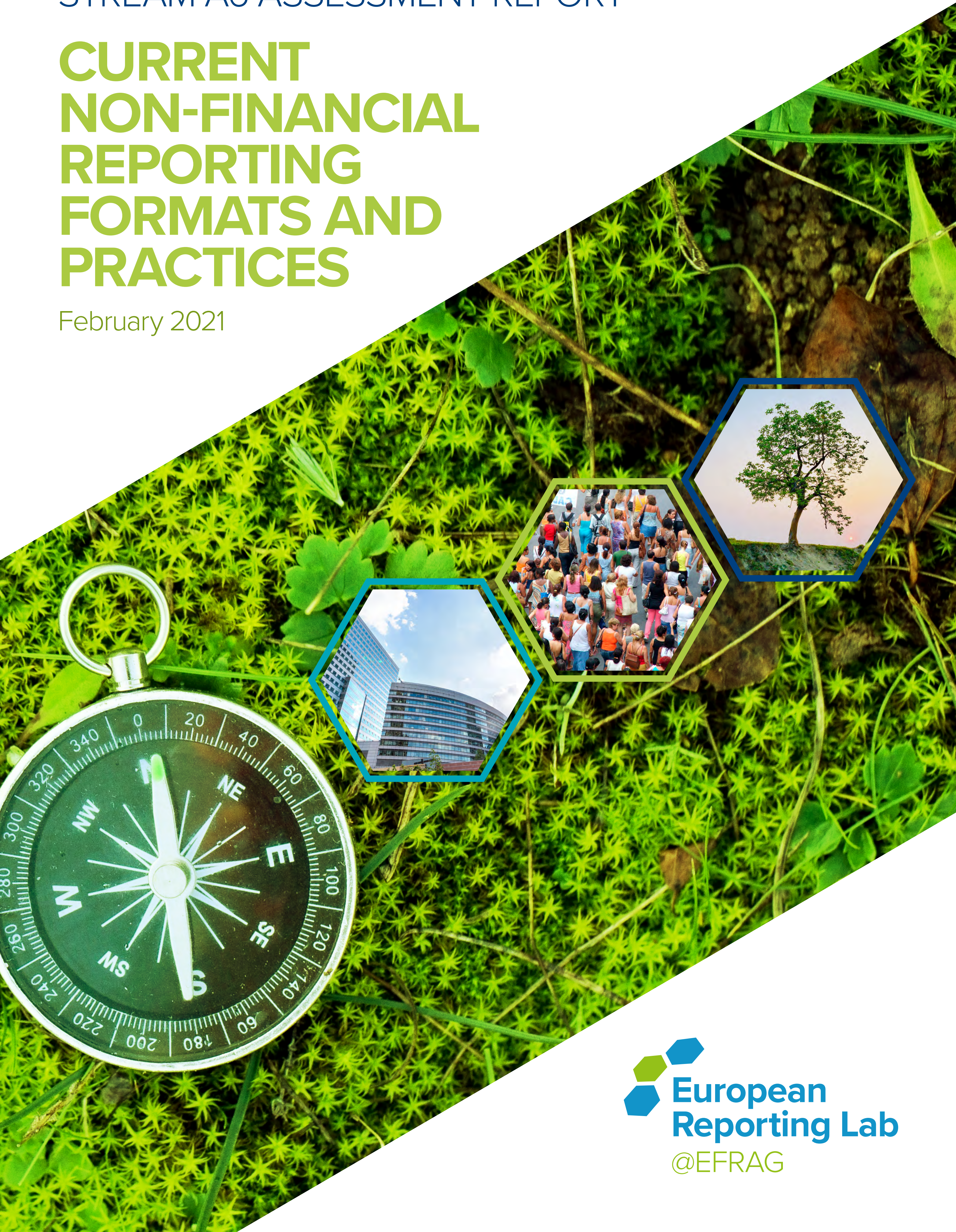
APPENDIX 4.6:
STREAM A6 ASSESSMENT REPORT

CURRENT NON-FINANCIAL REPORTING FORMATS AND PRACTICES

February 2021



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DISCLAIMER

This appendix forms part of a series of seven documents, comprising the report and its appendices prepared by the European Lab Project Task Force on preparatory work for the elaboration of possible EU non-financial reporting standards (PTF-NFRS), for submission to the European Commission in response to a mandate including a request for technical advice dated 25 June 2020.

The contents of the PTF-NFRS report and its appendices are the sole responsibility of the PTF-NFRS. The European Lab Steering Group Chair has assessed that appropriate quality control and due process had been observed to the extent possible within the context of the relevant mandate and the timeframe allowed, and has approved the publication of the PTF-NFRS report and its appendices. The PTF-NFRS report and its appendices do not represent the official views of EFRAG and are not subject to approval by the EFRAG governance bodies: EFRAG General Assembly and the EFRAG Board; or the European Lab Steering Group.

As regards the views expressed in the PTF-NFRS report and its appendices the following observations and clarifications should be noted:

- the PTF-NFRS report taken as a whole reflects a very large consensus;
- it is understood that members of the PTF-NFRS are not expected to endorse each and every one of the 54 detailed proposals in the PTF-NFRS report and may have different views on some of them;
- in addition the views expressed may not reflect the views of the organisations or entities to which individual PTF-NFRS members may belong;
- the assessment work for the different project focus areas, presented in Appendices 4.1 to 4.6 to the PTF-NFRS report, was the result of separate sub-groups of the PTF-NFRS, for which only peer review within the PTF-NFRS was performed.

Links are included in the PTF-NFRS report and its appendices to facilitate readers accessing the reference or source material mentioned. All such links were active and functioning at the time of publication.

Questions about the European Lab and its projects can be submitted to EuropeanLab@efrag.org.

EXECUTIVE SUMMARY

1 Stream A6 assessed the current situation of non-financial reporting for the following three dimensions of standard-setting:

a) **Content:** What is disclosed? How is it disclosed?

b) **Classification:** Where is the information located? Does the required information have an address / taxonomy of data?

c) **Reporting format:** How is the information reported?

2 The analysis focused primarily on the reporting practices followed by EU companies under the scope of the Non-Financial Reporting Directive (NFRD)[1]. The analysis took the form of desktop research that involved reviews of published research and data analysis.

3 Stream A6 observes that the large and increasing number of reporting requirements and frameworks, together with their heterogeneity (in scope, objective, implementation – voluntary or mandatory, technology, etc.), are a source of numerous inconsistencies in reporting practices. The assessment of Stream A6 is that these ultimately fail to address users' needs while being a burden for preparers of non-financial information, whose specificities and capacities (from large companies to SMEs) are not sufficiently considered.

4 Stream A6 finds that from a digitisation perspective, the non-financial reporting ecosystem is diversified in many ways, inflating costs, creating operational and compliance risks, and ultimately hampering access.

1 EU Directive 2014/95.

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INTRODUCTION AND OBJECTIVES

5 Based on the workplan that was presented and adopted by the PTF during its kick-off meeting on 11 September 2020, Stream A6 focused on the following assessment objectives:

a) To assess management reporting diversity, in terms of what, where and how non-financial information is currently reported;

b) To identify the hurdles and challenges faced by preparers of non-financial information, including a specific focus on the practices and experience of small and medium-sized entities (SMEs);

c) To review the experience and feedback of users (whether current non-financial information reporting practices are meeting their needs and which changes might be beneficial); and

d) To assess the digitisation progress.

DETAILED ANALYSIS OF THE CURRENT STATE OF PLAY

6 The starting point for the Stream A6 assessment was the rich – and partly confusing – diversity of non-financial reporting channels that currently exist and that give rise to many questions.

FRAMING OF THE WORK

Context

7 The PTF was requested to provide technical advice for a possible future non-financial reporting standard setter. Any such standard setting has **three dimensions**:

a) **Content:** What is disclosed? How is it disclosed?

b) **Classification:** Where is the information located? Does the required information have an address / taxonomy of data?

c) **Reporting format:** How is the information reported?

Scope

8 Stream A6 assessed the current situation of non-financial reporting for each of the three dimensions mentioned above.

9 The analysis focused primarily on the reporting practices followed by EU companies under the scope of the NFRD. The analysis mostly took the form of desktop research, based on reviews of published research and data analysis.

Objectives

10 Stream A6 sought to evaluate the following questions:

a) How is non-financial information produced? The evaluation focused on:

(i) **Regulatory and/or voluntary context**

On what basis do companies report? Do they report to meet regulatory requirements, other mandatory obligations or on a voluntary basis? What are the relevant rules? What are the trickle-down effects of mandatory reporting requirements applicable for large entities, into disclosure requests towards SMEs along the supply chain? Is external assurance required, and if so, which level?

(ii) **Company reporting**

How many companies and which companies report? Under which context, in which sectors and of which size? Is there uniform reporting across industries/countries?

(iii) **Frameworks, standards and guidance**

What are the frameworks, standards and guidance most frequently used to produce non-financial information and by what type of companies? Do companies use single or multiple references to fit their needs?

b) How is non-financial information **provided**? This question focused on:

(i) **Classification/taxonomy**

How is the information classified? Is a specific taxonomy applied?

(ii) **Format**

How is the information reported? Do companies use special platforms, websites, registration document filings or other formats?

(iii) **Location**

Where is non-financial information found in companies' publications (combined management report with financial report, separate sustainability report, registration documents, elsewhere…)?

(iv) **Technology**

What kind of technology is used to provide non-financial information? What is the progress of digitisation in non-financial reporting? Does digitisation play an important role?

Additional comment: Digitisation is a way of submitting content. How to improve and expand its use is an essential consideration for improvement of non-financial reporting, but the pressing need is about format: Where does the digitised content go? How was it produced? Is it verifiable?

c) What **challenges** are faced when producing or using the provided non-financial information, both from a preparer and a user perspective with focus on:

(i) **Content:** What are the issues faced with what is reported?

(ii) **Structure:** How is non-financial information reported?

(iii) **Technology:** What are the means used to report non-financial information?

Approach

11 Stream A6 conducted its assessment through a desktop review of relevant publicly available literature and data analysis. As such, most statements in this assessment report reflect the content of this literature and data analysis. These statements are synthesised and summarised into salient observations, for the Stream A6 own assessment and conclusion.

12 The full list of documents reviewed is provided in the Appendix to this assessment report. The most relevant sources for the information included in this assessment report were the following:

a) An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, Alliance for Corporate Transparency (2019). This document has been used as the primary source of information throughout the document, as it contains detailed data research on a significant number of companies under the NFRD scope, and its structure is aligned with the NFRD.

b) Carrots & Sticks – Sustainability reporting policy: Global trends in disclosure as the ESG agenda goes mainstream, GRI and University of Stellenbosch Business School (2020)

c) Insights into integrated reporting 4.0: The story so far, ACCA (2020)

d) Member State Implementation of Directive 2014/95/EU – A comprehensive overview of how Member States are implementing the EU Directive on Non-financial and Diversity Information & Spain update, Accountancy Europe (2017 & 2019)

e) Towards reliable non-financial information across Europe, Accountancy Europe (2020)

f) Falling short? Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve, CDSB (2020)

g) Enforcement and regulatory activities of European enforcers in 2019, ESMA (2020)

h) La Dichiarazione Non Finanziaria: la risposta delle aziende europee ed italiane, EY (2018)

i) Non-Financial Reporting in Italian SMEs: An Exploratory Study on Strategic and Cultural Motivations, International Journal of Business Administration, Vol. 5, No. 3, Donato Calace (2014)

j) A digital transformation brief: Business reporting in the fourth industrial revolution. IMA (2020)

SECTION 1: HOW NON-FINANCIAL INFORMATION IS PRODUCED

13 Non-financial reporting is mandated and/or shaped by specific legislation and by the rules of various bodies, from public agencies to stock exchanges. This contributes to a complex context that drives non-financial reporting diversity.

14 The first aspect of the Stream A6 assessment involved research on how non-financial information is produced by preparers. The assessment addressed the matter from three different angles, namely regulatory and/or voluntary context, company reporting and frameworks/standards/guidance used.

Regulatory/voluntary context

QUESTION 1.1:
What is the context (regulatory/voluntary) in which non-financial information is developed?

15 Based on information included in two reports published by Accountancy Europe[2,3] (hereafter 'the Accountancy Europe reports'), the countries in Europe where non-financial reporting is required by law, regulation or is otherwise mandatory are listed below:

a) **EU27[4]:** Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden;

b) **Europe (other than EU27)[5]:** United Kingdom, Iceland, Norway, Russia, Liechtenstein.

2 Member State Implementation of Directive 2014/95/EU – A comprehensive overview of how Member States are implementing the EU Directive on Non-financial and Diversity Information & Spain update, Accountancy Europe (2017 & 2019)

3 Towards reliable non-financial information across Europe, Accountancy Europe (2020)

4 In Croatia, Cyprus and Ireland the European enforcer does not have powers relating to the non-financial statement.

5 In Norway, the Accounting Directive, including Articles 19a and 29a, is not yet finally transposed into national legislation.

16 According to the Accountancy Europe reports and a study by EY Italy[6] all EU countries have already transposed the NFRD and have enacted legislation regarding non-financial reporting. Tables 1 and 2 below include the main relevant applicable laws:

Table 1: Regulatory requirements in EU27

COUNTRY	REGULATORY REQUIREMENT
Austria	Act. 257 / ME of 06 /12/2016
Belgium	Amd. 2564 of 03/09/2017
Bulgaria	Amd. 237 of 06/06/2017
Croatia	Amd. 51 of 12/12/2016
Cyprus	Amd. 3 of 19/05/2017
Czech Republic	Amd. 462 of 14/12/2016
Denmark	Stat. Act Amd. of 21/05/2015
Estonia	Acc. Act Amd. of 10/12/2015
Finland	Amd. 1376/2016 and 1441/2016
France	Art. L225-102-1 of 19/07/2017
Germany	CSR-Rich.-Umsetzug. of 11/04/2017
Greece	Law 4403/2016 of 07/07/2016
Hungary	Amd. Act C of 2000 on Accounting of 15/05/2016
Ireland	S.I, 360 of 30/07/2017
Italy	D.Lgs. 254/2016 of 30/12/2016
Latvia	Law 2016/254.4 of 29/12/2016
Lithuania	Amd. XIII-94 of 15/12/2016
Luxembourg	Law A156 of 29/ 07/2016
Malta	Act CAP 386 of 12/02/2016
Netherlands	L33014 / 03/2017
Poland	Amd. Act 61 of 15/12/2016
Portugal	D. Lei n. 89/2017 of 21/08/2017
Romania	Ord. 1.938 of 17/08/2016
Slovakia	Amd. Act 130/2015 of 06/05/2015
Slovenia	Amd. ZGD-1J of 29/03/2017
Spain	R.D. Ley 11/2018 of 28/12/2018
Sweden	2016/17:CU2 of 25/10/2016

Sources: Member State Implementation of Directive 2014/95/EU – A comprehensive overview of how Member States are implementing the EU Directive on Non-financial and Diversity Information & Spain update, Accountancy Europe (2017 & 2019); Towards reliable non-financial information across Europe, Accountancy Europe (2020); La Dichiarazione Non Finanziaria: la risposta delle aziende europee ed italiane, EY (2018)

6 La Dichiarazione Non Finanziaria: la risposta delle aziende europee ed italiane, EY (2018)

Table 2: Regulatory requirements in Europe (other than EU27)

COUNTRY	REGULATORY REQUIREMENT
United Kingdom	Regulation No. 1245 of 19/12/2016
Iceland	Amd. Acc. Act 3/2006 of 26/01/2006
Norway	Draft law (Norway has not official transposed the Directive 2014/95/EU)
Russia	Law n. 876-r of 5/05/2017
Liechtenstein	Bua 58/2016 of 3/05/2016

Sources: Member State Implementation of Directive 2014/95/EU – A comprehensive overview of how Member States are implementing the EU Directive on Non-financial and Diversity Information & Spain update, Accountancy Europe (2017 & 2019); Towards reliable non-financial information across Europe, Accountancy Europe (2020)

17 Most of the NFRD provisions have been similarly transposed by EU Member States. However, there is a significant degree of implementation diversity at national level, as the transposition of the NFRD has been significantly adapted on certain matters. These adaptations include which companies are subject to non-financial reporting regulatory requirements, the definition of public interest entities (PIEs), disclosure formats and non-compliance penalties. Figure 1 summarises the implementation of the NFRD by EU Member States according to the Accountancy Europe reports.

Figure 1: Summary of implementation of NFRD by EU Member States

	Definition of a large undertaking	Definition of a public interest entity	Report topics and content	Reporting framework	Disclosure format	Auditor's involvement	Non-compliance penalties	Safe harbour principle	Diversity reporting required
Similar application	18	5	19	21	6	19	0	23	19
Adapted application	9	22	8	6	21	8	24	0	8
Omitted application	0	0	0	0	0	0	3	4	0
Member States total	**27**	**27**	**27**	**27**	**27**	**27**	**27**	**27**	**27**

Sources: Member State Implementation of Directive 2014/95/EU – A comprehensive overview of how Member States are implementing the EU Directive on Non-financial and Diversity Information & Spain update, Accountancy Europe (2017 & 2019)

Which companies are subject to non-financial reporting regulatory requirements?

18 EU Member States have different definitions for what constitutes large undertakings subject to non-financial reporting obligations. Based on information in the Accountancy Europe reports, the companies subject to non-financial reporting regulatory requirements in Europe are determined by dimensional criteria as set out in Table 3 (EU27) and Table 4 (other than EU27), based on 2017 and 2019 data.

Table 3: Non-financial reporting dimensional criteria in EU27

DIMENSIONAL CRITERIA IN EU27			
COUNTRY	**EMPLOYEES (NUMBER)**	**NET TURNOVER (EUR MILLION)**	**BALANCE SHEET (EUR MILLION)**
Austria	500	40	20
Belgium	500	34	17
Bulgaria	500	76 (BGN)	38 (BGN)
Croatia	500	30 (HRK)	15 (HRK)
Cyprus	500	40	20
Czech Republic	500	1000 (CZK)	Not applicable
Denmark	250	313 (DKK)	156 (DKK)
Estonia	500	40	20
Finland	500	40	20
France	500	40	20
Germany	500	40	20
Greece	500	Not applicable	Not applicable
Hungary	500	12000 (HUF)	6000 (HUF)
Ireland	500	40	20
Italy	500	40	20
Latvia	500	40	20
Lithuania	500	40	20
Luxembourg	500	40	20
Malta	500	40	20
Netherlands	500	40	20
Poland	500	170 (PLN)	85 (PLN)
Portugal	500	40	20
Romania	500	Not applicable	Not applicable
Slovakia	500	40	20
Slovenia	500	40	20
Spain	500	40	20
Sweden	250	350 (SEK)	175 (SEK)

Sources: Member State Implementation of Directive 2014/95/EU – A comprehensive overview of how Member States are implementing the EU Directive on Non-financial and Diversity Information & Spain update, Accountancy Europe (2017 & 2019)

Table 4: Non-financial reporting dimensional criteria in Europe (other than EU27)

	DIMENSIONAL CRITERIA IN EU27		
COUNTRY	EMPLOYEES (NUMBER)	NET TURNOVER (EUR MILLION)	BALANCE SHEET (EUR MILLION)
United Kingdom	500	Not applicable	Not applicable
Iceland	250	6000 (ISK)	3000 (ISK)
Norway	500	40	20
Russia[7]	Not applicable	Not applicable	Not applicable
Liechtenstein	500	Not applicable	Not applicable

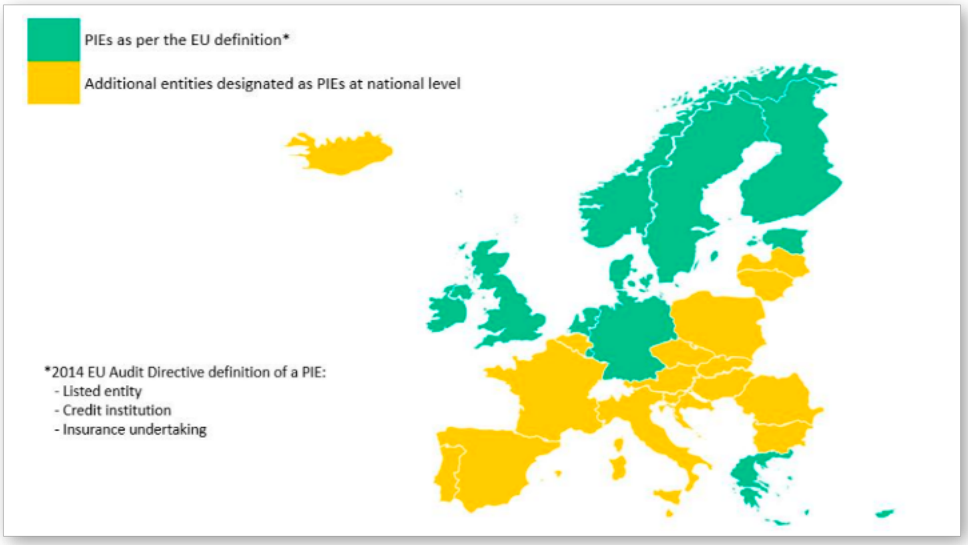
Sources: Member State Implementation of Directive 2014/95/EU – A comprehensive overview of how Member States are implementing the EU Directive on Non-financial and Diversity Information & Spain update, Accountancy Europe (2017 & 2019)

Definition of PIEs

19 Another report published by Accountancy Europe *'Definition of Public Interest Entities in Europe'*[8], shows that EU Member States also have different definitions for what constitutes PIEs.

20 There is a wide diversity of definitions of PIEs applicable across European countries. While some countries have implemented the minimum requirements, others, implicitly or explicitly, set a broader PIE definition, extending the scope of the definition to entities such investment companies, large non-listed companies according to specific size criteria, state-owned companies, pension funds etc. In other countries (including France, Slovenia, Sweden and the UK), there is no explicit definition of PIEs included in the local law. Instead, groupings of types of entities have been determined on which different requirements apply.

Figure 2: Overview of PIE definition in Europe



Source: Definition of Public Interest Entities in Europe, Accountancy Europe (2017, updated 2019) – page 6

7 In Russia dimensional criteria seem to be modulated based on different time periods.

8 Definition of Public Interest Entities in Europe, Accountancy Europe (2017, updated 2019)

Disclosure formats and non-compliance penalties

21 Based on information included in the Accountancy Europe reports[9,10] and the previously mentioned study by EY Italy[11], in some countries, as set out in Table 5, specific provisions are included in national law relating to disclosure formats and non-compliance penalties.

Table 5: Summary of specific disclosure provisions in Europe

DISCLOSURE PROVISIONS	COUNTRIES	NUMBER[12]
Specific sanctions for non-reporting	Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Latvia, Lithuania, Luxemburg, Malta, Norway, Poland, Portugal, Romania, Slovakia, Slovenia, Sweden, United Kingdom	27 out of 30
Distinct publication not allowed	Estonia, France, Greece, Hungary, Malta, Netherlands, Slovakia, United Kingdom.	8 out of 30
Reporting framework integrated/ limited	Bulgaria, Denmark, Italy, Poland, Slovakia, Spain	6 out of 30

Sources: Member State Implementation of Directive 2014/95/EU – A comprehensive overview of how Member States are implementing the EU Directive on Non-financial and Diversity Information & Spain update, Accountancy Europe (2017 & 2019); Towards reliable non-financial information across Europe, Accountancy Europe (2020); La Dichiarazione Non Finanziaria: la risposta delle aziende europee ed italiane, EY (2018)

22 In addition to specific non-financial reporting regulatory requirements, some stock exchanges have issued rules and guidance regarding non-financial information reporting. An estimated 64% of EU stock exchanges have published written guidance on environmental, social and governance (ESG) reporting while 73% provide an SME listing platform[13].

Involvement of auditors or other assurance providers

23 National regulatory requirements also differ significantly in respect of provisions relating to the involvement of auditors and assurance over reported non-financial information. A factsheet published by Accountancy Europe *'Towards reliable non-financial information across Europe'*[14] shows that out of the 26 European countries covered (as of February 2020):

a) 12 countries apply the minimum requirement for the statutory auditors to check whether non-financial information has been provided;

b) 11 countries include an additional requirement for the auditors to check the consistency of non-financial information reported with the financial statements;

c) 3 countries opted for mandatory independent assurance of the non-financial information reported; and

d) 14 countries opted for voluntary independent assurance.

9 Member State Implementation of Directive 2014/95/EU – A comprehensive overview of how Member States are implementing the EU Directive on Non-financial and Diversity Information & Spain update, Accountancy Europe (2017 & 2019)

10 Towards reliable non-financial information across Europe, Accountancy Europe (2020)

11 La Dichiarazione Non Finanziaria: la risposta delle aziende europee ed italiane, EY (2018)

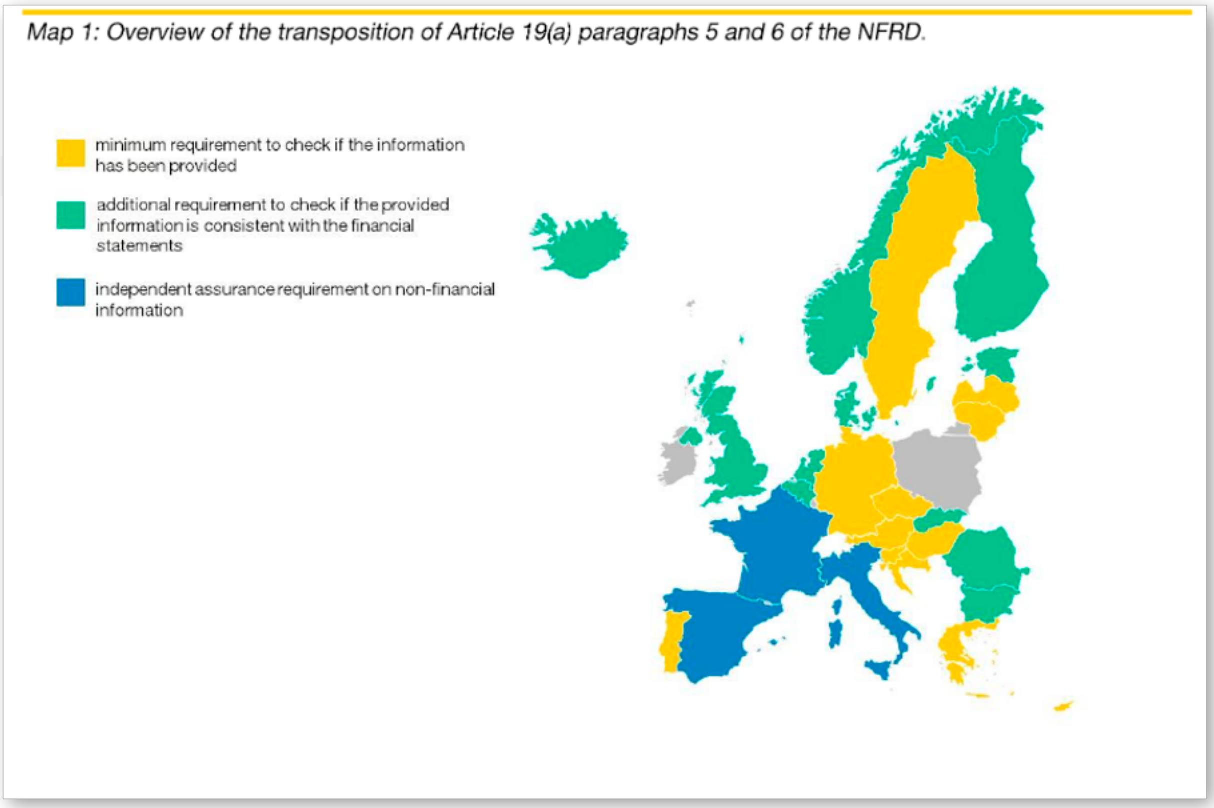
12 Russia and Liechtenstein are excluded from the analysis since relevant data is not available.

13 Source: https://sseinitiative.org/

14 Towards reliable non-financial information across Europe, Accountancy Europe (2020)

24 The map in Figure 3 from the Accountancy Europe factsheet[15] highlights the assurance requirements in force in different countries.

Figure 3: Overview of requirements for assurance over reported non-financial information in Europe



Source: [Towards reliable non-financial information across Europe](), Accountancy Europe (2020) – page 2

25 While it might be reasonably assumed that consistency checks and assurance requirements lead to higher levels of completeness, consistency and quality in non-financial information reporting, Stream A6 was not able to identify published research in this respect establishing whether such correlation currently exists.

QUESTION 1.2:

How many companies report to meet regulatory requirements or other mandatory obligations on a voluntary basis?

26 While many companies in the EU are subject to non-financial reporting laws and regulations, that number falls significantly short of the entire population of companies of the respective size. In particular:

a) EU rules on non-financial reporting cover approximately 6 000 large companies and groups across the EU[16], compared to a total of 38 368 large companies and of 16 616 PIEs in the EU (2017)[17].

b) Stock exchange regulations apply to a total of 7 770 listed companies in the EU, and only 6 300 of these (81%), possibly including SMEs, cover sustainability reporting in some way in their annual filings (2019)[18].

15 Towards reliable non-financial information across Europe, Accountancy Europe (2020)

16 Source: https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/non-financial-reporting_en#overview

17 Source: Eurostat

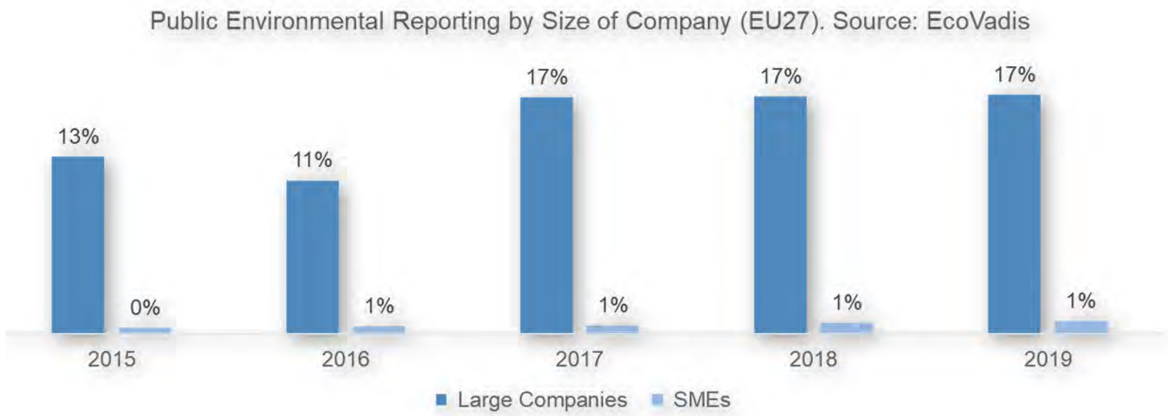
18 Source: https://sseinitiative.org/

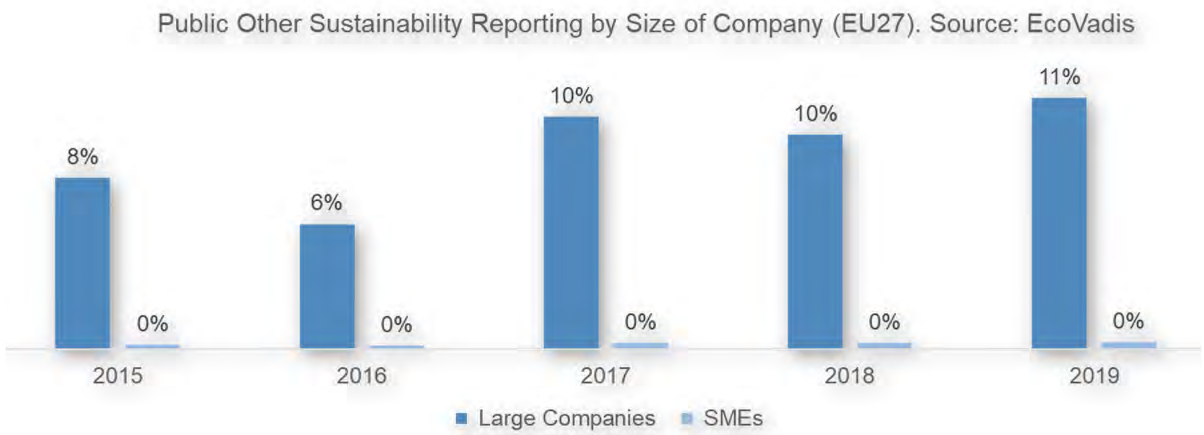
27 Only a limited number of companies disclose (on a mandatory or voluntary basis) non-financial information today. In fact, the number of companies, particularly SMEs, disclosing information in accordance with non-financial regulation is not known.

28 Public disclosure on sustainability topics is limited even amongst large companies. This is driven by the fact that many large companies fall outside the scope of the NFRD in the EU. In the absence of official figures, Stream A6 has sourced relevant non-financial information reporting data from analytics and ratings firms.

29 The information presented as Figure 4 below was obtained from Ecovadis[19]. For considering this information it should be emphasised that Ecovadis uses different size definitions to the NFRD[20]:

Figure 4: % of companies publicly disclosing sustainability information





Source: Ecovadis

19 Ecovadis is a sustainability ratings platform that assesses corporate social responsibility and sustainable procurement and that contains data from more than 65 000 companies globally.

20 Ecovadis define company size using the following criteria:
- SMEs: up to 999 employees;
- Large companies: more than 1000 employees.

QUESTION 1.3:

What are the frameworks/standards/guidance most frequently used to produce non-financial information and by what type of companies?

30 Reporting entities rely on many different initiatives, local and international, generic or industry/topic based for their non-financial information disclosures. The NFRD explicitly references some of these.

31 The most relevant frameworks, standards and guidance used to support the production of non-financial information, are shown in Table 6 below. The source of the data used to arrive at the percentage numbers disclosed in Table 6 are the Alliance for Corporate Transparency 2019 Research Report *'An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive'*[21] (hereafter the "2019 ACT report") and a report published by ACCA *'Insights Into Integrated Reporting 4.0: The Story So Far'*[22].

Table 6: Most used frameworks/standards/guidance

FRAMEWORKS/STANDARDS/GUIDANCE	NUMBER OF PREPARERS THAT USE THEM[23]
National standards, including the national transposition of the EU NFRD	53%
Global Reporting Initiative (GRI) Standards	54%
United Nation Global Compact (UNGC) – Sustainable Development Goals (SDGs)	39%
Task Force on Climate-related Financial Disclosures (TCFD) – TCFD Recommenda-tion	38%
United Nation Global Compact (UNGC) – UNGC Guidelines/Framework	37%
International Labour Organization (ILO) – ILO Guidelines and Standards (e.g. Labour Standards)	28%
Carbon Disclosure Project (CDP) – CDP Guidance	17%
Organisation for Economic Co-Operation and Development (OECD) – OECD Guide-lines	17%
United Nation Global Principles (UNGP) – UN Guiding Principles Reporting Framework	9%
International Integrated Reporting Council (IIRC) – The International Integrated Re-porting Framework (IIRF). This is mainly related to financial information.	6%
International Organization for Standardization (ISO) – ISO 26000 – Social Responsibil-ity Guidance Standard	5%
European Commission – Guidelines on non-financial reporting	5%
Sustainability Accounting Standards Board (SASB) – Sustainability Accounting Stand-ards (77 industry-specific)	3%
Climate Disclosure Standards Board (CDSB) – Framework for reporting environmental and climate change information	1%
Others	40%

Sources: Insights Into Integrated Reporting 4.0: The Story So Far, ACCA (2020); An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)

32 From Table 6, it can be seen that many companies use more than three frameworks/standards/guidance, mostly in a global context. It can also be reasonably deduced that these standards are complementary to each other, with some of them being generic while others are topic or sector specific.

21 An analysis of the sustainability reports of 1,000 companies pursuant to the EU Non-Financial Reporting Directive, Alliance for Corporate Transparency (2019)

22 Insights Into Integrated Reporting 4.0: The Story So Far, ACCA (2020)

23 Average figure using data from the two reports mentioned in footnotes 26 and 27

SECTION 2: HOW NON-FINANCIAL INFORMATION IS PROVIDED

33 The second aspect of the Stream A6 assessment involved research on how non-financial information is provided. The assessment addressed the matter from four different perspectives, namely classification, location, format, and technology.

Classification

QUESTION 2.1:
What topics are most reported upon and by what types of entities?

34 This question requires both an evaluation of the non-financial reporting topics dealt with companies and the degree to which the disclosure has been addressed. Considering this from several possible classification angles, the assessment was structured by following the topic classification and level of disclosure as articulated in the NFRD.

35 The 2019 ACT report[24] forms the backbone of this analysis. Where possible, this was supplemented with additional data from other sources, and in particular with TCFD data on climate-related disclosures.

36 In the 2019 ACT report, topics are presented under the NFRD classification in the following way:

Table 7: 2019 ACT report classification of topics

CATEGORY	SUBCATEGORY
Environment	Climate change
	Use of natural resources
	Polluting discharges
	Waste
	Biodiversity and ecosystem conservation
Employee and social matters	Employees and workforce
	Social matters
Human rights	General human rights reporting criteria
	Human rights in supply chains
	High risk areas for civil and political rights
	Impacts on indigenous and local communities
	Conflict resources
	Data protection
Anti-corruption and whistleblowing	Anti-corruption
	Whistleblowing channels
General positive impacts	General and sectorial positive impacts by prod-ucts/sources of opportunity

Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)

24 An analysis of the sustainability reports of 1,000 companies pursuant to the EU Non-Financial Reporting Directive, Alliance for Corporate Transparency (2019)

37 As regards the level of disclosure on NFRD topics, the 2019 ACT report, presents information as set out in Table 8.

Table 8: Presentation of level of disclosure on NFRD topics in 2019 ACT report

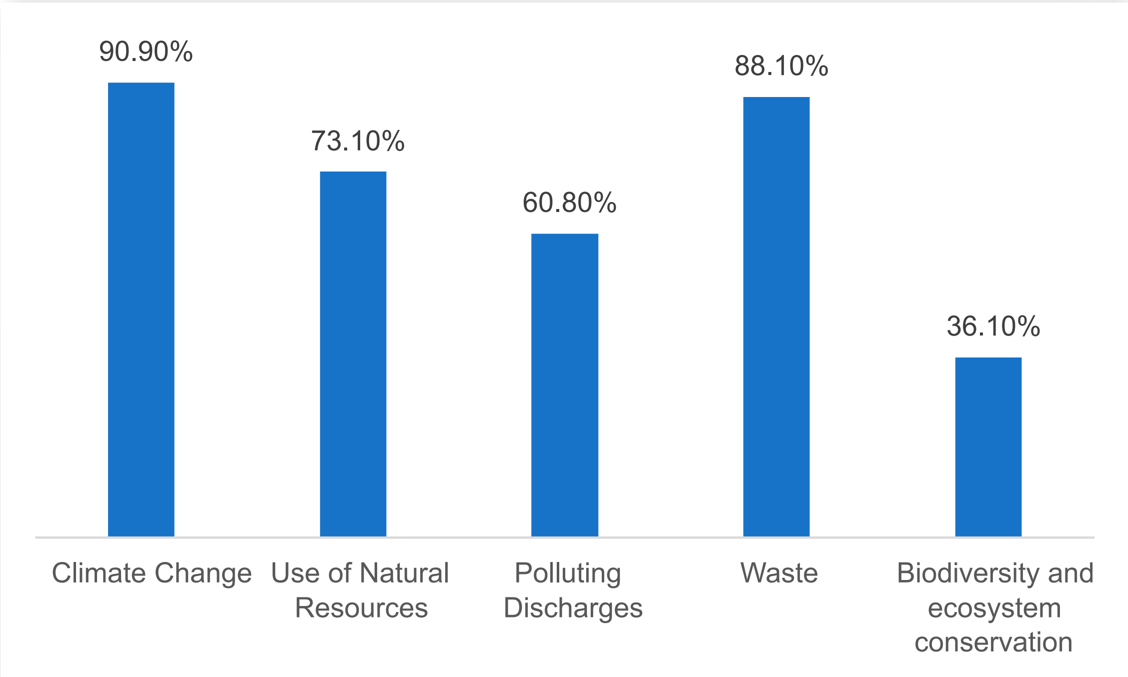
Policies and procedures	Policy description specifies key issues and objectives	Policy is described or referenced	No information provided
Risks management	Description of specific risks	Vague risks identification	No risks identification
Outcomes	Outcomes in terms of meeting policy targets	Description provided	No description

Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)

Environment

38 Figure 5 is sourced from the 2019 ACT report. This illustrates the proportion of companies providing disclosures for the different environment-related topics, based on a sample of 1 000 companies.

Figure 5: Proportion of companies addressing environmental issues in their annual reports



Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)

39 The 2019 ACT report finds that a great majority of companies address climate change in their disclosure (90,9%). This could reflect the increased demands in recent years from investors and other stakeholders for disclosure around climate risk, whether due to mandatory requirements or voluntary reporting initiatives. Climate risk has been a focus of established reporting standards, frameworks and principles including GRI, CDP and CDSB, as well as the NFRD.

40 Disclosure on waste is the second most frequent topic, but with varying levels of disclosure provided, as shown later in paragraph 66.

41 The 2019 ACT report indicates that only a minority of companies cover biodiversity and ecosystem conservation in their reports, as further elaborated in paragraph 67.

42 This conclusion on biodiversity and ecosystem conservation, however, is not consistent across all sectors, as companies in certain high-risk sectors such as the Energy & Resource Extraction and Infrastructure, typically do provide such disclosure. Yet, in other high-risk sectors such as Apparel & Textiles, Hospitality & Recreation and Food & Beverages, the percentage of companies disclosing on this topic is strikingly low.

43 Size emerges as a key criterion for environmental disclosures, as the proportion of companies providing relevant disclosures increases for all climate change topics as turnover increases. This is shown in Table 9.

Table 9: Number of companies addressing climate change by revenue size

	< EUR 300 MILLION	EUR 300 MILLION – EUR 1 BILLION	EUR 1 BILLION – EUR 3 BILLION	EUR 3 BILLION – EUR 20 BILLION	> EUR 20 BILLION
Climate change	73%	92%	97%	98%	100%
Use of natural resources	59%	69%	75%	83%	91%
Polluting discharges	40%	49%	56%	60%	72%
Waste	67%	73%	81%	82%	89%
Biodiversity and ecosystem conservation	20%	25%	34%	44%	62%

Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)

Climate change

44 The European Commission issued non-binding guidelines on climate-related reporting in June 2019[25]. This guidance aims to provide companies with recommendations on how to better report the impact of their activities on climate, whilst also providing meaningful disclosures on the impacts of climate change on their business. These guidelines integrate the TCFD recommendations as the de facto framework on climate-related disclosures. The guidelines include 85 provisions which explicitly address climate-related matters; while 42 address pollution, waste and hazardous substances; 33 cover environmental compliance and risks; and 30 refer to water.

25 Guidelines on non-financial reporting: Supplement on reporting climate-related information, European Commission (2019)

45 Figure 6 shows the proportion of companies addressing climate change and their corresponding level of disclosure, based on the 1 000 company sample analysed by the 2019 ACT report.

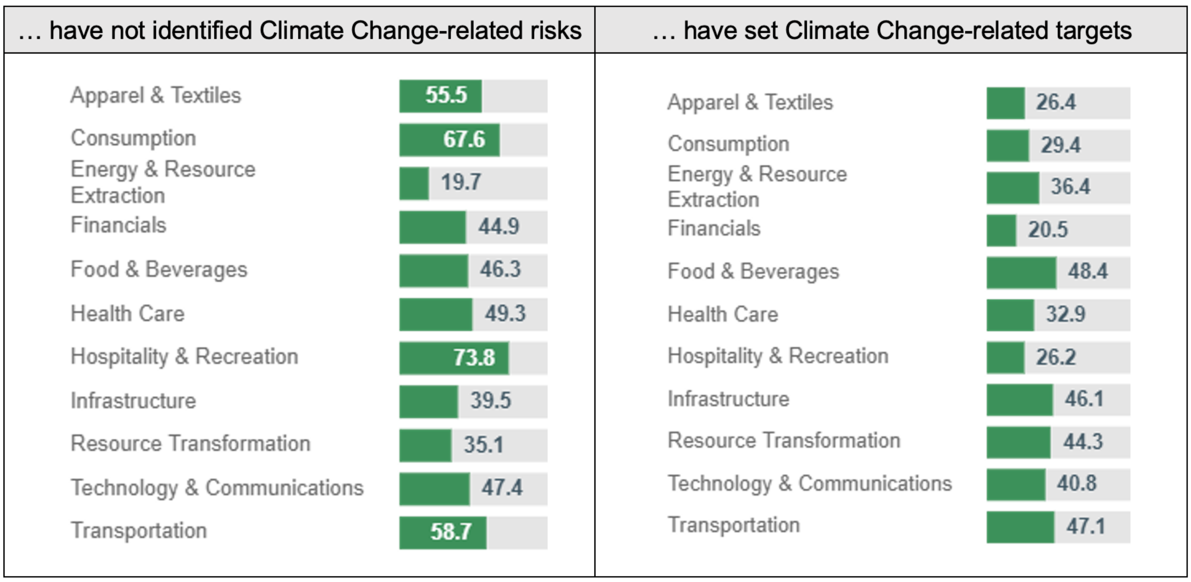
Figure 6: Proportion of companies addressing climate change by level of disclosure

Source: [An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive](), The Alliance for Corporate Transparency (2019)

46 This research found that 82% of companies already report on climate change-related policies while more than 70% address outcomes in this category to some degree.

47 However, as shown in Figure 7, significant differences are observed by industry on certain key issues such as setting targets or identifying risks.

Figure 7: % of companies in the different industries that...



Source: [An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive](), The Alliance for Corporate Transparency (2019)

48 In its 2020 report *'Falling short? Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve'*[26], the CDSB identified the top 3 strengths of disclosure, demonstrating a clear pattern in areas of good practice. In this report the CDSB reviewed the 2019 environmental and climate-related disclosures of Europe's 50 largest listed companies, with a combined market capitalisation of USD 4.3 trillion, under the NFRD. It

26 Falling short? Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve, CDSB (2020)

identified the following three areas as strength categories: (i) key performance indicators (KPIs), (ii) policies and due diligence, and (iii) business model.

49 For some of the companies in the CDSB sample, KPIs were one of the most mature aspects of their non-financial disclosure, however it was also an element where substantive variation in quality was observed.

50 All companies in the CDSB review sample disclosed climate or environmental KPIs, with the most frequently reported metrics being (i) greenhouse gas (GHG) emissions (100%), (ii) water consumption, withdrawals or intensity (88%), and (iii) energy consumption, intensity or generation (86%).

51 Overall, policies and due diligence were among the most consistent areas of environmental and climate-related disclosures, with 100% of companies describing their policies and 94% disclosing their due diligence arrangements. Although almost all companies disclosed these content categories, significant variation in the extent and quality of disclosures was observed. As ‘policies’ and ‘due diligence’ are not defined within the NFRD, there was variation in how companies interpreted these terms.

52 88% of the companies reviewed by CDSB disclosed some environmental and climate-related aspects of their business model, however only one-third did so in a manner that addressed the key aspects outlined in the guidelines to the NFRD.

53 In the 2020 status report of the TCFD[27] (hereafter ‘the 2020 TCFD status report’), it was noted that nearly 60% of the world’s 100 largest public companies supported the TCFD, reported in line with the TCFD recommendations[28], or both. This 2020 TCFD status report noted that disclosure of climate-related financial information, aligned with the TCFD recommendations, had steadily increased since the recommendations were published in 2017. The report also noted a continued need for progress given the urgent demand for consistency and comparability in reporting.

54 More specifically, the 2020 TCFD status report, which provides findings from the review of financial filings, annual reports, integrated reports, and sustainability reports of 1 701 public companies from 69 countries across eight industries, highlights that:

a) 42% of companies with a market capitalisation greater than USD 10 billion disclosed at least some information in line with each individual TCFD recommendation in 2019.

b) Approximately 60% of the world’s 100 largest public companies support the TCFD, report in line with the TCFD recommendations, or both.

c) Energy companies, and Materials and Buildings companies, are leading on disclosure, with an average level of TCFD-aligned disclosures of 40% for Energy companies and 30% for Materials and Buildings companies in fiscal year 2019.

d) Expert users of disclosure identified the impact of climate change on a company’s business and strategy as the ‘most useful’ information for financial decision-making. Notably, this information has the lowest level of disclosure across the recommendations, with just one in 15 companies providing this disclosure.

55 Disclosure of climate-related information has increased since 2017 both in terms of the number of companies reporting and the quality of such reporting. However, companies’ disclosure of the potential financial impact of climate change on their businesses, strategies, and financial planning remains low.

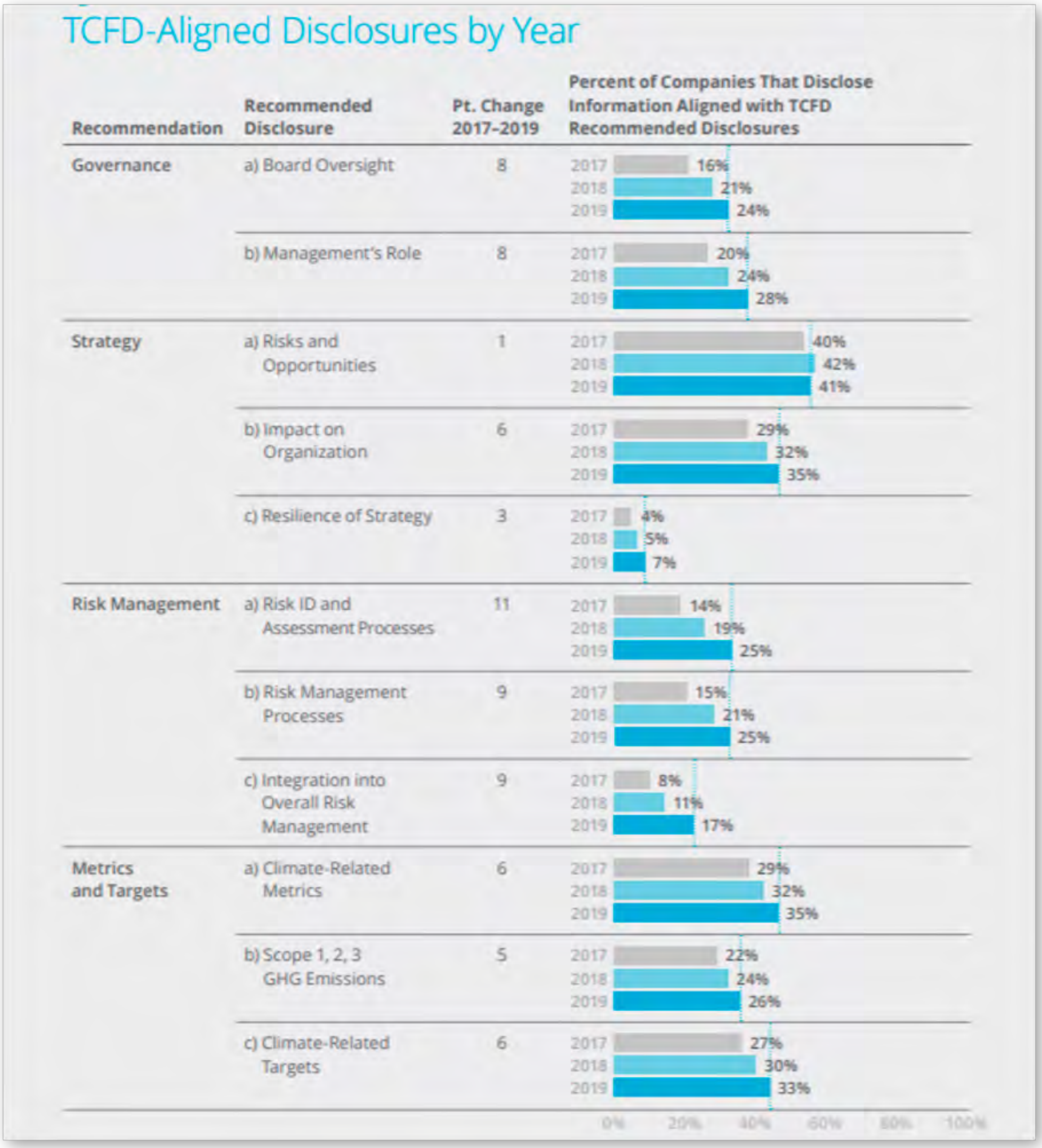
56 As shown in Figure 8 below, the greatest increase in the percentage of companies disclosing relevant information from 2017 to 2019 – 11 percentage points –relates to the disclosure of processes for identifying and assessing climate-related risks (TCFD recommendation: Risk Management a); whilst the smallest increase relates to the disclosure of companies’ climate-related risks and opportunities (TCFD recommendation: Strategy a), which increased by only one percentage point over the same time period. Additionally, while the percentage of disclosure for the five recommended disclosures

27 2020 Status Report: Task Force on Climate-related Financial Disclosures, TCFD (2020)

28 TCFD Recommendations, TCFD (2017)

related to governance and risk management is low, the percentage point increases for those five recommended disclosures are higher than the increases for the recommended disclosures related to strategy and metrics and targets.

Figure 8: Percentage of companies that disclosed information aligned with TCFD recommended disclosures in 2019



Source: 2020 Status Report: Task Force on Climate-related Financial Disclosures, TCFD (2020) – page 11

57 The review for the TCFD 2020 status report found that, on average, information aligned with the recommended disclosures was more likely to be disclosed in sustainability reports than in financial filings or annual reports. However, disclosure of climate-related risks and opportunities was nearly as likely to be found in financial filings or annual reports as it was in sustainability reports. In the case of metrics and targets, the review found that 79% of sustainability reports included information aligned with recommended disclosures for metrics and targets, compared to only 15% of annual reports and financial filings containing the equivalent information.

58 One in 15 companies reviewed disclosed information on the resilience of its strategy. The review found that the percentage of companies disclosing the resilience of their strategies, taking into consideration different climate-related scenarios, including a 2°C or lower scenario, was significantly lower than that of any other recommended disclosure in

each year. These results are consistent with feedback which the TCFD has received from companies on the challenges of disclosing such information.

59 Companies' disclosure of their specific climate-related issues stayed constant, indicating that few companies have revised their perspective on whether climate-related risks and opportunities are appropriate for inclusion in public reporting.

60 The percentage of companies disclosing TCFD-aligned information tends to increase with company size. On average, 42% of companies with a market capitalisation of greater than USD 10 billion disclosed information aligned with the TCFD recommendations in 2019, while the average was 15% for companies with a market capitalisation less than USD 2.8 billion.

61 Companies in Europe were found to have the highest percentages of TCFD-aligned disclosures for 10 of the 11 recommended disclosures. This may, in part, be due to the integration of the TCFD recommendations in the non-binding guidelines on climate-related reporting published by the European Commission in June 2019[29]. The Asia Pacific region followed Europe with the second highest percentage of disclosure for 8 of the 11 recommended disclosures. While the North American region had the highest percentage of disclosure of climate-related risks and opportunities, the Latin America, Middle East and Africa, and North American regions otherwise had broadly similar percentages of disclosure across the recommended disclosures.

62 The conclusions of the TCFD 2020 status report were supported by research carried out by Moody's Analytics for a study which reviewed the climate-related disclosures of roughly 12 000 companies. According to the TCFD 2020 status report the Moody's Analytics study found that about 17% of the companies reviewed reported climate-related information. The TCFD 2020 status report further notes that Vigeo Eiris, an affiliate of Moody's, also conducted an independent analysis reviewing almost 3 000 companies across regions and sectors, and found that most companies lag in terms of fully aligning with the TCFD recommendations.

63 The TCFD 2020 status report analysed and ranked disclosures by industry (see Figure 9 below). A higher average percentage of disclosure indicates that an industry generally disclosed at a higher rate across the 11 recommended disclosures. Energy companies had the highest average at 40%, with the highest disclosure percentage for 9 of the 11 recommended disclosures, while Materials and Buildings companies had the highest percentage for 2 of the 11 recommendations. Consumer Goods and Technology and Media Companies had the lowest percentage of disclosure in several areas, with overall disclosure averages at 18% and 13%, respectively.

Figure 9: Average percentage of disclosure by industry

Average Percentage of Disclosure by Industry

Industry	%
Energy	40%
Materials and Buildings	30%
Insurance Companies	27%
Ag., Food, and Forest Products	25%
Banks	23%
Transportation	23%
Consumer Goods	18%
Technology and Media	13%

Source: 2020 Status Report: Task Force on Climate-related Financial Disclosures, TCFD (2020) – page 17

29 Guidelines on non-financial reporting: Supplement on reporting climate-related information, European Commission (2019)

Use of natural resources

64 The level of disclosure on the use of natural resources, according to the 2019 ACT report and based on the sample of 1 000 companies analysed, is shown in Figure 10 below.

Figure 10: Proportion of companies addressing use of natural resources by level of disclosure

Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)

Polluting discharges

65 The level of disclosure on polluting discharges, according to the 2019 ACT report and based on the sample of 1 000 companies analysed, is shown in Figure 11 below.

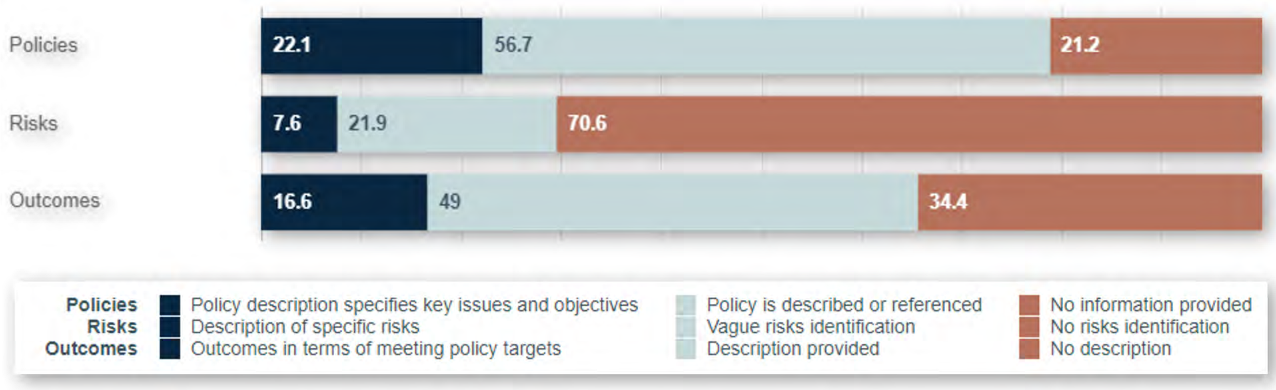
Figure 11: Proportion of companies addressing polluting discharges

Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)

Waste

66 The level of disclosure on waste, based on the sample of 1 000 companies analysed for the 2019 ACT report, is shown in Figure 12 below.

Figure 12: Proportion of companies addressing waste



Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)

Biodiversity and ecosystem conservation

67 The level of disclosure on biodiversity and ecosystem conservation, according to the 2019 ACT report and based on the sample of 1 000 companies analysed, is shown in Figure 13 below.

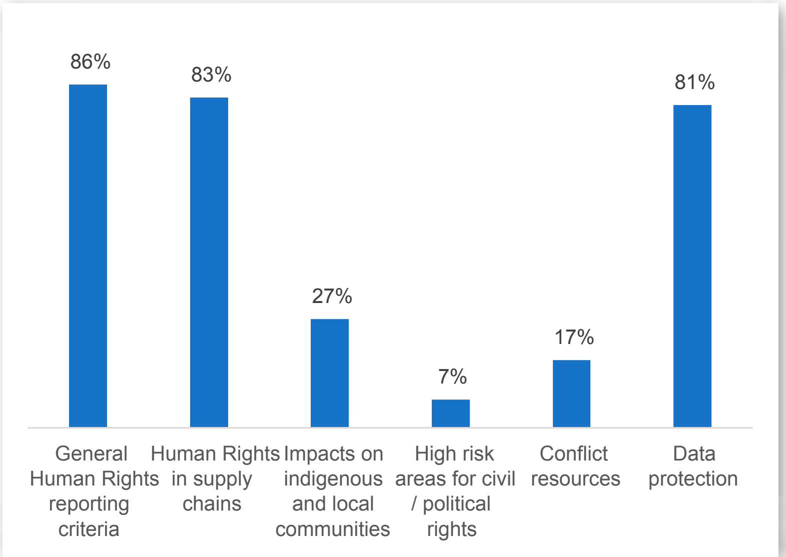
Figure 13: Proportion of companies addressing biodiversity and ecosystem conservation

Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)

Human rights

68 Significant differences can be found regarding disclosure of the different human rights issues, as shown in Figure 14 below prepared using information from the 2019 ACT report analysing the disclosures of a sample of 1 000 companies.

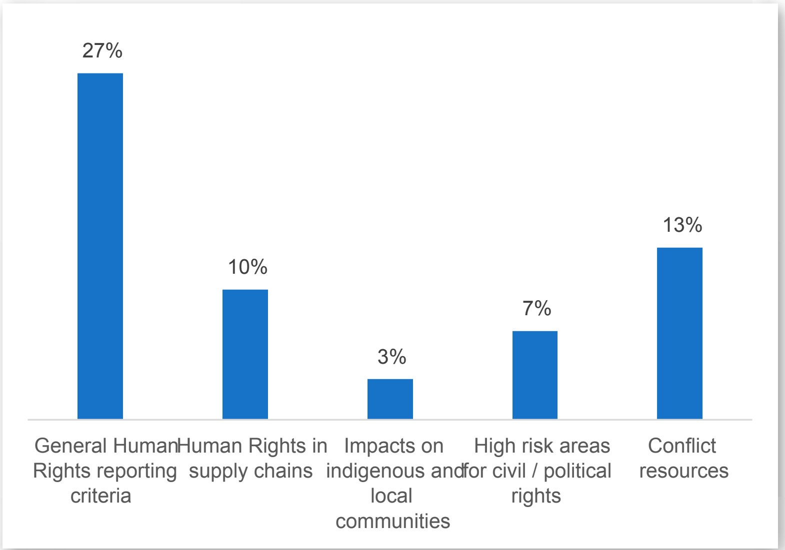
Figure 14: Proportion of companies addressing human rights issues in their annual reports



Source: *[An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive](), The Alliance for Corporate Transparency (2019)*

69 Given the discretionary nature of disclosing human rights issues, it is interesting to see how few companies consider any human rights dimension for disclosure purposes, particularly on topics that have a cross-sectoral impact, such as data protection of the supply chain. Figure 15 below was prepared using information from the 2019 ACT report.

Figure 15: Proportion of companies that identify salient human rights issues



Source: *An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)*

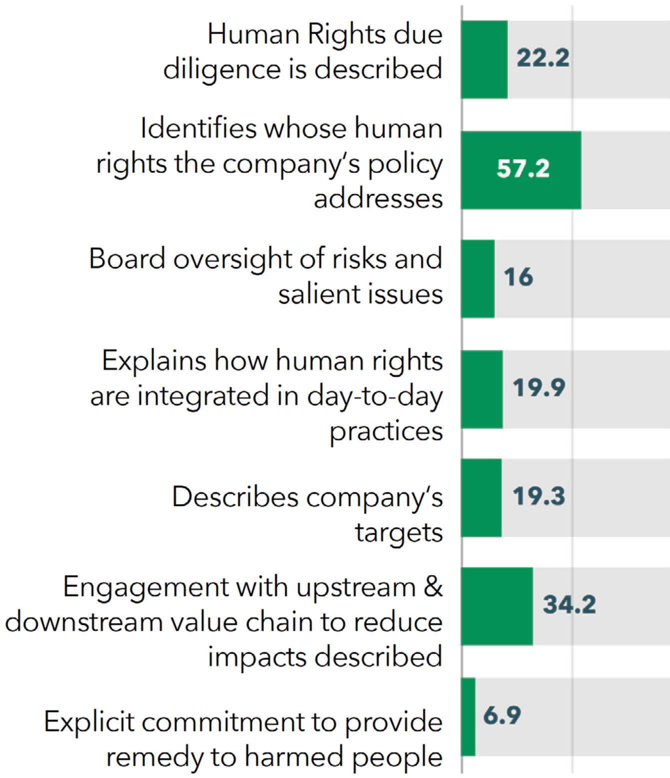
70 According to the 2019 ACT report, corporate disclosure on human rights is often narrative and case specific. Methodologies that allow to report on human rights in quantitative terms are not common, which in broad terms can be explained by the very nature of the matter, namely, that quantifying human rights issues and impacts is challenging.

71 For the purposes of the research leading to the 2019 ACT report, the methodology adopted for the assessment of human rights related disclosures focused on general criteria was derived from the UN Guiding Principles on Business and Human Rights Reporting Framework, concerning the identification of the salient human rights issues by companies and their management. It was stated that these criteria naturally fitted the categories of information the NFRD requires companies to report on, namely policies and due diligence procedures, outcomes, principal risks and KPIs. This approach leaves the choice of salient issues at the discretion of companies.

72 According to the research, most companies refer to and disclose policies on human rights, suggesting that many businesses view human rights as material. However relatively few companies disclosed relevant and specific details on policies.

73 An important finding included in the 2019 ACT report, based on the sample of 1 000 companies analysed, concerns disclosure on human rights due diligence. Only 22.2% of companies reported on due diligence processes and only 6.9% referred to their commitment to provide remedy for harmed people.

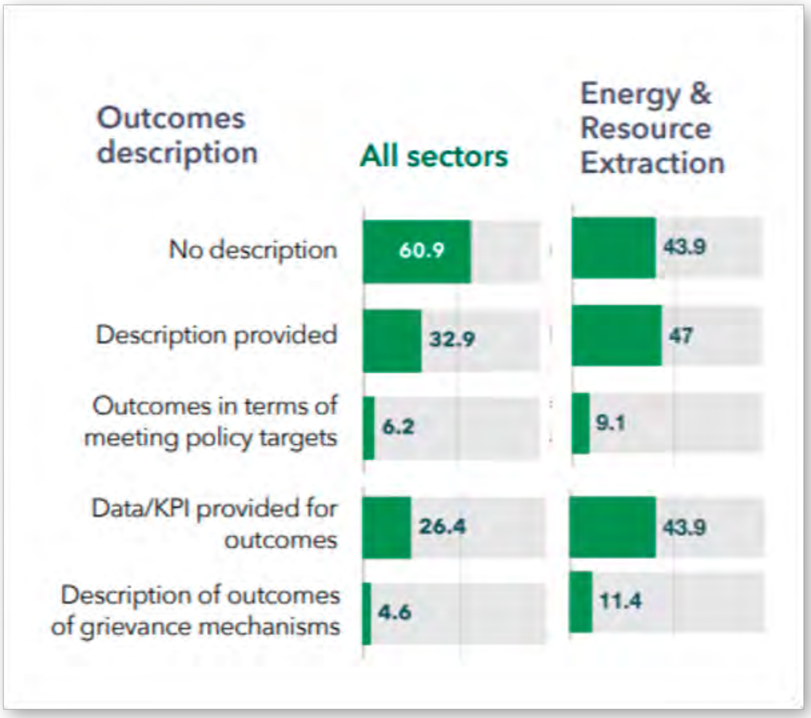
Figure 16: Disclosure on human rights due diligence



Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019) – page 19

74 The high percentage of companies reporting on human rights policies (over 80%) is in contrast with a much lower share describing policy outcomes (less than 40%, and only 6.2% with respect to policy targets). The fact that only 26.4% of companies report data or KPIs is more difficult to evaluate given the lack of methodologies to quantify human rights impacts and their management.

Figure 17: Description of policy outcomes



Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019) – page 69

75 A minority of companies address impacts on indigenous and/or local community rights across all sectors. However a different outcome is observed when reviewing the disclosures of companies on this topic in the Energy & Resource Extraction sector, where more companies refer to this issue in their reports.

76 The relevance of reporting on high risk areas for civil and political rights depends on a company's operational context. These risks are most often associated with the Energy & Resource Extraction sector. It is difficult to accurately estimate how many European companies operate in high-risk areas. The results provide a basic perspective on the level of awareness among businesses.

77 Only a small proportion of companies referred to high risk areas for civil and political rights in their reports and to a lesser extend identify high risk areas as a salient human rights issue. While a larger proportion of companies in the Energy & Resource Extraction sector addressed this issue in their reports, results in other sectors are lower still, including potentially high-risk sectors such as Technology & Communications, Apparel & Textiles, and Food & Beverages.

78 Conflict resources include conflict minerals covered by the EU Conflict Minerals Regulation – tin, tungsten, tantalum and gold – as well as other resources, such as timber. Technology & Communications and Resource Transformation are considered to be the two sectors most at risk of being linked to conflict minerals. The research behind the 2019 ACT report shows that most of the 1 000 companies reviewed did not cover the issue in their non-financial reporting, although a slightly higher number of companies in the Technology & Communications and Resource Transformation sectors reported on the topic.

Anti-corruption & Whistleblowing

79 According to the 2019 ACT report, anti-corruption issues are addressed by 96.4% of the sample of 1 000 companies reviewed, with similar results across industries.

80 Issues regarding whistleblowing have lower, but still significant coverage, with almost 77% of the sample of companies reviewed describing policies about this to some extent.

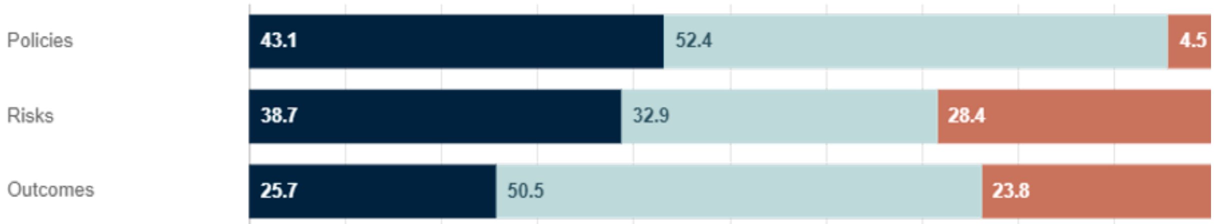
Social matters

81 The 2019 ACT report notes the difficulty in identifying concrete social issues that would not be classified as either a matter of respecting human rights or as employee-related matters as understood in the previous section.

82 To this end, the issues examined by the 2019 ACT report under the social matters umbrella are employee & workforce matters and taxes.

83 Employee & workforce matters are addressed by 98% of the sample of 1 000 companies analysed, to the degree shown in Figure 18 below.

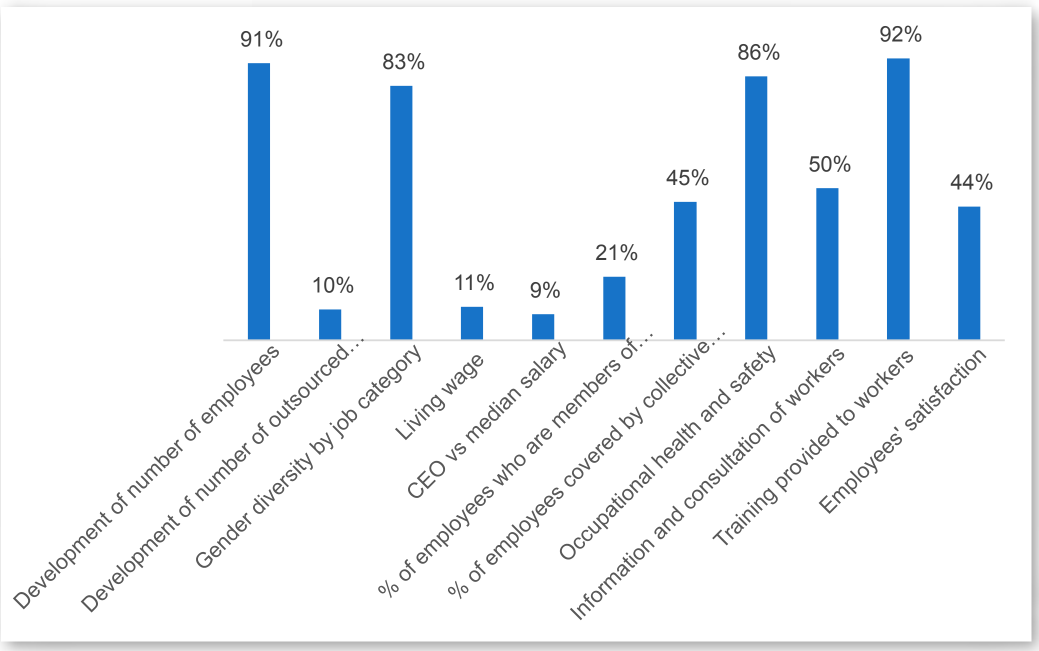
Figure 18: Proportion of companies addressing employee and workforce matters by level of disclosure



Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)

84 Further detail, regarding specific topics of particular social relevance, can be seen in Figure 19 below, prepared using information from the 2019 ACT report on the sample of 1 000 companies analysed.

Figure 19: Proportion of companies addressing specific topics of employee & workforce matters

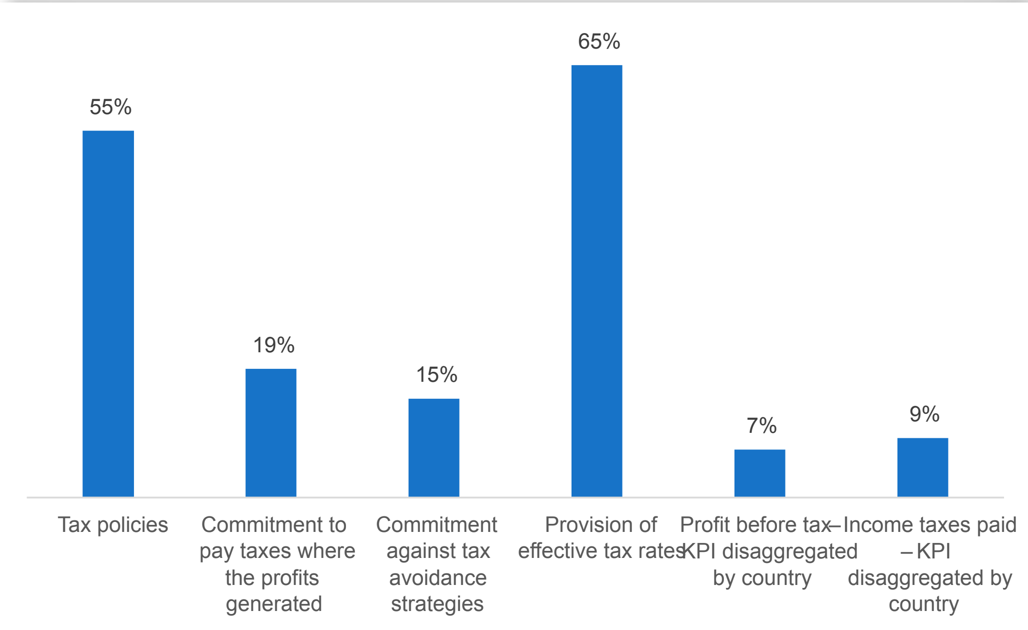


Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)

85 Significant differences can be observed when analysing these issues from an industry perspective. For instance, companies in Energy & Resource Extraction show significantly higher proportions on issues like trade unions and collective bargaining, as well as occupational health & safety, while those in Apparel & Textiles or Consumption have higher non-disclosure rates. Relevant differences can also be found at country level.

86 Tax issues are also addressed very differently, as shown in Figure 20 below, prepared using information from the 2019 ACT report on the sample of 1 000 companies analysed.

Figure 20: Proportion of companies addressing specific topics relating to taxes



Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019)

87 The results of the research for the 2019 ACT report suggest relatively low coverage of reporting on tax-related policies and commitments from a country-by-country perspective. While most companies report on tax policies, only a few companies express specific commitment about paying taxes where profits are generated, and even fewer companies provide information on income taxes paid disaggregated by country.

Governance

88 The NFRD does not explicitly require any specific governance-related disclosures even though such disclosures are recommended in a majority of reporting frameworks.

89 The 2019 ACT report notes that only 14% of the sample of 1 000 companies reviewed, report that their Boards discussed specific issues in their non-financial reporting, and only 15% report a link between sustainability objectives and executive remuneration.

90 Based on the sample of 1 000 companies analysed for the purposes of the 2019 ACT report, in terms of reporting in line with the NFRD:

a) Between 40 and 50% of companies disclose a declaration of social purpose, the Board's mandate and supportive procedural governance arrangements;

b) Nearly 30% of companies disclose information on Board engagement with workforce representatives; and

c) About 14% of companies disclose matters that have more immediate impact on the Board's accountability for sustainability performance, including compensation, independent assessment, and transparency concerning decisions.

Figure 21: Reporting practices

Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, The Alliance for Corporate Transparency (2019) – page 40

UN Sustainable Development Goals (SDGs)

91 The 2019 ACT report concluded that although many companies espouse the Paris Agreement[30] or the SDGs[31], they still fail to set specific targets in line with them, or measure their progress accordingly. Of those who set climate targets, only 14% align to Paris Agreement goals, for example.

92 Most of all, given the high level of business debate around the SDGs, the 2019 ACT report notes that with the exception of Austria, Belgium, Denmark, Spain and Sweden, only a minority of companies in other EU countries make any reference to the SDGs in their reports across the rest of the European Union.

93 The Carrots & Sticks 2020 report[32], which performed an analysis and high-level connections between reporting provisions and the SDGs, notes that the SDGs most implied by reporting provisions, directly or indirectly, are the ones more directly associated with business operations, e.g. SDG 12 on responsible production and consumption, SDG 16 on inclusive societies and accountable institutions, as well as SDG 8 on decent work and economic growth. These SDGs

30 Paris Agreement

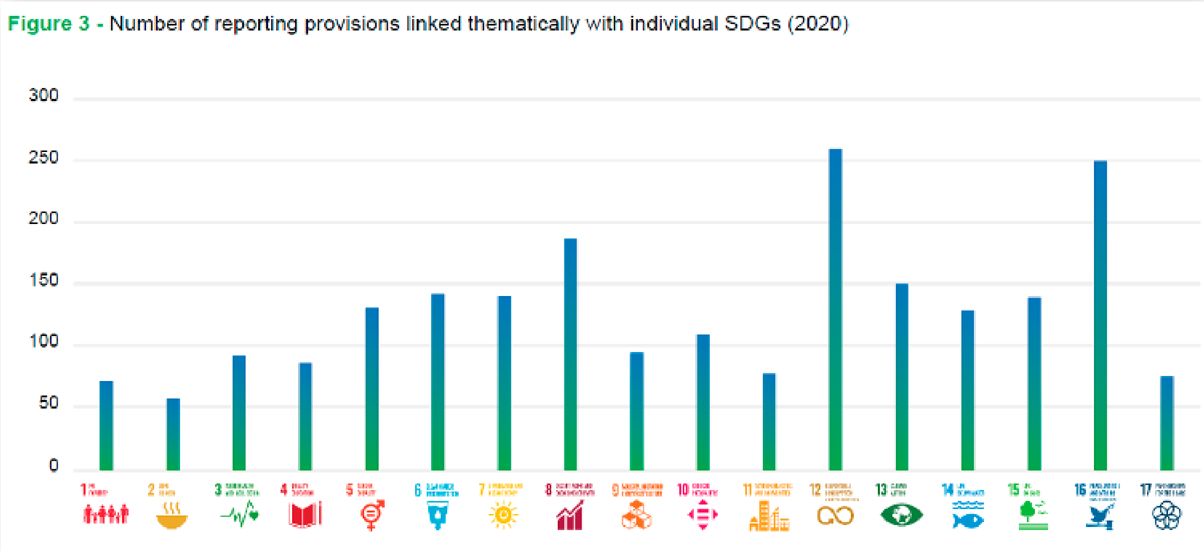
31 UN Sustainable Development Goals (SDGs)

32 Carrots & Sticks – Sustainability reporting policy: Global trends in disclosure as the ESG agenda goes mainstream, GRI and University of Stellenbosch Business School (2020)

are followed at significant levels by SDGs 13–15 related to climate, oceans and land, and SDGs 5–7 related to gender, water and energy.

94 The Carrots & Sticks 2020 report shows that reporting provisions cover the SDGs differently, as shown in Figure 22.

Figure 22: Number of reporting provisions thematically linked to individual SDGs



Source: [Carrots & Sticks – Sustainability reporting policy: Global trends in disclosure as the ESG agenda goes mainstream](), GRI and University of Stellenbosch Business School (2020) – page 10

95 This breadth of reporting provisions across the different SDGs leads to a heterogeneous coverage of reporting topics across companies. This becomes very transparent through the findings of the 2019 ACT report, which presents an analysis of the sustainability reports of 1 000 companies pursuant to the NFRD.

96 A study carried out by PwC in 2019[33], also across a sample of 1 000 company reports, found that nearly three quarters of the companies (72%) considered in their study publicly mentioned the SDGs in their reporting publications. Of the companies that mentioned the SDGs, 59% referenced them as part of their sustainability report while just over half (51%) mentioned them in their annual report. However, just 34% of those that mentioned the SDGs (25% of all companies analysed), did so in sections of their reporting that discussed business strategy. PwC found that out of the companies analysed, 65% mentioned specific SDGs with Decent Work and Economic Growth (SDG 8) being the most popular goal identified by business (a common observation in both years when the study was carried out).

97 The PwC study looked at how companies were focusing on the 169 targets that underpin the 17 SDGs as an indication of whether the goals were being integrated into business strategy. The findings indicated that only 14% (157 companies) mentioned specific SDG targets. Of those, 39% set qualitative ambitions and 20% set quantitative ambitions. Only 8% reported quantitative measures to show progress towards targets representing only 1% of all the companies analysed.

98 WBCSD's report *'Reporting Matters 2019'*[34], noted that the vast majority (93%) of the companies in their review referenced specific SDGs in their report. Nearly half (43%) prioritised five to eight SDGs, with a relatively small number (16%) referencing 12 or more SDGs. For the fourth straight year, the most referenced SDGs were: (i) SDG 13: Climate action (88%), (ii) SDG 12: Sustainable cities and communities (79%), and (iii) SDG 8: Decent work and economic growth (73%). Those SDGs least likely to be prioritised were SDG 1: No poverty (24%), SDG 14: Life under water (24%) and SDG 6: Peace and justice – strong institutions (29%).

33 PwC's SDG Challenge 2019, PwC (2019)

34 Reporting Matters 2019, WBCSD (2019)

99 Overall, the WBCSD report notes little improvement in the level of detail around the SDGs from the prior year study and highlights:

a) About a quarter (24%) of companies in the sample discuss target-level SDG information, with the remainder of disclosures focusing on goal-level information. This is up from 20% in 2019.

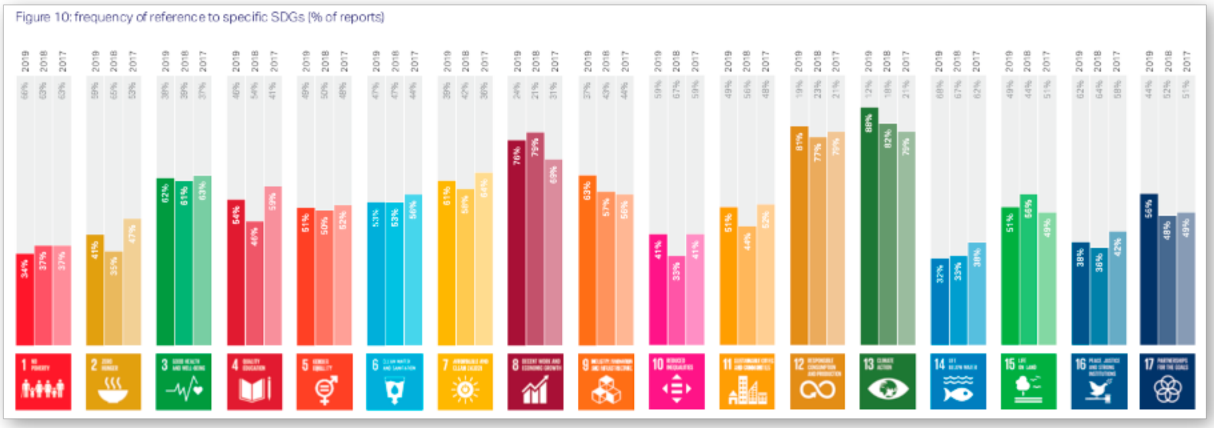
b) Nearly a third reference a prioritisation process (29%) and ties to strategy (33%). About one fifth explicitly discuss ties between the materiality assessment process and the SDGs (24%).

c) An increasing number of reports align KPIs (20% vs 6% in 2019) and targets (28% vs 15% in 2019) to the SDGs.

d) About a third (32%) tie SDGs to case studies or detailed evidence of sustainability programs and initiatives undertaken during the reporting period (19% in 2019).

100 As was the case in 2019, very few (1–3%) refer to enterprise risk management and human rights in relation to the SDGs.

Figure 23: Frequency of reference to specific SDGs



Source: [Reporting Matters 2019](), WBCSD (2020) – page 20

Sector specific disclosures

101 Common topics for the extractive industries are those related to transparency of payments to foreign governments, human rights and conflict minerals. An example is the Act on Transparency Measures in the Mining, Oil, and Gas Industries (2016) by the Government of Quebec in Canada. Provisions targeting the manufacturing industries often imply global supply chain management, such as the Corporate Sustainability Compact for the Textile and Apparel Industry (2018) issued by the China National Textile and Apparel Council (CNTAC).

Location

QUESTION 2.2:
Where is non-financial information found in companies' publications?

102 The NFRD provides an option for non-financial statements to be included in the annual report or in a stand-alone report (depending on Member States' decisions and choices). This leads to obvious variations in presentation of non-financial information across companies in the EU.

103 The examination of 145 European issuers in 2019 for the purposes of ESMA's enforcement and regulatory activities[35] showed that 67% of the companies examined included their non-financial statements directly in the management report

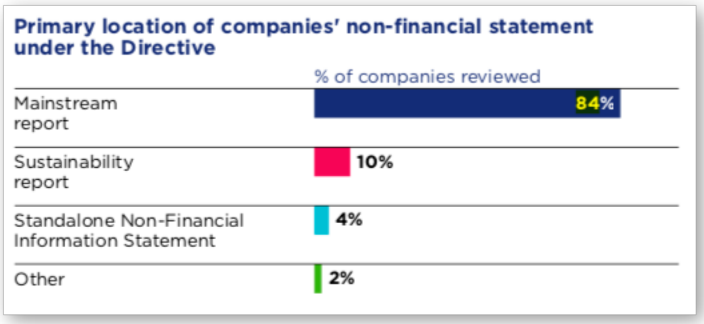
35 Enforcement and regulatory activities of European enforcers in 2019, ESMA (2020)

(9% via cross-reference), while 14% presented their non-financial statement separately, but still within the annual financial report. 19% of the examined issuers presented the non-financial statement separately outside the annual financial report.

104 The 2019 ACT report that analysed the provision of non-financial information by a sample of 1 000 companies in Europe, took into account any information on social and environmental issues presented in the annual report or in a clearly designated separate report, irrespective of whether it was formally identified by the company as a non-financial statement. This analysis showed that 60% of those companies integrated key non-financial information in their annual report.

105 For the CDSB 2020 report *'Falling short? Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve'*[36], the CDSB reviewed the 2019 environmental and climate-related disclosures of Europe's 50 largest listed companies, with a combined market capitalisation of USD 4.3 trillion. In this report the CDSB notes that 84% of companies used their mainstream report as the primary location of their non-financial statement. Approximately 10% used a separate sustainability report, with 4% preparing a standalone non-financial information statement in addition to their mainstream and sustainability reports. Of those that provided disclosure within the mainstream report, 55% integrated the content within relevant report sections (such as strategy, risk and corporate governance), whereas 45% included a stand-alone statement with the content presented in its own section. Those choosing to integrate the information adopted a 'hybrid' approach, where business model, due diligence and principal risk disclosures were integrated, but policies, outcomes and KPIs were published in a dedicated environmental or climate-related section of the report.

Figure 24: Primary location of non-financial statement required by the NFRD



Source: Falling short? Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve, CDSB (2020) – page 24

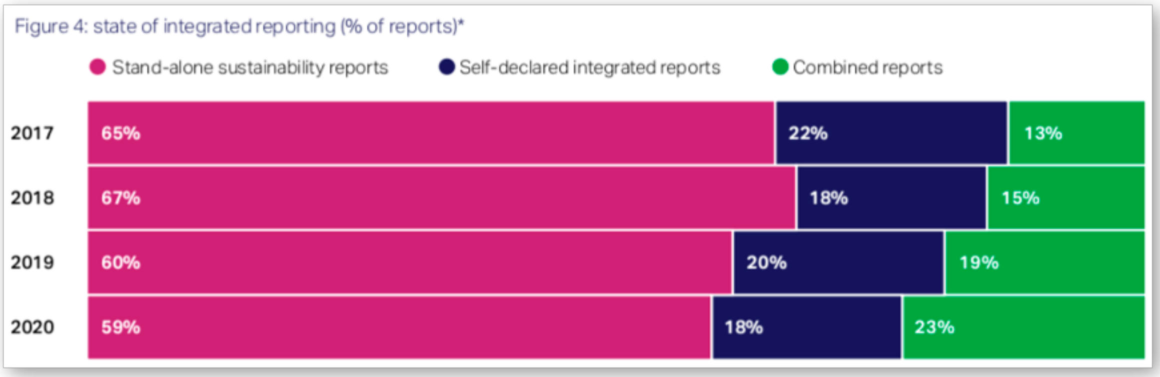
106 Regarding connectivity, the CDSB noted that many companies chose to include cross-reference tables within their mainstream report, sign-posting readers to the location of the specific content on 'environmental matters' within the mainstream report, and to separate disclosures where appropriate. Similarly, many disclosures included page references and links within and between report sections, for example linking risks to outcome disclosures, which are meant to support the reader in gaining an understanding of the company's overall position, performance and approach.

107 According to WBCSD's report *'Reporting Matters 2020'*[37] benchmarking its member companies worldwide, the relative percentage of stand-alone sustainability reports has dropped from 65% in 2017 to 59% in 2020, due to the increase in self-declared integrated/combined reports and annual reports that combine sustainability and financial information. WBCSD notes that its European headquartered member companies are more likely than its Asian and North American headquartered member companies to combine sustainability and financial information into a single report (55% compared with 32% and 11%, respectively).

36 Falling short? Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve, CDSB (2020)

37 Reporting Matters 2020, WBCSD (2020)

Figure 25: State of integrated reporting per WBCSD 'Reporting Matters 2020'



Source: Reporting Matters 2020, WBCSD (2020) – page 17

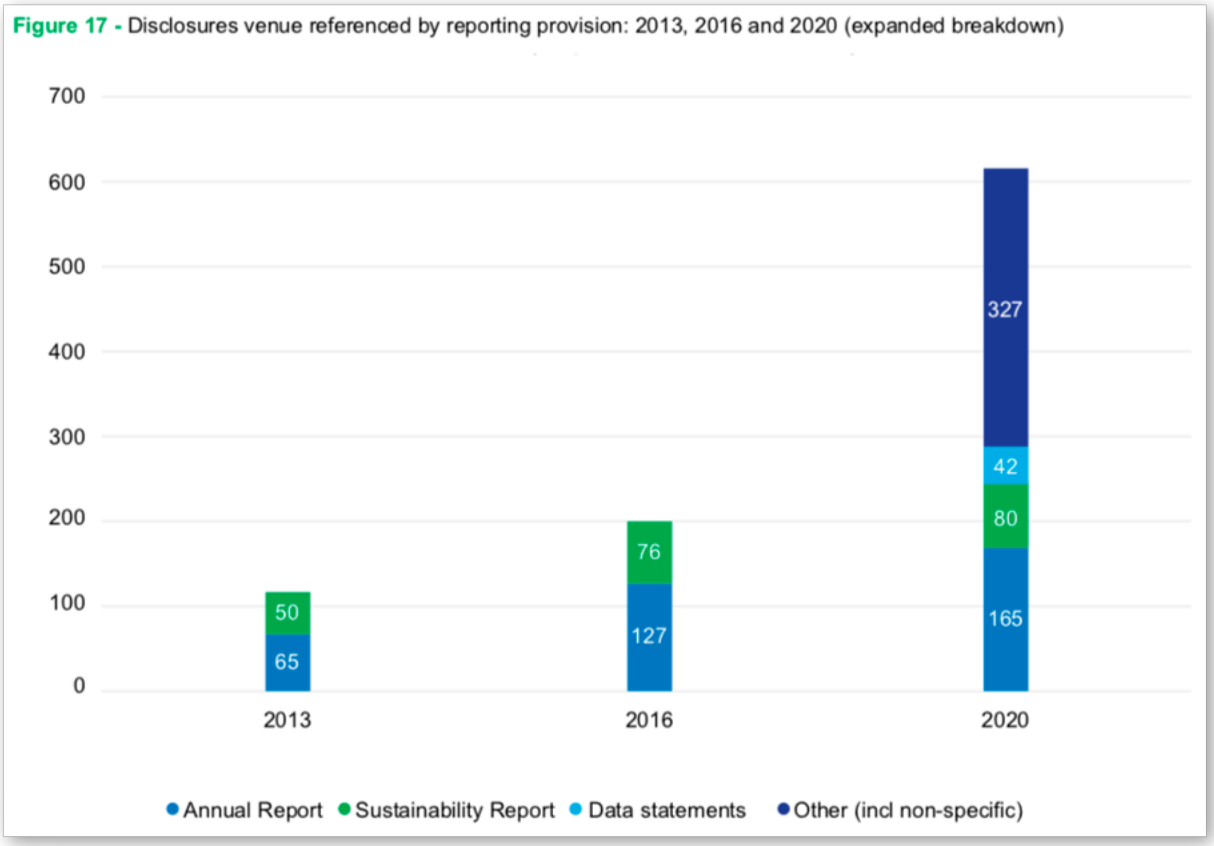
108 A paper by Frank Bold published in September 2017[38] (hereafter 'the Frank Bold paper') compared the implementation of the NFRD in the UK, Germany, Italy and France. According to this study, only the UK and France have required the non-financial information statement to be included in the annual management report rather than providing the option allowed by the NFRD to publish as a separate report. The Frank Bold paper posited that this requirement gives gravity and prominence to the non-financial reporting statement, which is circulated to shareholders on a yearly basis ahead of the general meeting. It went further to say that this approach also improves the integration of financial and non-financial reporting. Conversely, in Germany, if the non-financial information statement is not included in the annual management report, it can be published on the company's website up to four months afterwards, provided that the annual management report refers to this publication and the website. The paper posited that this time lag means that shareholders whose attention is captured for the purposes of reviewing the annual management report and preparing for the annual meeting, may be lost, and non-financial information may therefore not be given the same level of attention. The Frank Bold paper noted that BASF (a German chemical company), Deutsche Bank and Deutsche Börse AG have all said that providing information in a separate report would be a step backwards.

109 The Carrots & Sticks 2020 report[39] noted that large companies are currently disclosing non-financial information in their annual reports, periodic reports, investor briefs, newsletters, press releases as well as web announcements and engagement events. The report found 165 cases explicitly referring to annual reports (or components thereof such as management discussion & analysis, directors' report or governance report) and 80 cases that mention sustainability or non-financial reports, whilst the data collected included 175 cases where nothing was specified and 42 cases where specific reference is made to other data disclosures and statements. Other disclosure vehicles referred to included thematic reports, plans and online disclosure.

38 Comparing the implementation of the EU Non-Financial Reporting Directive in the UK, Germany, France and Italy, Frank Bold (2017)

39 Carrots & Sticks – Sustainability reporting policy: Global trends in disclosure as the ESG agenda goes mainstream, GRI and University of Stellenbosch Business School (2020)

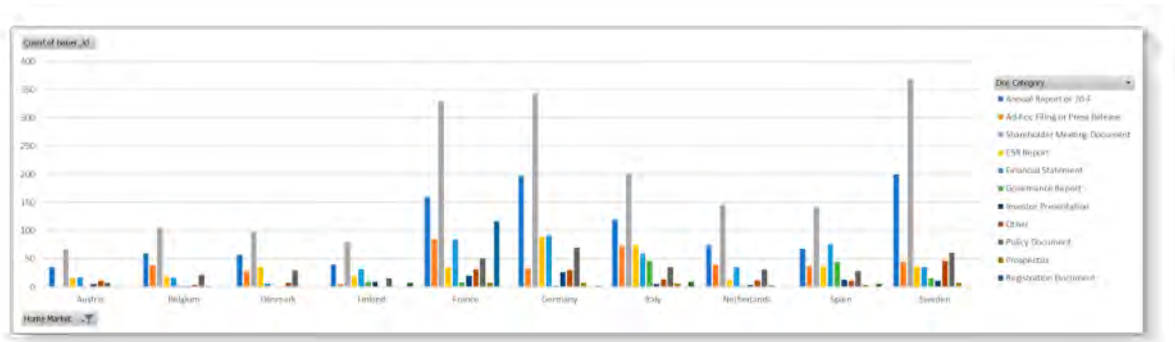
Figure 26: Location of disclosures according to the Carrots & Sticks 2020 study



Source: [Carrots & Sticks – Sustainability reporting policy: Global trends in disclosure as the ESG agenda goes mainstream], GRI and University of Stellenbosch Business School (2020) – page 30

110 The above is confirmed through data obtained from MSCI ESG Research LLC[40], presented in Figure 27 below, which also shows a scattered landscape of reporting locations over a selection of EU Member States.

Figure 27: Location of disclosures according to an MSCI analysis for 2019



Source: MSCI ESG Research LLC, Document Repository Analysis for 2019

40 MSCI ESG Research LLC, Document Repository Analysis for 2019

Format

QUESTION 2.3:

Are there any reporting initiatives which provide normalised metrics, digital electronic format representation, reporting tools or data repository for the reporting of non-financial information?

111 According to the European Commission' request for technical advice from the European Lab, users have difficulty in finding and exploiting the reported non-financial information, in part because the information is not sufficiently digitalised. As a matter of fact, non-financial reporting requires not only guidelines for reporting, but also normalised metrics, digital electronic format representation, reporting tools and data repository solutions to enable easier disclosure, accessibility and analysis of non-financial information. This assessment is supported by the information presented in Table 10 below:

Table 10: Non-financial reporting initiatives and disclosure production/consumption resources

Reporting initiative	Name of guideline or framework	Topic	Sector specific	Guidance for reporting	Normalised metrics	Digital format	Reporting platform/ tools	Data repository
European Commission	Guidelines on non-financial reporting (2017/C 215/01)	Business Model, Policies due diligence, Outcomes, Opportunities, and risks, Environmental, social and employee matters, Respect for human rights, Anti-corruption and bribery matters, Supply chain, Conflict minerals						
Global Reporting Initiative (GRI)	GRI framework	Sustainability						
Carbon Disclosure Project (CDP)	Guidance for reporting (Climate change, Water, Forest, Supply Chain)	Climate change, Water, Forest				(XBRL, 2017)		
Sustainability Accounting Standards Board (SASB)	SASB framework	Environment, Social capital, Human capital, Business model and innovation, Leadership and governance				(XBRL, 2020)		
Task Force on Climate-related Financial Disclosures (TCFD)	TCFD recom-mendations	Financial impacts of climate related risks and opportunities						
EU Eco-Management and Audit Schema (EMAS)	EMAS Framework	Energy efficiency, Material efficiency, Water, Waste, Biodiversity, Emissions						

Reporting initiative	Name of guideline or framework	Topic	Sector specific	Guidance for reporting	Normalised metrics	Digital format	Reporting platform/ tools	Data repository
Spanish Association of Accounting & Business Administration (AECA)	Integrated Reporting Model: Financial, Environmental, Social and Governance (IRM-FESG)	Business model, Due diligence, Risk management, Performance (Financial, Social Environmental, Governance)				(XBRL, 2006, 2009, 2013)		
European Federation of Financial Analysts Societies (EFFAS)	EFFAS-ESG Guidelines	Environmental, Social and Governance						
Global Impact Investing Network	IRIS framework	Environmental, Social and Governance						
International Standards Organization ISO 26000	ISO 26000 Guide on social responsibility	Social responsibility						
Japanese Environmental Ministry	Environmental reporting platform pilot project	Environmental						
International Integrated Reporting Council (IIRC)	The International Integrated Reporting Framework	Capitals (financial, manufactured, natural, social, human, intellectual organisational) overview, Governance, Business model, Risk and Opportunities, Strategy and resource allocation, Performance, Outlook						
International Labor Organization (ILO)	Tripartite Declaration of Principles on Multinational Enterprises and Social Policy	Social						
Organisation for Economic Co-operation and Development (OECD)	OECD Guidelines for Multinational Enterprises	Human rights, Labour rights, environment						
United Nations Human Rights Office of the High Commissioner	The Reporting Framework of the Guiding Principles on Business and Human Rights	Human rights						

Reporting initiative	Name of guideline or framework	Topic	Sector specific	Guidance for reporting	Normalised metrics	Digital format	Reporting platform/ tools	Data repository
United Nation Global Compact	Model Guidance on Reporting ESG Information to Investors: A Voluntary Tool for Stock Exchanges to Guide Issuers	Environmental, Social and Governance						

Source: An analysis of reporting initiatives and their efforts in providing resources to facilitate the disclosure, accessibility, and analysis of non-financial information (provided by AECA for this assessment report)

112 Looking at the outcome of the analysis in Table 10, non-financial reporting initiatives are evolving in the following areas:

a) Guidelines: Providing general recommendations and direction on the content to disclose, without concrete metrics, unit measures or methodology.

b) Normalised metrics: Providing concrete non-financial metrics to disclose, including unit measures and methodology.

c) Digital electronic format: Providing a structured representation in a digital format of the non-financial information to disclose.

d) Reporting platforms/tools: Providing tools to facilitate the disclosure and collection of the non-financial information.

e) Data repository: Providing a central repository where the non-financial information from companies can be collected and analysed.

113 The only electronic format that has been promoted by non-financial reporting initiatives is XBRL (eXtensible Business Reporting Language). Each of the European Banking Authority (EBA)[41], the European Insurance and Occupational Pensions Authority (EIOPA)[42], the European Central Bank (ECB)[43] and ESMA[44], have endorsed the European Single Electronic format (ESEF). ESMA's endorsement relates to issuers on EU regulated markets preparing their annual reports.

114 SASB[45], CDP[46] and AECA[47] support electronic formats not only to promote better data quality and analysis of the non-financial information, but also to overcome the misalignment between the reporting of material non-financial information and financial reporting, in effect amplifying the concept of double materiality.

115 In the financial reporting landscape, XBRL is already used by more than 10 million companies across 60 countries and implemented by 179 regulators covering the majority of public companies globally[48]. Figure 28 reflects the adoption and implementation of XBRL by capital markets for financial reporting, observing 53 instances on a global basis as of 2020. Figure 29 extends the population to include financial regulators, business registers, tax authorities, government oversight, Standard Business Reporting (SBR) and others, observing 179 regulatory instances. In the maps of Figures

41 EBA Reporting Framework, EBA (2018)

42 Technical specifications for EIOPA recommendations on supervisory flexibility regarding the deadline of supervisory reporting and public disclosure, EIOPA (2020)

43 ECB Reporting Taxonomy, ECB (2020)

44 The European Single Electronic Format, ESMA (2020)

45 As Markets Move Toward Structured Non-Financial Reporting, SASB Engages PwC's XBRL Practice to Support Build of XBRL Taxonomy, SASB (2020)

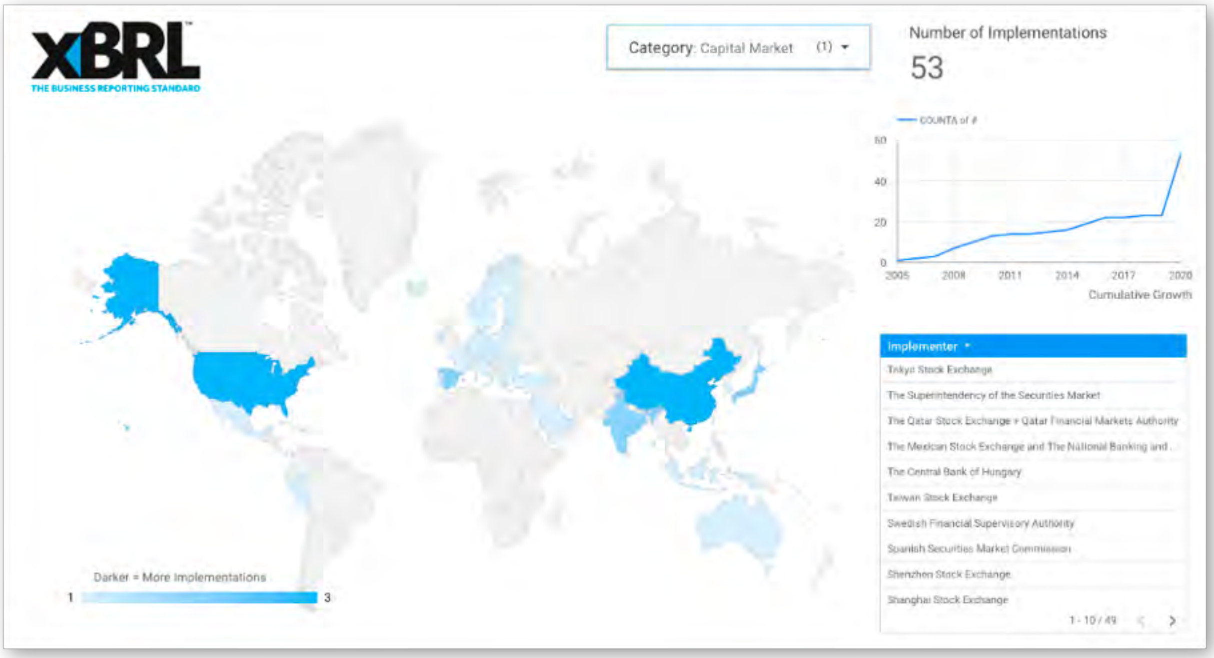
46 Technology and climate reporting: can XBRL help TCFD?, CDP (2017)

47 Integrated Reporting Model: Financial, Environmental, Social and Governance, AECA (2020)

48 XBRL Adoption, XBRL International (2020)

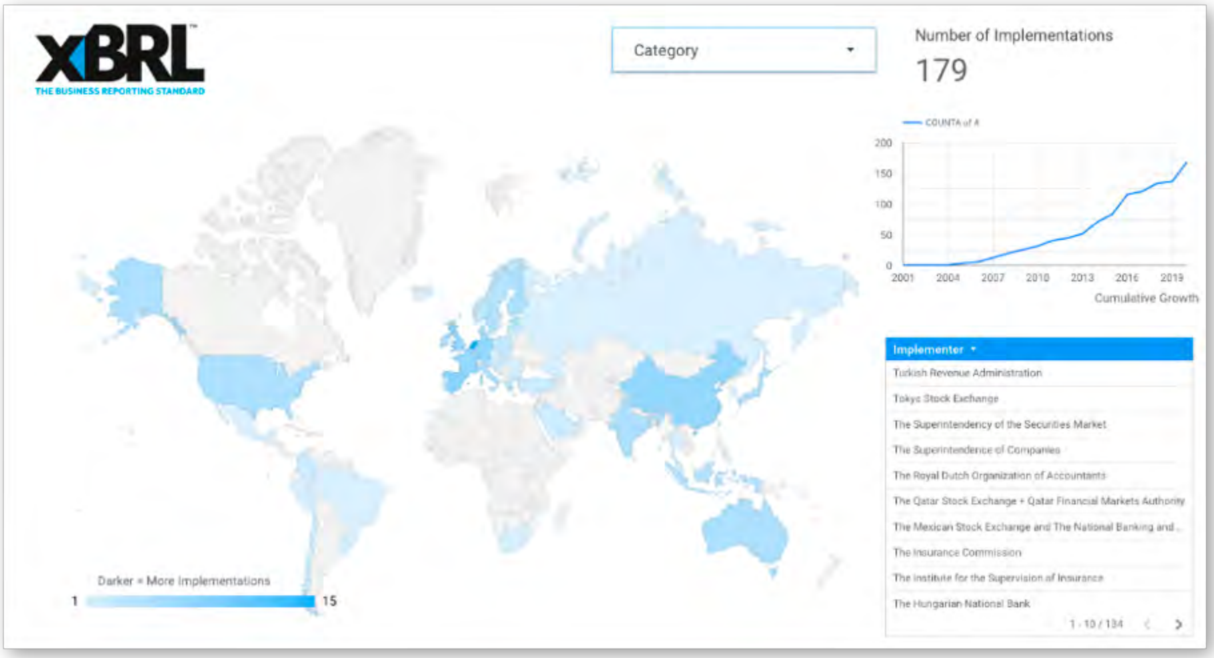
28 and 29, the darker the blue the higher the volume of implementation. The lag observed in the EU capital market is expected to be rectified through the implementation of ESEF.

Figure 28: Adoption and implementation of XBRL by capital markets for financial reporting



Source: [XBRL Project Directory](), XBRL (2020)

Figure 29: Extended adoption and implementation of XBRL by capital markets for financial reporting



Source: [XBRL Project Directory](), XBRL (2020)

QUESTION 2.5:
Which type of technology framework/platform was used to provide non-financial information?

116 The Association of Accountants and Financial Professionals in Business (IMA) published a report in 2020 entitled *'A digital transformation brief: Business reporting in the fourth industrial revolution'*[49], presenting research relevant to digital transformation. From the preparers' perspective, many entities covered by the NFRD rely on manual processes, large teams, third-party consultants, and a variety of proprietary point solutions, such as business productivity software, email, and general-purpose collaboration software, to provide the requested data and disclosure. Exacerbating these reporting challenges is the continued growth in size and complexity of many organisations with employees and data located all around the world. One of the issues identified is that traditional information management solutions may not provide the agility, scalability and scope to economically permit a more comprehensive NFRD information management process. Physically connecting disparate information from internal and external data systems creates a costly information processing environment that is not adequate or agile enough to support both internal and external supply chain non-financial information sources. Traditional information management solutions may not provide the agility, scalability and scope to economically permit this more comprehensive NFRD information management process.

117 According to a recent report by the Transparency Market Research Group[50] (a global market intelligence company), preparers are starting to implement cloud-based disclosure management solutions in order to publish statutory disclosures. The report states that disclosure management solutions are one of the steps expected to gain significant traction in the near future due to the rising need for managing disclosure information within organisations. Many software vendors are venturing into the disclosure management software market. Key players operating in the market include SAP, Oracle, Certent, IRIS Business Services, Workiva, CoreFiling, DataTracks, LucaNet, OCR Services, Tagetik Software, Synthesis Technology, Anaqua, Trintech, and Lecorpio. Accelerating digitisation has become more urgent as the COVID-19 pandemic highlighted the inadequacies of systems that rely on outdated, insecure technology and that operate with vast voids of fragmented disclosure information.

118 The abovementioned IMA study showed that physically connecting disparate information systems from internal and external data systems creates a costly information processing environment that may not be adequate or agile enough to support both internal and external supply chain information sources for non-financial information.

119 A challenge for non-financial information data management control systems and sustainability control systems is to support the implementation of an integrated sustainability strategy. The configuration of an organisation's control system and reporting system may vary across sustainability dimensions and type of company due to its size and activity. For example, it is plausible that an organisation's environmental and financial control systems might be tightly coupled in cases where there is a clear association between environmental performance (e.g. energy efficiency and waste reduction) and cost reduction. On the other hand, it may be difficult to determine such an association with respect to social activities (e.g. engagement in community activities) and financial performance. Thus, there is a need for empirical evidence that examines these differences so reporting alone may not be enough. NFRD reporting entities are seeking management systems that can meet many versions of non-financial information reporting. Assessing relevant information from across these comprehensive strategic areas is one of the most difficult tasks for NFRD reporting teams. It requires establishing common definitions for critical information and potentially rethinking the association between strategy drivers and the underlying processes and related performance metrics. This often requires a better, more holistic approach to company KPIs – those that are integrated into the company's long-term strategy for value creation across all stakeholders.

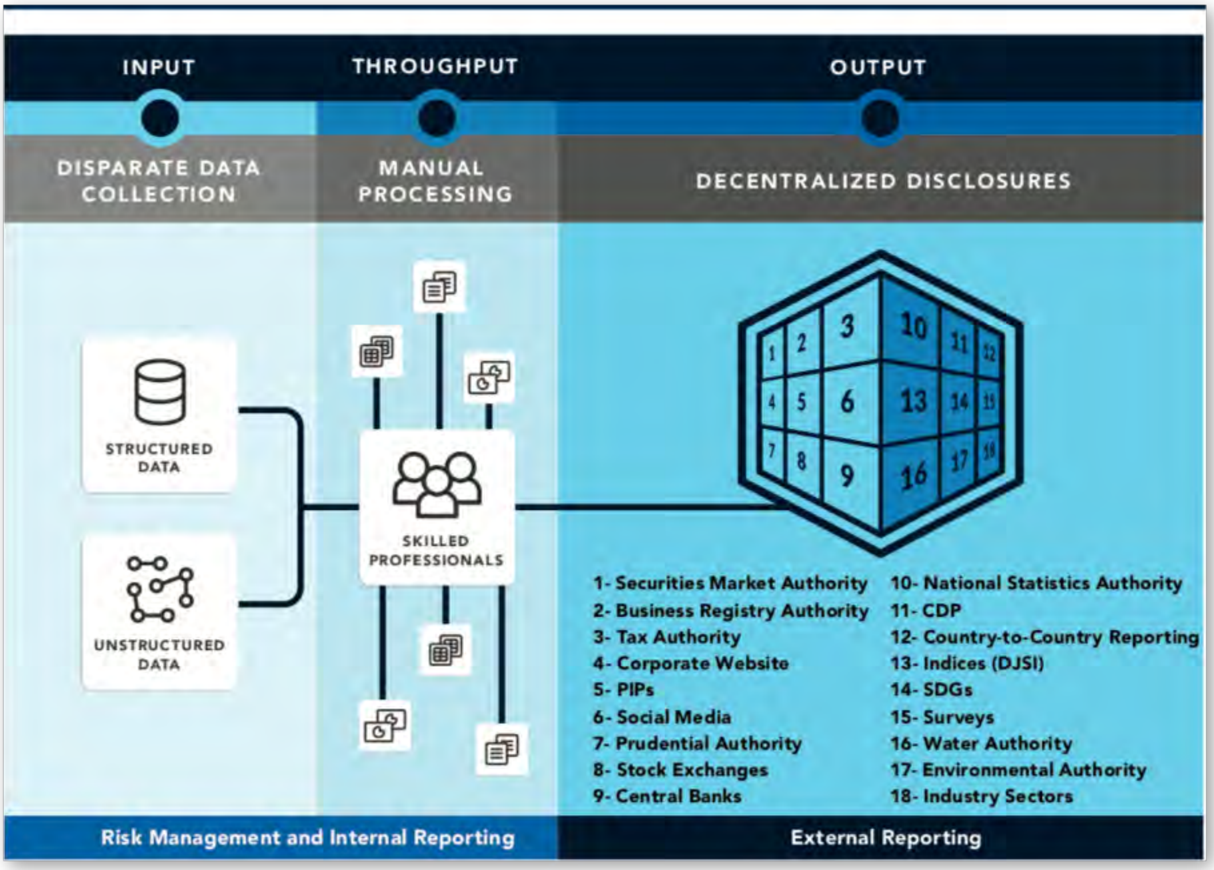
120 Building on these requirements, there is a need for well trained professional resources within companies that are responsible for sourcing, aggregating and consolidating this information, with well-designed controls, processes and procedures that ensure that the data is reliable, timely, comparable and accurate (Figure 30).

49 A digital transformation brief: business reporting in the fourth industrial revolution, IMA (2020)

50 Transparency Market research group

121 In fact, the entire non-financial reporting ecosystem (see Figure 30) is much more fragmented and impacts both NFRD companies as well as non-NFRD companies.

Figure 30: Regulatory reporting and compliance fragmented ecosystem



Source: A digital transformation brief: Business reporting in the fourth industrial revolution, IMA (2020) – page 11

122 Considering this large ecosystem, regulated entities, governments, and regulatory authorities are increasingly recognising the need to discard the information processing and reporting ways of the past. They are seeing the need to leave behind inflexible paper-based documents or proprietary digital data formats and embrace open data standards.

QUESTION 2.6:
How many companies report through which technology framework/platform?

123 Currently, every EU Member State has its own Officially Appointed Mechanism (OAM), which typically works as a storage facility that publishes statutory information related to its listed companies. Hence, any investor who wants to compare companies across different member states must access a different OAM for each company. Furthermore, member states have different national mechanisms for storing information about companies, which all work in slightly different ways, and the information they provide varies in terms of scope and quality.

Figure 31: The Transparency Directive reporting flow

Source: IMP's Non-Financial Digitisation Working Group and IMA

124 All companies, regardless of size, file reports to a national business registry in EU Member States. Different business registers operate within different legal frameworks, and companies need to comply with the laws of each jurisdiction. The national business registers validate the completeness of the filed reports and calculations and those reports are offered to the general public as a public database normally subject to a specific cost. It is important to note that there were estimated to be approximately 25.1 million SMEs in the European Union in 2018[51], with the vast majority being micro-sized enterprises which employed fewer than nine people. Only 1.47 million of those enterprises had between 10 and 49 employees and approximately 236 thousand had 50 to 249 employers.

Figure 32: Company annual reports and Business Registers disclosure process

Source: Graph Source: IMP's Non-Financial Digitisation Working Group

51 Source: Statista, 2018

SECTION 3: WHAT ARE THE CHALLENGES FACED FOR PRODUCING OR USING THE PROVIDED NON-FINANCIAL INFORMATION

125 The NFRD is the principle regulation in the EU that obliges companies to report ESG information. Applying to approximately 6 000 large companies in the EU (listed companies, banks, insurance companies, other companies designated by national authorities as PIEs)[52], the law requires these corporations to *'include in the management report a non-financial statement containing information to the extent necessary for an understanding of the undertaking's development, performance, position and impact of its activity, relating to, as a minimum, environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters'*.

126 The NFRD gives companies significant flexibility to disclose relevant information in the way they consider most useful. Companies may use international, European or national guidelines to produce their non-financial statements. In June 2017, the European Commission published guidelines on non-financial information reporting, to help companies disclose environmental and social information. These guidelines are not mandatory, and companies may decide to use international, European or national guidelines according to their own characteristics or business environment.

127 Considering the loose definition of which information to disclose in detail, and in which format, there is a high degree of inconsistency in non-financial information disclosures, in respect of content and structure This creates complexity on the side of preparers and ambiguity for users of the disclosed information. The field of technology for disclosing non-financial information is not yet well developed, which makes the processing and use of non-financial information difficult.

128 The following subsections describe the key issues related to content, structure and technology in more detail, with reference to respective evidence from the research reports reviewed for the purposes of the assessment of Stream A6.

Content

QUESTION 3.1:
What are the issues identified with what is reported in terms of content?

129 CDSB's 2020 report *'Falling short? Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve'*[53], analysing the 2019 environmental and climate-related disclosures of Europe's 50 largest listed companies with a combined market capitalisation of USD 4.3 trillion, observes that these companies report data which lack quality, comparability and coherence.

130 An article by CDP Europe[54] notes that achieving the urgent transition to a resource-secure economy depends on companies being accountable for their impact, as well as investors and other users having usable information when making their capital allocation decisions. Yet the scope of the directive as it stands today falls short on both principles.

131 The 2019 ACT report observes that about half of the 1 000 companies analysed do not generally disclose information useful for decision making. Approximately a third of the companies report well-developed sustainability policies, but these fail to provide evidence around impacts. Only 20% of the companies provide information that allows such understanding. This research concludes that the quality and comparability of companies' sustainability reporting across the NFRD's five topics is not sufficient for understanding their impacts, risks or plans.

132 In October 2019, the UK's Financial Reporting Council (FRC) issued an online consultation seeking stakeholder views and expectations for the future of corporate reporting. According to the published survey conclusions[55], 51% of respondents said that they are always interested in information about how a company's activities affect the environment, communities, customers and suppliers. Contrasting this, the FRC noted that existing sustainability reports rank among the least read

52 Source: Eurostat

53 Falling short? Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve, CDSB (2020)

54 A major chance to mainstream non-financial reporting in Europe, Mirjam Wolfrum, Director Policy Engagement, CDP Europe, (CDP May 2020)

55 Future of corporate reporting: conclusions from an online survey of FRC stakeholders, FRC (2019)

items in the survey. FRC's analysis suggested that one possible explanation for this may be that survey respondents do not expect sustainability reports to contain information that is relevant to them in meeting their communication objectives. A lack of comparability and a lack of trust are among the reasons cited qualitatively by users for not engaging with sustainability reports more thoroughly.

133 In summary, the evidence collected through the literature review carried out by Stream A6, regarding existing perceptions and issues noted by various stakeholder groups on what is reported in terms of content, highlights the following issues:

a) Lack of conciseness in reporting;

b) Matters affecting comparability, include:

(i) Lack of common frameworks and freedom to select and combine different frameworks;

(ii) Differences and lack of clarity in regulatory terminology, leaving key matters such as materiality open to interpretation;

(iii) Lack of common and standardised metrics;

(iv) Inconsistent national implementation of the NFRD in law;

(v) Different levels of maturity on the topic of sustainability across the EU;

(vi) Proliferation of sector specific requirements; and

(vii) Differing levels of maturity across reporting organisations of the reporting process including responsibilities, systems and processes;

c) Lack of consistency;

d) Lack of clarity on the definition of materiality;

e) Inconsistent interpretation and implementation of reporting boundaries, particularly regarding supply chain aspects;

f) Unclear definition of component parts of the business and the value creation model;

g) Lack of explicit requirements and methodologies for the disclosure of goals and targets as well as data to track progress on risks and KPIs;

h) Lack of connectivity of non-financial information disclosed at various points in time and across different channels, as well as lack of connectivity with financial information;

i) Difficulties in measuring and disclosing impacts and a focus on inputs and outputs which are not helpful in assessing performance;

j) Reluctance to provide meaningful forward-looking information on value creation;

k) Less forthcoming reporting of potential opportunities; and

l) Heterogeneous coverage of reporting topics across companies.

Conciseness

134 A report published in 2019 by BEIS on stakeholder perceptions of non-financial reporting[56] (hereafter 'the BEIS research report') concludes that corporate reporting has come under criticism in recent years for being lengthy and lacking focus. This trend has evolved as a reaction of corporations towards increasing regulatory requirements for disclosure,

56 Stakeholder perceptions of nonfinancial reporting – BEIS Research Paper Number 2019/027, UK Department for Business, Energy & Industrial Strategy (2019)

combined with non-regulatory pressure by investors and wider society for transparency particularly regarding non-financial information.

135 According to WBCSD's report *'Reporting Matters 2019'*[57], benchmarking its WBCSD member companies worldwide, large companies increasingly try to address the needs of very different stakeholders through self-declared integrated reports and annual reports that combine sustainability and financial information. In its publication *'Reporting Matters 2020'*[58], the WBCSD noted that, across its 159 member companies worldwide, the average length of corporate reports that combine sustainability and financial information was 246 pages – the shortest report reviewed being 7 pages while the longest was 620 pages. The WBCSD pointed out that the length of corporate reports varied widely and was influenced by ownership type (private vs listed) and geography given the differing regulatory obligations across jurisdictions.

136 CDSB's 2020 report *'Falling short? Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve'*[59], analysed the 2019 environmental and climate-related disclosures of Europe's 50 largest listed companies with a combined market capitalisation of USD 4.3 trillion. As part of their review, CDSB looked at the conciseness of the disclosures and noted that on average, companies included 14 pages of environmental and climate-related content in their mainstream report, with a range of 1-70 pages and an average of 5% of the mainstream report dedicated to the topic. The longest environmental and climate related disclosure which did not include all the requirements of the NFRD was 14 pages; the shortest disclosure which included all the relevant content categories was just 2 pages. CDSB observed that the strongest disclosures, which balanced comprehensive disclosure of relevant environmental and climate-related information with concise reporting, were no longer than 5-10 pages. It concluded that whilst some organisations are choosing to produce significant disclosures under the NFRD, this demonstrates that less might at times indeed be more.

137 As the ACCA 2019 report critique for the IIRC[60] points out, conciseness focuses the reader's attention on the most important aspects of the business by applying the materiality principle and not obscuring the significant information in a mass of less relevant information. Most readers want to have a succinct overall picture of the entity, at least as a starting point. Information on particular aspects and in greater detail could be referenced as linked reports – for example, the full financial statements and further non-financial information. Clearly there is a balance between keeping the report concise and ensuring the completeness of the information and its comparability over time or with that of other organisations.

138 The BEIS research report notes that, investor frustrations with the reports and the value they can derive from them, tend to centre on their length as well as the sometimes vague and wordy nature of the information contained within them. Some annual reports exceed 300 pages, making them inaccessible to investors, who find it difficult to quickly identify information which is relevant, interesting and/or material to their decision-making. The BEIS research report also notes that another criticism often heard is that non-financial reporting still tends to include a lot of 'generic marketing and public relations' type content that lacks substance, whilst failing to address key strategic risks. The length of reports could be driven, in some instances, by a desire to appease topical single-issue lobby groups.

139 The BEIS research report further notes there is resulting confusion around the purpose of non-financial reporting, which leads companies to follow a tick box approach to compliance rather than focusing on producing meaningful information on their value creation and performance. A lot of non-financial reports are rather limited to sustainability related information and mainly environmental information within that.

140 The clearer and more focused the objectives and more specific the key stakeholders of non-financial reporting are, the more concise and effective the reporting will be. In practice companies are providing non-financial information through separate channels in an attempt to keep their annual reports streamlined whilst meeting the specific needs of a wider group of stakeholders.

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57 Reporting Matters 2019, WBCSD (2019)

58 Reporting Matters 2020, WBCSD (2020)

59 Falling short? Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve, CDSB (2020)

60 Insights into integrated reporting 4.0: the story so far, ACCA (2019)

Comparability

141 A major area of criticism of non-financial reporting by companies across Europe is the lack of comparability. Non-financial reporting is criticised for being inconsistent, incomplete and difficult to compare, which impedes a robust analysis and decision making based on the information provided in corporate reports.

142 This lack of comparability of reporting across the EU is mainly triggered by:

a) a lack of a common framework and freedom of reporting entities to select and combine different frameworks to produce non-financial information;

b) differences and lack of clarity in terminology used in relevant national laws and regulations, leaving things open for interpretation;

c) lack of common and standardised metrics;

d) inconsistent transposition and implementation of the NFRD by Member States;

e) a proliferation of sector specific requirements; and

f) differing levels of maturity across reporting organisations of the reporting process including responsibilities, systems and processes.

Lack of common framework and freedom to select and combine different frameworks

143 Section 1 of this document makes reference to a vast number of different frameworks, standards and guidance initiatives currently in place. As pointed out in a discussion paper published by the FRC in October 2020 on the future of corporate reporting[61], there is some regulation relating to non-financial reporting but there is also a multitude of voluntary frameworks which creates a confusing landscape for companies and results in a lack of relevant, reliable, comparable and balanced information for users.

144 Although the NFRD does not prescribe a reporting framework, it encourages companies to disclose information in accordance with widely accepted reporting standards and frameworks, requiring companies to state which ones they have relied on. The European Commission non-binding guidelines on non-financial reporting[62] mention frameworks such as the TCFD, GRI, CDP, CDSB, SASB, IIRC and the EU Eco-Management and Audit Scheme (EMAS).

145 In transposing the NFRD into national law, Member States have also included other national standards and frameworks, adding to the confusion and variety of reporting across Europe.

146 Furthermore, the available standards and frameworks are not mutually exclusive, and compliance with more than one of them is possible and increasingly common (see Section 1 of this document).

Differences and lack of clarity in terminology used in regulation leaving things open for interpretation

147 The Frank Bold paper[63] comparing the implementation of the NFRD in the UK, Germany, France and Italy, points out that there are areas where the NFRD is not clear about its intention, particularly in relation to the meaning of materiality and the way the business model should be reported on. Frank Bold observes that the surveyed jurisdictions have replicated the wording of the NFRD, failing to provide any further clarity.

148 The same Frank Bold paper notes the NFRD's failure to specify the scope of reporting between companies and jurisdictions, as well as how the non-financial information statement should reference aspects of financial reporting, with the surveyed jurisdictions failing to provide clarity on these points as well.

61 The future of corporate reporting, FRC (2020)

62 European Commission non-binding guidelines on non-financial reporting

63 Comparing the implementation of the EU Non-Financial Reporting Directive in the UK, Germany, France and Italy, Frank Bold (2017)

149 For the UK, the BEIS research report on stakeholder perceptions of non-financial reporting[64], points out that over half of the respondents that participated in the research mentioned the variations in reporting between companies and the consequent difficulties in comparing reports. The need for clarity or greater guidance around some of the terminology was also suggested by the respondents.

Lack of common and standardised metrics

150 The Frank Bold paper comparing the implementation of the NFRD in the UK, Germany, France and Italy, notes that the NFRD fails to provide any specific KPIs that should be applied by companies, or any guidance as to what they should be trying to illustrate. From the countries surveyed for the Frank Bold paper only France sets out KPIs in the implementing legislation (such as frequency and severity of workplace accidents), while the other countries do not set out specific KPIs or how they should be measured.

151 According to the BEIS research report the multitude of KPIs used across companies makes comparative analysis very difficult.

Inconsistent implementation of the NFRD in different member states

152 Member States have implemented the NFRD in varying ways, with different approaches on key issues, such as the definition of PIEs or the level of assurance required (see Section 1 for more details).

Differing levels of maturity across reporting organisations of the reporting process including responsibilities, systems and processes

153 According to a report by ECIIA *'Non-Financial Reporting: Building trust with internal audit'*[65], the implementation of the NFRD has impacted organisations in differing ways. Some have already established reporting on non-financial information whereas others have not. Indeed, some may have decided not to implement the new reporting requirements and prefer to explain their reasons for not complying.

154 The ECIIA report notes that in order to fulfil their corporate social responsibility, companies should have in place a process to integrate social, environmental, ethical, human rights and consumer concerns into their business operations and core strategy, in close collaboration with their stakeholders, with the aim of: (a) maximising the creation of shared value for owners/shareholders, other stakeholders and society at large, and (b) identifying, preventing and mitigating possible adverse impact from operations.

155 A recent series of roundtables jointly conducted by ecoDa and Mazars during 2019 and 2020[66], highlighted that one of the key challenges for a wholehearted commitment to sustainability across the business community in Europe, was that the focus on sustainability is often seen by many businesses as primarily a box-ticking compliance exercise, rather than a process for deeply embedding considerations of sustainability across all aspects of the business. It was further noted that the emphasis of company boards tends to be on short-term financial performance, without much attention on sustainability considerations at board level.

156 According to the European Commission Summary Report of the Public Consultation on the Review of the Non-Financial Reporting Directive[67], there is strong support for assurance for non-financial information, with 67% of respondents believing that the EU should impose stronger audit requirements for non-financial information. The summary goes on to say that some respondents stated that auditors are best placed to provide assurance on non-financial information, while a smaller number mentioned that this should not necessarily be the case.

64 Stakeholder perceptions of non-financial reporting – BEIS Research Paper Number 2019/027, UK Department for Business, Energy & Industrial Strategy (2019)

65 Non-Financial Reporting: Building trust with internal audit, ECIIA (2014)

66 Time for Sustainability to be at the heart of business, Mazars & ecoDa (2020)

67 Summary Report of the Public Consultation on the Review of the Non-Financial Reporting Directive, 20 February 2020 – 11 June 2020, European Commission

Consistency

157 For the purposes of the Stream A6 assessment, consistency of non-financial information is considered in the context of applying the same frameworks and standards, and using the same approach for the same items. This should be the case from one reporting period to the next for a reporting entity, or in a single reporting period across different entities. The lack of consistency of non-financial information is currently a major issue which stems from different factors, including: the lack of explicit requirements for explanation of variances in the data e.g. frequent changes in the basis of measurement; the lack of requirements for systems, processes and controls around the collection and management of non-financial information; and the data still not being fully embedded in the business model. Until these issues are overcome, it will be difficult for management, auditors and other stakeholders to exercise a level of scrutiny over non-financial information similar to that in place for financial information.

158 This is further accentuated by the lack of mandatory requirements for independent assurance by regulated assurance providers and the ever-increasing number of reporting frameworks which mean that non-financial information disclosures may be subject to change from one year to the next, as a result of applying a different approach for measuring and disclosing data. Such changes are not in all cases fully explained in the notes, rendering the use and interpretation of the data rather difficult

159 In the ACCA 2019 report critique for the IIRC[68], that provides a picture of the trends and developments over a four year period, the authors note that consistency of the reporting over time is one area where improvement was observed in the reports reviewed by ACCA. Reviewers looked for performance with comparative figures and a continuity in the reporting of KPIs from one year to the next. ACCA highlights that this is essential for users in identifying trends in performance. In addition, retaining the same performance measures from one year to another helps to give readers a sense that the report has a balance between the reporting of good and bad news and that KPIs that have turned negative have not then been dropped out. ACCA concludes that consistency and comparability are both aspects that have shown an improving trend over the four year period of their reviews.

160 On the other hand, a Mazars UK study of FTSE 350 disclosures of GHG emissions, published in February 2020, uncovered big spikes in reported emissions, suggesting unexplained volatility. Where explanations were provided, they were 'not as elaborate or developed as would be expected for similar changes in profit or revenue'. The research shows that current disclosure of GHG emissions by listed companies is not fit-for-purpose and is in many cases a box-ticking exercise that does not appear to be integral to the way management runs the business.

Materiality

161 According to the Frank Bold paper[69] comparing the implementation of the NFRD in the UK, Germany, France and Italy, the materiality test (i.e. the test for what extent of information on each of the ESG factors needs to be provided) remains unclear across the surveyed jurisdictions.

162 The Frank Bold paper notes that although the NFRD prescribes that information must be provided to the 'extent necessary for an understanding of the company's development, performance and position and the impact of its activity', there has been very little information provided (in the UK, Germany, Italy and France) as to how to determine the 'extent necessary'.

163 Directive 2013/34/EU (the 'Accounting Directive'), which the NFRD amends to include the provisions relating to the non-financial information statement, provides that the 'extent necessary' requires information to be provided 'where its omission or misstatement could reasonably be expected to influence decisions that users make on the basis of the financial statements of the undertaking'. The Frank Bold paper notes that it is unclear who these 'users' or 'readers' might be. This led some of the countries in the sample addressed by the Frank Bold paper, specifically the UK and Italy, to taking the approach of 'investor materiality' rather than a wider range of stakeholders.

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68 Insights into integrated reporting 4.0: the story so far, ACCA (2019)

69 Comparing the implementation of the EU Non-Financial Reporting Directive in the UK, Germany, France and Italy, Frank Bold (2017)

164 In the case of principal risks, the NFRD states that companies 'should provide adequate information in relation to matters that stand out as being most likely to bring about the materialisation of principal risks of severe impacts', and for these purposes the severity of impacts should be judged by their 'scale and gravity'.

165 The Frank Bold paper notes that this suggests that as regards the impact of principal risks, the materiality test should be based on the scale and gravity of the materialisation of the risk, rather than whether knowledge of a principal risk would influence readers' economic decisions (which appears to be the applicable test for materiality elsewhere in the NFRD). This distinction in the materiality test for 'impact' as opposed to other aspects of the report does not appear to be clearly made in the transposition of the NFRD to national law in the four jurisdictions considered for the Frank Bold paper.

166 The Frank Bold paper further notes that the NFRD requires reporting on principal risks related to business relationships to be provided 'where it is relevant and proportionate'. With the exception of Italy, this condition is included in the national transpositions in the jurisdictions considered for the Frank Bold paper, but no guidance is provided for its interpretation.

167 According to the Frank Bold paper there is also substantial uncertainty over what 'impact' might mean. This is particularly unfortunate given that the countries surveyed (UK, France, Germany and Italy) previously required companies to report on their development, performance and position in the context of ESG factors, but none of them required impact reporting. European Commission guidance says this should cover 'positive or adverse' impacts and that a company should disclose material information on principal risks 'regardless of whether they stem from its own decisions or actions of from external factors'. On this basis, it can be assumed that both positive and negative impacts should be reported on.

168 The Frank Bold paper concludes that the lack of clarity from the NFRD on materiality leads to problems, as materiality is one of the most fundamental aspects of reporting. Without a clear definition, companies may take significantly diverging approaches in relation to the extent of information that they provide, whilst complying with the broader requirements for reporting in general. The risk is that even if the procedural aspect of preparing a report is complied with, the more substantive aspect of providing useful information on ESG factors is still not guaranteed.

169 The BEIS research report on stakeholder perceptions of non-financial reporting[70] noted that materiality was a key concern for respondents, particularly in terms of how significant and specific the risks identified are, and in relation to their potential impact. Several respondents highlighted the different ways in which companies determine what is material and what is not, which in turn leads to a lack of comparability between company reports.

Organisational reporting boundaries

170 Organisational boundary setting affects reporting of general sustainability and other non-financial information.

171 A paper issued by the CDSB *'Proposals for boundary setting in mainstream reports – Discussion paper on organizational boundary setting by groups of companies for non-financial reporting purposes'*[71] discusses the way in which a group of companies determines its boundaries for non-financial reporting purposes, highlighting that it is important for numerous reasons, including transparency, comparability and benchmarking. However, different requirements and interpretations exist on whether and to what extent non-financial reporting should include information about the activities of a parent company, its subsidiaries, joint ventures, associates, investees, suppliers, upstream and downstream activities and the impacts of the group's activities.

172 The CDSB paper points out that the structure of corporate groups can change regularly, expanding and contracting with different priorities, opportunities and economic cycles worldwide. This affects the way in which management defines the boundaries of groups of companies for reporting purposes, as do other factors including legislation, voluntary protocols, the objectives of reporting, the placement of information, financial reporting rules, the structure of the corporate group and the availability of data.

70 Stakeholder perceptions of non-financial reporting – BEIS Research Paper Number 2019/027, UK Department for Business, Energy & Industrial Strategy (2019)

71 Proposals for boundary setting in mainstream reports – Discussion paper on organizational boundary setting by groups of companies for non-financial reporting purposes, CDSB (2014)

173 For financial reporting purposes, International Financial Reporting Standards (IFRS) prescribe the way in which assets, liabilities and transactions are accounted for in relation to subsidiaries, joint arrangements, associates and investments as well as what disclosures should be made about respective interests. The CDSB paper notes that in the absence of an equivalent standardised approach to organisational boundary setting for non-financial corporate reporting purposes, it is not always clear how information prepared to comply with national legislation or under voluntary schemes, is 'consolidated' into a mainstream corporate report taking into consideration all entities included in a corporate group. As the CDSB paper explains, this reduces the transparency, reliability and comparability of information. For example, performance indicators and intensity metrics become difficult to create, compare and understand where the boundary selected for non-financial reporting does not align with the basis on which financial or production-related information has been prepared. Performance results and inventory figures may also be distorted. Furthermore, lack of clarity may lead to double counting of information or indeed double non-accounting.

174 The CDSB paper discusses how the concept of consolidation is firmly established in mainstream reporting practice in so far as the preparation of financial statements is concerned. However, the extent and how 'consolidation' is applied to non-financial reporting is less clear. The NFRD indicates that consolidation is required for non-financial reporting, and the content and scope of non-financial reporting seems to automatically extend the boundary of the organisation beyond those matters over which it has direct control and significant influence. This results from the fact that some of the most significant environmental and social risks and opportunities may be found outside a company's organisational boundaries, in the supply chain and the environment.

175 There is a need to reconcile non-financial reporting requirements that, by definition, extend beyond the established boundaries as organisations have taken different approaches to resolving this dilemma. The CDSB paper discussion summarises that although existing practice is varied, there is evidence of some coalescence (at least by CDSB, IIRC and SASB) around the view that non-financial results should be prepared according to or should be capable of reconciling with financial information prepared according to financial consolidation rules. This does not preclude other information being provided separately if it exposes the reporting organisation to risk.

176 In the CDSB paper, it is noted that organisational boundary approaches selected by 402 of the Global 500 companies that responded to CDP in 2011, show that operational control is the most selected approach. Although there is no obvious statistical evidence of trends within sectors, 20 of the 402 companies that make up the population in the first table of Figure 33 are categorised as being in the utilities sector. Of those companies, six used the equity share approach, six financial control and six used the operational control approach, with two companies indicating that they used 'other' approaches. This would suggest an even spread of approaches amongst Global 500 utilities companies. The second table of Figure 33 below shows the same information from CDP disclosures for 2012. Again, operational control is the most used approach.

Figure 33

Table 1 – Organizational boundary approaches for reporting

Scope 1 and Scope 2 GHG emissions to ***CDP in 2011***

Organizational boundary approach	Number of companies
Equity share	17
Financial control	103
Operational control	244
Other	38
Total	402

Table 2 – Boundary selection, CDP 2012 investor programme (CDP, 2013)

Organizational boundary approach	Number of companies	%
Equity share	1,248	55.15
Financial control	599	26.47
Equity share	78	3.45
Not specified	188	8.31
Other	**150**	**6.62**

Source: Proposals for boundary setting in mainstream reports – Discussion paper on organizational boundary setting by groups of companies for non-financial reporting purposes, CDSB (2014) – page 10

177 The research for the 2019 ACT report across 1 000 companies who were subject to the NFRD requirements, identified that, whilst the NFRD asks companies to focus not only on their direct operations, but also on their supply and subcontracting chains …

a) … over three-in-four of the companies assessed do not provide information about supply chain transparency in their reports;

b) … less than 1% of the companies assessed publicly list their suppliers, even in high-risk sectors;

c) The notable exception is the Apparel sector in which 36% of assessed companies provide at least a general description of the location of their supply chains, and an additional almost 14% disclose the list of the actual suppliers;

d) In the case of GHG emissions, more than two-thirds of the companies assessed provide specific KPIs for direct emissions (scope 1). However, this drops to little more than half when emissions from energy use are considered (scope 2), and just over one-third when applied to the company's value chain (scope 3).

178 A scholarly article published in 2013 by A Smith *'An Analysis of GHG Reporting Practices and their Implications for the Design of Reporting Programmes'*, mentions unpublished research which indicated that the choice of boundary can change GHG emissions results by as much as 73% in one case.

179 A study carried out by Oxford Brookes[72] found that 72% of FTSE 100 sustainability reports adopted very narrow reporting boundaries, restricting the scope of responsibility or using illustrative examples to suggest wider compliance, while in reality providing information that could be described as 'greenwashing'. According to the same study, other companies – 26% of the FTSE 100 – widened the boundary of their sustainability reporting to include impacts derived from operations they owned, controlled or significantly influenced.

Supply chain

180 The scope of data goes beyond the legal boundaries of a reporting entity. The purchase of goods and services can affect the impact an organisation has on society and increase its exposure to risk.

181 The NFRD requires companies to focus not only on their direct operations, but also on their supply and subcontracting chains. Yet according to the research carried out for the 2019 ACT report, over three in four of the sample of 1 000 companies analysed, do not provide information about supply chain transparency in their reports, with less than 1% publicly listing their suppliers, even in high-risk sectors.

182 Obtaining accurate and reliable information from an organisation's supply chain poses challenges around availability, quality and reliability. Such information from the supply chain might not always be available to a company, or not at the same standard as its own non-financial information.

183 As a result, the process for producing this type of information relies on estimates and judgements. There are different approaches for the estimation of information not readily available from the supply chain. Each company is free to choose the one that works for them, something that impacts comparability. Similarly, there are no requirements for disclosure of the methodology used, rendering it even more difficult for users of the information to consider it in their decision-making process.

184 For example, reported Scope 3 data may not always be complete and the way it is collected/arrived at can be highly subjective. The GHG Protocol Scope 3 Standard is the only internationally accepted method for companies to account for these types of value chain emissions. In a 2016 article *'The Scope 3 Emissions Challenge'*[73] the author notes that according to some estimates[74], more than 80% of the GHG impacts for most companies occur outside of their own operations. The article author concludes that from an environmental and business perspective, managing Scope 3 emissions becomes crucial, and if it can be found meaningful and measurable reduction targets, then this could represent not only the biggest opportunity in terms of potential emission reductions, but also potential financial savings.

185 An article published by ecoact in 2016[75] notes that measuring emissions in the value chain helps to identify key focus areas and where action needs to be taken. It also contributes to a range of business needs as well as addressing stakeholder demands.

186 Measuring Scope 1 and 2 emissions is standard practice for many large and listed companies. Research into the sustainability reporting performance of the FTSE 100 by ecoact[76] found only one company not providing this information publicly. According to another factsheet by ecoact *'Climate and the value chain: A roadmap for Scope 3 emissions reductions'*[77], in the context of stakeholder demand and the need to manage business risk, companies are increasingly looking to understand emissions in their value chain (Scope 3 emissions). FTSE 100 companies are already reporting some Scope 3 data. In many cases, these companies are reporting emissions that are easy to calculate, for example business travel. But these emissions may not be the most important to the business. In fact, the ecoact research showed that only a quarter of the FTSE 100 companies are performing materiality assessments of their Scope 3 emissions, suggesting that in many cases the reported Scope 3 categories may be the ones that are the most readily available, rather than those which are most significant within the business.

72 The Boundary of Sustainability Reporting: Evidence from the FTSE100

73 The Scope 3 Emissions Challenge, Kathryn Thomas (2016)

74 https://quantis-suite.com/Scope-3-Evaluator/

75 Good value chain: overcoming the challenge of collecting Scope 3 emissions, ecoact (2016)

76 The Sustainability Reporting Performance of the FTSE 100 – Annual Report, ecoact (2019)

77 Plan for Zero: Scope 3. Understanding the environmental impacts of your supply chain maintains your competitive advantage, ecoact

Business model / value creation model

187 The Frank Bold paper[78] comparing the implementation of the NFRD in the UK, Germany, Italy and France, points out that the NFRD requires a brief description of a company's business model to be included in its non-financial statement. However, it does not clarify how the description of the business model should refer to the ESG factors that the non-financial information statement considers. There is therefore a risk that companies provide a description of their business model that is disconnected from the ESG matters at hand (for example the impacts of carbon risk in the forecasting of an energy company), thus undermining the usefulness of such reporting.

188 The Frank Bold paper notes that, from the jurisdictions surveyed, only Italy has clarified the intention of the NFRD by including in its implementing legislation the requirement for a company's description of its business model to expressly refer to the ESG factors that are being reported on.

189 There is similar lack of clarity in the NFRD over the extent to which the non-financial information statement should make specific reference to a company's financial information.

190 The abovementioned Frank Bold paper notes that each of the countries surveyed makes reference to the fact that the non-financial information statement should refer to, and include additional explanation of, amounts included in the company's financial statements, although Germany and France qualify the need for such references on a 'required' basis. The Frank Bold paper concludes that further guidance is needed on how such references might be made, the level of detail they might go into, and how companies should integrate non-financial information into their forecasting, in order to strengthen this aspect of corporate reporting.

191 ESMA has provided guidance on how to deal with this aspect of reporting in its Public Statement *'European common enforcement priorities for 2020 annual financial reports'*[79]. ESMA emphasises that in order to enable users of non-financial statements to get an understanding of the business model and its relationship with and implications for the non-financial matters, issuers are expected to provide information about their strategy together with its implementation, and explain how the business model impacts on, and is being impacted by, the non-financial matters, taking into account their short-, medium- and long-term goals/objectives. ESMA further considers that it would be helpful if issuers were to disclose their definition of value creation and to explicitly mention, if relevant, the disclosure framework which provided this definition, and also to describe how an entity generates and preserves value through its products or services and provides an overview of how a company operates and the rationale of its structure by describing how it transforms inputs into outputs through its business activities. It also stresses that issuers are expected to highlight and explain when material changes to their business model and their value creation ability have taken place in the reporting year.

192 In the 2019 report critique for the IIRC by ACCA[80], that provides a picture of integrated reporting trends and developments over a four year period, the authors note that quality ratings for the description of the business model have been declining, and this is an area that the IIRC was contemplating to address in any revision of the <IR> Framework in 2020. They go on to note that this may be a result of the predominance of financial organisations in the sample reviewed which might find explaining their business model more difficult than other companies.

193 The ACCA report above also notes that information about strategy and resource allocation is not always linked to the value-creation process over the shorter and longer time frames. It further mentions that ACCA carried out reporting reviews for their corresponding 2017 research that investigated the links of strategy and value creation over the short, medium and longer term and the challenges for those preparing the corporate reports. Among the issues noted were a focus from management on the short-term, even where a business might be investing in long-term projects. Also, strategy and reporting may be handled by different teams in the organisation, which does not facilitate clarity of reporting in this respect. Furthermore, strategy and value creation inevitably include matters of commercial sensitivity and of interest to competitors or regulators, which may be difficult to address by providing the right and balanced level

78 Comparing the implementation of the EU Non-Financial Reporting Directive in the UK, Germany, France and Italy, Frank Bold (2017)

79 European common enforcement priorities for 2020 annual financial reports, ESMA (2020)

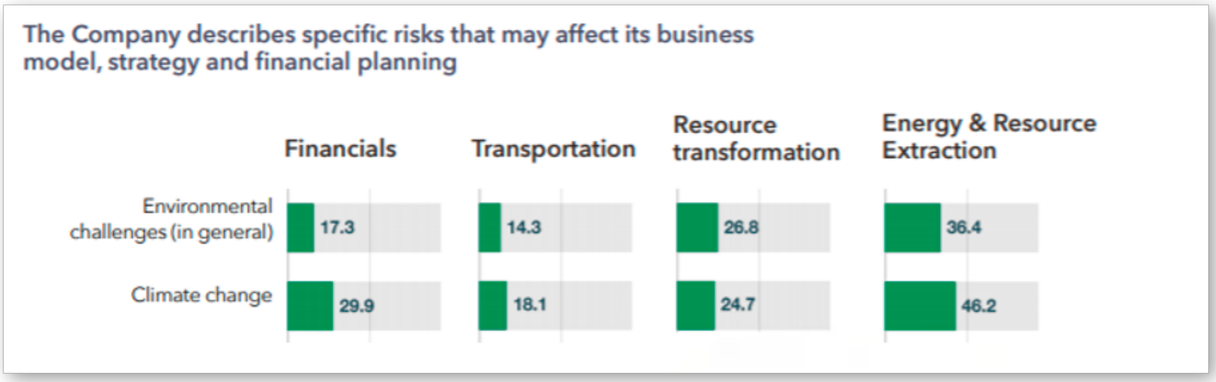
80 Insights into integrated reporting 4.0: the story so far, ACCA (2019)

of detail in corporate reports. Despite such difficult aspects, the ACCA report notes that some organisations claimed that their reporting had evolved and improved by responding to feedback from stakeholders.

194 For the 2019 ACT report, the assessment of the reporting of a sample of 1 000 companies has considered the presentation of business model disclosures both from a cross-sectoral as well as a sector specific perspective. The 2019 ACT report notes that the cross-sectoral perspective is useful to map the issues companies consider from a strategic perspective, even though materiality of a sustainability issue for any company depends on the company's sector and operational context. It also notes that on the other hand, the sector-specific overviews offer insights into the level of strategic awareness among companies of sustainability risks and impacts which are clearly associated with their sector. The overall results of the ACT assessment show that strategic disclosures are not common. The comparison with thematic results presented in various sections of the 2019 ACT report further indicate that there is a significant number of companies which provide information on their policies, risks, outcomes, and KPIs, but not on strategic, business model-related information.

195 The diagram in Figure 34 below presents one example of the findings from the 2019 ACT report for sectors that are highly exposed to climate-related risks and for which reporting on these risks from a business model perspective can be reasonably expected to be high.

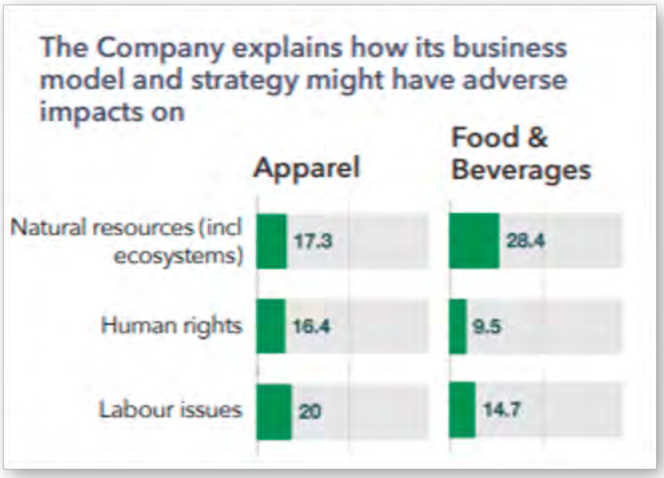
Figure 34: Reporting of climate-related risks for sectors that are highly exposed to such risks



Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, Alliance for Corporate Transparency (2019) – page 38

196 Another example, Apparel & Textiles companies and Food & Beverages companies that mostly rely on outsourced production located in regions with systemic human rights and natural resources abuse, including labour conditions and deforestation. Yet, the findings presented in Figure 35 show that only 10 30% of these companies report on these issues from a business-model perspective.

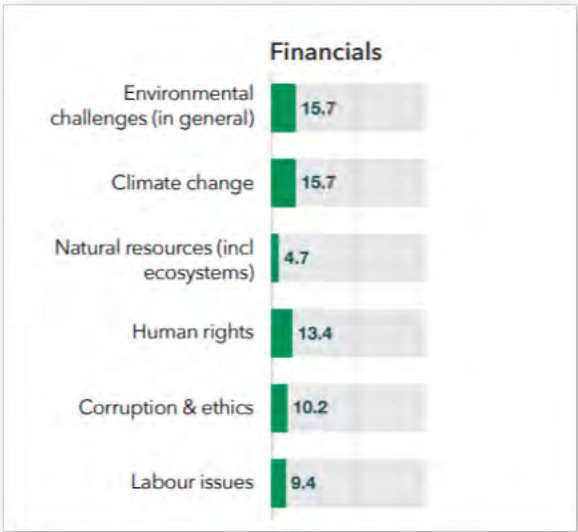
Figure 35: Reporting by companies in sectors relying on outsourced production located in regions with systemic risks



Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, Alliance for Corporate Transparency (2019) – page 38

197 A third example, financial companies are connected through their investment or lending activities with all types of sustainability impacts. The diagram in Figure 36 shows the extent to which they consider the related risks and impacts strategically important for their business models.

Figure 36: Extent, to which financial companies consider sustainability related risks and impacts as strategically important for their business models ...



Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, Alliance for Corporate Transparency (2019) – page 38

Reporting of quantitative goals and targets as well as data to track progress

198 There are several different definitions for the types of metrics presented by a company and used by an investor. There is no common nor correct way to define a number of these items, as they can vary between companies and investors, and even within those organisations.

199 Performance metrics include both financial and wider metrics. Financial metrics are those that are derived based on Generally Accepted Accounting Principles ('GAAP'), as well as those that incorporate financial information, but which are not the same as those measured under GAAP, e.g. adjusted EBITDA, operating earnings and free cash flows.

200 Many non-financial metrics are expressed in non-monetary units, e.g. employee engagement results, brand awareness/customer satisfaction scores, market share or environmental measures, which can either be standardised or company specific. However, due to a lack of a clear framework or defined metrics for reporting, there are a number of challenges both in comparing organisations with one another but also in monitoring and tracking year on year performance within individual organisations, as approaches to non-financial reporting can vary from one year to the next.

201 In addition to the above, there are clear difficulties in the quantification of impacts, including the inconsistent methods for taking into account non-financial information stemming from an organisation's supply chains (see section on reporting boundaries).

202 The examination of the sustainability reports of the 1 000 largest companies in Europe for the 2019 ACT report, noted the weakness of companies in reporting quantitative goals and targets, as well as data to track progress:

a) 22% of companies presented sustainability indicators in summary form, in stark contrast to the way financial metrics are disclosed.

b) 14% of companies reported on how they align their climate-change targets with the Paris Agreement goals or with the SDGs, and measure their progress accordingly. It appears that most companies need to improve their reporting on targets on climate change, with specific risk mitigation strategies.

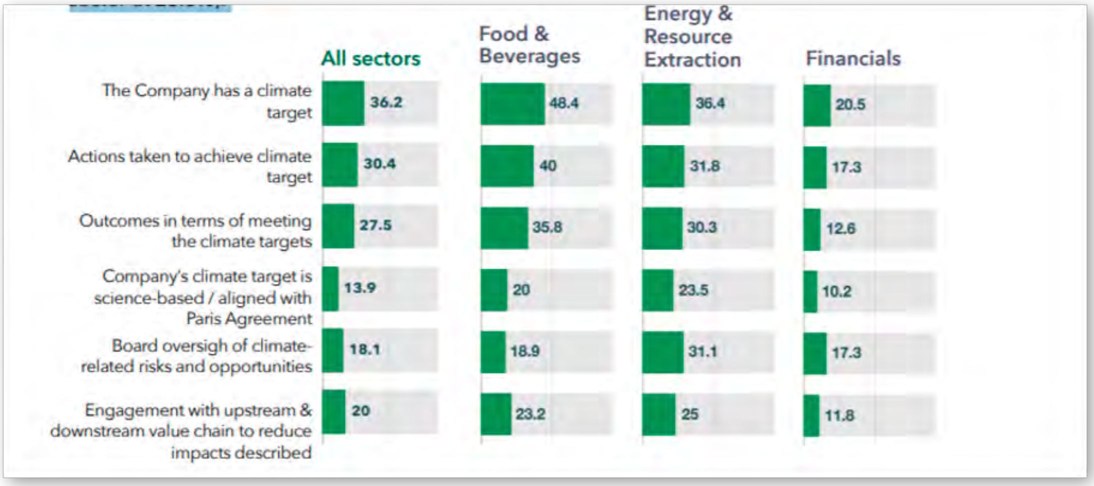
c) On social issues, companies in the research were too often conflating social goals with treatment of employees.

d) Strategic information on the integration of sustainability in the governance of companies was often missed, as the NFRD does not explicitly require such disclosures.

e) The clarity of reporting is often affected by the lack of homogeneity in the frameworks used, and in the presentation of KPIs which are often scattered across the narrative.

203 In addition to the examination of the specificity of company climate change policies, the analysis for the 2019 ACT report assessed whether company reports describe concrete targets related to climate change mitigation. The analysis considered only targets linked to the primary impact companies can effectively mitigate. Interestingly, only 36.4% of companies from the Energy & Resource Extraction sector report on climate-related targets. Companies from the Financial sector are those disclosing climate related targets the least (20.5%), which is worrying, given the sector's important role in contributing to the low-carbon transition. With regards to information on science-based targets, numbers recorded are even lower. From a cross-sectoral perspective, only 13.9% of companies disclose relevant data. Even in high scoring sectors, less than 30% of companies report relevant data (Energy & Resource Extraction sector at 23.5%).

Figure 37: Analysis of whether company reports describe concrete targets related to climate change mitigation

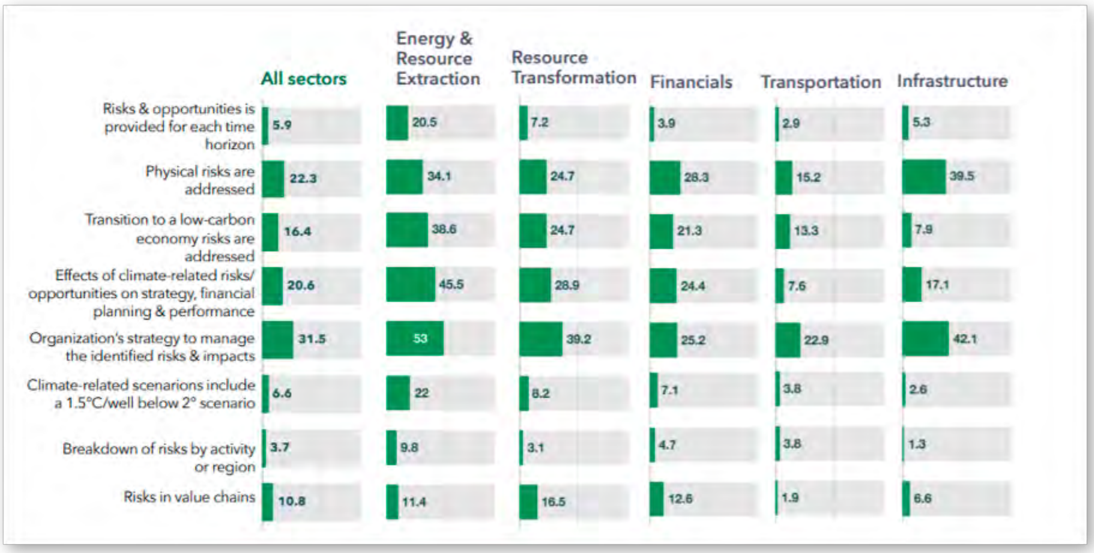


Source: [An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive](), Alliance for Corporate Transparency (2019) – page 16

Risks

204 the analysis of the reporting of 1 000 companies for the 2019 ACT report showed that there is a lack of maturity especially for disclosure on climate-related scenarios used to inform company strategies (6.6%). In this respect, sector differences are striking. While 22% of companies in the Energy sector report on climate-related scenarios aligned with 1.5°C or well below 2°C, just over 2% in the Infrastructure provide sufficient information (2.6%). With regards to the Finance sector, in addition to data in the overview below, very few organisations are specific about the exposure of their lending, investment and underwriting activities to sectors contributing to climate change (13.4%) or provide an estimation of the exposure of assets (financial, non-financial, under management) or the value of collaterals to climate-related risks (3.1%).

Figure 38: Extent to which companies in the most exposed sectors report information corresponding to specific TCFD criteria



Source: [An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive](), Alliance for Corporate Transparency (2019) – page 17

KPIs

205 With regards to specific metrics, the analysis of the reporting of 1 000 companies for the 2019 ACT report showed a relatively good image when considering the disclosures of highly polluting sectors. When looking at companies in the Energy & Resource Extraction, Infrastructure, Resource Transformation and Transportation sectors, Scope 1 and Scope 2 GHG emissions are disclosed by 76.6% (87.1% in the Energy & Resource Extraction) and 60.7% respectively. Lower values are observed in the case of Scope 3 emissions, where an average of 35% of all companies disclose such type of data. Even in high-impact sectors such as Apparel & Textiles and Food & Beverages, a majority of companies do not provide information on Scope 3 emissions (62.7% and 71.6% respectively). Of those that do, only a small fraction report on emission targets. GHG intensity indicators were reported by 29.8%, 13.4% and 5% for Scope 1, 2 and 3 respectively.

206 The CDSB 2018 review of 80 European companies' annual reports[81] found that companies have been able to disclose decision-useful information in line with the NFRD, however in some cases environmental targets/goals lack corresponding KPIs to show performance and progress towards them.

207 The 2019 report critique for the IIRC by ACCA[82] notes that most of the concerns raised by preparers of integrated reports in line with the IIRC Framework, were the problems they had in measuring and quantifying the impact on the different capitals, especially the environmental and social outcomes of their business. At times they struggled to find indicators that really reflected the value-creation process and others lacked practical value. Some preparers therefore discussed the impacts in a qualitative way. Others were ambitious and tried not only to quantify but also to monetise the impacts. Some traced the issue back to the business model in showing how the organisation uses or affects the various capitals.

208 The IIRC Framework expects that the report should record performance and progress towards strategic objectives. However, in the review by ACCA for the 2019 report critique, this aspect achieved average relative scores and was disappointing given that the information about strategic targets and performance must be readily available and would be of particular interest to providers of financial capital and most other stakeholders.

209 In the 2019 sample of 48 reports reviewed by ACCA, only 36% provided targets for the identified KPIs in full, 43% only for some and 21% provided no targets for any of their KPIs.

Connectivity

210 A 2020 EY Climate Change and Sustainability Services (CCaSS) Institutional Investor survey[83], conducted on a sample of 300 institutional investors globally, noted that among the top five challenges of investors regarding the usefulness and effectiveness of ESG reporting, is the disconnect between ESG reporting and mainstream financial information.

211 The 2020 report of the European Lab Project Task Force on climate-related reporting[84], that reviewed the reporting of approximately 150 companies from Europe and beyond, noted that the various relevant sections of companies' reports are not always clearly articulated or well-connected to allow getting a complete picture of companies' approaches to assessing and managing climate-related risks and opportunities. It also noted that climate-related reporting is not always included in companies' financial filings, but can often be found in other company documents. Consequently, it is sometimes difficult for users of corporate reports to understand how climate risks are evaluated and managed within the company, and who is responsible.

212 The connectivity between financial and non-financial information is crucial. Through corporate reporting, organisations can communicate their individual story based on their business and value creation models. By doing so, some of the criticism over the ability of financial reporting to meet the needs of key stakeholders could be overcome.

213 Bias towards quantification should be avoided, as narrative reporting is powerful and can provide relevant information and insights beyond the numerical facts.

81 First Steps: Corporate climate & environmental disclosure under the EU Non-Financial Reporting Directive, CDSB (2018)

82 Insights into integrated reporting 4.0: the story so far, ACCA (2019)

83 How will ESG performance shape your future?, EY (2020)

84 How to improve climate-related reporting: A summary of good practices from Europe and beyond, European Lab Project Task Force on climate-related reporting (2020)

214 Certainly, online and digital reporting platforms have the potential to link non-financial reports to other reports and provide cross-references between different parts. Technology can get ahead of regulation, which in some cases restricts the formats in which reporting can be done.

215 The CDSB 2018 review of 80 European companies' annual reports[85] found that companies have been able to disclose decision-useful information in line with the NFRD, however:

a) Many do not make the connection between the information disclosed. For example, a report may describe environmental policies, without explaining the company's strategies to implement them;

b) Coherent and connected reporting demonstrates the relationships between vision, mission, risks, policies, strategies, targets and KPIs. Reporting however is not always easy to navigate, read and search. This is important to aid user understanding.

216 Connectivity seems to be a principle with which some companies struggle. The 2019 report critique for the IIRC by ACCA[86] notes that some users seem to interpret the IIRC Framework as specifically the interconnection between the different capitals and how investment and good performance for one may positively or negatively affect others.

217 The IIRC Framework states the objective of connectivity as follows: 'An integrated report should show a holistic picture of the combination, interrelatedness and dependencies between the factors that affect the organisation's ability to create value over time'. It considers that there should be connectivity in different forms, including between: content elements, the past, present and future, the six capitals, financial and other information, quantitative and qualitative information, information for management and that reported externally. There may be a disconnect between non-financial indicators and financial ones because of time lags between them. In the same way, output measures may be ahead of outcome measures.

218 The issue of connectivity was also highlighted by respondents to the research on stakeholder perceptions of non-financial reporting conducted by BEIS in 2019[87]. Below are some relevant comments from respondents to this research:

a) 'There is a glaring disconnect between trends and risks discussed in the strategic report and key accounting assumptions and estimates used in the accounts themselves.' ClientEarth

b) A respondent highlighted the number of reports required, from a strategic report through to a directors' report, which means that reporting can get quite silo-ed.

c) 'There are lots of different pieces which, either through tradition, legislation or regulation have to be disclosed somewhere. However, it doesn't lead to a document which has a natural start, middle and end, which people can see and be told the story. It becomes quite broken up and I think that the legislation has made this worse rather than made it better.' Companies Alliance

Reporting impacts

219 According to the 2019 ACT report that analysed the reporting of a sample of 1 000 companies, the NFRD's firm intent to link 'policies, risks and results' together in the reporting, is falling short, with most reporting entities disclosing inputs rather than outcomes. The absence of 'impact' in the reporting demands urgent attention both in reporting companies and in the revision of the NFRD itself.

220 The 2019 ACT report notes that this issue is further accentuated by the fact the companies continue to use non-financial reporting as a means of marketing and providing 'boiler plate' disclosures that do not mean much.

221 On climate change, 82% of companies have policies, but only 35% have targets and even fewer – 28% – report on their outcome.

85 First Steps: Corporate climate & environmental disclosure under the EU Non-Financial Reporting Directive, CDSB (2018)

86 Insights into integrated reporting 4.0: the story so far, ACCA (2019)

87 Stakeholder Perceptions of Non-financial Reporting BEIS research Paper No. 2019/027, UK Department of Business, Energy & Industrial Strategy (2019)

222 Despite the controversies about data privacy and cyber security, 84% of ICT companies report data protection policies, but only 8% describe outcomes in terms of meeting policy targets.

223 Even where there are targets, this does not mean they are meaningful. The major extractives company in the sample analysed for the 2019 ACT report, that sets its objective as 'the wellbeing of our people, the community and the environment is considered in everything that we do,' discloses 'warm words' rather than concrete targets, which are espoused in too much of today's reporting.

224 The 2019 ACT report further notes that the problem of a failure to address concrete issues, targets and principal risks, remains largely unchanged between the 2018 and 2019 research cycles carried out by the Alliance for Corporate Transparency.

225 Of the 105 companies in the Energy, ICT and Health Care sectors analysed in both years, there was actually a reduction in the number of companies reporting specific issues and targets on climate change, a similar decrease in the number of business partners covered by human rights risk statements and a marked increase in companies that chose to give no information at all about the general structure and risks of their supply chain (from 51 to 70 companies).

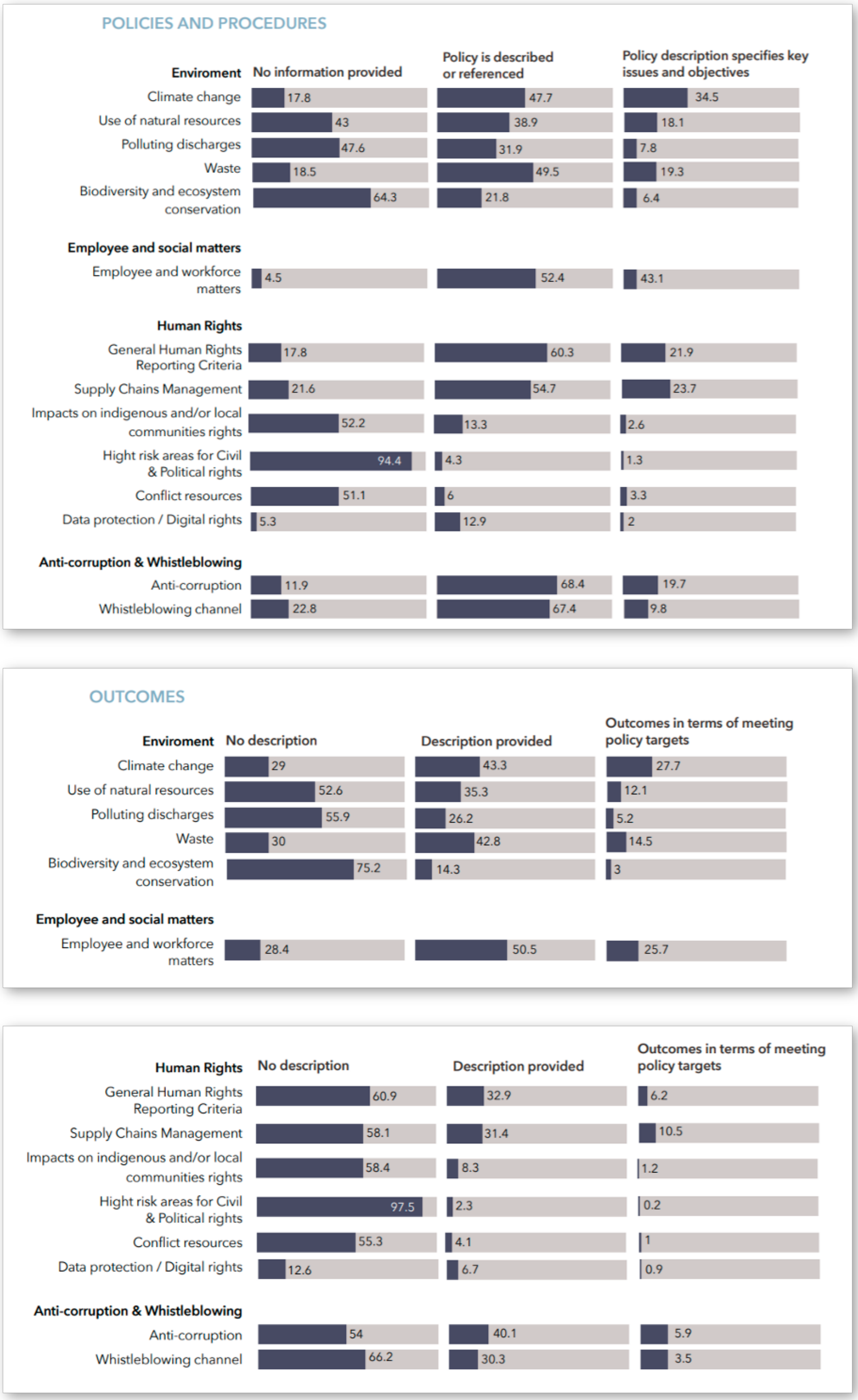
226 Data on universally or nearly universally applicable topics, namely climate change, employee and social matters, human rights, and anti-corruption, show that only a minority of companies provide information specific enough to understand company policies. This minority is stronger regarding climate change and employee matter disclosures (34.5% and 43.1% respectively), than for human rights (21.9%) and anti-corruption (19.7%). These numbers drop, especially for climate change, in the analysis of quality of disclosure of risks as well as policy outcomes in terms of targets set by the company.

227 As the 2019 ACT report points out, this suggests firstly that while many companies, albeit still a minority, disclose fairly detailed policies, significantly fewer companies provide information which is necessary to understand their situation and future development. The analysis of detailed qualitative criteria in the 2019 ACT report shows that the actual number of meaningful disclosures is even lower.

228 Secondly, the 2019 ACT report notes that for each category the number of companies reporting on individual sustainability issues is significantly higher than that of companies providing specific information on risks and implementations of their policies. This implies that the topic is either not material, and thus should ideally not be included in the disclosure of such companies, or that it is indeed material, but companies fail to provide material information.

229 Thirdly, always according to the 2019 ACT report, the results imply poor connectivity between the disclosures of individual categories of information. The detailed analysis in the 2019 ACT report confirms such a problem, and further points at weaknesses in how companies report on the integration of non-financial information with their overall strategies.

Figure 39: Reporting practices with respect to different sustainability issues

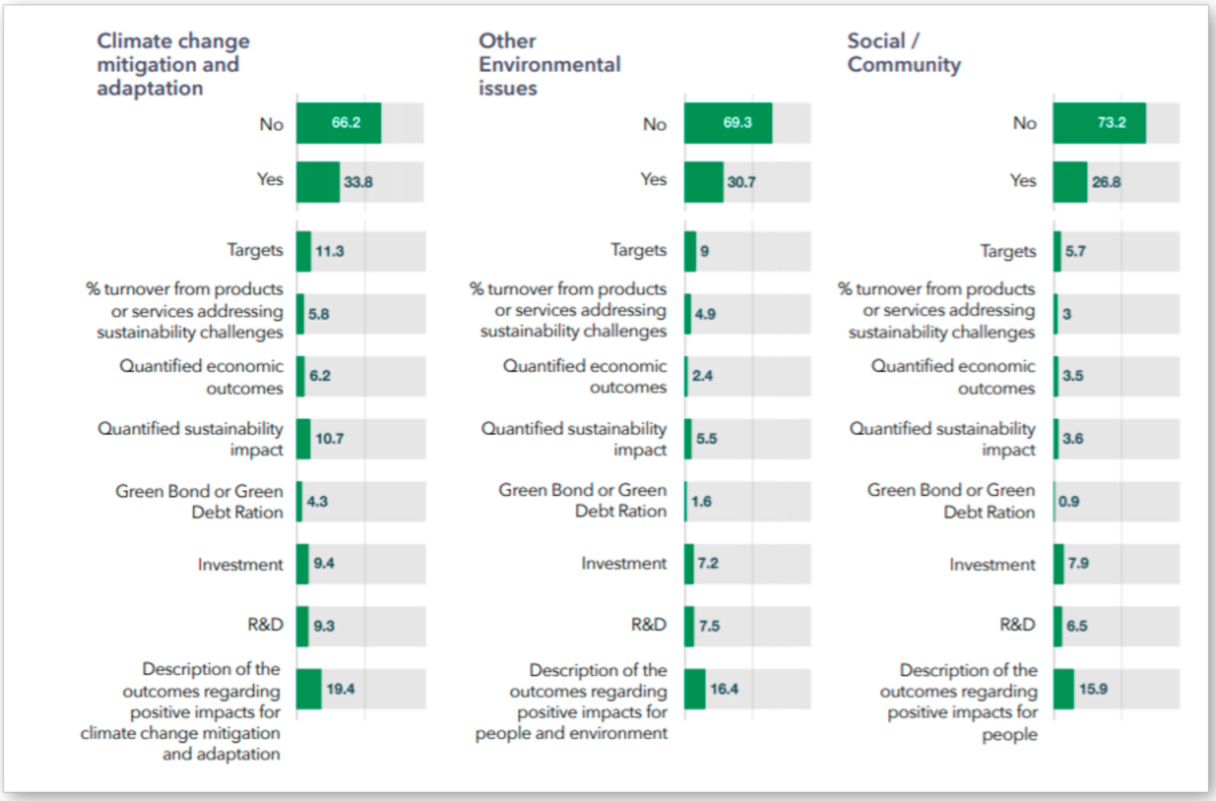


Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, Alliance for Corporate Transparency (2019) – pages 14 and 15

Positive impacts by products and services and sources of opportunity

230 According to the 2019 ACT report, based on the sample of 1 000 analysed, there is a gap between the proportion of companies reporting on strategies and initiatives for climate change, other environmental issues and social/ community matters (33.8%, 30.7% and 26.8% respectively), and those disclosing relevant and decision-useful information around such strategies. This is the case when looking at corporate disclosure on the turnover from products or services addressing sustainability challenges for these matters (5.8%, 4.9% and 3% respectively), and data on investment in the associated described strategies (9.4%, 7.2% and 7.9% respectively). Reporting on this is key if companies are to be transparent and provide investors with information about the sustainable activities they engage in, in line with the (future) requirements of the EU taxonomy for sustainable activities.

Figure 40: Companies reporting on strategies or initiatives around products or services that focus on sustainable development opportunities



Source: An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive, Alliance for Corporate Transparency (2019) – page 94

Long-term value creation

231 To be of value, corporate data must show companies' long-term value creation. The outlook facing the business and the challenges and uncertainties likely to arise in pursuing its strategy are of great interest to stakeholders. This is an area where reports could be improved.

232 A report by PwC in 2016 *'A foot in the past and an eye to the future'*[88], addresses the importance of forward-looking information in company reporting and presents trends and practices based on the review of the 2015 reporting of 52 FTSE 350 companies. This report highlights that a reluctance to provide meaningful forward-looking information is

88 A foot in the past and an eye to the future, PwC (2016)

evident in different forms of corporate reporting and could reflect a natural caution by management or legal or regulatory restrictions.

233 A 2018 report by EY *'Does your nonfinancial reporting tell your value creation story?'*[89] notes that investors seek more forward-looking information and closer connections between ESG activities and business. The EY report quotes an investor saying 'it's one thing for a company to report its ESG achievements over the past 6 months, 12 months, or 3 to 5 years, but we'd like to see what that will look like 20 or 30 years in the future'.

234 The Coalition for Inclusive Capitalism and EY brought together 31 companies, asset managers and asset owners, to identify new metrics to measure and articulate long-term value to investors and other stakeholders – the Embankment Project for Inclusive Capitalism (EPIC). EPIC published a report in 2018[90]. This report stresses that for a company to effectively measure and articulate its long-term value creation potential, a framework is necessary that combines a broader view on value creation beyond financials, with a broader stakeholder perspective and long-term orientation. It also states that although many of the existing frameworks may cover one or two of these aspects across a defined field, such as human or natural capital, none of them are sufficiently comprehensive.

235 The 2019 report critique for the IIRC by ACCA[91] highlights that during their 2018 reviews they explored with some preparers the management's perception of the outlook facing the business and what challenges and uncertainties are likely to arise in pursuing its strategy. It notes, that most interviewed preparers argued that although liability concerns should not hold back reporting of future prospects, there is concern that by discussing possible actions, reporting entities may be seen as committed to them and that the discussion should avoid any cases where talking about risk situations might heighten their likelihood. It also notes that some companies might find discussing the outlook in their integrated report easier than others, because they must produce a forward plan for their regulator.

Exposure to risks

236 To be of value, corporate data must show companies' exposure to risks. As the regulatory framework of the European Green Deal[92] comes into play, companies will face higher regulatory risks if they do not reduce their environmental impact. The NFRD should call for more accurate and comprehensive reporting of risks and opportunities linked to climate, the environment and social aspects.

237 The 2019 report critique for the IIRC by ACCA concluded that in order to understand strategy, performance and prospects, it is crucial that an integrated report assesses the risks to which the organisation is exposed. This comes out as an area of relative strength in reports reviewed by ACCA over a period of four years, identifying the risks that could affect value creation over the shorter and longer term and how the company was mitigating them. Companies have got more accustomed over recent years to discussing risks, not only via the IIRC framework but also as required by regulation or accounting standards. On the other hand, some reports were less forthcoming about the opportunities that also presented themselves. This seems aligned with the requirements of investors and other providers of financial capital, who often seem more interested in understanding risks than perceived opportunities. In addition, opportunities may have more commercial sensitivity.

238 The abovementioned ACCA report notes that in the interviews they carried out for the 2018 reviews, as regards opportunities, some of the preparing companies cited both less investor interest in them and commercial competitive concerns. There were also issues about overpromising investors about the potential of opportunities. These companies claimed that readers expected some degree of prudence and restraint and that this aided credibility. Some banks, for example, assessed and reported risk and opportunities together when discussing the different issues faced by the business.

89 Does your nonfinancial reporting tell your value creation story?, EY (2018)

90 The Embankment Project for Inclusive Capitalism, Coalition for Inclusive Capitalism (2018)

91 Insights into integrated reporting 4.0: the story so far, ACCA (2019)

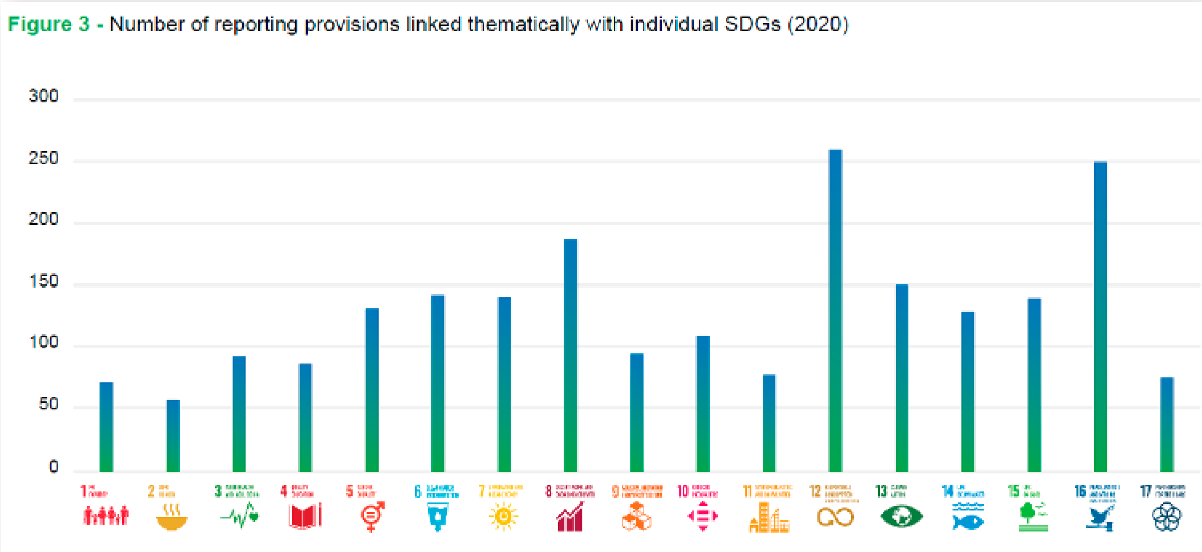
92 https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal_en

Topics

239 In line with NFRD provisions, companies must currently disclose information on four non-financial matters: environment, social and employment, human rights, and corruption and bribery.

240 Figure 41 from the Carrots & Sticks 2020 report[93] shows the number of sustainability reporting provisions linked thematically to individual SDGs.

Figure 41: Number of reporting provisions thematically linked to individual SDGs



Source: [Carrots & Sticks – Sustainability reporting policy: Global trends in disclosure as the ESG agenda goes mainstream](), GRI and University of Stellenbosch Business School (2020) – page 10

241 This breadth of reporting provisions across the different SDGs leads to a heterogeneous coverage of reporting topics across companies. This is validated through the findings of the 2019 ACT report which presents an analysis of the sustainability reports of 1 000 companies pursuant to the NFRD – information in this respect is included in Section 2 of this assessment report.

Structure

QUESTION 3.2:
What are the issues identified regarding how non-financial information is displayed?

242 The current landscape for non-financial reporting is fragmented.

93 Carrots & Sticks – Sustainability reporting policy: Global trends in disclosure as the ESG agenda goes mainstream. GRI and University of Stellenbosch Business School (2020).

243 The Carrots & Sticks 2020 report shows the diversity of reporting formats, and summarises the situation as follows:

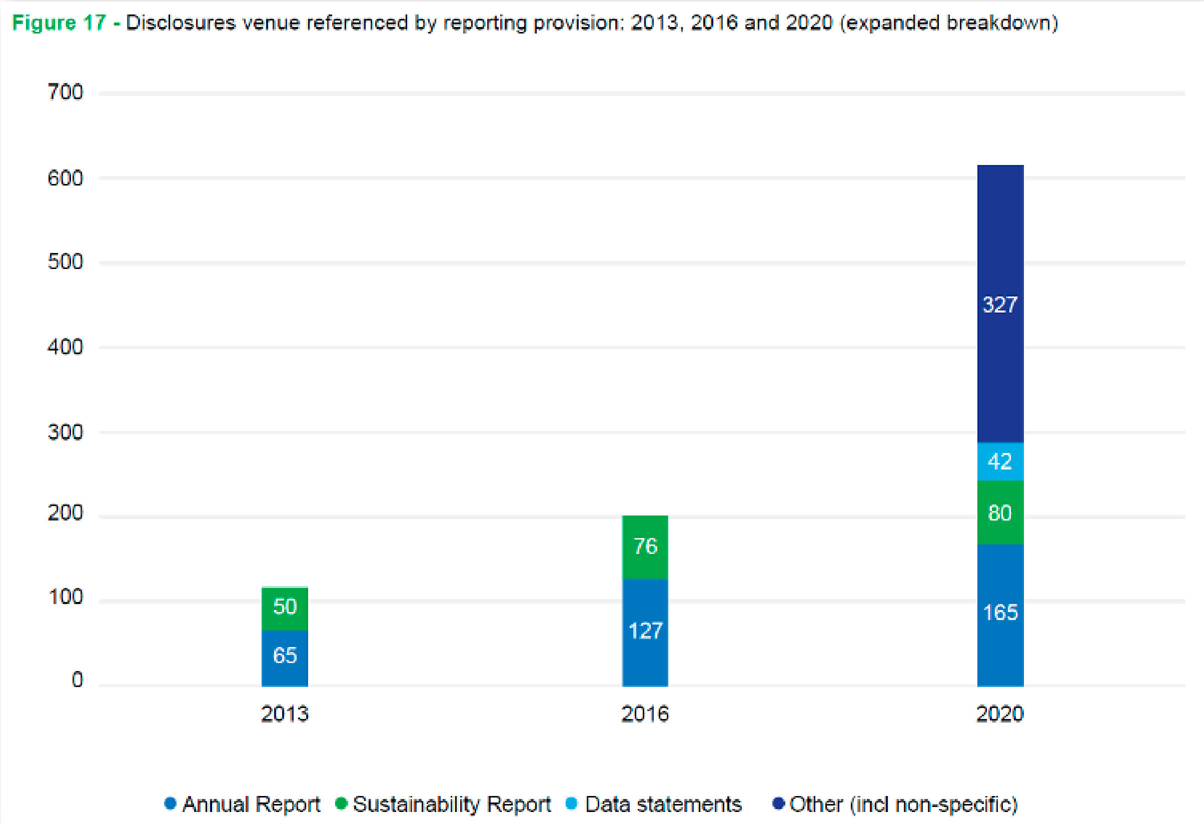
Quote 1

'Our 2020 stock-take looked in greater detail at disclosure venues and concluded that the variety of forms is too diverse to give a reliable conclusion on trends. While we found 165 cases explicitly refer to annual reports (or components thereof such as management discussion & analysis, directors' report or governance report) and 80 cases that mention sustainability or non-financial reports, our latest data also includes 175 cases where nothing is specified and 42 cases where specific reference is made to data disclosures and statements.

Other disclosure vehicles referred to include thematic reports, plans and online disclosure. The diverse nature of these specifications possibly calls for some standardization, for example consideration by regulators of what specifications are most effective and efficient in the digital age. Greater interest in data and the format in which data is communicated need to address ongoing concerns related to the reliability, comparability and timeframe of data disclosed. Reporting format or type also need to consider the specific user audience addressed and their information needs.'

Source: Carrots & Sticks – Sustainability reporting policy: Global trends in disclosure as the ESG agenda goes mainstream, GRI and University of Stellenbosch Business School (2020) – page 31

Figure 42



Source: Carrots & Sticks – Sustainability reporting policy: Global trends in disclosure as the ESG agenda goes mainstream, GRI and University of Stellenbosch Business School (2020) – page 31

244 Ultimately, the Carrots & Sticks 2020 report concludes that 'it is unclear whether recommendation of disclosure venue by regulators effectively consider the user target audience'.

245 The 2017 Frank Bold paper[94] comparing the implementation of the NFRD in the UK, Germany, Italy and France, concludes as follows:

Quote 2

'Of the four jurisdictions considered in this paper (UK, France, Germany and Italy), only the UK and France have gone beyond the requirements of the Directive to require the non-financial information statement to be included in the annual management report (rather than either being included in the annual management report, or being prepared as a separate report). The requirement for inclusion in the annual management report gives gravity and prominence to the non-financial reporting statement, which is circulated to shareholders on a yearly basis ahead of the general meeting. This also improves the integration of financial and non-financial reporting which can be seen as a positive step.

Conversely, in Germany, if the non-financial information statement is not included in the annual management report, it can be published on the company's website up to four months afterwards, provided that the annual management report refers to this publication and the website. This time lag means that a number of shareholders whose attention is captured for the purposes of reviewing the annual management report and preparing for the annual meeting, may be lost, and that the information will therefore not be given the same level of attention. BASF (a German chemical company), Deutsche Bank and Deutsche Börse AG have all said that providing information in a separate report is a step backwards.'

Source: Comparing the implementation of the EU Non-Financial Reporting Directive in the UK, Germany, France and Italy, *Frank Bold (2017) – page 3*

246 A survey conducted by EY on a sample of 300 institutional investors globally[95] highlights some of the challenges in non-financial reporting and includes the disconnect between ESG reporting and mainstream financial information as one of the top five issues affecting the usefulness and effectiveness of ESG reporting.

247 The TCFD recommendations ask for disclosures to be made in financial filings, alongside other financial disclosures. According to the EY Global Climate Risk Disclosure Barometer[96], this element of the TCFD recommendations is yet to be widely implemented. Some companies did include relevant climate-related disclosures within the annual report as part of a discussion on the business strategy in the directors' report or within the operating and financial review (which includes a description of the future prospects of the business). However, the overwhelming majority provided relevant climate-related disclosures within separate non-financial reports, sustainability reports or their Carbon Disclosure Project (CDP) reporting. EY notes that despite the call in the TCFD recommendations, there are several reasons why most companies have not taken the step to include disclosures in their annual reports or directors' reports. The relative immaturity of processes to capture and report on climate change risks is likely to be one reason, as well as the difficulty in setting timeframes on the potential implications of either transition or physical climate-related risks. It can also be difficult to translate these risks into financial implications. However, shareholder resolutions, enforcement of listing rules and regulator focus is likely to force companies to change this in upcoming reporting periods.

Technology

QUESTION 3.3:
What are the issues identified in respect of the means through which non-financial information is reported?

248 The non-financial reporting ecosystem is fragmented at various levels and variables, including data formats, modes of submission, data definitions for certain common elements, business rules, access controls, and validations for similar reporting elements across different forms and regulators.

94 Comparing the implementation of the EU Non-Financial Reporting Directive in the UK, Germany, France and Italy, Frank Bold (2017)

95 How will ESG performance shape your future?, EY (2020)

96 How climate change disclosures reveal business risks and opportunities, EY (2019)

249 Government agencies and regulatory authorities are under increasing pressure to reduce the costs of compliance, both to create economic conditions for business growth and capital allocation and to reduce operating expenses that are typically funded by treasury departments that must do more with less.

250 According to the OECD Regulatory Compliance Cost Assessment Guidance[97], compliance costs are incurred by both regulatory authorities and regulated entities. Regulatory authorities incur costs for publishing, administering, monitoring, and enforcing regulations, including the costs of:

a) Developing and implementing licensing or registration systems;

b) Assessing and approving applications;

c) Processing renewals;

d) Implementing inspection or auditing systems; and

e) Implementing systems for sanctions for noncompliance.

251 The fragmentation regarding technology is classified under six headings below. The information provided is sourced from the report published by IMA in 2020 entitled *'A digital transformation brief: Business reporting in the fourth industrial revolution'*[98] and supporting research.

Non-financial data processes

252 The flows and interfaces between input, throughput, and output across various systems are not aligned and often require manual intervention to ensure that the output of one system is reprocessed in the necessary format to be validated for submission to the next system. It is further connected to multiple output reports, where the need to ensure a single source of truth is essential. For example, the data from a regulated entity's enterprise resource planning (ERP) software needs to be compiled and repackaged in order to meet a regulator's 'form' and 'data format' requirements for filing submissions. Seamless integration between these internal and external interfaces depends on codified standards for data generation, validation, and sharing.

Data types

253 This is the most common area of fragmentation. Data held in an ERP system consists of one type, which often must be converted into a different type in order to be transmitted into another system. Different regulators require the same information in their specific formats or data types. Surprisingly, some individual regulators call for the same information in different forms and in different data formats. The assembling, dismantling, and repackaging of data in the required format can cause compliance issues and unintentional information errors when filing. Adoption of common codified standards for machine-readable data creation and exchange across all stakeholders within the compliance ecosystem could result in a giant leap toward coherence in the data flow.

Standards and supporting documents

254 Regulators adopt unique standards, data definitions, and business validation rules for similar non-financial data elements and metrics. A lack of cohesion in standards across regulators results in higher entity and regulatory costs in terms of time and resources. It also weakens auditability of information disseminated to a multitude of regulators and increases risks due to increased subjectivity, differences in interpretations, misinformation, and inadvertent partial compliance or non-compliance.

Technical standards

255 Different regulators have different access controls, validation rules, and data format specifications. These differences increase the complexity within a compliance ecosystem.

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97 OECD Regulatory Compliance Cost Assessment Guidance, OECD (2014)

98 A digital transformation brief: business reporting in the fourth industrial revolution, IMA (2020)

Submission modes

256 The modes of regulatory information submission differ for different forms and types of information. This creates additional hurdles both in creating standardised last-mile reporting validation rules and in creating seamless integration across internal and external systems.

Data definitions

257 Data definition fragmentation is more prevalent when reporting the same information to multiple regulators. The fragmentation occurs from the lack of clarity in communication and the lack of a single set of standards and definitions across multiple regulators. It is not uncommon to find differences in interpretation of the definition of various data elements among regulators. This naturally lends itself to an increased risk of misstatement and miscommunication and a corresponding increase in regulated entities' compliance costs for having to maintain multiple variants of the same data items (from entities having to validate each time they submit to the various regulators).

SECTION 4: WHAT IS THE SPECIFIC SITUATION OF SMEs RELATED TO NON-FINANCIAL REPORTING?

258 According to the European Investment Bank Group[99], SMEs represent 99.8% of all businesses in the EU.

259 SMEs are defined in the EU recommendation 2003/361[100]. The main factors determining whether an enterprise is an SME are staff headcount and either turnover or balance sheet total:

Table 11: SME definition in EU recommendation 2003/361

COMPANY CATEGORY	STAFF HEADCOUNT	TURNOVER	BALANCE SHEET TOTAL
Medium	< 250	≤ EUR 50 million	≤ EUR 43 million
Small	< 50	≤ EUR 10 million	≤ EUR 10 million
Micro	< 10	≤ EUR 2 million	≤ EUR 2 million

Source: EU recommendation 2003/361

260 These ceilings apply to the figures for individual enterprises only. An enterprise that is part of a larger group may need to also take into account staff headcount, turnover and balance sheet data relating to that group.

261 The assessment of non-financial reporting by SMEs needs to take into consideration that the world of SMEs' non-financial reporting is under-researched (which companies report, what they report, and what the information needs of the stakeholders are). The reasons for this lack of research are diverse: First, there is a lack of interest for and knowledge of the SME world amongst academics and researchers. Second, in particular regarding non-financial reporting, SMEs usually disclose on a voluntary basis or in an informal way, which leads to a lack of consistent data for possible research in this respect.

99 Small and medium enterprises Overview 2020, European Investment Bank Group (2020)

100 https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32003H0361

Regulatory/ voluntary context

QUESTION 4.1:
On what basis do SMEs report? Do they report to meet regulatory requirements, other mandatory obligations or on a voluntary basis? What are the relevant rules?

QUESTION 4.2:
How many SMEs report to meet regulatory requirements or other mandatory obligations on a voluntary basis?

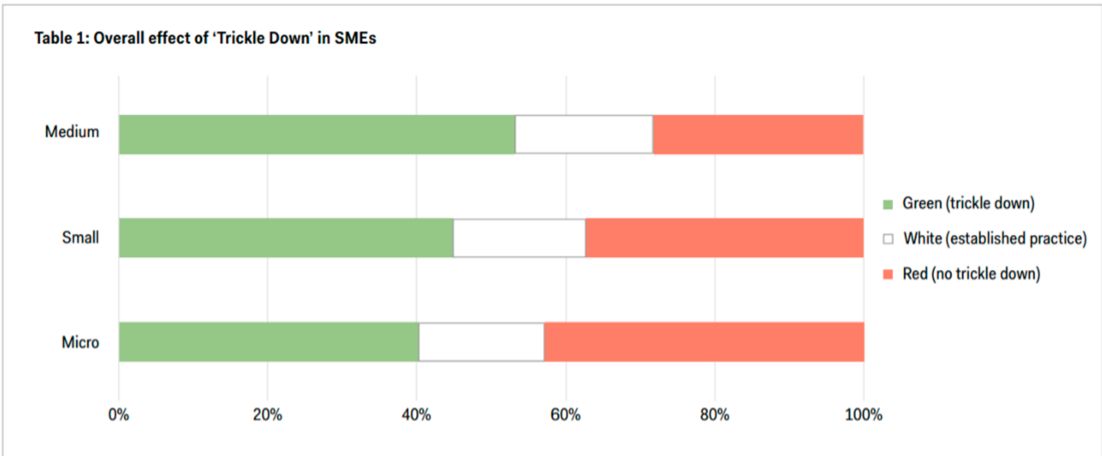
262 The number of SMEs that disclose non-financial information due to the trickle-down effect or on a voluntary basis is not known, nor is what they disclose and how they disclose it.

263 In a March 2017 report, the European Federation of Accountants and Auditors for SMEs (EFAA) analysed the trickle-down effect in financial reporting[101]. This survey covered Germany, the Netherlands, Portugal, Spain and the UK. Preparers were asked to identify and provide details of the application (or not) to SMEs of what were judged the main (not all) accounting treatments in full IFRS.

264 The EFAA report concludes 'that the impact of 'trickle down' is significant in all five countries. In all cases, convergence (...) of SME accounting with IFRS is at least 57% and the countries fall into a relatively narrow range of between 57% for Germany and the Netherlands, and 72% for the UK. All show clear signs that 'trickle down' has been a major factor in producing that convergence (ranging from 33% in the Netherlands to 59% in Portugal). It should be noted that distinguishing whether a current treatment derived from IFRS or from pre-existing practice can be a difficult matter to judge, in some cases. Difference in country ranges arise from specific actions taken by individual countries.

265 It is also observed that the extent of 'trickle down' is clearly greater for larger SMEs.

Figure 43: Extent of financial reporting standards trickle-down for SMEs



Source: The Trickle Down Effect – IFRS and accounting by SMEs, EFAA (2017) – page 5

266 The EFAA report further concludes 'Having concluded that the largest SMEs were most likely to have 'trickle down', a more detailed analysis of the medium-sized entities was carried out to ascertain what other conclusions might be drawn. The following factors were noted:

a) More 'trickle down' is likely in areas where the Accounting Directive is silent, because national GAAP will tend to use IFRS where that is so (...)

101 The Trickle Down Effect – IFRS and accounting by SMEs, EFAA (2017)

b) Less ‘trickle down’ will be seen in more complex matters, such as financial instruments and complex group structures.

c) Mixed impact is noted because some countries, for example Germany, have avoided implementing fair value principles in most instances.

d) In summary there is significant evidence of ‘trickle down’ and this increases with the size of the entity.’

267 Based on the EFAA report on financial reporting, it is fair to assume that non-financial reporting obligations towards large entities will also lead to a trickle-down effect for non-financial aspects. Such trickle-down effect is already visible today via the process of large entities asking their suppliers to provide non-financial information and to get such information validated by rating agencies (e.g. Ecovadis). However, this trickle-down effect would certainly be a less coordinated one compared to proper regulatory requirements for non-financial reporting towards SMEs.

Location

QUESTION 4.3:
Where is non-financial information found in SMEs’ publications?

268 Although there is no legal obligation deriving from the NFRD for SMEs to disclose non-financial information, many of them are under increasing pressure from their parent companies to provide certain non-financial information in order to meet group reporting obligations. Key stakeholders such as corporate clients that are introducing sustainability and transparency requirements in their supply chain, are also exercising pressure in this field (see also section above about the trickle-down effect). Those SMEs that cannot meet such requests due to insufficient human and financial resources, are penalised in terms of market access. Furthermore, with the increase in requests for non-financial information from investors or other finance providers, linked to new regulatory obligations, these SMEs could be denied access to finance.

269 Information reported by SMEs is often scattered across various documents, some of which are not accessible to the public. SMEs do not use the reporting tools used and developed for big corporations. SMEs work in a more informal way, while the existing non-financial information tools rather follow formal practices which require investment in time, resources and energy that SMEs cannot afford.

Classification

QUESTION 4.4:
What are the topics the most reported upon and by what types of entities?

270 No information was traced as readily available to indicate the non-financial information topics most reported upon by SMEs.

271 The question arises whether additional disclosure of non-financial information adds value for the stakeholders of every SME. In addition, depending on the type of SME one could argue that the value of additional information does not necessarily outweigh the costs. Examples are family-owned companies with closely involved shareholders. Those shareholders are aware of the purpose of the company and do not have to rely on non-financial information reporting to gain insights due to family involvement.

272 The size of an SME influences the reporting possibilities and capacities of that SME in terms of time, cost and from a technical perspective. Subsequently, the size and transparency of the suppliers of the SME influences the possibilities to obtain and provide information by the SME on specific topics.

SALIENT ASSESSMENT POINTS

273 The most significant and salient observations and assessment points of Stream A6 are identified and described below, including articulation of their relevance and importance in the perspective of possible non-financial standard setting.

274 The large and increasing number of reporting requirements and frameworks, together with their heterogeneity (in scope, objective, implementation – voluntary or mandatory, technology, etc), are a source of numerous inconsistencies in reporting practices, ultimately failing to address users' needs while being a burden for preparers of non-financial information, whose specificities and capacities (from large companies to SMEs) are not sufficiently considered.

275 Despite their increasing number, reporting provisions pursuing different objectives for different users fail to provide consistent guidance about what information to report (scope, breadth, depth), how and where. In this context of high complexity, companies are unsure whether they provide non-financial information that would be considered of good quality by users while at the same time being relevant to their main impacts, risks or policies. Users, on the other hand, struggle to locate and sometimes make sense of the reported data. This situation is further complicated by the lack of uniform requirements for monitoring of compliance and independent verification of the data.

276 Mirroring the fast-growing number and diversity of reporting provisions, non-financial disclosures have significantly increased in a somewhat unfocused manner. An increasing amount of non-financial data is disclosed in a variety of different places outside of the annual report or sustainability report via external links and complementary online content (investor briefs, press releases, newsletters, websites, etc). This makes it difficult for users to find decision-useful information and introduces uncertainty about whether the provided information is different between the different formats. The diversity of disclosure formats also makes it difficult for users to assess the relevance, comparability and reliability of the disclosed information.

277 The focus and momentum on environmental related matters both at policy level and in reporting frameworks is reflected in the efforts and focus put on reporting about climate or other environmental issues. In comparison, information given about other topics of interest to users seem to be less developed and elaborate.

278 Different reporting provisions put different emphasis on reporting of actual data compared to providing information on progress over time, on outcomes and impact, and/or on providing a forward-looking perspective. Existing provisions appear to rather focus on documentation and reporting per se, instead of driving real action. Consequently, reporting entities' efforts tend to be directed at describing policies rather than focusing on the impacts of such policies and highlighting the link between risks, policies and impacts. Although reporting increasingly includes references to the Paris Agreement or global policy priorities the extent of reporting specific targets to measure progress is limited (e.g. failure to report on targets on climate change, and measurement of actions to manage human right risks). This may be explained by challenges in the quantification of some of the topics (especially social issues), the lack of standardised metrics and the lack of maturity in the systems and processes which support the generation of this information.

279 Non-financial reporting provisions currently tend to focus on large and listed companies, meaning that some users' needs are not met. In this regard, the situation of SMEs that are part of the supply and value chain of companies subject to mandatory non-financial reporting is a challenging one. Existing reporting requirements have not been tailored to consider their limited resources and capacities, making their contribution to the overall non-financial reporting objectives a source of problems both for them and for the multitude of stakeholders that wish to use their data and information. Specific consideration on how to include SMEs in the non-financial reporting landscape at a reasonable cost and effort for them appears to be missing.

280 Beyond SMEs, preparers of all sizes are pointing at the difficulty of finding the right balance between satisfying the needs of a broad universe of users (having very different perspectives, expectations and therefore needs) and their own reporting needs, while keeping reporting costs at a reasonable level. In addition, while asking for clarification about

a non-financial reporting target structure, all preparers are also expressing the need for a proportionate approach to a staged implementation based on a proper cost/benefit analysis.

281 From a digitisation perspective, the non-financial reporting ecosystem is diversified in many ways, inflating costs, creating operational and compliance risks, and ultimately hampering access:

a) Regulators apply their own standards, data definitions (if any) and validation rules for similar non-financial data elements and metrics. In the EU currently there is no digital taxonomy of non-financial data allowing for efficient and consistent access to such non-financial data (except for Spain, although even the Spanish taxonomy is used little in practice).

b) The lack of cohesion in standards and (digital) taxonomy, results in higher entity and regulatory costs in terms of time and resources. It also weakens the auditability of information and increases risks due to increased subjectivity, differences in interpretations, misinformation, and inadvertent partial compliance or non-compliance. Also, the assembling, dismantling, and repackaging of data in the required format can cause compliance issues and unintentional information errors when filing.

c) Same inconsistencies and insufficiencies apply to access controls, validation rules and data format specifications. These differences and gaps increase the complexity and challenge the usefulness of a compliance ecosystem.

d) The flows and interfaces between input, throughput and output across various systems are not aligned and often require manual intervention to ensure that the output of one system is reprocessed in the necessary format to be validated for submission to the next system.

e) Modes of information submission differ for different forms and types of information.

APPENDIX: SOURCES USED FOR DESKTOP LITERATURE REVIEW

1 This appendix lists out the sources used for the desktop literature review carried out by Stream A6. These sources were identified by Stream A6 members to contain information potentially relevant for the scope of the assessment of Stream A6.

DOCUMENT TITLE	SOURCE	YEAR
2019 Research Report – An analysis of the sustainability reports of 1 000 companies pursuant to the EU Non-Financial Reporting Directive	Alliance for Corporate Transparency	2019
Insights into integrated reporting 4.0 – The story so far	ACCA	2020
Mapping the sustainability reporting landscape – Lost in the right direction	ACCA	2016
Towards reliable non-financial information across Europe	Accountancy Europe	2020
Follow-up paper: Interconnected Standard setting for corporate reporting	Accountancy Europe	2020
European Single Economic Format (ESEF)	Accountancy Europe	2020
Member State Implementation of Directive 2014/95/EU – A comprehensive overview of how Member States are implementing the EU Directive on Non-financial and Diversity Information & Spain update, Accountancy Europe (2017 & 2019)	Accountancy Europe	2017 & 2019
The ESG ecosystem: Understanding the dynamics of the sustainability ratings & rankings landscape	BrownFlynn	2018
Falling short? Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve	CDSB	2020
EU Environmental Reporting Handbook: What does environmental reporting look like in line with the EU Non-Financial Reporting Directive?	CDSB	2020
An evaluation of the current state and future of XBRL and interactive data for investors and analysts	Columbia Business School	2012
The international business registers report	EBRA	2019
Survey of non-financial reporting requirements for SMEs in Europe	EFAA	2018
The trickle-down effect – IFRS and accounting by SMEs	EFAA	2017
Enforcement and regulatory activities of European enforcers in 2019	ESMA	2020
Summary Report of the Public Consultation on the Review of the Non-Financial Reporting Directive, 20 February 2020 – 11 June 2020	European Commission	2020
Regulation (EU) 2020/852 (Taxonomy) on the establishment of a framework to facilitate sustainable investment	European Commission	2020
An SME strategy for a sustainable and digital Europe	European Commission	2020

DOCUMENT TITLE	SOURCE	YEAR
Financial data standardisation – RegTech Project	European Commission	2018
Regulatory fitness and performance programme – Refit scoreboard summary	European Commission	2017
Internal Market and Services DG NON-PAPER FOR DISCUSSION IN THE INFORMAL AD-HOC SME REFLECTION GROUP ON 15 DECEMBER 2008 – IFRS for Private Entities and the European Accounting Framework – Some considerations – 11 December 2008	European Commission	2008
Relevance and reliability of non-financial information	European Contact Group	2020
How to improve climate-related reporting, A summary of good practices from Europe and beyond	European Corporate Reporting Lab @EFRAG	2020
Does your non-financial reporting tell your value creation story?	EY	2018
Why corporate reporting standards are starting to converge	EY	2019
La Dichiarazione Non Finanziaria: la risposta delle aziende europee ed italiane	EY	2018
Non-financial reporting: What differences across European countries?	EY	2019
Why it's time to take a standard approach to non-financial reporting	EY	2019
How will ESG performance shape your future?	EY	2020
Comparing the implementation of the EU Non-Financial Reporting Directive in the UK, Germany, France and Italy	Frank Bold	2017
Trends in non-financial reporting	Global Public Policy Institute	2006
The 2020 Sustainability Leaders	Globescan	2020
A new vision of Europe's capital markets	High Level Forum on the Capital Markets Union	
Copy data management	IDC	2018
A digital transformation brief: Business reporting in the fourth industrial revolution	IMA	2020
XBRL in Europe	IMP	
Non-financial digital transformation Working Group	IMP	2020
Carrots & Sticks, Sustainability reporting policy: Global trends in disclosure as the ESG agenda goes mainstream	KPMG	2020

DOCUMENT TITLE	SOURCE	YEAR
Alignment of accounting for SMEs and handicraft enterprises – Criteria, scope and limits for their regulation in the Eu-ropean context	Ludwig-Fröhler-Institut	2009
More than values: The value-based sustainability reporting that investors want	McKinsey	2019
The role of data in sustainable investment, policy and regulation	OMFIF-Refinitiv	
Driving meaningful data: Financial materiality, sustainability performance and sustainability outcomes	PRI	2020
Standard business reporting: Open Data to cut compliance costs	PwC	2017
Statement of intent to work together towards comprehensive corporate reporting	SASB, IR, GRI, CDSB, CDP	2020
Non-financial reporting in italian SMEs: An exploratory study on strategic and cultural motivations, International Journal of Business Administration, Vol. 5, No. 3	Academic research – Donato Calace	2014
Non-financial reporting: Theoretical and empirical evidence	Academic research – Nidžara Osmanagić Bedenik, Petra Barišić	2019
What is corporate sustainability and how do firms practice it? A management accounting research perspective	Academic research – Satish Joshi, Yue Li	2016

2 Some supplementary documents and/or updates taken into consideration for the drafting of the report are referenced directly in the relevant report paragraphs.

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