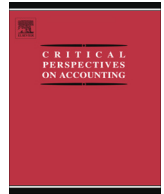


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## Connecting the COVID-19 pandemic, environmental, social and governance (ESG) investing and calls for 'harmonisation' of sustainability reporting



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### ABSTRACT

We critically examine the call for 'harmonisation' of sustainability reporting frameworks and standards that occurred alongside an increase in environmental, social and governance (ESG) investing during the COVID-19 pandemic. We identify three myths that have been promulgated in calls for 'harmonisation' that seek to: simplify sustainability reporting and ESG analysis and shift the control for standard-setting to an investor-oriented private sector body. We argue that the myths are based on deception, misunderstandings, and disregard for both academic research and the views of sustainability practitioners. They demonstrate a lack of regard for different users of corporate sustainability information, a lack of analysis of the alternatives, an overestimation of the International Financial Reporting Standards (IFRS) Foundation's expertise and mischaracterisation of sustainable/ESG financing.

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## 1. Introduction

The COVID-19 pandemic has highlighted the interconnectedness between people, planet and profits – and particularly between health, poverty, climate change and the stability of the global financial system. The pandemic put the 'S' in ESG (environmental, social and governance) under the microscope and provided a reason to re-assess the 'E'. The fragility of supply chains, labour markets, credit quality and liquidity are weaknesses in the financial system revealed by the pandemic (CFA Institute, 2020). And there's increasing concern that climate change could further expose the vulnerability of the financial system and test its resilience (Franklin, 2020)<sup>1</sup>. Further, researchers have drawn connections between biodiversity loss and a greater likelihood of the emergence of new zoonotic infectious diseases in humans (Gibb et al., 2020), suggesting that future pandemics may arise from anthropogenic climate change and deforestation.

There is concern that business, battered by the pandemic-induced financial crisis, might deprioritise costly environmentally sustainable policies and initiatives, undermining planetary survival (see Amankwah-Amoah, 2020). Yet business efforts to be environmentally responsible and more transparent about their sustainability performance during

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<sup>1</sup> There is some evidence of companies stepping away from environmentally friendly commitments and practices to overcome financial pressure brought about by the COVID-19 induced financial crisis (see, for example, Amankwah-Amoah, 2020).

the pandemic-induced volatile, uncertain, complex and ambiguous environment have paid off. This is because environmentally responsible businesses are less exposed to systematic risks (Broadstock, Chan, Cheng, & Wang, 2020; Wellalage & Kumar, 2020). John Streur, Chief Operating Officer of Calvert, a U.S large-cap core responsible investment fund, articulated the link between an ESG focus and corporate performance during the pandemic:

“... it's clear that companies that had been thoughtful about managing other environmental or social risks were ready for any kind of situation and have reacted quite well” (Whieldon, Copley, & Clark, 2020).

Amidst the 2020 pandemic, the flow of funds to sustainable investments reached new heights. Companies with high ESG ratings have earned comparatively higher stock returns and experienced lower volatility (Albuquerque, Koskinen, Yang, & Zhang, 2020; Broadstock, Chan, Cheng, & Wang, 2020; Whieldon, Copley, & Clark, 2020). In contrast, low-sustainability focussed funds have under-performed (Ferriani & Natoli, 2020; Pastor & Vorsatz, 2020)<sup>2</sup>. Funds with lower environmental and governance risks attracted the most investments and achieved greater stock returns (Broadstock et al., 2020; Ferriani & Natoli, 2020).

According to the Society of Pension Professionals<sup>3</sup>, 40 per cent of members responding to their survey claim that work-based pension schemes made at least some change in their approach to ESG as a direct or indirect result of the pandemic, while many others have started showing a genuine interest in ESG (Riley, 2020). The CFA Institute (2020) characterise this phase of ESG investing as ‘mainstreaming’, highlighting that ESG analysis has transformed from a niche investment strategy and the reserve of investors with ethical probity to a mainstream activity (CFA Institute, 2020). Pastor and Vorsatz (2020, p. 791) argue that the increased interest by investors in ESG aspects of companies during the pandemic “suggests that they view sustainability as a necessity rather than a luxury good”.

This increased interest in ESG has resulted in some investors seeking simpler ways of assessing sustainable development issues through comparable and consistent of metrics. This has intensified calls for the reduction in the number of sustainability reporting frameworks and standards (see, for example, Hume & Sanderson, 2020; Tett, 2020). Further, a brand-new industry has emerged, providing ESG data, ratings and rankings for the benefit of investors. These agencies are demanding more consistent and comparable ESG disclosure from companies leading to a frenzy of activity seeking to ‘harmonise’ the proliferation of frameworks, standards and national regulations for reporting this information.

More and more companies are seeking ESG credentials, publishing sustainability reports, and demonstrating their impact on sustainable development and contribution to the achievement of the United Nations Sustainable Development Goals (SDGs) (KPMG, 2018; van der Waal & Thijssens, 2020). However, while companies have broadened their thinking about value beyond profit in recent years, the discourse around the ‘harmonisation’ of ‘sustainability reporting’ has narrowed from value creation for the organisation and society to one of ‘enterprise value creation’ (Impact Management Project, 2020b).

Calls for ‘harmonisation’ of sustainability reporting practices by Accountancy Europe (2019, 2020), International Federation of Accountants (2020), International Financial Reporting Standards (IFRS) Foundation (2020a), the Impact Management Project (2020b) and World Economic Forum (2020) were fuelled by a plethora of newspaper (particularly the *Financial Times*) and magazine articles referring to the ‘alphabet soup’ of standard-setters (see, for example, Tett, 2020). Several reports (see, for example, Barker & Eccles, 2018, 2019; Accountancy Europe, 2019, 2020; Eumedion, 2020b; International Federation of Accountants, 2020) sought to push for the IFRS Foundation to act to remedy the ‘complexity’ in sustainability standard setting.

Table 1 details the stakeholder group served by each report, the problem it identifies, the proposed solution and the proposed approach to materiality. With the exception of Adams et al. (2020), they exclusively serve the interests of report preparers and investors. Most express concern that a proliferation of reporting frameworks and standards is causing confusion and call for consistency and comparability of information. They call for simplicity for investors and seek to ensure that the body determining required disclosures does so with that in mind.

The Trustees of the IFRS Foundation responded by setting up a Task Force and issuing a Consultation Paper proposing the establishment of a Sustainability Standards Board to sit alongside the International Accounting Standards Board (IASB), rather than by addressing financial statement implications through International Financial Reporting Standards (IFRS Foundation, 2020a). The Consultation Paper emphasised that consistent and comparable information is paramount in sustainability reporting. The possibility of facilitating the harmonisation of existing sustainability reporting frameworks and standards was rejected. It proposed that the sustainability standards provide “sustainability information most relevant to investors and other market participants” (IFRS Foundation, 2020a, p.14).

<sup>2</sup> There is also evidence contradicting these findings. For example, Döttling and Kim (2020) show that funds with high ESG ratings that received higher than average fund flows prior to the pandemic experienced a sharper decline in flows compared to other funds during the COVID-19 induced crisis. Further, Demers et al. (2020) find that after controlling for industry affiliation and accounting- and market-based measures of risk, firm-level ESG scores do not explain stock returns during the COVID-19 crisis period.

<sup>3</sup> The Society of Pension Professionals represents providers of advice and services to work-based pension scheme and their sponsors in the UK.

**Table 1**  
Summary of key materials relevant to the discussion on the harmonisation of sustainability reporting standards.

Report	Main stakeholder group served	Problem they address	'Solution' proposed	Proposed approach to materiality
Allison-Hope (2016) published by Business for Social Responsibility	Sustainability report preparers	What are the main features of sustainability reporting that can improve sustainability performance and enable informed decision making? How can sustainability reporting can be improved?	Proposes a triangular framework which provides a structure for various reporting frameworks to fit together, with a succinct narrative (Key Performance Narrative) at the top and detailed issue-specific disclosure (Key Performance Indicators) at the bottom	Double materiality - ESG information should meet the needs of multiple stakeholders. Hence, the impacts of society and environment on the organisation as well as the organisation's impacts on the society and environment should be disclosed.
Business for Social Responsibility (2018)	Sustainability report preparers	Proliferation of reporting frameworks and standards with varying or conflicting metrics, definitions, and priorities. Information needs of ESG rating and ranking agencies. Differing materiality concerns.	A single unified standard is a not desirable or a practical solution. The solution is "first, to understand in practical terms how the different standards can be used together in combination, and secondly, to undertake a substantial harmonization of disclosures, metrics, and indicators." (p. 1) Public reporting should be adapted to meet the information needs of multiple stakeholders.	Double materiality - ESG information should meet the needs of multiple stakeholders. Hence, the impacts of society and environment on the organisation as well as the organisation's impacts on the society and environment should be disclosed.
Williams and Fox (2018)	The U.S. Securities and Exchange Commission	Investor demand for a wide range of ESG information to understand long-term performance and risk management strategies of public-reporting companies.	"Calls for the Commission to initiate notice and comment rulemaking to develop a comprehensive framework requiring issuers to disclose identified environmental, social, and governance (ESG) aspects of each public-reporting company's operations" (p.1) Supports standardised ESG disclosure to meet the calls of large asset managers.	Financial materiality - "what is material depends on reasonable investors' perceptions of what information is already available in the market, and how any new or omitted information changes those perceptions of the quality of management, when voting or engaging with management, or the value of a company or its shares, when investing or selling." (p. 6)
Barker and Eccles (2018)	Investors	"Inadequate ESG information" (p.12) and "an absence of ESG reporting standards" (p.13)	Consider whether FASB and the IASB should set "non-financial" reporting standards.	Defines materiality with respect to the decision-making needs of investors.
Corporate Reporting Dialog (2019)	Report preparers	Improve the coherence, consistency and comparability of the frameworks and standards.	Suggests ways of improving stakeholders' understanding of connections between the five main frameworks and standards and how the connection between ESG and financial information can be better articulated.	Different frameworks and standards have different approaches to materiality.
Singh and Peters (2019) published by the CFA Institute	Report preparers and users and corporate regulators	Whether to reduce periodic reporting requirements for companies from quarterly to semiannually.	"specific ESG and sustainability disclosures should be a regulatory requirement for public companies and that securities regulators should either develop ESG disclosure standards or support an independent standard setter (i.e., a single, global standards setter in this field) to develop such standards" (p.3)	Not discussed but financial materiality is assumed.
Barker and Eccles (2019)	Market participants	"Corporate accountability matters" and "regulation has not kept pace." (p.1)	FASB and the IASB set Non-Financial Reporting Standards	Materiality defined with respect to the decision-making needs of investors.

(continued on next page)

Table 1 (continued)

Report	Main stakeholder group served	Problem they address	'Solution' proposed	Proposed approach to materiality
Accountancy Europe (2019)*	IFRS Foundation, European Commission, report preparers and investors	"...proliferation of initiatives has overwhelmed stakeholders, and risks greenwashing the system" (p. 2)	"... interconnected standard setting for corporate reporting to coordinate, rationalise and consolidate the many non-financial reporting initiatives..." (p. 2)	"... the impacts a company has on society and the environment can also affect its ability to create long-term value." (p. 12)
Accountancy Europe (2020)*	IFRS Foundation, European Commission, report preparers, investors	As above	A 'system solution' and 'building blocks' approach involving a core set of global metrics plus collaboration across existing framework/ standard setters	Issues that affect long-term value creation plus wider impacts
Adams et al. (2020)*	Organisations society and the environment	Lack of deep change to achieve sustainable development	Alignment with the International <IR> Framework, GRI Standards and TCFD recommendations with a focus on the SDGs. Disclosures on management approach, strategy, governance oversight and performance and targets. Fundamental concepts of: long term value creation for the organisation and society; sustainable development context and relevance; materiality.	"Material sustainable development information is any information that is reasonably capable of making a difference to the conclusions drawn by: <ul style="list-style-type: none"> <li>• stakeholders concerning the positive and negative impacts of the organisation on global achievement of the SDGs, and;</li> <li>• providers of finance concerning the ability of the organisation to create long term value for the organisation and society." (p. 9)</li> </ul>
Eumedion (2020a, 2020b)*	IFRS Foundation, Dutch Institutional Investors	Difficulty for investors in assessing the link between long term value creation and non-financial performance	IFRS Foundation to establish an International Non-financial reporting Standards Board (INSB). Full scope limited assurance of the 'management report'.	Issues that are financially material for investors – "... we struggled to identify topics that are of paramount importance for other key stakeholders of a company, and would not qualify as financially material for investors" (p 7–8)
International Federation of Accountants (2020a)*	IASB, IFRS Foundation and members of accounting bodies	Need for "...consistent, comparable, reliable, and assurable information relevant to enterprise value creation, sustainable development..." (p. 1)	IFRS Foundation to create an International Sustainability Standards Board adopting a 'building blocks' approach drawing on existing frameworks/ standards	Considered with respect to enterprise value creation and corporate impacts on sustainable development etc.
Impact Investing Institute (2020)	Consumers, investors, civil society, policy makers	Addresses the need for "transparent, consistent, comparable reporting of environmental, social and economic outcomes" (p. 2)	An international governance body "to develop and house global standards" (p. 2) "...improvements to data availability, methodology and technological solutions" (p. 2)	Materiality for enterprise value creation plus topics that are material for society, the environment and the economy that are <i>not</i> yet material for enterprise value creation.
Impact Management Project (2020)*	CDP, CDSB, GRI, IIRC, SASB and their users	"Confusion among producers and users of sustainability information" (p. 2)	"... help resolve this confusion and to show a commitment to working towards a comprehensive corporate reporting system" (p. 2)	Materiality defined with respect to both the organisation's impacts and 'enterprise value creation'. introduces 'dynamic materiality' – "Sustainability topics that a company once considered immaterial for disclosure can become material based on evidence of an organisation's impacts on the economy, environment and/or people." (p. 4)

Table 1 (continued)

Report	Main stakeholder group served	Problem they address	'Solution' proposed	Proposed approach to materiality
Department for Business Energy & Industrial Strategy (2020)	The U.K. government, report preparers	Understand the preferences of UK stakeholders around non-financial reporting standards	Internationally standardised framework or a nationally standardised framework in the absence of an international one to guide the development of nonfinancial reports and allow nonfinancial performance to be benchmarked against peers globally. The international reporting framework should provide flexibility to cater to local requirements.	'Core and more' model of materiality, possibly adopting dual materiality perspective—having a core set of mandatory disclosures.
World Economic Forum (2020)*	Report preparers and investors	Enhance transparency and alignment. Metrics need to be capable of verification.	Reporting of 21 core 'metrics' focussing primarily on activities within the organisation's own boundaries.	Materiality defined with respect to key stakeholders and the company.
SEC Investor Advisory Committee (2020)	Asset owners, asset managers, ESG data providers	Lack of material, comparable, consistent information available upon which to base investment decisions	Update the reporting requirements of issuers to include material, decision useful, ESG factors	"Materiality being demanded by investors" (p.4) "information upon which investors can rely to make investment and voting decisions" (p.6)
United States Government Accountability Office (2020)	The U.S Securities and Exchange Commission	The quality and consistency of reporting on ESG matters is poor. Improve public companies' disclosure of ESG information to satisfy the needs of large asset managers and investors.	No solution is proposed. The report provides perspectives of investors regarding ESG information needs, explains ESG disclosure practices of public companies in different industries, explains how SEC staff assess the effectiveness of review of public company disclosures, and identifies policy options.	Information that provides "investors with insight regarding the company's assessments and plans for addressing material risks to its business operations" (p.35)
IFRS Foundation (2020a)	Investors, companies, central banks, market regulators, public policy makers, auditing firms	"...urgent need to improve the consistency and comparability in sustainability reporting" (p. 4)	"...create a new Sustainability Standards Board (SSB) under the governance structure of the IFRS Foundation to develop global sustainability standards..." (p. 8)	"... sustainability information most relevant to investors and other market participants" (p. 14) Commencing with a "double-materiality approach would substantially increase the complexity of the task and could potentially impact or delay the adoption of the standards" (p. 14)

Note: The reports included in this table are only those relevant to the harmonisation of sustainability reporting standards and frameworks published up to the release of the IFRS Foundation Consultation Paper.

\*Referenced in the IFRS Foundation (2020a) Consultation Paper.

Five-hundred-and-seventy-seven comment letters were received in response to the consultation questions. Based on an (unpublished) review of responses to the first three questions concerning whether the IFRS Foundation should establish a Sustainability Standards Board, IFRS Foundation (2021, p. 1) concluded:

"The responses indicate growing and urgent demand to improve the global consistency and comparability in sustainability reporting, as well as strong recognition that urgent steps need to be taken and broad demand for the IFRS Foundation to play a role in this."

The IFRS Foundation Trustees plan to produce a definitive proposal (including a road map with timelines) concerning the establishment of the Sustainability Standards Board (IFRS Foundation, 2021).

The 'harmonisation' calls appear to be driven by a desire to remove control of sustainability reporting standard-setting away from a multi-stakeholder process (as used to develop the Global Reporting Initiative's [GRI] Standards) to one led by an accounting standard-setter established to serve investors' needs (without an evidence-based examination of what that means for sustainable development). To support these calls several myths have been promulgated. We examine

these myths next, how they have been promulgated, and some of the arguments against them, including some that have been voiced on social media.

## 2. Myths supporting the call for harmonisation

The literature is full of examples of the political nature of accounting practices, mandatory reporting requirements and voluntary disclosure initiatives (see, for example, Adams & Harte, 1998; Adams & McPhail, 2004; La Torre, Dumay, Rea, & Abhayawansa, 2019; Rowbottom & Locke, 2015). There are also documented accounts of accounting being used to serve vested interests or to drive efficiency and, hence, profit (Loft, 1986; Miller & O'Leary, 1987). In addition to the political, self-interested and profit motives, policy and practice in sustainability accounting and reporting is influenced by ignorance about the nature and complexity of the issues, a desire for legitimacy with stakeholders and impression management or greenwashing (McPhail & Adams, 2016; Humphrey et al., 2017; Liu et al., 2017; Narayanan & Adams, 2017). It should be no surprise then that the debate around the future of sustainability reporting is fraught with political manoeuvres, platitudes with dissent behind closed doors, half-truths, misleading statements, meaningless compromises and disrespect for contributions to date.

Here we focus on three myths and misunderstandings promulgated by various parties (see Table 1) since 2018 and intensified during 2020 in the quest for harmonisation:

1. There is an urgent need for a *global* sustainability standard-setting body (and it should be set up under the IFRS Foundation);
2. Financial materiality should be paramount in the determination of what to disclose; and
3. Consistent and comparable metrics should be a priority.

**Table 2**  
Characteristics and influence of main sustainability standards/framework setters.

Sustainability standards/framework setter	Foundation date	Purpose	Approach	Materiality focus	Take up*
Global Reporting Initiative	1997 (the first version of GRI guidelines launched in 2000)	Promote transparency and open dialogue about impacts and create a future in which reporting on impacts is common practice by all organizations (GRI, 2021).	<ul style="list-style-type: none"> <li>• Principles based</li> <li>• External reporting and organisational change (Promote sustainability considerations to be incorporated in the management approach, strategy and governance oversight)</li> </ul>	Double materiality	67% of N100 73% of G250
International Integrated Reporting Council	2010 (the first version of the International <IR> Framework was issued as a prototype in 2012)	Promote communication about value creation, preservation and erosion to improve the quality of information available to providers of financial capital to enable more efficient and productive allocation of capital (IIRC, 2021).	<ul style="list-style-type: none"> <li>• Principles based</li> <li>• External reporting and organisational change (Promote flow of connectivity of information into management reporting, analysis and decision making via the practice of integrated thinking)</li> </ul>	Financial materiality	37% of N100 50% of G250 <sup>#</sup>
Sustainability Accounting Standards Board	2012	"To establish and improve industry specific disclosure standards across financially material environmental, social, and governance topics that facilitate communication between companies and investors about decision-useful information" (SASB, 2021, p. 1).	<ul style="list-style-type: none"> <li>• Rules based</li> <li>• External reporting only</li> </ul>	Financial materiality	
Climate Disclosure Standards Board	2007 (the first edition of the CDSB Framework was published in 2010)	Provide investors with decision-useful environmental information via the mainstream corporate report, enhancing the efficient allocation of capital (CDSB, 2019).	<ul style="list-style-type: none"> <li>• Rules based</li> <li>• External reporting only</li> </ul>	Financial materiality	

\*Source: KPMG Survey of Sustainability Reporting 2020. KPMG (2020, p. 4) defines N100 as a "worldwide sample of 5200 companies comprising the top 100 companies by revenue in each of 52 countries and jurisdictions" and the G250 as the "world's 250 largest companies by revenue as defined in the Fortune 500 ranking of 2019". The sample from which the data was obtained to generate the statistics in this column includes 3983 N100 companies and 239 G250 companies (KPMG, 2020).

<sup>#</sup> The KPMG Survey provides adoption rates for sustainability reporting guidelines and standards. The statistics provided here apply to all other sustainability guidelines or standards except for GRI guidelines/standards and stock exchange guidelines. The true adoption rates for the three standard setters are likely to be less than what is stated in this cell.

An early contribution to these myths was [Barker and Eccles \(2018\)](#) Green Paper titled *Should FASB and IASB be responsible for setting standards for nonfinancial information?* with “for it to be most useful for investors” added on the title page. Although it claims to examine the question in a ‘neutral way’, the question itself is not neutral. The possibility of the GRI Standards becoming mandatory is not a proposition they entertained. The GRI Standards are the oldest, most used<sup>4</sup>, and the only ‘sustainability’ reporting standards that focus on the impact of the organisation on society and the environment (see [Table 2](#)). Others, such as Sustainability Accounting Standards Board (SASB) Standards, are concerned with sustainability issues only as they affect enterprise value or financial materiality.

[Barker and Eccles \(2018\)](#) also make assumptions about what an ‘investor perspective’ is and assume it should be paramount<sup>5</sup>. They argue that a standard must be ‘discriminating and prescriptive’. This is not the nature of standards that, for example, require disclosure of the process undertaken to identify material impacts on sustainable development. Further, ‘discriminating and prescriptive’ standards would not provide investors with information needed to assess a company’s response to systemic risks – though they would meet their calls for simplification. The point being, that apart from not being homogenous, investors are not in the best position to judge what they need, as opposed to what they can get cheaply and simply.

Since the [Barker and Eccles \(2018\)](#) Green Paper, there have been several other reports (see [Table 1](#)) contributing to the myths and, as noted earlier, with the aim of promoting the IFRS Foundation as the standard-setter for ‘sustainability reporting’. We discuss these myths below.

### 2.1. Myth 1: There is an urgent need for a global sustainability standard-setting body (and it should be set up under the IFRS Foundation)

IFRS Foundation Trustee Teresa Ko points to the success of the IASB and its forerunner, the International Accounting Standards Committee, in harmonising different national financial accounting and reporting approaches ([IFRS Foundation, 2020b](#)). But her comparison of that situation with sustainability reporting is inappropriate. Guidance on sustainability reporting started at the global level through the GRI in the late 1990s (before the establishment of the IASB). In the 1990s, sustainability reporting practices differed significantly across countries, even in Europe ([Adams, Hill, & Roberts, 1998](#)). The [KPMG \(2020\)](#) study shows that two decades of GRI Standards (and their predecessor Guidelines) have served to harmonise these variations in topics covered in sustainability reporting globally.

As discussed in the introduction, the mainstreaming of ESG analysis in investing has heightened calls for greater simplicity and consistency and harmonisation of reporting frameworks (see, for example, [Allison-Hope, 2016](#); [Business for Social Responsibility, 2018](#); [Accountancy Europe, 2020](#); [Department for Business Energy & Industrial Strategy, 2020](#); [Impact Management Project, 2020b](#)). Interestingly, these calls and accompanying research do not explicitly call for a single set of standards but intend to prompt elimination of overlaps, confusions and redundancies between existing standards, guidelines and frameworks. For instance, [Business for Social Responsibility \(2018, p.1\)](#) calls for the standards and framework setters to work together to build a framework for using different standards together and to “undertake a substantial harmonisation of disclosures, metrics, and indicators.” However, they note: “we do not believe that a single unified standard is a desirable or practical solution” (p.1). The calls for a single set of standards has not been backed by an independent assessment of the merits and demerits of existing sustainability standard-setting bodies and how the proposed Sustainability Standards Board will be superior<sup>6</sup>.

An umbrella conceptual framework for the various global standards would be helpful, and an updated IFRS Practice Statement 1 *Management Commentary* (Practice Statement) could be that conceptual framework by drawing on the International Integrated Reporting (<IR>) Framework with amendments to explicitly refer to sustainable development risks and opportunities. But progress on the update has been very slow - the project has been ongoing since 2017 (IFRS Foundation, n.d.). The current version of the *Management Commentary* (Practice Statement) predates the International <IR> Framework. Explicit inclusion of sustainable development considerations seems unlikely, given the IFRS Foundation’s focus on financial materiality (see Myth 2).

The notion that IFRS Foundation should host a global ‘Sustainability Standards Board’ may stem from a genuine lack of knowledge about the robustness of the governance structure of GRI and a belief that only the IFRS Foundation can muster appropriate mechanisms (presumably through national financial reporting standard regulatory bodies and International Organisation of Securities Commissions [IOSCO]) to make such standards mandatory<sup>7</sup>. The [IFRS Foundation \(2020a\)](#) notes that its three-tier governance structure<sup>8</sup> would be applied to the proposed Sustainability Standards Board. It would be overseen by the IFRS Foundation Trustees (who were not appointed on the basis of sustainable development

<sup>4</sup> The GRI Standards were identified in [KPMG \(2020\)](#) as the most used standard/framework for sustainability or non-financial reporting.

<sup>5</sup> In reality, investors have different views, and this has also come to the forefront during 2020. See, for example, the panel discussion at the Asia Sustainability Reporting Summit in December 2020 <https://youtu.be/bh4AX1Ep8VA>.

<sup>6</sup> [http://eifrs.ifrs.org/eifrs/comment\\_letters/570/570\\_27159\\_CarolTiltIndividual\\_0\\_CommentonIFRSsustainabilityReporting\\_CarolTilt.pdf](http://eifrs.ifrs.org/eifrs/comment_letters/570/570_27159_CarolTiltIndividual_0_CommentonIFRSsustainabilityReporting_CarolTilt.pdf).

<sup>7</sup> There also appears to be a lack of knowledge about where GRI disclosures are made and a belief that they do not appear in annual reports. For example, [Barker and Eccles \(2018\)](#) are incorrect in saying “the format for GRI is a separate sustainability report” (p. 21). GRI disclosures can go anywhere, and a ‘GRI Content Index’ is used to tell the reader where disclosures are located.

<sup>8</sup> See <https://www.ifrs.org/about-us/our-structure/>.

credentials), itself accountable to a Monitoring Board consisting of capital market authorities and securities regulators. But, like Barker and Eccles (2018), the IFRS Foundation's Consultation Paper does not consider the relative strengths of other approaches<sup>9</sup>. The IFRS Foundation has no experience in the discipline of sustainability. The IFRS Foundation Trustees do not consider the merits of a multi-stakeholder perspective, perhaps preferring to reinvent what sustainability reporting is, from an 'investor perspective'<sup>10</sup>, their area of expertise.

## 2.2. Myth 2: Financial materiality should be paramount in the determination of what to disclose

The myth that financial materiality should be paramount in determining what sustainability disclosures to make is perhaps the most troubling of all. It contradicts the view that:

"Sustainability reporting is the practice by which they [companies] disclose their significant economic, social and environmental impacts. This information is critical to inform decisions for a wide range of stakeholders, ranging from employees to policy makers and from customers to investors." (GRI, 2020, p.1)

The IFRS Foundation's (2020a) Consultation Paper does not acknowledge that an organisation's impacts on sustainable development are relevant to investors and proposes that material topics are those that are financially material to investors. This is also the approach that SASB takes (see Table 2). It assumes that there is a subset of sustainable development issues that can be readily translated into financial impacts for an organisation over an unspecified period and that all other sustainable development issues (such as physical risks of climate change or biodiversity loss perhaps) will not erode investor returns. As such, their approach to materiality does not allow identification of material matters that might impact an organisation's ability to create value in the long-term.

The term 'enterprise value creation' was introduced by the International Federation of Accountants (2020) and Impact Management Project (2020b). It is not defined, but the key concern of the Impact Management Project (2020b) appears to be with sustainability-related "drivers of enterprise value creation that are not already reflected and disclosed in the annual financial accounts" (p 4). Accountancy Europe (2019, 2020) stick with the International Integrated Reporting Council (IIRC)'s (2013) notion of long-term value creation, but, along with IFAC (2020), Impact Management Project (2020b) and the Big 4 together with the World Economic Forum (2020), also consider materiality with respect to the impacts of the organisation, for example, on sustainable development, stakeholders and the economy. IOSCO, whose members represent more than 95% of the world's securities regulators and, therefore, inherently investor focussed, calls for sustainability-related disclosures to focus on enterprise value creation. However, it also wants to see disclosures on the dependence of companies on stakeholders and the external environment and "investors' information needs on wider sustainability impacts" (IOSCO, 2021, pp. 1–2). Thus, the IFRS Foundation's (2020a) proposed approach to materiality is even narrower than called for by IOSCO and narrower than the definitions in the papers it draws on (see Table 1).

Some accounting academics (those who view the role of sustainability reporting as informing investors) also promote a utilitarian approach and advocate that sustainability reporting needs to be conceptualised from a financial materiality perspective (Roberts, 2018; Cho, 2020). Patten (2019) reinforces this contention by showing that the 'mainstream' North American accounting journals (taking the Accounting Review as an example) have failed to entertain the possibility that sustainability disclosure could also be understood from a non-functionalist view. The open letter to the Chair of the IFRS Foundation Trustees from 'professors of accounting researching in the field of sustainability accounting and reporting'<sup>11</sup> highlights the IFRS Foundations' lack of engagement with sustainability accounting research (published outside the 'mainstream' North American accounting journals).

The International Accounting Standards Board (IASB)'s focus on financial materiality comes through in a March 2020 board paper on the objective of an updated Management Commentary Practice Statement: "to support primary users in assessing the entity's prospects for future cash flows and in assessing management's stewardship of the entity's economic resources" [emphasis added] (IFRS Foundation, 2020d, p.10). The April 2020 IASB meeting considered a paper on 'resources and relationships' that should be discussed in the Management Commentary, but the list includes natural resources only insofar as the organisation's business model and strategy depend on them (IFRS Foundation, 2020c). Only 46% of respondents to the EU's consultation on the Non-financial Reporting Directive thought that defining materiality as

<sup>9</sup> The GRI, for example, already has an independent Global Sustainability Standards Board and a Due Process Oversight Committee whose members are appointed by an Independent Appointments Committee. Critical to sustainability reporting standards, and achieving the SDGs, GRI is a multi-stakeholder organisation with representation from key stakeholder groups in all governance bodies along with the Global Sustainability Standards Board (GSSB).

<sup>10</sup> The GRI's response to the IFRS Foundation consultation paper, available at [http://eifrs.ifs.org/eifrs/comment\\_letters/570/570\\_27193\\_BastianBuck-GRI\\_0\\_CL41GRI.pdf](http://eifrs.ifs.org/eifrs/comment_letters/570/570_27193_BastianBuck-GRI_0_CL41GRI.pdf), sets out what sustainability reporting means as widely practised, the extent of take up, their importance to investors and the extent of recognition of the GRI Standards by regulators. The GRI's multi-stakeholder approach is critical for sustainability reporting as the GRI defines it, i.e., in terms of the impacts the organisation has.

<sup>11</sup> <https://drcaroladams.net/open-letter-to-the-chair-of-the-ifs-foundation-trustees-from-professors-of-accounting/>.



“information where its omission or misstatement could reasonably be expected to influence decisions that users make on the basis of the financial statements” (European Commission, 2020, p.39) was sufficient for understanding a company’s impacts on society and the environment to a reasonable or very great extent.

The GRI’s response to the IFRS Consultation Paper<sup>12</sup> points out that faith-based and impact investors who were the early supporters and driving force behind the founding of the GRI are more concerned with impacts (e.g., contribution to the achievement of the SDGs) and externalities of their investees. Indeed, investors are diverse with different risk tolerances and time-horizons, and a significant proportion of them expect investee companies to adopt a double materiality focus when determining sustainability disclosure, and it is this approach that is increasingly exhorted by regulators (e.g., European Union’s Nonfinancial Reporting Directive – 2014/95/EU). This indicates that the IFRS Foundations’ (2020a) focus on financial materiality for investors would not have the support and would not guide sustainability reporting that meets evolving regulatory requirements. The double materiality approach of the Impact Investing Institute (2020), published after the IFRS Foundation (2020a) Consultation Paper, holds more promise in this regard. It considers material issues with reference to enterprise value creation plus topics that are material for society, the environment and the economy that are *not* yet material for enterprise value creation. (See Table 1 for a summary of these approaches.)

### 2.3. Myth 3: Consistent and comparable metrics should be a priority

The call by investors for consistent and comparable metrics (Abhayawansa, Eljido-ten, & Dumay, 2018) is consistent with a desire to make things simpler. However, sustainability issues are complex, interconnected, dynamic and uncertain. Michelin and her colleagues<sup>13</sup> in their response to the IFRS Consultation Paper note that attempts to reduce complexity by promoting consistency and comparability will only result in partial and potentially flawed information. The views of practitioners further illuminate the inanity of searching for consistent and comparable metrics. For instance, corporate social responsibility and sustainability reporting consultant Cohen (2020, p. 1) said of the World Economic Forum (2020) metrics:

“This set of metrics further confuses the sustainability reporting landscape and adds zero value to the current best practices that have been established over so many years.”

Zadek (2020, p. 1) takes a different tack, noting:

“we moved from “if you want to manage it, measure it” to “if you are clueless what to do, then measuring it is a good comfort blanket”.

Indeed, fund managers and sell-side analysts do want context. They seek to understand how nonfinancial matters are integrated within an organisations’ business model and strategy, as well as the management approach and governance oversight that supports this (Chen et al., 2014; Abhayawansa et al., 2015; Allison-Hope, 2016; IIRC & Kirkshhoff, 2020). In company valuation processes adopted by fund managers, qualitative nonfinancial information plays an important role in building a coherent narrative of the company (IIRC & Kirkshhoff, 2020; Holland, 2006). In fact, some of the sell-side analysts and buy-side investors interviewed by IIRC and Kirkshhoff (2020) stated that mandatory reporting requirements that standardise disclosure while increasing the quantity would reduce the richness and unique nature of disclosures. Comparable metrics are unlikely to provide material benefits (IIRC & Kirkshhoff, 2020) in any case - those conducting company valuations do not have full faith in company-provided metrics (Abhayawansa, Eljido-ten, & Dumay, 2018). Karina Funk, a portfolio manager and head of sustainable investing at Brown Advisory Inc, notes:

“...for us, sustainability is not an end in and of itself; it is a means by which we turn over more rocks, look at more information, and add a complementary lens in order to gain conviction on a company’s strategy, operations, and prospects for growth.” (Whieldon, Copley, & Clark, 2020).

This approach is not new. Ian Woods, Head of ESG Research at AMP Capital, said:

“More responsive businesses are looking at an issue or a process from a risk perspective and are identifying risks related to sustainability. For example, when a business is looking at risks in its supply chain, ESG issues will come up... Risk ... is one key business issue, another is ability to execute strategy.” (Adams, 2013, p.1)

Olsen (2020, p. 1), Global Lead, integrated reporting at Novo Nordisk, is concerned that the metrics in use are not good enough:

“It is crucial we get the measurements right and what is currently being merged [*or harmonised*] is simply not good enough to drive the change urgently needed to ensure sustainable business performance.” [*emphasis added*]

<sup>12</sup> Comment letters submitted to the IFRS Foundation Consultation Paper can be found at: <https://www.ifrs.org/projects/work-plan/sustainability-reporting/comment-letters-projects/consultation-paper-and-comment-letters/#comment-letters>.

<sup>13</sup> [http://eifrs.ifrs.org/eifrs/comment\\_letters//570/570\\_27415\\_GiovannaMichelonAccountabilitySustainabilityandGovernanceResearchGroupattheSchoolofAccountingandFinanceoftheUniversityofBristol\\_0\\_ASGGroupBristol\\_IFRSconsultation.pdf](http://eifrs.ifrs.org/eifrs/comment_letters//570/570_27415_GiovannaMichelonAccountabilitySustainabilityandGovernanceResearchGroupattheSchoolofAccountingandFinanceoftheUniversityofBristol_0_ASGGroupBristol_IFRSconsultation.pdf)

Allison-Hope (2016), drawing on insights gained from discussions with sustainability practitioners, provides several reasons to show that sustainability metrics can be deceiving. The positive (negative) movements in indicators do not necessarily equate to better (worse) sustainability performance overall. Improvements in one indicator can be offset a worsening in another, which might not have been reported. Indicators cannot be interpreted without an accompanying narrative, as in the example of a company choosing to use seawater rather than freshwater to cool a data centre. This action reduces the environmental impact but results in the total water-use number increasing, leading users to misinterpret the company's action as detrimental to the environment. Also, a company's action to reduce water use in a region where water is in abundance nonsensically places it on a higher environmental pedestal if the focus is on metrics alone.

As noted in our introduction, the growth in ESG investing and pressure on asset managers to integrate ESG risk factors in portfolio construction has created the demand for comparable ESG data and rankings and ratings. A metrics-based approach would benefit ESG ranking and rating agencies and ESG data and index providers who have struggled to compare companies on a common set of ESG indicators (Abhayawansa & Tyagi, 2021; Kotsantonis & Serafeim, 2019). Owing to the superior performance of ESG funds and indices during the current pandemic, it is the voice of these agencies together with asset managers<sup>14</sup> that have been the loudest and conveniently taken to represent the voice of the investor community in general. ESG metrics devoid of accompanying narratives are incapable of painting a comprehensive picture of organisational realities (Mattingly & Berman, 2006; Sadowski et al., 2010).

Privileging metrics reflects a rules-based (as opposed to a principles-based) approach preferred by FASB and SASB. It allows companies to hide material matters that are not specified in the metrics. This was also the case in early iterations of GRI Guidelines prior to the requirement to disclose information on processes (Adams, 2004). It is the requirement to disclose on strategy, management approach with governance oversight that gets organisations thinking about what they do and how they do it (Adams, 2017). A focus on 'metrics' detracts from disclosures that would provide better information to investors about management capabilities and intentions, albeit perhaps requiring more skilled resources to assess.

Rather than focus on consistency and comparability, the *Sustainable Development Goal Disclosure (SDGD) Recommendations* (Adams et al., 2020), call for disclosures on the integration of sustainable development considerations into strategy, management approach, and governance oversight as well as disclosure of performance and targets. The definition of materiality focuses on both long-term value creation for the organisation and society and the impact (positive or negative) of the organisation on sustainable development (or achievement of the SDGs). The *SDGD Recommendations* are SDG specific and align with the International <IR> Framework (IIRC, 2013), GRI Standards and the Task Force on Climate-related Financial Disclosures (TCFD) recommendations (TCFD, 2017).

### 3. Discussion and conclusions

The COVID-19 pandemic has heightened awareness of the risk posed by systemic issues and existential threats, such as climate change, to the stability of the financial system. During the pandemic, investment instruments labelled as sustainable have seen considerable growth, triggering investors and securities regulators to call for greater transparency, comparability and consistency of ESG-related information (IOSCO, 2020). These developments saw the growing momentum for harmonisation of nonfinancial reporting standards and frameworks suddenly being diverted into one for standardisation. Investors' interests have been placed at the centre of this developing discourse. The IFRS Foundation responded by proposing, and later confirming, the establishment of a Sustainability Standards Board to sit alongside the IASB to develop a single set of sustainability standards that would provide financially material sustainability information.

Through our discussion of three myths that lay the foundation for the current 'harmonisation' movement and the establishment of a standards-setting body within the IFRS Foundation we reveal deception, misunderstandings and a disregard for academic research and the views of sustainability practitioners. The myths are fuelled by a lack of analysis of the alternatives, an overestimation of the IFRS Foundation's expertise and mischaracterisation of sustainable development/ESG financing.

The Consultation Paper on Sustainability Reporting issued by the IFRS Foundation highlights (para 17) three contributions (i.e., Accountancy Europe, 2020; Eumedion, 2020a; International Federation of Accountants [IFAC], 2020) that call on it to set sustainability or nonfinancial reporting standards that build on existing frameworks and standards. Building on the work of other standard-setters was "considered the best option of those discussed to assist in reducing complexity and achieving comparability" (IFRS Foundation, 2020a, p.8). However, little consideration was given in the Consultation Paper as to what this might look like or what it might mean for the continued funding of those organisations.

GRI's response to the consultation contains key information that the IFRS Foundation Trustees appear to have been unaware of, and there is no mention of any conversation that had occurred between the Trustees and key people at GRI (such as the Chair of the Global Sustainability Standards Board, the Chief Standards Officer or the Chair of the GRI Board). A key concern in the GRI and other submissions is the lack of a clear definition by the IFRS Foundation Trustees of sustainability reporting. The limitations to knowledge gathering prior to issuing the Consultation Paper might come from

<sup>14</sup> BlackRock and State Street Global Advisors, two of the largest asset managers in the world, are exerting pressure on investee companies to adopt SASB standards and TCFD recommendations, possibly to develop their own proprietary ESG data and tools (see Dubois, 2020).

an assumption that demand by their stakeholders for their intervention was a forgone conclusion. And indeed, this would seem to be a reasonable assumption, based on the myths we discuss and the nature of the first consultation question dismissing other standard-setting initiatives (IFRS Foundation, 2020a, p.15):

“Is there a need for a global set of internationally recognised sustainability reporting standards?”

In taking this approach, the IFRS Foundation Trustees have arguably been disrespectful to other framework-/standard-setters amidst calls for collaboration. Mervyn King notes in his response to the consultation:

“GRI ... is the pioneer on sustainability reporting, but with the realisation of the importance of it, other organisations started occupying this space. Consequently, the formation of other framework providers on sustainability issues. This resulted in a dilution of comparability and confusion for preparers and users.”<sup>15</sup>

GRI is also the only framework-/standard-setter concerned with accountability for an organisation's impact on the environment, society and economy. It responds to the information needs of investors while also meeting other stakeholders' needs<sup>16</sup>. It could be that the creation of ‘The Five’ (i.e., CDP, Climate Disclosure Standards Board (CDSB), GRI, IIRC and SASB) referred to in [Barker and Eccles \(2018\)](#) and the [Impact Management Project \(2020b\)](#) was a convenient way of diminishing the status of the only body driving accountability for impact in favour of an approach more palatable to the likes of the world's largest asset owner BlackRock ([Norton, 2020](#)). BlackRock still invests in fossil fuels ([Jolly, 2021](#)). We would argue that GRI Standards do not go far enough in driving corporate target setting cognisant of planetary boundaries. The United Nations Development Programme's (UNDP) SDG Impact Standards (see [UNDP, 2020](#)) that draws on the SDGD Recommendations ([Adams et al., 2020](#)) seek to change organisational processes and decision making to facilitate contribution to sustainable development. Like GRI Standards, the UNDP SDG Impact Standards address the impact of an organisation and provide additional information relevant to investors.

We contend that the current sustainability discourse has been captured by large asset managers and other players in the ESG investing eco-system whose sustainability motives and credentials are questionable. A financial materiality and metrics-based approach to disclosure is suboptimal, if not misleading. It is detrimental to the long-term sustainability of capital markets and a step backwards from decades of progress that has been made in sustainability reporting. It threatens to make consideration of impact on sustainable development a marginal activity. It is, therefore, not in the public interest.

The regressive impact of the COVID-19 pandemic on the achievement of the SDGs needs to be curtailed ([The Lancet Public Health, 2020](#)). António Guterres, United Nations Secretary-General, urged that: “Everything we do during and after this crisis must be with a strong focus on building more equal, inclusive and sustainable economies and societies that are more resilient in the face of pandemics, climate change, and the many other global challenges we face” ([Guterres, 2020](#), p. 1). Businesses are expected to help ‘build back better’ and ‘reimagine capitalism in the shadow of the pandemic’ (see [Henderson, 2020](#)). It is a time to intensify efforts by business to incorporate sustainable development considerations into strategy, management approach and governance oversight and be accountable for them. Critical accounting scholars are urged to publicly input to the debate and conduct research that makes visible any decline in corporate accountability for, and action on, impact on sustainable development.

Immediately prior to finalising this paper (early March 2021), the IFRS Foundation sent out a short email update on their approach to Sustainability Reporting Standard Setting. A few hours later the European Financial Reporting Advisory Group (EFRAG) working at the behest of the European Union circulated 228-page document ([EFRAG, 2021](#)) on theirs. The latter contains 54 proposals and supporting information. The IFRS Foundation had yet to provide the analysis supporting their approach. The approaches of the two organisations are fundamentally different in all key aspects of approach. Firstly, while the audience for the IFRS Foundation is investors, for EFRAG it is all users of sustainability reporting and affected stakeholders, including with respect to potential future impacts. Secondly, while the scope of the IFRS Foundation is climate first, then ESG, for EFRAG it is sustainable development issues, including the impact of an organisation's products and services and its broader value chain. Thirdly, EFRAG takes a double materiality approach, including material impact of an organisation on sustainable development. The IFRS Foundation is only concerned about information deemed to be material to investors, lenders and other creditors. Finally, the IFRS Foundation will build on the TCFD recommendations and the (conceptually flawed<sup>17</sup>) prototype standard ([Impact Management Project, 2020a](#)) while EFRAG will build on overarching principles that support an inclusive range of stakeholders and initiatives that have similar goals. Our analysis points to the potential of the EFRAG approach facilitating organizational contribution to sustainable development and the IFRS Foundation approach hindering it. But the story does not end here, and these proposals are not yet cast in stone.

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<sup>16</sup> [http://eifrs.ifrs.org/eifrs/comment\\_letters/570/570\\_27159\\_CarolTiltIndividual\\_0\\_CommentonIFRSSustainabilityReporting\\_CarolTilt.pdf](http://eifrs.ifrs.org/eifrs/comment_letters/570/570_27159_CarolTiltIndividual_0_CommentonIFRSSustainabilityReporting_CarolTilt.pdf).

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