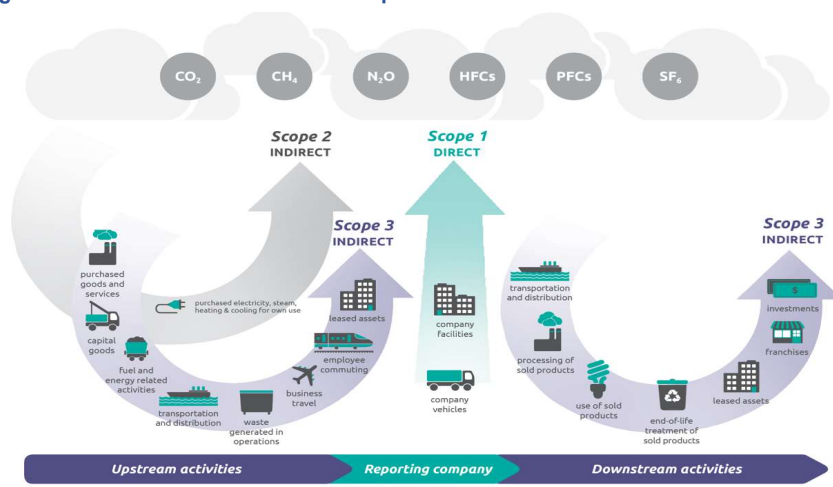
<sup>54</sup> IFRS, *S2 Climate-related Disclosures*, 39, para. 15(b)(ii), 7.

<sup>55</sup> Letter to IFRS Foundation from Dr. Peter Wells, Subject: Ed-IFRS S2 *Climate-related Disclosures*, 29 April 2022, <https://www.ifrs.org/content/dam/ifrs/project/climate-related-disclosures/exposure-draft-comment-letters/n/n-a-ddd0a390-4461-4af1-a403-5261dc0d1012/peter-wells---ifrs-s2.pdf>, [accessed 31 May 2022].



described above in Section II(B)(iv) and illustrated in the figure below.<sup>56</sup> These are an unacceptable metric akin to a farmer calculating and taking responsibility for what someone does

Figure 4 Overview of GHG Protocol Scopes and Emissions Across the Value Chain



Source: Greenhouse Gas Protocol, *Corporate Value Chain (Scope 3) Accounting and Reporting Standard* (WRI/WBCSD: 2011), 5

with a potato he grew. How did the potato get to the store? How did the person who bought it travel to the store where the potato was bought? Is it baked in an oven? Is it peeled? Is it washed? What happens to the peels? Is it boiled? Is it fried? Is it cooked on a fire? What did the person do with the bag in which the potato came, and so on? How is a farmer or a seller of potatoes supposed to calculate and quantify all of those “emissions”? It is an onerous burden to require constant monitoring of every interaction and relationship along the value chain and be responsible for it.

By insisting on the disclosure of **all gross** Scope 1, Scope 2, and Scope 3 emissions with nowhere to clearly report and quantify **net emissions** that take into account carbon capture/removal or offsets, any industries that produce, handle, or utilize hydrocarbons in any way are targeted and likely penalized, as are companies that actually make durable goods or manufacture any kind of product. Contrary to accounting practices, which take into consideration both gross and net revenues, only gross emissions and gross emission intensities are required rather than net emissions taking into account any carbon capture and storage or offsets. All emissions other than CO<sub>2</sub> are converted into CO<sub>2</sub> equivalent, essentially making CO<sub>2</sub> the “currency” of these standards. It would seem that as long as an entity does not actually produce anything or serve people who use hydrocarbons in any way, it will have lower emission numbers.<sup>57</sup> Scope 3 emissions reporting also leads to a duplication in accounting such that emissions are counted

<sup>56</sup> GHG Protocol, Scope 3 Emissions, <https://ghgprotocol.org/standards/scope-3-standard>, [accessed 31 May 2022].

<sup>57</sup> Indeed, Brian Moynihan commented that “the net-zero commitment of a company is effectively an internal tax on the use of carbon across a company...For net-zero not to cost a lot of money in the end is to get emissions down.” Yet, it is not true net-zero if carbon capture, storage, utilization, and removal is not included in the accounting. World Economic Forum, Annual Meeting 2022, 25 May 2022, Global ESG Standards: Are We There Yet?, Ramya Krishnaswamy, (Moderator), Brian T. Moynihan (CEO, Bank of America), Emmanuel Faber (Chair, IFRS), Gillian R. Tett (Financial Times), <https://www.weforum.org/events/world-economic-forum-annual-meeting-2022/sessions/global-esg-standards-are-we-there-yet>, [accessed 31 May 2022].



several times over and are not an accurate representation of climate-risk. There is no clear accepted means for preventing double-counting without a massive intrusion into the monitoring of every aspect of every person's life. Thus, requiring Scope 3 emissions in the disclosure generates the perverse circumstances that would assign a benefit for companies to having lower sales.

#### D. LIABILITY, REPUTATION, EXPENSE

A potential unforeseen outcome of these disclosures is that they create opportunities for entities to be made financially liable for any perceived misstatement on emissions, future scenarios, future global developments, future weather events, the behaviours and actions of those who use an entity's products, and reputational damage from any "controversies." Liability is a real concern with sustainability and climate-related disclosures since many jurisdictions will be looking for misstatements or material gaps in the disclosures.<sup>58</sup> For example, even though consistent metrics are not in use yet, German authorities recently raided the offices of Deutsche Bank in Frankfurt, Germany as part of an investigation into allegations of investment fraud and greenwashing or "overstating its claims of environmental, social and governance (ESG) investing."<sup>59</sup> This sets a terrible precedent and could be "the start of a broader trend: pressuring organizations into making unachievable sustainability targets and suing them when the targets aren't met."<sup>60</sup> As one commentator suggests, "While companies are under pressure to declare net-zero targets, which are only aspirational without the necessary technologies to achieve them, they are nonetheless being sued for not achieving them."<sup>61</sup> The global baseline will make the situation worse for companies because the disclosures will be tied to financial statements; in practice it could mean litigation of those individuals and executives identified under governance, strategy, and risk management not only for misstatements on targets, however that is interpreted, but also to be held responsible for not estimating properly weather events arbitrarily determined to have been caused by anthropogenic climate change.

This becomes quite apparent in the vague definition of "Materiality": "Sustainability-related financial information is material if omitting, misstating or obscuring that information could reasonably be expected to influence decisions that the primary users of general purpose financial reporting make on the basis of that reporting, which provides information about a specific reporting entity."<sup>62</sup> Interpreting what "information could reasonably be expected to influence decisions" by auditors, investors, insurers, and lenders could be open to abuse. "Omitting, misstating or obscuring" information may happen unintentionally, and there is no provision for unintentionality. As mentioned earlier, Emmanuel Faber, chair of the ISSB, made it sound as if there would be

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<sup>58</sup> Business and Human Rights Resource Centre, "Rising litigation risk is a reality for companies, says expert," May 2022, <https://www.business-humanrights.org/en/latest-news/rising-litigation-risk-is-a-reality-for-companies-says-expert/>, [accessed 1 June 2021].

<sup>59</sup> Aaron Foyer, "Companies Go to Court Over Sustainability," Energy Minute, 8 June 2022, <https://energyminute.ca/single/news/1950/companies-go-to-court-over-sustainability>, [accessed 8 June 2022]. See also, Matthias Goldschmidt and Ed Frankl, "Deutsche Bank, DWS Offices in Frankfurt Searched Over Greenwashing Claims," *The Wall Street Journal [online edition]*, 31 May 2022, <https://www.wsj.com/articles/deutsche-bank-dws-offices-in-frankfurt-searched-over-greenwashing-claims-11654004574>, [accessed 8 June 2022].

<sup>60</sup> Aaron Foyer, "Companies Go to Court Over Sustainability," Energy Minute, 8 June 2022, <https://energyminute.ca/single/news/1950/companies-go-to-court-over-sustainability>, [accessed 8 June 2022]. See also, McKinsey & Company, "Accounting for Values and Valuation," 3 March 2021, <https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/accounting-for-values-and-valuation>, [accessed 8 June 2022].

<sup>61</sup> Aaron Foyer, "Companies Go to Court Over Sustainability," Energy Minute, 8 June 2022, <https://energyminute.ca/single/news/1950/companies-go-to-court-over-sustainability>, [accessed 8 June 2022].

<sup>62</sup> IFRS, S1 *Sustainability-related Disclosures*, 33.

great latitude in what is considered material in the standards: “there needs to be proportionality, and materiality is absolutely fundamental. At the S1—if it’s not material, don’t report it. In climate, if it’s not material don’t report it. You need to be super pragmatic.”<sup>63</sup> Yet, as these standards are written, they really do not allow for picking and choosing or leaving information out. Companies, out of fear, may feel compelled to be extremely thorough rather than pragmatic to avoid potential litigation or reputational attacks.

The inclusion of “reputational considerations” under Climate-Related Risks and Opportunities or in any of these standards is problematic. It is unclear if there will be a separation or equivalence between real controversy, such as a product recall, and PR stunts that create false controversy to embarrass a company. Smear campaigns and eco-activist inspired terrorism could be empowered with this provision. Clearly, the use of “controversies” or “reputational considerations” is open for abuse, manipulation, and could be potentially costly.

It is not only potential litigation or reputation damage that is costly, the expense of implementing these standards is staggering. The requirement for “scenario analysis” alone is a rapacious expense. There is also the time required to amass, collate, assess, and report on all of the secondary information, particularly the Scope 3 emissions, outlined in these proposals. There is the significant cost for additional accountants, auditors, and legal teams to assess the reporting. While this cost may be absorbed better in a large multinational corporation, the same cannot be said for Small and Medium Enterprises (SMEs). Laura Cha from the Hong Kong Exchanges and Clearance explained that “disclosure is a significant cost for an SME, and they don’t see the benefit, so for us, as a market regulator, we need to educate that sector of the society and community.”<sup>64</sup> Investors ought to be concerned about the layering of expenses required for this level of compliance, and for what ultimate purpose that cannot be met by existing ESG reports. Despite the talk of the need to have a simplified system so that all companies, including SMEs, will comply and be compared equitably, these three layers of standards are not only incredibly complex and prohibitively expensive to implement, but they also omit significant elements that skew the system in a particular direction.

## E. CARBON EMISSION REMOVAL

By focusing on gross carbon emissions and emissions intensity, the standards preclude the possibility that a company employs technology that actually reduces its carbon emissions and serves to discriminate against companies that have more emissions than others. A company may be able to discuss in a qualitative manner how it utilizes carbon capture and storage or removal technology or participates in a project that captures and uses significant emissions. Offsets are only described under “Transition plans” with no place to account for them actually being utilized. Any offsets including “technological carbon removals,” shall disclose whether or not they have been “certified” by a third-party scheme. However, there seems to be no place in the standards

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<sup>63</sup> World Economic Forum, Annual Meeting 2022, 25 May 2022, Global ESG Standards: Are We There Yet?, Ramya Krishnaswamy, (Moderator), Brian T. Moynihan (CEO, Bank of America), Emmanuel Faber (Chair, IFRS), Gillian R. Tett (Financial Times), <https://www.weforum.org/events/world-economic-forum-annual-meeting-2022/sessions/global-esg-standards-are-we-there-yet>, [accessed 31 May 2022].

<sup>64</sup> World Economic Forum, Annual Meeting 2022, 24 May 2022, Global ESG for Global Resilience, Laura Cha (Chairman, Hong Kong Exchanges and Clearance), Emmanuel Faber (Chair, ISSB), Alan Jope (CEO, Unilever), Brian Moynihan (CEO, Bank of America), <https://www.weforum.org/events/world-economic-forum-annual-meeting-2022/sessions/global-esg-for-global-resilience>, [accessed 31 May 2022].

to quantify those emission reductions. What can be listed in the discussion are “technological carbon removals” and specific carbon “offsets” purchased and confirmed by an approved third party, and it is unclear if those offsets will be deducted from the company’s emissions as they are only listed under “Transition Plans”.<sup>65</sup> As discussed earlier, in unprecedented fashion, this quasi-financial accounting standard does not include net values. If the goal is to have “net-zero” emissions, it makes no sense to exclude the accounting of real emissions reduction activities and technology. One commenter wrote of the *S2 Climate-related Disclosures* proposal, “Without an accounting system that explicitly enables recording and tracking cumulative GHG emissions and removals over time, this target setting process will be untrustworthy....Statements of GHG Position and Performance, backed up by auditable GHG double entry bookkeeping should be the minimum to frame two types of targets: periodic targets (statement of performance), [and] overall/accumulated targets (statement of position).”<sup>66</sup> Perhaps this was an oversight.

## F. ASSET RETIREMENT

Discrimination is also evident with the issue of asset retirement. Under risk assessment, hydrocarbon companies must estimate and account for the cost of early asset retirement under varying policy scenarios. As discussed earlier, there is no specific provision for asset end-of-life/retirement/disposal calculations for solar, wind, or battery technology manufacturers or project developers. Given that there is currently no way to recycle or dispose of retired solar panels, wind turbines, or large-scale batteries, this is a glaring omission.

## G. ENERGY SECURITY AND GEOPOLITICS

Given recent geopolitical developments with respect to the Russian invasion of Ukraine and the subsequent sanctions against Russian oil and natural gas, energy security is a stunning omission within the draft disclosures. Indeed, there has been some discussion that the European energy crisis has awakened the west to energy reality and the pitfalls of this forced energy transition.<sup>67</sup> When asked if the war in Ukraine is a setback for the ambitions of the global baseline disclosures and energy transition, the response from Emmanuel Faber, Brian Moynihan, and others involved was an emphatic “no”.<sup>68</sup> An honest assessment of “Sustainability risks and opportunities” would include energy security (traditionally defined as reliable, affordable, and secure), and the political stability of the geographical area of operations. Unfortunately, the standards emphasize risks but offer little space for opportunities. Given that companies must estimate the emissions potential of their hydrocarbon reserves it is clear that the concept and value of energy security is absent. There is no place to include an assessment of energy security and geopolitical issues that could affect asset valuation, nor the benefits that an industry provides to the well-being of the society in which it operates. Since geopolitical risks and considerations are not taken into account in these

<sup>65</sup> IFRS, *S2 Climate-related Disclosures*, 36, para. 13b.

<sup>66</sup> Comment form to IFRS Foundation from Joel Houdet, Question 10, 010-AR, 7.

<https://www.ifrs.org/content/dam/ifrs/project/climate-related-disclosures/exposure-draft-comment-letters/j/joel-houdet-98a34a81-6f07-4a6e-a778-5acbd9aa2d3a/climate-joel-houdet.pdf>, [accessed 13 June 2022].

<sup>67</sup> McKinsey & Company, “The net-zero transition in the wake of the war in Ukraine: A detour, a derailment, or a different path?” 19 May 2022, <https://www.mckinsey.com/sustainability/of-the-war-in-ukraine-a-detour-a-derailment-or-a-different-path>, [accessed 20 May 2022].

<sup>68</sup> World Economic Forum, Annual Meeting 2022, 24 May 2022, Global ESG for Global Resilience, Laura Cha (Chairman, Hong Kong Exchanges and Clearing), Emmanuel Faber (Chair, ISSB), Alan Jope (CEO, Unilever), Brian Moynihan (CEO, Bank of America), <https://www.weforum.org/events/world-economic-forum-annual-meeting-2022/sessions/global-esg-for-global-resilience>, [accessed 31 May 2022].

standards, one could interpret this to mean that if a company is operating in a country or region with less stringent regulations, they will be considered at less risk than operating in a country or region with a more stringent regulatory environment. Investment could very well shift away from nations with strong regulations to regions with weak regulations and poor environmental, social and governance records.

#### IV. CONCLUSION

The proposed global baseline sustainability and climate-related financial disclosures in the IFRS Sustainability Disclosure Standard is being pitched as the best way to prevent “greenwashing,” replace current ESG reporting and facilitate the net-zero transition through accuracy, verifiability, and comparability. Emmanuel Faber, Chair of the ISSB, recently told an audience that these standards are not passing judgement on companies, it is just about the facts which will be used for decision-making.<sup>69</sup> The current problem with ESG funds and so-called “greenwashing” is not necessarily from the facts articulated in ESG reports or the claims of the funds, but rather with those ranking or rating a company’s ESG reports or an ESG fund. The same problem is bound to exist with these new standards: raters and rankers will provide varying interpretations of the same data because some data will be ranked higher than others depending on the ratings agency. Thus, one problem that the ISSB is claiming to solve will still exist.

A new problem added by the proposed Standard is the requirement of costly and time-consuming scenario analyses where companies must explain in detail how they will predict and plan for future policy scenarios, global developments, and weather events. In addition, companies are compelled to commit to the arbitrary Paris Agreement targets, thus making them liable for not meeting them and removing responsibility from governments that set the impossible emissions targets.

The new metrics demonize and penalize any company that has any kind of emissions. Only gross emissions are accounted for; there is no clear place to quantify net-emissions in relation to gross emissions. Thus, even if a company utilizes carbon capture that makes it net-zero, there appears to be no place in the standards to report it in the numbers. Furthermore, the gross emissions required are all Scope 1 (emissions produced directly by a company); Scope 2 (indirect emissions produced from acquired energy); and most significantly Scope 3 (all indirect emissions that can be linked from an entity). To put that into perspective, a company must account for the emissions from fifteen different areas including how its product is used, with no provision to address the duplication of accounting. It appears that as long as an entity does not actually produce anything or serve people who use hydrocarbons in any way, it will have lower emission numbers. Consequently, requiring Scope 3 emissions in the disclosure would assign a benefit for businesses having lower activity and sales.

The proposed IFRS Standard focuses on the “risks” rather than the “opportunities” of business activity. Metrics ought to take into account energy security, political stability of the geographical area of operations, the stringency of regulatory environments, and carbon capture technologies. However, the industry-based requirements are heavily skewed against companies that actually

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<sup>69</sup> World Economic Forum, Annual Meeting 2022, 24 May 2022, Global ESG for Global Resilience, Laura Cha (Chairman, Hong Kong Exchanges and Clearing), Emmanuel Faber (Chair, ISSB), Alan Jope (CEO, Unilever), Brian Moynihan (CEO, Bank of America), <https://www.weforum.org/events/world-economic-forum-annual-meeting-2022/sessions/global-esg-for-global-resilience>, [accessed 31 May 2022].

produce useful things, durable goods, or reliable and secure energy, while “acceptable” industries, like wind turbine producers and operators, are given “soft-ball” treatment compared to hydrocarbon or solar panel producers. It is clear that these standards omit important factors like energy security or geopolitical stability and are skewed to exclude any advantages that may accrue through technology that would permit the continued use of hydrocarbons. Through the demonization of CO2 emissions, the finances and operations of hydrocarbon companies, and any industry that has any emissions, will be seriously compromised to the point of extinction, which is why it is imperative that Canadian hydrocarbon companies submit feedback to the IFRS before the comment cycle closes on 29 July 2022.

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## ABOUT THE AUTHOR

Dr. Tammy Nemeth is a strategic energy analyst based in the UK. Trained as an analytical historian, she has a PhD in history from the University of British Columbia. Dr. Nemeth was a guest lecturer at a university in Germany, where she taught on the geopolitics of energy and the environment, and has published articles and book chapters on Canadian and international energy issues. She has served as a peer reviewer for academic presses and journals. She has been honoured twice by the Petroleum History Society with an article of the year award and an international achievement award. She contributed two contextual insight studies to the Public Inquiry into Anti-Alberta Energy Campaigns or the Allan Inquiry. Dr. Nemeth is the host of the ["The Nemeth Report"](#), a podcast discussing energy and geopolitical issues