The Valuation Technical and Practitioner Committee (VTPC)
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31 October 2023

RE: General Methodology 1: Conceptual Framework for Impact Accounting (Exposure Draft)

Dear Sir or Madam,

PwC International Ltd, on behalf of its network of member firms (PwC IL), welcomes the opportunity to respond to your invitation to comment on the General Methodology 1: Conceptual Framework for Impact Accounting (Exposure Draft).

We congratulate the International Foundation for Valuing Impacts (IFVI) and the Value Balancing Alliance (VBA) on the publication of this Exposure Draft which advances the development of future sustainability reporting. Businesses innovating with impact measurement and valuation are telling us about the tangible benefits they are seeing (including clearer language for decision making and steering towards sustainability pledges and for external stakeholders). Further, investors have told us that they are looking for information on business impacts including the attribution of a monetary value by the business. The valuation of impacts also facilitates a straightforward, holistic communication of business performance to a broader group of stakeholders (including NGOs).

Impact information requires certain consistent definitions and criteria to be applied in the preparation of impact information for there to be broad acceptance. We therefore draw your attention to the need in the Exposure Draft for definitions and measurement parameters for 'well-being', key principles for valuation techniques and determining value, principles for establishing impact pathways as well as appropriate disclaimers, ensuring that the users of impact information understand the nature of impact data and its limitations. We have provided detailed responses to individual consultation questions in the appendix to this letter.

To enable capital flows to sustainable businesses, there needs to be a set of standardised methodologies that allow for comparability and broader adoption. We therefore encourage the IFVI and VBA to continue to build consensus for the methodologies being developed for impact pathways at the sustainability topic and industry-specific level.

While impact accounting and valuation is at an early stage for many companies, we urge ongoing connection (and reference where applicable) to the work of the impact reporting standard setters (e.g. EFRAG, GRI) as this topic evolves and may support impact materiality assessment with quantitative analysis. To that end, we welcome the efforts for maximum alignment between the Exposure Draft and existing sustainability reporting frameworks (from the IFRS Foundation and EFRAG) and recommend caution in the introduction of new principles (such as conservatism).

If you have any questions in relation to this letter, please do not hesitate to contact me, Gilly Lord (gillian.lord@pwc.com), Andreas Ohl (andreas.ohl@pwc.com), or Superna Khosla (superna.khosla@pwc.com).

Yours sincerely,

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Gilly Lord,
Global Leader for Public Policy and Regulation, PwC

Appendix: Responses to the Exposure Draft Questions for Feedback

Question 1 – Preparers of impact accounts and users of impact information (paragraphs 5, 20, 22)
The Methodology proposes that the preparers of impact information are entities themselves or investors from an external perspective. The Exposure Draft states that preparing impact accounts from an external perspective may have limitations as a result of limited access to primary data of the entity. A reason for the challenge in identifying the preparers of impact accounts is that the institutional infrastructure for impact management is still being developed. It may be reasonable to imagine a future state in which entities prepare and publicly disclose audited impact statements. Alternatively, a future state may exist in which investors use sustainability-related financial disclosures to prepare impact accounts from an external perspective to inform a wide-range of investing decisions. The users of impact information are more clearly defined, as many decisions today are already informed by sustainability-related information. The users of impact information are described in paragraph 22. 1. Do you agree with the proposal to separate the preparers of impact accounts and users of impact information in this way? Why or why not? If not, how would you delineate between the preparers of impact accounts and users of impact information?

While investors may be able to use the Exposure Draft, we believe it should be focused on entity managers as the primary preparers of impact accounts, in line with other reporting frameworks. The exercise of judgement required for impact accounting means entity managers are better placed to prepare impact information, given their knowledge of the business activities and access to detailed information (at product, location level etc.).

We agree that there may be multiple users of impact information as set out in paragraph 22. However, we note that for the framework to provide a sufficient basis for preparation of information that can be assured, there needs to be consideration of 'intended users', which is not as broad as currently set out in paragraph 22. A distinction between groups allows preparers of impact information to clarify the distinct needs and interests of different groups, and respectively allows assurance practitioners to determine the nature and extent of audit procedures.

Additionally, clear guidance should be developed (or referenced) on how to take into consideration the information needs of different users, how to identify key stakeholders and what to do when their views are inconsistent.

Question 2 – Conservatism in faithful representation (paragraph 32)
The qualitative characteristic of faithful representation includes a sentence in paragraph 32 that implicitly introduces a principle of conservatism into impact accounts in cases of uncertainty. The sentence reads, “In cases of uncertainty, preparers of impact accounts should default to avoiding the overstatement of positive impacts and the understatement of negative impacts.” For reference, a principle of conservatism is not implied in the qualitative characteristic of faithful representation in European Sustainability Reporting Standards 1 General Requirements or IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information. For the avoidance of doubt, a principle of conservatism is distinct from a principle of prudence. Prudence refers to caution when making judgements under conditions of uncertainty, whereas `conservatism refers to a bias when making judgments under conditions of uncertainty. Conservatism is, however, an explicit principle adopted by frameworks and organizations focused on impact, for instance in Impact Economy Foundation’s The Impact-Weighted Accounts Framework. The proposal is included to acknowledge that impact accounting in its present state does not benefit from the same level of assurance and audit, regulatory authority, and widespread adoption as general purpose financial reporting. As such, conservatism may not be undesirable, particularly if a conservative bias generates impact information that is more relevant or faithfully represented. Specifically, implicitly implying a principle of conservatism when measuring and valuing impacts may help to counteract the effects of impact washing, or overstating the sustainability performance of an entity. 1. Do you agree with including a principle of conservatism in the Exposure Draft, primarily to legitimize impact accounting and counter-balance impact washing? Why or why not?

We do not agree with the inclusion of the statement ‘should default to avoiding the overstatement of positive impacts and the understatement of negative impacts’. The principle of faithful representation is well established in corporate reporting and we believe it to be sufficient to avoid overstating positive impacts or understating negative impacts.

Introducing a principle of conservatism could introduce a systematic bias in impact reporting and potentially compromise the objective of "faithful representation". Unlike prudence, which suggests caution in estimation but does not introduce a directional bias, conservatism explicitly incorporates such a bias. This can create complications for users of impact accounts who seek to make direct comparisons across entities or track performance over time.

To ensure maximum alignment with existing reporting frameworks, we recommend consideration of additional information in paragraph 31 e.g. “A neutral depiction is without bias in the selection or presentation of information.”

Question 3 – Impact pathways (paragraphs 51, 52, 53, 54)

Impact pathways are the foundational framework for measuring the impacts of corporate entities, linking the activities of an entity to impacts on people and the natural environment through a series of consecutive, causal relationships. The proposal in the Exposure Draft is to utilize the impact pathway logic of the Impact Management Platform.10

The stages of an impact pathway and how those stages are defined vary across frameworks, guidance, and protocols in the impact management ecosystem. Oftentimes, the boundaries between the different elements of the impact pathway, particularly outcomes and impacts, are dependent on the nature of the underlying phenomena. In some cases, certain components of the pathway may be implicitly modelled in the monetary valuation; in others, certain components are not relevant. This may depend on, for instance, the specific sustainability topic or industry of the entity.

1. For the purposes of impact accounting as set out in the Exposure Draft, do you have any concerns with the proposed logic of the impact pathway as described in paragraph 52? If so, please describe scenarios in which the proposed impact pathway may not be applicable and how you would change the proposed logic of the impact pathway.

We do not have concerns with the proposed logic of the impact pathways as described in paragraph 52.

We do note a need for further definition for human wellbeing with more explicit reference to specific parameters defining "human well-being" to ensure a solid basis for comparison. For instance, referencing frameworks like the OECD's well-being conceptual framework could provide clarity and alignment in this context.

The Exposure Draft should also define principles for identifying and assessing when establishing causality within impact pathways, including principles for considering time horizons when identifying impacts.

We also observed that the impact definition within the Exposure Draft (paragraph 46) varies slightly from the ESRS. For ease of implementation, we recommend reference to baseline reporting standards (e.g. ESRS) and then clarify further refinements for the purposes of placing a monetary valuation on impacts.

Question 4 – Impact materiality and the qualitative characteristic of relevance (paragraphs 25, 26, 27, 73, 74, 83, 84

To prepare impact accounts, an entity or investor must determine which impacts to include and exclude. The Exposure Draft addresses this need by applying an impact materiality perspective. Specifically, impact materiality is defined as an entity-specific aspect of the qualitative characteristic of relevance.

Practically, this means that when preparing impact accounts, and after a preparer has identified, measured, and valued an impact, the preparer should consider the three perspectives in paragraph 26 to decide whether to include an impact. The three perspectives are as follows:

a. the capacity of the impact information to influence the decisions of users;

b. the need for transparency as a public good and accountability towards affected stakeholders; and

c. the significance of the impact on affected stakeholders.

For the third perspective, that of affected stakeholders, the significance of an impact is further described in paragraph 27, which is determined by the scale and scope of the impact. After considering the three perspectives, the preparer should determine if an impact is material. Impact materiality is entity-specific, in that materiality varies for each entity and, as a result, the Methodology does not include mandatory impacts or a uniform threshold for impact materiality.

1. Are the paragraphs noted above in the question clearly written, in that they provide clear guidance on how to determine whether to include or exclude an impact from impact accounts? If not, which paragraphs are unclear and how might you enhance their clarity?

2. Do you agree with the three perspectives for determining relevance in section 3.2? If not, which perspectives do you disagree with and why?

3. Do you agree with defining impact materiality as an entity-specific aspect of relevance for the purposes of impact accounting? Further, do you agree with the proposal to not include mandatory impacts in the Methodology?

1. The paragraphs referenced above contain some ambiguity and potential for circularity, especially when identifying and assessing relevance. We suggest the following:

    a. Clearly define impact materiality (or reference it to other sources such as the ESRS where relevant) within section 3.2.

    b. Consolidate section 5.1 (paragraphs 73-74) with section 5.4 (paragraphs 83-84) to streamline the guidance on impact materiality, enhancing clarity and reducing redundancy.

    c. Clearly indicate that all relevance perspectives within paragraph 26 need to be satisfied for impact information to be deemed relevant.

    d. Add the decision-usefulness criterion “information may impact decisions of users if it has predictive value, confirmatory value or both”.

    e. Develop or reference supplemental guidance to further clarify and provide practical application guidance enabling consistent implementation.

2. We do not agree with the inclusion in 3.2 of the relevance determining perspective "the need for transparency as a public good and accountability towards affected stakeholders" on the basis that there is no framework for determining 'public good'. The inclusion of this perspective could deter from the aim of standardisation and comparability.

   Subsequently, paragraph 25 should be updated to reflect the removal of perspective "b", which implies that the notion of information relevance as a public interest activity in its own right no longer stands.

3. We agree with defining impact materiality as an entity-specific aspect of relevance. We also agree to not include a list of mandatory impacts as this goes against the concept of materiality assessment.

Question 5 – Additional feedback
1. Do you disagree or have concern with any additional proposal(s) in the Exposure Draft? For example, this could include feedback on the framing of the overall purpose and structure of the Methodology, references used, and definitions, among other areas. If so, what are they and what do you see as viable alternative approaches?

We have the following recommendations:

1. The inclusion of key principles underpinning valuation. Currently the exposure draft is silent on this, whereas to drive clarity and comparison between companies, there needs to be established key principles for available valuation techniques and criteria for selecting appropriate techniques depending on the purpose of the valuation, as well as other key factors to be considered for impact valuation, e.g. principles for generating/ selecting value factors, use of discount factors, etc. We understand based on information in paragraph 11, that measurement and valuation methods would be subject to subsequent general methodology statements and we recommend prioritising this aspect of methodology as a foundational element for driving consistency and comparability within impact accounting.

2. Clarification of the principles of netting in impact accounting, requiring transparency and caution to ensure individual positive and negative impacts are clearly disclosed, preventing the potential overshadowing of significant negative consequences by positive contributions.

3. Further refining section 4.10 Attribution of Impacts by providing more explicit criteria for distinguishing between where an entity is wholly or partially responsible for impacts, how to navigate and reconcile/disclose instances of double counting, and considering the capacity of the impact information to meet the decision-making needs of users.

4. Clarification (in paragraph 24) of which characteristics may no longer apply to impact information from prior time periods and what should be done in such instances.

5. Inclusion of an additional clause related to understandability qualitative characteristic of impact information [adapted] from paragraph D30 of ISSB S1:

   Some [impact information is] inherently complex and might be difficult to present in a manner that is easy to understand. An entity shall present such information as clearly as possible. However, complex information about these [impacts] shall not be excluded from [impact information] to make those reports easier to understand. Excluding such information would render those reports incomplete and, therefore, possibly misleading.

6. Inclusion of a definition of direct and indirect impacts within section 4.2 The Definition of Impact.

7. Removal of reference (currently in paragraphs 22.b) to use of this conceptual framework in the assessment of enterprise value to avoid any confusion for preparers with financial materiality (as implicit in the ISSB and proposed SEC disclosure approach). We recognise that while certain impacts may have a material monetary valuation, this will not always mean they are financially material.