REPORTING OF NON-FINANCIAL RISKS AND OPPORTUNITIES AND LINKAGE TO THE BUSINESS MODEL

SUMMARY REPORT

25 MAY 2021

European Reporting Lab @EFRAG

EFRAG European Financial Reporting Advisory Group

This report has been prepared for the convenience of European constituents by the EFRAG Secretariat and has not been subject to review or discussion by neither the EFRAG European Lab Steering Group nor the PTF-RNFRO by. It has been reviewed by the speakers at the event.

Background

The EFRAG Lab Project Task Force on Reporting of non-financial risks and opportunities and linkage to the business model (PTF-RNFRO) held a webinar on 25 May 2021. This report has been prepared for the convenience of the European Lab constituents to summarise the event. The programme can be found here and all of the speakers' biographies can be found here. The recording of the event can be consulted here.

The introduction and setting the scene of key findings and examples of good practices were presented by co-chairs of the PTF-RNFRO, **Mario Abela** and **Dawn Slevin** (see presented slides). They presented key findings on the reporting of the business model and sustainability risks and opportunities. They highlighted principles of good reporting with illustrative examples from six companies. They also presented findings on the uses of technology in reporting and highlighted a path to improvement.

The Panel members were the following:

- **Giulia Genuardi –** Enel, EFRAG European Lab PTF-NFRS and PTF CRR member
- **Filip Gregor –** Frank Bold, European Lab Steering Group member
- **Ron Gruijters –** Eumedion, EFRAG European Lab PTF-NFRS member
- **Nadia Humphreys** – Bloomberg, EC Platform Sustainable Finance member, co-Chair SG 5 Data and Usability
- **André Jakobs –** ABN/AMRO, EFRAG European Lab PTF- CRR member

Participants and panellists were welcomed by the EFRAG Board President and Chair European Lab Steering Group, **Jean-Paul Gauzès**. He stated that the discussion to be held in webinar would be relevant for the wider sustainability reporting work. He added that in preparing draft EU sustainability reporting standards, practice will be looked at and good practice can point the way forward and help other companies.

Panel discussion of key findings and examples of good practices

Common messages

The panellists congratulated the PTF-RNFRO on the work done and, in general, concurred with the findings of the PTF-RNFRO review. There was consensus on the inadequacy of current business model reporting practices and a need for improved transparency on how materiality assessments are conducted by preparers. It was observed that disclosures, if provided at all, were often boilerplate giving limited information for investors and other stakeholders. It was acknowledged that some clarity and standardisation was needed regarding reporting on risks and opportunities and linkage to the business model. The importance of connectivity between financial and non-financial information in conveying the enterprise value creation was underscored. There was a need for a strong reporting framework and standards to ensure comparability. Panellists were supportive of EFRAG undertaking work on EU sustainability reporting standards building on or at least compatible with a global standard. Furthermore, the importance of assurance was emphasised giving an indication of the quality of the information provided.

The following were specific comments made by the panellists.

Topic 1: Business model reporting

Filip Gregor, speaking from the perspective of reviewing large samples (1000+) of European companies, noted that it is very difficult to come up with objective criteria for how business model and strategic reporting should look like. Based on the findings of the Alliance for Corporate Transparency, there is no coherent practice, and the disclosures focus more on compliance rather than focusing on the dynamic perspective of the business model. Most of the examples provided only general information. Further information on the examples is needed with respect to a clear description of material issues and explanation why they were selected. In addition, information on strategic objectives that are relevant for the business model development would be helpful.

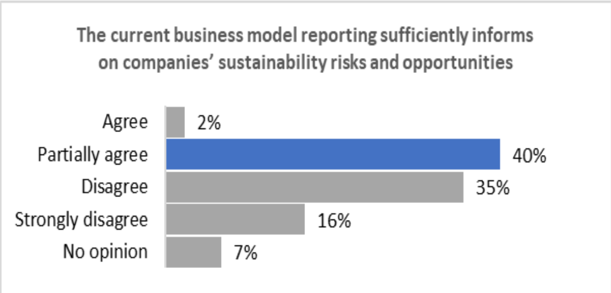
Giulia Genuardi, from a preparer perspective, explained that a company needs to start with linking the value chain to the business model in order to identify the relevant risks and opportunities. She added that both qualitative and quantitative information, if used appropriately, have the same importance in reporting. Also, companies should report both positive and negative aspects. Companies do not need to reinvent the wheel if there are good practice examples. However, some good practice guidance is needed in order to be coherent and comparable.

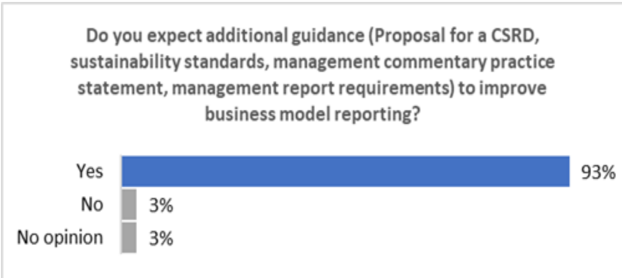
Ron Gruijters, from an investor perspective, highlighted that there is an unbalanced presentation of how sustainability considerations affect the business. There is more attention on aspects that went well and less attention on how the remaining key issues are expected to affect the company and how they will be addressed. However, he pointed out that there is an increased focus on reporting of value creation and the impact of sustainability frameworks on the reporting. There is more room for further development of reporting practices in order to promote a balanced and faithful representation of the business model. In addition, he underlined the importance of assurance of key information.

Nadia Humphreys, from a data aggregator perspective, observed that currently data is incomplete, inconsistent and varies across company jurisdictions, company sizes and sectors. Furthermore, there is a weak link between the financial statements and sustainability reports, including weakness in the time of delivery. Often, sustainability reports act as a public relations tool for their company and there is more of a narrative metric-based depiction rather than quantitative data. However, she agreed with Ron Gruijters on the willingness of companies to provide additional information. She supported data being reported and stored in an accessible format. She agreed with Ron Gruijters on the need for assurance.

André Jakobs, from a preparer perspective, pointed out that as there are many sustainability reporting frameworks, there are many visualisations of business model reporting. It would seem like companies provide unstructured data rather than insightful key performance indicators. Furthermore, information would depend on whether a company has a long-term or a short-term/medium-term perspective. Therefore, comparability of information was difficult.

Mario Abela summarised the takeaways noting that from the preparer perspective, there is a lack of clear reporting requirements, and the investors are trying to make sense of the information. He added that not one size fits all but there was a need for some standardisation and basic aspects such as the same formats to enable investors to compare the information. In addition, companies providing only narrative disclosures without quantifications is difficult for investors. Assurance adds value to the quality of what the company reports. The main challenges were in terms of a mismatch between the period over which a company creates value and the time horizon over which sustainability risks are likely to manifest. In response to an audience question on the source of business model information, he confirmed that multiple sources (sustainability reports, management reports, integrated reports) were relied on by the PTF-RNFRO. In response to a different question, he also noted the limitations of academic frameworks as a reference point.





Topic 2: Reporting on sustainability-related risks and opportunities

Giulia Genuardi commented that before reporting and defining the strategic plan and sustainability plan, which are interconnected, a company should analyse its Environmental Social and Governance (ESG) content, risks and opportunities and materiality. A company should also involve all the relevant stakeholders. She indicated that there is a need to identify current, medium-term, and long-term risks and opportunities. Furthermore, there is a need to create a single reporting framework of risks. Finally, a glossary needs to be created.

Ron Gruijters highlighted that companies struggle to be more specific on how risks and opportunities affect and help shape their strategy and business. The disclosures do not go beyond what is already obvious. In addition, there is no systematic assessment on the material risks and opportunities relating to ESG themes including the nature of the impact and how the company manages the risks. In addition, examples of forward-looking reporting are limited. Furthermore, there is no clear way to determine materiality.

André Jakobs pointed out that not every materiality matrix is the same in different reporting frameworks and standards and most of them do not relate to risks and opportunities relevant for a company. It is difficult to obtain good examples. Furthermore, the risk methodology is often based on IFRS reporting and broader aspects, including sustainability, need to fit into this methodology creating difficulty. Several audience questions revolved around the type of reporting framework that was appropriate. André Jakobs supported having one reporting framework in order to determine materiality for financial and non-financial reporting.

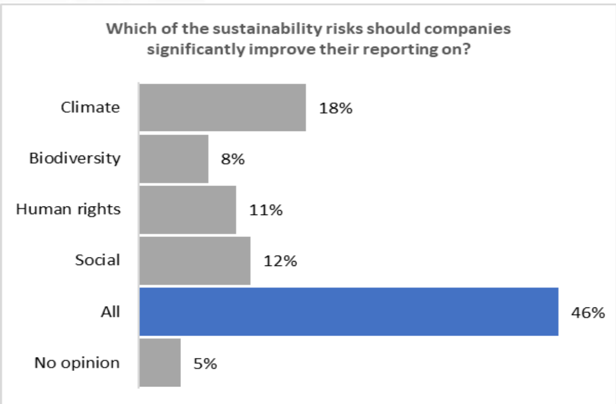
Nadia Humphreys commented that there is confusion on what good examples look like and companies need guidance or clear examples on this. There are many solutions and reporting frameworks and standards to solve the issue and there is a question on whether a company should exercise its discretion in the reporting or cater to what is required from regulation. Companies should not primarily cater for information that is investor relevant. They rather need to start with a simple map of what commonly accepted risks are within the sector and the impact on the business model for a wider range of stakeholders.

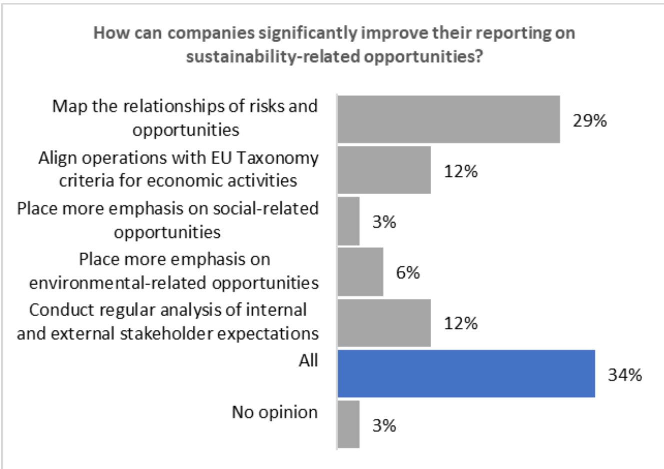
Filip Gregor mentioned that for double materiality[1] to be useful, the risks and opportunities need to be provided in the context of the business model and everything needs to be integrated. Financial materiality arises from impacts of the company (i.e., environmental and social impacts). What is important is the stakeholder perspective together with the impact on double materiality. There needs to be a process on how materiality should look like and what needs to be disclosed rather than only metrics. He also opined on an audience question on the feasibility of a standardised materiality matrix. Furthermore, good practice examples combine two things: clarity on the context and the company's value chain; and clear strategic objectives.

Dawn Slevin summarised the discussion stating that strategically companies need to stand back and look back at where they are going in the timeframes that are relevant for their business. The companies want to take a high-level view of risks and opportunities, but they need to more closely consider relevant aspects for their business model. This is because companies are faced with key environmental and social challenges, for example, climate, circular economy, human rights. Companies need to consider where do they need start to change their business-as-usual model and to redesign how they consider the risks and opportunities. Based on this, they can provide adequate reporting on the business model changes including the consideration of risks and opportunities. She indicated that all this would take time but where there is a will there is a way.

Closing of the event

Saskia Slomp concluded that the discussions were rich and fruitful and indicated that there was recognition by the panellists of the EFRAG PTF-RNFRO findings. She hoped that all present would be keen to see the PTF-RNFRO report that was expected to be published during the summer. She thanked the participants and panellists and closed the meeting.





[1] Double materiality requires that both impact materiality (inside-out) and financial materiality (outside-in) perspectives be applied in their own right without ignoring their interactions.