

Water-related disclosure briefing: The state of EU environmental disclosure in 2020

In our new report 'The State of EU environmental disclosure in 2020',¹ the Climate Disclosure Standards Board (CDSB) has taken a deep dive into the environmental disclosures of the largest listed companies in the EU. Third in the series, we pick up where our previous report 'Falling Short?'² left off, comparing where we were then and what progress has been made.

Supported by the LIFE programme of the European Union, CDSB reviewed the 2020 environmental disclosures of 50 of Europe's largest listed companies, with a combined market capitalisation of US\$3.5 trillion, under the EU Non-Financial Reporting Directive (NFRD) and the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). Our analysis assesses the effectiveness of environmental disclosures in meeting the NFRD's purpose of increasing the relevance, consistency and comparability of company reporting to support informed stakeholder decision-making on sustainable development. It also supports the corporate reporting process by identifying good practice case studies and tips.

This briefing will provide an overview of the findings of the review with respect water-related disclosures and provides recommendations for companies, policymakers and regulators. It complements two further topic briefings on climate-related³ and on biodiversity, deforestation and forest degradation-related disclosure⁴.

Insights on water-related disclosures

Overall Summary

Our latest review shows that most companies (94%) referred to water in their mainstream reports. 90% of companies reflected the disclosure of water-related KPIs such as water consumption. However further aspects of disclosure must still be improved, such as the description of how water is integrated in the overall business model and strategy, and the comprehensive illustration of water-related risks specific to the organisation. This information supports the clarification of water-business interactions. It contextualises water-related KPIs while providing investors with the consistent, coherent and comparable disclosure they need.

Regarding water issues, consumption was the most covered topic, while water degradation due to effluents was less frequently reported and not consistent among reports. Commitments to conservation and restoration of freshwater and marine ecosystem and biodiversity were predominantly absent.

The upcoming [CDSB Framework Application Guidance for water-related disclosure](#) (CDSB Water Guidance) supports preparers in the disclosure of material water-related information in corporate mainstream reports. It does this by providing detailed reporting suggestions and guidance on water governance, strategy and policy, risks and opportunities, impacts, performance and future outlook, reference to useful external resources and examples of good practices.

¹ CDSB (2020) The state of EU environmental disclosure in 2020. [PDF]. Available from: <https://www.cdsb.net/nfrd2020>

² CDSB (2020) Falling Short: Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve. [PDF]. Available from: <https://www.cdsb.net/falling-short>

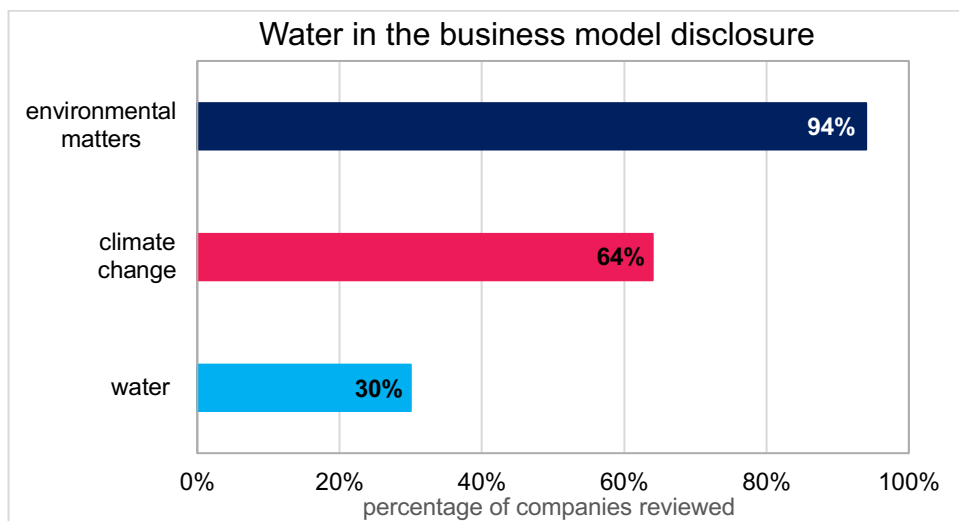
³ CDSB (2021) Climate and TCFD disclosure briefing: The state of EU environmental disclosure in 2020. [PDF]. Available from: <https://www.cdsb.net/nfrd2020>

⁴ CDSB (2021) Briefing on biodiversity, deforestation and forest degradation disclosure in the EU. [PDF]. Available from: <https://www.cdsb.net/nfrd2020>

Business model

CDSB's review found that water was less frequently disclosed (30%) within the business model description than other environmental matters such as climate change (64%).

- Water was mentioned as a resource input to the business by 20% of companies and 18% referred to water outputs (effluents), improvements and/or opportunities⁵;
- 13 of the 50 companies reviewed (26%) mentioned natural capital or resources in their business models, but not water explicitly. However, all these companies subsequently disclosed water-related KPIs and 10 also disclosed about water policy; and
- None of the companies examined disclosed the water-related resilience of the organisation's strategy, including the consideration of water future scenarios.



Policies and due diligence

Well-articulated corporate policies provide the basis to inform and structure a company's environmental disclosure. Additionally, given the site-specific nature of water issues, ideal water-related targets and goals should be contextualised, shared among involved water stakeholders, and consider the entire value chain. CDSB's review found most companies (74%) disclosed information about their water policies. Particularly in terms of water topics and coverage:

- 46% of the companies defined quantitative targets concerning the reduction of water consumption or withdrawals, while 24% did not disclose any quantitative target;
- 24% of companies committed to reduce their water pollution, but did not provide meaningful quantitative targets, beyond a commitment to meeting regulatory requirements; and
- 30% of companies referred to areas particularly vulnerable to water risks⁶, 24% considered suppliers and/or consumers, and only 10% considered stakeholder or community engagement.

⁵ 10% of the companies considered water both as input and output

⁶ Water-issues and risks are site-specific. Different areas in the world can be classified according to different levels of exposure to those risks such as water scarcity, water stress, or risk of floods. Water-related risks affecting an area can constitute risks for businesses operating in this area.

Outcomes

Reporting on policy outcomes enables investors to understand how companies are progressing against their commitments. The review found that 78% are disclosing water-related outcomes:

- 74% disclosed performance on water consumption or withdrawals, while 22% reported on water pollution;
- 48% disclosed outcomes clearly linked to quantitative timebound targets; and
- 30% provided geographical context to their water-related outcomes by referring to areas affected by significant water risks (e.g., reporting the fraction of water consumed in water-stressed areas).

Principal risks

Water-related risks span from physical to reputational categories. They not only impact operations but the entire value chain. They stem from interactions with stakeholders in a given area and are linked to other environmental topics such as climate or land-use change. CDSB's review found that 72% of companies disclosed water-related business risks.

- The types of risks considered included physical risks (70%), regulatory (20%) and reputational (14%). 8% disclosed other risk types, such as political instability, impacts on local communities and volatility of water prices;
- Physical risks commonly related to water availability (32%) and contamination (18%). 58% linked physical water risks to the effects of climate change, such as increased frequency of flood, drought and other extreme events, changes in water temperature, and sea level rise; and
- 20% of the companies included suppliers and 8% included consumers in their risk assessment.

Key performance indicators

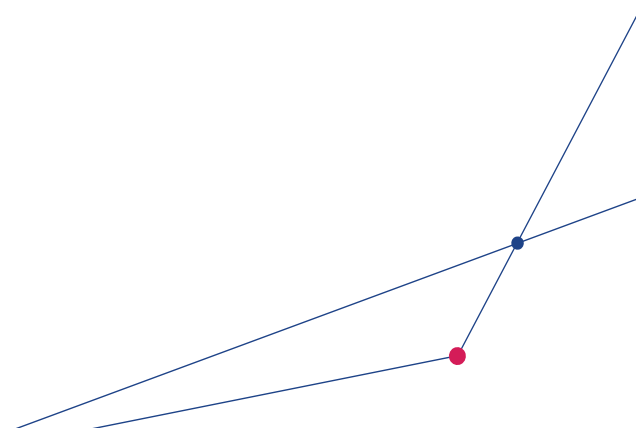
The review found promising results regarding the disclosure of water-related KPIs: 90% of companies disclosed water-related KPIs, second only to climate-related KPIs (100%).

- The most frequently disclosed metrics related to water consumption (76%), withdrawals (28%), and discharge (24%), with only 16% disclosing on water quality;
- Indicators were often broken down by water sources, destinations, geographic areas (of operations or supply), and business/production units. 22% of companies also provided details on areas affected by significant water risks, such as water stress or scarcity; and
- Very few companies linked their water-related KPIs directly to financial or business performance.

Materiality

Despite the promising result on the disclosures of water-related KPIs, only 32% of companies explicitly cited water as a material topic for their business. This discrepancy is reflected in the lack of consistency and connectivity of water-related information within many reports. For instance, water-related KPIs are often disclosed but without a clear description of the interactions between water and the specific business model or of water policy, goals and targets.

This current practice limits the provision of decision-useful information on material water-related risks and impacts to investors.



Recommendations for corporate report preparers

1. Explicitly describe the material interactions between water and the specific organisation in the business model description, and clearly explain how water-related policies are integrated in the overall business strategy.

The inclusion of the water-business interactions in the description of business model would provide useful context to material water-related disclosure. In particular, companies should describe how water is relevant to the company's value creation model, highlighting, for example, if water constitutes a key input resource, or if it is key to the provision of the company's products or services.

This description would provide a useful background for the explanation of water policies, which should reflect the water dependencies, impacts, and risks specific of the company. As recommended in the upcoming [CDSB Water Guidance](#), when disclosing water-related policies, companies should clarify how they are integrated into the overall business strategy. This includes describing due diligence processes and setting out the resourcing, both financial and personnel, to deliver the water policies and strategy.

2. Ensure water-related risk disclosures consider all relevant risk types, time horizons and potential impacts.

When assessing water-related risks, an organisation should consider different risk categories, namely physical, regulatory, reputational, and market risks. Additionally, the assessment should consider both operations and the wider value chain, such as customers and reliance on water infrastructure outside the direct control of the organisation. The upcoming [CDSB Water Guidance](#) provides examples of different corporate water-related risks and associated financial and business implications.

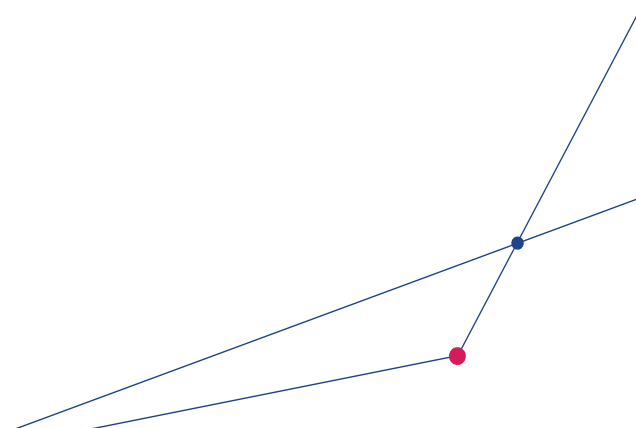
It is also important that business-specific context is provided on water-related risks, including clarifying how water-related risk assessments inform the business model, identifying specific water-related dependencies and impacts, and linking to wider financial and strategic implications for the business.

3. Disclose water-related outcomes through appropriate KPIs, historical data and narrative, which provide clear links to related policy goals and targets, and related financial performance.

When disclosing water-related outcomes, links with policy goals and targets should be ensured. In particular, when disclosing quantitative outcomes, it is important to provide the overall picture through appropriate historical data, and to support the KPIs with an explanation of major trends and drivers of change under and/or outside the control of the company.

As emphasised in the [CDSB Water Guidance](#), when disclosing water-related performance it is important to provide clear definitions of water terms and accounting methods used, time reference like baseline and target year of targets, and geographic contextualisation, e.g. providing details on areas affected by water issues or risks.

Finally, linking water-related outcomes to business and financial performance is critical to demonstrate the integration of water into business strategy, and their connection to water-related risks and opportunities. Illustrative metrics may include the fraction of revenue derived from operations in areas affected by high water risks, or from products that improve water efficiency.



Recommendations for policymakers and regulators

1. **Ensure policy coherence between the Non-Financial Reporting Directive review, the upcoming EU initiative on corporate governance and other EU Directives addressing water issues. This will support companies in making connected and coherent disclosure.**

Disclosure requirements should be developed in conjunction with existing EU water-related legislations (e.g., Water Framework Directive, Flood Directive, Nitrates Directive and Industrial Emissions Directive). This should include other resources that support the understanding of local and regional water-related issues, and risks and opportunities.

2. **Emphasise in the revision of the Directive the importance of ensuring that the different content elements provide a connected and contextual overall view on how companies ensure sustainable long-term value creation, stressing the importance of providing geographic context to water-related information.**

Explicitly embed the requirement to provide contextualised material water-related information into the Non-Financial Reporting Directive when considering environmental matters the company is exposed to. Water-related geographic contexts include information of environmental conditions influencing water availability and socio-economic conditions determining water demand and its patterns.

3. **Incentivise companies to consider the whole spectrum of water issues when preparing reporting information.**

This should span issues from freshwater depletion to the protection of freshwater. Marine ecosystems and biodiversity should also be linked with other environmental issues such as climate and land-use change. Key identified issues should inform ambitious policies and rigorous due diligence processes.

For questions relating to this briefing please contact our Environmental Specialist, Francesca Recanati Francesca.Recanati@cdsb.net who is leading on the development of CDSB's Water Application Guidance.

With the contribution of the LIFE Programme of the European Union Hosted by CDP Europe



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