Think Ahead ACCA

Smarter regulation non-financial reporting review: call for evidence

A public consultation issued by The Department for Business and Trade, and the FRC
Comments from ACCA to The Department for Business and Trade, and the FRC

16 August 2023

About ACCA:

ACCA (the Association of Chartered Certified Accountants) is the global professional body for professional accountants.

We're a thriving global community of **247,000** members and **526,000** future members based in **181** countries and regions, who work across a wide range of sectors and industries. We uphold the highest professional and ethical values.

We offer everyone everywhere the opportunity to experience a rewarding career in accountancy, finance, and management. Our qualifications and learning opportunities develop strategic business leaders, forward-thinking professionals with the financial, business, and digital expertise essential for the creation of sustainable organisations and flourishing societies.

Since 1904, being a force for public good has been embedded in our purpose. We believe that accountancy is a cornerstone profession of society and is vital in helping economies, organisations, and individuals to grow and prosper. It does this by creating robust trusted financial and business management, combating corruption, ensuring organisations are managed ethically, driving sustainability, and providing rewarding career opportunities.

And through our cutting-edge research, we lead the profession by answering today's questions and preparing for the future. We're a not-for-profit organisation. Find out more at accaglobal.com

For further enquiries please contact:

Glenn Collins
Head Technical and Strategic Engagement
glenn.collins@accaglobal.com

Joe Fitzsimons
Senior Manager – Policy and Insights, UK & EEMA
joe.fitzsimons@accaglobal.com

ACCA support for smarter regulation

The current non-financial reporting landscape in the UK has grown as a result of the demand for the provision of non-financial information from investors and other stakeholders seeking information to support more sophisticated decision making that is not focused solely on financial return. As a result, reporting is required for differing subjects, is not clearly connected, and may not provide companies, investors and wider stakeholders with the information they need to support in decision making.

Non-financial reporting is essential for resilience of the UK economy as business, society and the planet depend on each other. The way each organisation manages its key resources and relationships affects the value that it generates for economies, societies, and nature. Undertaking a non-financial reporting exercise enables increased awareness of how non-financial risks and opportunities will impact upon business, and the resilience of their strategy in the face of change.

Good quality non-financial reporting is also useful to demonstrate value drivers beyond financial performance. This includes intangibles not recognised on the balance sheet, such as innovative processes, know-how and corporate culture, which are fundamental for success, but not currently represented within a comparable framework.

ACCA therefore supports the UK Government in their objectives to:

- Improve regulation across the board to reduce burdens and drive economic growth
- Increase transparency
- Support the board of directors in making policy decisions and shaping future strategy
- Develop a framework to support informed investment decisions
- Respond to the work of the International Sustainability Standards Board; and
- Develop a framework that supports the UK's ambition to be the world's first net-zero aligned financial centre

ACCA's view is that non-financial reporting is key to attracting funds to the UK economy due to increased investment in and focus on green activities, from both an investor and a lender perspective, as investors and lenders seek to decarbonise and move toward more sustainable portfolios. We anticipate that the UK Government's objectives will support inward investment to the UK.

The importance of non-financial reporting

Non-financial reporting is key for enhancing decision making by managers, investors, and wider stakeholders as it supports organisations in understanding and reporting on wider risks and opportunities, the macroeconomic, socioeconomic and environmental trends that may impact upon their organisation, and supports their ability and understanding of how to create value in the short-, medium- and longer-term using a multi-capital approach. Reporting on these issues enables stakeholders to assess the resilience of an organisation in a changing landscape.

Non-financial reporting is also key to achieving global sustainability goals, and UK ambitions such as those relating to decarbonisation or biodiversity. Developing a reporting framework which supports the provision of data and information to monitor progress will be key to ensuring that targets can be monitored, and to ensure that interventions can be made as appropriate.

Developing a global and comparable landscape for reporting

The global non-financial reporting landscape is changing rapidly, and it is important to ensure that any revisions to the UK landscape are not at odds with wider global reporting developments such as the work of the International Sustainability Standards Board (ISSB). Developing a nuanced UK-specific reporting regime may reduce comparability of entities operating within the UK, and may deter investment and the ability to compare UK-entities across a global and comparable baseline. In addition, diversions from wider reporting regimes, such as those appearing within the EU (for example the European Sustainability Reporting Standards (ESRS) and the EU Taxonomy) may result in duplication and complexity of reporting for organisations reporting across a range of regions. In addition to regional nuances of reporting, the UK Government should ensure that reporting to regulations set by the FCA and PRA also enable comparability and avoids duplication of reporting.

The importance of a proportional and balanced approach

It is important to ensure that reporting obligations are proportionate to the size and complexity of an organisation. ACCA supports a principles-based approach, with a minimum core set of comparable metrics, to drive comparability across jurisdictions. A principles-based approach enables organisations to determine the elements of reporting that are relevant and specific for them, based on their own understanding of their business, the key regions within which they operate, and the industries they are part of. A small set of common mandatory metrics may support in comparability, but should be scoped and defined in precise terms. They should also be targeted and limited in number, to ensure ease of use by investors and other stakeholders. Any mandatory reporting should be supported with qualitative information, so that the strategic context behind an organisation's performance can be understood, rather than only providing a discrete set of data points. In this way, the narrative behind the metrics can provide enhanced understanding of the reasoning behind and actions being taken, relating to a particular topic.

ACCA also supports stepped reporting requirements that are specific to different sized entities, so that the costs and benefits of reporting are proportionate, and so that SMEs can focus on information that improves business management and so that business resources can be directed towards actively pursuing a green and just transition. It is important to ensure that it is clear where the burden of responsibility sits, so that the obligation for reporting does not flow to SMEs, and it is important to provide support to SMEs in overcoming the challenges in reporting and in taking action on sustainability. The UK Government has a role in underpinning standardisation of information requests, including coordinating when and how information is delivered, so that one entity does not need to report to a range of stakeholders with similar but nuanced information. The UK Government also has a role to play in providing simplified guidance for SMEs to support them in providing accurate data and information, and has a role in the development of automated tools and digital infrastructure to make information gathering and reporting as straightforward as possible.

Thresholds for non-financial reporting

The current non-financial reporting landscape in the UK has a range of different reporting thresholds, which relate to the nature of the reporting requirements set out by legislation. ACCA strongly recommend a simplified approach with a simplified set of reporting threshold criteria, that correlates with wider non-financial reporting requirements. This would support organisations in understanding their reporting obligations and applying them appropriately. It is important to regularly review and challenge the criteria that have been set in determining reporting thresholds to assess whether they are appropriate taking into account factors such as inflation and modern ways of working.

The importance of integration in reporting

An integrated reporting approach is preferred, so that users of reports can easily access the information they need, but ensuring that strategically-focused information is included within annual reports, alongside financial reporting, as connectivity between financial and other information is paramount to decision-making by both management and external stakeholders.

Wider considerations

Reporting is only one policy lever to promote more responsible business decision making and drive positive change for people and planet. Sustainable finance, corporate governance, taxation, regulation, and other policies to incentivise sustainable business models all play a part. Coherent and inter-connected policymaking is paramount. ACCA urges governments to consider all the different levers available to achieve their public policy objectives, and evaluate their impacts in a holistic way. Besides connectivity between a company's financial and non-financial disclosures, we would call upon the UK Government to enhance connectivity in regulations as much as possible so that companies, regardless of sizes, would be reporting the same information once.

Other considerations include achieving reporting that is assurable. Given the increasing importance placed on both the financial and non-financial information, independent assurance will give confidence to investors that the information provided by different parts of the business is high quality, consistent and reliable.

Non-financial reporting often requires the use of structured and unstructured data. The latter also poses challenges that need to be managed carefully. Technology is an important component to change the way that reports are produced, distributed, and used. Moving forward, information needs to be readable by both humans and machines. We iterate the UK Government plays an important role in the development of automated tools and digital infrastructure to make information gathering and reporting as straightforward as possible.

ACCA considers there are four key tenets or principles of business law that underpin a good environment for doing business, and we recommend the UK Government keeps these in mind when revising the UK non-financial reporting regime. These are:

- Simplicity – the laws that govern business should be stringent but not complex.
- Openness and transparency – lawmakers should be open and transparent with businesses when designing and implementing business law.
- Fairness – business law must be applied consistently and equally among business enterprises.
- Accountability – business law should facilitate the accountability of business, fostering trust in business.

Due to the fast-paced nature of change of the global non-financial reporting landscape, and the speed with which global trends out-pace regulation, it is also important to ensure regular review, monitoring, and adaptation, to ensure that the desired outcomes are being achieved.

Questions for preparers of non-financial information

Q1. How valuable, if at all, is the preparation and/or disclosure of non-financial information for the effective running of your company?

☑ **Highly valuable**

☐ Moderately valuable

☐ Somewhat valuable

☐ Not valuable

☐ Don't know

Responding to non-financial reporting requirements that are structured around the core pillars of Governance, Strategy, Risk Management, Metrics and Targets (such as those that relate to the Task Force on Climate-related Financial Disclosure or 'TCFD') can be helpful in ensuring that companies are aware of their risks and opportunities over the short-, medium- and long-term and the macroeconomic, socioeconomic and environmental trends that might impact upon their company and value chain. It is also useful in supporting companies in considering the resilience of their strategy in a range of future states, and in supporting growth and prosperity. Reporting against a governance requirement also ensures that companies understand the roles and responsibilities for taking action on matters such as sustainability and climate.

Non-financial reporting that seeks information about employment and pay differentials can be beneficial in highlighting inequalities within businesses, and supportive in encouraging companies to strengthen their future workforce pipeline by creating an environment that supports diversity and inclusion.

Reporting on issues such as modern slavery and human rights supports companies in assessing their employment and subcontracting practices, and assessing their supply chains, and minimising exposure to risk where malpractice arises.

Non-financial reporting requirements also play a role in setting out how companies should think about sustainability and how to practically embed it within their organisational processes, or how to respond to investor or customer expectations on non-financial reporting. This is especially true when reporting requirements are accompanied by guidance on the interpretation and application of non-financial reporting requirements.

However, it is important to ensure that any revisions to non-financial reporting meets the following criteria, as set out in ACCA Principles for Connected Corporate Reporting. ACCA believes that corporate reporting standards should:

1. Cover a broad scope of topics that highlight the interactions between the value that companies create for themselves, and the impact that they have on society and planet;

2. Be based on a common language and clear definitions, with special care needed to ensure that global, regional and national standard-setters align the language they use;
3. Strike a balance between being principles-based and providing a minimum core set of comparable metrics;
4. Avoid disclosure overload, so that users of reports can easily access the information they need, but ensuring that strategically-focused information is included within annual reports, alongside financial reporting, as connectivity between financial and other information is paramount to decision-making by both management and external stakeholders.
5. Balance the cost and benefits of reporting (see “costs” question below)
6. Be based on a building-block approach: with the ISSB Standards providing a global baseline, on which national and regional disclosure requirements can be built
7. Achieve reporting that is assurable
8. For small and medium-sized businesses, or enterprises (‘SMEs’), be proportionate and focus on information that improves business management
9. Use technology with an eye on context (ie ensuring that non-financial reporting can be captured and interpreted)

As regards SMEs, the great majority of limited liability companies around the world are micro-entities or small companies. The burden of preparation can be particularly onerous for these companies. However, companies not within the mandatory scope (including SMEs) can benefit from embracing non-financial reporting. A voluntary simplified and reduced reporting standard could be helpful in responding to what are likely to be increasing requests from customers or providers of finance, for example. A proactive approach to managing and reporting social and environmental impacts can help SMEs to seize business opportunities and pre-empt risks.

Q2. What challenges, or costs, if any, does the preparation, disclosure and distribution of non-financial information create for your company?

Good quality reporting on non-financial reporting requires time, resources, and novel skills and capabilities. Non-financial reporting can often also lead to action, where disclosed information highlights inadequacies in a company’s approach (for example ineffective action on modern slavery may highlight the need to increase oversight and action along the supply chain).

Whilst larger corporates may have sufficient resources and expertise to respond meaningfully, and to take action where required, small and medium sized businesses may struggle to respond to the complexity of reporting. Research from the OECD (Businesses' Views on Red Tape) has also shown that the smallest companies incur five times the administrative burden per employee than larger firms, so every effort must be made to increase efficiency of reporting. In a joint report from ACCA, The International Chamber of Commerce and Sage Think Small First: Enabling effective climate action by Small and Medium-sized Businesses (termed SMEs within this submission) the challenges and issues facing small and medium sized businesses are discussed and these include less capital and fewer resources, which makes it harder for them to respond to non-financial reporting requirements.

It is therefore important to ensure the impacts of new mandatory reporting requirements are proportionate. In developing regulatory requirements for non-financial reporting, the decision-usefulness of information to the intended audience should be weighed against the effort required to report the information. The impact on the quality of reporting should be monitored post-implementation. Reporting is only one policy lever to promote more responsible business decision making and drive positive change for people and planet. Sustainable finance, corporate governance, taxation, regulation, and other policies to incentivise sustainable business models all play a part. A proportionate approach to mandatory reporting requirements means that business resources can be directed towards actively pursuing a green and just transition. Coherent and inter-connected policymaking is paramount. ACCA urges governments to consider all the different levers available to achieve their public policy objectives, and evaluate their impacts in a holistic way.

However, it is important to note that non-financial reporting regulation targeted at larger corporates or particular industries are likely to also increase the burden of reporting for SMEs, as information requests flow through the value chain. For example, as monitoring and disclosure of Scope 3 emissions, driven by investor and regulatory demands becomes more widespread, more and more companies are asking their suppliers to be ready to report their own emissions, but they are frequently unprepared and do not have the necessary knowledge, tools or resources. ACCA believes it is in everyone's interest to facilitate effective reporting on climate and other sustainability-related data by SMEs. As this data is increasingly tied to financial activity and the main reporting frameworks are following financial reporting principles, the accountancy profession is in prime position to make a difference here, to galvanise and support the SME community in its journey. We have therefore undertaken research and convened experts, industry bodies and SMEs to understand what is needed to deliver useful data and, equally importantly, to maximise the potential of the SME sector to make a positive impact. As a result we are calling on policy-makers, environmental disclosure bodies, accounting standard setters and large corporates to take on this mission, bearing four principles in mind:

1. **Standardise** Large companies should work together within sectors and industries to ensure SMEs are being asked for information on a standardised basis. Government clearly has a role underpinning this consistency, including coordinating the time when this information should be delivered.
2. **Simplify** Much of the guidance for climate and ESG disclosure in particular is designed for large companies. Government and standard setters should develop simpler guidance, while large companies trying to gather data, such as their Scope 3 emissions, should commit to sending SMEs questionnaires no longer than two pages and to work together on simplifying and aligning the process by asking the same questions and keeping it to the most material issues.
3. **Automate** Governments and businesses need to support the development of automated tools to make information gathering and reporting as straightforward as possible. Large companies can develop the technology and offer training in those tools to SMEs where appropriate. Governments should create an enabling policy framework and invest in digital infrastructure so that SMEs can innovate and share data effectively.
4. **Enable** Government policy and action by large corporates must recognise the challenges for SMEs and enable them to overcome these. Investing in supply chain emissions reduction should be an ESG priority for companies, while government needs to provide an enabling policy framework by thinking small first when drafting climate policy, providing the right incentives that are accessible and actionable for SMEs.

The development of non-financial reporting should, as far as possible, aim to mimic the approach of the International Financial Reporting Standards (IFRS) which were created to establish a common accounting language that could be understood globally by investors and other users of financial statements, and which provide one set of accounting rules for the financial statements of public companies, that intend to make reporting consistent, transparent and comparable around the world. The provision of a single, clear standard for global uptake should be supported as far as possible by the UK Government when developing a non-financial reporting framework.

Q3. What, if any, are the key drivers of cost when having to comply with non-financial reporting requirements?

In order to meet non-financial reporting requirements, companies are often required to develop their skills, understanding and capabilities in order to address a novel set of reporting criteria. This could involve using consultants to support on particularly challenging areas, or by recruiting for positions which cover a broader range of expertise.

Investment into data and systems is also often required as existing data portals are often ill-equipped for dealing with the nature of information required to fulfil non-financial reporting requirements.

Government can support on these elements of cost by developing tools and support for the gathering and reporting of information (see comments to previous question)

Q4. Please select the most applicable statement:

☐ The benefits of preparing and disclosing non-financial reporting information outweigh the costs

☐ The costs of preparing and disclosing non-financial reporting information outweigh the benefits

☑ The benefits of preparing and disclosing non-financial reporting information are proportionate to the costs

☐ Don't know

As noted above, non-financial reporting is beneficial for corporate resilience and supporting strategic decision making. However, it needs to be applied in a proportionate way. See the ‘all respondents section’ for more detail on the benefits of non-financial reporting.

Q5. To what extent do the Companies Act non-financial reporting requirements align with other regulatory requirements your company might be in scope of?

As noted above, and within ACCA Principles for Connected Corporate Reporting. ACCA believes that corporate reporting standards should be based on a building-block approach:

with the ISSB Standards providing a global baseline, on which national and regional standards can be built. Eventually, reporting requirements need to be comparable and decision-useful for its intended audience, and avoid undue reporting burden on preparers. Jurisdictional or national disclosure requirements should be interoperable with global standards, including interoperability across regulations set by the FCA, PRA and other regulators.

Questions for users of non-financial information

Q6. To what extent do you agree or disagree that non-financial information prepared by companies is useful?

☑ **Strongly Agree**

☐ Agree

☐ Neither agree nor disagree

☐ Disagree

☐ Strongly disagree

☐ Don't know

Non-financial reporting is key to providing information to investors, customers and wider stakeholders on the resilience of a company, their ability to pay dividends and debt, and their approach to assessing and managing risk. Non-financial reporting can also be used by managers, tax authorities, employees, financial analysts and governments, to provide a basis for decision making, assessments across industries or regions, or statistical analysis.

Investors are now considering corporates' environmental and social impacts in evaluating the risks associated with investing or lending decisions, and clear and concise reporting is key to supporting decision-making. In addition, as large corporate develop strategies to increase resilience in a changing environment, transparent, clear and credible reporting is key to understanding the interdependency with wider value chains in achieving sustainability targets.

However, it is important to ensure that non-financial reporting meets the following criteria, as set out in ACCA Principles for Connected Corporate Reporting:

1. Cover a broad scope of topics that highlight the interactions between the value that organisations create for themselves, and the impact that they have on society and planet;
2. Be based on a common language and clear definitions;
3. Avoid disclosure overload, so that users of reports can easily access the information they need, but ensuring that strategically-focused information is included within annual reports, alongside financial reporting, as connectivity between financial and other information is paramount to decision-making by both management and external stakeholders;
4. Reported information is assurable; and

5. Proportionate and focus on information that improve business management.

Further commentary to explain the points above are as follows:

- Reporting should be principle-based, allowing entities to exercise judgement, to reflect what is being reported internally to deliver strategy
- They should be based on a multi-capital approach, focused on factors affecting an entity's ability to create value over time.
- Common mandatory metrics may support in comparability, but should be scoped and defined in precise terms. They should also be targeted and limited in number, to ensure ease of use by investors and other stakeholders.
- Disclosures should be concise, to ensure information reported is decision useful
- Reporting should be based on the work of the ISSB to enhance global comparability

Q7. How, if at all, do you use non-financial information?

Investors and stakeholders use non-financial information in a range of ways:

- To support investment / divestment decisions
- In assessing lending decisions and in shaping lending criteria
- To identify risks and opportunities throughout the value chain and to understand resilience of supply chain partners
- In developing transition plans to achieve net zero, stakeholders may look across supply chains to understand their own ambitions and targets
- To understand a company's positive and negative contribution to sustainable development

Q8. Which types of non-financial information are the most useful and/or which are the least useful?

Information around governance and oversight, strategy and decision making, risk management and metrics and targets to monitor progress are the most useful to support in decision making. Metrics and targets, including financial metrics, can also be a useful indicator to assess the significance of risk – for example disclosing financial information on a new "sustainable" product line is a useful indicator of the relevance of that product line in assessing resilience.

Statements without context are the least useful. For example, stating gender pay information with no indication of the reasoning behind such results, or actions being taken by the company to address inequality is not useful. Statements on modern slavery without information as to what checks and audits have undertaken to support those statements are not useful.

Please see our comments above regarding ACCA's Principles for Connected Corporate Reporting, which set out how to develop non-financial reporting that is useful for both management and wider stakeholders, and our comments within the 'general respondents' section for wider comments on specific elements of non-financial reporting.

Q9. How easy or difficult is it to interpret non-financial reporting disclosures?

☐ Very easy

☐ Easy

☐ Neither easy nor difficult

☑ **Difficult**

☐ Very difficult

☐ Don't know

Non-financial reporting requirements can result in a duplication of information across reports, and across different sections of the same report. For example, for entities reporting against the framework of TCFD, there may be a duplication of disclosure relating to the activities of directors, governance and risk, rather than a connected corporate report which integrates consideration on climate throughout wider processes. A connected corporate reporting approach (see above) supports progress toward a better integrated approach which is more meaningful for users of reports. This is a key area of practical challenge in non-financial reporting which should be addressed.

Key areas of consideration include:

- Ensuring the location and frequency of reporting is aligned with wider corporate reporting and is integrated with wider corporate reporting
- Ensuring that users of reports can consider the strategic context behind companies' performance, rather than viewing reported information as a discrete set of data points (for example providing further detail behind gender pay differentials and the strategic actions being taken).
- Applies the work of ISSB to standardise reporting and to develop a common global baseline.
- Considers the connectivity with wider market reporting requirements such as the EU Taxonomy and the ESRS, and the regulations set out by the FCA and PRA to ensure comparable disclosures across geographies and regulators

In alignment with our comments above, we are of the opinion that non-financial reporting standards should be principles-based, applicable to a broad range of businesses using them, with a minimum core set of common metrics that are scoped and defined in precise terms to ensure comparability. They should be targeted and limited in number to ensure ease of use by investors and other stakeholders.

In measuring a wider number of performance metrics, these are likely to be specific to each entity (based on a range of factors such as their sector, and the region of operation). A principles-based approach allows entities to exercise judgement, to reflect what is being reported internally to deliver strategy, and avoids a checklist approach.

Q10. How does non-financial information support your judgement in the following areas?

- **How the directors of the company have fulfilled their duties;**
- **The performance of the company;**
- **The company's future strategy, opportunities and risk;**
- **The company's approach to societal issues such as modern slavery and the gender pay gap;**
- **Whether or not to invest in a company - please consider the types of non-financial information that is most and least useful, and how it compares to other factors or information in your response**

Please see comments referred to above and more detail on specific non-financial reporting requirements within the 'all respondents' section.

<u>Questions for all respondents</u>

Q11. What changes, if any, would you like the UK Government to make to the current legal requirements for companies to prepare non-financial information, and why?

ACCA's support for smarter regulation

The current non-financial reporting landscape in the UK has grown as a result of the demand for the provision of non-financial information from investors and other stakeholders seeking information to support more sophisticated decision making that is not focused solely on financial return. As a result, reporting needs are required for differing subjects, are not clearly connected, and may not provide companies, investors and wider stakeholders with the information they need to support in decision making.

Non-financial reporting is essential for resilience of the UK economy as business, society and the planet depend on each other. The way each organisation manages its key resources and relationships affects the value that it generates for economies, societies, and nature. Undertaking a non-financial reporting exercise enables increased awareness of how non-financial risks and opportunities will impact upon business, and the resilience of their strategy in the face of change.

Good quality non-financial reporting is also useful to demonstrate value drivers beyond financial performance. This includes intangibles not recognised on the balance sheet, such as innovative processes, know-how and corporate culture, which are fundamental for success, but not currently represented within a comparable framework.

ACCA therefore supports the UK Government in their objectives to:

- Improve regulation across the board to reduce burdens and drive economic growth
- Increase transparency
- Support the board of directors in making policy decisions and shaping future strategy
- Develop a framework to support informed investment decisions
- Respond to the work of the International Sustainability Standards Board; and
- Develop a framework that supports the UK's ambition to be the world's first net-zero aligned financial centre

ACCA's view is that non-financial reporting is key to attracting funds to the UK economy due to increased investment in and focus on green activities, from both an investor and a lender perspective, as investors and lenders seek to decarbonise and move toward more sustainable portfolios. We anticipate that the UK Government's objectives will support inward investment to the UK.

ACCA's support for a common legal framework

ACCA believes that a common legal framework is central to economic activity and growth. The framework allows trade and business to flourish. Effective business law facilitates trade between friends and peers but also across long distances and national boundaries.

There are four key tenets or principles of business law that underpin a good environment for doing business as set out in ACCA's Tenets of business law. These are:

- Simplicity – the laws that govern business should be stringent but not complex.
- Openness and transparency – lawmakers should be open and transparent with businesses when designing and implementing business law.
- Fairness – business law must be applied consistently and equally among business enterprises.
- Accountability – business law should facilitate the accountability of business, fostering trust in business.

The required frameworks are further explained in our report Tenets of business law where we set out the following key considerations, which apply to frameworks for non-financial reporting:

- The business law framework should establish a system that encourages entrepreneurship and business enterprise while ensuring accountability and transparency
- The Government should aim to establish a stable environment for business to operate within, and instil a degree of confidence in the market in which businesses operate, including acting when there is unfairness in the market, and facilitating a financial system that provides confidence and serves the needs of businesses when performing transactions
- Law makers should formulate a framework in which business success makes a net positive contribution to society's prosperity, and where they engage positively within the society and environment in which they operate
- Law makers should avoid creating opportunities for abuse by enabling unnecessary discretion in the application of law
- Governments should support small and medium sized businesses, since they employ the majority of workers within most jurisdictions and are key to achieving sustainability targets

Whilst developing a framework for non-financial reporting in the UK, it is also important to:

- Align legislation with the most significant global markets as much as possible to make the UK an attractive place to do business.
- Ensure that reporting requirements are proportionate, recognising that SMEs and charity sector organisations need to adjust to regulatory changes and new regulatory requirements, with often limited resources.

Comments on existing reporting landscape

The current UK non-financial reporting requirements in the UK can be broadly split into the following categories:

1- Directors' responsibilities on non-financial matters
2- Governance, strategy, risks and opportunities
3- GHG emissions or energy use
4- Pay or employment (gender pay, director pay, employment of disabled persons)
5- Modern slavery
6- Engagement with employees, suppliers, customers and others
7- Other (political or charity donations, financial instruments, R&D)

Depending on the size or complexity of the company or partnership there are also requirements to comment on matters such as human rights, anti-corruption, anti-bribery, environment etc.

Directors, governance, strategy, risks and opportunities, GHG emissions

With regard to points 1-3, it is important to observe that these requirements closely correlate with the information that is being reported by corporates in regard to the response to the Task Force on Climate-related Financial Disclosure (TCFD), and the information that is required within the International Sustainability Standards Board's (ISSB) IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information (IFRS S1) and IFRS S2 Climate-related Disclosures (IFRS S2) (i.e. requirements relating to governance, strategy, risk management and metrics and targets).

All large companies and LLPs are now required to report against the recommendations of TCFD in the UK, and many companies have already successfully reported against the requirements, producing clear reports that are comparable between entities due to the consistency in reporting format.

Whilst TCFD relates only to climate, the uptake in disclosure suggests that UK corporates have sufficient knowledge and expertise to report against a standardised framework, in response to specific reporting requirements.

We therefore recommend that the UK Government considers the framework for reporting offered by IFRS S1 and S2, how the information requested within those frameworks compare to existing UK reporting requirements, and considers whether the frameworks offered by IFRS S1 and S2 could support in developing a simplified, comparable and internationally operable reporting environment that supports decision making.

Pay or employment

With regard to the reporting requirements for pay or employment, it is important to revisit why the reporting requirements were put in place, and to review whether the reporting outputs are supporting the outcomes that were intended. We recommend the UK Government undertakes a review to this effect.

In an ACCA Global article published in 2018 , we noted that Gender pay gap reporting is less helpful than had been hoped as the reporting provides information into the gaps on gender pay, but does not offer any insights into the reasons for those gaps, or strategies to address the gaps. It may therefore be necessary to include a suggestions for organisations to expand on their reporting to provide insights behind the numbers.

Wider reporting (modern slavery, political or charity donations, anti-corruption, anti-bribery etc)

As above, it is important to revisit why the reporting requirements were put in place, and to review whether the reporting outputs are supporting the outcomes that were intended. We recommend the UK Government undertakes a review to this effect.

As an example, the Modern Slavery Act requires organisations conducting business in the UK, with a global turnover greater than £36m, to produce a report annually detailing the steps they have taken to ensure that slavery and human trafficking does not exist within their organisation and their supply chain. In a ACCA Global article from 2018: *Internal Audit's important role in combating modern slavery* we noted that many corporates were viewing increased reporting requirements as a tick box exercise, rather than as an opportunity to minimise risk. It is therefore important to ensure that there is either a proactive monitoring system by government, or to ensure that the reporting requirements are simple and clear enough to ensure that customers and investors push for improved disclosure.

Consideration of wider value chain, employees, customers and wider stakeholders (including environment and wider society)

There are various elements where the current UK reporting landscape sets out the need to consider wider stakeholders other than investors and shareholders, ranging from how directors consider these stakeholder groups, and when considering risks, opportunities and corporate strategy. However, consideration of stakeholders and the value chain is key to strategic resilience and value creation. As such, we recommend a reporting framework that supports general consideration of stakeholders and the value chain as part of business processes, strategies and non-financial reporting requirements.

Thresholds for reporting

Please see our comments below on thresholds for reporting.

Q12. Thinking about the future of your organisation and the UK's transition to a net zero economy, what changes, if any, do you think may be required to the type of non-financial information produced to guide decision making, and why?

Supporting the UK's transition to a net zero economy

The UK Government has set an ambition to achieve Net Zero emissions by 2050 and to halt the decline of species populations by 2030 (along with a range of wider nature-based targets). Achieving these goals is significantly dependent on the action of UK organisations, many of whom have set their own non-financial targets. Non-financial reporting will be key to demonstrate progress toward corporate and governmental goals (such as decarbonisation) and instrumental in highlighting interventions needed by government to support or accelerate the decarbonisation agenda, and to support in wider non-financial goals.

Whilst TCFD and the associated UK reporting requirements go some way in encouraging companies to report on their climate-related risks and opportunities, and their strategy, more is required to ensure that the substance of reporting supports actionable change within the corporate landscape, and to support clear financial flows that support a low carbon transition and enhanced resilience.

Emissions reporting

ACCA calls for more ambitious policies to achieve net zero emissions by 2050. Early and global action is necessary and governments have a crucial role in reducing carbon emissions through regulation, the provision of green infrastructure and appropriately targeted subsidies. ACCA considers that carbon taxes are necessary to reach net zero, and that a global minimum carbon price, integrated globally, is a major step in reducing emissions.

Understanding and reporting on GHG emissions is a key element of wider regulatory and political mechanisms required to support decarbonisation and is an area where many corporates are already comprehensively reporting, due to investor or customer pressure, or as a result of existing reporting requirements.

In the UK, publicly quoted companies are required to report on GHG emissions (scope 1 and scope 2), whilst large entities are required to report on energy use for UK gas, electricity and transport activities, and the associated emissions. However, PIEs and AIM listed entities with more than 500 employees, or entities with a turnover of more than £500m and more than 500 employees are also required to report against the framework of TCFD, and are required to report on the KPIs used to assess risk. Many corporates are reporting GHG emissions against this element of the disclosure requirements (though this is not a prescriptive requirement of the reporting requirements under sections 414CA and 414CB of the Companies Act 2006 and regulations 12A and 12B of the Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008.

The ISSB's IFRS S2 standard, recommends that corporates disclose scope 1, 2 and 3 emissions and is intended to set a global and comparable baseline for reporting.

ACCA supports a consistent and comparable approach to GHG emissions reporting that is comparable across different entities. The content of IFRS S2 could be a useful starting point in setting out how corporates and partnerships should report on their emissions.

ACCA supports a proportionate approach to reporting requirements that does not put an undue burden on SMEs. However, it is important to consider that SMEs may already required to report on their GHG emissions as a result of supply chain requests, and it is likely that these requests will increase in future periods as large corporates develop a clearer picture of their supply chain emissions. In addition, the contribution of SMEs to GHG emissions cannot be understated. Whilst smaller businesses are responsible for nearly 50% of all GHG emissions from UK businesses, just 3% had measured their carbon footprint in 2016-2021 (Think Small First. ICC, ACCA, SAGE)

As set out in a joint report from ACCA, The International Chamber of Commerce and Sage Think Small First: Enabling effective climate action by Small and Medium-sized Businesses, Governments and businesses need to support the development of automated tools to make information gathering and reporting as straightforward as possible. Large companies can develop the technology and offer training in those tools to SMEs where appropriate. Governments should create an enabling policy framework and invest in digital infrastructure so that SMEs can innovate and share data effectively.

This will also support in building a detailed picture of emissions across organisations, to support in developing a clear decarbonisation trajectory for corporates and the Government.

Comment on UK Green Taxonomy

Non-financial reporting is key to attracting funds to the UK economy due to increased investment in and focus on green activities, from both an investor and a lender perspective, as investors and lenders seek to decarbonise and move toward more sustainable portfolios.

The development of a Green Taxonomy provides a common language for identifying "environmentally sustainable" economic activities and selling corresponding products. It can help increase access to financing, improve transparency and reduce opportunities for "greenwashing". It is designed to support the achievement of current and future climate goals.

The increased transparency that can be achieved through non-financial reporting requirements such as the UK Green Taxonomy is key to supporting the channelling of financial flows to sustainable activities, as it provides a clear and comparable indicator to the wider market over the sustainability status of a company and supports investors and lenders in achieving their own sustainability agendas. A number of UK organisations are now reporting voluntarily against the EU Taxonomy to enhance comparability against EU peers, and to obtain funding.

However, international convergence on environmental sustainability is crucial to meeting worldwide climate targets and the UK Government should ensure that this is taken into consideration when determining the non-financial reporting landscape within the UK. For example, there are concerns that the EU Taxonomy is not a global standard, and concerns that the UK Green Taxonomy would cause further differentiation. Although taxonomies can be a valuable reference for investors, an activity-based taxonomy may be of little use in some jurisdictions. Canada, a resource-based economy, is developing its own taxonomy (see more information here: Canada Taxonomy Roadmap Report. In addition, whilst a focus on economic activities rather than companies could help with transition, obtaining good-quality data, such as revenues or carbon emissions, by activity may be difficult, especially for smaller organisations with immature reporting systems. Other complexities exist within the EU Taxonomy, for example, investors typically use GICS global classification to identify sectors, whereas the EU Taxonomy uses the European industry-based NACE system. Although the EU Technical Expert Group recommends mapping between the two, there is concern that this is an unnecessary complication.

The UK Government can benefit from gaining insights into the adoption and roll out of the EU Taxonomy, to determine the ease with which corporates have responded to the reporting requirements, the usefulness of the reporting to investors and lenders, and to understand whether the classification systems are being used to drive green behaviours (such as redirecting financial flows). The UK Government should also ensure that developments in the UK are closely aligned and interrelated with the EU Taxonomy framework in particular, to support entities who may have to report in one or more jurisdictions.

Clarity over decarbonisation strategies – Transition Plans

The TCFD reporting framework within its 'strategy' section, calls for companies to set out an analysis of the resilience of a company's business model and strategy, taking into consideration different climate-related scenarios. The TCFD framework suggests consideration of a 'below 2 degree' scenario, though this element has not been transposed into The Companies (Strategic Report) (Climate-related Financial Disclosure) Regulations 2022 and The Limited Liability Partnerships (Climate-related Financial Disclosure) Regulations 2022.

Many companies are setting out a broad overview of their transition plans to achieve net zero within this section of the reporting, however there is a risk that broad targets have been set without the detailed strategic planning, budgeting and forecasting required to achieve those targets. This presents a risk that the targets will not be met.

The work of the Transition Plan Taskforce is useful in supporting organisations in considering their transition plans in depth, and considering the different levers, collaborations and dependencies that will be necessary in achieving their targets. However, applying the considerations as set out within the Transition Plan Taskforce's 'gold standard' is complex and resource intensive for companies. Therefore, a proportionate and balanced approach is required (see comments above on proportionality).

It is important to note that where larger corporates or LLPs develop clear transition plans, there will be significant dependence on the wider supply chain in achieving those plans, as such the burden of responsibility for understanding decarbonisation strategies is unlikely to be retained within large entities (see below).

Supporting the adoption of non-financial reporting and the impact on SMEs

There is a risk that the burden of reporting will result in reporting that meets non-financial reporting requirements, but does not result in a deeper understanding of strategic resilience, decarbonisation trajectories, or provide decision-useful information to investors and wider stakeholders. It is therefore important to ensure that any additional specific non-financial reporting requirements provide information in a clear, concise and coherent manner, to facilitate understanding by users of reports.

Supporting adoption by SMEs may come in the form of:

- proportionality and scalability in the reporting requirements – scaling of requirements to support application by companies with limited capabilities, experience, or resources.
- transitional reliefs in phasing in some disclosure requirements when they first become effective.
- technical assistance such as non-mandatory technical guidance on the application of the reporting requirements and a platform that publishes frequently asked technical questions and their solutions to support application.
- a capacity-building programme to build capabilities in, or for SMEs.

It is also important to provide clarity over where the burden of responsibility sits, so that reporting requirements do not filter down through to SMEs (please see expanded comments below).

Q13. How should the standards being prepared by the International Sustainability Standards board (ISSB) be incorporated into the UK's non-financial reporting framework?

ACCA welcomes the publication of IFRS S1 and IFRS S2 and supports the ISSB's work in creating a global baseline for comparable information on sustainability issues, which will help investors, financial markets and society more widely. The standards will make sustainability reporting more consistent, connected and meaningful.

ACCA supports integration of ISSB within jurisdictions to support the adoption of one universal standard for reporting. We recommend the UK Government also adopts consistency in reporting, aligned with the ISSB's issued standards.

Adoption should be under a similar approach to how IFRS is endorsed with or without amendments according to similar principles used by UKEB. As with all changes a focus on suitable transition or time is required to allow for cost effective and meaningful gathering of information.

The role of ISSB standards in simplifying the UK's legal framework

As noted above, the current UK non-financial reporting requirements include elements relating to Directors' responsibilities on non-financial matters, Governance, strategy, risks and opportunities, and GHG emissions or energy use. These requirements closely correlate with the information that is being reported by corporates in regard to the response to TCFD, and the information that is required within the ISSB's IFRS S1 and IFRS S2 (i.e. requirements relating to governance, strategy, risk management and metrics and targets).

All large companies and LLPs are now required to report against the recommendations of TCFD in the UK, and many companies have already successfullyreported against the requirements, producing clear reports that are comparable between entities due to the consistency in reporting format.

Whilst TCFD relates only to climate, the uptake in disclosure suggests that UK corporates have sufficient knowledge and expertise to report against a standardised framework, in response to specific reporting requirements, especially with regard to governance, strategy, risks and opportunities.

We therefore recommend that the UK Government considers the how the framework for reporting offered by IFRS S1 and S2 compares to existing UK reporting requirements, to determine whether IFRS S1 and S2 could support in developing a simplified, comparable and internationally operable reporting environment that supports decision making.

It should be noted that whilst the UK corporate landscape requires many corporates to report against TCFD, the required reporting within The Companies (Strategic Report) (Climate-related Financial Disclosure) Regulations 2022 and within The Limited Liability Partnerships (Climate-related Financial Disclosure) Regulations 2022 is a lot more simple than the requirements set out within IFRS S2. As such, reference to this wider reporting framework would be helpful to support enhanced reporting, and avoid corporates undertaking a 'tick the box' exercise.

It is also beneficial to point out that whilst certain elements of the standards are complex, such as scenario analysis, IFRS S2 includes provisions which ensures that scenario analysis requirements are aligned with the circumstances of an organisation, their exposure to risks and opportunities, and the skills, capabilities and resources available.

The role of IFRS S2 in the transition to net zero

The UK is dependent on the decarbonisation of corporates and organisations in achieving its net zero strategy, however corporates and organisations are currently unclear as to how they will achieve net zero and the interventions required. In addition, they may be unwilling to carry out significant capital expenditure or business model shifts, whilst there is significant uncertainty over how the regulatory and political landscape will change (for example in respect of the introduction of a carbon tax), and significant uncertainty over the economic benefits of making such a transition.

The TCFD recommendations, and consequently the content of IFRS S2 provides a useful framework against which corporates can consider the risks and opportunities that impact upon their organisation. The requirements for organisations to understand how a changing environment may affect them and to consider the financial impacts are bringing together executives in finance, sustainability, risk and board members in a new way. As a result, TCFD is driving real change at strategic level, as corporates gain a deeper understanding of what climate and sustainability means for them.

This strategic shift is likely to drive policy decisions which will drive decarbonisation, as entities gain more clarity over how they will increase their resilience and meet their decarbonisation targets (Nat West for example will stop financing oil exploration activities with effect from 2025).

As such, IFRS S2 is one lever that can be used to support the UK Governments transition to net zero.

Impact on SMEs

As noted above, we recommend that a proportionate response is adopted to avoid an undue burden on SMEs, including transitional relief for reporting. Reporting requirements for SMEs should ideally be aligned to what they would be required to reporting within the value chain.

Q14. To what extent do you agree or disagree that current size and company type thresholds for non-financial reporting information could benefit from simplification?

☐ Strongly agree

☑ **Agree**

☐ Neither agree nor disagree

☐ Disagree

☐ Strongly disagree

☐ Don't know

The existing reporting thresholds as set out within Annex: Individual reporting requirements vary considerably, and set different reporting requirements for PIEs, publicly traded or quoted companies, very large entities, large, medium and small entities. Regulations relating to employment use thresholds relating to the number of employees, and modern slavery requirements apply to companies based on turnover thresholds (amongst other requirements).

In simplifying the UK corporate reporting landscape, we would recommend that existing thresholds are reconsidered to provide clear and consistently applied thresholds, that consider the wider jurisdictional reporting requirements (such as those relating to the Corporate Sustainability Reporting Directive in the EU), and wider regulatory reporting requirements (such as those relating to the FCA and PRA).

We would anticipate differing levels of complexity of reporting for each company size, with simplified reporting applying to SMEs. This would ensure that non-financial reporting requirements are proportionate to the size and complexity of the entity, and focused on information that improves business management (please see comments within the 'Questions for preparers' section – specifically within the question '*What challenges or costs, if any, does the preparation, disclosure and distribution of non-financial information create for your company?.*

In the development of a UK non-financial reporting framework, we recommend that the UK Government apply the principles of financial reporting frameworks and standards. For example, the IASB's International Financial Reporting Standard ('IFRS') provides a global comparable standard for financial accounting. The IFRS for SMEs standard applies to small and medium sized entities that do not have public accountability to publish general purpose financial statements. FRS 102 is a financial reporting standard in the UK that sets out the financial reporting requirements for entities that are not applying the adopted IFRS, FRS 101, or FRS 105, and is based on IFRS for SMEs, with some significant amendments made for the application in the UK and Republic of Ireland. Whilst there is no current differentiation between the application of IFRS S1 and S2 for larger or smaller entities, we would recommend a similar approach is adopted when determining non-financial reporting requirements for different sized entities within the UK.

Q15. The Companies Act 2006 sets out size categories for UK companies that determine the type of accounts that need to be prepared and filed with Companies House. To support you in answering the questions you may want to refer to the annex that sets out the requirements under the Companies Act 2006 and supporting regulations here.

Current reporting requirements put a responsibility for reporting on entities that do not fit within the standard thresholds of small, medium and large, as defined by the Companies Act 2006 (s172, for example, applies to very large companies). Depending on the conclusions of the consultation, the UK Government may see fit to add an additional reporting category, for very large entities, which may support in targeted reporting to entities with different levels of resource and capacity to respond to shifting requirements, and which may support with a phased introduction to revised reporting requirements.

In addition, it is important to regularly review and challenge the criteria that have been set in determining reporting thresholds. For example, inflation is impacting UK entities significantly, and balance sheet and revenue criteria are unlikely to remain consistent over time, when taking inflation into account, meaning that smaller entities will are likely to creep into larger company thresholds, driven by a decrease in the value of money. In addition, employee numbers may need clear definitions to take into account the change in approach for working patters and flexible working.

Q16. Do you have any other comments that might aid the consultation process as a whole?

In ACCA's view, precise terminology and clear definitions that are well-understood by everyone are paramount to good standard-setting. Our preference is to refer to 'connected corporate reporting' instead of 'sustainability reporting' or 'non-financial reporting', to indicate that reporting outside of the financial statements should encompass a broad range of factors that affect organisations' ability to create value in the short, medium, and long term, beyond financial performance and position but equally beyond environmental or social impact. This also means that information outside of the financial statements must be consistent and connected with information in the financial statements.

In this response, we refer to "non-financial reporting" to mirror the terminology used within the consultation.