EUROPEAN COMMISSION
Directorate-General for Financial Stability, Financial Services and Capital Markets Union

FINANCIAL MARKETS
Corporate reporting, audit and credit rating agencies

CONSULTATION DOCUMENT

REVIEW OF THE NON-FINANCIAL REPORTING DIRECTIVE

Disclaimer

This document is a working document of the Commission services for consultation and does not prejudge the final decision that the Commission may take.

The views reflected on this consultation paper provide an indication on the approach the Commission services may take but do not constitute a final policy position or a formal proposal by the European Commission.

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You are invited to reply **by 11 June 2020** at the latest to the **online questionnaire** available on the following webpage:
https://ec.europa.eu/info/publications/finance-consultations-2020-non-financial-reporting-directive_en

Please note that in order to ensure a fair and transparent consultation process **only responses received through the online questionnaire will be taken into account and included in the report summarising the responses**.

This consultation follows the normal rules of the European Commission for public consultations. Responses will be published unless respondents indicate otherwise in the online questionnaire.

Responses authorised for publication will be published on the following webpage:
https://ec.europa.eu/info/publications/finance-consultations-2020-non-financial-reporting-directive_en

INTRODUCTION

Background information on the Non-Financial Reporting Directive

The Non-Financial Reporting Directive (Directive 2014/95/EU, the "NFRD") is an amendment to the Accounting Directive (Directive 2013/34/EU). It requires certain large companies to include a non-financial statement as part of their annual public reporting obligations. Companies under the scope of the NFRD had to report according its provisions for the first time in 2018 (for financial year 2017).

The NFRD applies to large Public Interest Entities with more than 500 employees. In practice it includes large listed companies, and large banks and insurance companies (whether listed or not) – all providing they have more than 500 employees.

The NFRD identifies four sustainability issues (environment, social and employee issues, human rights, and bribery and corruption) and with respect to those issues it requires companies to disclose information about their business model, policies (including implemented due diligence processes), outcomes, risks and risk management, and key performance indicators (KPIs) relevant to the business. It does not introduce or require the use of a non-financial reporting standard or framework, nor does it impose detailed disclosure requirements such as lists of indicators per sector.

The NFRD requires companies to disclose information "to the extent necessary for an understanding of the development, performance, position and impact of [the company's] activities." This means companies should disclose not only how sustainability issues may affect the company, but also how the company affects society and the environment. This is the so-called double materiality perspective.

In 2017, as required by the Directive, the Commission published non-binding guidelines for companies on how to report non-financial information. In June 2019, as part of the Sustainable Finance Action Plan, the Commission published additional guidelines on reporting climate-related information, which integrate the recommendations of the Task Force on Climate-related Financial Disclosures.

Current context

The non-financial information needs of users, in particular the investment community, are increasing very substantially and very quickly. The demand for better information from investee companies is driven partly by investors needing to better understand financial risks resulting from the sustainability crises we face, and partly by the growth in financial products that actively seek to address environmental and social problems. In addition, some forthcoming EU legislation, including the regulation on sustainability disclosures in the financial services sector (Regulation (EU) 2019/2088), and the regulation on a classification system (taxonomy) of sustainable economic activities, can only fully meet their objectives if more and better non-financial information is available from investee companies. The taxonomy regulation will require companies under the scope of the NFRD to disclose certain indicators of the proportion of their activities that are classified as sustainable according to the taxonomy.

The feedback received in the online public consultation on corporate reporting carried out in 2018 in the context of a Fitness Check that is currently being finalised by the Commission services, confirms that the non-financial information currently disclosed by companies does not adequately meet the needs of the intended users. The following problems have been identified:

(1) There is inadequate publicly available information about how non-financial issues, and sustainability issues in particular, impact companies, and about how companies themselves impact society and the environment. In particular:

   a. Reported non-financial information is not sufficiently comparable or reliable.
   b. Companies do not report all non-financial information that users think is necessary, and many companies report information that users do not think is relevant.
   c. Some companies from which investors and other users want non-financial information do not report such information.
   d. It is hard for investors and other users to find non-financial information even when it is reported.

(2) Companies incur unnecessary and avoidable costs related to reporting non-financial information. Companies face uncertainty and complexity when deciding what non-financial information to report, and how and where to report such information. In the case of some financial sector companies, this complexity may also arise from different disclosure requirements contained in different pieces of EU legislation. Companies are under pressure to respond to additional demands for non-financial information from sustainability rating agencies, data providers and civil society, irrespective of the information that they publish as a result of the NFRD.

In its resolution on sustainable finance in May 2018, the European Parliament called for the further development of reporting requirements in the framework of the NFRD. In December 2019, in its conclusions on the Capital Markets Union, the Council stressed the importance of reliable, comparable and relevant information on sustainability risks, opportunities and impacts, and called on the Commission to consider the development of a European non-financial reporting standard. In addition, ESMA has recently published a report on undue short-term pressure on corporations where it recommends the Commission to amend the NFRD provisions.

In its Communication on the European Green Deal, the Commission committed to review the Non-Financial Reporting Directive in 2020 as part of the strategy to strengthen the foundations for sustainable investment. Meeting the objectives of the European Green Deal will require additional investments across all sectors of the economy, the bulk of which will need to come from the private sector. In this sense review of the NFRD is part of the effort to scale up sustainable finance by improving transparency.

The European Green Deal also stressed that sustainability should be more broadly embedded into the corporate governance framework, as many companies still focus too much on short-term financial performance compared to their long-term development and sustainability aspects. As part of the Sustainable Finance Action Plan, work is being undertaken to prepare a possible action in this area.

In addition, to ensure appropriate management of environmental risks and mitigation opportunities, and reduce related transaction costs, the Commission will also support businesses and other stakeholders in developing standardised natural capital accounting practices within the EU and internationally.

The services of the European Commission have published an Inception Impact Assessment on the Review of the Non-Financial Reporting Directive. It summarises the problem definition, possible policy options and likely impacts of this initiative.

Objectives of this public consultation and links with other consultation activities

This public consultation aims to collect the views of stakeholders with regard to possible revisions to the provisions of the NFRD. The principal focus of this consultation is on the possible options for such revisions.

This public consultation builds on a number of recent consultation activities, including:

- An online public consultation on corporate reporting in 2018, in the context of the Fitness Check on the EU framework for public reporting by companies. That consultation enabled the Commission to gather data and views on the problems that need to be addressed with regard to non-financial reporting. Problem analysis is therefore not a principal focus of the current consultation strategy.
- An online targeted consultation on climate-related reporting in 2019, as part of the development of the new guidelines for companies on how to report climate-related information. In addition, the Technical Expert Group on Sustainable Finance organised a call for feedback on its recommendations with regard to reporting climate-related information. The results of these consultation activities, although specific to the issue of climate, are also useful when considering nonfinancial reporting more generally.

This consultation is one element of a broader consultation strategy in the context of the review of the NFRD. In addition to this public consultation, there will also be targeted surveys addressed to SMEs, and to companies currently under the scope of the NFRD. The targeted surveys will collect more detailed opinions and data from companies on certain issues, including costs related to non-financial reporting.

In addition, the services of the Commission will soon launch a public consultation on a Renewed Sustainable Finance Strategy, seeking for stakeholders’ views in other Sustainable Finance related issues, including questions related to sustainable corporate governance.

Consultation questions

1. Quality and scope of non-financial information to be disclosed

The feedback received from the online public consultation on corporate reporting carried out in 2018 suggests that there are some significant problems regarding the non-financial information currently disclosed by companies pursuant to Directive 2014/95/EU ("the Non-Financial Reporting Directive" or NFRD). Likewise, ESMA's 2018 Activity Report gathers evidence that shows there is significant room for improvement in the disclosure practices under the NFRD.

Question 1.: To what extent do you agree or disagree with the following statements about possible problems with regard to non-financial reporting?

	1	2	3	4	5	Don't know
The lack of comparability of non-financial information reported by companies pursuant to the NFRD is a significant problem.				X		
The limited reliability of non-financial information reported by companies pursuant to the NFRD is a significant problem.					X	
Companies reporting pursuant to the NFRD do not disclose all relevant non-financial information needed by different user groups.					X	

(1= mostly disagree, 2= mostly disagree, 3= partially disagree and partially agree, 4= mostly agree, 5= totally agree)

Article 19a of the Accounting Directive (which was introduced into the Accounting Directive by the NFRD) currently requires companies to disclose information about four non-financial matters, if deemed material by the particular company: (i) environment, (ii) social and employee issues, (iii) human rights, (iv) bribery and corruption. These correspond to the "sustainability factors" defined in Article 2(24) of Regulation (UE) 2019/2088 on sustainability-related disclosures in the financial services sector.

Question 2.: Do you consider that companies reporting pursuant to the NFRD should be required to disclose information about other non-financial matters in addition to those currently set-out in Article 19a? **YES** Please specify (no more than three matters).

1. ESG related information required in order to comply with the EU Taxonomy Regulation, including information to be provided under the final technical screening criteria, the 'Do No Significant Harm' principle and information regarding compliance with the minimum social safeguards

2. ESG related information required to comply with the Sustainable Finance Disclosure Regulation, including the final requirements to be adopted under the Regulatory Technical Standards

3.

For each of the four non-financial matters identified in Article 19a of the Accounting Directive, and subject to the company's own materiality assessment, companies are required to disclose information about their business model, policies (including implemented due diligence processes), outcomes, risks and risk management (including risks linked to their business relationships), and key performance indicators (KPIs) relevant to the business.

Question 3.: Are there additional categories of non-financial information related to a company's governance and management procedures, including related metrics where relevant, (for example, scenario analyses, targets, more forward-looking information, or how the company aims to contribute to society through its business activities) that companies should disclose in order to enable users of their reports to understand the development, performance, position and impacts of the company? **NO** Please specify (no more than three).

1. Disclosure of forward-looking targets and KPIs would be useful for assessing sustainability-related risks, particularly in fulfilment of the requirement to assess any "principal adverse impact" under EU legislation, as well as any sustainability-related opportunities.

2

3.

Investment in intangible assets currently represents the majority of investment carried out by the private sector in advanced economies.[1] There is a long-standing debate about the need for better reporting of intangible investments in company reports, including in relation to sustainability.[2] Irrespective of the potential future changes to accounting standards, it is likely to remain the case that a significant proportion of intangible assets will fail to meet the definition of an asset or the criteria for recognition as an intangible asset in the financial statements. The Accounting Directive currently makes no explicit reference to intangible assets in the Articles concerning the management report, other than the requirement to report about activities in the field of research and development in Article 19(2)(b).

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[1] https://voxeu.org/article/productivity-and-secular-stagnation-intangible-economy

[2] The European Financial Reporting Advisory Group (EFRAG) is currently carrying out a research projecton this topic. See http://www.efrag.org/Activities/1809040410591417/EFRAG-research-project-on-better-information-on-intangibles. The United Kingdom's Financial Reporting Council

issued a consultation document about business reporting of intangibles in 2019. See https://www.frc.org.uk/news/february-2019/consultation-into-improvements-to-the-reporting-of.

Question 4.: In light of the importance of intangibles in the economy, do you consider that companies should be required to disclose additional non-financial information regarding intangible assets or related factors (e.g. intellectual property, software, customer retention, human capital (etc.)?

Yes X	No	Don't know

In addition to the provisions of the NFRD, several other EU legislative acts require disclosures of sustainability-related information for financial sector entities:

- The Regulation on prudential requirements for credit institutions requires certain banks to disclose ESG risks as of 28 June 2022.
- The Regulation on sustainability- related disclosures in the financial services sector requires financial market participants to disclose their policies on the integration of sustainability risks in their investment decision- making process and the adverse impacts of investment decisions on sustainability factors, as of 10 March 2021.
- The Regulation establishing a framework to facilitate sustainable investment (the Sustainable Finance Taxonomy) creates new reporting obligations including for companies subject to the NFRD, starting in December 2021.

Question 5.: To what extent do you think that the current disclosure requirements of the NFRD ensure that investee companies report the information that financial sector companies will need to meet their new disclosure requirements?

Not at all	To some extent but not much X	To a reasonable extent	To a very great extent	Don't know

In order to ensure that the financial sector entities comply with the new disclosure requirements, laid down in the different pieces of legislation, in the most effective and efficient manner, there might be scope for better coherence between the different disclosure requirements.

Question 6.: How do you find the interaction between different pieces of legislation (You can provide as many answers as you want)

It works well	There is an overlap	There are gaps	There is a need to streamline X	It does not work at all	Don't know

<u>Question 7.:</u> In order to ensure better alignment of reporting obligations of investees and investors, should the legal provisions related to non-financial reporting define environmental matters on the basis of the six objectives set-out in the taxonomy regulation: (1) climate change mitigation; (2) climate change adaptation; (3) sustainable use and protection of water and marine resources; (4) transition to a circular economy (5) pollution prevention and control; (6) protection and restoration of biodiversity and ecosystems?

Yes X	No	Don't know

Please provide any comments or explanations to justify your answers to questions 1 to

We agree with and support the objective of providing meaningful, consistent, high quality ESG-related reporting from corporates. The lack of consistent and comparable data on sustainability-related risks and opportunities is currently a key challenge for financial participants. ESG issues can have a material impact on investee companies and it is an investment manager's duty as a steward of these companies to assess these risks for better-adjusted investment returns for their clients. Being able to do so is also necessary to meet obligations under the EU's emerging sustainable finance regulatory framework. A common EU initiative to enable more coherent reporting of this information is therefore critical to its success and to be welcomed.

However, it should be borne in mind that the financial services and investment sector is highly internationalised beyond the EU's borders. Therefore, the development of an EU based ESG reporting framework will have limitations for investors and financial products that invest in assets on a global basis, as well as for European companies operating outside Europe (and for their international investors). Converging non-financial reporting standards internationally should be strived for but will be a very complex exercise that will require multilateral engagement and take years to complete. Comparing companies across industries / sectors is still likely to present challenges even after an agreed EU framework is put in place.

It should be borne in mind that there are multiple stakeholders with their own specific ESG preferences and requests and different needs regarding comparability, reliability and completeness of non-financial reporting data. For example, different stakeholders (e.g. investors, policy makers, governmental organisations, NGOs) may request ESG performance information under all of the 17 UN Sustainable Development Goals. Investment funds may also be pursuing any one or more of the 17 UN Sustainable Development Goals. Meeting the demands of this diverse and dispersed audience in their entirety under one single initiative is highly challenging.

No single standard or reporting framework can currently satisfy all of the possible ESG-related preferences and requirements in this area. More consultation is therefore needed on a multilateral basis with various international standard-setters, professional bodies and interested stakeholders before any standard is devised.

A targeted approach might offer the best way forward, focussing in the first instance on core data needed in order to comply with the new EU sustainable finance regime.

Further, to achieve this level of transparency and availability of non-financial data and information, there will be associated costs – not only in gathering this data, but also in terms of the resourcing and expertise needed to fulfil the reporting requirements.. How costs will be borne and by whom is an important aspect to consider in seeking to strike the right balance of reporting requirements.

Some companies have been providing sustainability information for many years and have been able to gradually enrich their reporting as new requirements emerge. An extensive new reporting regime introduced in one instance will be very impactful and therefore striking the right balance in terms of new reporting requirements to be imposed is essential.

We would also note that questions 3 and 4 in particular relate to commercially sensitive and proprietary company information that may be very difficult to disclose.

We agree that the NFRD needs to be updated in view of the rapidly evolving area of sustainable finance and in particular to align the reporting obligations of investees/investors with the six environmental objectives set out under the EU's Taxonomy Regulation. Furthermore, in order to enable financial participants and financial products to meet their obligations under the EU Taxonomy Regulation, information relating to the 'Do No Significant Harm' principle and information regarding compliance with the minimum social safeguards set out under the Taxonomy should also be prescribed, as well as information required to comply with the Sustainable Finance Disclosure Regulation, including the final requirements to be adopted under the Regulatory Technical Standards.

We agree that there is a need to streamline the various ESG reporting requirements across the jurisdictions as part of this initiative.

2. STANDARDISATION

Note: in this section, the word "standard" is used for simplicity. This should not be read as a suggestion that all relevant reporting requirements must be specified in a single normative document. Rather, "standard" is merely used as a shorthand that could encompass a consistent and comprehensive set of standards. Reporting standards define what information companies should report and how such information should be prepared and presented.

A requirement that all companies falling within the scope of the NFRD report in accordance with a common non-financial reporting standard may help to address some of the problems identified in section 1 (comparability, reliability and relevance).

Question 8.: In your opinion, to what extent would a requirement on companies to apply a common standard for non-financial information resolve the problems identified?

Not at all	To some extent	To a reasonable	To a very great	Don't know

	but not much	Extent X	extent	

Question 9.: In your opinion, is it necessary that a standard applied by a company under the scope of the Non-Financial Reporting Directive should include sector-specific elements?

Yes X	No	Don't know

A number of non-financial reporting frameworks and standards already exist. Some, including the standards of the Global Reporting Initiative (GRI), the framework of the International Integrated Reporting Council (IIRC), and the standards of the Sustainability Accounting Standards Board (SASB), aim to cover most or all relevant non-financial issues.

Question 10.: To what extent would the application of one of the following standards or frameworks, applied on its own, resolve the problems identified while also enabling companies to comprehensively meet the current disclosure requirements of the Non-Financial Reporting Directive, taking into account the double-materiality perspective See section 4)?

	1	2	3	4	Don't know
Global Reporting Initiative			X		
Sustainability Accounting Standards Board			X		
International Integrated Reporting Framework			X		
Another framework or standard *					

1= not at all, 2= to some extent but not much, 3= to a reasonable extent, 4= to a very great extent

*Please specify other framework or standard (no more than three.)

1= not at all, 2= to some extent but not much, 3= to a reasonable extent, 4= to a very great extent

	1	2	3	4

1. **TCFD - 3**
2. **CDP- 2**
3.

On 5 December 2019, the Economic and Financial Affairs Council adopted conclusions on deepening the Capital Markets Union, in which it invited the Commission to "consider the development of a European non-financial reporting standard **taking into account international initiatives**".

Most existing frameworks and standards focus on individual or a limited set of nonfinancial issues. Examples include the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD), the UN Guiding Principles Reporting Framework (human rights), the questionnaires of the CDP (formerly the Carbon Disclosure Project), and the standards of the Carbon Disclosure Standards Board (CDSB). Several approaches have also been developed at EU level in the environmental area, including the Organisation Environmental Footprint and reporting under the Eco-Management and Audit Scheme (EMAS).

Question 11.: If there were to be a common European non-financial reporting standard applied by companies under the scope of the NFRD, to what extent do you think it would be important that such a standard should incorporate the principles and content of the following existing standards and frameworks:

	1	2	3	4	Don't know
Global Reporting Initiative			X		
Sustainability Accounting Standards Board				X	
International Integrated Reporting Framework			X		
Task Force on Climate-related Financial Disclosures (TCFD)				X	
UN Guiding Principles Reporting Framework (human rights)		X			
CDP		X			
Carbon Disclosure Standards Board (CDSB)		X			
Organisation Environmental Footprint (OEF)	X				
Eco-Management and Audit Scheme (EMAS)	X				
Another framework or standard *					

1= not at all, 2= to some extent but not much, 3= to a reasonable extent, 4= to a very great extent

*Please specify other framework or standard (no more than three).

	1	2	3	4	Don't know
1					
2					
3					

1= not at all, 2= to some extent but not much, 3= to a reasonable extent, 4= to a very great extent

Question 12.: If your organisation *fully* applies any non-financial reporting standard or framework when reporting under the provisions of the NFRD, please indicate the recurring annual cost of applying that standard or framework (including costs of retrieving, analysing and reporting the information).

Name of standard or framework (max 3)	Estimated cost of application per year, excluding any one-off start-up costs.
N/A	

Small and Medium-Sized Enterprises (SMEs) often do not have the technical expertise nor resources necessary to prepare reports in accordance with state-of-the-art, sophisticated standards. This may imply that requiring SMEs to apply the same standards as large companies may be a disproportionate burden for SMEs.

At the same time, many SMEs are under increasing pressure to provide certain nonfinancial information to other businesses, in particular if they are suppliers of large companies. In addition, financial institutions are increasingly likely to request certain non-financial information from companies to whom they provide capital, including SMEs. In this respect, SMEs that do not provide non-financial information may experience a negative impact on their commercial opportunities as suppliers of larger companies or on their access to capital, and may not be able to benefit from new sustainable investment opportunities.

Question 13.: In your opinion, would it be useful for there to be a simplified standard and/or reporting format for SMEs?

Yes X	No	Don’t know

Question 14.: To what extent do you think that a simplified standard for SMEs would be an effective means of limiting the burden on SMEs arising from information demands they may receive from other companies, including financial institutions?

Not at all	To some extent but not much	To a reasonable Extent X	To a very great extent	Don’t know

Question 15.: If the EU were to develop a simplified standard for SMEs, do you think that the use of such a simplified standard by SMEs should be mandatory or voluntary?

Mandatory	Voluntary X	Don’t know

In the responses to the Commission’s public consultation on public corporate reporting carried out in 2018, just over half of the respondents believed that integrated reporting could contribute to a more efficient allocation of capital and agreed that the EU should encourage integrated reporting.

Question 16.: In light of these responses, to what extent do you agree that the body responsible for developing a European non-financial reporting standard should also have expertise in the field of financial reporting in order to ensure "connectivity" or integration between financial and non-financial information?

Not at all	To some extent but not much	To a reasonable Extent	To a very great extent X	Don't know

Question 17.: The key stakeholder groups with an interest in and contributing to the elaboration of financial reporting standards have historically been investors, preparers of financial reports (companies) and auditors/accountants. To what extent to do you think that these groups should also be involved in the process of developing a European nonfinancial reporting standard?

	1	2	3	4	Don't know
Investors				X	
Preparers				X	
Auditors/accountants				X	

1= not at all, 2= to some extent but not much, 3= to a reasonable extent, 4= to a very great extent

Question 18.: In addition to the stakeholders referred to in the previous question, to what extent to do you consider that the following stakeholders should be involved in the process of developing a European non-financial reporting standard?

	1	2	3	4	Don't know
Civil society representatives/NGOs			X		
Academics			X		
Other*					

1= not at all, 2= to some extent but not much, 3= to a reasonable extent, 4= to a very great extent

*Please specify other categories (no more than three).

	1	2	3	4	Don't know
Third party fund service providers			X		
Professional bodies (Institutes of accountants, accountants, lawyers, etc.)				X	
Representatives of corporate issuers				X	

1= not at all, 2= to some extent but not much, 3= to a reasonable extent, 4= to a very great extent

Question 19.: To what extent should the following European public bodies or authorities be involved in the process of developing a European non-financial reporting standard?

	1	2	3	4	Don't know
European Securities Markets Authority (ESMA)			X		
European Banking Authority (EBA)			X		
European Insurance and Occupational Pensions Authority (EIOPA)			X		
European Central Bank (ECB)			X		
European Environment Agency (EEA)			X		
Platform on Sustainable Finance[3]			X		
Other*					

1= not at all, 2= to some extent but not much, 3= to a reasonable extent, 4= to a very great extent

*Please specify other European public bodies or authorities that you consider should be involved in the process of developing a European non-financial reporting standard (no more than three).

	1	2	3	4	Don't know
IOSCO			X		
OECD			X		
International standard setters (SASB, CDP, etc)				X	

1= not at all, 2= to some extent but not much, 3= to a reasonable extent, 4= to a very great extent

National accounting standards-setters of several EU Member States are represented in the European Financial Reporting Advisory Group (EFRAG), which acts as the EU's voice and technical advisor in relation to financial reporting.

<u>Question 20.:</u> To what extent to do you consider that the following national authorities or bodies should be involved in the process of developing European non-financial reporting standards?

	1	2	3	4	Don't know
National accounting standard-setters				X	
Environmental authorities			X		
Other*					

1= not at all, 2= to some extent but not much, 3= to a reasonable extent, 4= to a very great extent

* Do you consider that other types of national authorities or bodies should be involved in the process of developing a European non-financial reporting standard?

	1	2	3	4	Don't know

1= not at all, 2= to some extent but not much, 3= to a reasonable extent, 4= to a very great extent

Please provide any comments or explanations to justify your answers to questions 8 to 20.

Our response to Q. 8 is framed in terms of taking a global approach to a common framework for non-financial reporting. As noted earlier, there is no one single standard setter or standard that can currently satisfy all ESG preferences and requirements and moving to one single standard (or set of standards) may be difficult to achieve in practice. Devising a common EU non-financial reporting framework will still leave gaps for both investors that invest globally and companies operating internationally and convergence with existing international standards should be sought to the extent possible. This underscores the point that the NFRD regime should not operate in isolation of other global disclosure frameworks which are already in place (e.g. Sustainability Accounting Standards Board (SASB), the Task Force on Climate-related Financial Disclosures (TCFD), Global Reporting Initiatives (GRI) etc.). This consultation and review provides the opportunity to develop industry sector specific standards which draw the “best from the best” of existing standards that are already in place.

Additionally, the NFRD cannot operate in isolation of existing regulations and disclosure requirements, including UCITS and AIFMD reporting requirements and future amendments to same.

For the Commission to bring consistency to the non-financial reporting disclosures (including alignment with existing regulations) future consultation with professional bodies on an international basis is fundamental, as is the involvement of national accounting standard-setters, the European Supervisory Authorities, the European Central Bank, IOSCO and the OECD. The Commission could use the Platform on Sustainable Finance to assist in coordinating such an initiative.

SMEs are an important part of the European economy and we agree that a proportionate approach should be taken regarding application of the NFRD to SMEs. This could involve a transitional approach for SMEs involving voluntary application, with a focus on larger companies while the framework is still in the early stages. Equally, we think that the “S” and the “M” should be treated differently as medium-size companies are much more likely to access capital markets whereas small companies are most likely relying on bank financing.

The current NFRD regime only applies to a limited population of issuers. Whilst we agree with the need for setting a common standard that allows for sector specific elements, when it comes to standardisation, a balance needs to be struck in terms of the degree of prescriptiveness and flexibility – it cannot become a box ticking exercise. Our members have found that meaningful reporting on environmental and social matters tends to be that which moves beyond reporting on metrics and indicators (which could be considered as outputs) to reporting on the effect of those outputs on society and the environment, i.e. focusing on impacts. This is turn then informs discussion on what can be done to ameliorate negative impacts and further enhance positive impacts.

It is also essential that there is clarity in terms of what are mandatory disclosures and what disclosures could be considered best practices at a sector specific level. We would propose that the NFRD update focuses in the first instance on the key information and KPIs needed to comply with the Taxonomy Regulation and the Sustainable Finance Disclosure Regulation. Other information should be disclosed if material.

3. APPLICATION OF THE PRINCIPLE OF MATERIALITY

The NFRD requires companies to disclose information "to the extent necessary for an understanding of the development, performance, position and impact of [the company's] activities." This materiality principle implies that companies reporting pursuant to the NFRD must disclose (i) how sustainability issues may affect the development, performance and position of the company; and (ii) how the company impacts society and the environment. This is the double-materiality perspective.[4] The two "directions" of materiality are distinct although there can be feedbacks from one to the other. For example, a company that with severe impacts on the environment or society may incur reputational or legal risks that undermine its financial performance.

'Material' information is defined in Article 2(16) of the Accounting Directive as "the status of information where its omission or misstatement could reasonably be expected to influence decisions that users make on the basis of the financial statements of the undertaking. The materiality of individual items shall be assessed in the context of other similar items." This definition is geared towards financial reporting, which is principally intended to serve the needs of investors and other creditors. By contrast, non-financial information serves the needs of a broader set of stakeholders, as it relates not only to the increasing impact of non-financial matters on the financial performance of the company, but also to its impacts on society and the environment. This may imply the need to provide an alternative definition of materiality for application in the context of nonfinancial reporting, or at least additional guidance on this issue.

<u>Question 21:</u> Do you think that the definition of materiality set-out in Article 2(16) of the Accounting Directive is relevant for the purposes of determining which information is necessary to understand *a company's development, performance and position*?

No, not at all	To some extent but not much	To a reasonable Extent X	Yes, to a very great extent	Don't know

<u>Question 22.:</u> Do you think that the definition of materiality set-out in Article 2(16) of the Accounting Directive is relevant for the purposes of determining which information is necessary to understand *a company's impacts on society and the environment*?

No, not at all	To some extent but not much	To a reasonable Extent X	Yes, to a very great extent	Don't know

Question 23.: If you think there is a need to clarify the concept of 'material' non-financial information, how would you suggest to do so?

Please see comments included in commentary box after Q 24.

Question 24.: Should companies reporting under the NFRD be required to disclose their materiality assessment process?

Yes X	No	Don't know

Please provide any comments or explanations to justify your answers to questions 21 to 24.

We agree that in order to develop a standardised and widely accepted materiality framework, the concept of 'material' non-financial information needs to be more clearly defined. This needs to be done on an industry sector specific basis focussing on KPIs within a specific industry sector. A well-defined materiality framework by industry sector as it relates to non-financial information would aid in bringing clarity and consistency. It would also make the information and non-financial disclosures more relevant to the user, as they would be disclosed in line with industry sector guidelines. This will also assist in distinguishing between what are the “nice to have” disclosures as opposed to the “must haves” at industry sector level.

The inclusion of a materiality assessment is also important to show how corporates have assessed the various risk factors to their business and to explain why they believe a certain risk factors are material. Consultation with all stakeholders (asset managers and the funds industry, issuers and professional accounting bodies) in relation to this aspect is critical, as this is fundamental to many of the areas of non-financial reporting.

4. ASSURANCE

The NFRD requires that the statutory auditor or audit firm checks whether the nonfinancial statement has been provided if a firm falls within the scope of the Directive.

Article 34 of the Accounting Directive requires that the financial statements are audited, and that the statutory auditor or audit firm express an opinion whether the management report (i) is consistent with the financial statements for the same financial year; and (ii) has been prepared in accordance with the applicable legal requirements. Article 34 of the Accounting Directive also requires the statutory auditor or audit firm to state whether it has identified material misstatements in the management report and to give an indication of the nature of such material misstatements. However, the non-financial statement published pursuant to the NFRD – whether contained in the management report or a separate report – is explicitly excluded from the scope of Article 34 of the Accounting Directive. Consequently, the NFRD does not require any assurance of the content of the non-financial statement.

Question 25.: Given that non-financial information is increasingly important to investors and other users, are the current differences in the assurance requirements between financial and non-financial information justifiable and appropriate?

No, not at all	To some extent but not much X	To a reasonable extent	Yes, to a very great extent	Don’t know

Question 26.: Should EU law impose stronger assurance requirements for non-financial information reported by companies falling within the scope of the NFRD?

Yes X	No	Don’t know

There are two types of assurance engagement a practitioner can perform:

- Reasonable assurance reduces the risk of the engagement to an acceptably low level in the given circumstances. The conclusion is usually provided in a positive form of expression and states an opinion on the measurement of the subject matter against previously defined criteria.

- Limited assurance engagements provide a lower level of assurance than the reasonable assurance engagements. The conclusion is usually provided in a negative form of expression by stating that no matter has been identified by the practitioner to conclude that the subject matter is materially misstated.

Question 27.: If EU law were to require assurance of non-financial information published pursuant to the NFRD, do you think that it should require a *reasonable* or *limited* assurance engagement on the non-financial information published?

Reasonable X	Limited	Don’t know

Question 28.: If EU law were to require assurance of non-financial information published pursuant to the NFRD, should the assurance provider assess the reporting company's materiality assessment process?

Yes	No	Don't know
X		

Question 29.: If assurance of non-financial information was required by EU law, should the assurance provider be required to identify and publish the key engagement risks, their response to these risks and any related key observations (if applicable)?

Yes	No	Don't know
		X

Question 30.: If assurance of non-financial information was required by EU law, do you think that assurance engagements should be performed based on a common assurance standard?

Yes	No	Don't know
X		

If you answered yes in reply to the previous question, please explain whether there is an existing assurance standard that could be used for this purpose or whether a new standard would need to be developed.

In terms of an existing standard, ISAE3000, could be deployed – this is not specific to any subject matter. The standard deployed needs to be related to this area and one that is industry specific and acknowledges differences between different industries. One size cannot fit all. See, however, our overall feedback at the end of this section.

Question 31.: Do you think that an assurance requirement for non-financial information is dependent on companies reporting against a specific non-financial reporting standard?

Yes	No	Don't know
X		

Question 32.: If you publish non-financial information and that information is assured, please indicate the annual costs of such assurance.

This is very much dependent upon scope of assurance – limited versus reasonable, standard which is being applied, availability of data, etc.

If you provided an answer to the previous question, please describe the scope of the assurance services provided (issues covered, reasonable/limited, etc.).

As above

Please provide any comments or explanations to justify your answers to questions 25 to 32.

We agree on the importance of independent third-party external validation to provide some level of assurance over the non-financial disclosures.

For assurance to be provided, it must be ensured that there is available data, an industry sector specific reporting standard which covers these non-financial reporting disclosures and an industry sector specific assurance standard.

Given the progressive nature of these developments within Europe, consideration should be given to a tiered approach to assurance reporting, initially limited assurance, and as this area develops and transitions to these changes, this would then move to reasonable assurance over time.

Development of the format opinion and what it covers (e.g., engagement risks / response to risks / key observations, etc.) should not be determined in isolation of consultation with the relevant professional accounting bodies.

The professional accounting bodies must be involved in this discussion around what type of assurance will be required, i.e. limited versus reasonable and the framework to be put in place.

5. DIGITISATION

The EU has introduced a structured data standard, the European Single Electronic Format (ESEF) under the Transparency Directive. With effect from 1 January 2020 listed companies in the EU shall report their annual financial reports in XHTML (audited financial statements, management report and issuer's responsibility statements). Additionally, if the consolidated financial statements are prepared in IFRS, the XHTML document should also be tagged using iXBRL elements specified in the ESEF taxonomy. This allows the information to be machine-readable. This is expected to produce a number of benefits, including cost saving for users of annual financial reports, greater speed, reliability and accuracy of data handling, improved analysis, and better quality of information and decision-making.

Additionally, the Commission is exploring opportunities to establish a single access point for public corporate information. In this respect, the Commission expects the High-level Forum on CMU to examine this topic and formulate recommendations from the Capital Markets angle in the coming months.

Question 33.: To what extent do you agree or disagree with the following statements regarding digitalisation of non-financial information?

	1	2	3	4	5	Don't know
It would be useful to require the tagging of reports containing non-financial information to make them machine-readable.					X	
The tagging of non-financial information would only be possible if reporting is done against standards.					X	
All reports containing non-financial information should be available through a single access point.				X		

(1= totally disagree, 2= mostly disagree, 3= partially disagree and partially agree, 4= mostly agree, 5= totally agree)

Question 34.: Do you think that the costs of introducing tagging of non-financial information would be proportionate to the benefits this would produce?

No, not at all	To some extent but not much	To a reasonable extent X	Yes, to a very great extent	Don't know

Question 35.: Please provide any other comments you may have regarding the digitalisation of sustainability information:

Digital tagging of ESG data could greatly assist in enhancing data processing and analysis, both for investors and regulators alike.

In order to address issues of fragmentation, costs and in the interests of transparency towards all stakeholders, we recommend that ESG data required under the NFRD be publicly available and reported via a common utility.

Please provide any comments or explanations to justify your answers to questions 33 to 35.

Firms are increasingly turning to data analytics such as AI, machine learning and natural language processing to enable the processing of data, including ESG data. This enables investors to include different types of information in their investment analysis, which helps to provide a more comprehensive understanding of the ESG profile of a company.

6. STRUCTURE AND LOCATION OF NON-FINANCIAL INFORMATION

The default requirement of the NFRD is that companies under scope shall include their non-financial statement in their annual management report. However, the NFRD also allows Member States to allow companies to disclose the required non-financial information in a separate report under certain conditions, and most Member States took up that option when transposing the Directive. Companies can be allowed by national legislation to publish such a report up to six months after the balance sheet date.

The publication of non-financial information in a separate report has a number of consequences, including:

- Separate reports that include non-financial information are out of the legal mandate of the national competent authorities, whose mandate over periodic reports is limited to the annual and semi-annual financial reports (which include the management report).
- Separate reports that include non-financial information are not required to be filed in the Officially Appointed Mechanisms (OAMs) designated by Member States pursuant to Article 21(2) of the Transparency Directive.

<u>Question 36.:</u> Other consequences may arise from the publication of the non-financial statement as part of a separate report. To what extent do you agree with the following statements:

	1	2	3	4	5	Don't know
The option to publish the non-financial statement as part of a separate report creates a significant problem because the non-financial information reported by companies is hard to find (e.g: it may increase search costs for investors, analysts, ratings agencies and data aggregators).				X		
The publication of financial and non-financial information in different reports creates the perception that the information reported in the separate report is of secondary importance and does not necessarily have implications in the performance of the company.			X			

1= not at all, 5= to a very great extent]

<u>Question 37.:</u> Do you believe that companies should be required to disclose all necessary non-financial information in the management report?

Yes	No X	Don't know

Question 38.: If companies are allowed to publish the required non-financial information in a report that is separate from the management report, to what extent do you agree with the following approaches?

	1	2	3	4	5	Don't know
Legislation should be amended to ensure proper supervision of information published in separate reports.					X	
Legislation should be amended to require companies to file the separate report with Officially Appointed Mechanisms (OAMs).					X	
Legislation should be amended to ensure the same publication date for management report and the separate report.					X	

(1= totally disagree, 2= mostly disagree, 3= partially disagree and partially agree, 4= mostly agree, 5= totally agree)

Please provide any comments regarding the location of reported non-financial information.

See answer below.

The management report, including the non-financial statement, aims to provide a company's stakeholders with the information necessary to understand the company's development, performance, position and impact. Some non-financial information is also reported in the corporate governance statement, which is also part of the management report.

Question 39.: Do you consider that the current segregation of non-financial information in separate non-financial and corporate governance statements within the management report provides for effective communication with users of company reports?

No, not at all	To some extent but not much	To a reasonable Extent X	Yes, to a very great extent	Don't know

Please provide any comments or explanations to justify your answers to questions 36 to 39.

Not all information which is included within the annual report and financial statements (potentially including the disclosure of ESG risks which have been deemed to be financially material) is covered by the statutory audit opinion.

The potential for the non-financial information required by the NFRD to be included in a separate report could be considered. This would clarify to the reader of the reports the information that is covered by each opinion. This would also reflect the increasing importance of these non-financial disclosures.

This would, however, need to be prescribed by new legislation, and the report should be filed through officially appointed mechanisms and should be signed and published on the same day as the annual report.

Advantages of two separate reports:

- This would enable two different forms of opinions to be issued.
- Transparency to the reader of the documents as to what is being covered by each opinion.
- May address the concerns that information included in the non-audited section of the annual report / appendix to the annual report is not read - if it is included in a short separate document (which is released at the same time as the annual report).
- Addresses concerns of some that the annual report is essentially a historic based document whilst the sustainability report is a more current and forward-looking document.
- Attempting to complete other jurisdictional filings in one report may be challenging as there are different materiality reports. Two reports addresses this challenge.

Disadvantages of two separate reports:

- Two reports may mean there are additional costs.
- Two reports may mean there is an increased time burden in terms of man hours.
- Concerns could arise about the potential for inconsistency / lack of connectivity between the annual report and the sustainability disclosures if they are in two separate documents.

Given the wide number of interested stakeholders in this area, it is essential that prior to any decisions being made, that a further broad consultation with all relevant stakeholders is completed – and this is inclusive of international professional bodies and regulators internationally.

7. PERSONAL SCOPE (WHICH COMPANIES SHOULD DISCLOSE)

The NFRD currently applies to large Public-Interest Entities (PIEs) with more than 500 employees. In practice this means large companies with securities listed in EU regulated markets, large banks (whether listed or not) and large insurance companies (whether listed or not) – all provided that they have more than 500 employees.

The Accounting Directive defines large undertakings as those that exceed at least two of the three following criteria:

(a) balance sheet total: EUR 20 000 000;
(b) net turnover: EUR 40 000 000;
(c) average number of employees during the financial year: 250.

Some Member States have extended the personal scope of the NFRD by lowering the threshold to 250 employees, in effect capturing all large PIEs.

Companies that are a subsidiary of another company are exempt from the reporting requirements of the NFRD if their parent company publishes the necessary non-financial information at consolidated level in accordance with the NFRD.

There are a number of potential arguments to support the extension of the personal scope of the NFRD:

- Changes in the legislative framework: following the adoption of the Regulation on sustainability-related disclosure in the financial services sector and of the Taxonomy Regulation, investors may require non-financial information from a broader range of investees in order to comply with their own sustainability-related reporting requirements.

- Large unlisted companies can have significant impacts on society and the environment. There may therefore be no *a priori* reason to differentiate between listed and non-listed companies in this respect. In addition, the difference in treatment between listed and non-listed companies in this regard may serve as a disincentive for companies to become listed, and therefore undermine the attractiveness of capital markets.

- Exempting PIEs that are subsidiaries limits the information about impacts on society and the environment, thus undermining the ability of stakeholders of such exempted subsidiaries to hold them accountable for their impacts on society and the environment, especially at local and national level.

Question 40.: If the scope of the NFRD were to be broadened to other categories of PIEs, to what extent would you agree with the following approaches?

	1	2	3	4	5	Don't know
Expand scope to include all EU companies with securities listed in regulated markets, regardless of their size.				X		
Expand scope to include all *large* public interest entities (aligning the size criteria with the definition of *large undertakings* set out in the Accounting Directive: 250 instead of 500 employee threshold).			X			
Expand scope to include *all* public interest entities, regardless of their size.			X			

(1= totally disagree, 2= mostly disagree, 3= partially disagree and partially agree, 4= mostly agree, 5= totally agree)

Question 41.: If the scope of the NFRD were to be broadened to non-PIEs, to what extent would you agree with the following approaches?

	1	2	3	4	5	Don't know
Expand the scope to include *large non-listed* companies.			X			
Remove the exemption for companies that are subsidiaries of a parent company that reports non-financial information at group level in accordance with the NFRD.		X				
Expand the scope to include large companies established in the EU but listed outside the EU.		X				
Expand the scope to include large companies not established in the EU that are listed in EU regulated markets.				X		
Expand scope to include *all* limited liability companies regardless of their size.		X				

(1= totally disagree, 2= mostly disagree, 3= partially disagree and partially agree, 4= mostly agree, 5= totally agree)

Question 42.: If *non-listed* companies were required to disclose non-financial information, do you consider that there should be a specific competent authority in charge of supervising their compliance with that obligation?

Yes X	No	Don't know

If yes, please specify who in your opinion should carry out this task (National Competent Authorities, European Supervisory Authorities, other...) and how.

National Competent Authorities building on existing supervisory practices.

Due to the nature of their activities, credit institutions and insurance undertakings have larger balance sheets than non-financial corporations. Hence, the vast majority of such institutions will exceed the balance sheet threshold in the definition of large undertakings set-out in the Accounting Directive. Moreover, the application of some public disclosure requirement of EU prudential regulation for credit institutions and insurance undertakings is defined based on various size thresholds.

For example:

- the Regulation on prudential requirements for credit institutions and investment firms includes in its definition of large credit institutions those with a total value of assets equal to or greater than EUR 30 billion;

- the same Regulation defines small and non-complex institutions as those that have EUR 5 billion or less total assets;

- the consultation paper published by EIOPA in October 2019 proposes to revise article 4 thresholds of Solvency II (below which entities are excluded from the scope of Solvency II), doubling the thresholds related to the technical provisions (from EUR 25M provisions to EUR 50M) and allowing Member States to set the threshold referring to premium income between the current EUR 5M and until a maximum of EUR 25M.

Question 43.: To what extent do you agree with the following statements relating to possible changes of the personal scope of the NFRD for financial institutions?

	1	2	3	4	5	Don't know
The threshold criteria for determining which banks have to comply with the NFRD provisions should be different from those used by Non-Financial Corporates.						X
The threshold criteria for determining which insurance undertakings have to comply with the NFRD provisions should be different from those used by Non-Financial Corporates.						X

(1= totally disagree, 2= mostly disagree, 3= partially disagree and partially agree, 4= mostly agree, 5= totally agree)

Please provide any comments or explanations to justify your answers to questions 40 to 43.

From a fund or fund manager perspective, the more companies in scope, the more information will be available but there will be an associated indirect cost implication that needs to be carefully considered.

We have "mostly agreed" with the proposal under Q. 40 to include all EU companies with securities listed in regulated markets, regardless of their size. In that regard, we would like to highlight that listed financial products, such as investment funds structured as companies, should not be included within the scope of the NFRD nor should fund management companies. Investment funds and fund management companies will be subject to the disclosure requirements under the SFDR, a regime devised especially for financial products and financial market participants, whereas the NFRD is aimed at corporate (real economy companies) with disclosure requirements reflecting their business operations. Fund management companies and investment funds will use the data disclosed by companies under the NFRD in order to meet their own compliance and disclosure obligations under the SFDR and the Taxonomy Regulation. Therefore, it would not make sense for certain investment funds or fund management companies to become subject to the NFRD. Save for this point, we agree with inclusion of all EU companies with securities listed in regulated markets, regardless of their size.

Extending NFRD fully for all companies would incur significant initial costs / disruption so a gradual extension would be recommended. This could involve starting with listed companies and larger companies and expanding the framework to other types of non-listed companies after the framework is established.

There will be a need to apply different thresholds across different industry sectors. It is also acknowledged that different levels of reporting and exemptions for companies will cause challenges relating to consistency and availability of data. Furthermore, aggregating the underlying data for consistency is likely to be challenging. However, a balance also needs to be struck in extending the scope of the NFRD, particularly to smaller non-listed companies in terms of the costs incurred.

8. SIMPLIFICATION AND REDUCTION OF ADMINISTRATIVE BURDENS FOR COMPANIES

Question 44.: If your company publishes non-financial information pursuant to the NFRD, please state how much time the employees of your company spend per year carrying out this task, including time of retrieving, analysing and reporting the information? Please provide your answer in terms of full-time-equivalents (FTEs, 1 FTE= 1 employee working 40h a week during 250 working days per year). Please provide your answer for reports published in 2019, covering financial year 2018.

N/A

Please state the total cost per year of any external services, *excluding the cost of any assurance or audit services*, that you contracted to assist your company to comply with the requirements of the Non-Financial Reporting Directive. Please provide your answer for reports published in 2019, covering financial year 2018.

N/A

The majority of Member States have transposed the NFRD requirements into national legislation making very few changes to the wording of the legal provisions. Therefore, in the majority of the national legal frameworks, companies are required to comply with national legislation that is quite high level, not very prescriptive and do not require the use of any particular reporting standard.

Question 45.: To what extent do you agree with the following statements?

	1	2	3	4	5	Don't know
Companies reporting pursuant to the NFRD face uncertainty and complexity when deciding what non-financial information to report, and how and where to report such information.					X	
Companies are under pressure to respond to individual demands for non-financial information from sustainability rating agencies, data providers and civil society, irrespective of the information that they publish as a result of the NFRD.				X		
Companies reporting pursuant to the NFRD have difficulty in getting the information they need from business partners, including suppliers, in order to meet their disclosure requirements.				X		

(1= totally disagree, 2= mostly disagree, 3= partially disagree and partially agree, 4= mostly agree, 5= totally agree)

Please provide any comments or explanations to justify your answers to questions 44 to 45.

We understand that many companies do face challenges in seeking to determine what non-financial information to report, and how and where to report such information. We also note that given the rapidly evolving nature of the ESG landscape, companies are increasingly under pressure to respond to individual demands for non-financial information from sustainability rating agencies, data providers and civil society, irrespective of the information that they publish as a result of the NFRD. Greater convergence towards consistent, high quality non-financial reporting is therefore to be welcomed.

In that regard, we note that additional due diligence will be required on the underlying data. Financial reporting requires historic quantitative investment data at a point in time – non-financial reporting data requires multi-faceted ongoing continuous qualitative data disclosure.