esgbook

Beyond The Acroynm*

*A Guide on Navigating Global Sustainability Standards and Frameworks.

by Isabel Verkes

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"About 92% of the S&P 500 companies published a sustainability report in 2020, up from 90% in 2019. In 2020 disclosures, about 39% of Russell 1000 companies align with the SASB standards."

Source: GA Institute 2021 Research.

Investors are eager to incorporate environmental, social, and governance - ESG - considerations in their investment strategies, even outside of what is explicitly framed as "sustainable investing". In this blog, we explain how sustainability standards and frameworks are contributing to this trend; how they are ensuring a clearer rationale on sustainability in finance, and finally, where reporting guidance is headed towards.

The rise of sustainable investments has led to the burgeoning growth of sustainability standards, and frameworks for disclosure of investor critical ESG information. Among other things, Standards and Frameworks are helping companies and investors measure and disclose sustainability-related performance and make well-informed decisions while factoring in different emerging risks. In addition, they allow comparability over time, across sectors/industries, and in between peers or potentially with any company(s) operating anywhere in the world.

The emergence of various standards, frameworks, and different standard setters encouraging a wide range of disclosures has certainly created confusion regarding their usage and raise questions as to the credibility of ESG criteria/assessments in general. And more importantly, how do the investors perceive and respond to these disclosures (if, at all)?

The corporate sustainability reporting landscape has several players, including a host of sustainability standards and frameworks to guide reporting of companies' non-financial or sustainability performance over time. However, within this space alone, standards and frameworks are often used synonymously and interchangeably. They are in fact quite different, each of them catering to some specific demands of an Annual, Sustainability, or Integrated Report: showing how an organization's strategy, governance, performance, and prospects, in the context of its external environment, lead to the creation of value in the short, medium, and long term.

What makes standards and frameworks different?

Standards **Frameworks**

Standards and frameworks must be defined in relation to each other, in order to understand their role more precisely. For instance, the role of a sustainability standard as distinct from a sustainability framework should be clearly laid out including the process where and how they can be used together by any reporting entity.

Sustainability Standards are specific, detailed, and replicable requirements for what should be reported under different topics relevant to a particular company/industry/sector, including the applicable accounting metrics and technical protocol for compiling the data.

- Sustainability standards answer the questions like:
- What data is expected to be useful sustainability information?
- What information is most important to investors and other key stakeholders?
- What ESG indicators are financially material for the respective industry?

Standards spell out what companies should report, including the technicalities of data collection.

Some of the widely used standards today are those promoted by GRI (Global Reporting Initiative of Global Sustainability Standards Board) and The Value Reporting Foundation (overseeing the SASB Standards).[1]

The GRI standards are primarily popular among European companies. In 2020, around 54% of EU companies use GRI standards for their non-financial reporting requirements[2]. The GRI sets its sustainability indicators as industry-agnostic. SASB on other hand has industry-specific indicators for seventy-seven different industries and is mostly used by American companies. Different ESG topics weigh differently for different industries. Capturing the most material or vital information requires common sustainability "reporting scorecards" tailored for each industry, which is what SASB advocates through its standards.

However, both GRI (Global Reporting Initiative) and SASB (Sustainability Accounting Standards Board) standards are used by companies worldwide to measure and report their performances on various ESG related indicators. Some of the other standards which provide disclosure-related metrics are set by organizations such as the International Finance Corporation, the World Intellectual Capital/Assets Initiative, the United Nations Conference on Trade and Development, and the World Economic Forum.

Standards provide specific, detailed, and replicable requirements for what should be reported for each topic, including metrics. Standards define necessary information requirements.

Sustainability Frameworks are a set of principles-based guidance for "how" different sustainability information are to be structured and prepared, and what broad topics are to be covered while reporting non-financial information.

In practice, Standards make Frameworks actionable

Frameworks set the conceptual groundwork for what standards set out as requirements. They help structure and shape complex and scattered information into a final comprehensive piece, producing standardized reports that are comparable over time.

Frameworks provide principles-based guidance on how to structure and report different information together; and what broad topics should essentially be covered. In short, frameworks provide general direction on composition of ESG related disclosures within annual/integrated/sustainability reports or any other investor critical ESG disclosure.

What does this mean for report preparers?

< IR Framework >	SASB Standards
Industry-agnostic	Industry-specific
Principles-based	Metrics-based
Preparation and presentation	Standards application guidance
High-level content elements	Disclosure topics and metrics
Drives connectivity of information	Enables comparability of information

The relationship between Standards and Frameworks and how they are complementary to each other

Source: SASB Standards

Interestingly, standards and frameworks are complementary. They are both used in the preparation of investor communications, such as sustainability reports, sustainability chapters within annual reports, or any other ESG-related disclosures.

However, new sustainability-related reporting regulations and policies are emerging in various jurisdictions. This, combined with a wide range of standards and frameworks, leads to indecision and skepticism among reporting preparers. Reporting on investor-driven voluntary standards and frameworks, together with all the mandatory regulatory submissions, is often cumbersome and can look like an overload of reporting tasks.

This backdrop is why different standard-setting organizations are looking to simplify their requirements and join efforts to educate preparers. Take the example of the <IR> (framework designer) and SASB (standard setter) to combine forces as "The Value Reporting Foundation". Another global standardization effort is the International Sustainability Standards Board (ISSB), created by the IFRS in 2021, seeking to develop a global baseline of sustainability-related disclosure standards to provide capital market participants with decision-useful sustainability-related information from companies.

How do companies benefit from using standards and frameworks?

- **Shareholders appreciate and ask for it.** Shareholders are increasingly expecting companies to disclose non-financial information. Standards and frameworks help in ensuring the reporting of non-financial information - both qualitative and quantitative - is consistent over time.

- **Easier to start and maintain reporting practices.** Standards imply that companies don't have to invent their own disclosure logic. Instead, companies can use standards and frameworks to pro-actively engage in stakeholder dialogues on the economic, environmental, and social impacts of their business.

- **Reputation management.** Frameworks and standards allow companies to communicate industry-specific material information regarding sustainability issues, rather than leaving those narratives to the press and financial analysts only. In practice, non-financial issues can lead to reputational damage – even if they are posing unmaterialized risks. Disclosure following standards or frameworks gives companies more control over discussions around their sustainability profile and helps avoid unexpected brand deterioration. With an increasing number of companies disclosing non-financial information in standardized forms, the companies with the lowest disclosure (or not following standards) stand out negatively and raise the question of why they do so.

- **Improve operations.** Internally, frameworks and standards are a potential tool for companies to see what stakeholders regard as relevant in their industry. In other words, standardized sustainability disclosure is a management tool to guide internal improvement and decision-making. It directs management's attention to those topics that are deemed most important to the applicable industry, as guided by independent standard-setting bodies. Ideally, this facilitates communication within and across different functions and departments around sustainability topics. Furthermore, frameworks and standards give management an idea of their competitive positioning. Companies can be compared on financial performance, as well as their carbon emissions relative to peers. Lastly, the Amazon walk-outs show how sustainability topics are a crucial element to HR and culture building. Standardized disclosure helps companies to move beyond a media-created image – and communicate with employees based on actual data. If measuring sustainability performance seems a daunting task, frameworks and standards make it easier to do so.

How do institutional investors benefit?

- **Investment research costs.** Different accounting requirements (of differing quality) add to the cost, complexity and risk of investment.

- **Risks and opportunities.** Assessing and addressing risks and opportunities by having a historical track record of companies' non-financial information. This leads to better capital allocation decisions.

- **Validated models for ESG-information.** SASB and other standard-setters offer investors a vetted model of which ESG-related metrics are financially material.

How do governments, regulators and policy-makers benefit?

Financial and economic stability. Better anticipate and address risks at macroeconomic level by government and regulatory bodies, including financial stability risks (idiosyncratic, sector, systemic).

Less regulatory cost and litigation burden. Leverage emergence of standards and frameworks to encourage and advocate voluntary disclosures which can regulate corporate behaviour, before embedding these market-driven rules into the legal system. This helps policymakers to understand how certain regulations/laws would be perceived by companies and affect the market (esp. capital markets) without immediately having the need to pass formal legislation for the entire ecosystem.

***Example – From 2011 to 2021, India encouraged and mandated several ESG disclosure requirements for top 100 and 500 listed entities, before incorporating SDGs and making it applicable to top 1000 listed entities by market capitalization in May 2021.*[3]**

How are they evolving?

Even after a momentous growth over the last few decades, and a strong investor push, the idea of standardized ESG reporting remains highly contested. This is to some extent, a result of a huge mismatch between the demand for and supply of ESG data required by investors, asset owners, data aggregators and then the ability of other players to provide the same.

Investors are getting increasingly sophisticated in anything sustainable finance. That gives and amplifies the importance of standards, although this has created more standards variants as there are more and more use cases and unique investor needs.

However, the push to consolidate various standards too is growing stronger, from markets, companies, standard setters and even policymakers. The five global standard setters, that guide most of the sustainability and integrated reporting globally, are working together towards comprehensive corporate reporting. This in turn would enable these standards and frameworks to operate more complementary to each other.

With the growing reliance on timely and actionable ESG data, the space continues to evolve with standards and frameworks tailored to specific industries. As the regulations, policies, ordinances, stock exchange listings/rules related to reporting are expanding, we will do our best to keep you updated in this space.

For more information, visit esgbook.com or sign-up to our newsletter to get our latest insights and regulatory updates delivered direct to your inbox.

Bibliography

1. SASB was founded as a nonprofit organization in 2011 to help businesses and investors develop a common language about the financial impacts of sustainability. prospects. Over the years, the corporate sustainability disclosure landscape has become very complex. Many global businesses and investors have been calling for simplification and clarity in this landscape. In response, in November 2020 the International Integrated Reporting Council (IIRC) and the Sustainability Accounting Standards Board (SASB) announced their intention to merge into the Value Reporting Foundation, which was officially formed in June 2021. By integrating two entities that are focused on enterprise value creation, the merger signaled significant progress towards simplification. The Value Reporting Foundation offers a comprehensive suite of resources—including Integrated Thinking Principles, the Integrated Reporting Framework, and SASB Standards— designed to help businesses and investors develop a shared understanding of enterprise value.

2. See our regulatory update; more detail from the GRI.

3. Report of the Committee on Business Responsibility Reporting - Ministry of Corporate Affairs, Government of India ; Securities and Exchange Board of India