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Response of the Sustainability Accounting Standards Board to the Public Consultation on the Revision of the Non-Financial Reporting Directive

The Sustainability Accounting Standards Board (SASB) appreciates the opportunity to provide our views in response to the public consultation on the revision of the Non-Financial Reporting Directive (NFRD).

We strongly support a revision of the NFRD to provide specific benefits to a range of key constituencies, including companies, investors, and civil society. Further, we believe such a revision has the potential to spark transformative change. By laying essential groundwork for a globally accepted system of non-financial disclosure standards, the NFRD can help establish the market mechanism necessary to scale up sustainable finance in Europe and beyond, fuelling a 21st century global economy that will support shared prosperity and sustainable economic growth.

SASB believes the key to unlocking this future is reliable, comparable, and relevant non-financial information. This paper discusses key considerations in designing a system of non-financial disclosure standards including:

- Meeting the needs of all stakeholders through the double materiality perspective
- Alignment with international standards
- Meeting user needs with industry-agnostic and industry-specific metrics
- Use of complementary frameworks and standards as “building blocks”

Accountability to All Stakeholders and Double Materiality

Non-financial reporting—far more than traditional financial reporting—has attracted the interest of a broad range of stakeholders, including investors, companies, policymakers, and civil society. Because non-financial reporting is a relatively nascent and rapidly evolving practice, each group of stakeholders stands to benefit from revisions to the NFRD.

To help organisations provide users with relevant information, SASB believes the European Commission has already introduced a foundational concept with its double materiality lens. Relevance is in the eye of the beholder, and civil society often has different information demands than a company’s investors. The double materiality perspective appropriately acknowledges that non-financial information is important to multiple constituencies. It effectively captures the important interactions between businesses, the markets they serve, and the world in which they operate, and it enables meaningful accountability to a broad range of stakeholders. Therefore, we believe double materiality should be explicitly retained as a core element of the NFRD.

We also observe that the double materiality concept usefully recognises the dynamic nature of materiality in the context of sustainable business practices—that is, the idea that an issue that is

material solely from a social or environmental impact perspective can also become financially material over time. This is important to note for two reasons. First, because such financial impacts may materialise in the long term, often over a period much longer than what is considered for traditional financial reporting. Second, because it requires that a system of disclosure established by the NFRD be designed to nimbly adapt as issues emerge, understanding matures, and markets evolve.

Alignment with International Standards

As it envisions the future of non-financial reporting, the Commission is likely to face a natural tension between policy objectives related to EU governance and public oversight and a practical need for a system of disclosure that—like financial capital—travels easily across international boundaries while serving as a foundation for key European policy initiatives. SASB believes that in approaching this challenge the NFRD would benefit greatly from building upon the work that organisations around the world have done to enhance sustainability disclosure through regulation, exchange listing requirements, market forces, or some combination of these.

Key among these organisations are those that have developed and published guidance for voluntary non-financial disclosure by reporting entities—more commonly referred to as the “frameworks and standard setters.” The work of organisations such as the Global Reporting Initiative (GRI), the International Integrated Reporting Council (IIRC), the Climate Disclosure Standards Board (CDSB), and the Task Force on Climate-related Financial Disclosures (TCFD)—along with that of SASB—is vitally important because it can facilitate a foundational layer of high-quality data to support the entire environmental, social, and governance (ESG) landscape.

Today, the “ESG landscape” includes many different players with different roles including data aggregators, rating services, proxy advisors, index providers, and more, each working to shine a spotlight on one or more aspects of the relationship between ESG issues, financial risk-and-return, and societal impact. What these organisations most share in common is the primary hurdle they face: a lack of reliable, comparable, and relevant non-financial data from companies. Meanwhile, companies continue to face challenges identifying what information to disclose to what audience for what purpose, and they struggle to meet the needs of multiple audiences in an efficient and cost-effective manner. Disclosure frameworks and standards are important tools to address these challenges.

Frameworks and Standards: Complementary Tools

The frameworks and standard setters have invested considerable time and resources into developing guidance that can provide a foundational layer of information for multiple users across multiple markets. It is important to distinguish them.

As a starting point, it is necessary to understand that frameworks generally provide principles-based guidance on how information is structured, how it is prepared, and what broad topics are covered. Meanwhile, standards provide specific, detailed, and replicable requirements for what should be reported for each topic, including metrics. In other words, frameworks and standards are complementary tools, and each has a critical function.

In the realm of frameworks, those built for non-financial or integrated reporting have much to contribute to a system of disclosure established by the NFRD. For example, the core elements of the TCFD’s recommendations—governance, strategy, risk management, and metrics and targets—have been widely embraced as a useful rubric for assessing climate risk. SASB believes

this framework is equally useful for assessing a broader range of sustainability issues. As a result, SASB has incorporated these concepts into its Standards Application Guidance to facilitate a more robust understanding of how a company manages its full range of sustainability risks and opportunities. The CDSB Framework provides detailed guidance to help companies report environmental and natural capital information with the same rigour as financial information, and SASB believes this guidance could similarly be applied to a broader range of sustainability issues. The <IR> Framework adds important connectivity between financial and non-financial reporting, addressing a critical need of capital markets participants.

While the principles embedded in various non-financial reporting frameworks can ensure relevance and set the table for comparability, only standards with relatively specific disclosure requirements and metrics can facilitate reporting that is comparable and reliable at the level of granularity which capital markets require and which all users need to establish accountability.

In short, standards make frameworks **actionable**, ensuring comparable, consistent, and reliable disclosure. Standards facilitate disclosure that can be **assured** by an independent third party. Standards also facilitate structured disclosures that can be **digitised**, which will be essential for investors to incorporate non-financial information into investment decision making in a rigorous, scalable, and cost-effective way. This is why we have generally accepted standards in the world of financial reporting and why such a generally accepted system of standards is urgently needed in the world of non-financial reporting.

Meeting User Needs with Industry-agnostic and Industry-specific Metrics

The array of frameworks and standard setters that populate today's corporate reporting landscape has emerged and evolved for good reason: non-financial reporting is a complex, multi-faceted challenge for which there is no simple, one-size-fits-all solution. Importantly, however, that does not preclude an elegant system of solutions from being designed to meet the needs of multiple users and regulatory jurisdictions.

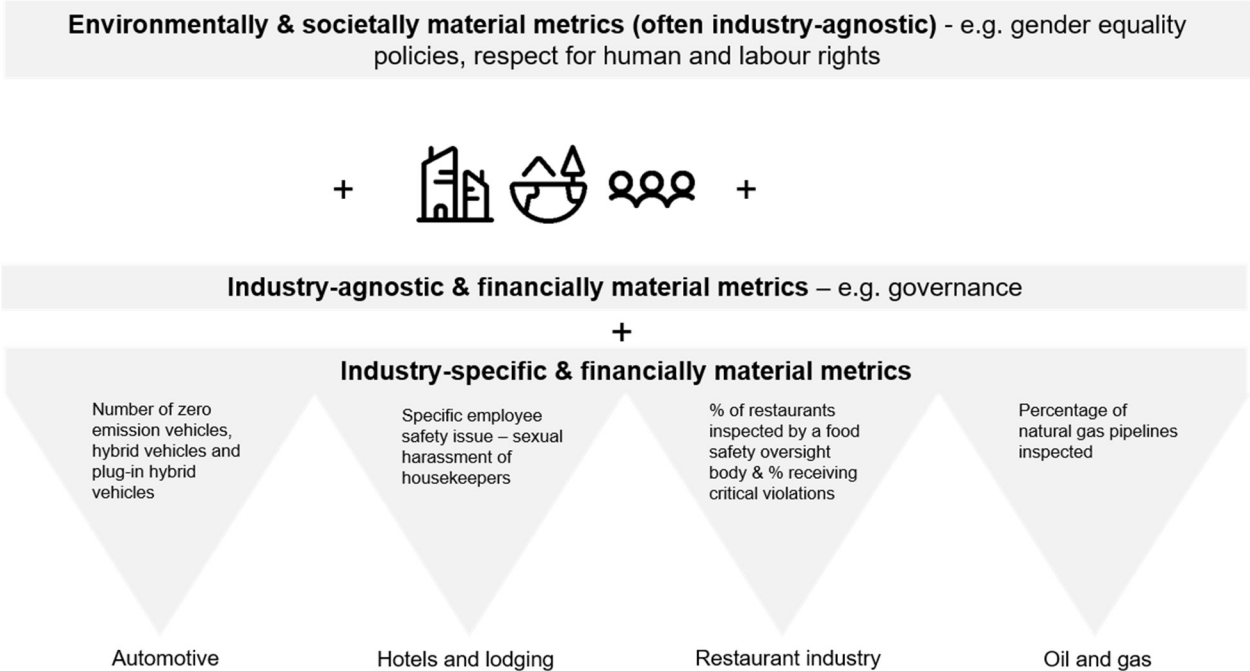
To a great extent, the inability of a single framework or standard to effectively stand on its own is a function of the heterogeneity of users. As SASB has learned during nine years of standard-setting work, even investors are not a monolith—each has their own unique investment strategy, risk tolerance, and time horizon, for example. This same dynamic holds true for other audiences, including corporate professionals, civil society organizations, and policy makers, whose needs fall at various points along the spectrum described by the double materiality concept.

Globally, there are two sets of widely used non-financial reporting standards that together cover the breadth of the double materiality continuum. The GRI Standards focus on the economic, environmental, and social impacts of the activities of a company, and hence its contributions—positive or negative—towards sustainable development. The GRI standards are intended for use by all stakeholders, including customers, employees, civil society, governments, and investors. Meanwhile, the industry-specific SASB standards identify the sustainability-related risks and opportunities most likely to affect a company's financial condition (i.e. its balance sheet), operating performance (i.e. its income statement), or risk profile (i.e. its market valuation and cost of capital) in the near, medium, or long term. The SASB standards are designed to meet the unique information needs of providers of financial capital, such as investors, lenders, and underwriters.

When evaluating the financial materiality of environmental and social issues, industry-specificity is critical, because such issues often manifest in unique ways in the context of specific business

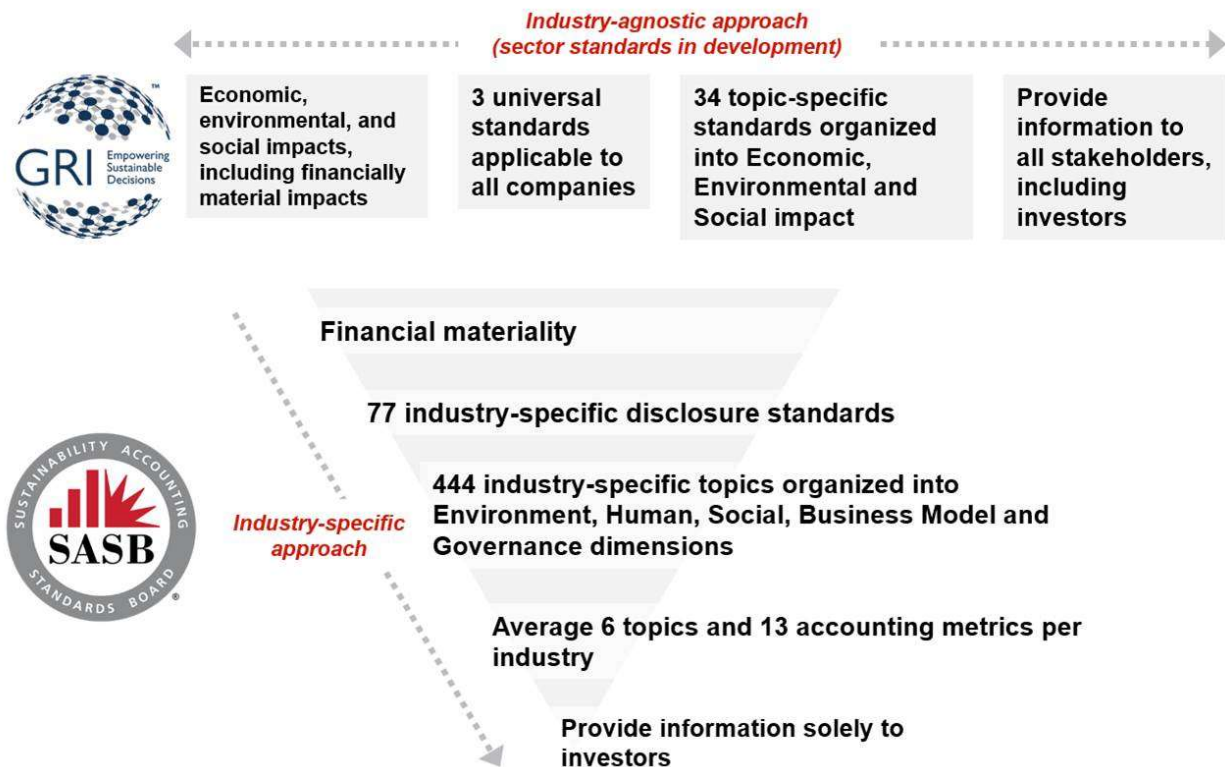
models. Thus, the decisions of companies and investors are shaped in large part by their assessments of sector-specific value-drivers, risks, and opportunities. In addition to enhancing relevance and comparability, industry-specific standards can also be cost-effective for companies to implement, because they can incorporate metrics that are already in use within an industry. In contrast with financially material topics, which tend to be industry-specific, we believe issues of environmental and social impact are more likely to be industry-agnostic, because such issues reflect societal norms and public policy objectives that apply to all industries. (See Figure 1).

Figure 1. The Value of Industry-Agnostic and Industry-Specific Metrics



As demonstrated by the large and rapidly growing number of companies around the world that use both SASB and GRI standards, they are complementary. When used in combination, SASB and GRI standards meet the needs of a broad range of users for information that is both industry-agnostic and industry-specific. They provide a strong foundation for a comprehensive solution under the double materiality concept. (See Figure 2).

Figure 2. GRI and SASB: Complementary Standards



The “Building Blocks” Approach

We believe a “building blocks” approach—underpinned by internationally accepted standards—can serve as a foundation for the revised NFRD. This approach can be used to tailor solutions for different users and markets around the world. It can enable both the customization needed to support key European policy initiatives and the international consistency needed by global capital markets.

Such a “building blocks” system could be based on existing international standards, including SASB and GRI, with SASB standards meeting the need for financially material, industry-specific information and the GRI standards meeting the need for information about a broader set of economic, environmental, and social impacts. As discussed earlier, the TCFD, CDSB, and Integrated Reporting frameworks also include important concepts regarding governance, strategy, risk management, and disclosure quality. Altogether, these standards and frameworks can form the basis for a comprehensive solution that can be adapted for EU-specific requirements.

Striking the Right Balance

Considering revisions to the NFRD brings to the fore a variety of points of tension that we believe can be effectively resolved using a “building blocks” approach with SASB and GRI standards providing the foundational layer:

- **The information needs of a breadth of stakeholders:** Although positive financial returns and sustainable outcomes are not mutually exclusive, different parties need different

information to understand where and how to focus their efforts most usefully in pursuit of their objectives. For example, some users may require industry-specific data to help identify leaders and laggards among peer companies, while others may prefer universally applicable metrics that can illuminate a given firm's contributions (positive or negative) to a specific aspect of sustainable development. Together, SASB and GRI standards provide a foundation for addressing a broad range of stakeholder perspectives and information needs.

- **The need to promote global comparability while allowing for regional specificity:** Although investment portfolios are often global and companies increasingly operate across international boundaries, firms nevertheless must comply with the disclosure requirements and expectations in their local jurisdiction(s). The EU can take a leadership role in solving this global challenge by establishing a “building blocks” approach—underpinned by internationally accepted standards—that can be used to tailor solutions for different markets and users while preserving comparability across borders.
- **The need to ensure European public sector oversight and alignment with the EU Taxonomy and Disclosure Regulation for financial institutions:** As previously mentioned, sustainability disclosure—far more than traditional financial reporting—has attracted the interest of a broad range of stakeholders, including investors, companies, civil society, and policy makers. Because of the broad range of stakeholders for this information, we understand the EU's need for public sector oversight of the standards and standard-setting process. Although not perfectly applicable, we believe the EU's endorsement process for International Financial Reporting Standards (IFRS) serves as a useful precedent. As non-financial standard setters, SASB and GRI have each established a governance structure and an extensive, inclusive, and transparent due process modelled after those of their financial reporting counterparts. With this accountability in place, we believe the EU could develop a governance structure and process to explicitly evaluate the SASB and GRI standards for EU use, and to add EU-specific requirements as needed, including reporting in accordance with the EU Taxonomy and the Disclosure Regulation.

Conclusion

SASB strongly supports the Commission's efforts to strengthen the NFRD. The consultation survey addresses many important questions, and we would welcome participating in the process and lending our expertise as may be necessary or appropriate. We believe the “building blocks” solution outlined here—using a system of existing, internationally recognised standards and frameworks, coupled with an EU-specific process to evaluate the standards and add EU-specific reporting requirements—combines the structure needed to create leading EU guidance with the flexibility to meet a broad range of user needs. This approach can be adapted by regulatory jurisdictions around the world. We view relevant, comparable, reliable non-financial information as the bedrock upon which effective decision-making rests, and thus we believe it can play an important foundational role in building a sustainable, prosperous, and resilient future.

ANNEX I: ABOUT SASB

SASB is an independent non-profit organisation established in 2011 to set standards for companies to use when disclosing sustainability information to investors. SASB standards are categorised into 77 industry-specific disclosure standards, incorporating 26 issues that relate to five dimensions of sustainability: environment, social capital, human capital, business model and innovation, and leadership and governance. By providing transparency into how companies are managing financially material sustainability risks and opportunities, SASB standards enable capital markets participants to more effectively allocate resources toward organisations and activities that create mutually beneficial value for companies, investors, and society more broadly.

SASB standards are created using a robust governance process, which is characterised by evidence-based research, broad and balanced market input, public transparency, and independent oversight. The standards are designed to be driven by input from capital market participants such as companies, investors, and other subject matter experts. This work is carried about by an independent standard-setting board and overseen by the SASB Foundation Board of Directors in a governance structure similar to that adopted by other internationally recognised bodies that set standards for disclosure to investors, including the International Accounting Standards Board (IASB).

SASB identifies sustainability disclosure topics and related performance metrics on an industry-by-industry basis, enabling companies to provide relevant, comparable, and reliable information on financially material sustainability topics. SASB's standards are designed to support independent, third-party assurance, providing a basis for "suitable criteria"—a requirement under professional auditing standards.

SASB standards are complementary to other frameworks and standards. For example, they are among the most frequently referenced tools for implementing the TCFD's recommendations. The SASB standards are often used in conjunction with the GRI standards.

SASB standards are used by investors and companies globally. More than 100 investment and analytics organizations, representing approximately €43 trillion in assets under management, now participate in SASB's Investor Advisory Group, SASB's membership program, and/or license the standards for use in investment processes. These organizations represent 25 countries. Within the last three years, 64 percent of companies that refer to SASB in their public documents are non-US companies, and companies reporting SASB metrics span 51 industries in 30 countries.