ALDERSGATE GROUP
LEADERS FOR A SUSTAINABLE ECONOMY

Aldersgate Group response to Non-Financial Reporting Review Call for Evidence

August 2023

Background

The Aldersgate Group represents an alliance of major businesses, academic institutions and civil society organisations, which drives action for a competitive and environmentally sustainable UK economy.[1] Our corporate members represent all major sectors of the economy, such as Associated British Ports, Aviva Investors, BT, CEMEX, the John Lewis Partnership, Johnson Matthey, Michelin, Nestlé, Siemens, SUEZ, Tesco, and Willmott Dixon. They believe that ambitious environmental policies make clear economic sense for the UK, and we work closely with our members when developing our independent policy positions.

The following questions are primarily aimed at the preparers of non-financial information.

How valuable, if at all, is the preparation and/or disclosure of non-financial information for the effective running of your company?

- ☐ **Highly valuable**
- ☐ Moderately valuable
- ☐ Somewhat valuable
- ☐ Not valuable
- ☐ Don't know

And why do you say that?

Amongst our corporate members, there is a clear acknowledgement that the preparation and disclosure of high-quality, comparable, and decision-useful non-financial information is fundamental to the effective running of a company. Members raised several reasons why they find it highly valuable to disclose this information:

- *Establishing credibility.* The disclosure of climate-related information (such as GHG emissions, risks and opportunities, and targets) is essential to be considered as both credible and transparent amongst shareholders, suppliers, consumers, employees, and other stakeholders. This information helps communicate companies' performance against non-financial targets and demonstrates they are meeting

[1] Individual recommendations cannot be attributed to any single member and the Aldersgate Group takes full responsibility for the views expressed.

info@aldersgategroup.org.uk www.aldersgategroup.org.uk

stakeholder expectations within tenders, expectations from investors, and regulatory compliance. Together, this helps companies become recognised as trusted partners of the services they provide.

- *Gaining a competitive advantage*. A recent survey by PwC found that nearly 80% of investors said ESG was an important factor in investment decision making. At the same time, polling has found that fear of greenwashing is the top reason holding back ESG investing. Providing robust and reliable information and data to assess long-term risks and opportunities, therefore, will help inform investors' financial decisions and risk appetites. A 2022 study of 465 firms with science-based emissions-reductions targets found a positive link between their corporate carbon emissions performance and their corporate financial performance.

- *A new business norm*. Growing external pressure from regulators, investors, and other stakeholders has made the disclosure of non-financial information a new business norm. Simply, as members put it, you can no longer transact or do business without it. This is reflected in the recent uptake of climate clauses in commercial contracts, such as supply chain agreements to reduce scope 3 emissions or in lender terms of sustainability-linked loans to confirm that a percentage of its lending is sustainable or 'green finance'.

- *Risk management tool*. The preparation of non-financial information helps companies to better manage risks as well as consider their current and future impacts on sustainability issues. This helps to mainstream climate and nature-related risks and opportunities within business planning and operational decisions: building company culture and ensuring management buy-in.

What challenges, or costs, if any, does the preparation, disclosure and distribution of non-financial information create for your company?

According to our corporate members, the greatest challenge related to the preparation, disclosure, and distribution of non-financial information is having to comply with multiple, overlapping sustainability reporting regimes.

In recent years, there has been a proliferation of reporting frameworks globally. In addition to the country-specific rules being adopted by the likes of the UK, EU, US and other jurisdictions, there are at least 182 different voluntary reporting frameworks – including CDP, Global Reporting Initiative, UN Global Compact, and the Sustainability Accounting Standards Board.

This complex sustainability reporting landscape increases companies' reporting burden, as different frameworks require different metrics - increasing the headcount, time, and resources required. The lack of comparable reporting standards also makes it more difficult

for investors to assess the relative risk profiles of different companies, which means they cannot properly embed climate considerations into their investment decisions.

Ensuring a degree of interoperability on disclosures between new UK regulation and European and global regulatory initiatives is key to reducing the compliance cost for companies. The UK Government should also publish ongoing guidance which outlines the differences and points of similarity between the UK and other jurisdictions' corporate sustainability reporting frameworks.

Members also raised that another cost created by the preparation, disclosure, and distribution of non-financial information is the cost of assurance. Whilst there is currently no mandatory requirement in the UK for companies to have their non-financial information externally assured (e.g., TCFD-aligned reporting), there is a market expectation for reported information to be robust and credible. This means many companies voluntarily obtain third-party confirmation of their emissions figures. According to an EU Commission-led public consultation reviewing the Non-Financial Reporting Directive, the average cost for respondents of any kind of assurance (limited, reasonable or a mix) is €50 000.

Similar to the U.S. Securities and Exchange Commission's climate disclosure proposals and the EU's Corporate Sustainability Reporting Directive (CSRD), the UK should look to introduce mandatory assurance requirements by an accredited independent audit/certifier over time, beginning with a 'limited assurance' requirement before progressing to a 'reasonable assurance requirement. This would help to create a level playing field, ensuring that companies that disclosure assured, robust information are not undercut by companies that do not.

What, if any, are the key drivers of cost when having to comply with non-financial reporting requirements?

Please respond in line with the following considerations listed below:

- *Staff costs;*
- *Time costs;*
- *Production costs;*
- *IT infrastructure costs;*
- *Any other relevant costs.*

As mentioned above, the complexity of the sustainability reporting landscape is a key driver of costs. Multinational companies will need to comply with multiple different frameworks, increasing the number of staff, length of time, and resources (such as consultancies, assurance, and staff training) required.

Members also emphasised the importance of having sufficient lead-time to prepare and get to grips with new non-financial reporting requirements. Few, if any, organisations are day-one ready to meet new requirements, yet uncertainty around timings and practicalities makes it hard for companies to budget, plan, and upskill – ultimately increasing compliance

info@aldersgategroup.org.uk www.aldersgategroup.org.uk

costs. The business community, for example, is still awaiting further details on the implementation of the Sustainability Disclosure Requirements (SDR) framework, first announced in the 2021 Chancellor's Mansion House speech. Companies need to know what reporting against this framework will look like, including guidance, rollout timelines, integration with the ISSB, and how it will streamline existing climate reporting requirements.

The UK Government can help address this market confusion by publishing a detailed roadmap setting out its plans and the trajectory of non-financial reporting in the UK, with clear timelines, expectations, and guidance for businesses in scope.

Please select the most applicable statement:

☐ The benefits of preparing and disclosing non-financial reporting information outweigh the costs

☐ The costs of preparing and disclosing non-financial reporting information outweigh the benefits

☐ The benefits of preparing and disclosing non-financial reporting information are proportionate to the costs

☐ Don't know

Please explain your answer.

Our corporate members report that, currently, the benefits of preparing and disclosing non-financial information is proportionate to the costs.

There is a concern, however, that as reporting requirements continue to grow – potentially integrating new elements such as ISSB, TNFD-aligned disclosures, and mandatory scope 3 emissions reporting – so will the costs, as inevitably companies will require more staff, time, and resources to generate additional information and have it assured.

To ensure the benefit to cost ratio remains proportionate, the UK Government must look to further maximise benefits and minimise costs. This can be achieved by simplifying the reporting framework, by ensuring a minimum degree of interoperability with reporting regimes in other jurisdictions and finding efficiencies in the reporting process – for example, removing unnecessary areas of duplication (see next section).

info@aldersgategroup.org.uk www.aldersgategroup.org.uk

ALDERSGATE GROUP LEADERS FOR A SUSTAINABLE ECONOMY

The following questions are aimed at all respondents

What changes, if any, would you like the UK Government to make to the current legal requirements for companies to prepare non-financial information, and why?

Above all, our corporate members would like to see the UK Government develop an *interoperable*, *streamlined*, and *coherent* reporting framework.

Interoperability. As mentioned above, multiple overlapping sustainability reporting frameworks is a major challenge for businesses, as it increases reporting costs and reduces investors ability to compare between companies and account for climate and nature-related risks and opportunities when making investment decisions.

Analysis by Refinitiv has found that 1,183 UK businesses will be subject to the EU's CSRD, due to come into effect in 2024. A study by the European Commission estimated that the recurring administrative costs for providing non-financial statements under the NFRD are on average €82 000 per year. Diverging from the CSRD will only increase reporting costs for UK companies operating in the EU and multinationals bridging both – making it harder to attract trade and investment.

To avoid the fragmentation of sustainability-related reporting standards globally, equivalence mechanisms (for example, on the introduction of a 'double materiality' principle, mandatory assurance, and phased reporting requirements across the economy) may be needed. In addition to this, the UK Government should also publish ongoing guidance which outlines the differences and points of similarity between the UK and other jurisdictions' corporate sustainability reporting frameworks.

Streamlining. The UK government can help further minimise costs and maximise benefits by simplifying the UK's corporate reporting regime, for example, by reducing unnecessary duplication.

A good case in point of unnecessary duplication in non-financial reporting is TCFD-aligned disclosures in annual reports. According to government guidance, relevant companies should include TCFD-aligned climate disclosure within the section of the Non-Financial and Sustainability Information Statement. found within the strategic report component of the annual report. As the TCFD-aligned disclosure is in a separate standalone section, there is a degree of repetition and cross-referencing across other areas of the annual report, such as the principle risk section of the strategic report. Removing areas of repetition such as this will help to reduce the length of annual reports. This will reduce the complexity for preparers and improve the accessibility for users.

The Department for Business and Trade and the Financial Reporting Council should seek to identify other areas of duplication in domestic reporting requirements.

Coherency. The UK government can help to maximise the benefits of non-financial reporting by ensuring it is coherent, both in terms of companies in scope of reporting requirements and the integration of financial and non-financial information.

info@aldersgategroup.org.uk www.aldersgategroup.org.uk

The government should ensure there is a level-playing field for companies disclosing non-financial information. For example, currently, there is no policy in place to mandate disclosure of transition plans for large private companies. As highlighted by the Independent Review of Net Zero, the transition to net zero is a whole economy one. The lack of requirement on large private companies omits a significant part of the business community in the development of strategies to achieve net zero emissions. The Aldersgate Group believes the UK government should set out a clear and interative timeline for extending mandatory requirements to all large companies, including private ones. This will help improve the availability, comparability, and transparency of information available to investors, help to mainstream net zero consideration in core business operations, and ensure listed companies are not at a competitive disadvantage.

The UK government should also look to issue guidance to further integrate non-financial reporting within companies' financial reports and audits. A 2022 research paper by Swiss Finance Institute found that 79% of global investors believe climate reporting is at least as important as financial reporting. Despite this, the World Business Council of Sustainable Development (WBCSD) found that only 35% of members reports combined financial and non-financial information.

Integrating non-financial reporting within annual reports and accounts not only improves accessibility and transparency for investors and consumers, but helps communicate a holistic view of a companies' financial health and long-term value. Additionally, research by WBCSD finds that integrated reports take less time on average to produce than stand-alone sustainability reports (3.4 months compared to 4.5 months after the end of the fiscal year).

Thinking about the future of your organisation and the UK's transition to a net zero economy, what changes, if any, do you think may be required to the type of non-financial information produced to guide decision making, and why?

In the future, the UK's corporate reporting framework must remain in lockstep with other reporting standards developing globally:

- Once the final Taskforce for Nature-related Financial Disclosure (TNFD) framework has been finalised, the government should look to integrate it into its corporate reporting framework. This should follow the same approach as with TCFD, that is, an initial voluntary period then a phased mandatory approach beginning with premium listed companies. More broadly, non-financial disclosures will need to align more closely with the UK's environmental targets, such as those under the 25 Year Environment Plan and the Environment Act 2021. Increasingly, companies and investors are recognising that a prosperous business relies upon nature and the ecosystem services it provides. Like with climate, nature-related risk must be factored into investment and lending decisions.

- In the update to the Green Finance Strategy 2023, the UK Government signalled its intention to integrate the UK Green Taxonomy into non-financial reporting

requirements – initially voluntarily for at least two reporting years. As noted by the Green Technical Advisory Group, requiring companies to disclose what proportion of activities are taxonomy-aligned will help provide greater clarity and consistency for investors and provide a reference point for companies. To avoid placing undue reporting burdens on companies, the government should provide a clearer timeline on when it expects to mandate taxonomy-aligned reporting. This will not only enable businesses more time to prepare to meet requirements, but will ensure the UK does not fall behind the pace of other jurisdictions (such as the EU) which are increasingly influencing the development of taxonomies globally.

- In the future, greater mandating of scope 3 emissions within disclosures will be required, as the voluntary requirements under the Streamlines Energy and Carbon Reporting (SECR) is not sufficient. For many businesses, value chain emissions account for more than 70% of their carbon footprint meaning, without this information, investors will not be able to properly assess risk. To avoid overdue reporting burden, scope 3 emissions reporting should be made mandatory once common data sharing platforms that automate SME sustainability reporting on a national scale (such as *Project Perseus*) have been suitably developed and piloted.

- The UK Government should provide greater clarity over its approach to introducing assurance requirements for certain companies. Assurance requirements will help to provide greater confidence among investors and will stimulate investment. A 2021 PwC global investor survey, for example, found that 80% of investors indicated that their trust in reported sustainability information increased if it has been assured. To avoid undue costs, the UK should align itself internationally with the SEC's climate disclosure proposals and the CSRD, by introducing mandatory assurance requirements by an accredited independent audit/certifier over time, beginning with a 'limited assurance' requirement before progressing to 'reasonable assurance' requirement.

How should the standards being prepared by the International Sustainability Standards board (ISSB) be incorporated into the UK's non-financial reporting framework?

As mentioned above, the fragmented sustainability reporting landscape globally creates significant complexity and costs for UK companies operating in other jurisdictions and multinational companies bridging both.

A global baseline approach, such as the ISSB, will help to create a level-playing field for companies and market participants across jurisdictions. This will not only minimise costs for companies operating internationally by simplifying the reporting process, but will provide investors with globally comparable sustainability-related information – facilitating international investment and trade opportunities. Ensuring the UK is an early mover to align

with the ISSB framework will ensure UK businesses are the most competitive globally and will steer other economies in that direction of travel also.

In line with the recommendations of the Independent Review of Net Zero, the UK Government should endorse and implement the ISSB standards (S1 and S2) as soon as possible without any major deviation. Companies in scope should be encouraged to apply the ISSB's standards voluntarily in 2023/4 and then on a mandatory basis from the 2024/5 sustainability reporting cycle onwards. This should follow the same approach as with TCFD, that is, an initial voluntary period then a phased mandatory approach beginning with premium listed companies before extender to wider parts of the economy. This staged-approach can be fairly quick, as the ISSB standards build upon the four pillars that make up the TCFD's core content components so should companies in scope of TCFD should be familiar already.

info@aldersgategroup.org.uk www.aldersgategroup.org.uk