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Reporting to build trust: A framework

Faced with a confusing menu of reporting frameworks and methodologies, companies must seek to find out what matters to their stakeholders now.

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What companies say can provide great insight into what they do. The way they describe how they are monitoring and addressing sustainability issues, including those related to environmental, social and governance (ESG) matters, through mandatory reporting or voluntary statements can be a lever for building trust with those around them. But any claims made should be intentional, achievable, balanced and verifiable. Just as there are pressures building from a variety of stakeholders—investors, employees, suppliers and customers—for information related to sustainability efforts, pressure from the industry of activism devoted to debunking any misleading, incomplete or false claims is also growing. And companies face consequences for not living up to their stated aims, even if the shortcomings can be validly explained. Companies are also more likely to be fined for getting things wrong as regulators are increasingly willing to enshrine penalties in law.

Creating a narrative that works for key stakeholders—one that is comprehensive, relevant, balanced and accurate—is no easy feat. It requires adherence to standards backed up by data and a clear understanding of stakeholder needs. What is important to one group may not matter to another. And not all the conflicting demands on companies will be reconcilable. Leaders need to be clear about what they are doing—and, critically, why—even if some stakeholders will disagree strongly.

Although a number of bodies have made a great amount of progress in sustainability reporting over the years and companies have developed narratives and metrics on their own that work for them, what's been sorely missing is some structure among the noise. This is set to change. In 2022, there are three important consultations on non-financial reporting standards: the US SEC's climate disclosure proposals, the EU's draft sustainability standards and the International Sustainability Standards Board's proposed global sustainability-related disclosures. Once finalised, these developments will move us away from a world of voluntary disclosure, where it is up to the company to decide what it wants to say, and into a mandatory-reporting environment, where the company is told what it must say. Such a change will help level the playing field for businesses and give users a better chance of understanding what they are reading.

But even with new guidelines that set the parameters for reporting, figuring out what information matters most, and to whom, is a complex task, and engagement with stakeholders will be paramount. In addition, collecting the information required to satisfy regulations (which are evolving) and stakeholders will involve planning; specialised expertise in areas like carbon footprinting at home and abroad to measure and assess the information; a way to assure it is reliable; and a strategy to deal with the results. Depending on the industry, the strategy could include ways to reduce carbon emissions, reduce water use and improve working conditions. But it will also require determining how to communicate the findings. The old adage that what gets measured gets managed will be a powerful motivator for action—both for informing a company's stakeholders and for running the business. In PwC's 2021 Global CEO Survey, when chief executives were asked which areas of their business they should be doing more reporting on, the largest share, 43%, chose their environmental impact.

Comprehensive corporate reporting can shine a light on the cases in which words are not matched by action. 'The recent avalanche of net-zero pledges by businesses, investors, cities and regions will be vital to keep [a global temperature increase of only] 1.5°C alive and to build towards a safe and healthy planet, but only if all pledges have transparent plans, robust near-term action, and are implemented in full,' said Catherine McKenna, the former Canadian Minister of Environment and Climate Change who now chairs a new UN initiative that was announced on 31 March to speed up the implementation of business's net-zero pledges. Ultimately, reporting is no substitute for taking action.

Here are three steps companies can take now to ensure that they can explain how they will deliver on a sustainability strategy and provide meaningful sustainability reporting that meets the requirements of its stakeholders.

1. Find out what matters to your stakeholders

From now on, and when the new reporting regulations are in place, companies will have to understand what matters to their stakeholders beyond what's formally required, and how best to present the information they need. The best way to do that is by asking them. Suppliers, customers, employees and investors are often aligned in the information they seek, but there are likely to be differences in the level of detail needed and how they consume it. Take climate change, for example. Customers and society at large want information about a company's carbon footprint and the actions the company and its suppliers are taking to reduce it. Investors, in addition, want to understand the risk that climate change poses for the business. This is where scenario analysis comes in.

There has never been a greater focus on the impact a business has on the people and world around it, and not just what is material to the financial performance of the business itself. Some companies have always understood that, and others will need to catch up. Everyone is watching—and, in a break from tradition, investors are looking at more than potential cost savings. Carl Icahn, for example, nominated two directors to the board of McDonald's in May 2021 to force the fast-food chain to address an animal welfare issue. As part of a ten-year plan, McDonald's had promised in 2012 to end the practice of confining pregnant pigs in tiny boxes, but hasn't done so. Although Icahn's move was unsuccessful, it's an example of a shareholder noticing when sustainability-related targets fall short and letting their dissatisfaction be known. This is one of a number of ways investors can take action when they feel a company is not sufficiently addressing ESG issues in the business, according to PwC's global investor survey.

The energy sector has long experience in answering stakeholder questions about climate change, and climate is a standard part of their corporate communications strategies. For example, BP produces a report on its engagement activities, which include conversations with its harshest critics and NGOs, attendance at climate forums, and live events with employees on climate topics.

Engagement can set priorities. It can also help boards assess the actions that need to be taken and over what time frames.

Actions companies can take now

- Ask both internal and external stakeholders what information they need—for example, on your investor calls, through customer surveys and in employee town halls—and why it matters to them.
- Discuss a variety of issues, including environmental issues, worker rights, equal pay and working conditions. Start broadly, then narrow it down to the highest priorities.
- Monitor regulations, including on new taxes, to understand what information is (or will be) required and by whom.

2. Get the right data

Once you understand what matters to your stakeholders, you can report what they need to know about it. But first, be clear about what data is required, and establish a mechanism to collect and analyse it. Doing so is not always easy, especially when the data is dispersed throughout the company, or not all of it is owned by the company. Being well-intentioned but having imprecise and incomplete data is a big red flag for investors and customers alike.

When Wipro, a large Indian computer company, wanted to know how its exposure to climate change should inform its enterprise risk assessment and corporate strategy, it worked with experts to model detailed scenarios based on temperature changes in 12 cities. Under one scenario in their report (see page 17), water stress in India will be aggravated in eight of the 12 cities studied, while heat waves are expected to worsen in six of them. The company now has the data it needs to assess what responses are necessary.

But understanding complex sustainability-related data is not always straightforward. To do it properly may require upskilling employees, as well as the board. Only a little over half, 55%, of respondents to PwC's 2021 global investor survey agreed that company board directors are sufficiently knowledgeable about the ESG issues facing the company. The frameworks in development for non-financial reporting will help companies understand where they need to build capabilities and collect the data they need.

Actions companies can take now

- Establish controls and processes for collecting and analysing the data that is needed both to make decisions internally and to report externally.
- Bring together finance and sustainability teams to create a holistic picture across the business.
- Develop high-quality scenario planning, which will identify gaps in information gathering.
- Upskill employees across the business and board members.
- Synchronise internal and external communications, backed up by data.

3. Tell the right—and full—story

Whether you're preparing an integrated annual report or a stand-alone sustainability report, the publication has to be informed by steps one and two. It's also critical to put the right resources in place, in terms of both time and people, along with the right incentives and the right oversight. Companies can truly be confident in what they report only when it is subject to board oversight, relevant to the company's strategy, and has the right governance, systems and controls in place to measure progress towards targets and plans.

Many large companies that have teams of hundreds working on financial reporting often have only a handful of people working on sustainability reporting. Even with the best intentions, less-resourced areas have a higher potential to miss something that turns out to be critically important. The business world's financial reporting capabilities have been built over 170 years. When it comes to sustainability reporting, we need to move quickly to build the right capabilities—using what we've learned from financial reporting.

And if sustainability reporting is to be on par with financial reporting for informing resource allocation decisions, it needs to be just as robust and relevant. Part of how this is done will be prescribed by the set of globally aligned reporting standards currently being discussed; and part will mean anticipating stakeholder requirements as they evolve, even before the reporting standards catch up.

Assurance will be critical to ensuring stakeholders have confidence in the information reported by companies. In PwC's 2021 global investors survey, 79% of investors said they place more trust in ESG information that has been independently assured. And an overwhelming majority of investors want the ESG metrics and narrative to be assured at the same level as financial statements (i.e., reasonable assurance).

Last, but by no means least, incentivising leaders is key. More than two-thirds of investors in PwC's survey expect ESG performance metrics to be built into executive pay packages. Recent research by PwC found that 45% of FTSE 100 companies have an ESG measure in both short- and long-term incentive packages. A broader survey of 632 business leaders, investors and HR-focused leaders in nine countries and regions in 28 industries found that 82% of leaders had ESG metrics in their rewards. This is important. An ESG strategy and the associated deliverables are often on time frames of a decade. The majority of CEOs don't stay in post that long, but their influence is critical to making progress on addressing ESG issues: in PwC's investor survey, 66% said they are more confident that companies are on top of ESG risks and opportunities if someone in the C-suite is accountable for them.

Actions companies can take now

- Formalise a reporting strategy that is linked to the business strategy.
- Put the right governance in place so the board can oversee the company's progress.
- Resource the reporting teams so they can cover financial and sustainability information on an equal footing.
- Be brave and talk openly about where to go next—and about the challenges and the risks.
- Determine what's needed for reasonable assurance, which might include independent assurance.
- Look at incentive structures to set the right targets, over sensible time frames.

sTelling the story of a company's sustainability performance is a complex job, and sustainability reporting is just one aspect. Far from being the endgame, it is just the start of presenting the company's strategy and performance to the world. Accordingly, companies need to tackle this meticulously, as they do financial reporting—in good faith and producing results that can stand the test of time. Compliance with the new standards will help, but it will also take engagement with stakeholders, with an intent to listen and learn. Businesses can't solve all the world's existential threats, but they can influence their own operations and the related reporting. By telling their sustainability story clearly, truthfully and transparently, they will build trust, which is fundamental to achieving sustained value creation. +

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