

# Unpuzzling the Sustainability Reporting Alphabet Soup

by Hilde Blomme & Jona Basha

The world is on a trajectory for a temperature rise exceeding 3°C above pre-industrial levels, surpassing the 2°C target of the Paris Agreement<sup>1</sup> and obviously, the ambitions for 1.5°C. In addition to climate change, environmental degradation, human rights and social issues are increasingly concerning companies, investors, policymakers, regulators and society in general. The coronavirus crisis brought a range of non-financial information (NFI)<sup>2</sup> issues to the forefront and underscored their relationship with the economy.

Stakeholders understand that companies' financial and NFI reporting impact and depend on one-another. Therefore, it is important to address NFI to ensure resilient business models. The International Financial Reporting Standards (IFRS) guide financial reporting almost globally, however, NFI reporting does not enjoy the same level of standardisation.

## NFI framework developers and standard setters

There are currently a number of voluntary NFI initiatives and frameworks, commonly referred to as the 'alphabet soup'. While the scope of each of these frameworks and initiatives differ based upon the needs of the users of those frameworks, they also share common elements and complement one-another.

An answer to calls for harmonisation came in September 2020 from CDP, the Climate Disclosure Standards Board (CDSB), the Global Reporting Initiative (GRI), the International Integrated Reporting Council (IIRC) and the Sustainability Accounting Standards Board (SASB). These 5 leading global organisations on sustainability reporting (collectively referred to as 'the Five') mapped how their initiatives fit to their vision for a comprehensive corporate reporting system<sup>3</sup>. Accountancy Europe welcomed their unprecedented and much awaited collaboration. Let's explore the Five's work in a bit more detail.

## Who is who?

Established by the Financial Stability Board in 2015, the Task Force on Climate-related Financial Disclosures (TCFD)<sup>4</sup> aims to inform investors on

the risks and opportunities of climate change. The recommendations are structured around 4 pillars:

1. governance
2. strategy
3. risk management
4. metrics and targets.

They are adopted in the European Commission's (EC) 2019 Guidelines on the Non-financial Reporting Directive (NFRD)<sup>5</sup>, and expected to become mandatory in New Zealand<sup>6</sup>, the United Kingdom<sup>7</sup>, Hong Kong<sup>8</sup> and Switzerland<sup>9</sup> as well as being supported by investors (e.g. BlackRock<sup>10</sup>, State Street Global Investors<sup>11</sup>, Norges Bank Investment Management<sup>12</sup>). Established in 2000, CDP<sup>13</sup> runs a disclosures system on climate change, water security and deforestation for investors, preparers, countries, and rates them based on these datapoints.

1 United Nations (2015), Paris Agreement, see: <https://unfccc.int/process-and-meetings/the-paris-agreement/the-paris-agreement>

2 Even though "non-financial information" lacks a formal definition, for the purposes of this article it is deemed to include information relating to environmental, social and governance (ESG), corporate social responsibility (CSR), internally generated intangibles (e.g., intellectual property, knowledge, relationships, teamwork, trust, branding, reputation, technology, etc.) and other value drivers that are not usually measured in monetary terms.

3 CDP, CDSB, GRI, IIRC, SASB, Statement of Intent to Work Together Towards Comprehensive Corporate Reporting, see: <https://29kjwb3armds-2g3gi4lq2sxl-wpengine.netdna-ssl.com/wp-content/uploads/Statement-of-Intent-to-Work-Together-Towards-Comprehensive-Corporate-Reporting.pdf>

4 TCFD (2017), Recommendations of the Task Force on Climate-related Financial Disclosures, see: <https://www.fsb-tcfd.org/publications/>

5 European Commission (2019), Communication from the Commission – Guidelines on non-financial reporting: Supplement on reporting climate-related information, see: <https://eur-lex.europa.eu/legalcontent/EN/TXT/?uri=CELEX%3A52019XC0620%2801%29>

6 New Zealand first in the world to require climate risk reporting, see: <https://www.beehive.govt.nz/release/new-zealand-first-world-require-climate-risk-reporting>

7 UK joint regulator and government TCFD Taskforce: Interim Report and Roadmap, see: <https://www.gov.uk/government/publications/uk-joint-regulator-and-government-tcfd-taskforce-interim-reportand-roadmap>

8 Securities and Futures Commission (2020), Consultation Paper on the Management and Disclosure of Climate-related Risks by Fund Managers, see: <https://apps.sfc.hk/edistributionWeb/api/consultation/openFile?lang=EN&refNo=20CP5>

9 Federal Council fleshes out proposals for sustainable Swiss financial centre, see: <https://www.admin.ch/gov/en/start/documentation/media-releases/media-releases-federal-council.msg-id81571.html>

10 Blackrock, Larry Fink Letter to CEOs, see: <https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter>

11 State Street Global Advisors, CEO's Letter on our 2021 Proxy Voting Agenda, see: <https://www.ssga.com/us/en/institutional/ic/insights/ceo-letter-2021-proxy-voting-agenda>

12 Norges Bank Investment Management (2020), Consultation on the FCA's Proposals to Enhance Climate-related Disclosures, see: <https://www.nbim.no/en/publications/consultations/2020/consultation-on-the-fcasproposals-to-enhance-climate-related-disclosures/>

13 CDP, see: <https://www.cdp.net/en>

Since 2007, CDSB<sup>14</sup> has provided a framework for reporting environmental information, useful for investor decision-making. It includes the characteristics of information, requirements for disclosures and guiding principles.

Founded in 2010, the IIRC<sup>15</sup> developed its' International Integrated Reporting Framework (<IR> Framework) which aims to provide investors with information on an entity's value creation story and how it uses and impacts the 6 capitals (financial, manufactured, intellectual, human, social and relationship, natural).

Since 1997, the GRI<sup>16</sup> has been developing standards that enable a broad range of stakeholders to understand the impact a company has on the environment, people and the planet. These consist of universal, sector and topic standards.

SASB<sup>17</sup> published industry-specific standards in 2018. They aim to provide investors with topics and metrics, which may have a material financial impact on the company. Similar to TCFD, they are very popular among investors.

### How do these initiatives fit together?

Accountancy Europe's Cogito Paper 2019 Interconnected standard setting for corporate reporting<sup>18</sup> (Cogito Paper 2019) elaborated a materiality lens that builds on the popular financial materiality<sup>19</sup>, expands time-horizons to include impacts on value creation and addresses wider impacts on the environment and society (see Figure 1).

The Five built on these ideas in their paper and developed "dynamic materiality", which guides their vision for corporate reporting (see Figure 2).

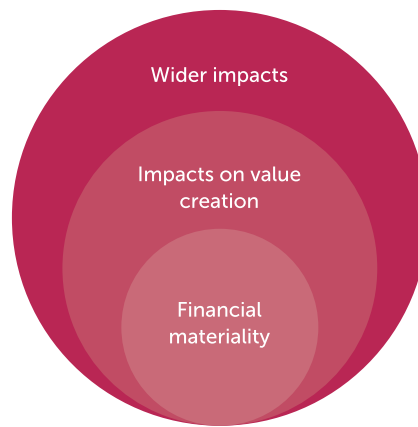


Figure 1.

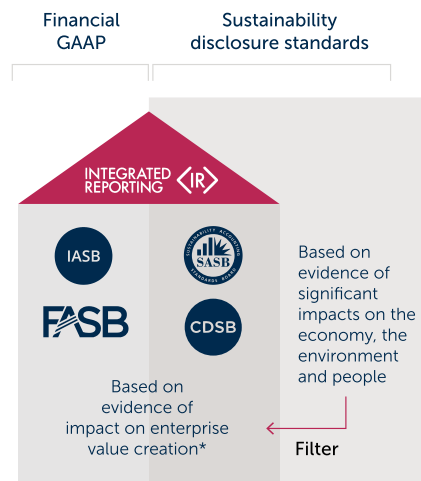


Figure 2.

In addition to financial materiality, they categorise NFI matters as material to:

1. enterprise value creation (important for investors as they eventually have a financial impact on the company), and
2. the economy, environment and people (important to broader stakeholders).

The International Accounting Standards Board (IASB), SASB and CDSB would provide the standards to address enterprise value creation, underpinned by the principles of the <IR> Framework.

GRI standards would both complement the enterprise value creation standards and provide the basis for wider impacts.

The Five further illustrated reporting for enterprise value creation with a prototype standard on climate-related financial disclosure<sup>20</sup>.

### What is missing?

While the Five may provide the content of NFI standards, adequate governance (including due process) is necessary to legitimise the standards. The Cogito Paper in 2019 proposed enhancing IFRS structures to address NFI reporting and ensure interconnected standard setting. These ideas were broadly referenced by the IFRS Foundation in its recent consultation paper on sustainability reporting<sup>21</sup>.

Following 576 overwhelming responses, the IFRS Foundation may announce the establishment of a sustainability standards board (SSB), in parallel to the IASB, at the UN Climate Change Conference COP26 meeting in November 2021<sup>22</sup>.

The International Organization of Securities Commissions<sup>23</sup> noted that, when put together, the Five and the IFRS

14 CDSB, see: <https://www.cdsb.net/>

15 IIRC, see: <https://integratedreporting.org/>

16 GRI, see: <https://www.globalreporting.org/>

17 SASB, see: <https://www.sasb.org/>

18 Accountancy Europe (2019), Interconnected standard setting for corporate reporting, see: <https://www.accountancyeurope.eu/publications/interconnected-standard-setting-for-corporate-reporting/>

19 The IASB notes that "[i]nformation is material if omitting, misstating or obscuring it could reasonably be expected to influence the decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity."

20 CDP, CDSG, GRI, IIRC, SASB, Reporting on enterprise value Illustrated with a prototype climate-related financial disclosure standard, see: [https://29kfw-b3armds2g3gi4lq2sx1-wpengine.netdna-ssl.com/wp-content/uploads/Reporting-on-enterprise-value\\_climate-prototype\\_Dec20.pdf](https://29kfw-b3armds2g3gi4lq2sx1-wpengine.netdna-ssl.com/wp-content/uploads/Reporting-on-enterprise-value_climate-prototype_Dec20.pdf)

21 IFRS Foundation Consultation Paper on Sustainability Reporting, see: <https://www.ifrs.org/projects/work-plan/sustainability-reporting/>

22 News, IFRS Foundation Trustees announce next steps in response to broad demand for global sustainability standards, see: <https://www.ifrs.org/news-and-events/2021/02/trustees-announce-next-steps-in-response-to-broad-demand-for-global-sustainability-standards/>

23 IOSCO, Open response to the open letter from CDP, Climate Disclosure Standards Board (CDSB), Global Reporting Initiative (GRI), International Integrated Reporting Council (IIRC) and Sustainability Accounting Standards Board (SASB) proposing avenues for Working together to meet the needs of the capital markets, see: <https://www.iosco.org/library/speeches/pdf/20201029-Erik-Thed%C3%A9n.pdf>

address the contents and governance for NFI standard setting.

### The European and global state of play

The European Union (EU) has been leading the NFI agenda for years. Currently, there are 3 processes running in parallel:

1. The revision of the NFRD<sup>24</sup>.
2. Potential changes to the governance and funding of the European Financial Reporting Advisory Group (EFRAG) if it were to be mandated with EU NFI activities<sup>25</sup>.
3. EFRAG Lab preparatory work for the possible elaboration of EU NFI standards<sup>26</sup>.

These critical developments will crystallise in 2021: EFRAG will report to the EC by the end of February 2021, whereas the proposals on the revised NFRD are expected in April 2021.

In the EU, NFI standards are important to achieve public policy objectives, including the ambitions of the European Green Deal<sup>27</sup>. Therefore, the EFRAG Lab has been developing its technical advice to the EC for future EU NFI standards. Their outreach document<sup>28</sup> lays out ideas on the foundations, operational guidelines, architecture and reporting structure of the future European NFI standard setter.

On a global level, SASB and IIRC announced their intention to merge and form the Value Reporting Foundation<sup>29</sup>, with CDSB potentially joining at a later stage<sup>30</sup>.

### The potential way forward?

Accountancy Europe's Follow-up paper to Cogito Paper 2019<sup>31</sup> suggested a "building block" approach to NFI standard setting. The foundation block would be a set of globally accepted NFI standards, applicable to all companies. This would help improve market transparency and guide capital to sustainable investments. Additional "blocks" of EU NFI reporting standards important to meet EU public policy objectives could be added.

The Value Reporting Foundation and CDSB could join the SSB under the IFRS Foundation to develop NFI reporting standards, material to value creation. In the longer term, the IFRS structures may be enhanced to address wider stakeholders, and therefore potentially welcome GRI. EU leadership is critical to achieve this global base.

Ultimately, the future European NFI standard body could play a double role: (1) endorsing (SSB's?) standards and (2) developing an additional EU layer of standards.



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Hilde leads the professional expertise team and provides regulatory and technical expertise in the areas of reporting, assurance, (sustainable) finance, tax and practice development.



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Jona is also part of the corporate reporting team. She engages in various financial reporting matters and specialises in non-financial information reporting and standard setting.

24 EC, Non-financial reporting by large companies (updated rules), see: <https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12129-Revision-of-Non-Financial-Reporting-Directive>

25 EFRAG, Ad-personam governance mandate, see: <https://www.efrag.org/Activities/2010051124018235/Ad-personam-governance-mandate>

26 EFRAG, Non-financial reporting standards, see: <https://www.efrag.org/Activities/2010051123028442/Non-financial-reporting-standards#>

27 EC, A European Green Deal, see: [https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal\\_en](https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal_en)

28 EFRAG Lab Project Task Force Non-financial reporting standards, Outreach meeting European standard- setting (ESS), see: <https://www.efrag.org/Assets/Download?assetUrl=%2Fsites%2Fwebpublishing%2FSiteAssets%2FPTF-NFRS%2520Outreach%2520Document%2520final.pdf>

29 Press release (2020), IIRC and SASB announce intent to merge in major step towards simplifying the corporate reporting system, see: <https://www.sasb.org/wp-content/uploads/2020/12/IIRC-SASB-Press-Release-Web-Final.pdf>

30 CDSB (2020), The Value Reporting Foundation – What is next for CDSB?, see: <https://www.cdsb.net/harmonization/1125/value-reporting-foundation-%E2%80%93-what-next-cdsb>

31 Accountancy Europe (2020), Follow-up paper: Interconnected standard setting for corporate reporting, see: <https://www.accountancyeurope.eu/publications/follow-up-paper-interconnected-standard-setting-for-corporate-reporting/>