

THE STATE OF PLAY IN SUSTAINABILITY REPORTING IN THE EUROPEAN UNION

EXECUTIVE SUMMARY

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Introduction

Since the 1990s, the number of companies disclosing information on their environmental, social and governance (ESG) performance has grown significantly. For many large multinational companies (MNEs) sustainability reporting has become a mainstream phenomenon, while for many small and medium-sized companies (SMEs) reporting is still a challenge. Expectations of reader groups and the information provided by reporting organisations do not always match, even though the quality of sustainability reports improves and web-based reporting offers opportunities to tailor the information to the reader.

The State of Play in Sustainability Reporting in the European Union¹ provides a general overview of the current practices and trends in sustainability reporting in EU Member States.

The study examines:

- What reporting activities companies perform in general, and which challenges reporting organisations and readers of sustainability reports face.
- To what extent companies' reporting practices and readers' needs match with each other. This match and mismatch between the two perspectives is limited to the different groups of readers in general, to what they expect from the reports, and to what companies generally provide and aim for.
- Which public policy instruments are available to governments, to regulate or stimulate the uptake and quality of sustainability reports, and what the effects of these instruments are.

The general term used in this study is sustainability reporting, which means the provision of environmental, social and governance information within documents, such as annual reports and sustainability reports (hard-copy or web-based, e.g. downloadable in PDF-format).

The information provided in the study can be used by the European Commission, individual Member States and other stakeholders, to formulate their own recommendations, and to take further steps to optimize the role of sustainability reporting in society.

Main Developments in Sustainability Reporting

Over the last decade, the following trends and developments in sustainability reporting have become visible:

- Companies use a wide variety of communication instruments, tools and channels to reach the respective audiences for their sustainability reporting.
- Reporting is growing in numbers (around 4,000 reports are registered globally and 2,000 in Europe), but is still quite limited compared to the total number of companies (around 82,000 MNEs and many more SMEs worldwide).
- There is a growing use of reporting schemes like the G3 Guidelines of the Global Reporting Initiative (GRI), and the Communication on Progress (COP) prescribed by

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the United Nations Global Compact (UNGC), as well as of online communication tools and web-based applications, such as XBRL (eXtensible Business Reporting Language), for a better exchange and comparability of business data. In the debate on the future of reporting, integrated reporting is one of the major topics.

- There is an increasing cooperation between the different organisations involved in sustainability reporting. Nearly all of the various platforms and organisations promoting sustainability reporting have developed partnerships with the GRI. This includes the UN Global Compact, AccountAbility, OECD, UNEP, the Carbon Disclosure Project and many governments and sector organisations.
- Looking at the key topics that companies report on, it shows that disclosure of carbon emissions has become quite common, while reporting on human rights is relatively new, but of growing importance.
- Online reporting is becoming common practice, offering an opportunity to provide additional information, to tailor information to the target group and to enable stakeholder feedback.
- External verification is growing, as is stakeholder engagement and integrated reporting.
- Reporting rankings, awards and schemes may constitute an interesting stimulus to the uptake of sustainability reporting and the quality of sustainability reports. Most stakeholders regard reporting schemes as a valuable tool to improve the quality of reporting and to improve comparability between companies. GRI is regarded as ‘the best available’ and ‘a good starting point’. However, some argue that the GRI Guidelines are too complicated for SMEs. Also the provision of a UNGC COP is a new global trend. The use of sector supplements is regarded by many interviewees as a positive development, while others indicate that reports may become too specialised. Furthermore, some argue that using one reporting scheme may result in a ‘tick-box’ exercise, leaving too much room for green-washing.

The Companies’ Perspective on Sustainability Reporting

With regard to the companies’ perspective on sustainability reporting the main conclusions can be drawn concerning their motivations to report or not to report, and their challenges:

- Motivations to report vary among companies. Ethical considerations, reputation and brand value have become more important, while the relevance of economic considerations has decreased. Reputation as a motivation for sustainability reporting is especially important for MNEs, due to potentially large environmental and social impacts and the involvement in international supply chains where labour issues, environmental issues and human rights issues play an important role.
- Reasons for companies not to report in most cases relate to the fact that they do not expect much benefit from reporting. Reasons for SMEs not to report are mainly connected to the associated costs of reporting. On the other hand, experience from supporting SMEs shows that when they are given the right support and tools, progress is possible.

- Challenges with regard to reporting include the selection of topics to report on, the sensitivity of information and the (perceived) costs of data collection. Key challenges to reporting companies are related to the reporting boundaries and to issues related to the content ('materiality', 'stakeholder inclusiveness', 'sustainability context' and 'completeness'), and to the quality ('balance', 'comparability', 'accuracy', 'timeliness' and 'clarity') of the report. These issues are described in the reporting principles of the GRI G3 Guidelines, which constitute an important reference for decisions on the content of reports. Another important reference is the UNGC (for producing a COP), in which the 10 UNGC Principles and UN Goals can be used to define content.

The Readers' Perspective on Sustainability Reporting

With regard to the readers, the main findings of their perspective on sustainability reporting are that:

- To them, the key indicators of a quality report, are transparency, completeness and balance. Companies should provide information with a high degree of credibility and relevance.
- Many stakeholders are no longer satisfied with reactive corporate responses to the world's problems. With considerable media coverage of environmental and social issues, companies have an opportunity to align their brands with positive values and earn credit for their improved performance.
- Quality reporting also requires a context for the information presented, allowing comparisons between different products and actors.
- Readers from business, civil society and other groups tend to share the same opinions regarding the desired contents and quality of the reports. The main differences lie in how the various reader categories use the reports. .
- Readers tend to require the following information to be part of such reports:
 - A link between sustainability strategy and overall business strategy and planning.
 - Commitment to sustainability.
 - Actions taken to address sustainability issues showing what actual measures are being taken by the company regarding sustainability impacts in practical terms. Innovative thinking to solve sustainability challenges.

From the interviews, it can be learned that, for example:

- Very different types of readers agree with the view that reports often lack materiality, are often incomplete and are sometimes selective in their content. They argue that in many cases the balance between good and bad news often turn to the side of good news, favouring the positive image of a company.
- Important differences were observed by most of the people interviewed between the reporting quality of large companies and SMEs. One explanation for this could be that large companies may have a professional division dealing with reporting, while SMEs often lack the time and financial resources to report.

Matching the Companies' and Readers' Perspective

The companies and readers interviewed agreed on several important characteristics of sustainability reporting, corresponding to information found in recent literature:

- Reporting is not a goal in itself, but is meant to improve a company's sustainability performance.
- Regulation of the development of sustainability reports, the content of the reports and the verification of these reports (assurance) could offer important benefits when it comes to quality, credibility and comparability of reporting.
- Integrated reporting constitutes a promising way of further increasing the status of non-financial information.
- The relevance of a stronger stakeholder engagement in the reporting process.

However, expectations of readers are not always being met, which might be the result of real or perceived limitations to sustainability reporting:

- Many readers are still sceptical about the credibility of sustainability reports.
- They are still under the impression that there is an imbalance in the information presented (between success stories and issues a company still needs to improve on).
- They feel that the issues, which are of importance to them, are not adequately covered.
- Some (potential) reader groups have not yet been adequately reached with current sustainability reports.

The key challenge for reporting companies then, is to put together a sustainability report that reflects all issues of importance both to the enterprise and its stakeholders, and that is still easy to read for the wide variety of readers with very different needs and interests. A company has to address various external and internal stakeholders at the same time. The company's choice of target groups may depend on the sector, the motivation for reporting, the interests of the company, and its strategic focus.

The information on the companies' and readers' perspective with regard to sustainability reporting, shows that there is still room for improvement on both the content and quality of reporting.

EU Governments' Role in Sustainability Reporting

The EU and its Member States are very active regarding sustainability reporting and public policy instruments on sustainability reporting, which vary widely, in type, focus and actors involved. Information on the effect and impact on reporting practices of public policy instruments is limited, however, some conclusions can be drawn:

- Governments are increasingly assessing the effects of their policy instruments, showing that public policies have contributed to a stronger uptake of sustainability reporting (recent studies in Denmark and Sweden).
- At the same time, many companies had already been reporting before legislation was introduced. In the case of the UK for example, apart from lobbying and media attention, the driving forces of reporting practices were the financial communities, business players and NGOs, and the fact that many reporting experts are based in the UK.
- Individual national frameworks and legislation may lead to different schemes and obligations. Especially in the case of publishing local reports, as well as a global report that summarizes information from the local level, differing disclosure requirements become problematic.
- Tools for governments, which are already effectively being used, and which can be used more to optimize sustainability reporting, are, for example:
 - Creating instruments to benchmark and recognize good performance.
 - Setting an example by producing a sustainability report in public agencies.
 - Promoting awareness of the benefits of reporting within government.
 - Actively participating in discussions on the future of reporting.
 - Assisting developing countries in data-collection technologies.
 - Requiring state-owned companies to publish sustainability reports.
 - Playing a role against fragmentation of sustainability reporting regulations.

For many large multinational companies, sustainability reporting has become a mainstream phenomenon. Also EU governments are very active regarding sustainability reporting. However, the quantity of sustainability reports is still very small compared to the large number of MNEs in the EU. Furthermore, both the quality of the reports and the public policy instruments on sustainability reporting still vary widely. In cooperation with companies and organisations active in the field of (sustainability) reporting, governments may be able to further enhance the number of reports and the quality of reporting substantially.



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