
Master in Management

# FINANCIAL AND ESG REPORTING
# Class 2

Fall, 2025

ISEG
Lisbon School of Economics & Management
Universidade de Lisboa

# Objective of this class:

Sustainability and sustainability reporting

Sustainability reporting frameworks

European sustainability reporting standards (ESRSs) and updates

# Reading:

Main reading:

Rankin, M., Ferlauto, K., McGowan, S., & Stanton, P., 2022. *Contemporary Issues in Accounting*. 3rd ed. Australia: Cengage. ISBN 978-0-730-39782-3.

- Chapter 10

Supplementary reading:

Christensen, H. B., Hail, L., & Leuz, C. (2021). Mandatory CSR and sustainability reporting: Economic analysis and literature review. *Review of accounting studies*, *26*(3), 1176-1248.

# Sustainability and sustainability reporting

# From profitability toward sustainability

- From a reductionist focus on profit, toward a holistic perspective and a balance between economic, social and ecological aspects of company's business accountability.

- **Business sustainability** is often defined as the triple bottom line management, a process in which companies manage their **financial**, **social**, and **environmental** risks, threats and opportunities. These three impacts are often called "Profit, People, and the Planet" or **3P** (Elkington, 1994).

# What is sustainability?

- **Sustainable development:**
  - ‘development that meets the needs of the present without compromising the ability of future generations to meet their own needs’.
  - This definition relates to three main areas:
    - economic development
    - environmental development and
    - social development.

# Similar terms

- Sustainability: emphasizes the long-term horizon
- Environmental, social and governance (ESG): explicitly incorporates governance factors, often covering a wider scope
- Corporate social responsibility (CSR): tends to be defined slightly more broadly and normatively
- Triple bottom line: people, planet and profit.

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# An open discussion: why do we need ESG?

# An open discussion: How to achieve it?

# An example: nuclear energy

Corporate report

## Nuclear Decommissioning Authority: Business Plan 2023 to 2026

Published 20 April 2023

**Sites**

| Outcome number | Activity | End date |
|---|---|---|
| 44 | All land delicensed or relicensed | 2135 |
| 45 | All land in End State - all planned physical work complete | 2134 |
| 46 | All land delicensed or relicensed | 2135 |
| 47 | All land in End State - all planned physical work complete | 2333 |


From: https://www.gov.uk/government/publications/nuclear-decommissioning-authority-business-plan-2023-to-2026/nuclear-decommissioning-authority-business-plan-2023-to-2026#preface

# Sustainability reporting

- A **sustainability report:**
  - presents information about the economic value of an entity, and
  - information upon which stakeholders can judge the environmental and social value of an entity.

- Sustainability reports are presented by a large range of organisations from most sectors, including not-for-profit entities and the government sector.

https://www.iseg.ulisboa.pt/sustentabilidade/wp-content/uploads/sites/20/2023/11/Relatorio-de-Sustentabilidade-2022.pdf

# Sustainability reporting

"Sustainability reporting helps organizations to set goals, measure performance, and manage change in order to make their operations more sustainable. A sustainability report conveys disclosures on an organization's impacts – be they positive or negative – on the environment, society and the economy. In doing so, sustainability reporting makes abstract issues tangible and concrete, thereby assisting in understanding and managing the effects of sustainability developments on the organization's activities and strategy."

-- Global Reporting Initiative (GRI 2015, p. 3)

# Sustainability reporting

"…we refer to CSR and sustainability reporting as the measurement, disclosure, and communication of information about CSR or ESG topics, activities, risks, and policies…"

-- Christensen *et al.*, 2021, RAST

# Characteristics of sustainability reporting

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Compare to traditional financial reporting…

- Diversity of users and uses
- Diversity of topics
- Diversity of objective functions
- Diversity in measurement
- Voluntary nature of CSR activities
- Long-term horizon
- Central role of externalities

# Why to develop a ESG Report?

## Financial reporting is not enough!

- They do not reflect the entire business activity of a company.
- Reflects only short-term monetary aspects of business, but does not provide insight into environmental, social, and managerial aspects of business, which are, in the long term, much more important.
- Nonfinancial reporting is a ‘must’ in the modern economy as it reflects the responsibility of a company to conduct business activities in a sustainable way.
- This helps investors, consumers, policy makers and other stakeholders to evaluate the **non-financial performance** of large companies and encourages these companies to develop a responsible approach to business

# Sustainability reporting

- **Benefits:**
  - Embedding sound corporate governance and ethics systems throughout all levels of an organisation.
  - Improved management of risk through enhanced management systems and performance monitoring.
  - Formalising and enhancing communication with key stakeholders such as the finance sector, suppliers, community and customers.

# Sustainability reporting

- **Benefits:**
  - Attracting and retaining competent staff by demonstrating an organisation is focused on values and its long-term existence.
  - Ability to benchmark performance both within industries and across industries.

# Motivation for ESG disclosure

- ❑Signalling future performance
- ❑Reputation insurance
- ❑Reduction in information asymmetry
- ❑Managers’ agency issues
- ❑Information demand
- ❑Costs of CSR disclosure

# Determinants of ESG disclosure-Research evidence (Christensen et al., 2021)

## ❑Generic firm and manager characteristics

- Firm size:
  - Greater public scrutiny, which incentivizes larger firms to engage in CSR activities and reporting
  - Less costly for larger firms

- Ownership structure:
  - Dispersed private-sector ownership (+), concentrated ownership (-), foreign ownership (+)
  - CSR reporting is more prevalent when information asymmetry is high or when firms need to communicate with a larger set of shareholders

# Determinants of ESG disclosure-Research evidence (Christensen et al., 2021)

## ❑Generic firm and manager characteristics

- Corporate governance:
- Robust corporate governance mechanism (long-term incentives schemes, number of board meetings) (+), stakeholder orientation in corporate governance policies (+)

- Managerial characteristics:
- Educational levels and training (MBA + vs. law degree -)
- Compensation (+)
- Career concerns (+) and power (-)
- Whether the CEO has a daughter
- CEO fixed effects explain 59% of the variation in CSR scores, whereas firm fixed effects only explain 23%

# Determinants of ESG disclosure-Research evidence (Christensen et al., 2021)

## ❑Firms' economic activities

- Sin and polluting industries (+)
- CSR performance (+/-)

## ❑External stakeholder and societal pressure

- Institutional investor
- Government and policymakers
- NGOs, customers, employees…

# The different types of report



- **Stand-alone reports** that focus on social and environmental issues
- **Combined reports** that introduce social and environmental issues into the existing financial annual report
- **Integrated reports** that highlight linkages across financial and non-financial information

# Integrated reporting


## What is Integrated Reporting?

*' A concise communication about how an organisation's strategy, governance, performance and prospects, in the context of its external environment, lead to the creation of value over the short, medium and long term.'*

Paul Druckman, CEO of IIRC, 2013

HOW VALUE IS CREATED?
Communicate the full range of factors that materially affect value

The International Integrated Reporting Council (IIRC) defines an integrated report as one that 'brings together material information about an organization's strategy, governance, performance and prospects in a way that reflects the commercial, social and environmental context within which it operate

# Integrated reporting

10 YEARS OF INTEGRATED REPORTING ‹IR›

Concise communication on how organizational strategy and management lead to value creation:


www.youtube.com/watch?v=EFm0sKeBLh0

https://://www.youtube.com/watch?v=Hx4dvrlunpw

# Integrated reporting framework

**2010:** the Prince of Wales' Accounting for Sustainability Project (A4S) and Global Reporting Initiative (GRI) formed the International Integrated Reporting Council (IIRC)

**2013:** the IIRC developed its International Integrated Reporting Framework, known as the International <IR> Framework

- requires information about organisations' strategies, governance, impacts, performance and prospects and aims to 'secure the adoption of integrated reporting by report preparers and gain the support of regulators and investors'

**2021:** <IR> Framework revision

- simplify the required statement of responsibility for the integrated report, improved insight into the quality and integrity of the reporting process and create a clearer distinction between outputs and outcomes

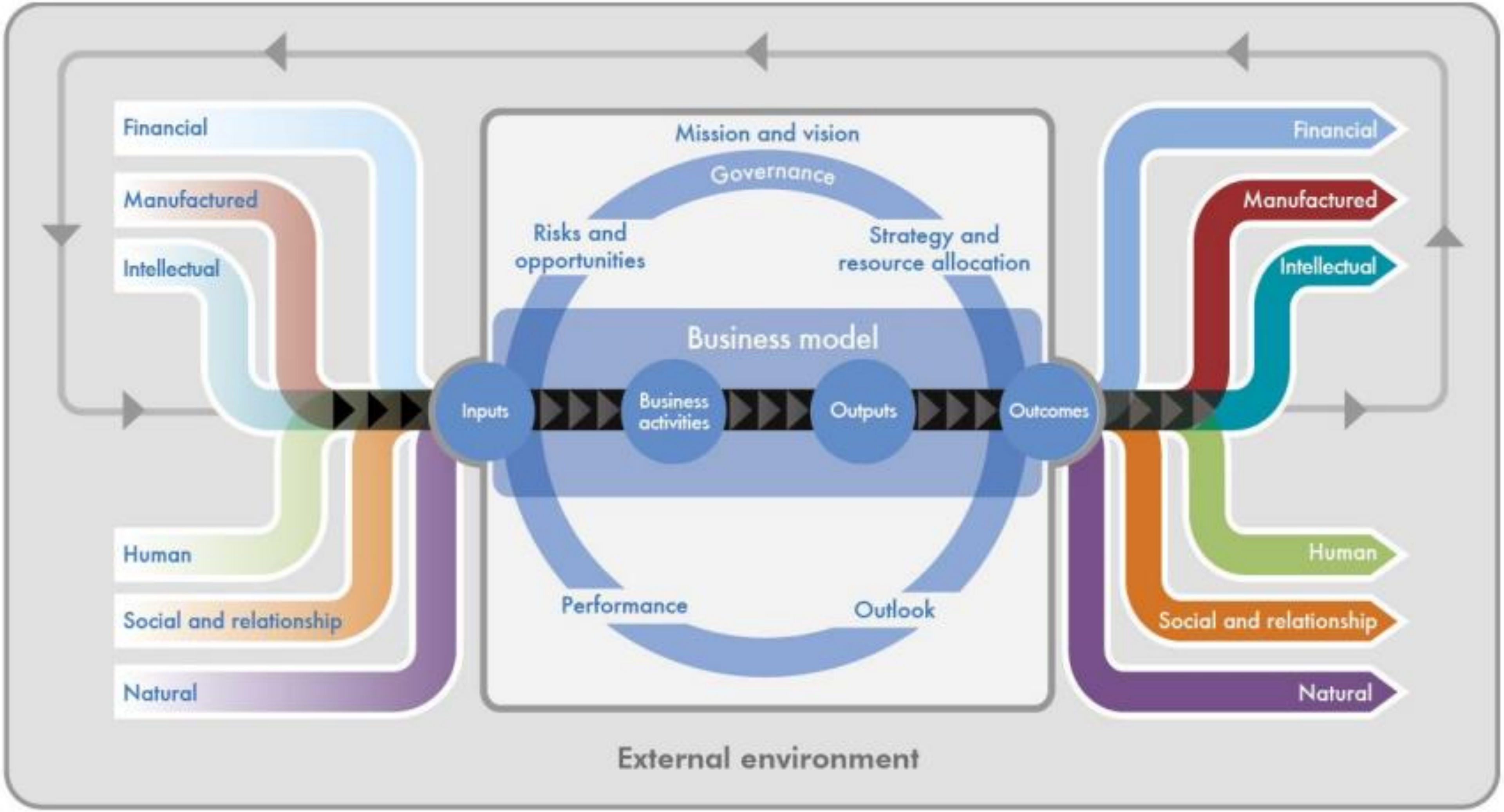
**June 2021:** IIRC merged with the Sustainability Accounting Standards Board (SASB) to form the Value Reporting Foundation (VRF)



# Integrated reporting framework

- Interrelates financial with non-financial reporting to provide an **integrative and comprehensive overview of the business** activities of a company, their results, and consequences for people and the environment.
- While sustainability reports and nonfinancial reports can be disclosed autonomously, an integrated report represents a **single report** that includes not only social and ecological but also economic aspects. In that sense, integrated reports are comprehensive, reflecting a **holistic perspective** on business activity.

# Integrated reporting should provide:




Holistic picture of dependencies between the factors that affect organization’s ability to create value over time.

# Sustainability reporting frameworks

# Sustainability reporting standard and framework

**Why do we need sustainability reporting standards?**

- Standards and frameworks are often advertised as an opportunity to get more **regularity, consistency and comparability** into the voluntary disclosures, but also with the claim to enhance the **materiality** of the disclosures. This implies that the standards and frameworks help organisations focus on the more important and relevant matters while leaving the less important issues with limited or no attention.

# Sustainability reporting frameworks

- Most well-known global guidelines

  GRI, IIRC, SASB

- Some other specific frameworks

  CDP, TCFD

https://view.genial.ly/616cd3a3f1952d0dd5cd4c15/interactive-content-untitled-genially

# Sustainability reporting standard and framework

| | Global Reporting Initiative (GRI) | International Integrated Reporting Council <IR> | Sustainability Accounting Standards Board (SASB) |
|---|---|---|---|
| Founded | 1997 | 2010 | 2011 |
| Aim | To empower decisions that create social, environmental and economic benefits for everyone | Establish integrated reporting and thinking within mainstream business practice as the norm in the public and private sectors | Establish industry-specific disclosure standards across environmental, social, and governance topics that facilitate communication between companies and investors about financially material, decision-useful information |
| Main users for the report | Stakeholders at large | Mainly investors, but also others | Financial markets, investors |
| Key concepts | Materiality, accountability | Integrated thinking, value creation | Financial materiality, decision-usefulness, value relevance |

Source: Tregidga and Laine (2021)

# The Global Reporting Initiative (GRI)

The GRI is the **most used** reporting framework.

- "Today, more than two-thirds of the N100 use the GRI(68 percent) — although this is only a slight increase of1 percentage point from 2020. The corresponding figure for the G250 is 78 percent — an increase of5 percentage points in the past 2 years" (KPMG, 2022)

The GRI guidelines have been rebranded in 2016 and are now called the GRI standards.

While in the early years, the GRI guidelines offered a list of indicators, now the standards prescribe more precisely how companies have to approach the reporting process.

Another important change is that the concept of materiality has increased in importance,

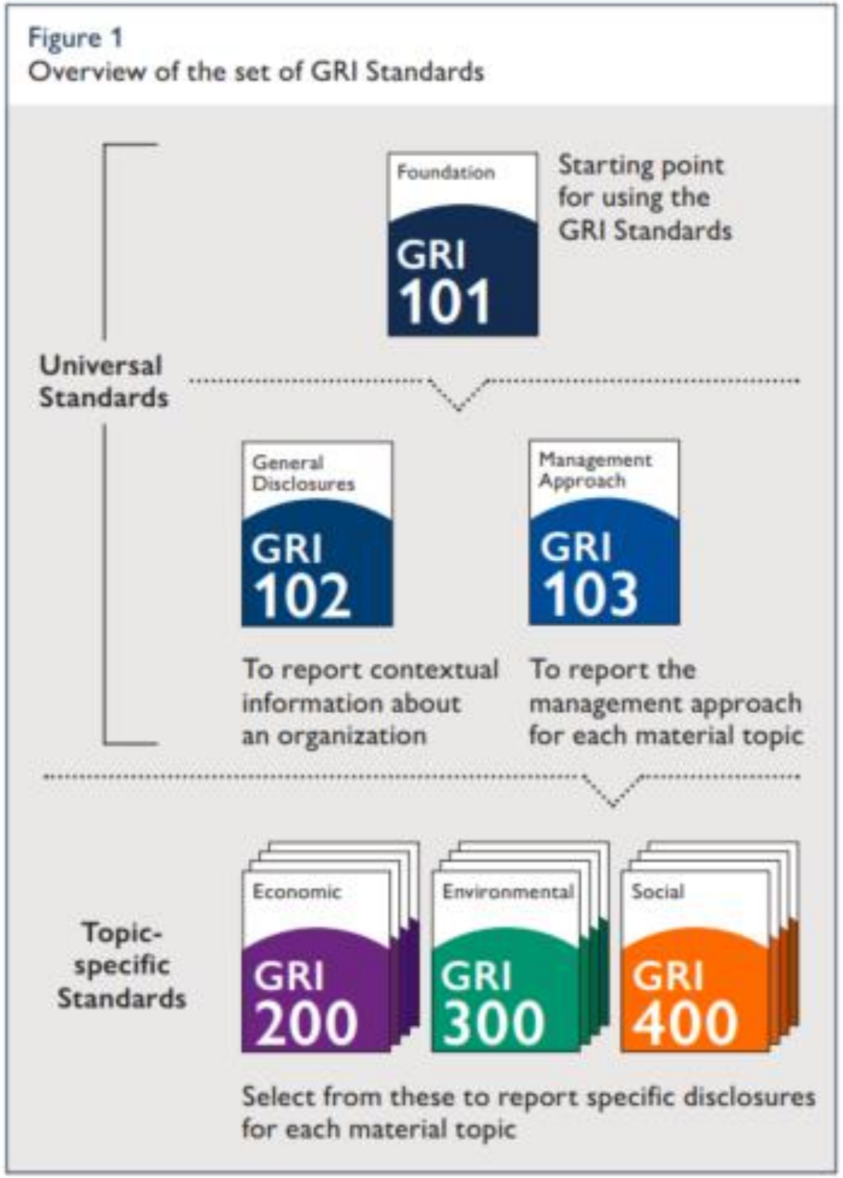
and that companies have to more clearly define which topics are material

- **there are 3 topic specific standards: social, environmental and economic.**

# The Global Reporting Initiative (GRI)

- The underlying idea of the GRI approach has been to **enhance the quality** of sustainability disclosures by standardising the way different organisations report, thereby making the information **more consistent and comparable** both over time as well as across organisations.
- A key role here is played by **materiality analysis**, which has been a core feature of the GRI guidelines since the G4 version published in 2013.
- With materiality considerations at the centre of the reporting process, organisations need to evaluate and focus on the most essential sustainability matters. These are evaluated **not only from the perspective of the organisation's activities, but also from the viewpoint of the stakeholders**.

# What are the GRI standards about?




[Video: The GRI Sustainability Reporting Standards: The Future of Reporting - YouTube]

https://www.globalreporting.org/how-to-use-the-gri-standards/gri-standards-english-language/

Source: GRI standard 101

# Global Sustainability Standards Board (GSSB)

- The GRI Standards are issued by the Global Sustainability Standards Board (GSSB), an independent multi-stakeholder standard setting body created by GRI.
- The role of the GSSB is to ensure that the GRI Standards are developed in the public interest, through a multi-stakeholder, transparent and independent process. The Standards are developed according to due process and all meetings are recorded and available on GRI's website.

# SASB STANDARDS (now part of the IFRS Foundation)

- SASB aims to create sustainability reporting standards that help organisations produce material information to **investors** in a cost-effective way.
- the SASB guidelines aim at simplifying the process, and define material aspects **on the level of the industry**.
- Purpose: help firms cost-effectively identify and manage a well-defined set of key sustainability performance indicators; provide investors with comparable and concise information to aid decision-making.
- SASB Standards enable organizations to provide industry-based sustainability disclosures about risks and opportunities that affect enterprise value. In August 2022, the IFRS Foundation assumed responsibility for SASB Standards when it merged with the Value Reporting Foundation, which previously maintained these Standards.

# SASB STANDARDS (now part of the IFRS Foundation)

- SASB Standards identify the subset of environmental, social and governance issues most relevant to financial performance and enterprise value for 77 industries. The Standards were developed using a rigorous and transparent standard-setting process that included:
- evidence-based research;
- broad and balanced participation from companies, investors and subject-matter experts; and
- oversight and approval from the independent SASB Standards Board.
- Global investors recognise SASB Standards as essential requirements for companies seeking to make consistent and comparable sustainability disclosures.

# SASB STANDARDS (now part of the IFRS Foundation)

- The IFRS Foundation's International Sustainability Standards Board (ISSB) has committed to building on the industry-based SASB Standards and adopting SASB's industry-based approach to standards development. SASB Standards play an important role in the IFRS Foundation's *Climate-related Disclosures Exposure Draft* and *General Requirements for Sustainability-related Disclosures Exposure Draft*. The ISSB encourages companies and investors to continue to support and use the SASB Standards until they are replaced by IFRS Sustainability Disclosure Standards

# Sustainability reporting standard and framework



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Which one do you support?

Source: Tregidga and Laine (2021)

# Friedman vs Freeman

**Friedman (1970s):**

The primary purpose of a business is to maximize its revenue along with its returns to its shareholders.

All other factors, including social responsibilities, are not obligations of a company and are only done if the shareholders decide to do so.

**Freeman (1984):**

businesses do have moral responsibilities that are best served by considering all stakeholders, such as consumers, employees, and communities.

While Freeman is not advocating for ignoring investors, he argues their disproportionate value to the rest of the stakeholders disrupts a company's long-term success.

Source: https://www.texasulj.org/post/the-corporate-purpose-debate-friedman-vs-freeman

# CDP

- CDP is an investor-led initiative, originally founded under the name **Carbon Disclosure Project**, seeking to gather comparable information about corporate actions related to climate change.
- The CDP runs a large **dataset**, which has been collected through annual surveys of large corporations and other large organisations.
- The first Carbon Disclosure Project's survey was launched in the year 2000 and focused on collecting climate-related information from corporations at a time when organisations seldom included such information in their sustainability reports. Since then, CDP has expanded its scope, and it now hosts a large database of corporate information around **climate, water, forests and supply chains, hence the name change**.

# TCFD

- Task Force for Climate-Related Financial Disclosure (TCFD)
- Launched in 2015.
- Focus on providing a framework for reporting the financial implications of **climate-related risks**, opportunities and dependencies.
- Underlying logic: markets are efficient and can hence be useful for solving the global climate emergency. The goal is to have organisations produce consistent, comparable and clear information regarding the financial implications of climate change, and then have markets efficiently evaluate and value the risks and opportunities. It is also pointed out that should the information be misleading, markets will effectively use that information to misallocate capital and thereby hinder societies' aim at curbing global climate risks.

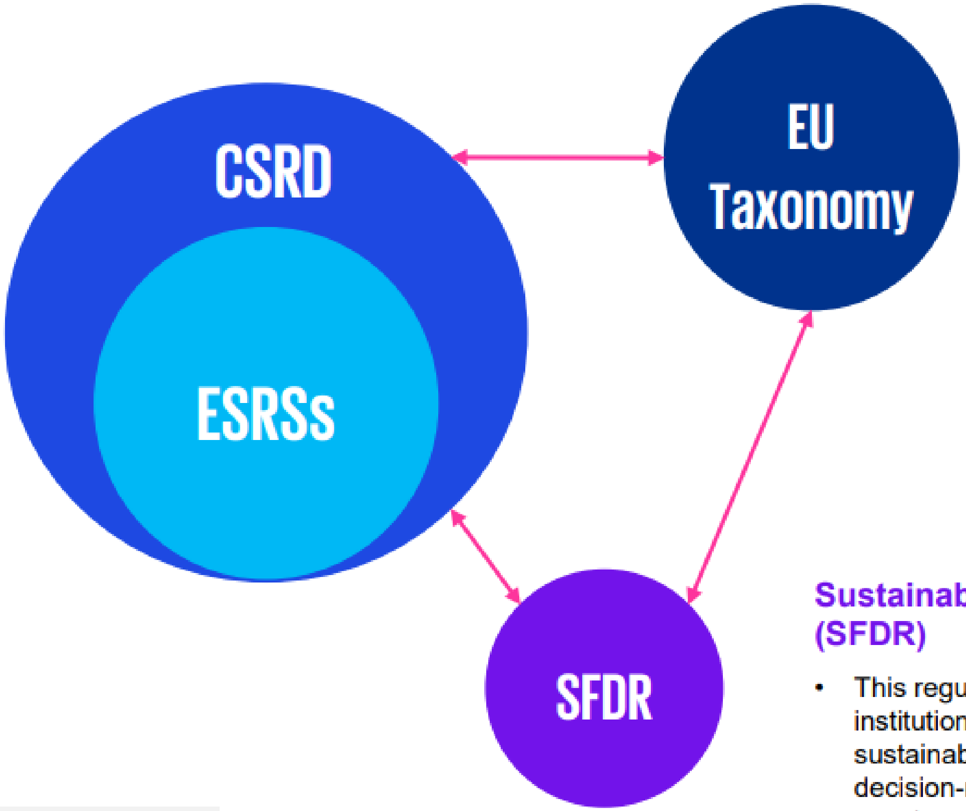
# European sustainability reporting standards

# (ESRSs)

# Legal basis for applying ESRSs

### Corporate Sustainability Reporting Directive (CSRD)

- The CSRD sets out which companies need to report sustainability-related information and when. The ESRSs support this with detailed reporting requirements.
- It is a key component of the EU's sustainable finance action plan[1] – which also includes reporting under the EU Taxonomy and SFDR.
- It requires companies to report on their sustainability-related information with the aim of:
  - providing investors and stakeholders access to necessary information for assessing investment risks related to climate change and other sustainability-related matters; and
  - establishing greater transparency about a company's impact on people and the environment.




### EU Taxonomy

- The EU Taxonomy is a classification system that defines activities deemed to be aligned with a net-zero trajectory by 2050. It aims to help direct investment towards activities that will support the transition to a greener economy.
- As part of the CSRD, in addition to ESRS requirements, companies in scope are also required to report under the EU Taxonomy regulation. This regulation sets out specific KPIs about the extent of a company's sustainable activities.

### Sustainable Finance Disclosure Regulation (SFDR)

- This regulation requires asset managers and other institutional investors to disclose information about how sustainability is integrated into their investment decision-making process. To report this information, asset managers and others captured by the SFDR require data from the companies they invest in.
- ESRSs are designed to provide this information, where material.

The CSRD does **not** apply solely for EU-based companies. Its scoping requirements capture a range of companies, including non-EU companies with significant operations in the EU and non-EU-based companies listed in the EU.

Source: KPMG (2023)

# Legal basis for applying ESRSs

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**CSRD:**

On 5 January 2023, the Corporate Sustainability Reporting Directive (CSRD) entered into force.

A broader set of large companies, as well as listed SMEs, will now be required to report on sustainability. Some non-EU companies will also have to report if they generate over EUR 150 million on the EU market.

The new rules will ensure that investors and other stakeholders have access to the information they need to assess the impact of companies on people and the environment and for investors to assess financial risks and opportunities arising from climate change and other sustainability issues.

# Legal basis for applying ESRSs

**CSRD:**

The first companies will have to apply the new rules **for the first time in the 2024 financial year, for reports published in 2025**.

Companies subject to the CSRD will have to report according to **European Sustainability Reporting Standards (ESRS)**.

The standards are developed in a draft form by the **EFRAG**, previously known as the European Financial Reporting Advisory Group, an independent body bringing together various different stakeholders.

# Legal basis for applying ESRSs

## EU taxonomy:

- The taxonomy is a **classification system** that defines criteria for economic activities that are aligned with a net zero trajectory by 2050 and the broader environmental goals other than climate.

- It helps **direct investments to the economic activities most needed for the transition**, in line with the European Green Deal objectives.

- A common language and a clear definition of what is ‘sustainable’.

- The EU taxonomy allows financial and non-financial companies to share **a common definition of economic activities that can be considered environmentally sustainable**.

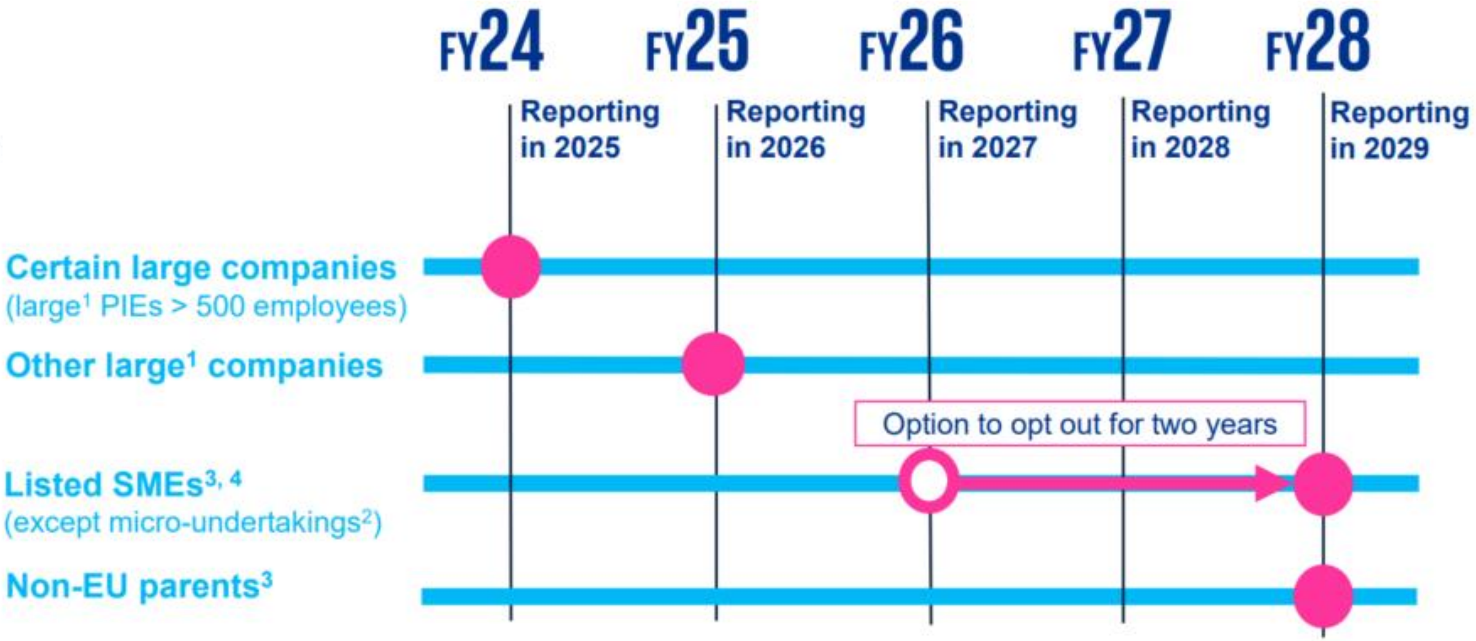
https://www.youtube.com/watch?v=1O6YCCbHvHc

# When and to whom will ESRSs (old) apply?

**When:** ESRSs will apply for years beginning on or after 1 January 2024 (reporting in 2025). Phased introduction will start with Public Interest Entities (PIEs) and companies with listed securities on EU-regulated markets which are large and have more than 500 employees (e.g. those already subject to reporting requirements under the NFRD).

**Who:** Ultimately, ESRSs will be applied by (group exemptions may apply):

- large EU companies[1];
- most companies with listed securities on EU-regulated markets (irrespective of whether they are based in the EU or not[2]); and
- ultimate non-EU parent companies[4] with a combined group turnover in the EU of more than EUR 150 million.




1 Large companies are those that, on the balance sheet date, exceed two of the following three criteria (including EU and non-EU subsidiaries): 250 employees, net revenue of EUR 50mn (formerly EUR 40m) or total assets of EUR 25m (formerly EUR 20m). The new thresholds take effect from FY 2024. EU member states can choose to adopt them early from FY 2023.

2 Exemptions apply, for example, for micro-undertakings (companies that do not exceed two of the following three criteria (including EU and non-EU subsidiaries): 10 employees, net revenue of EUR 900,000 (formerly EUR 700,000) or total assets of EUR 450,000 (formerly EUR 350,000) and for certain debt listings. The new thresholds take effect from FY 2024. EU member states can choose to adopt them early from FY 2023.

3 Separate standards will be developed for SMEs and non-EU parent companies.

4 Small and non-complex institutions and captive insurers are treated like listed SMEs (the option to opt out until 2028 does not apply unless they also meet the definition of an SME).

EFRAG will develop and publish additional sets of ESRSs in due course. These will include sector-specific standards, standards for SMEs and a standard on non-EU parent companies.

Source: KPMG (2023)

# An open discussion:
# If you were a senior executive and your firm were required to disclose a CSR report under the ESRS, how would you view this requirement?

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# ESRS in 2025: Simplification

## Brussels under pressure to curb green agenda in response to Trump

Industry and EU member states urge European Commission to wind back sustainability rules

"There are too many complex and generally vague definitions and terms, as well as unclear reporting scopes and disclosure requirements," it said.

European Commission president Ursula von der Leyen was urged by business leaders in Davos last week to swiftly ease the regulatory burden on companies. One European chief executive said Europe was "losing competitiveness every day". Another said it was imperative to change the perception of US financiers who considered Europe to be "uninvestable" at the moment.

April 2025: A pause in the implementation of CSRD was finalized

# ESRS in 2025: Simplification

## New proposal:

- Cut complexity and improve usability
  - Double materiality assessment (DMA)
  - Focus on identifying the **most obvious topics**
  - Add more information to clarify the criteria for determining the significance of information.
- Reduction in scope
  - The threshold for large companies has been adjusted to more than 1,000 employees on average, with either a turnover greater than EUR 50 million or a balance sheet greater than EUR 25 million.
- Postponement
  - Other large EU companies & SMEs: a 2-year delay

# ESRS in 2025: Simplification



## New proposal:

- The new standards have been shortened in length by more than 55% compared to the initial ESRS, with mandatory datapoints reduced by 57%, and total datapoints, including the elimination of voluntary disclosures, by 68%.
- The European Commission estimates that if the proposals were adopted now as written, they would save companies around €6.3 billion in administrative costs annually.

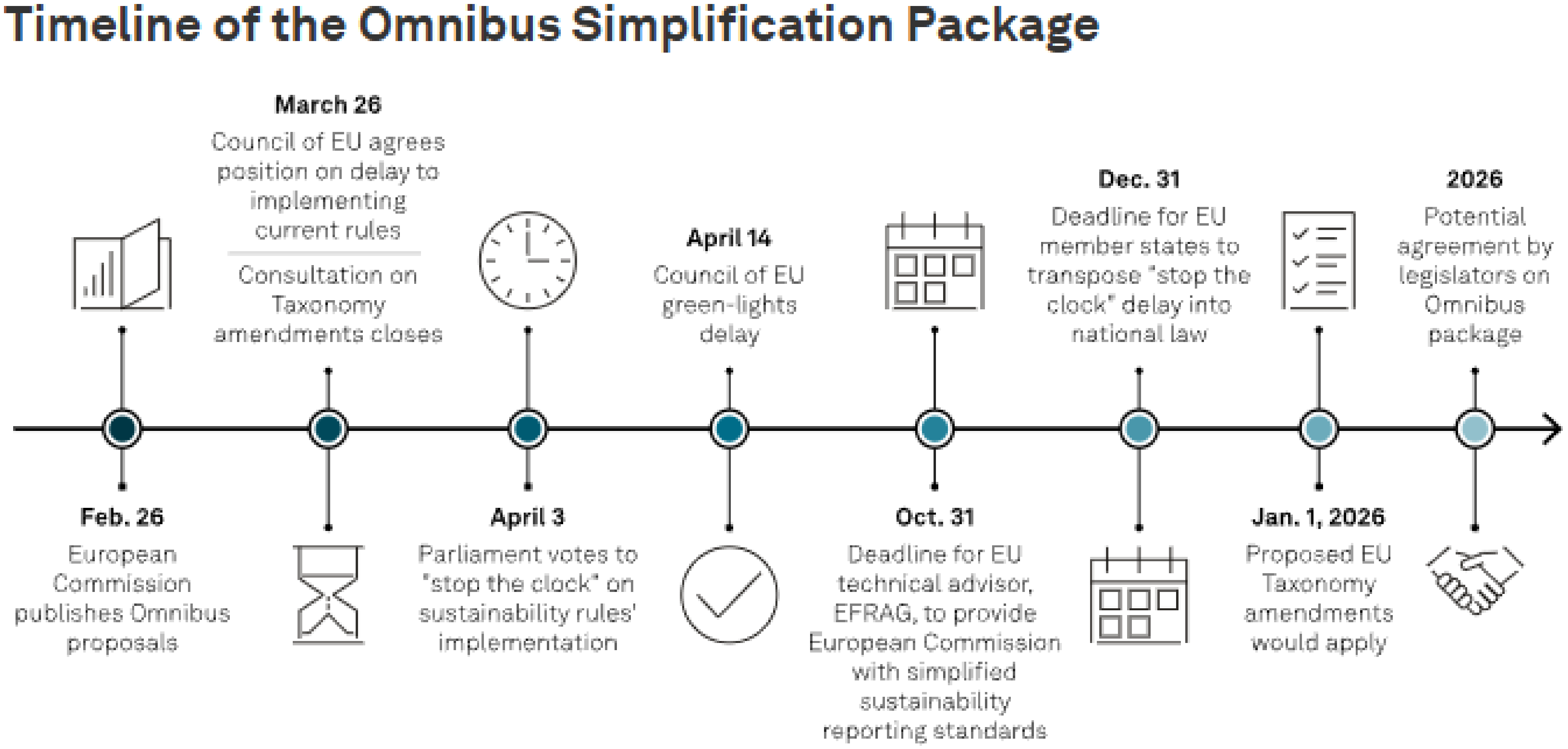
# ESRS in 2025: Simplification

**Key changes to the corporate sustainability reporting directive**

| Element | CSRD (current directive) | New proposal |
|---|---|---|
| Scope of reporting companies | First wave: All companies falling under the NFRD (Non-Financial Reporting directive)<br><br>Second wave: Reporting is mandatory for large undertakings fulfilling two of three criteria:<br>- >250 employees<br>- >€50 million net turnover<br>- balance sheet above €25 million<br><br>Third wave: SMEs | Second wave: Reporting should be mandatory for undertakings with more than 1,000 employees and either turnover of €50 million or a balance sheet above €25 million |
| Postponing reporting requirements | Second wave mandatory to report in financial year 2025, third wave in 2026 | Reporting requirements for both waves postponed for 2 years |
| European Sustainability Reporting Standards (ESRS) | Companies falling under the CSRD are required to use the ESRS | Reducing the number of data points. |
| Sector-specific standards | Sector-specific standards should be developed to simplify the reporting requirements | No sector-specific standards should be adopted |
| Assurance | Limited assurance should be extended to reasonable assurance in the future | Only limited assurance |

Source: World Economic Forum

# ESRS in 2025: Simplification




Source: S&P Global Sustainable1.

# Conclusion:

Sustainability and sustainability reporting

Sustainability reporting frameworks

European sustainability reporting standards (ESRSs) and updates