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# European Directives and Principal International Frameworks for Corporate Sustainability and Climate Change Reporting: Responding to the Challenges Facing Our Planet

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**Abstract:** *Over the last few decades, significant progress has been made in the development of a global baseline for corporate sustainability reporting and disclosure, including a focus on climate change issues. However, the author's main concern, and the argument at the heart of the paper, is that the observed proliferation of frameworks focused on sustainability and sustainable development may compromise the comparability of disclosed information, thereby reducing its usefulness and even confusing stakeholders. The author argues that humanity urgently needs to do much more. Based on the author's research, observations and reflections from discussions with leading practitioners and experts, it is suggested that the transparency, consistency and relevance of corporate policies and activities and information on sustainability and climate-related issues, whether provided through voluntary or mandatory reporting and disclosure, are not of sufficient quality to adequately address and respond to the unique challenges facing humanity due to climate change.*

*Sustainability disclosure has become an important part of the corporate reporting process, with climate-related information being a key component. The author's thesis is that the trustworthiness, transparency and relevance of climate-related disclosures have proven to be of great importance in achieving disclosure effectiveness and usefulness for interested parties – potential and current investors, creditors, lenders, employees and all members of society and the European Union community. The author aims to highlight, discuss and justify the need for a global framework and coherent standards to support meaningful and consistent disclosure of climate-related matters, risks and opportunities. It will be a prerequisite for improving the transparency and quality of climate-related information and data and will support appropriate decision-making in the management of climate-related risks. The author considers it to be an essential part of the governance, process and system of corporate governance reporting.*

*The author's paper aims to highlight and discuss the considerations, criticisms and concerns of researchers, professionals and experts on the issues discussed, to outline perspectives for future research and to emphasize that benefits for all members of society, sustainability and sustainable development and the future are highly probable and can therefore be expected. The development of international standards for climate-related disclosure should be seen as the most important part of establishing a global regulatory framework for corporate sustainability reporting at the international level. The research methods used by the author are analysis and synthesis, induction and deduction, descriptive approach, comparison, analogy and observation, as well as a thorough study of many recent academic research and normative sources on the subject.*

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## 1. INTRODUCTION

Over several decades, the humanistic concepts of sustainability and sustainable development have been developed, legally adopted and endorsed by the most influential and respected international organizations such as the United Nations. Powerful social movements and other global events have emerged. Stakeholders have launched international and global initiatives, and dedicated scientists, environmentalists, ecologists and other committed researchers have brought the issue of corporate sustainability reporting to the forefront through in-depth scientific research. Climate change reporting and disclosure have become one of the cornerstones of sustainability reporting. The author does not use the terms 'sustainability' and 'sustainable development' synonymously or interchangeably. The author has considered and discussed the fine distinction between these terms in another study on the subject (Oreshkova, 2022a, 2023). The author believes that it is more appropriate to use the terms 'sustainability reporting and disclosure' or 'reporting and disclosure on sustainability issues' rather than 'non-financial reporting'. The author believes, as do other researchers in the field, that the term 'non-financial' is not the most appropriate because it implies a nuance of meaning that the information it refers to has no financial relevance or significance. Many organizations, initiatives across the world, and practitioners in the field of sustainability reporting refer to 'sustainability information' rather than 'non-financial information'. The author considers it preferable to use 'sustainability information' rather than 'non-financial information'. Directive 2013/34/EU, as amended by the Non-Financial Reporting Directive – 2014/95/EU, should have been amended to reflect this change in terminology. As a result, the new Corporate Sustainability Reporting Directive has been adopted. The author believes that reporting on climate change and climate-related issues, risks and opportunities is the most important part of sustainability reporting. For many companies operating in geographically distant regions of the world, sustainability reporting has evolved from a voluntary opportunity and option to a legal obligation. In particular, certain large companies are expected to contribute to the global response to climate change and mitigate its effects through transparent and relevant information and disclosure. Environmental, social and governance issues, and the risks and opportunities they present, have moved to the top of corporate governance strategies, tactics, and agendas. There is growing evidence that companies are increasingly embracing the concepts of sustainable development. It demonstrates and highlights perceptions, views and insights that the role of business activities undertaken in support of sustainability and sustainable development can be critical to achieving the strategic goal of the United Nations (and not just the goals of stakeholders interested in the relevance of financial indicators).

Combating climate change is one of the European Parliament's top priorities and a structural component of the strategy and long-term policy of the European Union institutions. The main objective of the United Nations Paris Agreement is to limit and mitigate the rise in global temperatures and to avoid a potential increase of 2 degrees Celsius (preferably 1.5 degrees, according to experts) compared to pre-industrial levels. The nature of the target implies that countries, governmental and non-governmental organizations and institutions, initiatives around the world, current and potential investors, creditors and lenders, and other stakeholders will increasingly be expected to play a key role in the transition to a low-carbon economy and sustainable growth. It is an undeniable fact that low-carbon technologies become increasingly competitive today (Oreshkova, 2022b). Large and publicly traded companies are required by EU law to publish regular reports on the social and environmental risks they face and how their activities affect people and the environment (European Commission, 2023a).

## 2. RESEARCHER CONSIDERATIONS, CRITICISMS AND CONCERNS

European Union legislation, in particular the Non-Financial Reporting Directive (NFRD), requires certain large companies operating in the European Union to provide information on key issues related to sustainability, sustainable development, and climate change. The NFRD was adopted and implemented in the Member States of the European Union to support the sustainability paradigm and the Sustainable Development Goals. EU policy and the NFRD represented a necessary shift towards a more robust regulatory regime and system. However, limitations and weaknesses remained. Researchers such as Tsagas and Villiers (2020) argue that *the NFRD has not achieved its objective of improving the relevance, consistency and comparability of information disclosed by large companies across the European Union because it remains very broad and generic in its approach*. In particular, based on a thorough analysis, the authors show that large companies' sustainability reporting practices are haphazard and arbitrary as they comply with different reporting initiatives and frameworks, making these practices "less rather than more transparent". By providing a comprehensive overview of existing reporting frameworks, Tsagas and Villiers (2020) highlight the global need for greater clarity in such a complex international landscape.

The results of the implementation of the NFRD in the European Union have also been the subject of discussion, analysis and criticism by other authors. The impacts and effects are analyzed by Aureli et al. (2020) in light of the economic, social, societal, governmental and other dominant factors that characterize each of the countries studied. *The in-depth analysis reveals evidence of divergence and discrepancies, catalyzed by differences in the national economic systems of each country. Practices and reporting vary between countries and companies*. The authors argue that accounting studies using institutional theory show that even where there is coercive pressure to converge, local practices and domestic traditions are other types of pressure that play a key role in maintaining divergence. Similarly, legal studies show that attempts at harmonization by the institutions of the European Union are usually challenged by member state authorities seeking to maintain the status quo of the local context, and this may be true of CSR reporting harmonization. The findings of other researchers, Jamali and Neville (2011), argue that local and indigenous historical, cultural, economic and political factors influence and shape the profile of corporate social responsibility (CSR) conceptualization that exists in a given country, and that convergence of different CSR practices is only apparent.

## 3. THE NEW EU DIRECTIVE ON CORPORATE SUSTAINABILITY REPORTING

European Union (EU) policy responds to climate change in many ways. Tackling climate change is a priority for the European Parliament. The EU has committed itself to a series of targets to reduce greenhouse gas emissions. Global average temperatures have risen significantly since the Industrial Revolution and the last decade, from 2011 to 2020, was the warmest on record, causing concern among scientists, environmentalists and ecologists. The European Commission's 2001 Green Paper "Promoting a European Framework for Corporate Social Responsibility" was the cornerstone of the European Union's policy on corporate social responsibility. However, it was not until the Non-Financial Reporting Directive 2014/95/EU that the regulatory framework for CSR reporting was consolidated.

The new EU Directive on corporate sustainability reporting came into force on 5 January. The Directive introduces detailed reporting requirements and ensures that large companies are obliged to disclose information on sustainability issues such as environmental rights, social rights, human rights, and governance factors. The CSRD also introduces a certification requirement for sustainability reporting (European Council, 2022) and improves the accessibility of information by requiring it to be published in a separate section of the company's annual report. The aim of the EU institutions, the Parliament, the Council, and the Commission, is to modernize and promote the rules on the production and provision of information on social, environmental and climate change issues using the instruments of EU law. The CSRD is designed and developed to ensure that stakeholders such as investors and other interested parties have access to the information necessary to assess the financial risks arising from social, environmental and climate change issues. A wider range of companies and listed small and medium-sized enterprises will be required to provide sustainability information. All large companies and all listed companies, except listed micro-enterprises, will be required to disclose information on social and environmental issues, risks and opportunities that they consider relevant and material, and on the impacts of their activities on people and the environment. It is expected that the European Green Deal will help current and potential investors, creditors and other lenders, civil society organizations and representatives, customers and other stakeholders to better assess the sustainability performance of companies.

The first reporting companies affected by the adoption of the CSRD in the European Union will have to apply the new rules for the first time in the financial year 2024, for annual reports published in the financial year 2025. The European Sustainability Reporting Standards (ESRS) developed by the European Financial Reporting Advisory Group (EFRAG) will apply to companies subject to the CSRD. On 6 June 2023, the Commission launched a public feedback period on the first set of sustainability reporting standards for companies, taking into account EFRAG's technical advice of November 2022 (European Commission, 2023b). There is considerable evidence and broad consensus that the sustainability information currently provided by companies is insufficient, inadequate, or inappropriate. Based on the author's research, literature review and observations of relevant practice, the author argues that the difficulties and complications in practice are mainly caused by the following reasons:

- ***Non-disclosure, formal and artificial disclosure, or incomplete disclosure****, whether intentional or unintentional, of information that may be material (significant) from the perspective of investors and other stakeholders in the decision-making process;*
- ***Disclosure of information on an inconsistent basis****, which in turn makes it difficult for stakeholders to compare information from period to period, company to company, or industry to industry and to understand trends;*
- ***Uncertainty and even confusion among investors, company employees, and other stakeholders*** *about whether and to what extent disclosed information can be trusted and relied upon to objectively assess the value of the company;*[2]
- ***Many of the frameworks have different focuses as they are designed for different audiences and use different metrics****, which is where much of the confusion comes from;*
- *The organization, structuring, and presentation of financial and sustainability information, whether intentionally or unintentionally, in a way that* ***obscures or renders unclear, vague, or inexplicable the material relationships between financial and sustainability performance indicators****;*

[2] The ISSB has issued proposals to create a comprehensive global baseline for sustainability disclosures by 31 March 2022. Additional information states that "enterprise value is the total value of a company – the market value of its equity and its net debt. The information that could be relevant to the assessment of enterprise value is broader than the information reported in the financial statements. It includes information about a company's impacts and dependencies on people, the Planet and the economy when [it is] relevant to the assessment of the company's enterprise value", IFRS Foundation (2022).

- ***Incoherence between inside and outside information****, lack of obvious connection between information inside and outside the financial statements;*
- *The climate-related information provided in the financial statements is sometimes too* ***high level and inadequate, with many shortcomings identified****;*
- ***The multiplicity of frameworks primarily affects practitioners****, as it introduces complications and difficulties and is of great concern to those who are genuinely committed to the sustainability reporting process;*
- *Due to any or all of the above,* ***the quality and/or quantity of disclosed information on the material (significant) environmental, social, governance, and other related issues is insufficient, inadequate, or unsatisfactory****.*

It is fair to say that the proliferation of corporate sustainability reporting frameworks around the world is flourishing. The global need for greater coordination of international efforts at a higher level, and the very diverse and varied global landscape, can mean that sustainability reporting tends to become a major barrier to sustainable corporate behaviour and policies, leading to a lack of real incentives for high corporate governance to act more sustainably. Madelyn Antoncic CEO of the Sustainability Accounting Standards Board (SASB) Foundation expressed a similar concern. "When one considers the overall universe of sustainability information that could be relevant for all corporate stakeholders, it can seem overwhelming," Antoncic suggested. This view is echoed by David Parham, SASB's director of research, who is concerned about the proliferation of standards, which Parham says can be a problem for people in all parts of the sustainability community. For the reporter, Parham says, it can mean at best recalculation and at worst the collection of completely different underlying data, depending on the requirements of each framework. "For the user, unless it is apparent that the data has been calculated on a different basis and the underlying methodologies are clearly and transparently articulated, this can make it difficult to compare, and therefore, to make decisions regarding variable performance on a given factor" (Parham, quoted by Gaetano, 2019).

*Importantly, many of the frameworks look at different metrics for different audiences*. Renee Mikalopas-Cassidy provides evidence and highlights some indicative facts – the Carbon Disclosure Project focuses on a single area, while the International Integrated Reporting Council (IIRC) focuses on a broader range of issues. The Global Reporting Initiative follows a public good model, while the SASB, originally designed for US investors, focuses on the company itself. It was specifically designed to be relevant to the needs of American investors, which can prove problematic when trying to align SASB standards with global partners. Each framework reflects the specificity of the context in which it was developed. The apparent differences can make it difficult to conclude definitively whether a company is sustainable, although Mikalopas-Cassidy says that such a binary approach is unrealistic anyway. An initiative like the Better Alignment Project "works to some extent", says Georg Kell, director of the United Nations Global Compact, which promotes the UN's Sustainable Development Goals (SDG) framework. Despite the project's good intentions, there is a limit to how fully these frameworks can be aligned, concludes Kell, chair of Arabesque, and he is skeptical that there will be any real alignment in the immediate future. However, he does not necessarily see this as a cause for great concern, as he acknowledges the inconvenience of having to wade through all the frameworks; ultimately, Kell sees it as many roads to one destination. As Kell admitted, he is not inclined to define the lack of harmony as a major problem because all frameworks have the same goal and many, many ways to get there. Michael Kraten, a member of the Sustainability Investment Leadership Council, is similarly optimistic but with a different motive. The Council was established to provide insight into how accountants and lawyers can incorporate sustainability practices that align economic opportunities with sustainable policies. While there are many different sustainability frameworks, the market has started to develop its own big four – the GRI, the SASB, the UN's SDG and the IIRC. Unlike Kell, Kraten believes that these four can work very well together, noting that they produce complementary standards (Gaetano, 2019).

Climate change reporting and disclosure, which the author considers to be the most important part of sustainability reporting, has evolved significantly over the past year. The International Sustainability Standards Board (ISSB) of the International Financial Reporting Standards (IFRS) Foundation (in London), which aims to provide a global baseline for climate-related financial disclosures, has been consulting on its standard-setting priorities and Exposure Drafts (the ISSB EDs) for endorsement by various jurisdictions. In the European Union, the European Financial Reporting Advisory Group consulted on its European Sustainability Reporting Standards Exposure Drafts (the ESRS EDs), which incorporate the reporting requirements of the Corporate Sustainability Reporting Directive (CSRD). At a regional level, overseas, the US Securities and Exchange Commission (SEC) consulted on its proposed rule on mandatory climate change reporting for SEC registrants. As noted above, there are hundreds of frameworks focusing on sustainability and sustainable development issues, with each organization claiming to be motivated by the humane cause and mission to save people and the Planet. It seems that organizations, economies and regions are struggling to compete and dominate in the global race to achieve this goal, but each is motivated by its specific interests and pursues its particular objectives.

The proliferation of frameworks is a real cause for concern. Rather than providing guidance and real support as intended, the proliferation of frameworks tends to become a prerequisite for compromising or significantly reducing the comparability and usefulness of disclosed information. Hoogervorst, the former chair of the International Accounting Standards Board, has acknowledged this fact (London, 2019), highlighting that there are now at least 230 initiatives for corporate sustainability standards across more than 80 sectors. "There are simply too many standards and initiatives in the area of sustainability reporting," Hoogervorst (2019) warned, citing a telling example: "Tesla is the top-ranked company in [investment research firm] MSCI's sustainability index, while [the Financial Times Stock Exchange 100 Index] ranks it as the world's worst carmaker on ESG issues. Another agency puts it somewhere in the middle."

Due to identified problems with the quality and/or quantity of information in sustainability reporting and disclosure, investors and other stakeholders do not have a reliable picture of the sustainability risks faced by companies. Companies' impacts on people and the environment and their plans to reduce these impacts in the future, should increasingly be known to all stakeholders. The significantly improved quality of information would better support stakeholders in meeting their specific disclosure requirements under the Sustainable Finance Disclosure Regulation (SFDR). Stakeholders and investors in particular need relevant, consistent and comparable information on the sustainability impacts of the companies in which they invest, as the green investment market cannot be credible without such information. Companies' impacts on people and the environment, and their strategies to reduce these impacts in the future, should increasingly be known to all stakeholders.

Mackintosh, a former chair of the CRD and vice-chair of the IASB, acknowledges that the TCFD has been quite successful over the years and points out that a study of participants' frameworks against the TCFD recommendations was undertaken because the Task Force has gained a lot of traction and many companies are interested in using the recommended metrics in their corporate reporting. The TCFD (2017) framework is based on four pillars:

- ***Governance*** *on climate-related risks and opportunities, board oversight and management's role in assessing and managing such risks for both investors and companies;*
- ***Strategy****, on the risks and opportunities posed by climate change, the implications for asset allocation and the processes investors use to assess performance;*
- ***Risk Management*** *on the processes investors use to measure, monitor and manage climate-related risks; and*
- ***Metrics and targets****, on the measures investors use to manage their climate-related risks and opportunities.*

Although significant international and global efforts have been made in recent decades, important issues remain to be addressed in the future. The author's research and a thorough review of EFRAG's recent publications on the topic central to this paper identify common problems (lack of consistency and transparency, lack of clarity about the links between information within and outside the financial statements, and others) encountered in practice that need to be addressed (EFRAG, 2023a).

- *In some cases, companies disclose climate-related risks in the front section (part) of the financial statements without any quantitative disclosure*[3];
- *Management reports and sustainability reports include disclosed information on commitments and investments that are not reflected in the financial statements;*
- *The carrying values/amounts, remaining useful lives and residual values of assets, impairment of assets and information within segment reporting are often not linked to the disclosures outside the financial statements relating to companies' investments and business model adaptations as a result of their transition.*
- *In practice, it is often unclear when failures to meet the relevant 'net zero' related commitments will be recognized by reporting entities as provisions or disclosed as contingent liabilities;*
- *The use of terms such as commitments, compensation, neutrality, etc. in sustainability reporting may not be consistent with the use of the same terms in financial reporting.*
- *It is difficult to reconcile the information on climate-related risks and opportunities in sustainability reports with the information provided in the financial statements*[4]*;*

## 4. FUTURE RESEARCH AND DEVELOPMENT

The directions for future research and development in sustainability reporting are outlined and predetermined by the nature and character of the problems identified. The global trend is likely to be towards a high degree of consistency, comparability, and transparency of information within and outside the financial statements, including sufficient clarity about their interrelationships. Further development of industry-specific requirements, building on the SASB standards, can be expected to address the wide range of sustainability issues. As noted by Kathryn Cearns (2015), chair of the ICAEW's Financial Reporting Advisory Board and Financial Reporting

[3] One insurance company's annual report, which included sustainability disclosures in the front section, referred to climate risk 330 times, but the financial statements did not provide (disclose) any quantitative information on this risk.

[4] For example, reconciliation of EU taxonomy-related investments to financial statements line items or segment information. Differences in the unit of account used for sustainability reporting and financial reporting may also cause difficulties. For instance, assets, vulnerable as exposed to climate-related physical risks, are disclosed at the site level in the sustainability disclosures but this is not reconcilable to the information in the financial statements line items or the segment disclosures.

Committee, the accountancy profession has a great heritage and legacy. To ensure future prosperity through successful and sustainable business practices, Kathryn Cearns argues that it is essential to consider new forms of corporate reporting. Recently, at the 45th Annual Congress of the European Accounting Association (EAA) in Finland, EFRAG hosted a symposium on the critical importance of the link between the information provided by (general purpose) financial statements and sustainability reporting information (EFRAG, 2023b).

Mackintosh recommends three key things to consider – whether a framework can be compared with other frameworks, what is material to the business, and what the business hopes to achieve with the framework, admitting that he does not believe there is a clear answer. "There is still a lot of overlap and potential for confusion," argues Mackintosh (2019). Undoubtedly, each company or organization's approach should be tailored to the nature and specifics of its activities and the particular risks faced by its activities and inherent assets, as well as the climate-related risks created by the activity itself (Oreshkova, 2022a).

Corporate reporting is an essential part of a company's accountability system. Corporate reporting is not only the system and process of collecting and recording the necessary data and transforming it into information using specific methodologies, technologies and procedures; it is also how companies communicate with stakeholders about their position and performance. The operation of the accountability system and the communication process have long-term implications for a wide range of external and internal stakeholders and societies, which is critical to corporate sustainability reporting. These considerations should be at the forefront of the minds of academics and researchers; politicians and policy makers; accounting, financial reporting and sustainability standard setters and regulators; company managers and stakeholders; and the accountancy profession.

## 5. CONCLUSION

Corporate boards and managers are increasingly aware of, and even openly acknowledge their growing concern about, the potential (likely) impact on their bottom line of worsening climate change and environmental factors other than social and governance issues. This has led to a growing need for clarity about where a company stands on these issues and how it is acting to improve these broader practices. In response, many regional and international organizations have emerged to develop and provide frameworks for assessing sustainable corporate behavior. However, many of these frameworks appear to be competing with each other, while others have different (single or broader) focuses and approaches, looking at different metrics for different audiences. As a result, companies around the world are adopting and applying different frameworks, which is the main reason for the reduced comparability and usefulness of the information disclosed and the reduced effectiveness due to the lack of information of sufficient quality for stakeholders.

It is equally important and fair to acknowledge that the proliferation of frameworks primarily affects those who are truly committed to sustainability reporting. The multiplicity and proliferation of frameworks are a major concern for practitioners involved in the sustainability reporting process. It creates complications, difficulties, and barriers that prevent practitioners from presenting the true picture and status of the organization in terms of sustainability and sustainable development, enhancing its reputation and achieving the proposed positive impacts from the organization's perspective, as well as positive ecological, environmental and social impacts.

The issue of the global need for sustainable business practices, once largely an afterthought in the corporate world, is gaining momentum as it proves to be of paramount social and human importance. The author's main concern remains whether humanity has reached the point where its inaction, unresponsiveness, or inability to respond adequately to the worsening problems of accelerating climate change, environmental degradation, loss of biodiversity, etc. has allowed such processes to become irreversible on a global scale.

The effectiveness and efficiency of disclosure will depend on the priorities, concerns and understanding of those at the highest levels of corporate governance and management. Climate change is emerging as a critical factor and key driver of investment decisions in the global allocation of financial capital. Investors are increasingly seeking to understand the potential and existing risks and benefits of the transition to a low-carbon economy. Not surprisingly, the innovative proposals from the US SEC, the EFRAG and the ISSB come at a time when climate-related disclosure requirements are flourishing around the world.

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