# Towards Sustainable Businesses: Good Practices in Business Model, Risks and Opportunities Reporting in the EU

SUMMARY

**100+** STAKEHOLDERS ENGAGED WITH THROUGH SURVEYS, INTERVIEWS, WEBINAR EVENTS

**44** COMPANIES REVIEWED

**19** PROJECT TASK FORCE MEMBERS

**12** MONTHS VIRTUAL COLLABORATION

European Reporting Lab @EFRAG

## Key highlights at a glance

- Focus on reporting of sustainability risks and opportunities and the linkage to the business model
- A collaborative effort of 19 experts with preparers, users, and other key stakeholders in the task force
- Findings are presented in a main report and supplementary document with examples of good reporting practices
- Draws on insights from the stakeholder outreach to illuminate on the drivers of current reporting practices
- Explores the application of technological solution in reporting of sustainability information
- Charts a path to improvements and provides tips (do's and don'ts) for sustainability reporting

### Main Report

- Highlights the state of play findings based on the review of a sample of EU companies and corroborated by outreach to stakeholders
- Develops a Practices Evaluation Approach to aid the review and selection of good reporting practices

### Supplementary Document

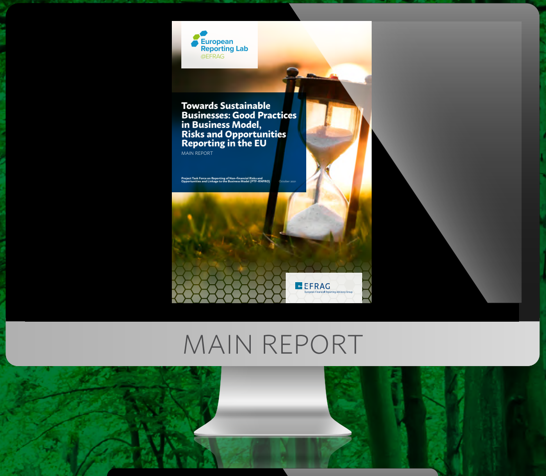
- Shares 37 examples of good or leading practices extracted from 27 companies- with reasons why these are good practices and suggestions for improvement
- Enables electronic navigation/ interactive access to the examples of good reporting practices

## OUTCOMES

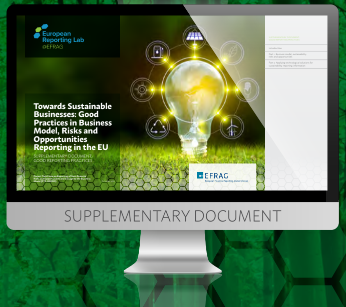
**37** GOOD REPORTING PRACTICE EXAMPLES

**27** COMPANIES HIGHLIGHTED

**7** PATH TO IMPROVEMENT STEPS




MAIN REPORT




SUPPLEMENTARY DOCUMENT

EFRAG
European Financial Reporting Advisory Group

## Overview – what and how?

| Mandate and scope | PTF-RNFRO evaluation of reporting practices | Outcomes |
|---|---|---|
| • Focus on sustainability risks and opportunities linkage to business model<br>• Identify good or leading reporting practices<br>• Review state of play of reporting practices<br>• Assess use of technological solutions in reporting sustainability information | • PTF-RNFRO member expert perspective<br>• Review of reporting practices (**sample of 44 EU companies**)<br>• Applying Practices Evaluation Approach to assess reporting practices<br>• Outreach to stakeholders (survey, interviews and two webinar events) | • Key reporting challenges identified<br>• Proposed path to improvement steps and reporting tips<br>• **37 examples of good or leading practices from 27 companies** |

## Overview – why and who?

| Objective | Audience |
|---|---|
| • Enhanced reporting is an important component of the EU Sustainable Finance policy objective<br>• Examples can enable companies to benchmark themselves and improve their reporting practices | • Preparers<br>• Users (investors and analysts)<br>• Other reporting stakeholders<br>• Sustainability reporting guidance providers |

# Key findings – challenges of sustainability reporting

Set out below is a summary of the key findings on the challenges of sustainability reporting observed from our review of the sample companies and outreach feedback.

## Quality of disclosures

### *Business model – performance and viability reporting*

- **Reporting on the business model is not holistically developed** and lacks sufficient information to allow for linkage to sustainability risks and opportunities over relevant timeframes, necessary for users to assess the long-term viability of business models. There are front-runners in this space, however, even leaders do not show a high level of sophistication on all aspects of reporting on their business model.
- **Value creating aspects of the business model have not found their way into corporate reporting**, although it remains at an early-stage development, where the focus remains on qualitative and descriptive disclosures. In terms of financially material information, current disclosure practices often fail to provide content that can be used by capital providers to predict the future performance of the business. There was little evidence from the reviewed companies that sustainability-related intangibles are considered to be major drivers of value creation.
- **Destruction of value, such as may be caused by underestimation of environmental or social risks and/or inaction was also found to be inadequately developed and discussed in disclosures**. New methods of “value” and “impact” assessment are more inclusive of risks related to social and governance issues, and it remains difficult to relate the “direct” and “indirect” impacts of decisions on either the company or its stakeholders. We also note that even among the identified good reporting examples, opportunities are sometimes only presented as a way to mitigate value destruction.
- **Disclosures were sometimes found to lack a balanced perspective** and sometimes only portray positive impacts. Stakeholders expressed a need for a better balance between the reporting of positive and negative impacts and dependencies.

### *Sustainability risks, opportunities and linkage to performance, strategy*

- **Sustainability risks are disclosed in various locations across corporate reports and lack coherence**. Current general practices lack a structured approach where risks are clearly linked to the business model. For example, companies rarely explain if, and how, their business model and strategy are resilient to environmental and social risks.
- **Sustainability opportunities are disclosed as part of material themes identified in sustainability reporting**. Accordingly, opportunities are often difficult to define with respect to risks and their connection to the business model.

- Generally, the PTF-RNFRO identified **less mature reporting of sustainability opportunities compared to sustainability risks, possibly suggesting that sustainability is perceived as a restraint on the business rather than an opportunity** for growth and development of the business. Stakeholder feedback shows an increasing recognition that sustainability is a relevant and necessary component of business models, but the leap is still to be made by some to move from construing it as a cost or risk rather than as an opportunity that brings potential new areas of growth.

- Although a majority of respondents to the PTF-RNFRO survey considered the application of the EU Taxonomy to investments as an opportunity to review/enhance their business models, only a **few of the reviewed companies report on their current alignment with the EU Taxonomy** or describe a future plan for its implementation.

- **A quantification of sustainability risks and opportunities is rarely disclosed**, even though it is essential for the evaluation and decision-making process of the business model. This finding is consistent with the conclusions of the PTF-CRR report.

- Disclosures on sustainability risks and opportunities have **limited utility for users (investors and analysts) due to inadequate disclosure on the future cash flow implications of achieving sustainability targets and strategy**. Inadequate disclosures can mask how an entity's future cash flows are affected by changes to the business model, either positively or negatively.

- The link between **sustainability strategies and companies' financial objectives is quite limited**. Many companies tend to only report through a general qualitative statement or objectives associating their strategy with the Sustainability Development Goals of the United Nations General Assembly (SDGs), and a few report other factors such as adding value to specific stakeholders.

Furthermore, the stakeholder outreach highlighted that some of the trends observed in practice are driven by nuanced factors such as data availability bias, potential liabilities and litigation risk, different perspectives on risks and opportunities by teams within companies working in isolation (i.e., in siloes) and the considerable challenge to distinguish a trend from an opportunity or risk.

## Other key findings on sustainability reporting practices

### *Application of standards*

- **Use of a variety of existing standards, guidance and frameworks was observed**. Stakeholders including preparers and investors told us that they currently struggle with reporting requirements because of the vast array of voluntary frameworks, standards, and other guidance. In addition, the existing reporting requirements do not sufficiently articulate the disclosure objective that drives the reporting of sustainability information.

- This finding aligns with the European Lab Project Task Force for the elaboration of Non-Financial Reporting Standards report (PTF-NFRS report) conclusion 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.

- **Definitions differ and there is a varied use of terms across existing reporting standards, guidance and frameworks** which leads to ambiguity in how those terms are used in reports.

### *Application of technology*

- There is an **insufficient deployment of possible technological solutions** (e.g., structured data, AI and other technologies) to report sustainability information by the reviewed sample of companies.
- Due to companies being at the early stages of applying technological solutions for reporting sustainability information, we were only able to identify a few leading practices.
- Data technology has the potential to play a significant role in minimising the reporting burden such as managing data collection, dissemination, and verification, applying science-based targets, and enhancing and enabling the qualitative characteristics that define good disclosures. Relatedly, the PTF-NFRS report noted 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 to information by stakeholders. It recommended that to facilitate digitisation, the EU standard-setter should translate the architecture's classification and segmentation of sustainability disclosures into a digital taxonomy from the outset.

### *Credibility of information (targets and assurance)*

- **Absence or patchy application of science-based targets** when reporting on sustainability outcomes and impacts was a key issue identified. Standardisation of sector-specific definitions and metrics is needed in order to measure the degree of sustainability of activities and to steer actions and finance towards a sustainable economy.
- **Inconsistent use of third-party assurance on non-financial information**. Assurance is necessary to provide confidence to users that the corporate reporting process and controls produce information that is reliable, accurate and complete and the appropriate principles as specified by the selected reporting standards, guidance and frameworks have been properly applied. It was observed that there are large differences in the scope of assurance and application of assurance standards. Furthermore, the wording of the assurance report varied significantly across assurance providers. During the stakeholder-outreach interviews, assurance providers underlined the need to standardise the criteria of the assurance process for all sustainability matters.

## Path to improvement

Based on the key findings, it is the view of the PTF-RNFRO that there is considerable scope for improving the quality and usefulness of reporting on sustainability risks and opportunities and their linkage to the business model. We present what we consider to be needed steps in the path to improvement, specifically:

- a **clearer** description of the business model and **linkage** to sustainability risks and opportunities;
- more emphasis on **reporting opportunities**;
- **quantification** of risks and opportunities and **cash flow generation**;
- better **connectivity of financial and sustainability information**;
- application of **evidence-based** and science-based targets;
- optimising the **use of available technologies**; and
- attaining credibility through third-party **assurance**.

Inspired by the feedback from outreach to stakeholders, **we also suggest sustainability reporting tips that companies can consider (i.e., do's and don'ts)**. These proposed steps and tips only represent the PTF-RNFRO views on how reporting practices relating to sustainability risks, opportunities and the business model can be improved, and these should not be construed as guidance.

# Learnings from the identified good reporting practices

The identified good practices are detailed in the *Supplementary Document: Good reporting practices*. In the Table below, we summarise a selection of the key positive features of the good or leading practices as well as aspects of reporting that could be improved more broadly. We recognise that not all good or leading reporting practices that have been identified are relevant for all preparers and users, since they may be only applicable to specific industries or sectors and relevance changes over time.

We furthermore recognise that our study did not capture all companies that report using good or leading practices.

*Table 1: Learnings from the identified good or leading practices*

| Analytical considerations | Positive features of good or leading practices | What could be better |
|---|---|---|
| **Business model reporting** | | |
| Clarity and comprehensiveness of overall business model disclosure (i.e., value creation model) | • Concise and sufficient description of the business model's inputs, business activities, outputs, and impacts made with disaggregation by ESG categories.<br>• Effective visual representation of the business model.<br>• Distinguish between direct and indirect upstream and downstream inputs and outputs.<br>• Have a connectivity table and additional contextualising information that shows how material sustainability topics affect different business segments.<br>• Leverage technology (e.g., website interactivity features) to provide readers easy access to comprehensive business model-related information. | • Some companies only provide partial business model related information and miss out on key elements (e.g., do not provide sufficient information on impacts, business activities).<br>• There remains a need for disclosure that conveys the resilience of business models (i.e., going beyond only presenting a static view of the business model). |
| Disclosure of potential across time horizons | • A clear definition of short-, medium- and long-term horizons and goals related to these horizons.<br>• Provide scenario analysis information with a definition of short, medium, and long term and the effects of carbon pricing on the value of the asset portfolio.<br>• There is a clear alignment between the company's disclosed business planning timeframes and policy goals timelines. | • Some of the disclosures only provide broad sectoral information of risks and opportunities across different timeframes and not company-specific information.<br>• Some companies do not define what short, medium and long term means for them. |

| Analytical considerations | Positive features of good or leading practices | What could be better |
|---|---|---|
| Disclosure of dependencies and impacts | • Reader-friendly graphic presentation of the monetised impact for each of the six Integrated Reporting (IR) capital stakeholders showing positive or negative impact per IR capital category, and thereafter the net positive impact.<br>• Transparent on the methodology applied for the determination of impacts.<br>• Visually outline both positive and negative impacts on different stakeholders with a distinction by the six IR capitals. An explanatory note of how the visual depictions translate to monetary equivalents is provided. Highlight the impact on SDGs.<br>• Are transparent about what went wrong. | • In many cases, the description of impacts including links to SDGs is only done by generic statements.<br>• Some companies could better outline positive and negative impacts.<br>• For some companies, there is a need for a greater degree of quantification of impacts (i.e., going beyond only diagrammatic representations and a qualitative description of impacts).<br>• Companies are generally not ranking or signalling what their top impacts and dependencies (resources and relationships) are. |
| **Sustainability matters linkage to business model, strategy** | | |
| Disclosure of material sustainability matters that are likely to affect company performance | • Provide a clear link between identified Top 10 risks and opportunities and the company KPIs.<br>• Have a connectivity table matrix that shows the interrelationship between sustainability issues and KPIs.<br>• Provide information on an available lending facility whose margin depends on fulfilling emission targets and this shows how impacts on the environment can translate to material financial information. | • Some companies have an insufficient quantification of the effect of sustainability matters on company performance and KPIs.<br>• It being hard to link identified sustainability matter to performance KPIs due to fragmentary reporting and in the absence of a connectivity map. |
| Disclosure of sustainability risks | • Provide a succinct summary of different categories of sustainability risk exposure and risk mitigation measures.<br>• Disclose the level of risk across the value chain including that faced by suppliers and contractors. Quantifies sustainability risk exposures in terms of impact on financial performance.<br>• There is connectivity between financial and sustainability information with a clear link between the information in the annual report and the sustainability report. | • Some companies only qualitatively describe their risk exposure.<br>• Some companies could better show the possible effect of sustainability risks on financial performance.<br>• There is a need to disclose how sustainability risk exposures may affect the company's financial position (i.e., the resilience of balance sheets). |

| Analytical considerations | Positive features of good or leading practices | What could be better |
| --- | --- | --- |
| Disclosure of sustainability opportunities | • Quantifies opportunities at a macro-level.<br>• Are specific on revenue potential (e.g., percentage of green revenues), and the opportunities related to different products and business segments. | • Some companies only qualitatively describe their opportunities.<br>• Some companies could better show the possible effect of sustainability risks on financial performance.<br>• The companies could highlight opportunities across short-, medium- and long-term timeframes.<br>• Some companies only describe opportunities in non-monetary units and for these companies, it would also be helpful to have monetised information.<br>• Information on business segmental or product level opportunities would be insightful.<br>• Reporting on circular economy and other sustainability opportunities tend to be less mature than reporting on climate-related opportunities. |
| Disclosure of sustainability strategy, targets, KPIs, and progress | • Describe how the company's business model is linked to SDG targets.<br>• Link external macroeconomic environment, strategic sustainability issue and ambitions/ targets.<br>• Identify and rank material issues and link these to targets and KPIs.<br>• Succinct presentation of economic value creation and sustainability topics KPIs with multi-year comparatives and also highlights research and development spend on sustainable innovations.<br>• Provide a triple bottom line (financial and non-financial bottom line) presentation.<br>• Provide detailed KPIs for different sustainability topics on a multi-year basis. | • Some companies do not sufficiently outline monetised effects in their presentation of KPIs.<br>• Targets and commitments are often described using generic language. |

# Identified good reporting practices

*Table 2: Summary of good reporting practice examples*

| Analytical considerations | Good or leading reporting practice examples |
|---|---|
| **Business model reporting** | |
| Business model reporting: clarity and comprehensiveness of value creation description | • Neste (Energy)<br>• Stora Enso (Forest products and paper)<br>• Schneider (Electronic component and equipment)<br>• FMO (Development banking) |
| Business model reporting: potential across time horizons | • Allianz (Insurance)<br>• Schneider Electric (Electronic component and equipment)<br>• Orsted (Energy) |
| Business model reporting: dependencies and impacts | • SGS (Business support services)<br>• EnBW (Electric and gas utilities)<br>• ABN Amro (Diversified banking)<br>• DSM (Chemicals) |
| **Reporting sustainability matters linkage to business model, strategy** | |
| Sustainability matters effects on company performance | • EnBW (Electric and gas utilities)<br>• Arcadis (Consulting engineering and construction)<br>• ABN Amro (Diversified banking)<br>• SGS (Business support services)<br>• Norsk Hydro (Aluminium and renewable energy) |

| Analytical considerations | Good or leading reporting practice examples |
|---|---|
| Sustainability risks | • Enel (Energy)<br>• Schneider (Electronic component and equipment)<br>• AB Volvo (Automotive)<br>• Novozymes (Pharmaceutical and biotechnology)<br>• BNP Paribas (Diversified banking) |
| Sustainability opportunities | • Enel (Energy)<br>• Schneider (Electronic component and equipment)<br>• CH Hansen (Bioscience)<br>• Acciona (Energy and infrastructure)<br>• Signify (Industrial products-electrical equipment) |
| Sustainability strategy, targets, KPIs, and progress | • Acciona (Energy and infrastructure)<br>• Peugeot (Automotive)<br>• Lenzing (Chemicals)<br>• GlaxoSmithKline-GSK (Pharmaceutical) |
| **Application of technological solutions for reporting sustainability information** | |
| Possible technological solutions (structured data, multimedia and interactive technologies, satellite imagery, artificial intelligence-AI, blockchain and data management systems) | • Unilever (Consumer goods) application of AI for materiality analysis<br>• Ferguson plc application of interactive website<br>• Novartis (Pharmaceuticals) use of video<br>• Stellantis (Automotive) use of satellite imagery<br>• Unilever (Consumer goods) application of AI<br>• Lenzing (Chemicals) use of blockchain technologies<br>• Hotchief use of structured data (ESEF/iXBRL) to block tag management report |

** the listing of companies within each category of Table 2 does not indicate a ranking in reporting quality. It is the order of their presentation in the Supplementary Document: Good reporting practices*

## Disclaimer

The European Lab Project Task Force on Reporting of non-financial risks and opportunities and linkage to the business model (PTF-RNFRO) published its report (*Towards Sustainable Business: Good Practices in Business Model, Risks and Opportunities Reporting in the EU*) and supplement (*Supplementary Document: Good reporting practices*) (herein collectively referred to as the PTF-RNFRO report). This summary to the PTF-RNFRO report has been prepared by and is the sole responsibility of the PTF-RNFRO.

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## Feedback on the PTF-RNFRO report

Any feedback on the PTF-RNFRO report can be submitted to EuropeanLab@efrag.org.