is ESG a pipe dream for fossil fuels?

The proliferation of sustainability accounting standards is leading to 'reporting fatigue,' but how is this impacting the validity of data? Rebecca Pardon reports

Nowhere are corporate social responsibility efforts more proudly displayed than in a company's sustainability report. Between photos of blooming flowers and laughing children, companies find the space to add their environmental, social and governance data, including their carbon footprint or the numbers of women on boards. Many global businesses already voluntarily report climate information: today, 96% of the world's leading 250 companies report on sustainability, according to a KPMG study. But the information that is carefully selected to be disclosed differs wildly for each company.

The business of carbon accounting is booming as regulators, investors and consumers demand more information about corporate greenhouse gas emissions, but a confusing alphabet soup of ESG regulations has led to some concerns around the validity of the data being released.

This year is poised to be a critical one for companies' climate disclosures. Thousands of businesses will be expected to report their climate impact under the European Climate Sustainability Directive (CSRD). These new reports will contain information around pollution, water consumption and impact on local communities. Also beginning this year, the International Sustainability Standards Board (ISSB) will be taking over the monitoring of companies' climate disclosures that adhere to the Task Force on Climate-related Financial Disclosures (TCFD).

At the same time, the Securities and Exchange Commission (SEC) in the US is adopting climate disclosure rules. If the rules the SEC proposed in 2022 come into effect this year, it will be imposing a new requirement to reveal unprecedented detail about companies' climate risks. Certain information on emissions would also need to be audited. Mandatory climate disclosure is starting to be enforced worldwide, with Australia proposing reporting beginning from July, which will align with the ISSB.

> "It is necessary to avoid generic wording that does not apply to the specific company or is too broad to be decision-useful."

Other dominant sustainability accounting frameworks today include the Global Reporting Initiative (GRI), which focuses on metrics showing the impact of firms on society and the planet, the Greenhouse Gas Protocol (GHG-P) and the Sustainability Accounting Standards Board (SASB), which focuses on ESG factors with a material impact on company performance. "One size will not fit all," says Barbara Davidson, head of accounting at the

think tank Carbon Tracker. "So, these principles-based standards allow for flexibility when considering the disclosures needed for different sectors, geographies, strategies, et cetera."

> "Without more consistent and uniform requirements, we allow disclosures to be manipulated to present a skewed image of sustainability efforts, which will contribute to greenwashing"

This proliferation of reporting standards, however, makes for a landscape that is frequently changing and evolving, leading to confusion and even 'reporting fatigue.' Investors increasingly struggle with how best to interpret clumps of data that can be often contradictory. If the problem was once a lack of data, the challenge now is how best to validate and interpret the data we have. "Ostensibly, the variation [in reporting standards] is permitted because companies' operational contexts are very different across, and sometimes within, industries," says Chad Frischmann, CEO and founder of Regenerative Intelligence. "The claim is that it is hard to find a 'one-size-fits-all' framework.

"This is problematic because it can lead to inconsistencies, confusion and double counting, and makes comparisons and benchmarking difficult," he continues. "This can be changed by establishing more uniform disclosure requirements within frameworks, coupled with sector-specific guidelines to ensure relevance and interoperability." Frischmann believes that stronger regulatory oversight and "standardised reporting requirements" are essential.

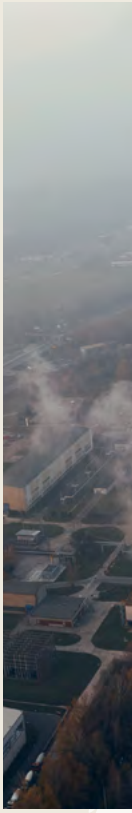
With investors frequently complaining that too many reporting frameworks hinders comparability, environmental activists arguing that it lets companies cherry-pick flattering results and business leaders moaning that they do not know what to disclose and that the array of options is confusing, there has been ample pressure for change. The organisations which write the standards for climate disclosures have recognised the challenges that companies have been are facing and are trying to simplify obligations. The ISSB, for example, was established in 2021 by accounting standards setter the International Financial Reporting Standards Foundation to improve the interoperability of ESG reporting frameworks.

However, the boom in carbon accounting has led to questions over the validity of the data being released, particularly in sectors which are characteristically opaque. Amid an abundance of reporting standards and a lack of concrete rules, companies have turned to a variety of different methods. Some go directly to suppliers to obtain granular data, and many use so-called 'emissions factors' - a unit that, when multiplied by the amount spent or the amount used, allows for the equivalent amount of carbon dioxide to be calculated.

A Carbon Tracker report published in December has highlighted that a lack of consolidation across sustainability accounting standards has meant gaps in reporting by oil and gas companies have been overlooked. According to its research, no publicly available figure currently exists for how much oil and gas was added to global reserve stocks last year. "There is still a lack of transparency in this space," says Davidson. "Accordingly, an increasing number of investors are asking for this information. Many have started to increase pressure on companies via proxy voting, or in various climate-related resolutions.

"One of the main issues is that the current definition of fossil fuel reserves by standards and regulators does not take climate constraints into account," she continues. "The result is that there are more than seven times the global carbon budget worth of emissions embedded in coal oil and gas reserves globally. The definition and approach taken to determining whether fossil fuel reserves are viable is at odds with the Paris Climate Agreement and international net zero policies."

Transparency is a serious problem. Some suppliers, such as the oil and gas industry, are reluctant to provide information due to the commercial sensitivity of the data. This is leading to concerns around the possible exaggeration of environmental efforts and greenwashing. Fischmann fears that there is the potential for companies to "exploit these discrepancies to conceal unsustainable practices, leading to misrepresentation and even fraud."



Dr Elli Siapkidou, director of insight and innovation at Black Sun Global, says: "In an era of climate crisis, accurate climate data and information is key to economic and business decisions. Lacking

this information means we have fewer tools to form accurate climate transition plans and hold companies accountable for their actions and implementation of these plans.

"It is up to the wider civil society to create the pressures to impose these reporting and accountability mechanisms to the private sector."

Davidson believes the energy transition, as the world attempts to wean itself off fossil fuels, requires a new reporting metric altogether, covering the volumes of embedded emissions added, relative to the remaining carbon budget. "The impact of new fossil fuel production and reserves on the global carbon budget – and the lack of public transparency and accountability in this area - is precisely why Carbon Tracker has been developing the Global Registry of Fossil Fuels," she says. "The transition away from a fossil-fuel based energy system is likely to lead to lower long-term oil and gas prices, which is likely to impact the portion of resources that are currently classified as reserves.

"It is crucial that the determination of reserves uses long-term commodity prices that are appropriate given the accelerating energy transition. Investors, auditors and policymakers should hold ensure that companies do this."

A paper published by Columbia University's Center on Global Energy Policy in 2022 found US oil and gas companies use different standards when choosing how and what to report, and few give details about how they plan to achieve the sustainability goals they promote. A study by the Japan Society for the Promotion of Science of the same year found that Shell, for example, had announced its goal to reach net zero emissions by 2050 in its report, but there was no evidence of we an explicit plan to achieve such a transition beyond 2025. Frischmann believes too much trust is placed on oil and gas companies to report accurately. "In the context of the current trajectory of global warming and the science telling us we are already on the course to deviate from the 1.5 degrees Celsius pathway, it is imperative that governments take immediate actions and not wait for the private sector to self-regulate.

"The current system of reporting in the oil and gas sector is woefully inadequate for the challenges of the energy transition," Frischmann continues. "It needs a radical overhaul to incorporate future-oriented metrics that reflect a genuine commitment to reducing carbon emissions and transitioning to renewable energy sources."

Despite its many flaws, however, most experts still believe there is value in attempting to estimate emissions. With COP29 coming up this year, Davidson reflects on how these summits can be opportunities to draw attention to such issues and catalysts for change.

"The overall direction of travel coming out of the COP is clear: the increasing focus on the energy transition and how we need to diversify away from fossil fuels if we are to meet the Paris climate goals,"she says.

"Against this background, there will be more attention on transition planning over this coming year; but the key will be how the COP outcomes are translated into policy and regulatory implementation, at the national, regional and international level, when considering ISSB standards."

Dr Siapkidou is also optimistic. She adds: "Although the final statement at COP28 was encouraging in that governments agreed to 'transition away from fossil fuels', it is still a weak statement given the urgency of the climate crisis. However, it does reinforce the message to corporations and civil society that the drive towards more aligned sustainability reporting and more detailed, higher quality and comparable data will continue. ■