



The Institute of
Chartered Accountants
of Pakistan

CA
PAKISTAN

Sustainability Updates



Accounting Standards Board
January 2023



Foreword

Sustainability has gained significant importance for global economy and the financial system. It is the key for a better world.

In the last few years, the need to address climate change and nature loss has gained momentum. It is on the agenda of many jurisdictions and organizations. Pakistan is one of most affected countries of climate change. Pakistan is ranked as the 8th most vulnerable country due to climate change according to “Global Climate Risk Index 2021” in terms of climate related challenges. We have witnessed the devastating affects of floods, in the recent past. To make a better and sustainable pakistan, all stakeholders, including regulators and corporates have to take timely and effective measures for promoting, developing and adopting best international practices for sustainable operations, businesses and economy.

In this sphere, Institute of Chartered Accountants of Pakistan (ICAP) being the statutory regulator of accountancy profession is aware of its role. It is cognizant of the international and local developments in the area of sustainability reporting and auditing. Internationally, the establishment of International Sustainability Standards Board (ISSB) at COP 26 was a key milestone in corporate sustainability reporting. On the other hand, the International Auditing and Assurance Standards Board is developing an assurance standard for sustainability.

The Accounting Standards Board (ASB) of ICAP has formulated a strategy for considering, reviewing and adopting international sustainability standards issued by ISSB, in Pakistan. The strategy is based on the principles of collaboration, consultation and transparency. The key aspects include:

- Consideration and tracking of international developments in sustainability reporting.
- Engagement with stakeholders, including regulators, industry and practitioners.
- Awareness creation of all key stakeholders through seminars, publications and roundtables.
- Capacity building of all key stakeholders through educational courses and workshops.
- Development of a roadmap for adoption of ISSB issued standards in Pakistan - after engaging with the regulators, corporates, and assessing the readiness of all stakeholders.
- Implementation of the international corporate sustainability standards in Pakistan.

About the publication

The purpose of this publication is to update ICAP members and other stakeholders about key local and international developments and initiatives in the area of sustainability, including developments in regulatory regimes, corporate sustainability reporting standards, assurance standards on sustainability, carbon trading schemes, and endorsement of the work of ISSB. The publication:

- Briefly discusses some significant steps taken by:
 - Securities and Exchange Commission of Pakistan (SECP)
 - State Bank of Pakistan (SBP)
 - Pakistan Stock Exchange (PSX)
 - ICAP
- Provides an overview of international developments in sustainability reporting and carbon trading in:
 - European Union (EU);
 - China; and
 - United States
- Sums up the work and latest tentative decisions of the ISSB in finalizing the two (2) IFRS Sustainability Disclosure Standards.
- Summarizes the work of International Auditing and Assurance Standards Board (IAASB) in developing assurance standard for sustainability reporting.
- Provides an overview of the International Organization of Securities Commissions (IOSCO) support to the work of ISSB and IAASB.

Farrukh Rehman

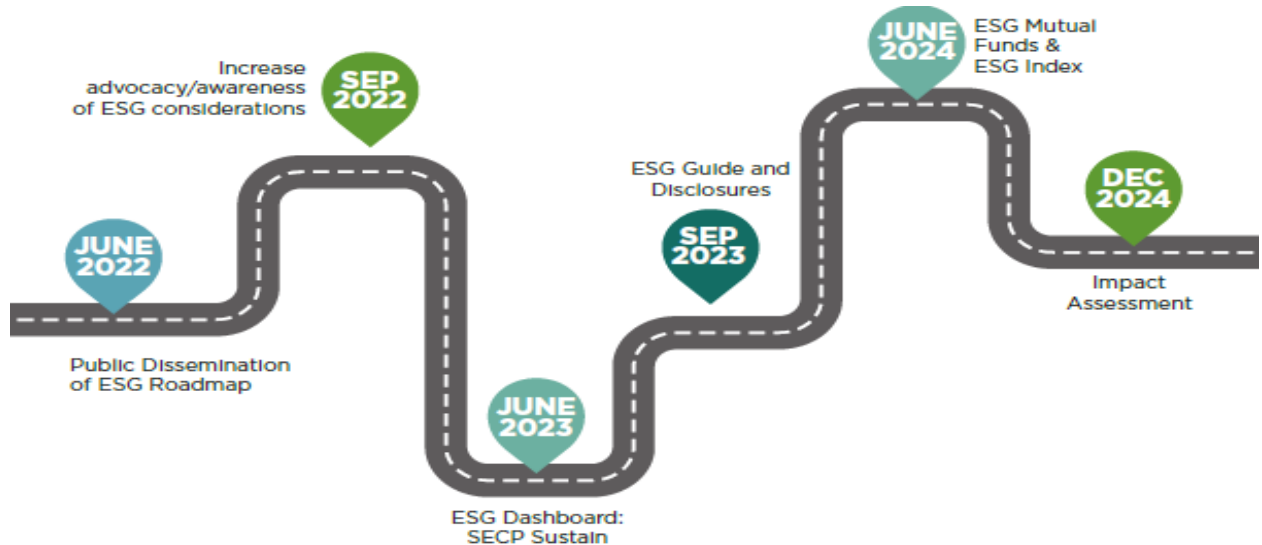
Chairman Accounting Standards Board



SECP publishes Position Paper on ESG Regulatory Roadmap

In June 2022, SECP published a Position Paper on ESG Regulatory Roadmap for stakeholders' consultation. The Position Paper highlighted SECP's priority to corporate ESG. SECP noted that the proposed ESG Roadmap is the first step in gaining understanding and bringing more clarity on long-term objectives and priorities under the ESG regulatory regime.

The Position Paper contained following key milestones



SECP expects that its efforts on corporate ESG reporting will pave the way in promoting ESG based investing, enhancing ESG disclosures and facilitate launch of ESG-based financial products and ESG based Index at Pakistan Stock Exchange in due course.

SBP issues Environmental & Social Risk Management Manual

In November 2022, State Bank of Pakistan launched the Environmental & Social Risk Management (ESRM) manual for banks and DFIs.

SBP, in 2017, issued the Green Banking Guidelines (GBGs) for Pakistan's financial sector. The GBGs have three main pillars: Managing Environmental risk in lending, Green Business Facilitation, and, Own Impact Reduction. The ESRM manual is related to GBGs. It is a procedural guide for the banks/DFIs, providing procedures, tools and templates related to the first pillar of managing environmental impact in lending. In addition to environmental risks manual also focuses on social and climatic risks, explaining that banks and DFIs are required to assess environmental and social risks of clients, and integrate these risks into bank's overall credit policy.

The manual:

- Provides a comprehensive Environmental & Social Management System (ESMS) for systematic guidance to banks/DFIs on assessing and managing environmental and social risks.
- Outlines a robust, quantitative risk rating system.
- Provides E&S Due Diligence Checklist and Supervision Checklist
- Provides a Green Banking Monitoring and Evaluation Reporting Template for reporting of banks/DFIs' GBGs implementation progress (including ESRM activities) to SBP, on annual basis.



In the context of applicability, ESRM Manual states that the loan categories for which the manual is applicable are retail, trade, microfinance, SME, corporate finance and project finance. All new loan renewals and credit proposals have to be screened against the required standards. SBP expects that the banks and DFIs will fully implement the ESRM within three (03) years of issuance of this Manual.



PSX joins Sustainable Stock Exchanges Initiative

In June 2022, Pakistan Stock Exchange joined the Sustainable Stock Exchanges (SSE) Initiative. The SSE Initiative’s goal is capacity building of stock exchanges and securities market regulators around the world to promote responsible investment in sustainable development and help improve corporate performance on ESG issues. By becoming a member of SSE Initiative PSX joined a network of 115 stock exchanges around the world that are committed to promoting sustainable development.



PSX also intends to develop an ESG index. In this regard, the ESG task force established by PSX and Pakistan Institute of Corporate Governance (PICG) will develop and operationalize an ESG Index through consultations with the corporate and financial sectors and assessment of existing industry practices. The objective of the task force is to develop best practice ESG methodology and scoring system, ensuring regular reporting and disclosure guidelines for all businesses in Pakistan and thereby put forward an ESG governance structure for publicly listed companies as a step towards establishing an ESG Index.

To understand companies’ challenges and experiences with ESG reporting, a series of consultations through roundtables with companies in three key sectors (i.e., Automobile, Textile Composite, and Banking) have also been conducted by the PSX. Further, to support corporates’ efforts to improve reporting practices, online training on the Task Force for Climate-Related Disclosures (TCFD) was organized with the SSE Initiative and conducted by CDP for all market participants in October 2022, witnessing great interest from TREC holders, listed companies, and industry association groups etc., with around 200 registrations for each of the two sessions.

ICAP promotes sustainability and engages with the key local and international stakeholders

ICAP is working to bring together different stakeholders for promoting the understanding and relevance of sustainability, climate change, and the chartered accountant’s role in advancing these agendas.

In June 2022, ICAP through Accounting Standards Board formed a multi-stakeholder working group to consider the international developments in sustainability reporting, most noticeably the issuance of two (02) draft IFRS Sustainability Disclosure Standards (IFRS Sustainability Standards) by ISSB. In this context:



Sustainability was one of the themes of All Pakistan CA Conference. The Conference brought together different stakeholders, and a range of sustainability-related topics, including the evolving global landscape, and role of accountancy profession in sustainability reporting and assurance, and key challenges in adopting global standards were discussed.

ICAP has also reviewed SECP’s Position Paper on ESG Regulatory Roadmap, and detailed comments have been shared with the SECP.

In November 2022, ICAP representatives participated in the AOSSG annual meeting and IFRS Conference. ICAP representative while presenting the *Sustainability Reporting – Need and Challenges*, explained the relevance and need for corporate sustainability reporting and the key challenges in the effective adoption of a global set of standards.

ICAP has also been engaged with the ISSB. In Seminar on Sustainability Reporting (held in July 2022) ISSB technical staff participated and shared their input during the Q&A session. In December 2022, on ISSB’s invitation ICAP participated in the roundtable of jurisdictions from the global south. During the roundtable, ICAP representative shared the current sustainability reporting landscape of Pakistan and also informed ISSB team about the significant challenges in the adoption IFRS Sustainability Standards.



International Sustainability Standards Board deliberates on IFRS Sustainability Standards

In March 2022, the ISSB issued the exposure draft of two sustainability reporting standards *General Sustainability-related Disclosures* (IFRS S1) and *Climate-related Disclosures* (IFRS S2), for public consultation and feedback.

IFRS Foundation established the ISSB in November 2021. ISSB has been mandated to develop global set of standards for corporate sustainability reporting. During 2022, several existing organizations and their disclosure sustainability-related frameworks and material have been consolidated into the work of the ISSB.

ISSB, in the light of stakeholders comments, is now deliberating and deciding on the changes to the proposed requirements of the standards. It has tentatively decided on some key areas of the proposed standards.

IFRS S1 outlines the general requirements for the preparation of sustainability reports

Some key aspects of IFRS S1 that have been tentatively decided by ISSB, include:

- The purpose of the proposed disclosure requirements (i.e. to meet the information needs of the primary users of general purpose financial reporting).
- The definition of value chain.
- Disclosure of sustainability related risks and opportunities for the value chain.
- Use of 'material' definition as per IFRS Accounting Standards.
- The timing of sustainability reporting i.e. at same time as financial statements (ISSB plans to introduce transition relief to allow companies to report sustainability-related financial disclosures after their financial statements for a short period of time).

ISSB has also agreed to remove the definition of 'enterprise value' that was included in draft IFRS S1. It has also tentatively decides to expand and clarify various aspects of the draft illustrative guidance.

IFRS S2 relates to climate-related disclosures, including the disclosure of green-house gases

After considering stakeholders' feedback on IFRS S2, ISSB has tentatively decided to:

- Require Scope 1 and Scope 2 GHG emissions.
- Proceed with the requirement to disclose Scope 3 GHG emissions (ISSB intends to provide a relief by introducing a later effective date for disclosures about Scope 3 GHG emissions).
- Allow the use of GHG Protocol Standards or any other standard.
- Require climate-related scenario analysis to report on climate resilience and to identify climate-related risks and opportunities to support their disclosures (ISSB also agreed to provide application support to preparers including making use of materials developed by the TCFD to provide guidance to preparers on how to undertake scenario analysis).

In addition to finalizing and issuing IFRS S1 and IFRS S2 in 2023, the ISSB has initiated discussions on topics for other sustainability standards. ISSB has agreed to propose four projects for prioritization in its upcoming consultation on agenda priorities:

Biodiversity, ecosystems and ecosystem services

Human capital

Human rights

Connectivity in reporting with the IASB

ISSB launches 'Partnership Framework for Capacity Building'

At COP 27, ISSB has also announced the launching of 'Partnership Framework for Capacity Building'. Partnership Framework will focus on enabling capacity building among stakeholders. It is designed to support preparers, investors and other capital market stakeholders as they prepare to use IFRS Sustainability Disclosure Standards. The three targeted interventions of the Partnership Framework will provide:

- Tailored jurisdictional engagement in selected developing and emerging economies,
- Structured partnerships that leverage organizations with specialist expertise (thematic, industry, jurisdictional) to build local expertise for standards implementation and assurance.
- Key initiatives and champions across multi-stakeholder communities and jurisdictions that help translate the ISSB ambition into tangible action.



EU makes sustainability reporting mandatory

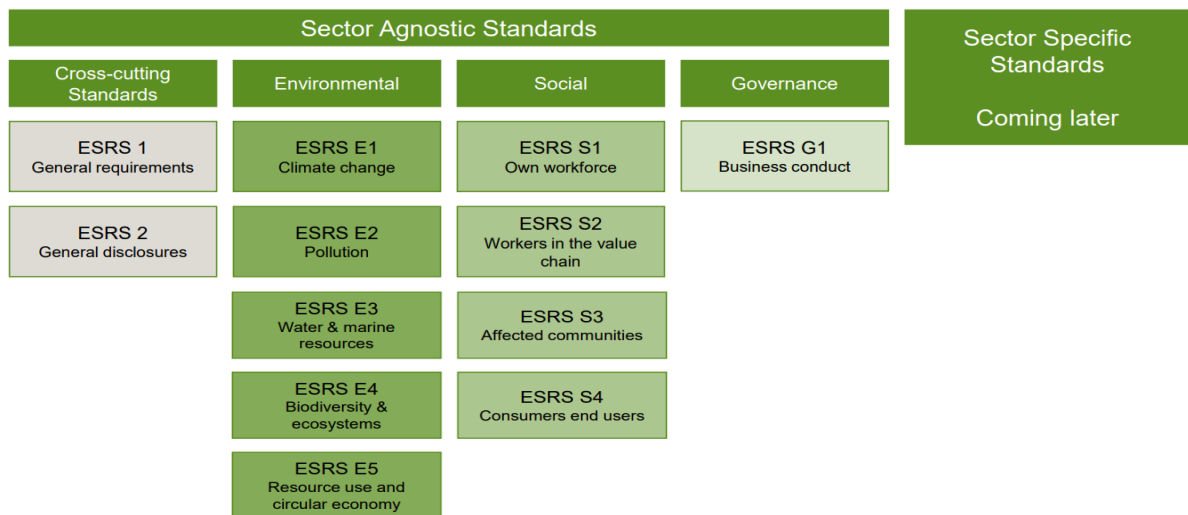
In December 2022, EU issued the Corporate Sustainability Reporting Directive (CSRD). Through this directive, EU has prescribed mandatory sustainability reporting as per the European Sustainability Reporting Standards (ESRS).

ESRS have been developed by the European Financial Reporting Advisory Group (EFRAG), and these standards now provide a common set of standards for all ESG topics, requiring companies to disclose material information on sustainability related risks and opportunities.



ESRS include 12 standards which are divided into cross-cutting and topical standards.

- 1 standard on general principles for sustainability reporting (ESRS 1)
- 1 standard on overarching disclosure requirements (ESRS 2)
- 10 topical ESG standards, each with specific disclosure requirements (E1-E5, S1-S4, G1)



CSRD besides prescribing ESRS also outlines the scope and timelines of sustainability reporting.

- Scope - Annual sustainability reporting is mandatory for:
 - EU Listed companies (except micro-sized listed companies);
 - Large-sized unlisted EU companies; and
 - International and non-EU companies with more than 150 million € annual revenue within the EU and which have at least one subsidiary or branch in the EU
- Reporting period - Company should use the same reporting period in its sustainability reporting as the one used for its financial statements.

CSDR outlines a phased adoption approach. Listed companies are required to provide sustainability report for the year beginning January 2024 (therefore first reporting will be in 2025). Companies are also required to obtain third party limited assurance on the sustainability reports.

In the next step, the EFRAG will now focus on developing:

- Sector specific standards (5 sectors covered by the Global Reporting Initiative (GRI): Agriculture, Coal Mining, Mining, Oil and Gas (upstream), and Oil and Gas (mid-to downstream); and 5 high-impact sectors: Energy Production, Road Transport, Motor Vehicle Production, Food/beverages, Textiles.
- SME proportionate sustainability standard (Expected to be issued in 2023).



U.S. Securities and Exchange Commission proposes climate-related disclosures



In March 2022, U.S. SEC issued draft climate-related disclosure for public consultation. The new rule would require consistent, comparable, and reliable disclosure of climate-related risks and greenhouse gas emissions from public companies. These disclosures would also be subject to management's internal control over financial reporting and external audit.

SEC had targeted to finalize the climate-related disclosures by October 2022. SEC, at present is still reviewing the stakeholder comments on the draft disclosures.

In terms of adoption timelines, SEC proposed a gradual approach. Based on the SEC's goal of adopting the climate disclosure rule by the end of 2022, the compliance date for disclosure for calendar year-end registrants was proposed for:

- Large, accelerated filers, 2023 (filed in 2024)
- Accelerated and non-accelerated filers, 2024 (filed in 2025)
- Smaller reporting companies (SRCs), 2025 (filed in 2026)

EU launches Carbon Border Adjustment Mechanism

The Emissions Trading System (ETS), introduced by EU in 2005, was world's first international emissions trading scheme.

In 2022, EU introduced a new carbon pricing framework termed as Carbon Border Adjustment Mechanism (CBAM). CBAM will initially apply to imports of cement, Iron and steel, aluminum, fertilizers, electricity (as these sectors are considered as high risk for carbon leakage and high carbon emissions). Going forward, more products may fall under the scope of CBAM.



The carbon pricing framework of CBAM will be applied in a phased manner.

- Starting from 2023, importers of above-noted products are required to report for the emissions in the imported goods every quarter (detailing the direct and indirect emissions and any carbon price effectively paid in the country of origin).
- From 2026, importers of above-noted products will have to purchase CBAM certificates (The number of CBAM certificates held must be equal to the total emissions embedded in the imported product, reduced to account for carbon prices already paid in the country of origin. The quantity of embedded emissions will be calculated according to established EU methodologies, and must be independently verified).

A number of countries such as Canada and Japan are also planning similar initiatives. In addition, the IMF and the OECD have recently carried out work to study how such measures could support international efforts to reduce greenhouse gas emissions.

China has launched National Emissions Trading Scheme

In June 2021, China launched carbon trading market i.e. "National Emissions Trading Scheme" (ETS). ETS started with the power sector, and 2,000 power sector companies have been obligated to account for their emissions. These power sector companies account for 40% of China's total annual CO₂ emissions. Once fully implemented, ETS will cover large entities in seven additional sectors: petroleum refining, chemicals, non-ferrous metal processing, building materials, iron and steel, pulp and paper, and aviation.

ETS is a rate-based system. It targets reductions in CO₂ emissions per unit of output rather than total CO₂ emissions (a mass-based system). Under the ETS, entities are to:

- Provide information on the volume of emissions as well as economic output.
- Receive allowances whose allocation is based on historical emissions levels and output, as well as allowances that are adjusted according to actual output during a specified period.

Allowance allocation has begun free of charge, but the plan suggests that entities will need to purchase them over time.



IAASB is developing assurance standard for sustainability reporting



IAASB as per its 2021-2023 work plan has dedicated resources and efforts to the assurance of sustainability/ESG reporting. It has started to develop a suite of standards for assurance on sustainability reporting, including an overarching standard for assurance on sustainability reporting.

IAASB has started with the development of overarching standard for assurance on sustainability reporting. It envisages that a suite of standards for assurance on sustainability reporting that provide more specificity than an overarching standard will likely need to be developed over time.

Currently, IAASB is deliberating on the draft of the overarching standard (ISAE 5000). In developing this standard, IAASB is building upon the existing IAASB Standards and guidance that deal with this topic more broadly, including ISAE 3000 and ISAE 3410.

IOSCO endorses the work of ISSB and IAASB

IOSCO is the leading international policy forum for securities regulators and is recognized as the global standard setter for securities regulation. Its membership regulates more than 95% of the world's securities markets in some 130 jurisdictions. SECP is also a member of IOSCO.

IOSCO has been interacting with stakeholders, and during its engagement IOSCO noted that:

- Among investors, there is growing demand for assurance to enhance the reliability of corporate sustainability reporting.
- While limited assurance may be the most realistic objective in the short term, investors typically see reasonable assurance as the long-term target, especially in respect of metrics such as those related to greenhouse gas emissions.
- Issuers expressed a need for assurance standards that are effective in the current landscape of sustainability reporting and are capable of keeping up with evolving standards and practices.
- Investors and issuers see consistent and comparable assurance standards for sustainability-related information as key to supporting high-quality assurance engagements.



IOSCO supported setting up the ISSB under the umbrella of the IFRS Foundation, and earlier this year it welcomed the publication of the draft sustainability reporting standards by the ISSB. During the year, IOSCO continued its engagement with the ISSB on the development of its first reporting standards. In a statement, IOSCO noted that endorsement of the final standards once these are issued by the ISSB would be a landmark in sustainable finance; it would support IOSCO members as they consider how to adopt, apply or be informed by the ISSB standards as the baseline for their own sustainable reporting requirements. The process for IOSCO's potential endorsement of the ISSB's standards will begin after the ISSB has issued its final standards.

On assurance of sustainability-related corporate reporting, IOSCO has been supporting the work of International Auditing and Assurance Standards Board (IAASB) and the International Ethics Standards Board for Accountants (IESBA).

Disclaimer

This publication has been developed to update ICAP members and other stakeholders about key local and international developments and initiatives in the area of sustainability. It is neither a substitute for reference to the pronouncements mentioned in the document, nor does it constitute accounting or other professional advice. Further, this publication should not be interpreted as a legal interpretation or requirement. While care has been taken to ensure the summarize key developments related to sustainability, this publication may contain errors or omissions that may be relevant to any particular reader. ICAP, ASB and ICAP's staff accept no responsibility for losses incurred by any party as a result of acting or not acting on the basis of this publication.

