Perspectives on ESG Reporting

Oceania – The future of ESG reporting explored

On Tuesday 30th November, the GPPC[1] brought together 18 professionals representing various stakeholder groups in the corporate reporting ecosystem[2] to explore Environmental, Social and Governance (ESG) corporate reporting and assurance of the future. Individuals from the Oceania region (mainland Australia and South Pacific island groups) were invited based on their knowledge and expertise on ESG reporting and assurance matters. The roundtable was conducted virtually.

The Oceania roundtable was one of a series of regional discussions, held under the Chatham House Rule[3], that explored the current ESG reporting landscape in terms of 1) Where we are now, 2) Where we want to go, and 3) How to get there. Grounded in the understanding that there may be a disconnect between what current accounting and auditing reporting practices require and permit, and what some investors and stakeholders are expecting and demanding, the discussion was designed to explore potential approaches to better align corporate reporting and auditing standards with stakeholder and societal objectives.

The report below draws out key points that were made by the participants at the roundtable discussion. The roundtable participants' remarks are quoted (in italics) throughout the report. In accordance with the Chatham House rule, attribution of quotes is by category of participant rather than name and organisation. It is designed to help understand the perspective from which comments were made, rather than to suggest that any position is typical or otherwise of a particular stakeholder group. For a full list of participant categories, please see Appendix A.

1. **Where we are:** exploring current gaps between what is desired and what is delivered, with a focus on climate

1.1. Participants expressed that more needs to be done to understand and disclose climate related risks.

Roundtable participants noted that while reporting standards are improving, many disclosures today exist outside of financial reports. Participants expressed that current financial reporting, accounting,

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[1] The Global Public Policy Committee (GPPC) is the global forum of representatives from the six largest accounting networks: BDO, Deloitte, EY, Grant Thornton, KPMG, and PwC, which has as its public interest objective the enhancement of quality in auditing and financial reporting.

[2] Participants represented stakeholder groups including investors and asset managers, investor associations, corporate preparers and ESG leaders, business organizations, those charged with governance (TCWG) including audit committees and corporate boards, auditors/assurers, and professional bodies.

[3] When a meeting, or part thereof, is held under the Chatham House Rule, participants are free to use the information received, but neither the identity nor the affiliation of the speaker(s), nor that of any other participant, may be revealed.

and auditing requirements are outdated and need to evolve and that the reporting landscape is siloed and lacks an integrated structure.

> *"Greenwashing is very easy to identify, and it was one of the issues that has come out of COP 26. So, it's not just a case of creating a glossy report, but those companies that really provided a cogent analysis of their exposures and management of non-financial risks and demonstrated quality of management."*
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> *"We cannot discuss climate-related risks without a better understanding of* how to assess *climate-related risks. There are gaps between investor expectations of reporting on climate risks and what companies deliver."*
>
> *TCGW*

Capital allocation appears to be an area of particular interest to investors, especially with regards to setting specific targets and allocating capital accordingly. When companies respond to requests for more robust information about a company's goals to reach net zero, investor participants reported that they often come up lacking.

> *"How are you actually allocating capital and determining whether that is a viable and realistic use of capital for investors? And it's hard because it's very forward and future looking. But we need a little more than what we currently see."*
>
> *Investor and Investor Associations*

One participant referred to a new indicator in the financial statements called "climate accounting" that their organization is using in the assessment of companies. Others commented that in the future, corporate reporting will require strong focus on how companies report their ever-growing inventories of intangible assets, including intellectual capital, social capital, environmental interests, and human capital.

> *"When we think of some of the largest companies today, their values aren't tied up in real estate or operating plants and – tying this back to integrated reporting – you look at that intangible component. So, what makes it up? Human capital, social capital, environmental capital, and intellectual capital. And current financial reporting processes just do not incorporate these issues and have left the gap for investors to seek this additional information."*
>
> *TCGW*

1.2. There are different opinions about what has caused the gap between the current and desired features of financial reports, as well as what it will take to close that gap.

Although the majority of participants favoured the move to disclosures of more climate-related information (especially with regard to risks) into the annual reports, most participants expressed the view that current reporting practices do not currently meet investor desires. Opinions varied about why this is the case.

Some felt that current IFRS standards are broadly adequate, and the issue rests in how the standards are applied. In particular, there was a view that climate is often a material financial risk and, therefore, should be factored into financial statements under current standards:

"We are dealing with perceptions, including a lack of evidence that companies are incorporating material climate-related matters in their financial statements, that climate-related assumptions are not visible in financial statements, and that companies don't have a consistent story in their ESG reporting."

Academics and policymakers

Others believed that reporting standards related to ESG can conflict with accounting standards because they require companies to predict values in hypothetical situations and, therefore, should be revised.

"There's a disconnect between what current accounting and auditing standards require and what a growing number of stakeholders are expecting."

Academics and policymakers

"In some cases, the accounting standards prohibit disclosure or doing an impairment test; in doing future capex activities because it's asking you to test the value of your assets in today's environment. So, transforming those assets or changing them to meet a net zero target might actually be contravening the accounting standards in certain cases […] There is a role for climate-specific reporting"

Assurers and professional bodies

"There's a regulator need here as well…. The financial reporting and accounting standards at the moment don't go anywhere near scenario analysis and data requirements that's being called for and demanded in sustainability."

TCGW

1.3 It's important to remember that all corporate reporting ecosystem stakeholders have important roles and responsibilities

Roundtable participants discussed how the impact of the individual and integrated responsibilities of stakeholders, including regulators, standard-setters, auditors, and investors cannot be underestimated when it comes to shrinking the gap between current and desired corporate reporting practices. The opportunity to offer clarity and insight about required metrics, benchmarks, and expectations is tremendous – for organizations and society!

"ESG related data that is out there is quite extensive like the number of standard setters and is thankfully now moving closer together while for some aspects like reliable or accurate data it is

hard to obtain and what we can also see is that in addition ranking and rating agencies are often not consistent in their focus area."

Academics and policymakers

2. **Where we should go:** The evolving role of ESG in corporate reporting

2.1. Which ESG-related disclosures have the greatest impact?

Participants expressed that companies that have strong understanding of their material risks and opportunities demonstrate their understandings and commitments to transparency as part of embracing high-quality governance principles and practices. While companies must report on matters that are material to them, stakeholder engagement helps inform decisions about what constitutes materiality *to them*. In the view of many participants, one of the benefits of leveraging frameworks like the one published by the Task Force on Climate-Related Financial Disclosures (TCFD) is that companies work through the risks and relevant scenarios, and subsequently report against the tenets of those frameworks.

"Just saying that you [are putting] systems in place, [and] 'we expect to be able to disclose targets in 2 years' time- or provide a timeline' … [This] gives investors the confidence that the work is being done. … [It is] quite reasonable not to disclose a target unless you've got the systems in place. But getting the narrative out to investors [is] important so they've got the confidence that the process is underway."

TCGW

"It's really important for companies to define what is material to them, and it will differ for [each] company, but what I think is really key to that is that they reach out to the appropriate stakeholders. … We have seen materiality maps that are sometimes questionable in terms of the issues that a company identifies as material. For example, if a company in a high emission industry does not identify climate change as material risk, that is a significant red flag. I think [companies] need to reach out to the broader market that includes investors, but potentially also consumers, … to have broader stakeholder assessments."

"I would say we have seen a lot of our clients actually use their TCFD reporting as the basis for their testing in the financial statements."

Investors and investor associations

"One pleasing trend that we are seeing over time is that actual size of sustainability reports is shrinking, but the detail and the numbers attached to key metrics is increasing."

Assurers and professional bodies

2.2 Is ESG information ready for assurance?

Participants communicated that there should be assurance on ESG-related data:

"The credibility that's provided by assurance is really important."

Investors and investor associations

However, most believed that the data is not yet mature enough for assurance in most organizations. The Roundtable discussed the need for companies to put appropriate controls and governance practices in place first in order to prepare information that is relevant and reliable in response to investor requests.

"Where do you draw this line, what are you compared to, where are the targets companies are committed to? It is very difficult..."

Assurers and professional bodies

"We want to encourage people to have a go around at these things [quality data, controls] … where you're trying to set up the control and systems that may not be quite mature enough to be able to be open to an audit."

Assurers and professional bodies

3. Achieving the desired future state of ESG-related reporting has challenges, but the outcomes are worth the effort.

Given the pros and cons, participants communicated that the benefits of expanded reporting outweigh the challenges in embarking on a journey to evolve for the future. Market participants, regulators and standard setters all have valuable insights, opinions, and expertise in crafting ESG reporting for the future.

3.1 What are some major obstacles to using and reporting on ESG information?

Participants asserted that companies struggle to collect consistent data or encounter situations where they receive multiple sources of data which lack comparability and usefulness. Different approaches used by different companies create inconsistencies in the market.

Others said that they continue to see information collected on rudimentary spreadsheets that are prone to errors and overall status of the systems in the ESG space is lacking maturity.

"Companies do need some more time to do their climate assessments. This is very difficult work. There's a lot of uncertainties, a lot of assumptions that need to be made, and there needs to be a strong process before companies can be making announcements to the market during these types of matters."

Assurers and professional bodies

"Companies are sometimes in a difficult position on working out exactly how and what to report … but financial reporting has evolved over the last 500 years and ESG reporting hasn't been going for more than about a decade."

Companies and business organizations

"For example, if a large company is setting a target, their base year may be 2008, another may say 2019. Some might include divestment of assets as a totally credible way to meet their target, others won't. They might set absolute targets; others might set density targets. They might include different scopes; some might include equity emissions. I've just used the targets as an example … The lack of consistent approach is really a problem because it makes it hard to know what you're looking at, but also impossible to compare."

Investors and investor associations

3.2 What could help companies meet sustainability goals that address investors' needs?

Some participants thought that government policies, including clarification on the definition of consistent data, offer a path for enhanced company reporting and that government adoption of ISSB standards globally would lead to greater comparability as well.

"Consistency is the key. You never like to see certain countries reporting a certain way. We've become such a global environment … I would dare to think that we would have different systems, we need to try and prevent as much as possible separate systems coming around – even if it isn't initially so. I think governments need to show leadership in this area."

Assurers and professional bodies

Many participants felt the ISSB framework is largely cause for optimism, especially if it serves as a baseline that allows for supplemental reporting based on local markets and industry needs. Some believed that the ISSB framework would address the current challenges and clarify reporting requirements that meet investor and societal expectations and improve consistency of reporting.

"Having reporting standards for matters of local importance is really important but one thing that we've discovered looking at climate benchmarking is there's also probably a need for sector standards… not necessarily saying that we go down the path of kind of developing up sector standards right now, but that's kind of the logical long-term trajectory that there will be kind of a common set of standards, but also specific sector standards developed as things evolve."

Investors and investor associations

"Mandating some requirements by different countries together with their accounting standards is really important … I view it as not necessarily coming through financial reporting but being a separate arm in itself."

Academics and policymakers

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Appendix A: Participant Categories

Participant Category	Description
Companies and business organizations	Publicly-traded companies or organisations that represent them
Investors and investor associations	Investment funds or associations representing investors
Academics and policymakers	Professors of accounting or civil servants with a role in corporate governance
Assurers and professional bodies	Auditors at GPPC member firms or leaders at professional bodies

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Appendix B : Quantified responses

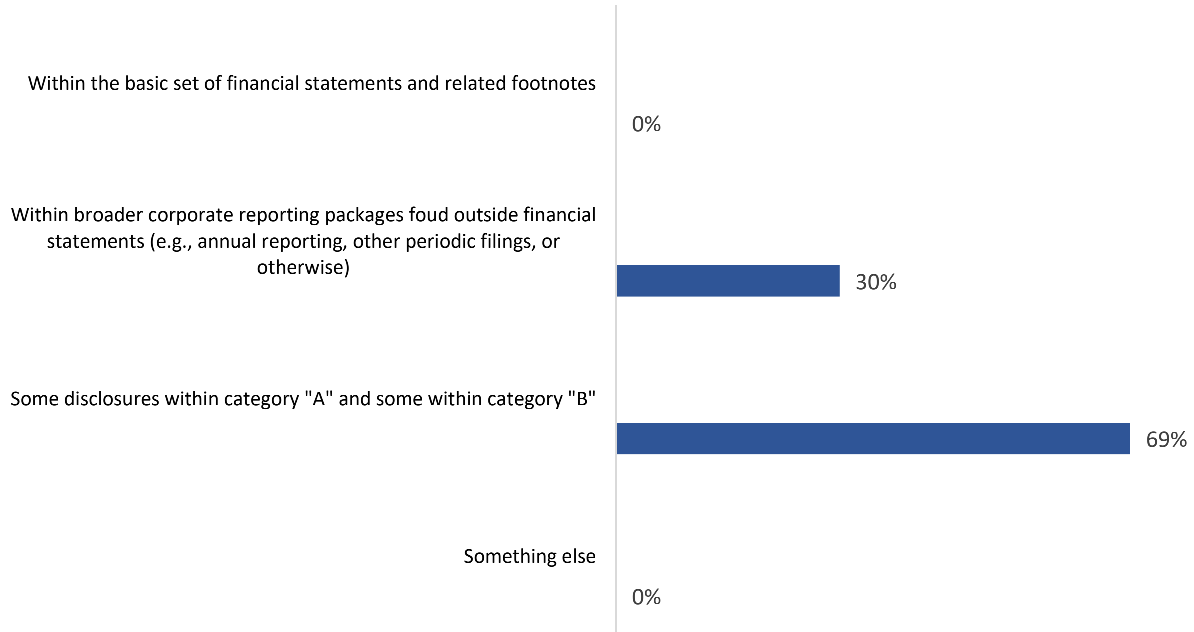
During the discussion, a number of probing questions were asked to catalyse debate. The results are below. These reflect the views of participants at the start of each discussion section. They are not purported to be representative of wider stakeholder opinion, nor opinion once informed by the discussion. They are included here for completeness. Participants did not have to answer every question; and in most cases could select more than one option.

Question 1:

What do you believe is driving the gap between what investors and others expect companies to present in their financial statements regarding climate risks and the information that is currently being presented? Select all that apply.

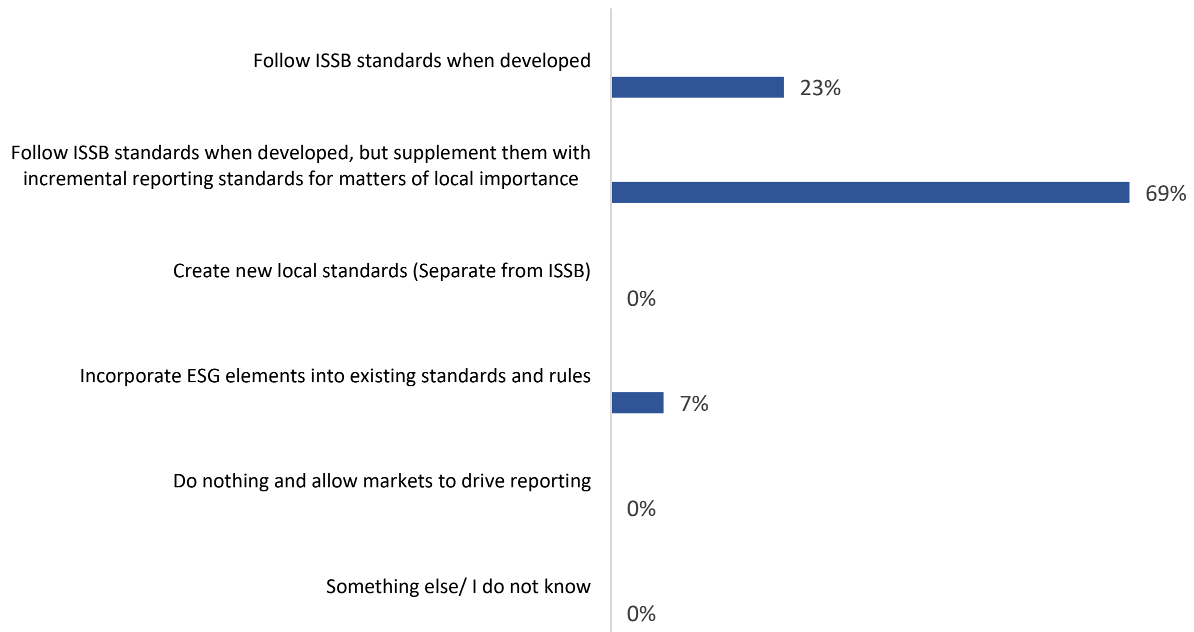
Question 2:

Where do you think companies should report ESG disclosures?



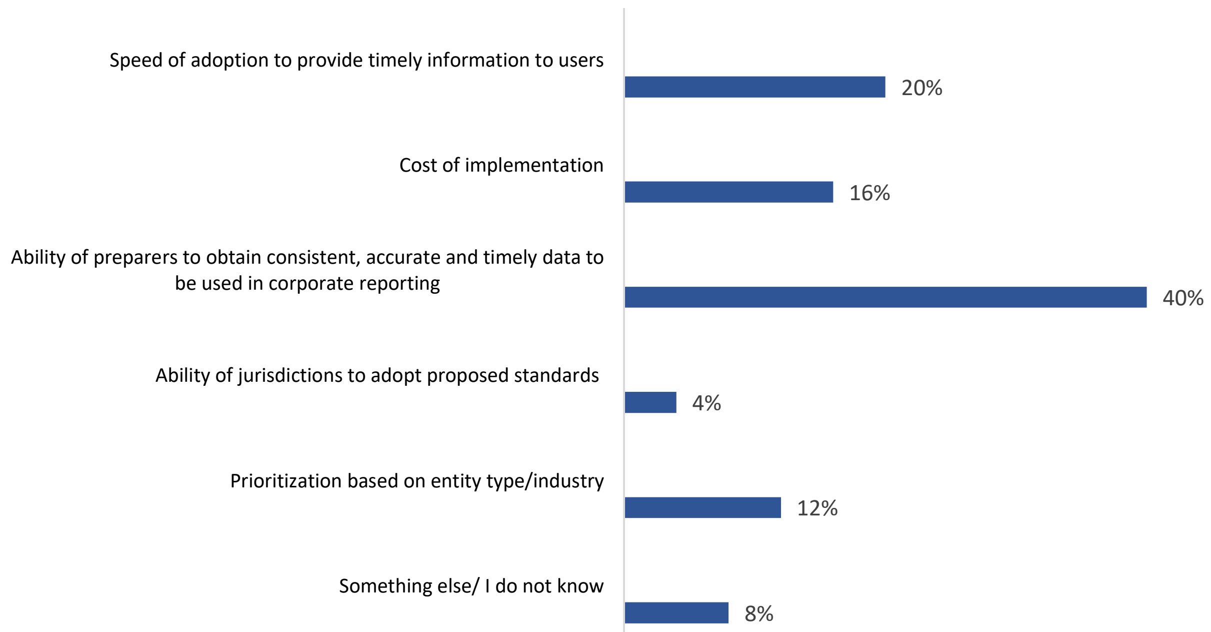
Question 3:

Which approach do you believe should be adopted for corporate reporting around ESG matters?



Question 4:

What factors do you believe standard setters and regulators should consider when developing reporting requirements specific to ESGs? Select all that apply.



Question 5:

What do you consider the major obstacles to the reporting and use of ESG information? Select all that apply.

Question 6:

Other than changing ESG corporate reporting standards, what actions do you believe should be taken to help companies meet their sustainability goals and address investors' needs?