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# Towards more sustainable reporting in Singapore

**Non-financial information such as a company's ESG data can carry equal or even more weight for decision makers than financial data.** BY WANG JIWEI

IN his seminal article *The Market for Lemons: Quality Uncertainty and the Market Mechanism*, Nobel laureate Professor George Akerlof demonstrates that information asymmetry will result in an adverse selection problem which drives away high-quality goods from the market.

The adverse selection market mechanism may lead to market collapse as uninformed buyers are not willing to pay the price the informed sellers believe in.

In a market with more transparent information disclosure and less information asymmetry, market participants are more likely to secure a deal at its fair market value, which reduces the cost of doing business or cost of capital.

This theory lays the foundation for mandatory information disclosure in capital markets to reduce information asymmetry and mitigate the adverse selection problem.

Singapore has been trying to establish a more transparent and sustainable reporting for its capital market.

In 1974, the Institute of Singapore Chartered Accountants, the Singapore Institute of Directors and *The Business Times* introduced the Best Annual Report Award (Best ARA) under the Singapore Corporate Awards.

The objective of the Best ARA is to encourage transparent corporate reporting and a wider scope of disclosures beyond the minimum regulatory requirements that are in tandem with the needs of investors and other stakeholders such as employees, creditors and the general public.

The final assessment criteria for the Best ARA include performance review, business plan and prospects, risk assessment and management, presentation clarity and format.

The Best ARA has also incorporated criteria on sustainability reporting including environmental, social and governance (ESG) information in order to increase awareness that businesses and organisations are responsible to the community both as employers and corporate citizens.

The weightage of sustainability and corporate governance in the final assessment criteria for the Best ARA has increased from 32 per cent in 2011 to 41 per cent in 2019, which signifies the growing importance of sustainability reporting to stakeholders.

As a judging panellist of the Best ARA since 2011, I am glad to see that the Singapore Exchange (SGX) has finally made the sustainability reporting mandatory on a "comply or explain" basis for public listed companies with financial year ending on or after December 31, 2017.

Although the voluntary sustainability reporting regime has been in place since 2011, less than half of the SGX mainboard-listed companies provided sustainability reporting before 2017.

However, all the 633 annual reports for fiscal year 2018 we assessed this year have complied with the sustainability reporting requirement. This is an important milestone to establish a more sustainable reporting environment in Singapore.

Financial information contained in financial statements used to be the only key pillar of annual reports as it provides relevant and faithfully representative information for decision makers.

However, non-financial information such as a company's ESG data provides equally or even more important information to decision makers. The disclosure of ESG information will encourage corporate accountability and responsible behaviour. This may also help companies to have better enterprise risk management and achieve more sustainable firm performance.


**More efforts and resources should be spent on integrating sustainability reporting into annual reports, which enables the presentation of a clearer picture of companies' overall performance in one integrated annual report.** BT FILE PHOTO

## STUDY FINDINGS

Three scholars from Harvard Business School and London Business School compared 180 American companies that voluntarily adopted sustainability policies by 1993 (high sustainability companies) with another 180 matched companies that did not adopt such policies (low sustainability companies).

They found that both the boards of directors and top executives of high sustainability companies are more accountable for sustainability.

For example, high sustainability companies are more likely to employ sustainability metrics in compensation packages to incentivise their top executives.

In addition, high sustainability companies are more likely to be engaged with stakeholders, be long-term oriented, and to disclose more non-financial information.

They also found that high sustainability companies significantly outperform their counterparts over the long term, both in terms of stock market and accounting performance.

The research findings provide theory support to regulators' mandatory sustainability reporting in countries like China, India and Singapore.

The winners of this year's Best ARA have much better sustainability reporting than their peers. Singtel has a dedicated microsite to its sustainability report which presents a very well-balanced reporting of its sustainability activities and strategy.

It also obtains external independent assurance from EY on its sustainability report.

Olam International has integrated its sustainability report into its financial report to present an integrated annual report since 2015.

Its Group CEO review also discusses its sustainability framework and how the framework can support its corporate strategy.

In general, all winners have identified material ESG factors and set out policies, practices and performance in relation to these factors identified.

They have also set out targets for the forthcoming year and issued a board statement on the sustainability report. Well-known and globally-recognised sustainability reporting frameworks such as the Global Reporting Initiative (GRI) Sustainability Reporting Guidelines and The International Integrated Reporting Council's Framework have also been used by the winners.

## A QUESTION OF SIZE?

It is not surprising that big-cap firms with market capitalisation of S$1 billion and above provide much more comprehensive sustainability reports than their smaller counterparts as they have more resources to initiate sustainability activities and prepare sustainability reporting.

Nevertheless, the mid- and small-cap companies have shown commendable efforts in their disclosure of sustainability reports.

I have been a Best ARA judging panellist for nine years and I notice that the same group of companies have won the award multiple times, which shows the continuous efforts in more transparent corporate reporting for these companies.

I believe the collective efforts from various stakeholders such as the regulator, the professional bodies and the media will encourage more companies to catch up with their counterparts, and there will be more new companies to win the award in future.

The real challenge is how to make sustainability reporting sustainable. Compared with financial statements reporting which follows generally accepted accounting principles and prescribed format, sustainability reporting has various approaches and formats to disclosure, which limits the comparability and reliability of the information disclosed.

Companies may follow a sustainability reporting framework such as the GRI Guidelines, but reporting complexity including indicator contingency, ambiguous information, data heterogeneity, and report opacity makes sustainability reporting less comparable across companies.

Although independent assurance on sustainability reporting is encouraged by the SGX to increase stakeholder confidence in the reliability of sustainability reporting, there are still very few who have obtained external assurance on their sustainability reports. Nevertheless, the challenges should not deter our efforts in promoting sustainable reporting in Singapore.

Sustainability reporting has emerged as a key pillar of corporate reporting and it will promote the formulation of long-term strategies and policies for resilient business models. More efforts and resources should be spent on integrating sustainability reporting into annual reports, which enables the presentation of a clearer picture of companies' overall performance in one integrated annual report.

I strongly believe mandatory sustainability reporting will provide an excellent opportunity for companies to review their long-term sustainable strategies regularly, which helps to propel companies' brand value and competitive advantages.

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