Chartered Governance Institute UK & Ireland

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Dear Sir / Madam,

Non-financial reporting review: Call for evidence

We welcome the opportunity to comment on the Department for Business and Trade's call for evidence on non-financial reporting.

The Chartered Governance Institute UK & Ireland is the professional body for governance and the qualifying and membership body for governance professionals across all sectors. Its purpose under Royal Charter is to lead 'effective governance and efficient administration of commerce, industry and public affairs', working with regulators and policy makers to champion high standards of governance and providing qualifications, training and guidance. As a lifelong learning partner, the Institute helps governance professionals to achieve their professional goals, providing recognition, community and the voice of its membership.

One of nine divisions of the global Chartered Governance Institute, which was established 130 years ago, The Chartered Governance Institute UK & Ireland represents members working and studying in the UK and Ireland and in many other countries and regions including the Caribbean, parts of Africa and the Middle East.

As the professional body that qualifies Chartered Secretaries and Chartered Governance Professionals, our members have a uniquely privileged role in companies' governance arrangements. They are therefore well placed to understand the issues raised by this call for evidence. In preparing our response we have consulted, amongst others, with our members. However, the views expressed in this response are not necessarily those of any individual members, nor of the companies they represent.

Our views on the specific questions raised in the call for evidence are set out below.

The following questions are primarily aimed at the preparers of non-financial information.

Q1. a) 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

Q1. b) And why do you say that?
Please consider whether the information:
Helps to attract investment;
Supports setting of strategy, understanding and improving the long-term value creation of the company and;
Your transition to net-zero.

The Institute’s members, which include governance professionals and Company Secretaries working in companies of all sizes, ranging from FTSE 100, to AIM-listed, to SMEs, have a uniquely privileged role in companies’ governance arrangements, including in the preparation of non-financial information. We have consulted with them in preparing this response, although the views expressed are not necessarily those of any individual members, nor of the companies they represent.

The preparation and disclosure of non-financial information is increasingly expected and even demanded by investors, employees, clients and other stakeholders. As such, companies are required – both by regulators and by stakeholder expectations – to disclose increasing amounts of non-financial information. This has instrumental value for companies themselves, in that it increases transparency and the flow of information between companies and their investors. In turn, non-financial information can increase investor confidence in a company, its practices and its underlying strategy, which can ultimately attract further investment.

Internally, the requirement to disclose non-financial information can also contribute to changes to business practices, by ensuring that appropriate conversations are happening at board level – and ultimately, that action is taken. In some areas, it is clear that reporting requirements can increase companies’ willingness and capacity to bring about change. For example, when the Davies Review was produced in 2011, only 9.5% of FTSE 350 board positions were held by women, whilst in 2023, the FTSE Women Leaders Review was able to report than this had risen to 40.2%. Notably, this change was brought about against a backdrop of significant stakeholder demand for change and on a voluntary basis, in which companies were offered support and suggestions for concrete actions (beyond simply reporting) which they could choose to undertake. In other areas, the relationship between reporting on an issue and adopting more stringent policies and practices around that issue is less clear. For example, a recent report by Scientific Beta found that companies with good ESG scores produce just as much carbon as their peers with low scores – and that this holds true even if a company's carbon intensity is compared only to its environmental rating (a constituent part of its ESG rating). Whilst ESG ratings are, of course, produced by third parties and do not form part of companies' own reporting, they are based on information contained in annual reports (as well as gathered in separate surveys), which implies that the requirement to report on emissions has not (as of yet) necessarily resulted in emissions reductions.

There are also less positive outcomes from the increased requirement for non-financial information. One of the ways in which that requirement manifests is through questionnaires submitted to companies by third-party data collectors or single-issue pressure groups; we are told that it is not unusual for a large company to receive at least one of these every week. Many of them will be asking for information that the company already has easily to hand or that the company has already made public, but others will be asking for data that the company may regard as commercially sensitive or, indeed, that the company may not have.

Any new non-financial reporting requirements must be very clear in their desired aims and outcomes, to avoid being at risk of becoming mere tick-box exercises. The ever-increasing breadth and depth of required topics for disclosure can contribute to a rise in boilerplate disclosures, in particular where companies feel obliged to report on issues which they believe are simply not material to their business, but which are demanded by investors, regulators or other stakeholders. There are further challenges for companies, which are addressed in more detail below.

Q2. What challenges, or costs, if any, does the preparation, disclosure and distribution of non-financial information create for your company?
Please consider the aspects which are difficult to comply with, the cost related to compliance or the production of information.

The underlying data and information that needs to be collected, aggregated and analysed for non-financial reporting can often be more difficult to measure than the underlying data and information used in financial reporting. Companies' processes for measuring, collecting and handling such data are less developed, and they may struggle to quantify and to identify metrics for certain non-financial information. In addition, the processes of assurance and verification for non-financial information are significantly more challenging.

The resources required to fulfil reporting obligations can be significant. There is concern amongst our members as to the ever-increasing length of annual reports, and that these documents are expected to stretch to accommodate more and more information year by year. Much of this increase is driven by non-financial reporting. The risk is that material information, specific to a company's particular business model, can become lost within a sea of required, but fundamentally less significant, disclosures. The various voluntary frameworks and standards with which companies can choose to comply in preparing their non-financial information can muddy the waters further, particularly as these evolve and where they result in overlap or duplication.

Q3. What, if any, are the key drivers of cost when having to comply with non-financial reporting requirements?
Please respond in line with the following considerations listed below:
Staff costs;
Time costs;
Production costs;
IT infrastructure costs;
Any other relevant costs.

All of the above considerations are considerable drivers of costs for our members. In particular, non-financial reporting places a resource and time burden on senior management. It is right and important that management attention is spent on reporting – but this should not unduly redirect attention away from business matters.

The same can be said for the board. In this year's version of our annual Boardroom Bellwether (publication forthcoming), the Institute asked Company Secretaries from FTSE 350 companies whether increasing reporting requirements are reducing the time available for strategic discussions at board level. 81% of respondents believe that they are, to some or to a large extent. 55% of the FTSE 100 respondents and 65% of the FTSE 250 respondents indicated that reporting requirements reduce the time available to some extent, whilst 17% of the FTSE 100 and 30% of the FTSE 250 signalled that time is reduced to a large extent. This implies that there is a (largely unsurprising) relationship between the size of the company and how onerous they perceive reporting requirements to be – likely due to the availability of in-house experience, established non-financial reporting processes, and human resource. It also emphasises that the time spent on reporting is time that cannot be spent on other strategic or business-critical matters.

Beyond the costs associated with the time and resource spent on reporting, there are also production and IT costs. These include the design costs, printing and postage, as well as the cost of converting a text document into website pages and tagging it. Despite these costs, the Institute maintains that it is important for annual reports to continue to be provided both in print and online. Nevertheless, there are certain non-financial topics, specific to a company's particular business model and the risks to which it is exposed, which may be well-suited to online disclosure on a company's website, rather than needing to be included in its annual report.

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

Please explain your answer:

The volume of information which companies are expected to provide can create significant amounts of work, within short timeframes, for all sizes of company; although larger companies have more resources, they are typically asked for more data. Whilst some of the benefits of non-financial reporting are felt by business, many are mostly for the benefit of investors and other stakeholders. Our members have described preparing non-financial information as “a compliance cost of doing business”. As such, the focus of non-financial reporting regulation should be on ensuring not only that investors have access to consistent, comparable, decision-ready information, but also that companies have proportionate reporting burdens. The keys means for achieving this is to give companies the ability to focus on what is material for their own business, and to ensure that adequate support, guidance and time is provided for the implementation of new reporting requirements. This is not to say that companies need to be given carte blanche – indeed, there is certainly a significant amount of non-financial information which is highly important for both strategic and financial reasons. The Institute believes that reporting ought to go beyond mere compliance and instead be outcome-oriented.

Q5. To what extent do the Companies Act non-financial reporting requirements align with other regulatory requirements your company might be in scope of?
For example these might include requirements that are set by the Financial Conduct Authority (FCA) and the Prudential Regulatory Authority (PRA) (or other regulators).

As this depends largely on the specific sector and type of organisation, we cannot provide a comment which accurately reflects the myriad regulatory requirements that apply to all of our members. There are a wide variety of requirements from different stakeholders, including the requirements under the Companies Act, the Corporate Governance Code and the FCA’s listing rules, and our members would benefit from such requirements becoming better aligned and streamlined where possible. In addition, despite Brexit, many UK listed companies continue to have to comply with EU regulatory and reporting requirements, and many, especially larger companies, also have to comply with US and other regulatory and reporting requirements, either as a result of the extra-territorial reach of these requirements, or by virtue of the companies’ own areas of operation and investor base. Resources which support a better understanding of the relationships between different requirements are welcome, as they enable companies to pick up on areas of overlap or divergence. This facilitates more streamlined reporting and less duplication.

The following questions are aimed at all respondents.

Q10. 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?
You may wish to consider:
The merits and disadvantages of individual requirements;
The level of difficulty in using or preparing certain types of non-financial information;
Whether there are opportunities to rationalise or simplify reporting requirements.

Our members have emphasised that the most important change the government could make would be the streamlining, alignment and simplification of non-financial reporting requirements. This extends not only to UK requirements, but also to EU and other requirements wherever possible, in so far as they often apply to large UK listed companies.

In this year's Boardroom Bellwether, the Institute asked Company Secretaries from FTSE 350 companies how difficult their companies find it to meet non-financial reporting requirements which relate specifically to ESG topics. Overall, two thirds (66%) of respondents reported that meeting these requirements is fairly difficult, whilst 15% of respondents stated that it is very difficult, meaning that a total of 81% find it at least somewhat challenging. Another 15% of respondents answered that it is fairly easy to meet ESG-related reporting requirements, but none said that it is very easy. Our members have regularly told us that they face a number of challenges when preparing non-financial information, including collecting and accessing the right data across such a diverse range of topics, choosing and adhering to the most appropriate reporting framework, and securing the appropriate levels of assurance and verification.

Notably, the Boardroom Bellwether also includes a 'regulation wishlist', which is compiled from respondents' answers to the question 'What areas of regulation would you most like to see change?'. Regulation regarding non-financial reporting, specifically ESG-related, came top of the list both this year and last year. 30% of respondents stated that they are seeking greater clarity, consistency and harmonisation on ESG-related reporting. This gives a clear articulation of the need for change.

Alongside the requests for greater harmonisation, our members stress the importance of proportionality. As the demands for non-financial information increase, our members are keen for the reporting burden to be reduced in other areas wherever possible.

Q11. 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?
You may wish to consider whether additional information is required to support decision making (such as Transition Plans and Green Taxonomy disclosures covered by the recently published [Mobilising Green Investment: 2023 Green Finance Strategy]).

Companies already report extensively on their greenhouse gas emissions, as well as their performance towards near-term science-based targets. This information is crucial for investors and stakeholders to evaluate progress towards a net zero transition, although this does beg the question as to whether it is appropriate for them to do so. Similarly, many larger companies have published net zero pledges and we are seeing this evolving from mere ambitions into more detailed transition plans, complete with milestones and targets. Amongst the respondents to this year's Boardroom Bellwether, 43% have published a transition plan, whilst another 39% have one in development. Only 8% had neither a pledge not a transition plan. This indicates, at least amongst the very largest companies, that stakeholder demand for this information is there and that companies are responding to it.

Nevertheless, companies will require more support in producing such disclosures. The Institute welcomes the work of the Transition Plan Taskforce and was encouraged by the overwhelmingly positive response to its consultation on the Disclosure Framework and Implementation Guidance. We are hopeful that the publication of these in their final form, complemented by further resources and case studies, will support companies in creating more consistent, decision-ready disclosures about their transition plans.

Amongst our members, there are areas of concern about disclosures relating to net zero. For example, reporting on emissions at a country or legal entity level poses difficulties when companies operating worldwide are capturing emissions from across a global value chain. Additionally, it is challenging to benchmark and report on progress towards long-term net zero targets (although near-term targets are more straightforward). Perhaps more significant is the concern from some companies that the only reason they are reporting some data is to feed the demand from investors and other stakeholders – it is not data that is used for the purpose of managing the company.

Finally, whilst the Institute welcomes the trend towards increasing levels of assurance and verification on non-financial information to improve quality and consistency, the expectation for companies to publish additional information on the quality of, and the methodologies applied to, underlying data can be burdensome.

Q12. How should the standards being prepared by the International Sustainability Standards board (ISSB) be incorporated into the UK's non-financial reporting framework?

You can access the IFRS General Sustainability-related Disclosures here and You can access the IFRS Climate- related Disclosures here

You may wish to consider:

The role that reporting against any of these standards could have in simplifying the UK's legal framework;

The role that reporting against any of these standards could have in guiding the transition to a net zero economy;

The Exposure Drafts for IFRS S1 General Sustainability-related Disclosures and IFRS S2 Climate-related Disclosures first two standards issued by the ISSB.

The ISSB's inaugural standards should, if implemented well, go a long way in allaying the demands for alignment and simplification. The Institute welcomes the transfer of the monitoring responsibilities of the TCFD to the ISSB, which is a logical step given IFRS S1 and IFRS S2 largely incorporate the recommendations of the TCFD.

Additionally, the Institute will be responding to the Call for Evidence from the UK Sustainability Disclosure Technical Advisory Committee on the UK endorsement of IFRS S1 and IFRS S2, which was announced after this Call for Evidence was launched. The guiding principle for the UK endorsement and eventual implementation of these standards ought to be sufficient time and supporting resources for companies to apply them.

Whilst both the TCFD and ISSB have adopted a single materiality approach, EFRAG's ESRS apply a double materiality approach. This means that UK companies with sizeable operations in the EU will be required to provide disclosures under both approaches. It may be, however, that double materiality proves more effective in guiding the transition to a net zero economy, as it emphasises not only environmental risk but also environmental impact.

Q13. 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

Please explain your answer:
You may wish to consider:
The different scope requirements and the ease or difficulty of following these;
Whether there are any size and/or type thresholds that are particularly well targeted, or by contrast, inappropriate or no longer fit for purpose;
Application of exemptions and ease of use;
How thresholds interact with requirements set by other regulators (for example the Financial Conduct Authority and Prudential Regulation Authority).
Please note that there is a separate question on size thresholds (micro, small, medium) as they apply more broadly to the preparation and filing of accounts with Companies House.

When considering reporting thresholds, the Institute's view is that proportional requirements must be balanced against the need for accountability and transparency at all levels and sizes of businesses. Thresholds need to strike a fine balance between stakeholder demands and the burden on companies, and particular attention must be paid to companies' capacity to produce meaningful disclosures, rather than falling into the trap of boilerplate reporting when confronted with requirements which are too onerous. Overall, the variety of size thresholds applied to non-financial reporting do not currently provide companies with enough clarity.

For example, the change in the threshold for small companies, from fewer than 50 employees to fewer than 500, as announced in October 2022, had the opposite effect of streamlining and simplifying reporting thresholds. It was intended to remove 40,000 businesses from certain reporting requirements and is now applied to all new regulations under development and also regulations under review. The Institute is largely in favour of reasonable changes (in an upwards direction) being made to company size thresholds. However, such changes can introduce extra complexity. In this example, the changes have not meant a blanket exemption from requirements and are able to be overridden in various cases – meaning that companies have to navigate different thresholds for different reporting requirements.

Additionally, for companies with subsidiaries, our members believe that these subsidiaries should be exempt from reporting where this is undertaken at the holding company level – which in many, if not most, cases it is. This would avoid duplication and the significant costs associated with the preparation and disclosure of non-financial information for a subsidiary company for whom, effectively, it is meaningless. Finally, the Institute eagerly awaits clarity on the thresholds for public interest entities (PIEs), which will have significant implications for private companies' reporting and audit.

Q14. 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*.*
Do these size thresholds remain appropriate?
☐ Yes
☐ No
☒ Don't know
Please explain your answer and what, if any, changes you would like to see.

Whether these thresholds are appropriate could likely be the topic of an entirely stand-alone consultation. According to the latest Business Statistics from government (a research briefing published in December 2022), 74% of businesses have no employees, whilst 26% of businesses are employers. Over 99% of UK businesses are SMEs (including micro), employing 0 – 249 people, which together account for 61% of UK employment and 51% of business turnover. Micro businesses are 95% of UK businesses, but only account for 32% of employment and 19% of turnover. 8000 large businesses account for just 0.1% of the business population, but support 39% of jobs and 49% of all business turnover. Changes to reporting thresholds, therefore, would likely be mostly impactful for those few, but economically significant, companies at the upper end of the SME range and the lower end of the large category.

The Institute is of the view that any changes to these (now rather familiar) thresholds should be made wholesale, rather than piecemeal tweaks, and should apply as universally as possible, in order to give companies clarity and consistency. Such changes would require significant industry input and long lead times. Whether or not such changes are made, the central concern of our members is that such thresholds should not function as 'cliff edges'. For example, for those at the upper end of the medium threshold, the reporting requirements for large companies can appear sufficiently daunting that they are incentivised to avoid any further growth. There may be options for reducing this effect, without necessarily introducing any further categories which would only contribute to the complexity. For example, a company which moves up a band could be given a year's grace period to implement the additional non-financial reporting requirements that it now faces.

If you would like to discuss any of the above comments in further detail, please do feel free to contact me.

Yours faithfully,

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