

**DRAFT INTERIM DELIVERABLE PAPER:
*CONNECTIVITY & BOUNDARIES OF ANNUAL
REPORT SECTIONS***

**PRESENTATION TO EFRAG SRB-
AGENDA PAPER 07-01**

04 JUNE 2024



Phase 1: Operationalises connectivity under current reporting requirements- *Discussion Paper expected in H2 2024, Interim Deliverable Paper to be published in Q2 2024*

CONCEPTUAL SCENE SETTING

PRACTICAL ILLUSTRATIONS

Real world and mock-up examples

Scope of SR: ESRS, IFRS Sustainability Disclosure Standards, other

Scope of FR: GAAP agnostic, starting with IFRS Accounting requirements

Possible Phase 2: Scope to be determined later

If phase 2 is undertaken, **will consider learnings from Phase 1**

Need to monitor other initiatives- IASB, ISSB, other National Standard Setter and regulator connectivity initiatives

RECAP- WHY AN INTERIM DELIVERABLE PAPER (IDP)?

- Ideas, format, and merits of an interim deliverable were discussed at the October 2023 FR-SR TEG joint meeting, October 2023 EFRAG CAP Meeting, and the February 2024 joint EFRAG TEGs and joint EFRAG FRB/SRB meetings

STRATEGIC CONTRIBUTION

- Connectivity is a topic of **strategic significance in the ongoing enhancement of the corporate reporting system** (EFRAG is a key actor in the process)

ENSURES EFRAG'S TIMELY AND ONGOING CONTRIBUTION TO THE EVOLVING THINKING ON CONNECTIVITY

- Conceptualisation on connectivity within EFRAG has been ongoing for several years (PTF-NFRS and other European Lab publications in 2021) and through discussions at the EFRAG CAP and EFRAG FR-SR TEG and EFRAG FRB-SRB meetings in 2023/4
- EFRAG connectivity research project was initiated in June 2022, the project's objectives, scope and approach were agreed in early 2023; and EFRAG CAP was constituted and became operational in Q3 2023. It is **time to show some outputs**
- Need to share and possibly engage with stakeholders on the thinking within EFRAG so far. It is a nascent and multidimensional topic with **varied understanding, cross-purpose communication and expectation gaps amongst stakeholders** and **IDP can help foster a shared understanding about connectivity and lessen the expectation gap**
- Evolving thinking on the topic- with multiple actors (IASB, ISSB, other NSS, regulators) and related publications sharing their perspectives. **EFRAG's perspectives should also get timely visibility.**

IDP DEVELOPMENT & ENHANCEMENT

- IDP developed after discussions with the EFRAG CAP and EFRAG CAP concepts subgroup (October 23-Jan 24), and discussions/feedback from EFRAG FR and SR TEG and EFRAG FRB and SRB on related papers during meetings in 2023 and February 2024
- In February 2024, two papers ‘Connectivity concepts’ and ‘Boundaries’ were presented to EFRAG CAP, EFRAG FR-SR TEGs and EFRAG FRB-SRB and suggestion made that these be published as interim deliverables
- In February 2024, EFRAG FRB&SRB recommended the merging of the two papers and for these to be published as an interim deliverable. This has been done and the IDP title is ‘**Connectivity considerations & Boundaries of different Annual Report sections**’
- **A caveat has been added** making clear that the **EFRAG research project IDP and forthcoming Discussion Paper that will also include examples are not part of EFRAG’s SR standard-setting activity and do not constitute ESRS implementation guidance**. It is clarified that the objective of the connectivity project is similar to that of other EFRAG proactive research projects (i.e., **primarily to stimulate debate related to ongoing corporate reporting enhancement**).
- **Enhanced readability and content of IDP** based on suggestions made across meetings.

IDP FINALISATION STEPS

- EFRAG FRB&SRB and joint TEGs recommendations made in February 2024 for the IDP were implemented
- Presentation to ESMA Climate working group in March 2024
- Presentation at April 2024 IFASS meeting (draft IDP shared as a meeting paper), draft IDP updated subsequently based on IFASS member discussions and comments gotten from some international standard setters
- Presentation to EFRAG CAP at end of April 2024, draft IDP subsequently updated
- Presentation to EFRAG SR TEG for final comments on 8 May 2024 and written comments gotten until 14 May 2024, draft IDP subsequently updated
- Presentation to EFRAG FR TEG and FRB and approval for publication gotten on 15 May 2024, draft IDP subsequently updated for comments received
- Presentation to EFRAG SRB for final comments on 4 June, draft IDP will be updated based on feedback
- Thereafter, IDP final text will be sent to publisher. Visual enhancements and any further editorial, proofing and format enhancement will also be addressed during final publication.

PUBLICATION OF THE IDP EXPECTED TO BE IN MID-JUNE 2024



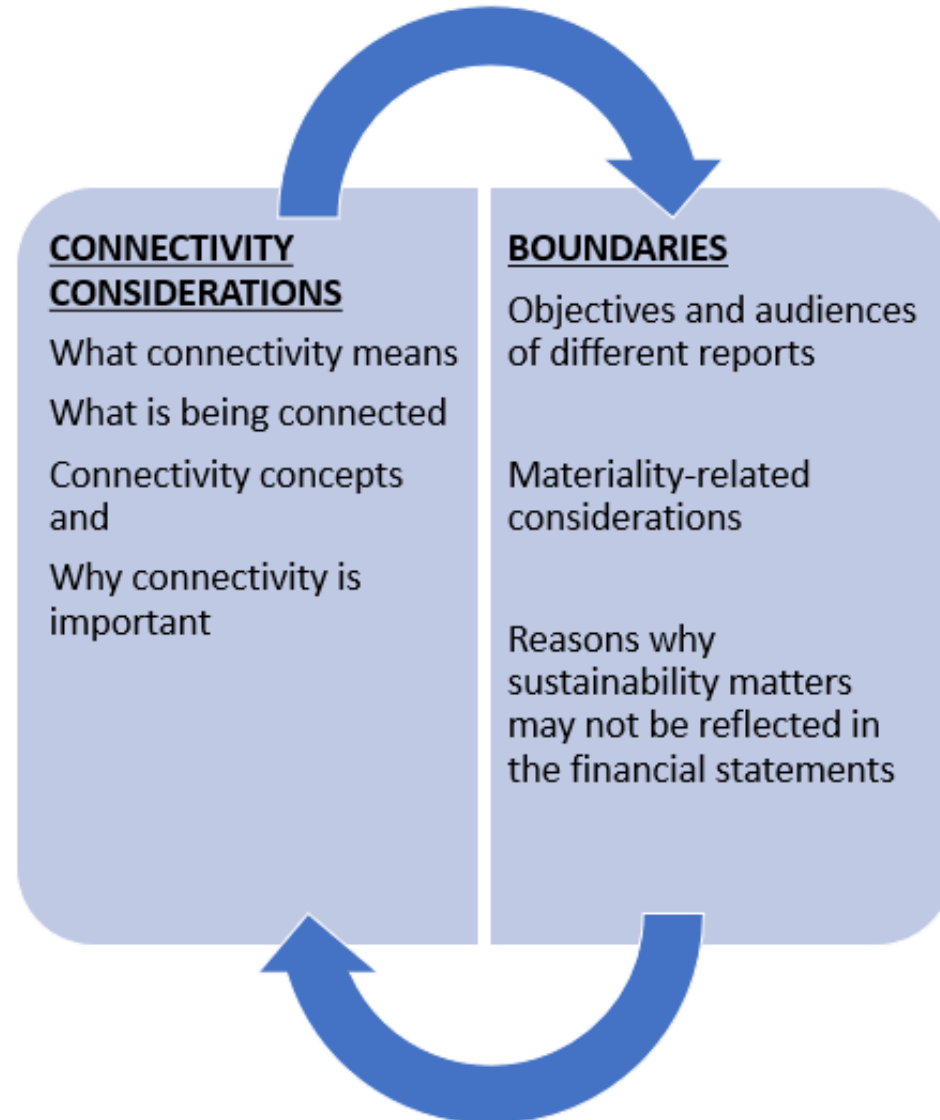
**POINTS OF NOTE:
DRAFT EFRAG
INTERIM
DELIVERABLE
PAPER
AGENDA PAPER
*07-02***

**EFRAG Connectivity Project: Draft Interim
Deliverable Paper - 04 June 2024**

*Connectivity considerations & Boundaries of different
Annual Report sections*

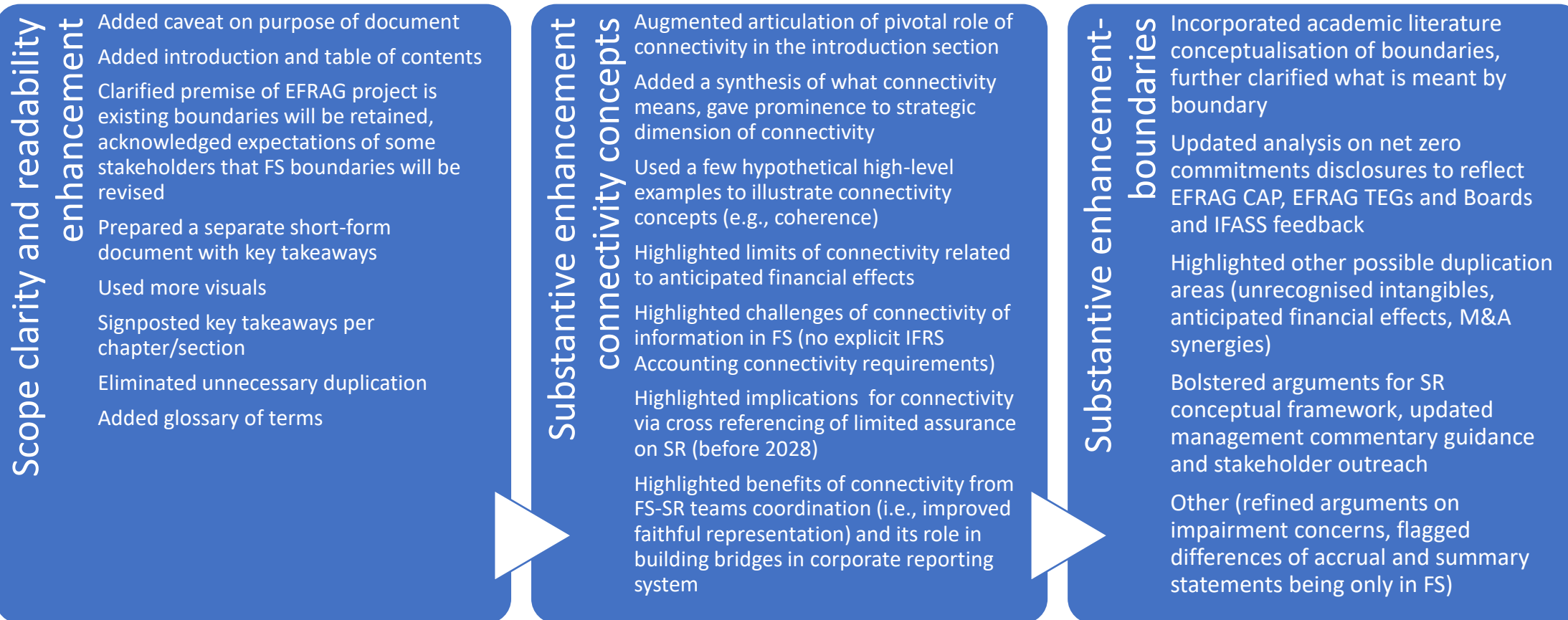


IDP STRUCTURE

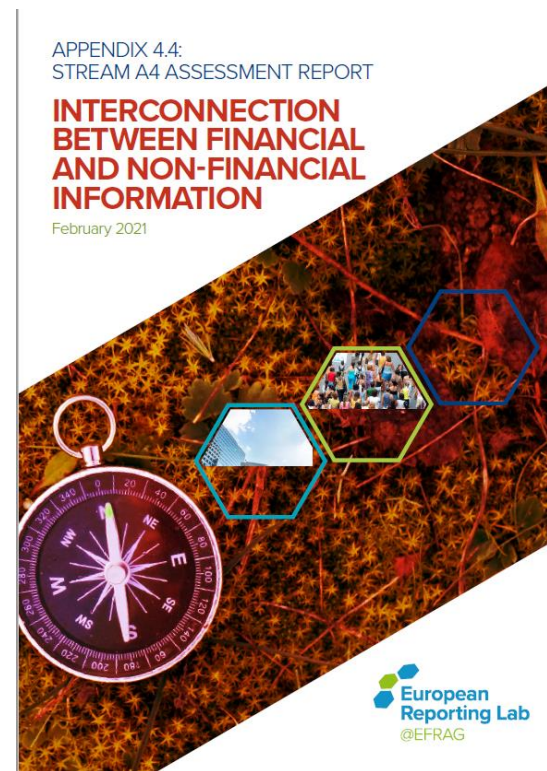


IDP ENHANCEMENT SINCE LAST MEETING

Incorporated suggestions made across the various meetings to enhance the substance and readability of IDP



IMPORTANCE OF CONNECTIVITY FOR ROBUST EU CORPORATE REPORTING



IN THE EFRAG EUROPEAN LAB PROJECT TASK FORCE FOR NON-FINANCIAL REPORTING STANDARDS (PTF-NFRS) PREPARATORY WORK FOR ESRS, CONNECTIVITY WAS IDENTIFIED AS ONE OF THE KEY STEPS FOR SETTING UP A ROBUST CORPORATE REPORTING SYSTEM (BOTH FR AND SR) IN THE EU. REQUIREMENTS FOR RECIPROCAL (TWO-WAY) CONNECTIVITY SUGGESTED.

CONNECTIVITY LESSENS GAPS, OVERLAPS/DUPLICATIONS AND CONTRIBUTES TO COHERENT REPORTING

IMPORTANCE OF CONNECTIVITY HIGHLIGHTED IN SEVERAL OTHER EFRAG PUBLICATIONS & EVENTS

CLIMATE-RELATED RISKS IN THE FINANCIAL STATEMENTS



EFRAG SECRETARIAT BRIEFING

SUMMARY: EFRAG OUTREACH, LEARNINGS FROM REVIEWS OF EUROPEAN REPORTING TRENDS

SEPTEMBER 2023

MULTI-STAKEHOLDER PERSPECTIVES ON CONNECTIVITY

SUMMARY REPORT

26 MAY 2023 - EAA 45TH ANNUAL CONGRESS



EFRAG CONFERENCE 2023

EUROPEAN CORPORATE REPORTING: TWO PILLARS FOR SUCCESS



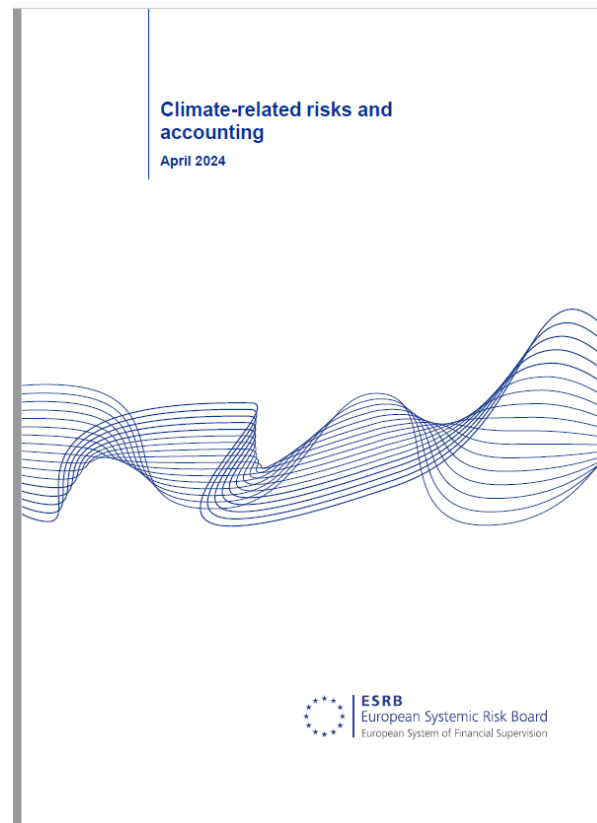
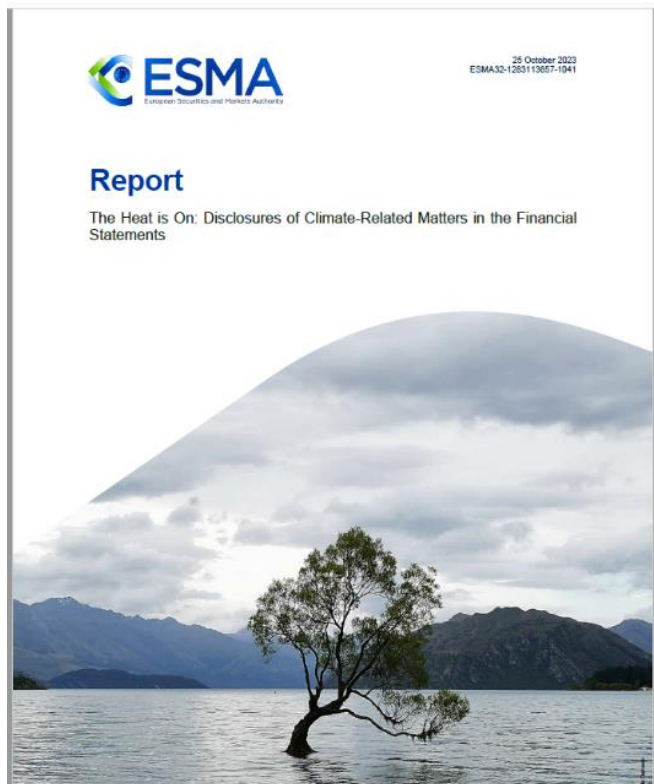
Summary Report
EFRAG



CONNECTIVITY WAS THE TOP RANKED PROJECT DURING THE 2021 EFRAG PROACTIVE RESEARCH AGENDA CONSULTATION

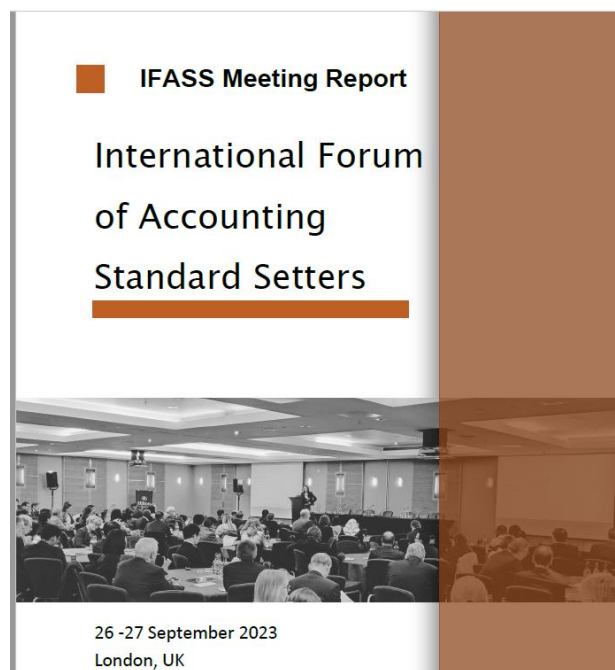
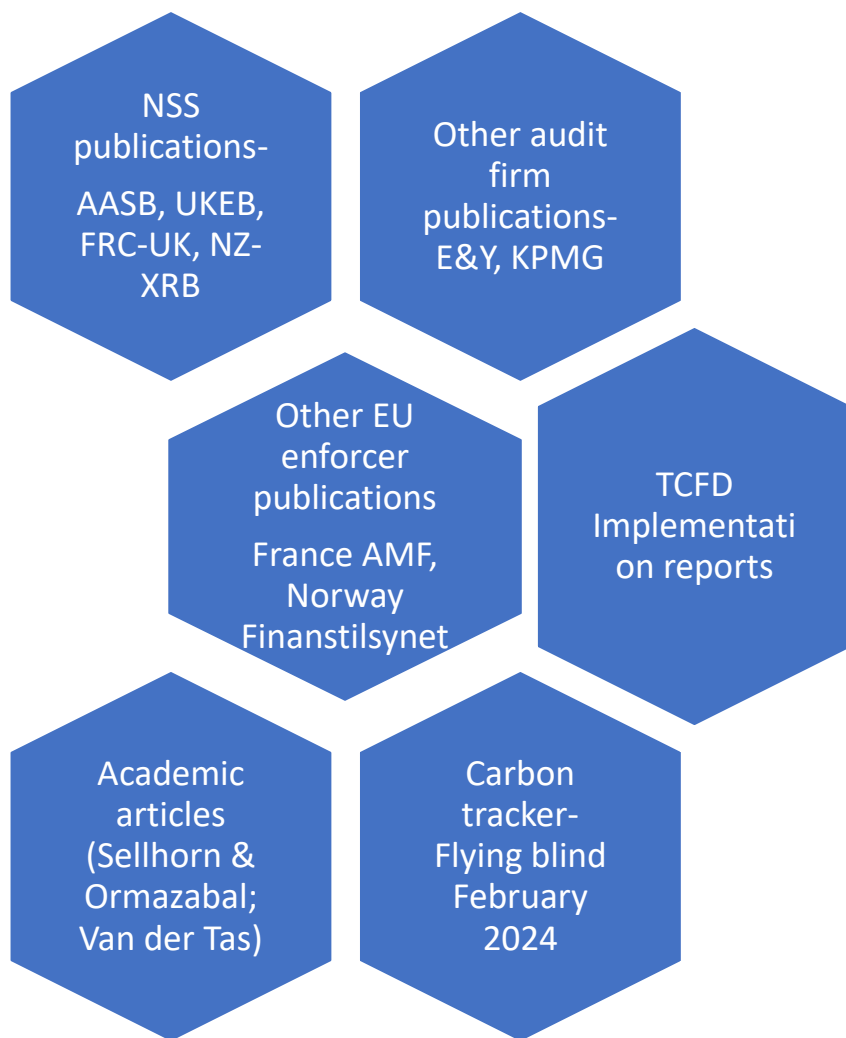
STAKEHOLDERS HAVE EXPRESSED CONCERN THAT IN THE ABSENCE OF CONNECTIVITY THERE CAN BE A DOUBLE REPORTING BURDEN FOR PREPARERS, USERS CAN ALSO DOUBLE COUNT INFORMATION DURING VALUATION

IMPORTANCE OF CONNECTIVITY HIGHLIGHTED IN OTHER RECENT PUBLICATIONS ON EUROPEAN REPORTING



FAILING TO ENSURE CONNECTIVITY BETWEEN ACCOUNTING AND SUSTAINABILITY STANDARDS CAN HAVE NEGATIVE EFFECT ON THE QUALITY OF INFORMATION DISCLOSED TO CAPITAL MARKETS, WITH POTENTIALLY SYSTEM-WIDE CONSEQUENCES- ESRB REPORT

IMPORTANCE AND RELATED ISSUES ALSO COVERED IN MULTIPLE NSS, REGULATOR AND OTHER STAKEHOLDER PUBLICATIONS AND IFASS MEETINGS



CONNECTIVITY AND BOUNDARIES OF DIFFERENT CORPORATE REPORTS ARE INTERRELATED



Boundaries of different reports = (what information is included or excluded in different reports)

Boundaries both necessitate and affect the connectivity of information

Varied evolution, maturity and objectives of different corporate reports has resulted in their distinct boundaries

Connectivity of information with different boundaries is necessary for coherent annual reporting package with complementary components

At the same time criteria for inclusion can limit connectivity (e.g., level of aggregation, SR consideration of value chain)

Expectation gaps on what can be reported arise due to lack of clarity on boundaries.

The premise of the EFRAG research is that the existing distinct boundaries of different corporate reports (financial statements and the ESRS sustainability statement) will be retained for the foreseeable future.

Possible revision of boundaries not included in the EFRAG project articulation of connectivity

PART 1: CONNECTIVITY CONSIDERATIONS

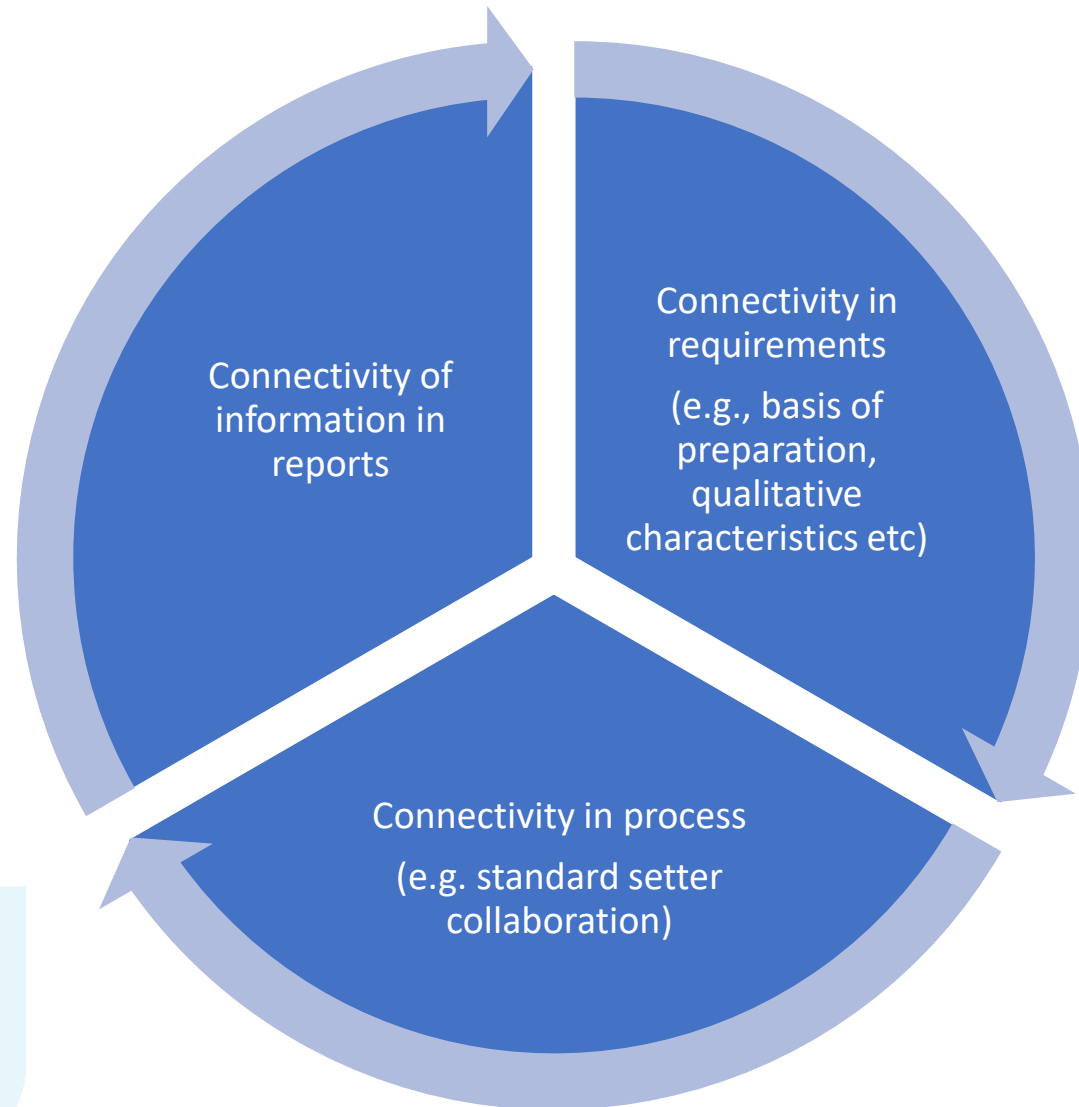
WHAT IS CONNECTIVITY?

WHAT IS BEING CONNECTED? (i.e. EU vs IFRS general purpose financial reporting)

CONNECTIVITY CONCEPTS & EFFECTS ON REPORTING

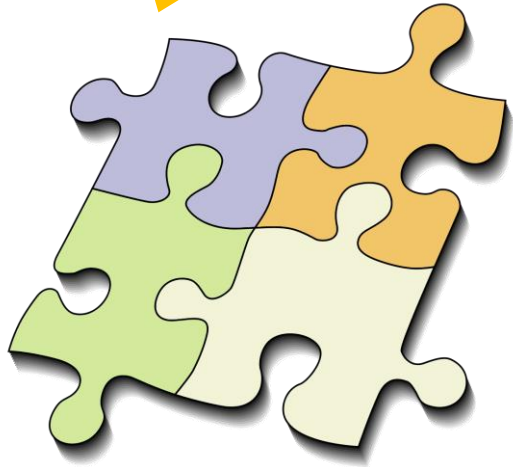
WHY CONNECTIVITY IS IMPORTANT

WHAT IS CONNECTIVITY



**Integration in reporting
(as per ISSB agenda
consultation) is a
broader notion than
connectivity**

Synthesis of what connectivity of information means



Communication/depicting the connection between strategic choices, value creation factors, and financial effects

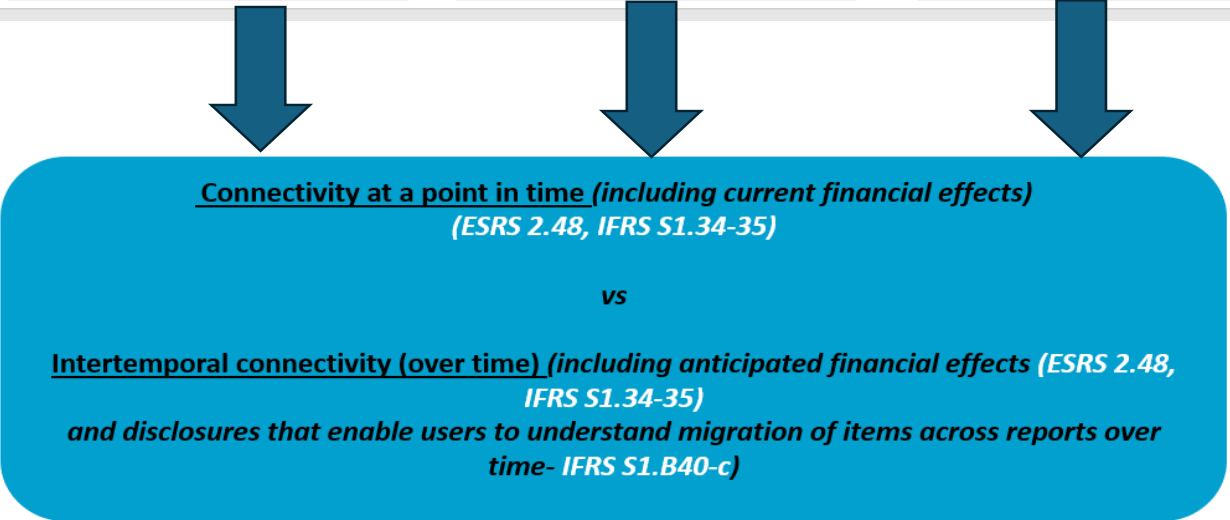
- Entity's explaining how their SBM, risks and opportunities are linked to financial position, financial performance, cash flows, other metrics and targets in short, medium and long term (ESRS 1.123 and IFRS S1.35 and IFRS S1.B44)
- Linking disclosures of risks entities face from reliance on resources/dependencies to entities actions/strategy to mitigate these risks and disclosed related current and anticipated financial effects (ESRS 1.123 and IFRS S1.B 43)
- Explaining trade-offs between risks and opportunities faced when setting strategy (IFRS S1.B44)
- Presentation and disclosure of information within and across different corporate reports in a manner that gives a more complete picture of an entity's value creation while depicting the interrelatedness of the overall reported information (i.e. coherence) (Derived from IASB MCPS ED)

Techniques/methods for connecting interrelated quantitative, narrative information

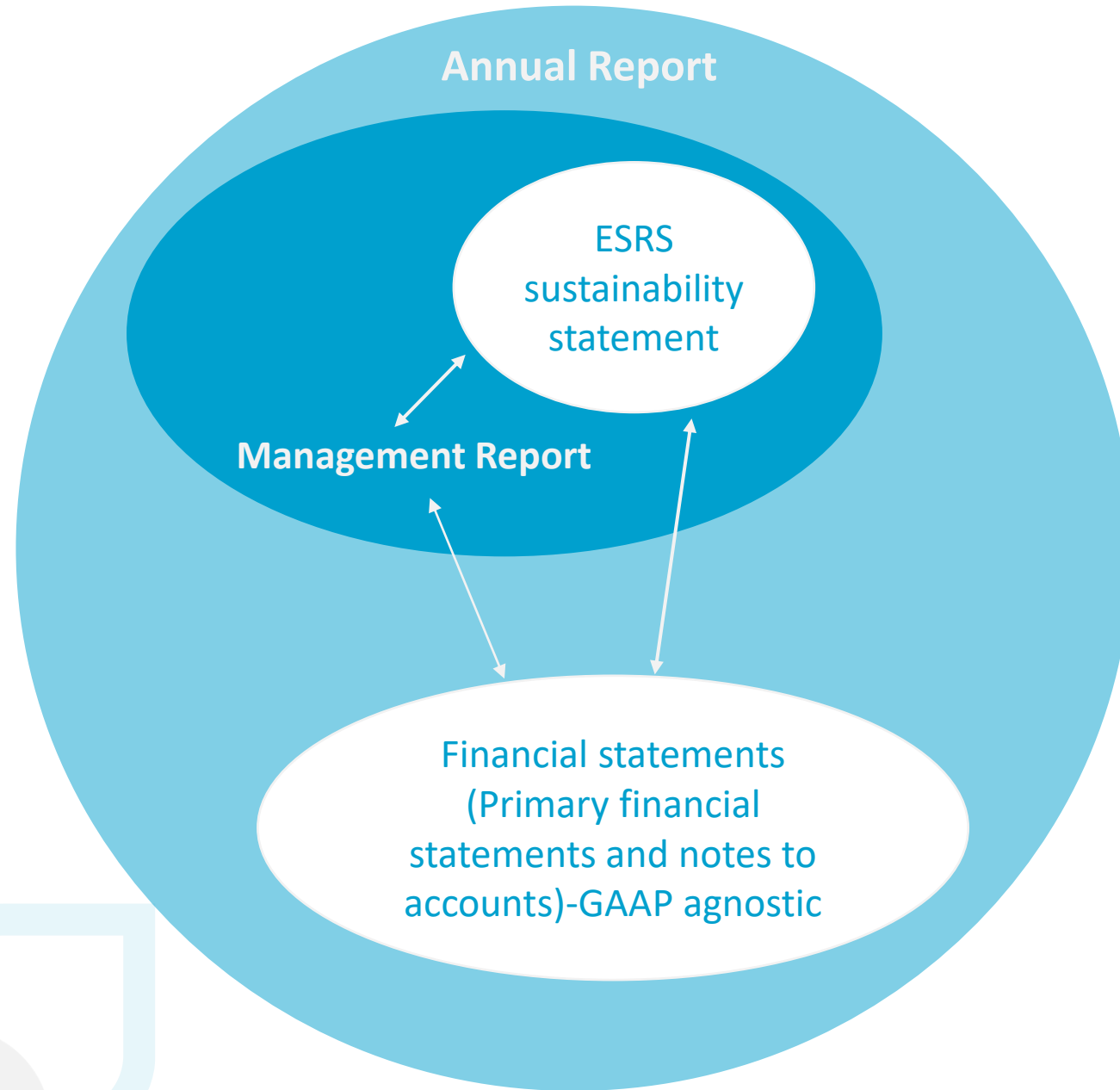
- Linking quantitative via cross-referencing (direct connectivity as per ESRS) (ESRS 1.124-125)
- Linking quantitative information via reconciliations (indirect connectivity as per ESRS) (ESRS 1.124-125)
- Qualitative disclosures stating financial statements line items affected by disclosed risks and opportunities if unable to disclose quantitative current and anticipated financial effects (IFRS S1.40)
- NON-MANDATORY ELEMENTS BELOW**
- Not required, stakeholders have also suggested explaining why information cannot be connected (e.g., due to differing level of aggregation) could be useful
- Correlation and cause and effect links (voluntary practice, e.g., SAP past reports)

Consistency (ESRS 1.127-128 and IFRS S1.23)

- Consistent data, narrative/qualitative disclosures, assumptions and units of measurement (presentation currency) across SR and the financial statements
- Disclosure and explanation of lack of consistency



WHAT IS BEING CONNECTED UNDER EU CORPORATE REPORTING?



ESRS sustainability statement- SR (objectives, location and scope)

- Clear demarcation of SR versus financial statements objectives
- Clear placement within management report
- Entities in scope (large undertakings: IFRS and local GAAP applicants)

SR audience and materiality

- Broad set of users (including investors), investors deemed to consider financial and impact material information
- Double materiality perspective
- Same definition of financial materiality as financial statements

What is being connected under IFRS general purpose financial reporting



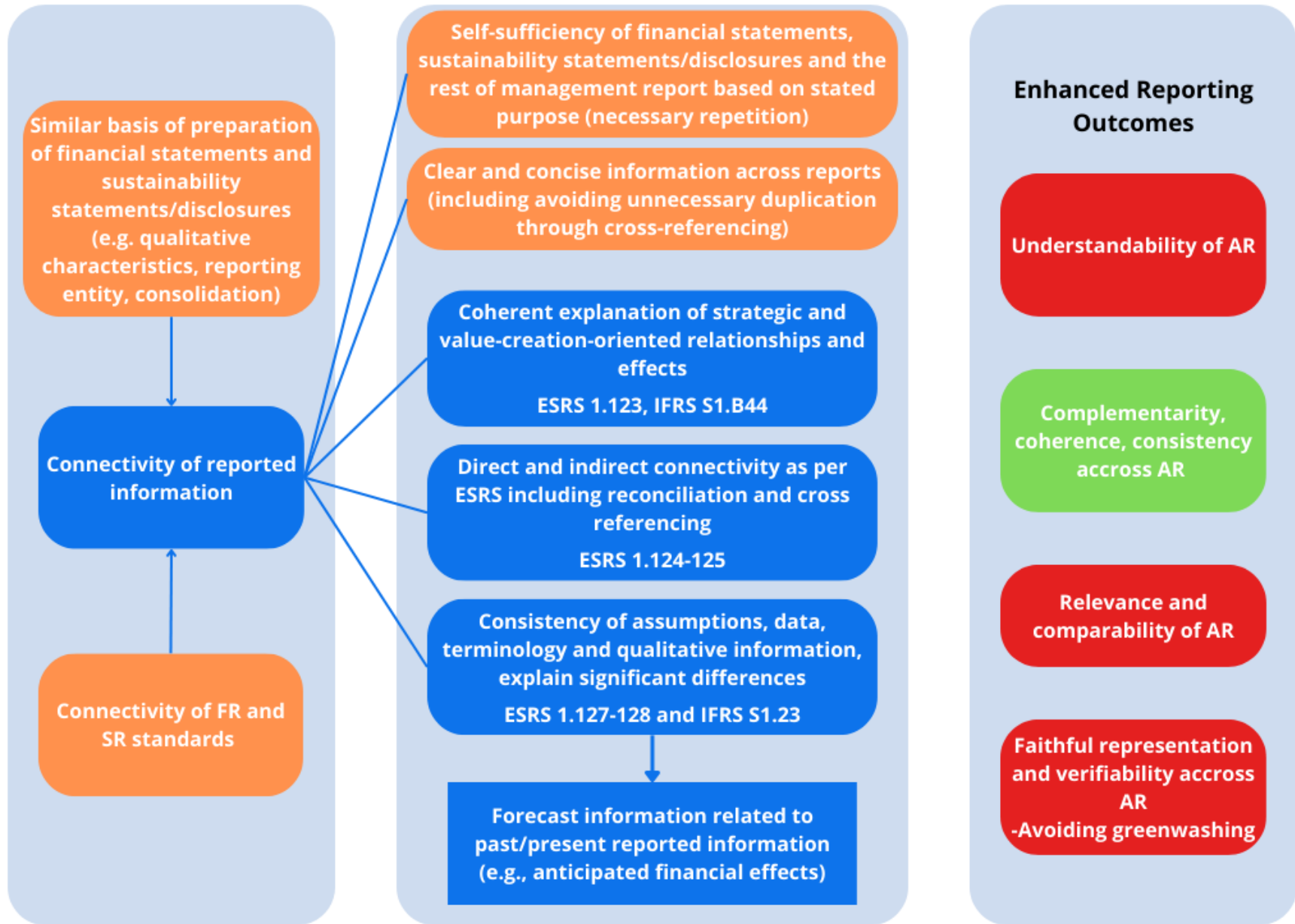
SR information (sustainability-related financial disclosures)

- Component of general purpose financial reporting, has same materiality as financial statements, management commentary
- Location agnostic (e.g., can be in notes to accounts)

Audience of SR information

- Same primary audience as financial statements (i.e., investors, lenders)

CONNECTIVITY CONCEPTS & EFFECTS ON REPORTING



CONNECTIVITY FROM INSIDE TO OUTSIDE THE FINANCIAL STATEMENTS

- Conceptualisation and illustration of two-way connectivity (i.e. SR to FS, and FS to SR) is in the scope of the EFRAG connectivity project.
- **No explicit IFRS Accounting connection requirements.** Can ESRS and IFRS Sustainability standards connection requirements (SR requirements) be extended to FS information? This question is pertinent for assessing the illustrations of connectivity of financial statements information in Discussion Paper.
- **EFRAG connectivity project is not proposing connection guidance for financial statements information. It is the IASB's job to do that (e.g., through current project on climate-related and other uncertainties in the financial statements)**

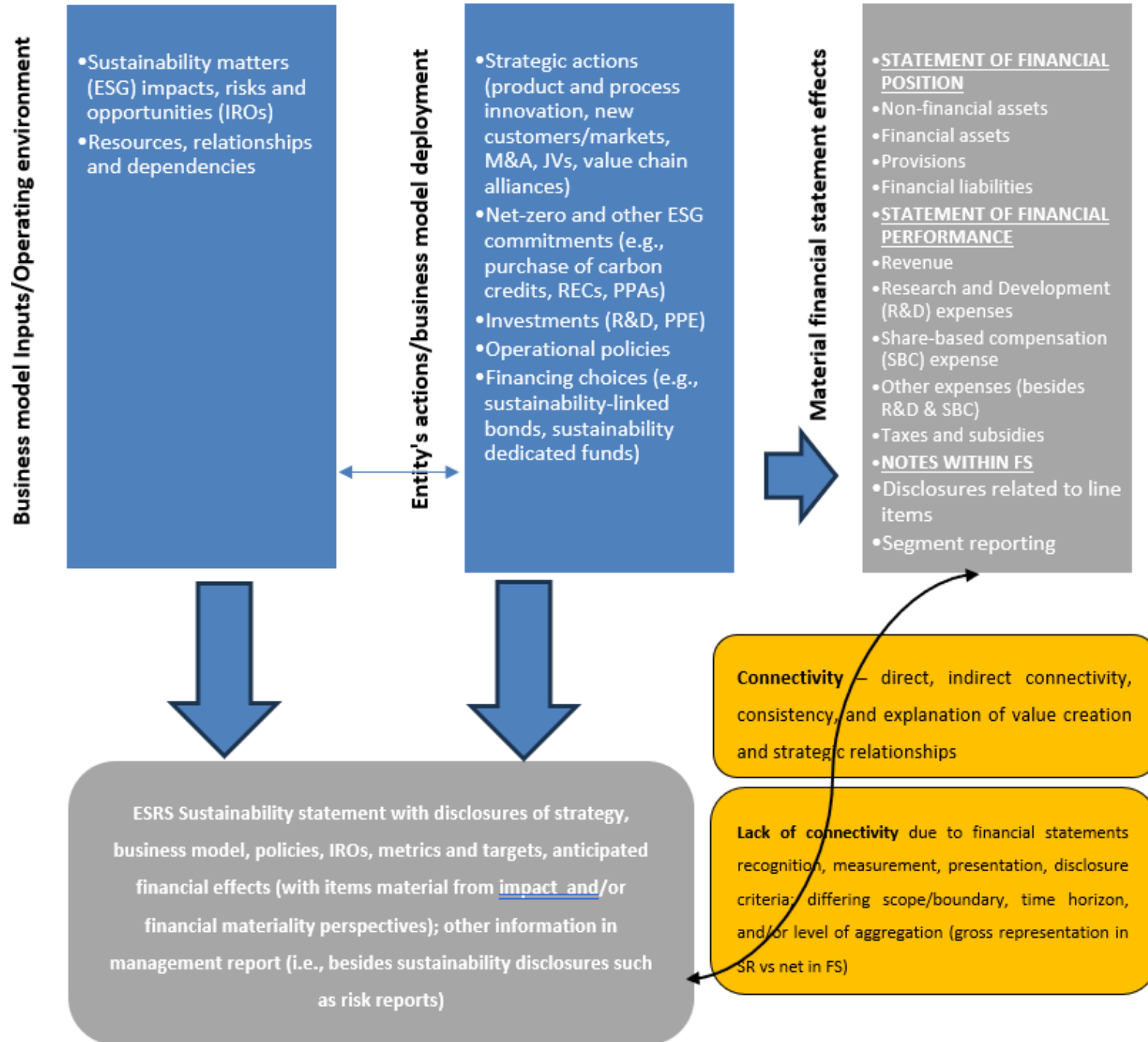
SOME SR CONNECTION REQUIREMENTS CAN BE CONSIDERED FOR FS INFORMATION

- Explaining relationships (effect of strategic choices to IROs on financial statements) and ensuring consistency of assumptions, narrative could be applied between financial statements information and SR information
- No explicit prohibition to cross-referencing material information or signposting supplemental information outside the financial statements

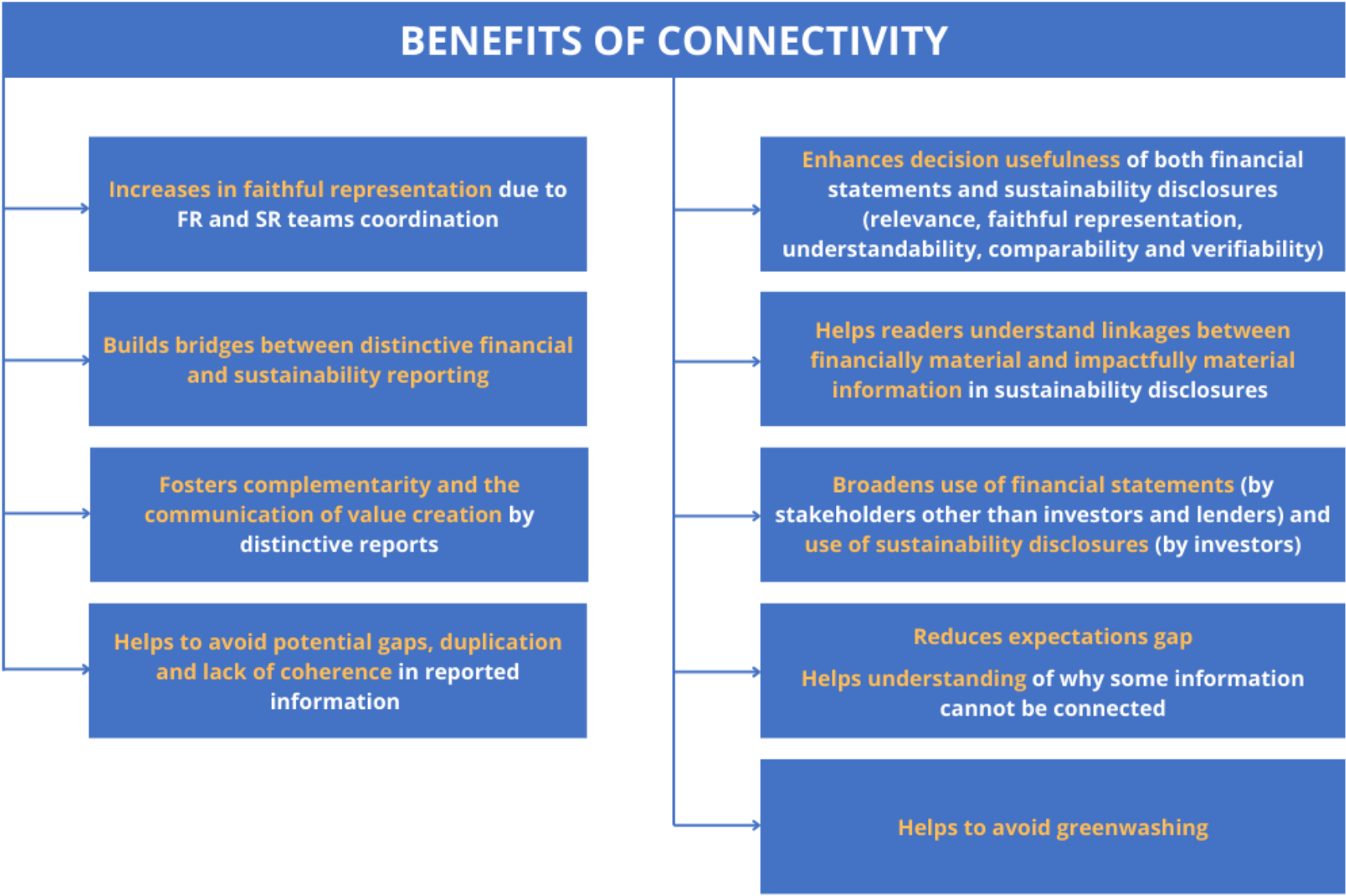
CONSTRAINTS TO APPLYING SR CONNECTION REQUIREMENTS FOR FS INFORMATION

- Limits to cross-referencing SR information in FS (legal risk on forward-looking information, excessive cross-referencing could impair understandability, different level of assurance (current limited assurance of SR) could be an impediment to incorporating information outside the financial statements by cross reference into the financial statements)
- View expressed within EFRAG CAP that techniques/approaches related to indirect connectivity concept (e.g., reconciliations to information outside the FS) are hard to apply for financial statements information

CONNECTIVITY LINKS BUSINESS MODEL, STRATEGY TO REPORTING



SYNTHESIS- WHY CONNECTIVITY IS IMPORTANT



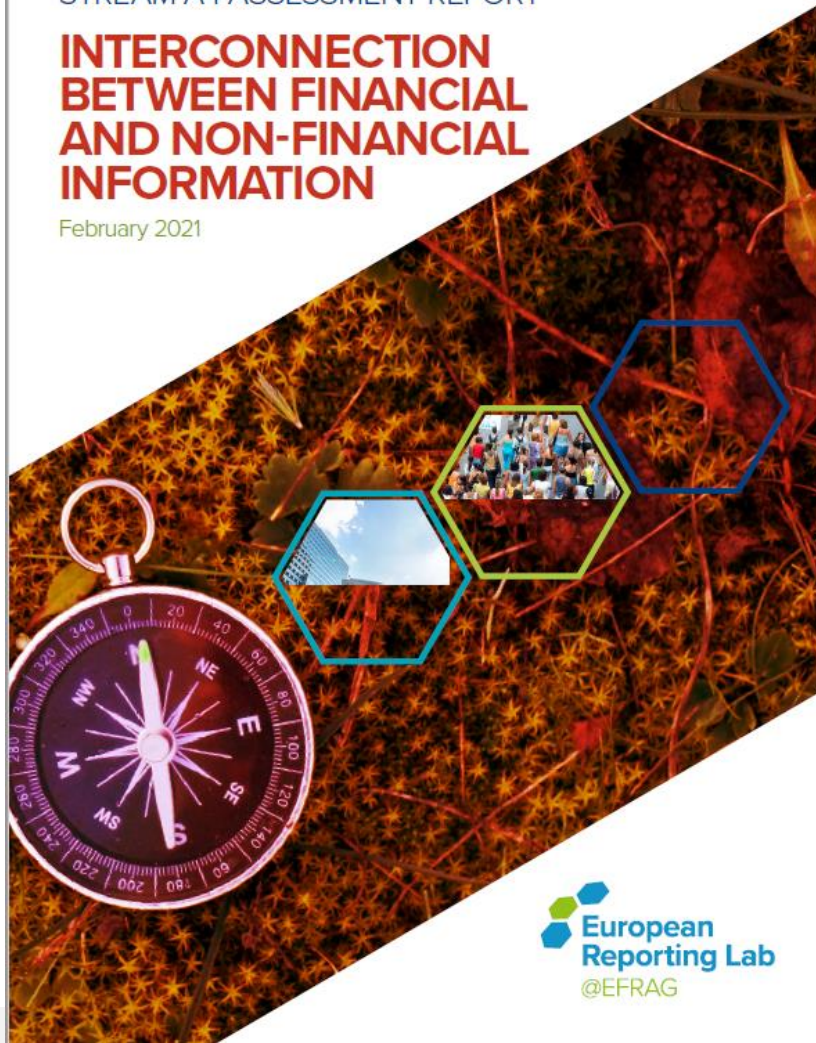
**BOUNDARIES OF FINANCIAL STATEMENTS,
MANAGEMENT REPORT, SUSTAINABILITY STATEMENT**

**BOUNDARY= DIVIDING LINE OF INFORMATION
INCLUDED OR EXCLUDED WITHIN CORPORATE REPORT,
REPORTING DOMAIN, SECTION OF AR**

APPENDIX 4.4:
STREAM A4 ASSESSMENT REPORT

INTERCONNECTION BETWEEN FINANCIAL AND NON-FINANCIAL INFORMATION

February 2021



European
Reporting Lab
@EFRAG

EFRAG CAP CONCEPTS SUBGROUP DISCUSSIONS , NSS

Materiality publications

EFRAG OUTREACH INCL ON IASB CLIMATE RISK PROJECT

Understanding reporting boundaries in annual reports: a conceptual framework

Lyndie Bayne

UWA Business School, University of Western Australia, Perth, Australia

Abstract

Purpose – The purpose of this paper is to enhance conceptual understanding of reporting boundaries in corporate annual reports by developing a conceptual framework of the rules and principles, referred to here as dimensions, underlying boundaries. A total of nine contemporary regulations/guidelines are compared in terms of the boundary dimensions identified to illustrate similarities and differences in boundary concepts.

Design/methodology/approach – To develop a conceptual framework of reporting boundary dimensions, academic and industry literature were analysed to identify boundary dimensions. Thereafter, nine contemporary regulations/guidelines were compared in terms of these dimensions. A qualitative approach was taken including document analysis and content analysis.

Findings – A total of 10 key boundary dimensions were identified through an analysis of academic and industry literature. Each dimension represents a continuum along which regulations/guidelines can position themselves. Taken together, the 10 dimensions provide a comprehensive description of the chosen boundary concept.

Originality/value – The paper contributes to accounting theory by providing a holistic conceptual framework of dimensions relating to reporting boundaries, thus answering calls for more conceptual development of the boundary construct. The conceptual framework and comparison of contemporary regulations/guidelines adds to scarce literature considering financial and non-financial boundaries simultaneously, which is relevant for annual reports. From a practical perspective, the paper brings renewed visibility to boundaries with implications for preparers, users, standard setters and auditors of annual reports.

Keywords Boundary setting, Reporting boundary, Corporate reporting, Narrative reporting, Non-financial, Corporate social responsibility, Sustainability reporting

Paper type Research paper

THE BOUNDARIES IN FINANCIAL AND NON-FINANCIAL REPORTING

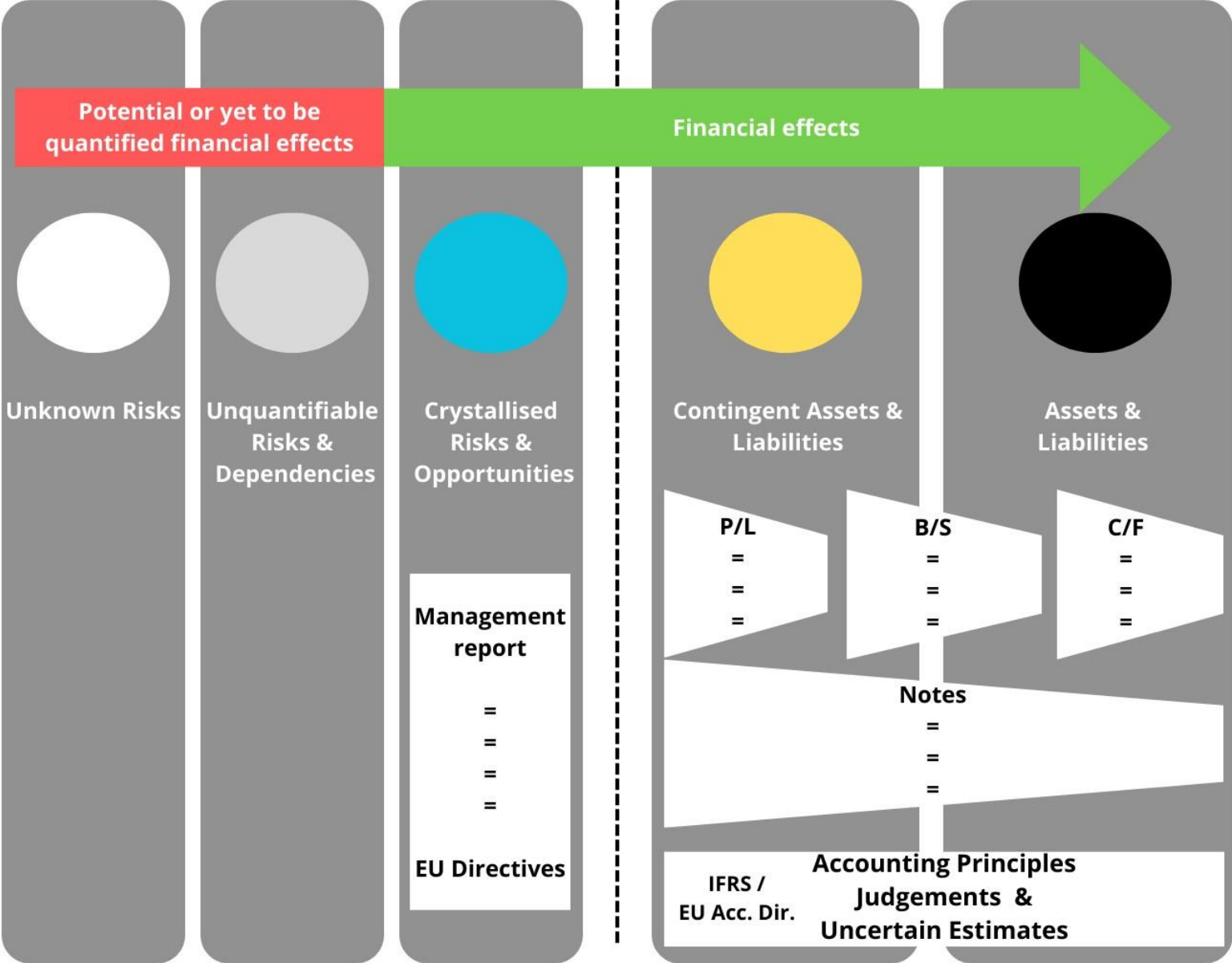
A Comparative Analysis of their
Constitutive Role

Laura Girella

- Objectives, audiences of different corporate reports (FS, management report, sustainability statement)
- Materiality considerations (materiality is interrelated with objectives and audience of different reports)
 - Impact materiality applied in SR, financial materiality applied in both FS and SR but differing objectives result in different information
 - Dynamic dimension of materiality and inter-temporal connectivity
 - Possible grey areas (i.e., duplicated and/or diverse view on suitable location of material information)
 - For example, net-zero commitments related disclosures, i.e. *should disclosures be in SR only or in both SR and FS?*;
 - EFRAG CAP members have noted the need to distinguish between mere intentions vs a constructive obligation that is not a present obligation (valid expectation) vs constructive obligation that is either recognised as provision or disclosed as contingent liability based on current accounting requirements
 - Some users in the CAP have expressed satisfaction with current IFRS criteria for recognising provisions, these users conveyed they do not expect forewarning of potential liabilities to be disclosed within the financial statements
 - Possible overlap between IAS 1.125 (i.e., disclosure of factors in next 12 months that may affect carrying amounts of assets and liabilities) and anticipated financial effects in the short term
- Other dimensions (besides objectives, audiences, reporting entity materiality considerations) affecting boundaries and connectivity- **in following slide**

DYNAMIC DIMENSION OF MATERIALITY AND CONNECTIVITY

MIGRATION OF ITEMS ACROSS REPORTS OVER TIME



OTHER KEY FS versus SR DIFFERENCES

DIFFERENTIATING DIMENSIONS IN ADDITION TO OBJECTIVES, AUDIENCES, MATERIALITY CONSIDERATIONS ARE

- **Recognition, measurement, disclosure, presentation criteria** in FS
- **Differing level of aggregation** (e.g., can arise due to gross exposure disclosure in sustainability reporting- SR versus mitigated/net exposure effects reflected in FS) Example 19 of EFRAG MAIG
- **Anticipated financial effects may not crystallise in future period FS** (anticipated financial effects may be related to value chain, and also due to outcome/occurrence uncertainty and measurement uncertainty)
- Extent to which **forward looking information** is incorporated (done to a greater extent in SR)
- **Time horizon** typically applied for SR vs FS albeit there are no time horizon limits for FS
- Extent to which **non-monetary metrics** are incorporated
- Application of **accrual principle (inter-period allocation of amounts) and preparation of aggregated summary statements** only done in FS
- Consideration of **value chain** in SR
- Consideration of **operational control** while calculating metrics in SR allowed

TECHNOLOGY CAN FOSTER CONNECTIVITY- ADDRESSED IN APPENDIX OF IDP

How can this be achieved?

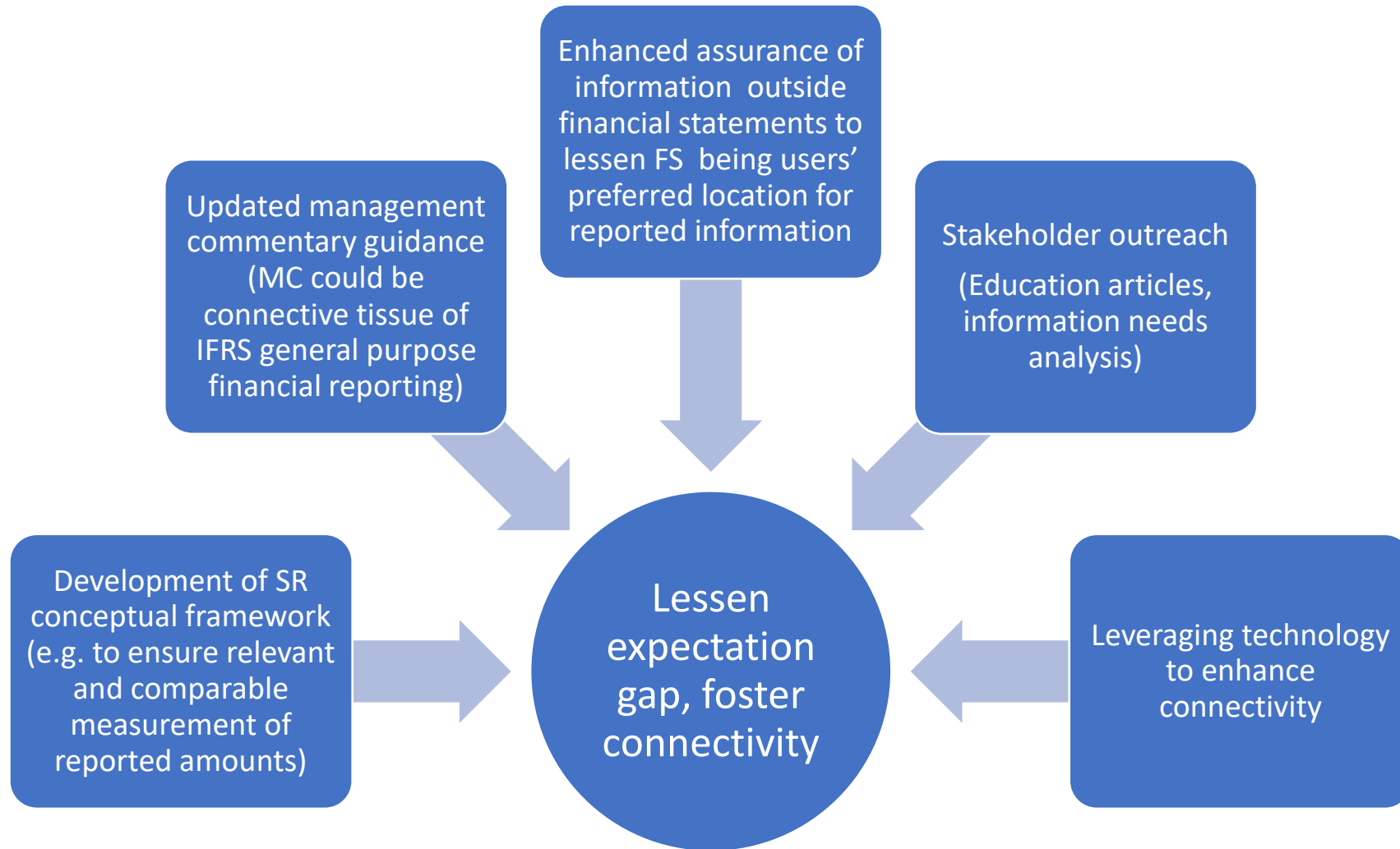
- Use of interactive technology
- Use of natural language processing to identify the co-occurrence of information
- Tagging information using XBRL
- Possible use of AI in tandem with XBRL tagged for analysis of information (i.e., by users)

Availability of 3 taxonomies (IFRS Accounting, ESRS, and Article 8-EU taxonomy) presents an opportunity

- Potential creation of interoperability of 3 taxonomies
- Reconciliation of financial statement line items and operating segments with ESRS sectors and related data points



TAKEAWAYS - LESSENING THE EXPECTATION GAPS & FOSTERING CONNECTIVITY





Questions for EFRAG SRB MEMBERS

Q1: Do you have any final suggestions for the enhancement of the interim deliverable paper content?

