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IMPACT ASSESSMENT

Accompanying the document

Proposal for a Directive of the European Parliament and of the Council

amending Directive 2013/34/EU, Directive 2004/109/EC, Directive 2006/43/EC and Regulation (EU) No 537/2014, as regards corporate sustainability reporting

{COM(2021) 189 final} - {SEC(2021) 164 final} - {SWD(2021) 151 final}

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Glossary

Term or acronym	*Meaning or definition*
KPIs	Key Performance Indicators
NFRD	Non-Financial Reporting Directive
ESG	Environmental, social and governance
SMEs	Small and medium-sized enterprises
SFDR	Sustainable Finance Disclosure Regulation
GRI	Global Reporting Initiative
CRR	Capital Requirements Regulation
SASB	Sustainability Accounting Standards Board
IIRC	International Integrated Reporting Council
ESAP	European Single Access Point
CMU	Capital Markets Union
ESMA	European Securities and Markets Authority
TR	Taxonomy Regulation
EMAS	Eco-management and Audit Scheme
LPD	Late Payments Directive
TCFD	Task Force on Climate-related Financial Disclosures

1. INTRODUCTION: POLITICAL AND LEGAL CONTEXT

This impact assessment concerns a proposed initiative on annual public reporting of non-financial information by companies. It considers different policy options, taking account of the existing legal provisions introduced by the Non-Financial Reporting Directive.[1]

1.1 How does this initiative contribute to the political priorities of the Commission and the EU?

This initiative is part of the Commission's 2020 Work Programme and is one of the actions proposed by the European Commission to implement the **European Green Deal**.[2] The European Green Deal is Europe's new growth strategy. It aims to transform the Union into a modern, resource-efficient and competitive economy with no net emissions of greenhouse gases by 2050. It will decouple economic growth from resource use, and ensure that all regions and citizens of the EU participate in a socially just transition to a sustainable economic system.

Private finance has an important role to play in meeting the objectives of the European Green Deal. This initiative will support sustainable private finance, by helping investors identify companies that carry out sustainable activities.[3] The Commission will present a renewed sustainable finance strategy in the fourth quarter of 2020, building on the 2018 Sustainable Finance Action Plan.[4]

This initiative also supports the current European Commission's objective of ensuring **An Economy that Works for People**. It contributes to the completion of the Capital Markets Union, by enabling investors, and other stakeholders, to access comparable non-financial information from investee companies across the EU. It aims to enable SMEs to better contribute to and benefit from the transition to sustainable economy. This impact assessment takes an "SME-first" approach. A culture of greater accountability and transparency from companies regarding their impacts on society and the environment could also help to strengthen the social contract between business and citizens, and contribute to a greater sense of social fairness.

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[1] This impact assessment uses the terms "non-financial information" and "non-financial reporting", consistent with the existing Non-Financial Reporting Directive. Other terms commonly used to refer to the same or similar concepts are "sustainability reporting/information" and "environmental, social and governance (ESG) reporting/information". The use of "non-financial reporting/information" in this document does not prejudge any decision on the terms that may be used in the Commission's legislative proposal.

[2] Communication from the Commission on the European Green Deal, COM(2019)640 final, 11 December 2019. Commission Work Programme 2020: A Union that Strives for More, COM(2020) 37 final, 29 January 2020. Adjusted Commission Work Programme 2020)

[3] Investors in its broader sense, includes as well asset managers.

[4] Communication from the Commission - Action Plan: Financing Sustainable Growth COM(2018)097 final This text will be updated as appropriate after adoption of the Renewed Sustainable Finance Strategy, which is scheduled for adoption after this draft impact assessment is submitted to the RSB, but before the Commission adopts a proposal on the revision of the Non-Financial Reporting Directive.

In addition, this initiative supports the objective of **A Europe Fit for the Digital Age.** The Commission has stated that the "twin challenge of a green and digital transformation has to go hand-in-hand".[5] Non-financial information reported by companies should become part of the single European data space. This initiative can create opportunities for reporting companies, investors, civil society and other stakeholders to radically improve the way in which non-financial information is reported and used through the use of digital technologies.

The Covid-19 pandemic is expected to further accelerate the growth in demand for non-financial information from companies. At the same time, the economic crisis generated by the pandemic makes it ever more important to avoid the imposition of unnecessary administrative costs on business. Annex 6 summarises the implications of the Covid-19 pandemic for this initiative.

This initiative reflects the calls by the Council and the European Parliament to consider further action to improve non-financial reporting. 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.[6] 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 Non-Financial Reporting Directive.[7]

A wide variety of different organisations and stakeholders have called for consideration of a new regulatory approach to non-financial reporting, including the International Monetary Fund, central banks in the Network for Greening the Financial System, investors, some business associations, civil society organisations and trade unions.

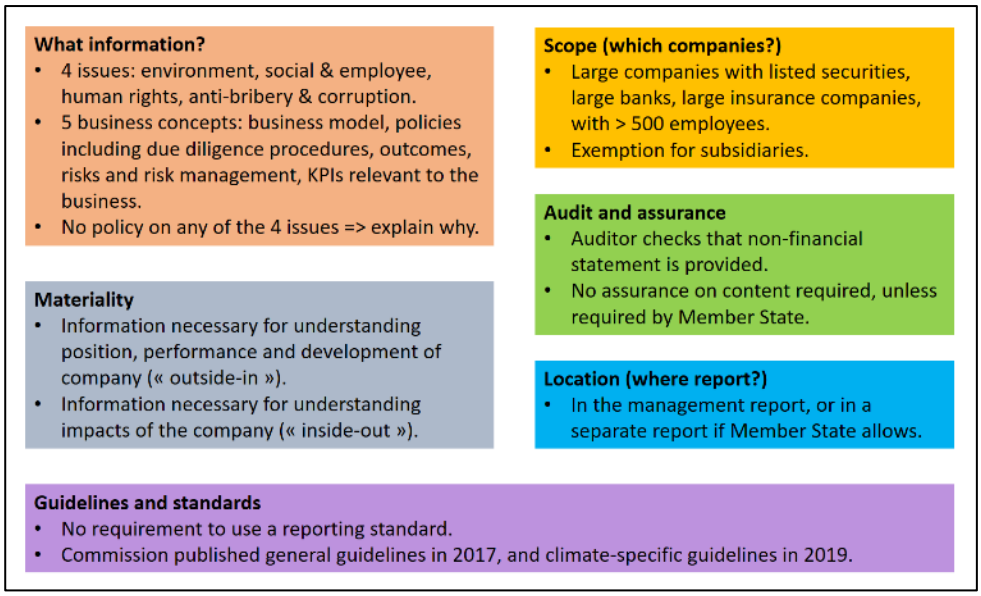
1.2 What is the legal and policy context?

1.2.1 The Non-Financial Reporting Directive

In 2014 the EU agreed the Non-Financial Reporting Directive (Directive 2014/95/EU), which amended the Accounting Directive (Directive 2013/34/EU). The Non-Financial Reporting Directive (NFRD) imposed new reporting requirements on certain large companies. Companies under the scope of the NFRD had to report according to its provisions for the first time in 2018, for information covering financial year 2017. This section highlights some of the main provisions of the NFRD. Annex 7 provides a full description of the NFRD.

[5] Communication from the Commission: Shaping Europe's Digital Future.
[6] Council Conclusions on the Deepening of the Capital Markets Union (5 December 2019)
[7] European Parliament resolution of 29 May 2018 on sustainable finance (2018/2007(INI))

The Non-Financial Reporting Directive at a glance



As required by the NFRD, in 2017 the Commission published non-binding guidelines for companies under the scope of the Directive.[8] In 2019, the Commission published additional guidelines, specifically on reporting climate-related information.[9] If companies use reporting frameworks, then they have to specify which frameworks they have used. The NFRD does not, however, require the use of a reporting framework or standard.

The NFRD applies to large public interest entities with more than 500 employees.[10] In practice this means that it applies to large EU companies with securities listed in EU regulated markets, large banks (whether listed or not) and large insurance companies (whether listed or not) – all provided they have more than 500 employees. The NFRD exempts the subsidiaries of parent companies from the reporting obligation, if the parent company itself reports the necessary information on a consolidated basis. We estimate that approximately 11 700 companies are subject to the reporting requirements of the NFRD.[11]

The NFRD identifies four non-financial 'matters': environment, social and employee matters, human rights, and anti-corruption and anti-bribery. With regard to those four matters, it requires companies to disclose information about five business concepts: business model, policies (including due diligence processes implemented), the outcome of those policies, risks and risk management, and key performance indicators (KPIs)

[8] Communication from the Commission — Guidelines on non-financial reporting (methodology for reporting non-financial information) C/2017/4234
[9] Communication from the Commission — Guidelines on non-financial reporting: Supplement on reporting climate-related information C/2019/4490
[10] It also applies to public interest entities which are parent companies of a large group with more than 500 employees.
[11] This figure takes account of how Member States have transposed the Directive. Not taking account of national transposition, about 2 000 companies are under scope of the NFRD.

relevant to the business.[12] Annex 8 provides illustrative examples of the kind of information that companies could be expected to disclose under the NFRD.

Companies under the scope of the NFRD are required to disclose information "to the extent necessary for an understanding of [their] development, performance, position and impact of [their] activity." The reference to "impact" represented a significant innovation: it introduced a double materiality perspective, whereby companies have to report information not only on how non-financial issues affect the company ("outside-in" perspective), but also regarding the impact of the company itself on society and the environment ("inside-out" perspective).

The NFRD requires the auditor to check that the company has provided a non-financial statement, but does not require the auditor to assure the content of the information. However, Member States may require assurance on the content of the information reported and three Member States (Italy, Spain and France) have used this option.

Annex 9 provides an overview of how Member States have transposed the NFRD.

1.2.2 Other relevant EU legislation and policy

The Sustainable Finance Disclosure Regulation and the Taxonomy Regulation, together with the NFRD, are the central elements of the sustainability reporting regime that underpins the EU's Sustainable Finance Strategy.

The **Sustainable Finance Disclosure Regulation** (SFDR) governs how financial market participants (including assets managers and financial advisers) should disclose sustainability information towards end investors and asset owners.[13] Financial market participants can only meet the requirements of the SFDR if they have access to adequate information from investee companies. Since the NFRD governs reporting by investee companies, there is an obvious case for ensuring alignment between the disclosure requirements of the NFRD and the SFDR.

The **Taxonomy Regulation** creates a classification system of environmentally sustainable economic activities with the aim of scaling up sustainable investments and combatting greenwashing of 'sustainable' financial products.[14] It requires companies under the scope of the NFRD to disclose the extent to which their activities are considered environmentally sustainable according to the taxonomy. Financial market participants subject to the SFDR must disclose the extent to which financial products marketed as sustainable are aligned with the taxonomy. The taxonomy therefore

[12] Due diligence in this context refers to the process by which companies identify, prevent, mitigate and account for how they address actual and potential adverse impacts in their own operations, their supply chain and other business relationships (OECD Guidelines for Multinational Enterprises).
[13] Regulation (EU) 2019/2088. Financial market participants have to comply with the SFDR as from 10 March 2021.
[14] Regulation (EU) 2020/852

represents an important reference point that further strengthens the interactions between the SFDR and the NFRD.

The goal is to create a consistent and coherent flow of sustainability-related information through the financial value chain. To achieve this, consistency and alignment between the future technical standards of the SFDR and any possible standards developed under the NFRD will be especially important. Annex 10 describes in more detail the interactions between the NFRD, the SFDR and the Taxonomy Regulation, including a graphical representation of these interactions.

This initiative will also be closely coordinated with certain other Commission initiatives, including in particular:

- **European Single Access Point**: as part of the Action Plan on the Capital Markets Union, the Commission will put forward a legislative proposal in 2021 to set up a European Single Access Point (ESAP) – an EU-wide digital access platform to companies' public financial and non-financial information.[15] It will facilitate access to the non-financial information that companies disclose under the NFRD, provided that such information is digitally tagged in the appropriate way.

- **Sustainable corporate governance**: the Commission will propose a new initiative in 2021 to embed sustainability in the corporate governance framework and foster behavioural change in companies by addressing issues such as the duty of care of company directors, the integration of sustainability into corporate strategies, the setting of science-based sustainability targets, and due diligence for environmental and human rights impacts. To ensure coherence and maximum alignment, the NFRD could mandate the disclosures that may be necessary under the proposed sustainable corporate governance initiative.

- **Pay Transparency**: the Commission has adopted a proposal aimed at strengthening the application of the principle of equal pay for equal work or work of equal value between men and women through pay transparency and enforcement mechanisms.[16] This proposal includes requirements on certain companies to make information regarding the gender pay gap publicly available. Some of these companies may also be covered by the Non-Financial Reporting Directive (NFRD). Both initiatives will be aligned so that any public reporting on the gender pay gap pursuant to the Pay Transparency Directive by companies subject to the NFRD would be taken into account in possible standards for non-financial reporting under the NFRD.

[15] Commission Communication "A Capital Markets Union for people and businesses – new action plan", 24 September 2020, COM(2020) 590 final.
[16] COM (2021)93

- **Green Claims Initiative**: the Commission is considering a new legislative initiative to tackle false claims of environmental sustainability. Under the Green Claims Initiative, companies that voluntarily choose to make green claims would have to substantiate such claims against a standard environmental impact methodology. Environmental information published in company annual reports, which is regulated by the NFRD, does not fall within the definition of "green claims". Any legislation of green claims would therefore not apply to the information in company annual reports. Nevertheless, to promote coherence and maximum alignment, the revision of the NFRD could as far as possible refer to the environmental impact methodologies that are likely to form the basis of any Commission initiative on green claims.

- **Environmental accounting**: the Commission is co-financing a new business led initiative to develop standardised environmental accounting principles within the EU and internationally. Company-level environmental accounting practices can play an important role in quantifying companies' environmental impacts and should help to underpin the content of environmental information that they disclose under the NFRD.

Annex 10 provides a more comprehensive list of relevant EU legislation and policy initiatives, and a more in depth analysis of the interactions.

2. PROBLEM DEFINITION

This section summarises the identified problems, and the consequences and drivers of those problems. Annex 12 provides a more detailed analysis of the problems.

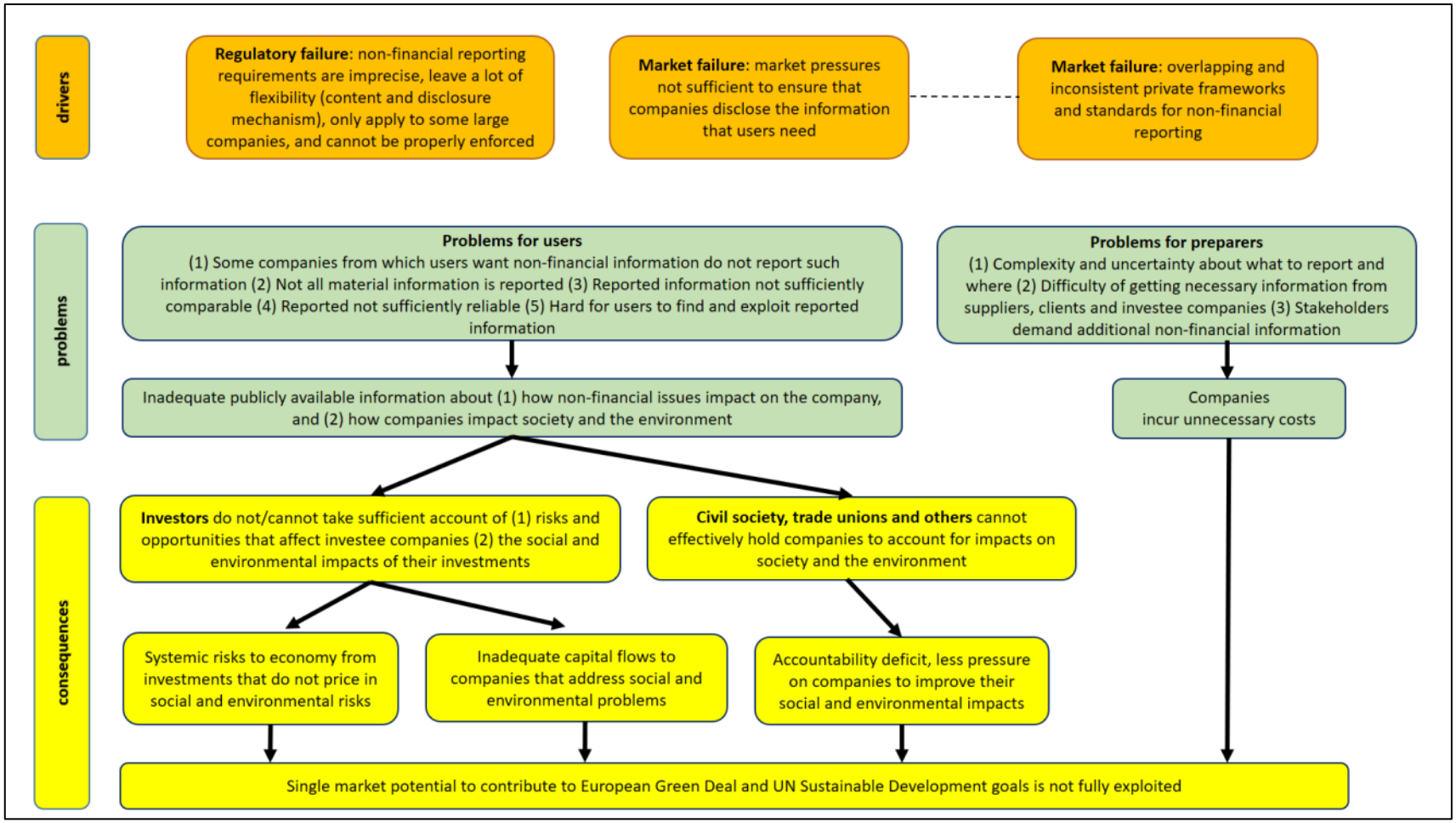
In March 2021, the Commission published a Fitness Check on the overall EU framework for public corporate reporting by companies (financial reporting and non-financial reporting), together with a report on the NFRD itself as required by the review clause (Article 3) in the Directive.[17]

The deficiencies in current non-financial reporting identified in this section reflect the principal findings of the Fitness Check and the review clause report. In addition, this section extends beyond the Fitness Check and the review clause report with regard to presenting the consequences and the drivers of those deficiencies.[18]Stakeholder consultations have helped to validate the problem definition, in particular open consultations organised in 2018 for the Fitness Check and in 2020 for this review of the NFRD. Annex 2 provides a summary of all stakeholder consultations and their results.

[17] Publication office please insert reference to Report from the Commission to the European Parliament, the Council and the European Economic and Social Committee on the review clauses in Directives 2013/34/EU, 2014/95/EU, and 2013/50/EU, and accompanying SWD- Fitness Check.

[18] Since the Fitness Check covered the whole public corporate reporting framework, it could not go into such depth on some of the specificities of non-financial reporting.

Figure 1 - Integrated overview of drivers, problems and consequences



2.1 What are the problems?

It is useful to make a distinction between problems for users of non-financial information disclosed in company annual reports, and problems for preparers of that information (that is to say, reporting companies).

2.1.1 Problems and consequences from a user perspective

This problem analysis focusses on the primary intended users of non-financial information disclosed in company annual reports:

- on the one hand investors, including asset managers, who want to better understand the risks and opportunities that non-financial issues pose to their investments, as well as to better understand the social and environmental impacts of those investments;
- and on the other hand, non-governmental organisations, trade unions and other stakeholders, who want to better hold companies to account for their social and environmental impacts.[19]

Many investors and asset managers purchase non-financial information from third party data providers, who collect information from various sources including public corporate reports. However, investors remain the end users of this information, and third party data providers are therefore not considered primary intended users of this initiative.

Other stakeholders may also make use of non-financial information disclosed in annual reports. Policy makers and environmental agencies may make use of such information, in particular on an aggregate basis, to monitor environmental and social trends, to contribute to environmental accounts, and to inform public policy. Few individual citizens and consumers directly consult company non-financial statements, but more use such information indirectly, for example when considering the advice or opinions of financial advisers or non-governmental organisations.

The **specific problems from the user perspective** of non-financial information are:

a) Some companies from which users want non-financial information do not report such information.
b) Many companies that do report non-financial information nevertheless do not report all relevant information that users need or want.
c) Reported information is not sufficiently comparable.
d) Reported information is not sufficiently reliable.
e) It is hard for users to find and exploit the information they are looking for even when that information is reported.

[19] Such organisations seek to hold companies to account in a number of different ways. They may engage directly with individual companies in light of information about specific adverse social and/or environmental impacts. They may run campaigns regarding individual companies, or on particular issues or sectors.

Whether a company reports against a recognised reporting standard, and whether the reported non-financial information is assured, are useful proxies for assessing the relevance, comparability and reliability of the reported information. They therefore help to illustrate the size of the problems from a user perspective. Based on CEPS study, we estimate that only around 20% of large limited liability companies in the EU comprehensively apply recognised reporting standards, and only around 30% publish non-financial information that has been assured at least to a minimum level.

It is widely recognised that information on intangible assets is underreported, even though such assets currently represent the majority of investment carried out by the private sector in advanced economies.[20]

Amongst other reasons, the lack of digitalisation of the information reported and the lack of clarity about which company in a group is required to report non-financial information, lead to problems of searchability and accessibility of the information.

These specific problems lead to the following **general problem from the user perspective**: users do not have access to adequate information about how non-financial issues, and sustainability issues in particular, might impact companies, or about how the company itself impacts society and the environment.

The **consequences of the problems from a user perspective** depend on which users are considered:

a) Investors are unable to take sufficient account of sustainability-related and other non-financial risks and opportunities in their investment decisions. This has the potential to create systemic risks that threaten financial stability.[21]
b) Investors are also less able to channel financial resources to companies and economic activities that address and do not exacerbate social and environmental problems.
c) Non-governmental organisations, trade unions and other stakeholders are less able to hold companies accountable for their impacts on society and the environment. This creates an accountability deficit, and may be a contributory factor in the weakening of the social contract between business and citizens, with effects on the efficient functioning of the social market economy.

[20] See for example: "Investment in intangible assets in the euro area" in *ECB Economic Bulletin, Issue 7/2018*, European Central Bank, 2018; and *Productivity and secular stagnation in the intangible economy*, Jonathan Haskel, Stian Westlake, 31 May 2018

[21] This is most obviously the case with regard to climate change: see for example on "Climate change and financial stability" in *Financial Stability Review*, European Central Bank, 2019. However it also applies to other non-financial issues. See for example analyses by the Dutch National Bank on the exposure of the Dutch financial sector to biodiversity risk, water scarcity and risk related to human rights, amongst other issues (*Indebted to nature: Exploring biodiversity risks for the Dutch financial sector*, DNB, 2020 and *Values at risk: Sustainability risks and goals in the Dutch financial sector*, DNB, 2019).

2.1.2 Problems and consequences from a preparer perspective

The **specific problems from a preparer perspective** are:

a) Preparers face difficulty and complexity when deciding what information to report.
b) Preparers find it difficult to get the non-financial information they need from suppliers, clients and investee companies to report adequately.
c) Preparers receive information requests from stakeholders in addition to the information they report to fulfil their legal requirements.

The **general problem from a preparer perspective** created by these specific problems is that preparers incur unnecessary costs associated with the reporting of non-financial information.

2.1.3 Overall consequences

The **overall consequence of these general and specific problems** is that the potential of the European Single Market to contribute to the objectives of European Green Deal, and to the achievement of the UN Sustainable Development Goals, is not fully exploited.

2.2 What are the problem drivers?

The drivers of the identified problems are market and regulatory failures.

2.2.1 Market failures

Non-financial information from companies can be considered a public good, since one user's "consumption" of the information does not reduce the amount available for others. In addition, it is not possible to charge for access to publicly available non-financial information because there is an obvious free-rider problem. This leads to a supply of non-financial information that is below market demand. Although some companies would publish non-financial information in the absence of an obligation to do so (because they find it beneficial, for example in terms of reputation or access to capital), overall, in the case of an unregulated market, the supply of information is unlikely to meet users' demand.

There has been a very significant increase in demand for non-financial information in recent years, especially on the part of the investment community. This increase in demand is driven by the changing nature of risks to companies and by growing investor awareness of the financial implications of those risks.[22] It is also driven by the growth in

[22] An analysis of World Economic Forum reports over recent years shows a dramatic increase in the perception of the likelihood and impact of environmental risks. The 2020 World Economic Forum Global Risk Report shows the top 5 global risks as estimated by the WEF from 2007-2020. In the period 2007-13 (which covers the years up to the approval of the NFRD by the EU), environmental risks accounted on average for 17% the top 5 risks per year in terms of likelihood and just 6% of the top 5 risks in terms of impact. For the period 2014-2020 (since the NFRD was approved), the figures rise to 54% and 46% respectively. The figures for the just the last three years 2018-2020 are higher still: 73% and 60% respectively.

investment products that explicitly seek to meet certain sustainability standards or achieve certain sustainability objectives.[23]

However, market forces on their own have not so far been sufficient to ensure that companies report the non-financial information that is needed to meet the increase in demand. Recognition of this failure lies behind many of the calls for stronger policies on non-financial reporting, including regulatory action, from organisations such as central banks and the International Monetary Fund.[24] The European Securities and Markets Authority (ESMA) has recommended stronger non-financial reporting requirements as a means of addressing undue short-termism in securities markets.[25]

Market forces have catalysed the creation of a large number of non-financial reporting standards and frameworks, at international, national and sector level.[26] Furthermore, new initiatives continue to emerge. The market on its own however has not ensured that many companies fully apply any of the existing standards and frameworks. For example, the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) are widely respected as authoritative guidance on climate reporting, but the 2020 TCFD status report suggests that significant implementation challenges remain.[27]

The market on its own has also not so far been able to ensure adequate convergence and consolidation between the different frameworks and standards. There are overlaps and inconsistencies between them, including in terms of the non-financial issues they cover, and the intended audience of the disclosures they recommend. This is a significant driver of the reporting burden for preparers, and of the problems faced by users in terms of limited comparability and relevance of reported information.

2.2.2 Regulatory failure

The EU agreed the NFRD before a number of landmark EU and global policy developments, including the UN Sustainable Development Goals (2015), the Paris

[23] This phenomenon is often referred to as "Environmental, social, and governance investing", or "ESG investing". There are many different approaches to and definitions of ESG investing, which significantly complicates the task of measuring its growth (see *European Sustainable and Responsible Investment (SRI) Study 2018*, EUROSIF). Nevertheless, the OECD has concluded that "the growth of assets under management that incorporates some element of ESG review and decision-making has grown exponentially over the past decade" (Boffo, R., and R. Patalano (2020), *ESG Investing: Practices, Progress and Challenges*, OECD). According to the OECD, "in the US, the current level of ESG investing is now over 20% of all professionally managed assets, at over USD 11 trillion", while in Europe, "industry data related to a broader range of ESG practices suggests the level is over USD 17 trillion." According to a report in the Financial Times, research carried out by PwC has predicted that "ESG funds will experience a more than threefold jump in assets by 2025, increasing their share of the European fund sector from 15 per cent to 57 per cent."

[24] See *October 2019 Global Financial Stability Report (GFSR)*, International Monetary Fund, and *A call for action: Climate change as a source of financial risk*, Network for Greening the Financial System, April 2019.

[25] *Report on Undue Short-term Pressure on Corporations from Financial Markets*, ESMA, December 2019

[26] Annex 13 provides an overview of the principal international standards and frameworks, highlighting some of the most relevant similarities and differences.

[27] *Task Force on Climate-related Financial Disclosures: 2020 Status Report*, Task Force on Climate-related Financial Disclosures. The report notes that the disclosure of TCFD-aligned information increased by six percentage points, on average, between 2017 and 2019. While applauding the progress made, report states that "companies' disclosure of the potential *financial* impact of climate change on their businesses and strategies remains low."

Agreement on climate change (2016), the EU Sustainable Finance Action Plan (2018) and the European Green Deal (2019). These more recent policy developments reflect a growing political and social awareness of the intensity of the sustainability crisis. For most sectors of the economy, including the financial sector, sustainability has clearly moved from the margins to the mainstream in a relatively short period of time. Overall, the political choices that shaped the NFRD in 2014, while valid at the time they were made, may not be appropriate in the current circumstances.

The following characteristics of the NFRD are drivers of the specific problems identified in section 2.1:

- Scope: The NFRD only ensures that large listed companies, large banks and large insurance companies disclose non-financial information, and only if they have more than 500 employees. This does not include some companies from whom users need non-financial information.
- Flexibility and lack of granularity of reporting requirements: The reporting requirements in the NFRD are high level and principles based. The NFRD does not specify in any significant detail the information that companies should disclose, and does not require companies to use a non-financial reporting standard. The accompanying guidelines are not binding, and, with the exception of the climate reporting guidelines, do not provide detailed guidance to companies. Companies therefore have considerable discretion in deciding what information to report and in the application of the materiality principle. Together, these characteristics of the NFRD help to explain why there are problems with the comparability of information, and why many companies do not disclose all information that users think is relevant. The inadequate reporting of intangible assets is at least partly explained by the fact that the Accounting Directive, even as amended by the NFRD, does not explicitly require companies to report on intangibles.
- Assurance: The statutory auditor has to verify that the non-financial statement is included in the report, but is not obliged to verify the content of the statement or the internal processes behind it. This limits the reliability of reported information.
- Location of reported information: The NFRD allows Member States to allow companies to report non-financial information in a separate report rather than in the management report. This helps to explain why many companies do not adequately address the connectivity between financial and non-financial information in their reports. Publication of non-financial information in a separate report also makes information harder to find and impacts negatively on its perceived reliability.
- Enforcement: the provisions of the NFRD are difficult to enforce. This is mainly because the disclosure requirements are high level, principles-based and flexible. Additionally, the non-financial statement falls outside the scope of supervision of some national competent authorities due to the lack of coordination between the

provisions of the NFRD and the Transparency Directive.[28] The difficulty of enforcing the NFRD contributes to many of the problems experienced by users, in particular the limited comparability and reliability of reported information and the fact that much information considered relevant by users is not reported.

A comparison with EU rules for financial reporting helps to illustrate how certain characteristics of the NFRD are drivers of the specific problems identified in section 2.1. Overall, and in spite of certain specific problems, the Fitness Check on corporate reporting found that the EU framework for financial reporting broadly meets its intended objectives and ensures that users' needs are adequately met.

Most significantly, the EU framework for financial reporting requires companies to report according to clear rules set out in the Accounting Directive, and in practice Member States require compliance with national accounting standards. In addition, EU companies listed on the EU financial markets are required by the International Accounting Standards Regulation to prepare their consolidated financial statements in accordance with International Financial Reporting Standards (IFRS). The mandatory use of common financial reporting standards is a major explanation for why users face far fewer problems regarding the relevance and comparability of financial information than is the case for non-financial information. Mandatory common standards mean that companies have much less discretion about what financial information to report compared to the very considerable discretion that they have in the case of non-financial information. In the view of the European Securities and Markets Authority (ESMA), "the effectiveness of the applicable framework and the comparability of the resulting disclosures would have been greater had the [NFRD] set up or indicated a specific framework and accepted a single set of standards to report this type of information."[29]

In addition, the EU framework for financial reporting covers all companies from which users need financial information, with no apparent gaps, and it imposes audit requirements for financial information that provide a significantly higher level of reliability than is the case for non-financial information. Finally, supervision and enforcement of non-financial information lags behind what is done in the case of financial information, and this is partly the result of differences in the respective regulatory frameworks. ESMA believes that "the optionality that characterises the non-financial disclosure requirements (e.g. in relation to the applicable frameworks, the location and timing of publication of the NFS and the assurance) does not yet allow a satisfactory convergence of disclosure practices thus undermining the consistency of supervisory approaches which is urgent to achieve in this area."

[28] The Transparency Directive lacks an explicit reference to the non-financial statement in its mandate to national competent authorities to supervise reporting by companies (Articles 7, 24(4)h, 24(4b), 28, 28a, 28b, 28c and 29 of the Transparency Directive).

[29] *Enforcement and Regulatory Activities of European Accounting Enforcers in 2018*, ESMA

2.3 How will the problems evolve?

Some analyses find that the quality of non-financial reporting is improving.[30] Others acknowledge that the quality of reporting is improving but conclude that these improvements are nevertheless insufficient to meet users' needs.[31] Still other analyses find little evidence of improvement, and even some negative trends.[32] At the same time, most observers predict that the information needs of users, in particular investors, will continue to grow significantly.[33] The Covid-19 pandemic is likely to accelerate this trend (see annex 6). Overall, we conclude that the gap between the information needs of users and the non-financial information reported by companies will continue to grow.

There is little evidence to suggest that the complexity and burden experienced by preparers will diminish. Indeed responses to the public consultation indicate that for many preparers these problems are intensifying.

Section 5.1 (the baseline scenario) provides a more detailed description of the expected evolution in the case of no new policy initiative by the European Union.

3. WHY SHOULD THE EU ACT?

3.1 Legal basis

In this Impact Assessment we consider two Articles of the TFEU as legal basis for the proposed initiative. Firstly, Article 50 TFEU, the traditional legal basis for company law legislation, and in addition, Article 114 TFEU, *lex generalis* that applies as well with the objective of establishing or ensuring the functioning of the internal market. See further details in annex 15.

3.2 Subsidiarity: Necessity of EU action

The disclosure of non-financial information is already regulated at EU level by the Accounting Directive (as amended by the NFRD). Transparency rules are necessary to ensure investor protection and financial stability across the EU, while allowing civil society organisations and other stakeholders hold companies accountable for their impacts on the environment and society. Additionally, common rules on non-financial reporting ensure a level playing field among companies established in the different

[30] For example: *In Balance 2019 - Survey of value creation and follow-up to the Non-Financial Information (Disclosure) Decree*, Dutch Authority for the Financial Markets (AFM), December 2019.
[31] For example: *Social and environmental value creation*, Association of Chartered Certified Accountants, 2019; and *October 2019 Global Financial Stability Report (GFSR)*, International Monetary Fund
[32] For example: *2019 Research Report An analysis of the sustainability reports of 1000 companies pursuant to the EU Non-Financial Reporting Directive*, Alliance for Corporate Transparency 2020; and *Corporate Climate Crisis Awareness Study 2019*, Piotr Bernacki, Michal Stalmach, Foundation for Reporting Standards, Polish Association of Listed Companies (SEG), Bureau Veritas Poland.
[33] For example: *Stakeholder Perceptions of Non-Financial Reporting*, UK Department for Business, Energy and Industrial Strategy, 2019

Member States. If non-financial reporting requirements are significantly different in different Member States, this would create additional costs and complexity for companies operating across borders and therefore undermine the Single Market. Member States acting alone are not able to ensure the consistency of non-financial reporting requirements across the EU.

Member States acting alone are also not able to ensure the comparability of the reported non-financial information across the Single Market. The comparability of reported information enables potential investors and other users of non-financial information such as civil society organisations to better compare companies across national borders. It is therefore important on the one hand for the free movement of capital and the Capital Markets Union, especially in light of the growing relevance of non-financial information for investment decisions, and on the other hand to enable civil society organisations and other stakeholders to compare impacts of companies in different EU Member States and better hold them accountable.

Finally, only EU intervention can ensure that companies disclose the information that investors need to comply with their own disclosure obligations under the SFDR.

3.3 Subsidiarity: Added value of EU action

As attention to non-financial reporting grows in jurisdictions around the world, it becomes ever more important for the EU to engage with its partners on the basis of a coherent and comprehensive European approach. Compared to individual action by Member States, EU intervention can ensure a strong European voice in policy developments at the global level regarding non-financial reporting. This could translate into a competitive advantage for EU companies with respect to non-EU companies, as investors' interest in non-financial information increases. In addition, EU intervention can ensure that companies in all Member States report relevant, reliable and accessible non-financial information needed by European investors and civil society organisations.

4. OBJECTIVES: WHAT IS TO BE ACHIEVED?

4.1 General objectives

The general objective is – by improving EU non-financial reporting at the least possible cost – to better exploit the potential of the European Single Market to contribute to the transition towards a fully sustainable and inclusive economic and financial system in accordance with the European Green Deal and UN Sustainable Development Goals. This will be achieved by:

a) helping to reduce systemic risks to the economy resulting from the fact that many investment decisions currently do not take adequate account of sustainability-related issues;

b) improving the allocation of financial resources, so that more financial resources flow to companies and activities that address social and environmental problems and fewer resources flow to companies and activities that exacerbate such problems;
c) making companies more accountable for their impacts on society and the environment, thereby strengthening the social contract between companies and citizens.

4.2 Specific objectives

The specific objectives can be distinguished between objectives for users of non-financial information, and objectives for preparers (reporting companies).

For users, the specific objectives are to ensure that there is adequate publicly available information about the risks and opportunities that non-financial issues present for companies, and about the impacts of companies themselves on society and the environment. In order to achieve these objectives:

a) companies from which users need non-financial information should report such information;
b) companies should report all information that users consider to be relevant;
c) reported information should be comparable;
d) reported information should be reliable; and
e) reported information should be easy for users to find and exploit.

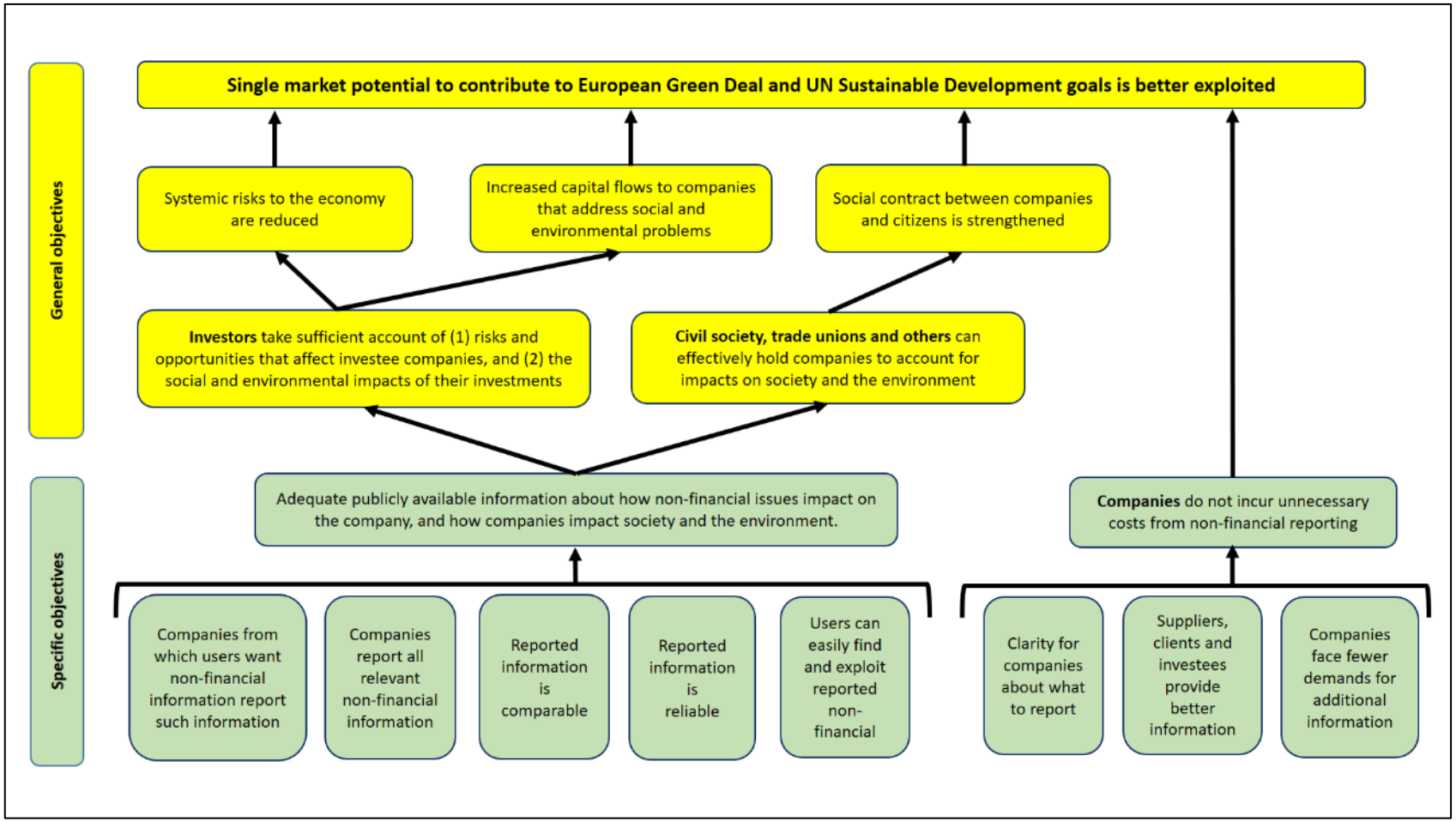
These objectives imply changing the status of non-financial information, so that over time it is more comparable to the status that the EU framework currently gives to financial information.

For preparers, the specific objective is to reduce unnecessary administrative costs associated with non-financial reporting, in particular by:

a) bringing greater clarity and certainty about the non-financial information and the methodologies behind the information they are expected to report;
b) making it easier for preparers to get the non-financial information they need for reporting purposes from their own business partners (suppliers, clients and investee companies);
c) reducing the burden created by demands for non-financial information that come in addition to the non-financial information included in company reports.

There may be trade-offs between reducing burden for reporting companies on the one hand, and meeting the information needs of users on the other hand. At the same time, the wider costs of not meeting users' information needs – for example in terms of not contributing to the objectives of the European Green Deal – will also need to be considered.

Figure 2 - Integrated overview of specific and general objectives



5. WHAT ARE THE AVAILABLE POLICY OPTIONS?

5.1 What is the baseline from which options are assessed?

Under the baseline, the EU would not develop any new regulatory or non-regulatory action specific to reporting of non-financial information. The existing provisions of the NFRD would continue to apply, together with the general and the climate-specific non-binding guidelines.

We predict that the baseline scenario is highly dynamic, with a very significant increase in the intensity of problems for users and preparers. The principal characteristics of the baseline scenario are:

- **A very significant increase in the information needs of users**. Some of this increase is the logical consequence of previously agreed EU legislation, notably the SFDR and the Taxonomy Regulation, and some would have happened in any case, due to fast-changing citizen awareness, consumer preferences and market practices, driven by the sustainability imperative. The Covid-19 pandemic will further accelerate the increase in users' information needs (see annex 6). Users will need and expect more and better information from an increasing number of companies, especially large companies but also a growing proportion of SMEs.

- **A growing gap between the information that users want and need, and the information that companies report**. In the absence of widespread consensus and clear rules about what companies should report, any improvements in non-financial reporting will remain insufficient to meet the increasing needs of users. Specifically, in the absence of requirements to report in a more standardised manner, and to assure the reported information, the gap between users' needs for relevant, reliable and comparable information and the relevance, reliability and comparability of reported information, are expected to grow. Additionally many companies from which users want information would not report, as the personal scope of the current requirements would remain the same.

- **Lack of coherence with other EU sustainability disclosure regulations, which will undermine the EU's sustainable finance objectives**. Once disclosure requirements of the SFDR and Taxonomy Regulation become applicable, there will be a growing situation of incoherence if investee companies do not report the specific information that entities subject to the SFDR and the Taxonomy Regulation need in order to meet their own reporting requirements. This in turn would seriously undermine the achievement of the EU's sustainable finance objectives.

- **An increase uncoordinated in information requests to preparers**. In an attempt to address the information gap, more users will directly contact companies to ask for the necessary information. Data providers will further develop their own proprietary questionnaires and data-collecting methodologies, which will involve more uncoordinated requests to companies for specific information.

- **Ongoing expectations on companies to use a variety of different frameworks and standards**. The proliferation of different private and public-private reporting frameworks and standards will continue and may even intensify as the value placed on non-financial information continues to grow. Different users and regulators will pressure companies to use different frameworks and standards.[34] The International Financial Reporting Standards Foundation (IFRS Foundation) is developing plans for the creation of a Sustainability Standards Board, which could be created by the end of 2021. The intention of the IFRS Foundation is, for the time being, to address climate reporting only, and to do so only from a financial materiality perspective ("outside-in" risks to the company). If the IFRS Foundation initiative is successful, it could clarify and simplify reporting expectations on companies, but only with regard to climate reporting from a financial materiality perspective. For all other sustainability issues, and for reporting on company impacts, the problems created by the co-existence of multiple different standards and frameworks would remain.

- **Significant increases in costs and burden for preparers and for users**. Users will have to dedicate more resources to finding and collecting the additional information that they need. Preparers will face higher costs due to the increase in uncoordinated information demands from users, due to the ongoing absence of consensus about what information they should report in order to meet users' needs, and due to persistent difficulties in obtaining the non-financial information they need for reporting purposes from suppliers, clients and investee companies.

- **An increase in the application of information technology and artificial intelligence to the field of non-financial information, but without resolving underlying problems**. Current trends in the use of innovative information technology and artificial intelligence will intensify, will provide new opportunities for accessing and exploiting non-financial

[34] CEPS study shows that the majority of the surveyed companies subject to the NFRD report against multiple standards and frameworks at least to a certain extent, and that the more standards or frameworks used, the higher the reporting costs companies present. For example, the Global Reporting Initiative is the single most commonly used reporting framework by companies under the scope of the NFRD, and companies in Spain and Belgium are required to use it to a certain extent. Many investors and some regulators, including the European Commission, recommend that companies report climate-related information in line with the recommendations of the Task Force on Climate-related Financial Disclosures. Meanwhile Blackrock, the world's largest asset manager, has announced that it expects companies to report according to the standards of the Sustainability Accounting Standards Board.

information, and may offset some of the predicted increases in cost and burden. However, such developments on their own will not resolve the problems faced by users if the underlying information is not relevant, comparable and reliable.

- **Growing likelihood that Member States take national initiatives that undermine the Single Market**. Policy-makers at national level are increasingly convinced of the need to address existing problems regarding non-financial reporting. If the EU does not act, there is a high probability that individual Member States will introduce national rules or standards that undermine the right of establishment and the free movement of capital across the EU.[35]

5.2 Description of the policy options

In order to focus the impact assessment on a limited number of key variables and improve its readability, this section presents different policy options for three main variables: the standardisation of reported information, assurance requirements, and scope (i.e. which companies should report). These are the most important variables in terms of addressing the identified problems and they are also the principal determinants of costs.

Annex 16 examines policy options for a number of other variables: digitalisation, sanctioning regime and enforcement, reporting on intangibles, location of reported information, clarification of materiality concept, and clarification of exemption to subsidiaries. These are additional variables that the Commission will need to consider when formulating its proposal for this initiative, but they are less important in terms of addressing the identified problems and determining costs, and are therefore presented in an annex in order not to overburden the reader.

[35] Carrots & Sticks report provides an analysis of the latest trends in reporting provisions, and shows an increasing number of reporting provisions in recent years.

Table 1. Overview of which principal variables for policy options address which specific objectives

		Policy options		
		Standardisation	Assurance	Scope
Specific objectives	Companies from which users need information do report			x
	Companies report all relevant information	x	x	
	Reported information is comparable	x		
	Reported information is reliable	x	x	
	Reported information is easy to find and exploit	x		
	Companies have clarity about what to report	x		
	Companies have better info from suppliers, clients & investees	x	x	x
	Reduced burden from additional demands for information	x		x

Table 2: Overview of policy options

Standardisation	Assurance	Scope
Option 1 Mandatory EU standards **Option 2** Voluntary EU standards	**Option 1** Requirement for reasonable assurance **Option 2** Requirement for limited assurance	**Option 1** All large PIEs (remove 500 employee threshold) **Option 2**: Option 1 plus: • Large non-listed companies • Large non-EU companies listed in the EU **Option 3**: Options 1 and 2 plus • Listed SMEs **Option 4:** options 1, 2 and 3 plus • Non-listed medium sized companies

5.2.1 Standardisation options

i) Option 1. Develop EU non-financial reporting standards for mandatory use by companies under scope (and simplified SME standards for voluntary use)

According to this approach, the EU would support the development of EU non-financial reporting standards, and mandate their use by companies under the scope of the NFRD.[36]

These standards would specify all information necessary to allow companies to meet the legal requirements of the NFRD, and would provide guidance on how to present this information. This means that for all sustainability matters and areas addressed in the legal provisions of the NFRD, the standards would specify disclosures, including indicators, that cover how non-financial issues affect the company's financial performance ('outside-in' perspective), and how the company impacts society and the environment ('inside-out' perspective). For most quantitative indicators, the standards would also specify the methodology to be used.[37]

The standards would cover appropriate forward-looking information, as well as information about past performance. They would specify which information companies need to report on the supply chains, taking into account their international dimension and the specificities of different geographies where relevant. Such standards would be significantly more comprehensive and more detailed than the existing guidelines on non-financial reporting published by the Commission.

These standards would take into account the information needs of investors and specialised civil society organisations. They would also take account of the needs of other potential users, such as policy-makers and statistical agencies.

Additionally, these standards would take into account the information needs of the financial sector that result from their obligation to comply with the SFDR and the Taxonomy Regulation. The EU standards would be consistent with EU non-financial reporting laws, and would specify disclosures that allow entities subject to those laws meet their legal obligations.

[36] In June 2020 Executive Vice-President Dombrovskis issued a mandate to the European Financial Reporting Advisory Group (EFRAG) to carry out preparatory work for the possible development of European non-financial reporting standards. He also mandated the President of EFRAG to make proposals for possible changes to EFRAG's governance if it were asked to move ahead with the technical development of such standards. EFRAG published both reports in March 2021 (https://www.efrag.org/Lab2 and https://www.efrag.org/Assets/Download?assetUrl=%2fsites%2fwebpublishing%2fSiteAssets%2fJean-Paul%2520Gauz%c3%a8s%2520-%2520Ad%2520Personam%2520Mandate%2520-%2520Final%2520Report%2520-%252005-03-2021.pdf). The description of standards in this section is consistent with the recommendations from EFRAG.

[37] Most existing reporting standards include indicators. When they do, they usually also include guidance for calculating such indicators (e.g. GRI 305 emissions). EU standards could use a range of approaches for this, from simple cross-referencing to credible and well-recognised methodologies described in normative documents produced by other organisations, to developing new methodologies for certain indicators where necessary.

These EU non-financial reporting standards would build on the most widely accepted elements of the existing private standards and frameworks. It would ensure as much continuity and consistency as possible with the private standards and frameworks that some companies currently use. In addition, EU non-financial reporting standards would build on the Commission's guidelines on reporting non-financial related information as necessary.

The standards would comprise a number of different normative documents built on a modular structure. For example, different standards might address general disclosure requirements applicable to all enterprises (e.g. description of the business model, risk management system, or due diligence) and thematic disclosure requirements (e.g. on particular environmental or social matters). Other standards might cover certain economic sectors, justified by the sustainability-related impacts and dependencies specific to those sectors.

Consistent with the "think small first" approach, the standard-setter would develop a simplified standard for voluntary use by SMEs who are not under the scope of the NFRD. The simplified nature of this standard would reflect the fact that SMEs often do not have the technical expertise nor resources necessary to prepare reports in accordance with state-of-the-art, sophisticated standards.

The standards would consider the particularities of consolidated reporting; they would ensure that information about subsidiaries is appropriately included in consolidated reporting in order to meet users' needs. The standards setter would explore the best ways to disaggregate subsidiaries' information, to ensure useful, efficient reporting.

An adequate degree of political and democratic oversight of the content of the standards and a coordinated approach between the different EU bodies in charge of developing the different level 2 measures of other Sustainable Finance legislation would be ensured.

Organisations that have advanced the cause of sustainability/non-financial reporting, such as the Global Reporting Initiative (GRI), the IFRS Foundation (and/or the possible future sustainability standards board created under its auspices), the Sustainability Accounting Standards Board (SASB) and the TCFD, would be invited to work closely with the future EU standards setter. EU standards would build on the content of existing and future international standards and frameworks where appropriate. The standard-setting process would be inclusive and carried out by experts. All relevant stakeholders would be involved, including preparers (reporting companies, including SMEs) and users (the investment community, and specialists in civil society and trade unions) of non-financial information.

EU non-financial reporting standards should ensure connectivity between financial and non-financial information, as increasingly demanded by investors. Synergies between financial and non-financial reporting are essential to ensure that investors can form an integrated view of the

financial and sustainability-related risks and impacts of investee companies. The strategic importance of these synergies is growing rapidly, as the interactions between sustainability and company value become ever more evident.

Under this option, EU non-financial reporting standards could be adopted by means of delegated regulations, based on an empowerment that would be granted to the Commission in the Accounting Directive. This would permit the direct applicability of the standards, i.e. no need to wait for transposition of amendments to the Directive by Member States before adopting the delegated act, and no delay in the date of entry into application. The revision of the NFRD could specify the conditions that need to be met in order for the Commission to adopt EU non-financial reporting standards in level 2 legislation. These conditions could include the principal elements of the standards as described in this section.

ii) Option 2. Develop EU non-financial reporting standards for voluntary use

The EU would develop EU non-financial reporting standards described under option 1, but would not mandate their use.

No action will be directly required by businesses, who would be free to use this standard if they find it useful.

5.2.2 Assurance options

Most experts agree that an independent assurance services provider can only adequately check compliance of the reported information if companies report against non-financial reporting standards. The feasibility of the assurance options is therefore closely linked to the policy choice made for standardisation. 44% of respondents to the open public consultation, and 40% of preparers, believe mandatory reporting against standards is prerequisite to require assurance of non-financial information.[38]

i) Option 1: Require reasonable assurance

The auditor would be required to perform a reasonable assurance engagement on the non-financial reporting. The conclusion of reasonable assurance is usually provided in a positive form of expression and states an opinion on the measurement of the subject matter against previously defined criteria. The work effort in this type of engagement is significantly higher than in a limited assurance engagement. It entails extensive procedures including consideration of internal

[38] In an assurance engagement the practitioner aims to obtain sufficient appropriate evidence in order to explain a conclusion designed to enhance the degree of confidence to the intended users ('Buyer's guide to assurance on non-financial information', the Audit and Assurance Faculty of the Institute of Chartered Accountants in England and Wales (ICAEW) and the WBCSD). This means that the auditor would obtain sufficient evidence to reduce the risk of material misstatements to an acceptably low level in the given circumstances.

controls of the reporting company and substantive testing. EU law imposes a reasonable assurance requirement for the audit of financial statements.

ii) Option 2: Require limited assurance

The auditor would be required to perform a limited assurance engagement on the non-financial reporting. The work in providing limited assurance engagements is less than for reasonable assurance (see option 1). The auditor performs fewer tests, providing a lower level of assurance. The conclusion of limited assurance 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.

5.3.3 Scope options

The scope options are presented cumulatively, so each option builds on the previous one.[39] The order in which the options are presented follows a logical progression, starting with companies that users are most in favour of including under scope (mainly larger companies) and gradually expanding the scope towards smaller companies. This approach allows us to analyse clearly the impacts of adding different categories of company to the scope, while keeping the presentation as clear and as simple as possible.

i) Option 1: Broaden scope to all other large public interest entities (PIEs) i.e. removal of 500 employee threshold

The personal scope would be broadened to all other large PIEs, i.e. deleting the 500 employee size threshold of the current legal provisions. This means that the size threshold delimiting the personal scope of this obligation would correspond to the definition of 'large undertaking' of the Accounting Directive.[40] In other words, all large PIEs as defined in the Accounting Directive would be required to comply with the requirements.[41]

ii) Option 2: Further broaden scope to all other large limited liability companies

In addition to the changes in scope indicated under Option 1, the current non-financial disclosure requirements would be extended to large companies that are not PIEs: non-listed EU companies

[39] In analysing the policy options with regard to scope it is assumed that every time that we refer to scope extensions to companies of a certain size, the same extension applies to parent companies of groups of the corresponding size, who are required to report at group level.

[40] Large undertakings are those that meet two out of three 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.

[41] Financial institutions play a key role in the transition towards a fully sustainable and inclusive economic and financial system as they can have significant positive and negative impacts via their lending, investment and underwriting activities. All scope options include banks and insurance companies beyond those with limited liability, such as cooperatives or mutual undertakings, provided they meet the relevant size criteria.

(including large EU companies with securities only listed outside EU regulated markets) and non-EU companies with securities listed in the EU regulated markets.

iii) Option 3: Further broaden scope to SMEs with listed securities

In addition to the changes in scope indicated under Option 1 and 2, the current non-financial disclosure requirements would be extended to (1) EU SMEs with securities listed in EU regulated markets and (2) non-EU SMEs with securities listed in EU regulated markets, excluding micro-undertakings as defined in the Accounting Directive.[42]

iv) Option 4: Further broaden scope to non-listed medium sized companies

In addition to the changes in scope indicated under Options 1, 2 and 3, the current non-financial disclosure requirements would be extended to non-listed EU medium-sized companies as defined in the Accounting Directive.

5.3 Options discarded at an early stage

The following options have been considered but discarded at an early stage: (1) European Transparency Benchmark; (2) Additional non-binding guidelines issued by the Commission; (3) Endorsement of an international standard; and (4) Expanding the scope to include all SMEs. Annex 18 describes each of these options and the reasons for discarding them at an early stage.

6. WHAT ARE THE IMPACTS OF THE POLICY OPTIONS?

We have adopted a two-step approach to assessing the impacts of the policy options. In the first step, we individually analyse the impacts of the policy options for standardisation (section 6.1) and assurance (6.2), and identify a preferred option for each of these two variables. In the second step we analyse the impacts of the policy options for scope (section 6.3), assuming the preferred policy options for standardisation and assurance. Each scope option is therefore a package that includes the preferred options on standardisation and assurance.

We have adopted this methodology because it is not possible to analyse the impacts of expanding the scope without knowing the main features of the reporting requirements that companies under scope would have to meet. This is especially the case for estimating the costs for reporting companies, since assurance and reporting standards are the two principal determinants of costs.

[42] Small undertakings are those that do not exceed two out of three criteria: (a) balance sheet total: EUR 4 000 000; (b) net turnover: EUR 8 000 000; (c) average number of employees during the financial year: 50. Medium-sized undertakings are those that are not micro-undertakings or small undertakings and that do not exceed two out of three 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.

The policy options regarding other variables are individually analysed in annex 16, as they individually would not significantly influence the outcome of the preferred policy package. The preferred policy option for each of those variables is included in Section 7 (Preferred option).

The analysis of impacts of each option is structured as follows:

- Firstly, we analyse the effectiveness of meeting the specific objectives identified in section 4.2 regarding the provision of adequate non-financial information for users.
- Secondly, we analyse the costs of the option for different stakeholders, in particular preparers. Since the specific objectives regarding preparers are to reduce unnecessary costs, this analysis also covers the effectiveness of meeting the specific objectives from a preparer perspective. A detailed analysis of the costs and their calculations for each option can be found in annex 17.
- Thirdly, we analyse other potential significant impacts that do not directly correspond to the specific objectives identified in section 4.2.

We address the coherence with other EU policies throughout the whole analysis as appropriate.

6.1 Impacts of standardisation options

6.1.1 Analysis of impacts of Option 1: Develop EU non-financial reporting standards for mandatory use by companies under scope (and simplified SME standards for voluntary use)

Effectiveness in meeting specific objectives

Mandatory requirements on all companies under scope to use common EU reporting standards would contribute to meeting the specific objectives in the following ways:

- Relevance: All companies under scope would report the information that users find relevant, as defined in the common standards through a consensual approach involving representatives of all relevant stakeholder groups. In particular, this option can significantly enhance the coherence of EU sustainability reporting requirements: the common standards would ensure that all companies under the scope of the NFRD report information that financial market participants and other entities need to meet the reporting requirements established in the SFDR and the Taxonomy Regulation. 79% of financial sector respondents to the public consultation said that there was a need to better streamline the different reporting requirements.
- Comparability: Reported information would be comparable between all companies under scope of NFRD. Respondents to the public consultation highlighted comparability as being particularly important: 84% of users agreed that the limited comparability of information is a problem.

- Reliability: The use of standards would indirectly improve the reliability of information since it is easier to give effective assurance if information is reported against a standard.[43] In addition, mandatory standards would ensure the transparency and robustness of methodologies behind the disclosed information, enabling greater control and scrutiny by users themselves.
- Usability: Common standards should contribute to a more standardised presentation of information, which should mean that users experience fewer difficulties in finding the information they are looking for. Standards are pre-requisite for the digital tagging of information, so this option would also facilitate the digitalisation of reported information.[44]

Overall, a requirement on companies to use mandatory EU standards would make a major contribution to the achievement of the specific objectives. It would represent a significant step in terms of making the status of non-financial information more comparable to the status that the EU framework currently gives to financial information.

There is a strong consensus amongst users and other stakeholder groups, such as policy-makers and supervisors, that the mandatory use of common standards is necessary to address the identified problems. 82% of respondents to the public consultation (including 80% of preparers) believed that requiring companies to use common standards would help to address the problems of relevance, comparability and reliability to a reasonable or to a very great extent. The percentage of social and environmental organisations believing that mandatory common standards would help to address the identified problems to a reasonable or to a very great extent was especially high (89%).[45]

Some business associations and individual companies oppose this option. Firstly, they argue that a common set of standards cannot meet the needs of a variety of different users who demand different kinds of information. However, the information needs of users are converging. This is most evident in the case of information about adverse impacts of companies, where the information needs of investors, civil society, trade unions, and also policy-makers and statistical agencies, are increasingly similar. The standardisation process itself should further contribute to

[43] In response to the public consultation, 47% of users said that a requirement for assurance would be dependent on companies using standards, whereas 29% said this was not the case.

[44] In response to the public consultation, 65% of respondents to the consultation agree tagging of information would only be possible when done against reporting standards.

[45] For organisations wishing to hold companies to account for their social and environmental impacts, mandatory common standards would have a number of major benefits. For example, it would enable them to better compare companies, in the knowledge that companies would be required to disclose all relevant information in a comparable way. It may also enable them to identify companies that they believe are performing poorly with regard to the avoidance and mitigation of adverse social and environmental impacts.

such convergence. This option would in any case not prevent companies from publishing additional communication material for specific audiences if they see value in doing so.

Secondly, some business associations and individual companies argue that a mandatory reporting standard would not be sufficiently flexible to allow them to report the information that they think is relevant. However, even if one objective of requiring the use of common standards is indeed to reduce the discretion of companies in deciding what to report, common standards would be based on the principle of materiality and would guide companies on how to apply that principle. It would therefore ensure all relevant information is reported but would not require companies to report information that is not relevant to their particular circumstances.[46]

Costs analysis

Costs for preparers. The annual incremental costs of reporting against EU non-financial as a consequence of this new requirement would be approximately EUR 210 million.[47] Additionally, one-off incremental costs would amount to EUR 29 million. These costs are not very high because around 50% of companies under the NFRD are already reporting against comparable detailed standards.

On average, the estimated annual costs of reporting against EU standards for an individual company would be approximately EUR 106 000.[48] This estimation is based on the current reporting practices assessed in CEPS study (see annex 17). At the same time, reporting costs for companies are expected to decrease in the medium term due to the following three factors:

- If more adequate information was publicly available, the number of requests for additional information should decrease.[49] As a result, costs associated with meeting multiple different users' demands would be reduced in the medium term.[50] In addition, if EU standards were

[46] In this respect, mandatory common standards for non-financial information would be the same as mandatory common standards for financial information.

[47] Companies brought into the scope of the NFRD due to national transposition are included in these calculations. We assume that as a minimum, Member States would retain the current scope definitions in national law, and would require the use of standards by all companies covered.

[48] This figure amounts to EUR 63 000 for the additional companies brought under the scope of the NFRD by member states, due to their smaller size (see annex 17). The cost analysis undertaken has confirmed the wide dispersion of reporting costs: according to the survey carried out by CEPS, costs reported by companies under the scope of the NFRD who report against standards in a detailed manner ranged between ranged between 437 EUR and 800 000 EUR with a median of 61 000 EUR, and an interquartile range (difference between the first and third quartile) of 25 000 EUR and 138 000 EUR.

[49] The study carried out by SustainAbility indicates that companies who spend more time in reporting (which suggests better reporting in principle), spend less time filling in questionnaires.

[50] Cost savings could amount to EUR 24 200 - 41 700 per company per year, and around EUR 280 - 490 million per year for the current NFRD population (including national transposition), if standards were to completely eliminate the need for additional information requests to preparers. These calculations are based on the replies to the survey carried out by SustainAbility. See annex 17 for a detailed cost analysis.

applied by companies in the world's largest market (as a minimum by those subject to the NFRD), there would be less incentive or need for users to ask for additional information according to other standards or formats.[51]

- Companies would have greater clarity and certainty about what information to report, reducing any inefficient investment in time or resources in trying to understand how best to comply with EU legislation.[52]
- Companies would face reduced costs from trying to get the necessary information from suppliers and clients, to the extent that those suppliers and clients are also required to use EU standards. Likewise, companies operating across different Member States would see a reduction in the overall costs of reporting of the group, given that requirements would be aligned throughout the EU.

Costs for users. If many of the largest EU companies reported against EU standards, more relevant and comparable information would be publicly available for users. Costs associated with trying to find adequate information would be reduced. Specifically, investors would rely on rating agencies and data providers to a lesser extent, if more standardised information was publicly available, and would trust more the underlying source of the information.[53] 59% of users who replied to the open public consultation face difficulties finding the reported information.

Costs for the EU. The EU would incur certain costs for developing the EU reporting standards.[54] These costs would be limited if the work was done in partnership with organisations active in non-financial reporting. Additionally, mechanisms could be set up to draw upon private sources of finance, while ensuring proper governance structures, limiting the impact on the EU budget.[55]

As a result of these reporting requirements, ESMA's enforcement priorities would further expand towards non-financial reporting and it might dedicate additional resources to ensure supervisory convergence in the area of non-financial reporting.

Costs for national authorities. Costs of enforcement activities by national authorities could slightly increase due to the resources needed to check compliance against a more detailed set of

[51] CEPS study shows that the majority of the surveyed companies subject to the NFRD report against multiple standards and frameworks at least to a certain extent and incur higher costs the more standards and frameworks they follow (see figure 5.26 of CEPS study).

[52] CEPS study shows that companies that find it more difficult to decide which information should be included in the non-financial statement usually incur greater administrative and incremental costs.

[53] Today, investors rely on many data providers, as they want to be able to compare information obtained from different sources. Smaller investors (e.g. smaller asset managers) do not have the resources to be subscribed to third party data providers, and can only rely on data available, which is not comparable. Also, some ESG rating agencies use a significant amount of data from third parties (36% of the interviewees in SustainAbility study said that they use over 50% of the data from a third party).

[54] The annual budget of the GRI, who develops comprehensive set of non-financial reporting standards in a multi-stakeholder approach comparable to the EU standards described in section 5.2.1, is EUR 9 million.

[55] The Commission is already using this approach for the preparatory work for the possible future development of EU reporting standards mandated to the European Financial Reporting Advisory Group (EFRAG).

requirements.[56] At the same time, national authorities would gain clarity about what information companies should report according to the NFRD, which could translate into costs savings.

Other economic, environmental, social and fundamental rights impacts

- Company impacts on the environment, society and fundamental rights. Companies that are required to report against standards will have to identify and report on their most significant non-financial risks, dependencies and impacts, and explain how they manage them. This discipline will have an indirect beneficial effect on the environment, society and fundamental rights, to the extent that it affects company decisions and the way companies behave. These impacts would be biggest in the case of companies that have not previously used standards, which is approximately 50% of companies under the scope of the NFRD. There is, however, mixed evidence about the extent to which reporting requirements on their own will induce companies to mitigate and avoid their negative impacts, especially in comparison to policies and regulations that effectively price negative externalities.[57]
- Company resilience. To the extent that reporting against a standard raises company awareness of sustainability-related risks and improves the way in which risks are managed, this option should help to make companies more resilient. It would, for example, enhance company awareness of dependencies on natural capital. This impact will be biggest for companies under scope that have not previously used reporting standards or have not fully applied them.[58]
- Better policy on the environment, society and fundamental rights. Availability of better non-financial information for policy-making, can inform policy actions that lead to positive environmental, social and fundamental rights impacts (e.g. environmental agencies and national environmental accounts).
- Competitive advantage for more sustainable companies. Equal transparency requirements on companies reporting according to the NFRD would allow front runners in terms of performance regarding sustainability issues to be more easily identifiable. This could give them a competitive advantage, for example in terms of reputation, or to attract capital in the context of the Sustainable Finance agenda. This option also sets a more level playing field between companies under the scope of the NFRD, compared to the current situation in which

[56] See annex 16.2 Sanctioning regime and enforcement.

[57] CEPS study found some evidence of limited changes in company policies that could be partly attributed to the current requirements of the NFRD. Close to 45% of all surveyed companies by CEPS have implemented new due diligence processes on environmental or human rights matters (at least to some extent) as a consequence of the reporting obligations. The study also pointed out that it is very difficult to disaggregate the effect of the NFRD from other factors that may drive changes in company policies and behaviour.

[58] Two-thirds of companies surveyed by CEPS indicated that the obligation to publish a non-financial statement has contributed to changes in internal practices and procedures, including a greater integration of non-financial risks.

companies that report the best quality and most relevant information incur higher reporting costs than other companies.

- International competitiveness of EU companies. Under this option there is a risk that EU companies incur higher reporting costs than non-EU companies. However, given the increasing interest of global investors and other stakeholders in sustainability-related information, some global companies are likely to decide voluntarily to align some elements of their non-financial reporting with the mandatory EU standards, and other jurisdictions are already introducing requirements or policy initiatives in the field of sustainability-related disclosures (see annex 14).[59] Furthermore, the competitive situation of EU companies is likely to be enhanced in the longer term if EU standards shape global alignment and possible future global standards. By taking a leading role in this respect the EU and its companies could benefit from first-mover advantage.
- Risk of international fragmentation. In response to the public consultation, many respondents, including European Supervisory Authorities, the European Central Bank and some Member States stated that the ultimate goal should be global non-financial reporting standards. There could be a risk that the development of EU standards leads to global fragmentation. However, this risk can be mitigated by ensuring that EU standards incorporate and build upon existing international standards and frameworks. In addition, the EU can foster discussions on global coherence through the International Platform on Sustainable Finance. Annex 18 explains the reasons for not requiring EU companies to use an international standard.
- Knock-on effects on SMEs: Making the use of standards mandatory for companies under the scope of the NFRD would increase the number of companies that seek detailed information from their suppliers or clients, which would include SMEs. While this phenomenon is to some extent an inevitable part of the transition to a sustainable economic system, it can also create administrative burden for SMEs. On the other hand, SMEs that do not provide certain non-financial information may suffer negative consequences in terms of access to finance and to commercial opportunities. The availability of simplified standards for voluntary use by SMEs, which is an integral part of this option, would aim to provide an effective solution and facilitate SMEs' participation in the transition to a sustainable economy.[60]
- Single Market. Risks to the Single Market from Member States endorsing different non-financial reporting standards would be significantly reduced, and probably removed altogether.

[59] According to the Global Reporting Initiative, 82% of the world's largest 250 corporations, make use of the GRI's Standards to report sustainability information. Such companies are likely to take a strong interest in the content of mandatory EU reporting standards, even if they are not obliged to use them.

[60] 74% of respondents to the open public consultation indicated that simplified standards would be useful for SMEs, and that figure rises to 88% for respondents who are or who represent SMEs. The same percentage of SMEs and respondents (66%) believe that a simplified standard would limit the burden for SMEs arising from information requests.

- The quality of ESG ratings. Improving the quality and comparability of published information could improve the reliability and quality of ESG ratings. It would improve clarity about the underlying data used for different methodologies by different third parties.

6.1.2 Analysis of impacts of Option 2. Develop EU non-financial reporting standards for voluntary use

The impacts described in this section are highly dependent on the extent to which companies use the EU standards on a voluntary basis. Companies may continue to use different standards or no standard at all.

Effectiveness in meeting specific objectives

This option would address problems regarding relevance, comparability, reliability and usability amongst those companies that decide to fully apply the standards. A plausible scenario would be as follows:

- Companies under the scope of the NFRD that currently use standards (approximately 50%) would be likely to use the new EU standards. However, as is the case with current standards, only a small minority of these companies would fully apply the standards, while most would use the EU standards selectively, possibly in conjunction with other standards.
- Companies under the scope of the NFRD that do not currently use standards (50%) would be less likely to use the EU standards immediately, but a significant proportion may nevertheless begin to do so in the medium to long term, especially if pressured to do so by supervisors, investors and other stakeholders. However, most of these companies will apply the EU standards selectively, and some companies under scope will use no standards at all.

In such a scenario, this option would make a moderate contribution to achieving the specific objectives but could not ensure that any of the objectives are fully met. The principal limitations would be that a) not all companies under scope would use the standards, even if the number increases over time, and b) only a minority of companies using the standards would apply them fully, while most would use them selectively.

Costs analysis

Costs for preparers. The reporting requirements would remain the same and therefore incremental costs of reporting due to EU intervention would be zero. Reporting companies that voluntarily decide to report against EU standards might incur higher costs. Nevertheless, because of the voluntary character of the standards, companies would only use the standards if they consider the benefits of doing so are higher than the costs.

This option could result in some of the medium-term costs savings identified for option 1 (reduction in demands to companies for additional information, greater clarity about what to report, and better information from suppliers and clients). However, any such benefits are highly dependent on the degree of uptake of the voluntary standards.

On the other hand, there would be a risk that voluntary EU standards would be perceived as another standard to add to the list of voluntary (private) standards already in existence. It would therefore run a significant risk of adding to the confusion, and adding to the administrative burden and costs for companies.

Costs for users. The reduction in costs for users associated with trying to find adequate information would not be as significant as according to Option 1, as it would depend on the degree of uptake of the EU standards by reporting companies.

Costs for the EU. Costs for the EU would be the same as the ones presented under Option 1 (section 6.1.1).

Other economic, environmental, social and fundamental rights impacts

- International competitiveness of EU companies. Because the use of standards is voluntary, this option would create a low risk of competitive disadvantage for European companies compared to non-EU companies that are not subject to similar reporting requirements. European companies could take account of the reporting done by their international competitors when deciding whether and to what extent to use the EU standards. On the other hand, the EU would be in a less strong position in any global negotiations on alignment of standards, and the EU and its companies would not benefit fully from first-mover advantage.
- Risk of international fragmentation. The risk of international fragmentation exists for this option as it does for the mandatory standards option, and it can be mitigated in the same way.
- Single Market. The risks to the Single Market from Member States endorsing different non-financial reporting standards would probably be reduced, since if a Member State wanted to endorse a standard it would probably, but not inevitably, choose the new EU standards. However, this option also creates a new risk: the very existence of high quality EU standards may tempt some Member States to make the EU standards mandatory at national level, thereby introducing new barriers to the Single Market so long as other Member States do not do the same.

As for the mandatory standards option, this option could also have impacts regarding a) company resilience b) better public policy on the environment, society and fundamental rights, c) company impacts on the environment, society and fundamental rights, d) knock-on effects for SMEs, and

d) the quality and consistency of ESG ratings. However, these impacts will only materialise to the extent that companies use or fully apply the standards on a voluntary basis.

6.1.3 Comparison of standardisation options

The analysis of options is summarised in tables 3 and 4. The scores for effectiveness directly reflect the analysis carried out in previous sections 6.1.1-6.1.2, whereas efficiency considers the costs associated with each option in relation to its effectiveness and other positive impacts (benefits). Compared to the baseline scenario, Option 1 would increase the amount of comparable, reliable and relevant information available from companies, very significantly contributing to several of the objectives of this initiative (most effective). Option 2 is less effective as it cannot guarantee that companies would publish information according to standards, and therefore cannot significantly contribute to the identified objectives. Costs under Option 2, mainly costs for the EU as preparers would not be required to report against standards, would not be justifiable given the limited and uncertain effectiveness of this option. This option does not significantly reduce the risk of increasing unnecessary costs on preparers in the medium term and other negative impacts identified in the baseline scenario.

Although Option 1 presents the highest costs, it achieves the best efficiency, as it presents the greatest benefits in terms of effectiveness and other positive impacts and would reduce unnecessary costs for preparers in the medium term. Additionally, significant improvement in the usability of reported information is only granted by Option 1; only if the use of reporting standards is mandatory, the amount of information reported that users consider not to be relevant would be significantly reduced. The availability of simplified standards would help SMEs to address the increase in uncoordinated demands for information that SMEs will face as a result of general market developments and as a result of the SFDR and the Taxonomy Regulation.

With regard to coherence, although Option 2 contributes to enhance coherence with other EU policy objectives, Option 1 is the only one that guarantees this consistency.

Table 3 - Comparison of standardisation options

	Option 1 (Mandatory Standards)	**Option 2 (Voluntary Standards)**
Effectiveness	+++	+
Costs for preparers	-	0
Efficiency[61]	++	+
Other economic, environmental, social and FR impacts	++	+
Coherence	++	+

[61] Efficiency looks at the costs associated with each option in relation to its effectiveness and other positive impacts. It reflects the net effect of the positive impacts and the costs associated to the policy option. For example, positive economic impacts can contribute to a better efficiency rating of the policy option.

Table 4 - Comparison of standardisation options in terms of impacts on different stakeholders

	Option 1 (Mandatory Standards)	**Option 2 (Voluntary Standards)**
Investors	++ • improved usability of reported information (complete, relevant and comparable) •informed decision making process •costs savings from trying to find relevant information •benefit from coherence between EU sustainability reporting requirements	+
Civil society organisations	++ • enabled to hold companies accountable for their impacts • costs savings from trying to find relevant information	• impacts described for option 1, but only to the extent that companies voluntarily decide to report according to standards
EU and national authorities	+ • improvement of policy making thanks to the availability of information	
Society at large	+ • behavioural changes of reporting companies • increase of investment flows to more sustainable companies	
Reporting companies	+/- • increase of admin burden due to detailed reporting requirements • clarity about which information to disclose • reduction in number of ad hoc demands of information received • better access to information from suppliers and clients, to the extent that they are also required to use EU standards	0 • availability of a reference standard to comply with the NFRD • but possible confusion about an additional standard alongside the rest
SMEs	+/- • knock on effects from the requirement, mitigated by the availability of simplified standards for voluntary use	+ • the availability of simplified standards for voluntary use by SMEs would help them address info demands, to the extent that counterparts do not ask for different information
National supervisors	+ • supervision facilitated by a clear set of information required to be disclosed • however, enforcement priorities further geared towards non-financial reporting, might need additional resources to ensure supervisory convergence	+ • supervision facilitated by a clear set of information

6.2 Impacts of Assurance options

6.2.1 Analysis of impacts of Option 1: Require reasonable assurance

Effectiveness in meeting specific objectives

This option would very significantly contribute to achieving the specific objective regarding the reliability of reported non-financial information. It would mean that non-financial information and financial information are assured to the same level. This option can also contribute, although to a lesser extent, to the specific objectives regarding the comparability and relevance of reported information.

However, the effectiveness of this option is currently limited by certain aspects:

- Reporting practices are not yet well developed in most companies, with relatively weak internal control systems for non-financial reporting that suggest that reasonable assurance would not be immediately appropriate or possible at this stage.
- The relative immaturity of the assurance market for non-financial information, especially if compared to the assurance market for financial information. There is some doubt about the ability of the assurance market to immediately meet the demand for reasonable assurance, especially if the EU were to decide to bring a significant number of additional companies under the scope of the reporting requirements (see section 6.3).
- The absence of a commonly agreed assurance standard for the assurance of non-financial information. A majority of both users (75%) and preparers (71%) responding to the public consultation believed that such a standard would be necessary.

There is consensus amongst most respondents to the open public consultation that assurance is needed for non-financial information, with the exception of some preparers who consider that companies should be left to choose whether they will assure or not their reported information. Overall, respondents were evenly divided as to whether the EU should require limited or reasonable assurance, if it were to introduce stronger audit requirements. Although 51% of users favoured a reasonable assurance requirement (compared to 31% who preferred limited), only 35% of preparers agreed with this approach. Many respondents noted that the maturity of non-financial reporting is far from the maturity of financial reporting and that a reasonable assurance requirement would only be a valuable and reliable option over time, when reporting and assurance practices have further evolved.

Costs analysis

Costs for preparers. The estimated total annual incremental costs for companies in scope of the NFRD resulting from the requirement to perform a reasonable assurance engagement on non-financial reporting would be approximately EUR 280 million. These incremental costs do not include costs from companies already doing reasonable assurance on non-financial information, and considers a lower increase in costs for companies already doing limited assurance than for those that would be required to start from scratch. For companies in Spain, Italy and France, where assurance is mandatory, limited assurance is the common practice. This cost estimate also assumes companies currently doing limited or reasonable assurance would continue doing so.

The estimated average annual costs of performing reasonable assurance for an individual company subject to the NFRD go from EUR 96 000 for companies not reporting against detailed standards to EUR 125 000 for companies reporting against detailed standards.[62] The cost of assurance, especially reasonable assurance, was a common point raised by many categories of respondents to the public consultation, being a major concern for preparers.

Other economic, environmental, social and fundamental rights impacts

- Resilience of companies. A reasonable assurance requirement would translate into more rigorous reporting processes within the company, as auditors would help companies identify any flaws in their internal controls, methodologies for data collection and reporting or in the identification of material risks and impacts.
- Single Market. A requirement for reasonable assurance, the highest level of assurance, would avoid obstacles to the Single Market resulting from different levels of assurance requirements in different Member States.
- Connectivity and consistency between financial and sustainability information. Auditors are already required to audit financial statements, to ensure their consistency with the management report and to check compliance of the management report with applicable legal requirements. A large number of respondents to the public consultation believe that auditors are best placed to provide assurance on non-financial information, while a smaller number stated that this should not necessarily be the case. This policy option allows to ensure the connectivity and consistency between financial and sustainability reporting, as the third party that verifies sustainability information would also have an understanding of the financial performance of the company.
- Risk of concentration of the audit market. This requirement would contribute to a certain extent to maintain the current situation of concentration in the audit market.

[62] The general approach of cost estimation was to apply a stratified approach, i.e. attempting to estimate costs that reflects the size of the preparer . Accordingly, the estimated average costs of performing reasonable assurance for companies brought into the scope of the NFRD due to national transposition go from EUR 32 000 for companies not reporting against detailed standards to EUR 57 000 for companies reporting against detailed standards. See Annex 17for further details.

- Assurance of non-financial information would facilitate supervision of non-financial reporting by national competent authorities.[63]

6.2.2 Analysis of impacts of Option 2: Require limited assurance

Effectiveness in meeting specific objectives

This option would contribute to achieving the specific objective regarding the reliability of reported non-financial information. Currently, the non-financial statement is explicitly exempt from the requirement to have an auditor's opinion on the information in the management report. Therefore, making limited assurance of non-financial information mandatory would be a significant step to improve the reliability of reported information. It would also contribute, although to a lesser extent, to the specific objectives regarding the comparability and relevance of reported information. However, the effectiveness of this option in the case of all three of these specific objectives (reliability, relevance and comparability) is restricted by the nature of the assurance requirement, as limited assurance ensures the reliability of information to a lesser extent than does reasonable assurance.

52% of preparers favoured a limited assurance requirement (compared to 35% who preferred reasonable), but only 31% of users agreed with this approach.

Costs analysis

Costs for preparers. The total estimated annual incremental costs for companies in scope of the NFRD resulting from the requirement to perform a limited assurance engagement on non-financial reporting would be around EUR 80 million.[64] These incremental costs do not consider costs from companies already assuring non-financial information. This is the case for companies in Spain, Italy and France, where assurance is mandatory, and for companies that voluntarily verify non-financial reporting in other member states. This cost estimate also assumes companies currently doing limited or reasonable assurance would continue doing so.

The estimated average annual costs of performing limited assurance for an individual company subject to the NFRD go from EUR 56 000 for companies not reporting against detailed standards to EUR 75 000 for companies reporting against detailed standards.[65]

[63] See annex 16. According to the proposed policy option regarding sanctioning regime and enforcement, the role of NCA with regard to non-financial information would be clarified in law.
[64] Companies brought into the scope of the NFRD provisions due to national transposition are included in these calculations.
[65] The general approach of cost estimation was to apply a stratified approach, i.e. attempting to estimate costs that reflects the size of the preparer. The estimated average costs of performing limited assurance for companies brought into the scope of the NFRD due to national transposition go from EUR 21 000 for companies not reporting against detailed standards to EUR 37 000 for companies reporting against detailed standards. See Annex 17 for further details.

Other economic, environmental, social and fundamental rights impacts

To a lesser extent than the reasonable assurance option, this option could also have impacts regarding a) company resilience, b) reduction of risks to the Single Market, c) connectivity and consistency between financial and sustainability information, (d) risk of concentration of the audit market and e) facilitation of supervision.

6.2.3 Comparison of assurance options

The analysis of options is summarised in tables 5 and 6. The scores for effectiveness directly reflect the analysis carried out in previous sections 6.2.1-6.2.2, whereas efficiency looks at the costs associated with each option in relation to its effectiveness and other positive impacts.

In terms of effectiveness, option 1 contributes to a greater extent than option 2 to meeting the identified objectives. However, in a context where reporting practices are not very advanced and the assurance market of non-financial information is not mature enough, costs for preparers would probably outweigh the benefits of this option in the short term. Therefore, the most efficient option with regard to assurance in the short term would be option 2 (require limited assurance).

In the absence of a complete set of assurance standards, a significant number respondents to the open public consultation, both users and preparers, preferred a gradual approach starting with a requirement for limited assurance and then moving to a system with reasonable assurance in the longer term.[66] A review clause to analyse whether conditions have been met for a transition towards a requirement for reasonable assurance would accommodate these concerns while enabling the initiative to maximise its contribution to the objective of improving the availability of reliable information in the medium term. The review would need to assess conditions such as how advanced reporting and assurance practices are in the market, and, although not an absolute condition for requiring a reasonable assurance engagement, the availability or not of assurance standards in the market.

Therefore, given that option 1 would be the most coherent and efficient option in the medium term, a phase-in approach towards reasonable assurance is the preferred policy option. Requiring limited assurance and having a review clause to analyse whether conditions have been met for a transition towards a requirement for reasonable assurance allows for a phase-in approach with regard to costs for preparers, and for an assessment of the maturity of the industry in the medium term, significantly contributing to the specific objectives of the initiative.

[66] Open public consultation, written contribution from the Committee of European Auditing Oversight Bodies (CEAOB): "Reporting and assurance on non-financial information are rather new areas. As such, it would be premature to require reasonable assurance at the current stage and until a shared understanding has been developed by the various stakeholders as well as an appropriate framework".

In order to reduce the risk of concentration in the audit market, Member States could decide to allow other third party assurance services providers to provide the opinion on sustainability reporting.

Table 5 - Comparison of assurance options[67]

	Option 1 (Reasonable assurance)	**Option 2 (Limited assurance)**
Effectiveness	+++	++
Costs for preparers	--	-
Efficiency[68]	+	+
Other economic, environmental, social and FR impacts	+	+
Coherence	+	+

Table 6 - Comparison of assurance options in terms of impacts on different stakeholders

	Option 1 (Reasonable assurance)	**Option 2 (Limited assurance)**
Investors	++ • information available would be considered significantly more reliable and useful.	+ • information available would be considered more reliable and useful.
Civil society organisations	++ • information available would be considered significantly more reliable and useful.	+ • information available would be considered more reliable and useful.
EU and national authorities	++ • significant improvement of policy making thanks to the availability of reliable information	+ • improvement of policy making thanks to the availability of reliable information
Reporting companies	+/- • would incur significant additional costs • companies would significantly improve their reporting processes • reduction in number of ad hoc demands of information received	+/- • would incur additional costs • but some offsetting benefits as companies would improve their reporting processes
National supervisors	+ • additional 'line of defence' in the supervision of non-financial reporting by national authorities	+ • additional 'line of defence' in the supervision of non-financial reporting by national authorities

[67] The + and the – signs reflect positive and negative implications stemming from different factors in each case. Even if aspects of both policy options are rated with the same sign, the reasons behind the rating might be different. When comparing the policy options we explain how all the ratings interacting together contribute to the selection of the preferred option.

[68] Efficiency looks at the costs associated with each option in relation to its effectiveness and other positive impacts. It reflects the net effect of the positive impacts and the costs associated to the policy option. For example, positive economic impacts can contribute to a better efficiency rating of the policy option.

6.3 Impacts considering different scope options

In this section we analyse the impacts of the expansion of the scope of the NFRD to additional categories of company, assuming the preferred options for standardisation (mandatory use of EU standards for companies under the scope of the NFRD) and assurance (limited assurance requirement with review clause to possible reasonable assurance requirement at a later date).[69] As explained at the start of section 6, we have adopted this approach because it is not possible to analyse the impacts of expanding the scope, in particular the costs, without knowing the main features of the reporting requirements that companies would have to meet.

Each scope option analysed in this section is therefore a package that includes the preferred options on standardisation and assurance. We could theoretically have analysed other possible packages that combine different scope options with non-preferred policy options on standardisation and assurance. In particular, in an effort to balance benefits and costs, we could have analysed packages that expand the scope but do not require the use of EU standards and/or do not require any assurance. We have discarded such packages because we concluded that the identified problems can only be effectively addressed if reporting companies are required to report against standards and to seek at least a minimal level of assurance. We concluded that it would not be realistic to require more companies to report without ensuring they report comparable and reliable information, and therefore we have not analysed packages that reflect such a scenario.

For the sake of clarity and to avoid repetition, this section does not include an analysis of the effectiveness and impacts of the preferred options for standardisation and assurance. Their contribution to the objectives of this initiative, and all their impacts (positive/negative), would apply to all additional companies brought into scope, and therefore would be overall greater the more the scope is broadened. The assessment of the costs for preparers of the different scope options takes into consideration the preferred options for standardisation and assurance.

All companies under the scope of the (revised) NFRD will be required according to the Taxonomy Regulation to calculate and disclose the extent to which their activities substantially contribute to one of the EU environmental objectives as defined by the taxonomy. The Services of the European Commission are preparing a staff working document that will contain proper cost estimates of the Delegated Act that will specify this disclosure requirement in more detail (to be adopted by mid-2021). Annex 3 includes a preliminary, illustrative estimation of the magnitude of these costs for preparers.

[69] The general approach of cost estimation was to apply a stratified approach, i.e. attempting to estimate reporting and assurance costs that reflects the size of the preparer. See Annex 17 for further details.

Table 7. Overview of packages

	Standards (preferred option)	**Assurance** (preferred option)	**Scope**
Package 0	**Option 1** Mandatory EU standards	**Option 2** Requirement for limited assurance	**Baseline** No change
Package 1	**Option 1** Mandatory EU standards	**Option 2** Requirement for limited assurance	**Option 1** + Other large PIEs
Package 2	**Option 1** Mandatory EU standards	**Option 2** Requirement for limited assurance	**Option 2** + Other large PIEs + Other large categories
Package 3	**Option 1** Mandatory EU standards	**Option 2** Requirement for limited assurance	**Option 3** + Other large PIEs + Other large categories + Listed SMEs
Package 4	**Option 1** Mandatory EU standards	**Option 2** Requirement for limited assurance	**Option 4** + Other large PIEs + Other large categories + Listed SMEs + Non-listed medium sized companies

6.3.1 Analysis of impacts of Package 0

	Standards (preferred option)	**Assurance** (preferred option)	**Scope**
Package 0	**Option 1** Mandatory EU standards	**Option 1** Requirement for limited assurance	**Baseline** No change

This package would require all companies currently under the scope of the NFRD to report against EU standards and to seek limited assurance.[70] It would have a major impact on improving the relevance, comparability and reliability of reported information, consistent with the analysis in sections 6.1 and 6.2, but only for companies currently under the scope of the NFRD. It would not help to address the problem that some companies from whom users want non-financial information do not report such information.

[70] Taking into account how Member States have transposed the Directive, approximately 11 700 companies are subject to the reporting requirements of the NFRD. Not taking account of national transposition, about 2 000 companies are under scope of the NFRD.

Compared to the baseline scenario, the estimated annual incremental recurring costs of this package for companies would be approximately EUR 400 million.[71] This results from considering the annual incremental costs of reporting according to EU standards (approx. EUR 210 millions) and requiring limited assurance (approx. EUR 190 millions).[72] Additionally, companies would incur approximately EUR 30 million incremental one-off costs.

6.3.2 Analysis of impacts of Package 1

	Standards (preferred option)	**Assurance** (preferred option)	**Scope**
Package 1	**Option 1** Mandatory EU standards	**Option 2** Requirement for limited assurance	**Option 1** + Other large PIEs

Effectiveness in meeting specific objectives

This package contributes to meeting users' needs for information from all other large PIEs in addition to the ones already in scope. These additional companies are listed companies, banks and insurance companies with under 500 employees that qualify as 'large' according to the criteria of the Accounting Directive.[73]

There are 1 150 such companies, of which only about 20% currently report non-financial information on a voluntary basis.

The co-legislators decided to treat these PIEs differently from other larger PIEs when they agreed the NFRD in 2014, principally in order to mitigate the overall cost implications. However, in view of the growth of users' needs for non-financial information since 2014, the inclusion of these companies under scope would now make a significant contribution to the effectiveness of the initiative. A large majority of users responding to the public consultation (70%) were in favour of including all large PIEs under scope.

These companies are already defined in EU law as public interest entities, and there is by definition a public interest in ensuring that they disclose non-financial information. The additional listed companies that would come under scope account for 13% of all EU listed companies. This package is therefore important in terms of meeting the information needs of

[71] This figure does not include costs from reporting against standards from companies that were already doing so, nor does it include costs from performing limited assurance from companies that were already doing so.
[72] This figure is greater than the costs of limited assurance presented in section 6.2.3 (EUR 80 million) because according to this package companies would be required to report against standards and assurance costs are higher when companies report against standards.
[73] Undertakings that meet two out of three 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.

financial market participants: it enables them to better understand the risks and opportunities of potential investments, and to meet their own disclosure requirements under the SFDR.

Costs for preparers

This package would add EUR 100 million in annual incremental recurring costs compared to package 0. It would also add EUR 20 million incremental one-off costs compared to the previous package.

6.3.3 Analysis of impacts of Package 2

	Standards (preferred option)	**Assurance** (preferred option)	**Scope**
Package 2	**Option 1** Mandatory EU standards	**Option 1** Requirement for limited assurance	**Option 2** + Other large PIEs + Other large categories

Effectiveness in meeting specific objectives

This package includes a broader range of companies under the scope of the NFRD compared to the extension in scope described in package 1, and therefore contributes to meeting users' needs for information to a greater extent. Specifically, this package would add the following categories of companies:

- **Large non-listed EU companies** (including large EU companies with securities only listed outside EU regulated markets). The expansion of scope to large-non listed companies is driven mainly by concern for the impacts and accountability of such companies, including through their supply chains. Civil society organisations are strong supporters of bringing large non-listed companies under the scope of the NFRD. Whether or not a company has listed securities is not a determinant of its social and environmental impacts. All large companies should in this respect be subject the same requirements to report publicly about their impacts.

- **Large non-EU companies with securities listed in EU regulated markets**. The expansion of scope to large companies not established in the EU but listed in EU regulated markets is driven by two main concerns. Firstly, financial market participants need information from such companies to understand the risks and impacts of their investments, and to meet their own disclosure requirements under the SFDR. Secondly, it would create a more level playing field between EU and non-EU listed companies, in terms of administrative burden and accountability for social and environmental impacts.

In response to the public consultation, the overwhelming majority of users supported the expansion of scope to both these categories of company.

This package would add an additional 35 300 companies to the scope compared to the previous package.[74] Of these companies, about 24% currently report non-financial information on a voluntary basis, and only about 14% report against recognised standards.

The additional companies added under this package represent 27% of the total turnover of all EU limited liability companies. This package therefore significantly increases the proportion of private economic activity that would be subject to non-financial reporting requirements, so making a major contribution to improving the accountability of companies for their impacts.

Costs for preparers

This policy option would add EUR 2,9 billion in annual incremental costs compared to package 1. It would also add EUR 600 million incremental one-off costs compared to the previous package.

6.3.4 Analysis of impacts of Package 3

	Standards (preferred option)	**Assurance** (preferred option)	**Scope**
Package 3	**Option 1** Mandatory EU standards	**Option 1** Requirement for limited assurance	**Option 3** + Other large PIEs + Other large categories + Listed SMEs

Effectiveness in meeting specific objectives

According to this package the scope of the NFRD would be further broadened to include SMEs listed in EU regulated markets in addition to the categories of companies defined in Package 2.

Information from listed companies is especially important in terms of meeting investors' needs, especially given the new requirements on financial market participants coming from the SFDR. There is a risk that if SMEs do not report the information needed by investors subject to SF legislation, they will be excluded from investments regulated by these SF legislation. This package therefore enables SMEs participation in the transition to a sustainable economy in the context of other EU Sustainable Finance legislation (SF legislation).

[74] Close to 100 of them are large non-EU companies.

Investors in principle need equal information from all listed companies.[75] Therefore, listed SMEs would be required to report against the full set of EU standards and to perform limited assurance of their reports, ensuring consistency between financial and non-financial reporting requirements and bringing greater coherence to the corporate reporting legal framework.

Listed SMEs comprise 26% of all listed companies in the EU. Their inclusion under the scope would therefore be highly effective in terms of meeting investors' needs. This package would ensure that companies that represent almost 100% of the total EU market capitalisation, report relevant, comparable and reliable non-financial information. A significant majority of users responding to the public consultation (74%) favoured extending the scope to listed SMEs. SMEs themselves were divided as to whether they should be brought into the scope or not.

This package would add an additional 1 050 companies to the scope compared to the previous option. Of these companies, only 5% are estimated to be already reporting non-financial information.

Costs for preparers

This package would add EUR 40 million in annual incremental costs compared to package 2. It would also add EUR 10 million incremental one-off costs compared to the previous package.

There could be a risk that these costs would discourage SMEs from listing, which would be contrary to the objectives of the Capital Markets Union. However, the costs of non-financial reporting are very low compared to the overall costs of listing for SMEs. A requirement to report non-financial information is therefore not likely to make the difference between an SME deciding to list or not.[76] Additionally, issuers more concerned about costs of listing than about broadening their investor base, would remain free to choose to list on Multilateral Trading Facilities (MTFs) or SME growth markets.

Moreover, the costs for listed SMEs of not disclosing non-financial information will be high in terms of probable exclusion from investment portfolios. This is especially true once the SFDR comes into force, since financial market participants may simply chose not to invest in companies from whom they cannot easily obtain the non-financial information that they need for

[75] Financial reporting requirements are the same for all listed companies, regardless of their size, given the utmost importance of transparency in capital markets. This is the reason why the report does not consider simplified reporting requirements for listed SMEs, as it would be an inconsistent approach to EU corporate reporting requirements on listed companies.

[76] Illustratively, if we apply the costs of going and being public indicated in page 12 of The European IPO Report 2020 (6 to 10% of the amount raised from an initial offering of less than EUR 50 million) to an estimated average initial offering of SMEs of around EUR 15 million (study of the Centre for Strategy and Evaluation Services "A Public-Private Fund to Support the EU IPO Market for SMEs", 2021), the estimated costs for one SME for going and being public would be between EUR 0,9 – 1,5 million, compared to approximately EUR 50 000 one-off and recurring costs from reporting against standards and assuring the report (i.e. reporting costs only 3,3 – 5,5 % of the costs of going and being public).

their own reporting purposes. Even not considering the impacts of the SFDR, the use of non-financial information in investment decisions is becoming mainstream to an extent that companies not disclosing such information will face increasing challenges in accessing financial markets. If listed SMEs do not report similar information to other listed companies, then the benefits to them of listing will be much reduced.

Information from listed companies is especially important in terms of meeting investors' needs, especially given the new requirements on financial market participants coming from the SFDR.

Positive impacts such as SME participation in the transition to a sustainable economy in the context of other EU Sustainable Finance legislation (SF legislation) feature as well in the assessment of the effectiveness of the options. There is a risk that if SMEs do not report the information needed by investors subject to SF legislation, they will be excluded from investments regulated by these SF legislation. There is therefore a strong link between the inclusion of listed SMEs under the scope of the NFRD and the first question on coherence

6.3.5 Analysis of impacts of Package 4

	Standards (preferred option)	**Assurance** (preferred option)	**Scope**
Package 4	**Option 1** Mandatory EU standards	**Option 1** Requirement for limited assurance	**Option 4** + Other large PIEs + Other large categories + Listed SMEs + Non-listed medium sized companies

Effectiveness in meeting specific objectives

Under this package the non-financial disclosure requirements would be further extended to non-listed EU medium-sized companies. A majority of users who replied to the open public consultation supported the mandatory use of simplified standards by SMEs. Given the challenges that medium sized enterprises would face to report against a complete set of standards, this option would require reporting against the simplified SME standards described in section 6.1.1. A minority of the SMEs that replied to the open public consultation and the SME Panel survey, favoured a requirement on SMEs to report against simplified standards.

This package would add an additional 160 200 companies to the scope compared to the previous option. These additional companies represent 9% of the total turnover of all limited liability companies. This package would therefore represent a further significant increase in the proportion of private economic activity that would be subject to non-financial reporting requirements, contributing to improving the accountability of companies for their impacts.

User demand for non-financial information is currently lower for non-listed medium-sized companies than it is for listed companies and for large companies. Individually, medium-sized enterprises tend to have less significant impacts on society and the environment than larger companies.

Costs for preparers

This policy option would add EUR 3,6 billion in annual incremental costs compared to the previous option. It would also add EUR 830 million incremental one-off costs compared to the previous package.

Table 8 - Overview table of companies covered in different packages

Coverage of options					
	Baseline	**Option 1**	**Option 2**	**Option 3**	**Option 4**
Total number of companies	11.653	12.810	48.080	49.139	209.344
% of total turnover of all EU limited liability companies	47%	48%	75%	75%	84%
% of all market cap	88%	90%	99%	100%	100%
% of all listed companies (equity/bonds)	41%	53%	55%	81%	81%
Compared to baseline					
Additional number of companies compared to baseline		1.157	36.427	37.486	197.691
Increase in % of total turnover of all LLC compared to baseline		1%	28%	28%	37%
Increase % of total market cap compared to baseline		2%	11%	12%	12%
Increase in % of all listed companies (equity/bonds)		13%	14%	40%	40%
Compared to previous package					
Additional number of companies compared to previous package		1.157	35.270	1.059	160.205
Increase in % of total turnover of all LLC compared to previous package		1%	27%	0%	9%
Increase % of total market cap compared to previous package		2%	9%	1%	0%
Increase in % of all listed companies (equity/bonds)		13%	2%	26%	0%

6.3.6 Comparison of Packages

Each package contributes to a greater extent than the previous one to meeting the initiative's objectives: the more companies that are included under the scope of the NFRD, the greater the number of companies that are guaranteed to report relevant, comparable and reliable information. Therefore, package 4 is the most effective of the policy options.

The overall costs incurred by preparers also increase the more the scope is broadened. Package 0 presents the lowest costs for preparers, and package 4 the highest costs. Conversely, the costs for users in terms of accessing the information that they need are highest in package 0 and lowest in package 4.

To find an appropriate trade-off between effectiveness and costs (i.e. to find the most efficient package) it is necessary to consider from which categories of company users are most in need of relevant, comparable and reliable information. The results of the public consultation and the SME panel clearly show that the priority for users is to receive information from large companies and from listed companies, and that user demand for information reduces with the size of the company.

Packages 0, 1 and 2 do not expand the scope to all large and listed companies, which significantly reduces their effectiveness in addressing the identified problems. In terms of the number and importance of companies brought under scope, the additional effectiveness of package 1 is only marginal compared to package 0. Package 2 is significantly more effective because it ensures that all large companies are under scope, but it does not include all listed companies. Package 3 expands the scope to all large and all listed companies, thereby ensuring that the most important categories of company from a user perspective report relevant, reliable and comparable information. In particular, information from listed companies is especially important in terms of meeting investors' needs, especially given the new requirements on financial market participants coming from the SFDR. Package 4 is more effective still, although user demand from non-listed medium-sized companies is lower than it is for large and listed companies.

This analysis suggests that the principal choice from the point of view of efficiency is between package 3 and package 4. The total costs for preparers of package 4 are more than two times higher than for package 3. Although package 4 is more effective than package 3 in meeting users' needs, the increase is effectiveness is not proportionate to the increase in costs, mainly because users do not prioritise information from non-listed medium sized companies. We therefore conclude that package 3 represents the best trade-off between effectiveness and costs, and is the most efficient package.

All packages are coherent with different EU initiatives. The availability of a voluntary simplified standard for SMEs out of the scope of the NFRD is a proportionate measure coherent with the SME Strategy that would give SMEs the opportunity to report in a standardised manner, mitigating any knock on effects as a result of this invite, and to participate in the transition to a sustainable economy. The different packages contribute also to ensuring consistency of the overall assurance framework of annual corporate reporting and to ensuring consistency with other sustainable finance legislation by considering the disclosure requirements of these laws in the standards setting process. However, package 3 stands out as being the most coherent, as it does not impose disproportionate burden on SMEs, coherent with the SME Strategy,[77] while still

[77] Issuers which choose to list on Multilateral Trading Facilities (MTFs) or SME growth markets would not be subject to the NFRD requirements.

ensuring that information from a great number of investee companies is available for investors subject to other SF legislation. It enables the participation of SMEs in in the transition to a sustainable economy in the context of other EU Sustainable Finance legislation and it ensures consistency between financial and non-financial reporting requirements, translating into greater coherence of the corporate reporting legal framework.[78]The analysis of all packages is summarised in tables 9 and 10.

Table 9 - Comparison of packages[79]

	Package 0	**Package 1**	**Package 2**	**Package 3**	**Package 4**
Effectiveness	+	+	++	++	+++
Costs for preparers	-	-	--	--	---
Efficiency[80]	+	+	++	+++	-
Other economic, environmental, social and FR impacts	+	+	++	+++	++
Coherence	-	+	++	+++	++

Table 10 - Comparison of packages in terms of impacts on different stakeholders

	Package 0	**Package 1**	**Package 2**	**Package 3**	**Package 4**
Investors	Impacts presented for preferred options for standardisation (section 6.1.1) and assurance (6.2.3)	+	++	+++	++++
Civil society organisations		+	++	+++	++++
EU and national authorities		+	++	+++	++++
Reporting companies[81]		+/-	+/-	+/-	+/-
SMEs[82]		+/-	+/-	+/-	+/-
National supervisors		+/-	+/-	+/-	+/-

[78] Financial reporting requirements are the same for all listed companies, regardless of their size, given the utmost importance of transparency in capital markets. This is the reason why the report does not consider simplified reporting requirements for listed SMEs, as it would be an inconsistent approach to EU corporate reporting requirements on listed companies.

[79] The + and the – signs reflect positive and negative implications stemming from different factors in each case. Even if aspects of different policy options are rated with the same sign, the reasons behind the rating might be different. When comparing the policy options we explain how all the ratings interacting together contribute to the selection of the preferred option.

[80] Efficiency looks at the costs associated with each option in relation to its effectiveness and other positive impacts. It reflects the net effect of the positive impacts and the costs associated to the policy option. For example, positive economic impacts can contribute to a better efficiency rating of the policy option.

[81] Costs would be in all cases partly offset by other factors presented for preferred options for standardisation (section 6.1.1) and assurance (6.2.3)

[82] Knock on effects on SMEs will be mitigated by the availability of simplified standards for voluntary use.

7. PREFERRED OPTION

The preceding section (section 6.3.6) compares the five packages considered in this impact assessment. It explains why package 3 represents the best overall trade-off between effectiveness and costs, and is the most efficient package in the medium term. Package 3 is therefore the preferred policy option regarding the three principal variables and it comprises the following options:

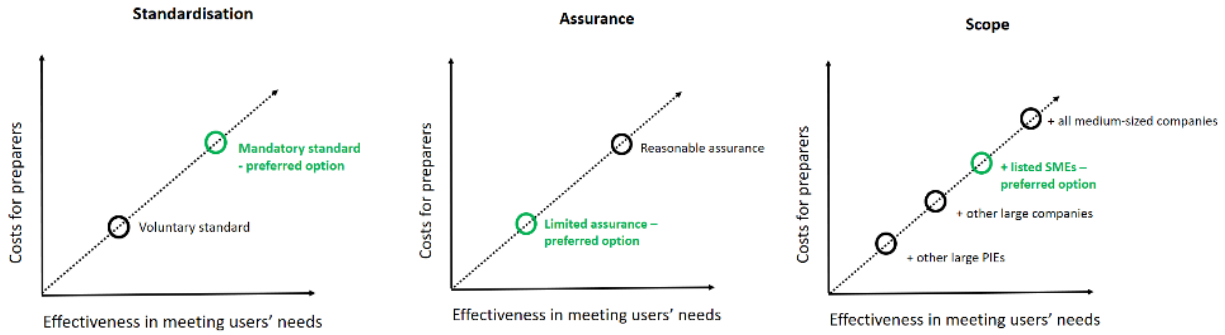
- *Standardisation*: all companies under the scope of the NFRD would be required to report against EU standards. For the standardisation variable the principal trade-off is between the high effectiveness and the high costs for preparers under the mandatory standards option, and the low effectiveness and low initial costs for preparers under the voluntary standards option. The mandatory standards option is the most efficient option because it is the only option that would adequately contribute to the objectives of the initiative (effectiveness) and because the dynamic baseline suggests that preparers would face significant costs increases even under the voluntary standards option.

- *Assurance*: all companies under scope of the NFRD would be obliged to seek limited assurance for reported non-financial information, while the NFRD would include a review clause to explore the need to move to reasonable assurance in the medium term. For the assurance variable the principal trade-off is between higher effectiveness and higher costs for preparers under the reasonable assurance option, and lower effectiveness and lower costs under the limited assurance option. The limited assurance option, with a review clause for a possible move to reasonable assurance in the future, is the most efficient option because it is nevertheless significantly more effective than the baseline in terms of ensuring that reported information is reliable, and because it avoids for the time being the higher costs for preparers of reasonable assurance. This is especially important in the context of the economic crisis created by the Covid-19 pandemic. In addition, there are concerns about whether reporting and assurance practices would be sufficiently mature to meet the demand for reasonable assurance in the short term.

- *Scope*: all large EU limited liability companies, and all companies with securities listed on EU regulated markets, would be brought under the scope of the NFRD (approximately additional 37 500 companies). For the scope variable, the principal trade-off is between a wide scope that brings higher effectiveness but also higher costs for companies, and a narrower scope that is less effective but also brings lower costs. As described in section 6.3.6

the most efficient option is the extension of the scope to all large companies and to SMEs listed on EU regulated markets, but not to all medium-sized companies.[83]

Trade-offs and preferred options for the three main variables



The preferred option is proportionate and does not go beyond what is necessary to achieve the objectives. In particular, it would only impose new reporting obligations on the companies from whom users most need information, and imposes no new obligations on the great majority of SMEs. At the same time, a simplified voluntary reporting standard for SMEs will better enable SMEs to participate in and contribute to the transition to a sustainable economy. In addition, there is a gradual approach to the introduction of assurance requirements, beginning with a limited assurance requirement and a provision for moving to reasonable assurance at a later date.

The preferred option is adapted to the new circumstances created by the Covid-19 pandemic. It meets the information needs of users, which are expected to intensify further as a result of the pandemic, while also paying very close attention to costs for preparers in the context of the current economic crisis. Companies subject to any new reporting requirements under the revised NFRD would not have to dedicate resources to meeting those requirements until 2022 at the earliest.

With the regard to the other variables, presented and analysed in annex 16, the preferred option would also include:

- Digitalisation: companies in scope of the NFRD would be required to tag their reports to allow for machine readability of non-financial information.
- Sanctioning regime and enforcement: for listed companies, the remit of the powers of supervisory authorities with regard to non-financial reporting would be clarified in law. Equivalent sanctions between listed and non-listed companies would also be specified.

[83] The application of the new requirements to SMEs listed on EU regulated markets could potentially be phased in. Issuers which choose to list on Multilateral Trading Facilities (MTFs) or SME growth markets would not be subject to the NFRD requirements.

- Intangibles: in addition to the non-financial matters identified in the NFRD, reporting on intangibles would be required.
- Where to report: all required non-financial information should be disclosed in the company's management report.
- Materiality: the legal requirements would specify in more detail when companies should consider non-financial information material (double materiality).
- Exemption for certain subsidiary companies: Subsidiaries exempted from the reporting obligations according to the NFRD would be required to publish the consolidated management report of their parent company containing sustainability information, and to refer to it in their individual management report. EU standards would ensure that information about subsidiaries is included in consolidated reporting appropriately to meet users' needs.

The preferred option adequately meets the objectives identified in section 4.2, both for users and for preparers of non-financial information. It will improve EU non-financial reporting at the least possible cost and meet the general objective of better exploiting the potential of the European Single Market to contribute to the transition towards a fully sustainable and inclusive economic and financial system in accordance with the European Green Deal and UN Sustainable Development Goals. The preferred option will: reduce systemic risks to the economy created by investments that take insufficient account of non-financial risks; enable higher financial flows to companies and economic activities that address and do not exacerbate social and environmental challenges; and strengthen the social contract between companies and citizens by making companies more accountable for their impacts on society and the environment. For preparers, it will minimise unnecessary costs associated with non-financial reporting. It will ensure a high degree of coherence between sustainable finance reporting requirements by aligning the requirements of the NFRD with those of the SFDR and the Taxonomy Regulation.

These preferred changes would require the proposal of a Directive amending the Accounting Directive (as amended by the NFRD), the Transparency Directive,[84] and the Audit Directive to address the specific changes proposed for the variables of standardisation, assurance and scope. Specifically, greater coherence between all reporting requirements in the Accounting Directive would be ensured. Additionally, based on an empowerment granted to the Commission in the Accounting Directive, the Commission would adopt EU non-financial reporting standards by means of delegated regulations. This would permit the direct applicability of the standards, i.e. no need to wait for transposition of the level 1 by Member States in order to adopt the delegated act, and no delay of the date of entry into application. Possibly, this policy option would also require amendments to the Delegated Regulation 2019/815 supplementing the Transparency

[84] The Transparency Directive is based in Articles 50 and 114 TFEU, and therefore the amending directive would be based in Articles 50 and 114 TFEU.

Directive with regard to regulatory technical standards on the specification of a single electronic format (ESEF Regulation) for the adoption of the accompanying IT taxonomy that would allow the digital tagging of reports.

7.1 REFIT (simplification and improved efficiency)

Simplification to the existing legislation will be achieved in the sense that EU law will impose clearer reporting requirements, according to the preferred policy option. This will allow for better and more efficient reporting by companies, ensuring that the objective of the law of making adequate information publicly available for users is met. Although costs for reporting companies will increase as a consequence of the detailed requirements, it is important to emphasise that these costs will increase very substantially even if the EU takes no action. Most companies can expect to receive a significant increase in demands for non-financial information in the coming years. The preferred policy option should provide an orderly and efficient solution, based on building consensus around the essential information that companies should disclose, as opposed to an uncoordinated and costly increase in demand for non-financial information, with investors and other stakeholders asking for different information in different formats across different Member States.

In addition, the proposed revision of the NFRD would reduce costs for users of non-financial information. Improvements in the relevance, comparability, reliability and accessibility of the reported information should enable users to exploit non-financial information more efficiently and in more powerful ways. The proposed revision of the NFRD will also lower compliance costs for entities subject to the reporting requirements of the SFDR and the Taxonomy Regulation as well as future Ecolabel for financial products. Without improvements in reporting from investee companies, client companies and supplier companies, entities subject to the SFDR and the Taxonomy Regulation will incur significantly higher costs to find and aggregate the information they need to meet their own legal requirements.

Although costs will overall increase as a result of this initiative, the following table highlights elements of the preferred package which improve its efficiency and/or reduce associated costs.

REFIT Cost Savings – Preferred Option		
Description	***Amount***	***Comments***
Developing and requiring use of EU reporting standards	• administrative costs savings for preparers due to clarity about what information is required to be reported;[85] • reduction of costs for preparers from addressing investors ad hoc requests for information;[86] • costs savings for users from trying to find adequate non-financial information;[87]	Stakeholders who save costs: • investors • civil society organisations and trade unions • reporting companies
Requiring limited assurance on reported information	• clarity about what is the minimum work that the third party assurance services provider has in fact undertaken avoids further costs for users of checking the reported information	Stakeholders who save costs: • investors • civil society organisations and trade unions
Requiring tagging of reports according to IT taxonomy	• costs savings for users from trying to find adequate non-financial information;[88]	Stakeholders who save costs: • investors • civil society organisations and trade unions

8. HOW WILL ACTUAL IMPACTS BE MONITORED AND EVALUATED?

To monitor progress towards meeting the *specific objectives*, the Commission services will explore the possibility of organising periodic surveys of users and preparers. The surveys would gather data on (1) users' perceptions of the evolution of non-financial reporting, in particular with respect to the specific objectives identified in section 4 and whether those objectives are being met, and (2) the costs and benefits of non-financial reporting from a preparer perspective. Such surveys will be dependent on the availability of financial resources.

Progress towards meeting the specific objectives can also be monitored through analyses of:

[85] CEPS study shows that companies that find it more difficult to decide which information should be included in the non-financial statement usually incur greater administrative and incremental costs. It also shows that the majority of the surveyed companies subject to the NFRD, report against multiple standards and frameworks at least to a certain extent and incur higher costs the more standards and frameworks they follow (see figure 5.26 of CEPS study).

[86] Cost savings could amount to EUR 24 200 - 41 700 per company per year, and around EUR 1 200 – 2 000 million per year for the preferred option, if standards were to completely eliminate the need for additional information requests to preparers. These calculations are based on the replies to the survey carried out by SustainAbility. See annex 17 for a detailed cost analysis.

[87] 59% of users who replied to the open public consultation face difficulties finding this information, which could translate into costs.

[88] 62% of users who replied to the open public consultation believe that costs of tagging reports would pay off.

- the ratings of company transparency on non-financial issues carried out by certain rating agencies and data providers, in particular whether such ratings show a positive trend over time;
- the extent to which ESG scores that in principle measure the same things vary between different rating agencies and data providers, and in particular whether they start diverging less. Lower levels of divergence might be indicative of more comparable underlying data being reported by companies.[89]

Monitoring progress towards meeting the *general objectives* is by definition considerably more complex, since it is methodologically difficult to distinguish the impacts of the proposed revision of the NFRD from other possible causes. Nevertheless, the Commission services propose to monitor progress regarding the general objectives by:

- Monitoring trends in investments in companies that carry out sustainable economic activities;[90]
- Engaging with banking supervisors and other relevant stakeholders to assess whether systemic risks to the financial system are being reduced as a result of investors taking better account of sustainability risks.

It may also be possible to use the proposed surveys of users and preparers to gather evidence about whether stakeholders perceive that companies are more accountable for their social and environmental impacts.

In addition, different stakeholders, including civil society organisations, rating agencies, business organisations and public authorities are likely to publish reports that monitor developments in corporate non-financial reporting and that will be a useful complement to monitoring carried out by the Commission services.

[89] At the same time, divergence may also be explained by difference in methodologies used by rating agencies and data providers, and is to some extent welcomed by investors interested in different assessments and views (SustainAbility study). These methodological issues should be resolved before applying this method to monitor the success of the initiative.

[90] This will be done in close cooperation with the Platform on Sustainable Finance, which will monitor trends regarding capital flows towards sustainable investments as set out in Article 20 of the Taxonomy Regulation.

ANNEX 1: PROCEDURAL INFORMATION

1. Lead DG, Decide Planning/CWP references

This Impact Assessment Report was prepared by Directorate C " Financial Markets " of the Directorate General "Directorate-General for Financial Stability, Financial Services and Capital Markets Union" (DG FISMA).

The Decide Planning reference of the "Initiative on the review of the Non-Financial Reporting Directive" is PLAN/2019/6123.

This initiative is part of the Commission's 2020 Work Programme[91] and is one of the actions proposed by the European Commission to implement the European Green Deal.[92]

2. Organisation and timing

Several services of the Commission with an interest in the initiative have been involved in the development of this analysis.

Three Inter-Service Steering Group (ISSG) meetings, consisting of representatives from various Directorates-General of the Commission, were held in 2020.

The first meeting took place on 21 January 2020, attended by DG ENV, CLIMA, JUST, GROW, ECFIN, EMPL, TRADE, ENER, SJ and the Secretariat General (SG).

The second meeting was held on 23 April 2020. Representatives from DG ENV, CLIMA, JUST, GROW, ECFIN, EMPL, DEVCO, TRADE, ENER, AGRI, SJ, JRC and the Secretariat General (SG) were present.

The third meeting was held on 23 July 2020 and was attended by DG ENV, CLIMA, JUST, GROW, ECFIN, EMPL, DEVCO, TRADE, ENER, AGRI, SJ, JRC, EEAS and the Secretariat General (SG). This was the last meeting of the ISSG before the submission to the Regulatory Scrutiny Board on 9 September 2020.

The meetings were chaired by SG.

DG FISMA has considered the comments made by DGs in the final version of the IA. In particular, it has simplified the structure of the policy options, reduced the length of the report and clarified the links with other EU legislation and initiatives. The analysis of impacts and the preferred option takes account of the views and input of different DGs.

[91] Commission Work Programme 2020: A Union that Strives for More, COM(2020)37 final, 29 January 2020. Adjusted Commission Work Programme 2020.
[92] Communication from the Commission on the European Green Deal, COM(2019)640 final, 11 December 2019.

3. Consultation of the RSB

The Impact Assessment report was examined by the Regulatory Scrutiny Board on 7 October, 2020. The Board gave a positive opinion with reservations, following which the Commission addressed the Board's comments in the final version of the Impact Assessment.

4. Evidence, sources and quality

The impact assessment draws on an extensive amount of desk research, external studies, studies carried out on behalf of the Commission, interviews, experts' workshops, meetings with stakeholders, open public consultations, staff working documents, opinions and advice by the supervising authorities, academic research papers and other. The material used has been gathered since the Commission Services started monitoring the implementation of the NFRD in 2018. This material includes but is not limited to the following:

- External studies or reports: "Undue short-term pressure on corporations", European Securities and Markets Authority (ESMA), December 2019; "2019 Research Report: An analysis of the sustainability reports of 1000 companies pursuant to the EU Non-Financial Reporting Directive", Alliance for Corporate Transparency, 2020; "In Balance 2019 - Survey of value creation and follow-up to the Non-Financial Information (Disclosure) Decree", Dutch Authority for the Financial Markets (AFM), December 2019; "Compliance by Belgian listed companies with the requirement to publish a non-financial statement", Belgian Financial Services and Markets Authority, March 2019; "Integration of Sustainability into Corporate Governance: A survey of financial firms' public sustainability information", Finansinspektionen (Swedish Financial Supervisor), November 2018; Ensuring the relevance and reliability of non-financial corporate information: an ambition and a competitive advantage for a sustainable Europe, Patrick de Cambourg, May 2019.

- A workshop on the application of the materiality principle under the Non-Financial Reporting Directive was held on 11 November 2019 with the participation of 13 representatives of preparers, investor, auditors, supervisor and academics.

- A workshop on assurance of sustainability information was held on December 2019 with the participation of 15 representatives of preparers, auditors and accountants, national governments and policy makers, assurance standard setters and oversight bodies.

- A virtual exchange with preparers of non-financial information (companies and business organisations from different sectors) to discuss the issues of costs of non-financial reporting for preparers. The meeting was held on11 May 2020.

- A virtual meeting to discuss the revision of the Non-Financial Reporting Directive with civil society organisations took place on 12 May 2020. More than 20 organisations including standard-setters, human rights and justice, disability people, environment and corporate transparency organisations have the opportunity to express their views.

- A virtual meeting with 8 representatives of trade unions to discuss the revision of the NFRD and to hear their views and concerns. The meeting was held on 15 May 2020.

- A targeted survey to SMEs, managed by the European Enterprise Network (EEN), which was open to receive responses from 3rd March 2020 through 27th May 2020. The SME Panel Consultation comprised thirteen questions that aimed to provide a good understanding of the current views and experiences of SMEs around non-financial information processes and requirements. The survey provide 348 responses of micro companies (58% of total), small companies (27%), and medium companies (15%) across the EU and the United Kingdom.

- Two (virtual) meetings with Member State representatives in the Accounting Regulatory Committee, to gather the views of regulators at national level on the revision of the NFRD.

- A meeting with SMEs representatives in the context of the COSME Programme.

- An Open online public consultation. The consultation document was published on 20 February 2020; due to the corona virus pandemic, the deadline for responses was extended by one month, to 11 June 2020. A total 588 organisations and persons responded to the consultation. Individual companies were the biggest single group of respondents (32%), followed by business associations (20%) and non-governmental organisations (14%). The remainder represented citizens (8%), public authorities (7%), academic and research institutions (6%) and trade unions (3%). The consultation consisted of 45 questions divided into 8 thematic sections including quality and scope on non-financial information, standardisation, application of the principle of materiality, assurance, digitalisation, structure and location of non-financial information, personal scope and simplification of administrative burdens. A Feedback Statement providing an overview of the contributions to this public consultation was published on the Commission's website. We do not have identified any campaigns or similar action with major impact on statistical results on the open public consultation.

- A study commissioned by DG FISMA on the implementation of the NFRD (consortium led by Economisti Associati), presents data from companies regarding current reporting practices under the NFRD, including the costs of such reporting and associated assurance of reports, and the impacts of the new requirements on company behaviour.

- A study commissioned by DG FISMA on sustainability ratings and research (consortium led by SustainAbility Institute, ERM) provides information about the trends and business models in the market for sustainability rating agencies and data providers, including information about the extent to which public disclosures are a source of data in the market of sustainability rating agencies and data providers and about the process of compilation and assessment of non-financial information by third party data and ESG rating providers.[93]

- An open online public consultation on corporate reporting. Previous consultation activity carried out by the European Commission in 2018. DG FISMA organised an open online public consultation on corporate reporting whose results enabled the Commission to gather data and views on the problems that need to be addressed with regard to non-financial reporting.

- A targeted online consultation on climate-related reporting, organised before the issuance in June 2019 of new guidelines for companies on how to report climate-related information. The results of this survey are an important complement to the sources of information for this initiative.

- Target survey on due diligence requirements through the supply-chain organised in 2019 by consultants contracted by DG JUST.

The material used to inform this impact assessment comes from reputable and well-recognised sources that act as benchmarks and reference points for the topic. Findings were cross-checked with results in different publications in order to avoid biases caused by outliers in the data or vested interests by authors.

93 https://op.europa.eu/en/publication-detail/-/publication/d7d85036-509c-11eb-b59f-01aa75ed71a1/language-en/format-PDF/source-183474104

ANNEX 2: STAKEHOLDER CONSULTATION

I. Introduction

As highlighted in the Consultation strategy, the objective of the consultation activities is to gather data and stakeholder views for the review of the Non-Financial Reporting Directive.

Specifically, the consultation aims to:

- Firstly, gather the views of preparers, users, and other important stakeholders on different policy options, including the scope for cost reduction and simplification measures.
- Secondly, gather data that can be used to better assess the costs and benefits of different policy options.
- Thirdly, gather additional knowledge about certain specific issues, such as: the application of the materiality principle in non-financial reporting; the assurance of non-financial information; the particular situation of SMEs; and the digitalisation of non-financial information.

This consultation strategy built on previous consultation activities carried out by the European Commission. In 2018 DG FISMA organised an open online public consultation on corporate reporting whose results enabled the Commission to gather data and views on the problems that need to be addressed with regard to non-financial reporting.

Moreover, the results of two others surveys are an important complement to the current consultation strategy. On the one hand, a targeted online consultation on climate-related reporting organised before the issuance in June 2019 of new guidelines for companies on how to report climate-related information. On the other hand, a target survey on due diligence requirements through the supply-chain organised in 2019 by consultants contracted by DG JUST.

Finally, DG FISMA published an open online public consultation on a Renewed Sustainable Finance Strategy on 8 April with a deadline for stakeholder responses by 15 July. Their results are being analysed and will be also considered.

II. Stakeholder groups covered by the consultation activities

According with the consultation strategy, the primary stakeholders concerned by the Non-Financial Reporting Directive can be divided as follows:

- The preparers of non-financial information, i.e. the companies that already publish non-financial information or that may do so in the future. SMEs are also relevant stakeholders

independently of whether they are subject to non-financial disclosure requirements at EU level. This is because companies that fall under the scope of the NFRD may request additional non-financial information from their suppliers and clients, including SMEs.

- The direct users of non-financial information published by companies comprise two major groups: i) financial sector institutions and investors, who require such information to assess the related financial risks and opportunities, and ii) civil society organisations and trade unions, who require such information to monitor the social and environmental performance of companies and hold them accountable for their impacts. Few individual citizens and consumers directly consult company non-financial statements, but more use such information indirectly, for example when considering the advice or opinions of financial advisers or non-governmental organisations.

Most financial sector companies such as banks and insurance companies are likely to be both preparers and users of non-financial information.

Other important stakeholder groups concerned by the Non-Financial Reporting Directive are national regulators and supervisory authorities, assurance providers, sustainability rating agencies and research and data providers, reporting frameworks and standard-setters, academics, and researchers, and policy makers.

All relevant stakeholders, particularly key stakeholders — preparers and users of non-financial information — provided relevant input for the revision of the Directive, particularly on proposals for improving existing rules.

III. Consultation activities and other information sources

The services of the European Commission have used a wide range of methodologies to build this consultation strategy, including open public consultation, surveys, workshops, meetings and interviews. In particular, DG FISMA employed the following activities:

- The Inception Impact Assessment for the revision of the Non-Financial Reporting Directive was published on 30 January with a deadline for stakeholder comments by 27 February. The Commission received 78 responses to the inception impact assessment. The biggest number of responses came from non-financial sector companies and business associations, representing about 43% of responses. Financial sector companies and associations (including insurance) represented about 16% of responses, and non-governmental organisations and trade unions 14%.

- Open online public consultation: The consultation document was published on 20 February 2020; due to the corona virus pandemic, the deadline for responses was

extended by one month, to 11 June 2020. A total 588 organisations and persons responded to the consultation. Individual companies were the biggest single group of respondents (32%), followed by business associations (20%) and non-governmental organisations (14%). The remainder represented citizens (8%), public authorities (7%), academic and research institutions (6%) and trade unions (3%). The consultation consisted of 45 questions divided into 8 thematic sections including quality and scope on non-financial information, standardisation, application of the principle of materiality, assurance, digitalisation, structure and location of non-financial information, personal scope and simplification of administrative burdens. A Feedback Statement providing an overview of the contributions to this public consultation was published on the Commission's website. We do not have identified any campaigns or similar action with major impact on statistical results on the open public consultation.

- Consultants contracted by the Commission (CEPS) conducted a **targeted survey** addressed to all companies currently under the scope of the Non-Financial Reporting Directive. The survey collected data from companies regarding current reporting practices under the NFRD, including the costs of such reporting and associated assurance of reports, and the impacts of the new requirements on company behaviour. Follow-up interviews with different stakeholder groups were carried out to confirm the conclusions obtained.

- Consultants contracted by the Commission (consortium led by SustainAbility) conducted an online survey and interviews with the 219 respondents from 14 Member States regarding ESG ratings. The main stakeholder groups included asset managers and asset owners, benchmark administrators, ESG rating agencies and data providers and companies. Users of ESG data were asked about sources and quality of corporate non-financial information. Companies were asked about their opinions regarding the process of compilation and assessment of non-financial information by third party data and ESG rating providers.

- The European Commission deployed a **targeted survey to SMEs,** managed by the European Enterprise Network (EEN), which was open to receive responses from 3rd March 2020 through 27th May 2020. The SME Panel Consultation comprised thirteen questions that aimed to provide a good understanding of the current views and experiences of SMEs around non-financial information processes and requirements. The survey provide 348 responses of micro companies (58% of total), small companies (27%), and medium companies (15%) across the EU and the United Kingdom.

- The services of the Commission organised stakeholder workshops and meetings to gather views, knowledge and data on specific issues, and to gather the views of different stakeholder groups in more detail. These activities have provided an opportunity to go into greater depth on particular points and to exchange and compare viewpoints in a dynamic setting.

    1) A **workshop on the application of the materiality principle** under the Non-Financial Reporting Directive was held on 11 November 2019 with the participation of 13 representatives of preparers, investor, auditors, supervisor and academics.
    2) A **workshop on assurance** of sustainability information was held on December 2019 with the participation of 15 representatives of preparers, auditors and accountants, national governments and policy makers, assurance standard setters and oversight bodies.
    3) A virtual **exchange with preparers of non-financial information (**companies and business organisations from different sectors) to discuss the issues of costs of non-financial reporting for preparers. The meeting was held on 11 May 2020.
    4) A virtual **meeting to discuss the revision of the Non-Financial Reporting Directive with civil society organisations** took place on 12 May 2020. More than 20 organisations including standard-setters, human rights and justice, disability people, environment and corporate transparency organisations have the opportunity to express their views.
    5) A **virtual meeting with 8 representatives of trade unions** to discuss the revision of the NFRD and to hear their views and concerns. The meeting was held on 15 May 2020.

Two virtual meetings took place on 24 April and 23 June 2020 with Member State representatives in the Accounting Regulatory Committee and the Audit Regulatory Committee, to gather the views of regulators at national level on the revision of the NFRD.

A virtual meeting with the Member States Expert Group on Sustainable Finance was held on 13 May 2020 to gather views and concerns of their members on the revision of the NFRD.

A meeting with SMEs representatives was held in the context of the COSME Programme on 5 February 2020.

IV. Impact of the Covid-19 pandemic on stakeholder consultation

The Covid-19 pandemic probably reduced the number of stakeholders directly responding to online surveys. The number of respondents to the online public consultation (just under 600) was

somewhat lower than predicted. At the request of a number of stakeholders, the services of the Commission extended the consultation period from 3 months to 4 months, in an attempt to compensate for the effects of the pandemic.

The number of SMEs responding to the SME Panel survey (348) was significantly lower than predicted. In some Member States, the members of the European Enterprise Network decided not to promote the survey to SMEs because of the pandemic. The duration of the survey was extended by one month to enable more SMEs to respond.

Other consultations activities were not significantly impacted by the pandemic. In the case of the meetings with preparers, with civil society organisations, with trade unions and with Member States, the virtual format of the meetings may have enabled more people to participate.

V. The results of stakeholder consultations

The first section of this chapter analyses the results by stakeholder group and highlights their views on the potential changes to the NFRD, especially scope, assurance, and the obligation to use a standard. The second section is structured according to some of the key issues that emerged from the consultations.

Section 1: Analysis of results per stakeholder group

A. Preparers of non-financial information

Standards. Many preparers consider that development of common non-financial reporting standards would help them to know exactly what they should report and to better meet users' expectations, reducing any inefficient investment in time or resources in trying to understand how best to comply with the EU law.

However, some preparers consider that as companies report different information to a wide range of different stakeholders, it is unrealistic to expect that one standard can meet all stakeholder demands. Some companies and business associations have pointed out that they should have flexibility to report on the sustainability information considered material/relevant, taking into account their specificities. This is emphasised more in some Member States, such as Germany, than others.

Reporting companies also complain about the burden of having to respond to additional information requests from sustainability rating agencies and data providers, even if they publish a non-financial statement in compliance with the NFRD. In this respect, some preparers pointed out that standards would increase the information publicly available in the market and they would reduce these additional information requests.

Consultant activities such as open public consultation and CEPS study shows that the majority of reporting companies use multiple standards and frameworks at least to a certain extent incurring higher costs the more standards and frameworks they follow. Most preparers stressed that the design of any possible common European non-financial reporting standards should build on existing standards and frameworks, such as the GRI, SASB and the TCFD.

Multinational companies stated that different reporting formats, content requirements and deadlines imposed by individual Member States create an additional burden. They stressed the need to promote the establishment of international (global) non-financial disclosure standards. If this would not be possible, they think that the EU should cooperate with other major jurisdictions and non-EU investors to make sure that possible EU standards are widely recognised.

Assurance. Many preparers agreed that assurance is needed to improve the reliability of non-financial information. However, many preparers also consider that companies should be left to choose whether or not they will assure their reported non-financial information.

Most preparers raised concerns over the cost of assurance. According to them, the costs of assurance should be representative and reflect the substance of what is being assured in the reports.

On the other hand, there is currently a lack of expertise and experience in the assurance of non-financial information. Some preparers consider that the immaturity of the assurance market for non-financial information could increase their costs. For this reason, most preparers generally prefer a limited level of assurance.

Some preparers stressed the need of consistent assurance requirements for non-financial information across the Member States and across companies. This would allow a level playing field within the EU.

Scope. Many preparers raised concerns about administrative costs of reporting non-financial information. Regarding the scope of the NFRD, they consider that the guiding principle to add additional categories of company should be to focus on those companies from whom users most need non-financial information.

According to business associations and companies, the very challenging economic situation caused by the pandemic COVID-19 means it would be even more necessary to ensure the proportionality of reporting requirements and avoid excessive administrative burden, especially in the case of SMEs.

Preparers from financial sector need to have access to the data from their counterparties to manage ESG risks and to understand the impact of their lending and investment decision on ESG aspects. In this respect, they argue that SMEs should be considered in a proportionate way and

the NFRD should define clear proportionality criteria to delimit to which SMEs the reporting obligations apply.

Concerning listed SMEs, some argued that they should not be subject to the obligatory reporting at all, as it may discourage SMEs from listing and push listed ones from the regulated markets due to additional burden and costs. Others argued that all listed SMEs or at least listed SMEs from the high-risk sectors should be required to report non-financial information.

The SME panel consultation provided a good understanding of the current views and experiences of SMEs around non-financial information processes and requirements. Regarding the possible development of a non-financial reporting standard for SMEs, most SMEs or organisations that represent SMEs believe that having a simplified standard or reporting format would help, while most of them think that such standards should be voluntary.

Some preparers stressed the need to ensure sufficient time for collection and analyses of data from the supply chain companies as well as subsidiaries, and argued for a difference between the deadline for financial and non-financial reports.

B. Users of non-financial information

Standards. The majority of users believe that a common reporting standard would be useful to address the challenges regarding comparability, reliability and relevance of information.

They also stated that the revision of the NFRD must consider sector specific standards and strategic KPIs. Most users responding to the open public consultation agreed that the non-financial reporting standard should include sector-specific elements. They also proposed that companies should set targets and forward based objectives on specific strategies (e.g. EU Green Deal, Sustainable Development Goals) for users to see an evolution against such objectives and help improve the comparability process.

Some civil society representatives commented that because companies have a lot of flexibility when reporting non-financial information, the current reporting practice is to be of "picking and choosing" what to disclose. For this reason, they favour a more prescriptive standard that would help to reduce the reporting gap. They also mentioned the need for better mechanisms to ensure completeness of non-financial information.

Most users stressed that a wide range of stakeholders should be involved in the standard setting process. For example, trade unions considered that their expertise on working conditions is key for the drafting of NFI standards and they should be included in their setting process.

Assurance. According to users, both investors and civil society, assurance would increase the level of confidence of the stakeholders in the disclosures of an entity. Most users are more in

favour of reasonable assurance to allow for reliability of the reported information. However, considering the lack of maturity of the non-financial information framework some of them would support a limited assurance requirement in the short term.

Some civil society organisations pointed out that an assurance requirement would improve the resilience of companies, as auditors would help them to identify any flaws in their internal controls, methodologies for data collection and reporting or in the identification of risks.

Scope. Most users, including both investors and civil organisations, believed that the revision should broaden its scope of the NFRD to include all large companies whether listed or non-listed. According to many investors, a broad scope is important in terms of meeting the information needs of financial market participants: it enables them to better understand the risks and opportunities of potential investments, and to meet their own disclosure requirements under the SFDR. Civil society organisations are strong supporters of bringing large non-listed companies under the scope of the NFRD. They point out that whether or not a company has listed securities is not a determinant of its social and environmental impacts. All large companies should in this respect be subject the same requirements to report publicly about their impacts.

Trade union representatives shared the importance of companies disclosing information about their supply chains and subcontracting chains in Europe and beyond, whenever labour and human rights are at risk. Similarly, it is relevant for trade union and civil society representatives to have non-financial information presented on a country-by-country basis so they may assess which companies (and where) engage with sustainable practices.

A significant majority of users responding to the public consultation favoured extending also the scope to listed SMEs.

Section 2: Key issues that emerged from the consultation

Cost versus benefits, especially in light of the Covid-19 pandemic.

Many companies and business association raised concerns on the administrative costs of preparing non-financial information. Moreover, some of them stressed that companies are currently focusing their efforts on dealing with the deep crisis cause by the COVID-19. Then, any initiatives, which would disproportionally increase the administrative burdens and costs for companies, especially for SMEs, should be avoided.

Many users, both investors and civil society organisations, argue that we need to compare the costs of a revised NFRD with the future costs that companies would incur anyway if the EU does not act. They argue that theirs needs for non-financial information are likely to grow significantly in the coming years, so that companies will in any case face increasing costs for collecting and reporting this kind of information even if the EU does not revise the NFRD.

According to many stakeholders, the COVID-19 pandemic has underlined the importance of transparent reporting of the non-financial risks facing entities, including the resilience of their business models and global supply and value chains, and the interconnected role that financial and non-financial information play in achieving that goal.

Coherence of disclosure requirements. Most stakeholders, especially from the financial sector, stressed that EU legislation regarding reporting and disclosure should be coordinated, avoiding gaps and overlaps. They argued that the revised NFRD should be aligned with the Sustainable Finance Disclosure Regulation (SFDR) and the EU Taxonomy Regulation.

In this respect, some financial sector companies stressed the need to ensure that investee companies report the necessary information for financial sector companies to be able to meet their own future reporting obligations under the Sustainable Finance Disclosure Regulation (SFDR) and the Taxonomy regulation.

According to some financial sector representatives, there is a timing mismatch between the application deadlines for the legislative measures, such as the SFDR and the Taxonomy Regulations and the foreseeable timing of the first non-financial reporting cycle under the revised NFRD.

Many stakeholders such as academics, credit rating agencies and business associations consider that common definitions of the environmental matters based on the six objectives set out in the Taxonomy Regulation would be helpful to streamline definitions and ensure, at least regarding these matters, the coherence between the NFRD and the SFDR.

Digitalization. Many stakeholders believe that developing non-financial information standards and making non-financial information machine-readable and easily accessible via an EU central access point would enhance its searchability, readability and comparability. They underline in any case the difficulty of enabling the machine-readability of information when it is of qualitative or narrative nature. They believe that, to be fully usable, machine-readable non-financial information would require prior standardisation, i.e. non-financial reporting standards and preferably sector-specific KPIs. Some stakeholders flag the risk of having digitalisation driving the standard setting as this may entail poorer or misleading information.

A majority of stakeholders support an IT format as a way to enable machine readability, even if some see it as an intermediate step. Civil society supports IT formats such as CSV, XML, JSON or XSLX. Many others, including business, would rather support tagging techniques, XBRL and ESEF being the most cited ones, with taxonomies to be derived from non-financial information standards. Public authorities generally eye the extension of the ESEF once it has been evaluated. Interoperability is a key concern. This could be achieved with an EU (or global) common

standard, but several stakeholders, especially academics or citizens, are wary of the fact that this might stifle innovation.

Materiality assessment process. The open public consultation show a strong support among stakeholders for a requirement on companies to disclose their materiality assessment process. Moreover, some supervisory authorities considered that the future standards for non-financial information should provide details on how to perform the materiality assessment specifically in relation to each of the non-financial matters – environment, social and employee issues, human rights, anti-corruption and bribery.

Location of reported information. There is moderate support for requiring all information to be disclosed in the management report.

Some stakeholders, mainly preparers, think that it is convenient that both financial and non-financial information is published in the management report as it provides a better understanding of the company´s overall performance and strategy. However, some also argue that it should not be required and expect the market to regulate itself. As it is costly and challenging to implement this approach for companies not already doing so, some preparers propose they should be able to continue choosing how to publish their information over a transition period, with the ambition to integrate all reporting in the long term.

Some stakeholders – mostly users, but also preparers – consider that EU legislation should provide for a harmonized rule and provide for the location of non-financial information in the management report. Some argue that the non-financial information should be in a specific section within the management report to allow easy access to the information and strengthen the links between non-financial and financial information. They argue that this approach might be justified by the interactions between financial and non-financial information and the increased importance of non-financial information in the stakeholder's decision process.

Conclusion

Different stakeholder groups expressed general agreement with the problem definition as defined in the Inception Impact Assessment, both from a preparer perspective (reporting companies face costs, complexity and multiple demands for information) and from a user perspective (reported non-financial information does not adequately meet user needs). However, users tend to have stronger views on the severity of the current problems compared to preparers.

Some of the main ways in which stakeholder views have influenced the impact assessment are as follows:

1. SMEs: With the exception of listed SMEs, the preferred policy exclude SMEs from the scope. We consider that a requirement on all SMEs to report non-financial information would have been

disproportionate. However, stakeholder consultations also stressed that it was important to support SMEs as active participants in and contributors to the transition to a sustainable economic system, and that the provision of some non-financial information by SMEs is likely to be important in that context. Partly for this reason, the preferred option includes the development of a voluntary standard for SMEs.

2. Alignment of sustainability reporting obligations: stakeholders raised concerns about the alignment of the NFRD reporting requirements with the SFDR and the taxonomy. They also stressed the importance of aligning EU reporting requirements as far as possible with existing global standards and frameworks used in the market. These considerations have strongly influenced the policy options regarding the development of EU non-financial reporting.

3. Costs versus benefits in the context of Covid-19: stakeholder consultations revealed that the Covid-19 pandemic both increases the need for better non-financial reporting while at the same time making it especially important to avoid unnecessary burden and administrative costs for preparers. This has influenced the analysis of the trade-offs regarding the costs and benefits of different policy options. On the one hand, it reinforces the costs of non-action and the baseline scenario, and of the voluntary standards option that would not adequately address identified problems. On the other hand, it has also influenced consideration of the costs for preparers of different policy options: it has influenced the relative assessment of possible requirements for limited assurance or reasonable assurance, and has also influenced the analysis of different scope options, to ensure that the proposal focuses on those companies from whom users most need non-financial information.

ANNEX 3: WHO IS AFFECTED AND HOW?

1. Practical implications of the initiative

According to the preferred policy option, a more harmonized legal framework for non-financial reporting would be established at EU level. The adoption of delegated regulations for the adoption of EU reporting standards would ensure harmonised regimes across Member States and comparable disclosures, as provisions would be directly applicable to companies. Changes to other variables would be done via amendments to different EU directives and would guarantee minimum harmonization across the EU. These changes would be limited and Member States would need to transpose them into national legislation. Reporting companies would need to adjust their reporting practices to changes in the resulting national frameworks and in the delegated regulations adopted.

This option is broadly supported by relevant stakeholder groups such as investors, supervisors, Member States and industry stakeholders. Reporting companies (preparers) present more divergent views on the benefits of the initiative. This option fits with the Council's conclusions on the CMU in December 2019, where the importance of reliable, comparable and relevant information on sustainability risks, opportunities and impacts was stressed, and the Commission was called to consider the development of a European non-financial reporting standard;[94] and with the European Parliament's resolution on sustainable finance in May 2018, which called for the further development of reporting requirements in the framework of the Non-Financial Reporting Directive.[95]

2. Summary of costs and benefits

Benefits and costs of the preferred policy option for each category of stakeholders have been summarised in table 1.

Main benefits refer to users, who would enjoy access to public reliable, comparable and relevant non-financial information presented in a digitalised manner. On the one hand, investors would be able to take sufficient account of the risks and opportunities that affect investee companies stemming from sustainability matters, and the social and environmental impacts of their investments. On the other hand, civil society organisations would be able to hold companies more accountable for their impacts on society and the environment, thereby strengthening the social contract between companies and citizens.

[94] Council Conclusions on the Deepening of the Capital Markets Union (5 December 2019)
[95] European Parliament resolution of 29 May 2018 on sustainable finance (2018/2007(INI))

This will help to improve the allocation of financial resources, so that more financial resources flow to companies and activities that address social and environmental problems and fewer resources flow to companies and activities that exacerbate such problems; and would reduce systemic risks to the economy resulting from the fact that many investment decisions currently do not take adequate account of sustainability-related issues, especially environmental and climate matters.

Additionally, reporting companies will get clarity about the reporting obligations and the kind of information they need to report, and standardised public information will reduce the amount of ad hoc requests they receive from different users, resulting in a reduction of the unnecessary costs in which companies incur today. However, overall administrative costs will inevitably increase for preparers, as an increasing number of companies would be required to report in a more detailed manner. Users, on the other hand, will experience costs savings, as a result of adequate information being publicly available in a digital manner.

Table 1– Impacts on different stakeholders of preferred policy option compared to baseline

	Reporting companies[96]	Investors	Civil society organisations & trade unions	EU & national authorities (e.g. env. agencies)	Society at large	National supervisors
Benefits	↑↑	↑↑	↑↑	↑↑	↑↑	↑↑
Costs	↑↑	↓↓	↓↓	↓	↓	↑

Tables 2 and 3 present the benefits and costs deriving from the specific actions that will be undertaken in order to implement the preferred option. Benefits and costs are described for different categories of stakeholders. In some cases, the benefits of concrete actions could only be described in qualitative terms. The contribution of the specific actions to the general objectives could not be quantified as there are methodological limitations in quantifying the general objectives themselves. Annex 1 presents the main sources used for gathering this evidence. The following tables will therefore mainly follow a descriptive approach, specifying the concrete actions along with their benefits and costs.

[96] The arrows in table 1 do not intend to express a net cost effect on companies of zero. In addition to costs savings resulting from increased clarity about the reporting obligations and the reductions of the amount of ad hoc requests received by companies, these arrows also reflect other benefits for preparers, such as enhanced company resilience or greater access to capital.

Table 2– Overview of benefits: preferred option

I. Overview of Benefits (total for all provisions) – Preferred Option		
Description	***Amount***	***Comments***
Direct benefits		
Developing and requiring use of EU reporting standards	• public availability of complete, relevant and comparable information; • improved usability of information (standardised presentation); • greater control and scrutiny of robustness of methodologies behind the disclosures by users;	Stakeholders who benefit: • investors • civil society organisations and trade unions • policy makers • national supervisors national authorities (e.g. environmental agencies and national environmental accounts) • third party data providers and sustainability rating agencies • reporting companies (in their capacity of users of information: from suppliers, clients and investee companies)
	• administrative costs savings for preparers due to clarity about what information is required to be reported;[97] • reduction of costs for preparers from addressing investors ad hoc requests for information;[98] • simplified SME standards for voluntary use, enable SMEs to participate in the transition to a sustainable economy, as it would facilitate SMEs to provide information to investors and thus attract capital;[99]	Stakeholders who benefit: • reporting companies (preparers)
Requiring limited assurance on reported information	• public availability of reliable information; • ensure all companies under the scope of the NFRD	Stakeholders who benefit: • investors

[97] CEPS study shows that companies that find it more difficult to decide which information should be included in the non-financial statement usually incur greater administrative and incremental costs. It also shows that the majority of the surveyed companies subject to the NFRD, report against multiple standards and frameworks at least to a certain extent and incur higher costs the more standards and frameworks they follow (see figure 5.26 of CEPS study). Assuming that as a result of the obligation to report against standards, all companies would find "easy" the decision about what information to disclose, the estimated total reporting costs would be reduced by around 20% or around EUR 600 million under the preferred option. These estimates however must be treated with appropriate caution, as the reporting costs are mostly driven by the nature and complexity of the business (i.e. the costs of collecting and analysing information itself may not depend only on the clarity on what to disclose). See Annex 17 for costs analysis.

[98] Cost savings could amount to EUR 24 200 - 41 700 per company per year, and around EUR 1 200 – 2 000 million per year for the preferred option, if standards were to completely eliminate the need for additional information requests to preparers. These calculations are based on the replies to the survey carried out by SustainAbility. The same study also indicates that companies who spend more time in reporting (which suggests better reporting in principle), spend less time filling in questionnaires. See annex 17 for a detailed cost analysis.

[99] 88% of respondents to the open public consultation who are or who represent SMEs indicated that simplified standards would be useful for SMEs. The same percentage of SMEs and respondents (66%) believe that a simplified standard would limit the burden for SMEs arising from information requests. The results of the SME panel consultation show most SMEs (68%) would welcome the development of a simplified standard for SMEs to be used either in a voluntary (53%) or a mandatory basis (15%).

	are reporting appropriately; • reduction of expectation gap from users perspective, brining clarity and a common level of assurance to all information reported;	• civil society organisations and trade unions • policy makers • national supervisors • national authorities (e.g. environmental agencies and national environmental accounts) • third party data providers and sustainability rating agencies • reporting companies (in their capacity of users of information: from suppliers, clients and investee companies)
Requiring tagging of reports according to a digital taxonomy	• better searchability/accessibility to and comparability of reported information needed by users; • improvement of data analysis, greater speed and accuracy of data handling; • better decision-making; • costs savings for users: fewer difficulties in finding the information they are looking for; • Availability of digital information from clients, suppliers and investee companies;	Stakeholders who benefit: • investors • civil society organisations • policy makers • national supervisors • national authorities (e.g. environmental agencies and national environmental accounts) • third party data providers and sustainability rating agencies • reporting companies (in their capacity of users of information: from suppliers, clients and investee companies)
Require reporting on intangibles	• greater availability of essential information about a company's value; • contribute to explain the gap between the accounting book value of many companies and their market valuation as indicated by the ECB;[100]	Stakeholders who benefit: • investors • reporting companies (in their capacity of users of information: from suppliers, clients and investee companies)
Requiring disclosure in management report	• better searchability/accessibility to and comparability of reported information needed by users • greater coherence with the financial reporting legal framework; • improvement of availability of relevant information linked to other financial information; • more comparable information, given it will be easier to find (i.e. always in the management report), and it	Stakeholders who benefit: • investors • civil society organisations and trade unions • policy makers • national supervisors • reporting companies (in their

[100] "Investment in intangible assets in the euro area" in *ECB Economic Bulletin, Issue 7/2018*, European Central Bank, 2018

	will be available at the same time by all companies reporting according to the NFRD.; • costs savings for users from looking for non-financial information;	capacity of users of information: from suppliers, clients and investee companies)
Strengthening of supervision regime of non-listed companies	• ensure all companies under the scope of the NFRD are reporting appropriately; • increase trust in reported information; • improve quality of reporting;	Stakeholders who benefit: • investors • civil society organisations and trade unions • policy makers • national supervisors • national authorities (e.g. environmental agencies and national environmental accounts) • third party data providers and sustainability rating agencies • reporting companies (in their capacity of users of information: from suppliers, clients and investee companies)
Tasking ESMA with issuance of guidelines	• ensure supervisory convergence, ensuring consistent information across the single market; • costs savings for supervisors due to clarity about how to supervise non-financial reporting	
Clarification in law of double materiality concept	• clarity that reported information is relevant from either of both of the materiality perspectives	Stakeholders who benefit: • investors • civil society organisations and trade unions • policy makers • national supervisors • national authorities (e.g. environmental agencies and national environmental accounts) • third party data providers and sustainability rating agencies • reporting companies (in their capacity of users of information: from suppliers, clients and investee companies)
	• clarity about what information is required to be reported, costs savings for prepares	Stakeholders who benefit: • reporting companies (preparers)
Clarification in law of the exemption to subsidiaries	• clarity about which companies are required to report which information; • users of information have access to adequate information; • level playing field between EU companies and non-EU companies with activities in the EU, which would be reporting non-financial information either at consolidated level or via subsidiaries	Stakeholders who benefit: • investors • civil society organisations and trade unions • policy makers • national supervisors • national authorities (e.g. environmental agencies and national

		environmental accounts) • third party data providers and sustainability rating agencies • reporting companies (in their capacity of users of information: from suppliers, clients and investee companies)
	• clarity about which companies are required to report what information;	Stakeholders who benefit: • reporting companies (preparers)
Require broader categories of companies to report according to the NFRD	• availability of more relevant, comparable reliable, timely and accessible information, from a wider range of companies; • enhanced coherence with reporting obligations under other sustainable finance initiatives	Stakeholders who benefit: • investors • civil society organisations and trade unions • policy makers • national supervisors • national authorities (e.g. environmental agencies and national environmental accounts) • third party data providers and sustainability rating agencies • reporting companies (in their capacity of users of information: from suppliers, clients and investee companies)
Indirect benefits		
Developing and requiring use of EU reporting standards	• improvement of reliability and quality of ESG ratings; • greater accountability of companies would affect company behaviour and have a beneficial effect on the environment, society and fundamental rights; • better policy-making related to environment, society and fundamental rights matters; • costs savings for users from trying to find adequate non-financial information; • enhance coherence of EU sustainability reporting requirements, i.e. SFDR and TR; • costs savings for supervisors due to increased clarity about what information companies should report	Stakeholders who benefit: • investors • civil society organisations • policy makers • third party data providers and sustainability rating agencies • society at large
	• more awareness and a better management of sustainability-related risks would result in more resilient companies, ; • first-mover advantage for EU companies, in light of international developments; • The public availability of comparable information	Stakeholders who benefit: • reporting companies (preparers)

	would translate into a competitive advantage for more sustainable companies (will be more easily identifiable);	
Requiring limited assurance on reported information	• line of defence that facilitates supervision; • costs savings for supervisor; • greater coherence with assurance provided for the rest of information included the management report;	Stakeholders who benefit: • investors • civil society organisations and trade unions • policy makers • national supervisors • national authorities (e.g. environmental agencies and national environmental accounts) • third party data providers and sustainability rating agencies • reporting companies (in their capacity of users of information: from suppliers, clients and investee companies)
	• more rigorous reporting processes, that allow companies better comply with the NFRD provisions and identify risks to their business;	Stakeholders who benefit: • reporting companies (preparers)
Requiring disclosure in management report	• greater trust in information reported, as it is part of annual financial report; • raise the profile of non-financial information, internally and externally;	Stakeholders who benefit: • investors • civil society organisations • policy makers • national supervisors • reporting companies (in their capacity of users of information: from suppliers, clients and investee companies)

The following table presents the total costs of the preferred option. Costs for preparers have been based mainly on data collected via the survey and interviews carried out by CEPS in their study on the NFRD. Costs for the EU and national administrations build on the cost-benefit analysis for the Regulatory Technical Standard on the European Single Electronic Format.[101] See all detailed cost analyses in annex 17.

[101] Feedback Statement on the Consultation Paper on the Regulatory Technical Standard on the European Single Electronic Format (ESEF), Annex IV.

Companies in particular would also incur costs as a result of the reporting requirements of the Taxonomy Regulation. Although we do not have final calculations of these costs yet, a preliminary, illustrative estimation of their magnitude is included in the draft staff working document that will accompany the Delegated act on a climate change mitigation and adaptation taxonomy.[102] The final calculation of these costs will be presented in the Impact Assessment of the Delegated Act that will specify the taxonomy disclose requirement on NFRD companies in more detail (to be adopted by mid-2021).

Table 3– Overview of costs: preferred option

II. Overview of costs – Preferred option							
		EU		Member States (administrations)		Reporting companies (preparers)	
		One-off	Recurrent	One-off	Recurrent	(Incremental) One-off	(Incremental) Recurrent
Total		EUR 0,5 million	EUR 9,1 million	EUR 35,5 million	EUR 5 million	EUR 1 200 million	EUR 3 600 million
Admin costs: Reporting against standards	Direct costs	NA	EUR 9 million (max.) for development/ maintenance of EU standards. There are different possible mechanisms to limit these costs	NA	NA	EUR 700 million, include costs of familiarising with the reporting obligations	EUR 2 100 million yearly costs from reporting against EU standards
	Indirect costs	NA	NA	Marginal costs incurred by national supervisors from familiarising with new reporting obligations	Enforcement priorities geared towards non-financial reporting might translate into some costs.	NA	NA

[102] Based on these costs estimates, and bearing in mind the very limited data currently available, the additional costs on NFRD companies stemming from taxonomy-related disclosures according to the preferred policy option of this Impact Assessment would amount to: EUR 1 200 – 3 700 million one-off costs and EUR 600 – 1 500 million recurring costs per year. These figures are calculated on the assumption that only 60% of the 49 000 companies that would be subject to the NFRD according to the preferred policy option of this Impact Assessment will have taxonomy eligible activities. A longer explanation about the methodology used for this preliminary calculation can be found in the draft Impact Assessment of the Delegated act on a climate change mitigation and adaptation taxonomy.

Admin costs: Tagging reports against digital taxonomy[103]	Direct costs	EUR 500 000 for developing an IT taxonomy against which companies would tag their reports	EUR 80 000 for the annual maintenance of the IT taxonomy	EUR 35,5 million implementation costs for the development of digital ad hoc processes by Officially Appointed Mechanisms (listed companies) and by Business Registers (non-listed companies)	EUR 5 million for the annual maintenance and update of digital registers	EUR 480 million for implementing the IT taxonomy in the company's reporting processes	EUR 80 million for the yearly tagging of reports according to the IT taxonomy
	Indirect costs	NA	NA	NA	NA	NA	NA
Compliance costs: Assurance of report	Direct costs	NA	NA	NA	NA	NA	EUR 1 400 million annual costs of hiring assurance services
	Indirect costs	NA	NA	NA	NA	NA	NA

[103] Changes to this variable are assessed in annex 16.

ANNEX 4: SME TEST

(1) Preliminary assessment of businesses likely to be affected	
Preferred option - package 3: *Directly affected: SMEs in the scope of the revised NFRD:* Listed SMEs (about 1.000 companies) would be brought under the scope of the NFRD. The primary reason for including listed SMEs under scope is that investors in principle need equal information from all listed companies. Listed SMEs comprise 26% of all listed companies in the EU. *Indirectly affected: SMEs that are suppliers or clients of companies under scope of the NFRD.* Making the use of standards mandatory for companies under the scope of the NFRD, and expanding the number of companies under scope (from around 11 700 to more than 49 000), would increase the number of companies that seek detailed information from their suppliers or clients, including SMEs. This phenomenon is an inevitable part of the transition to a sustainable economic system, and it would occur to some extent regardless of the revision of NFRD. In order to benefit from and contribute to the transition, more SMEs will in any case have to share more non-financial information. Changing markets and consumer preferences mean that a growing number of large companies and brands want to know about the social and environmental risks and impacts of their supply chains. Banks and asset managers want better information on the risks and impacts of their financing activities. Sustainable procurement practices are becoming more prevalent, in the public and in the private sector. In addition, already agreed EU legislation in the field of sustainable finance will have an indirect effect on SMEs. The Taxonomy Regulation requires companies under scope of the NFRD to disclose their alignment with the taxonomy and they may need information from suppliers and clients, including SMEs, to do that. The Sustainable Finance Disclosure Regulation (SFDR) requires financial market participants to disclose information about the adverse impacts of their investments, and for that they will need information from SMEs whose equity is part of the portfolios they manage. On the one hand, the proposed revision of the NFRD may accelerate and intensify these trends. On the other hand, it can help to avoid a situation in which non-financial information demands on SMEs increase in an incoherent and burdensome way.	See section 5.3.3 (Scope options), 6.3.4 (Analysis of impacts of Package 3), and 7 (Preferred option)

(2) Consultation with SMEs representatives	
SME Panel: a targeted consultation of micro, small and medium enterprises was conducted from 3 March to 27 May 2020. The consultation was extended by 1 month in order to allow SMEs to provide input. However, due to the corona virus crisis the number of replies (350) was lower than expected. Annex 5 provides a summary of the results of the SME Panel. *Open Public Consultation on NFRD*: was organised from to 20 February-11 June 2020. The public consultation was extended by 1 month in order to give stakeholders, especially corporates and representatives of SMEs, more time to reply.	See annex 2 (Stakeholder consultation)
(3) Measurement of the impact on SMEs	
Listed SMEs: Bringing listed SMEs under the scope of the NFRD would create an additional EUR 39 million incremental costs. The costs of non-financial reporting are marginal compared to the overall costs of listing for SMEs. A requirement to report non-financial information is therefore not likely to make the difference between an SME deciding to list or not, and should not therefore have a significant impact on SMEs' access to capital. **Indirect impacts on other SMEs**: It has not been possible to quantify the costs of these indirect effects. In particular, it would not be possible to disaggregate the indirect effect of the proposed revision of the NFRD from the effects of the overall transition to a sustainable economy described in point 1. Additionally, we have not been able to find reliable data on the number of SMEs in the supply-chains of large European companies[104]. The results of the SME Panel do nevertheless provide some context that help to understand these indirect impacts. For example: • 28% of the medium-sized SMEs that responded to the SME panel already publish detailed non-financial information their websites, whereas only 9% of small enterprises do so. • 48% of respondent SMEs (and 80% of medium-sized companies) have already received at least one request for non-financial information. The	See sections 6.1, 6.3, specifically 6.3.4 (Analysis of impacts of Package 3), annex 17 (Costs Analysis) and Footnote 70 (Estimation of costs of listing)

[104] EcoVadis estimtaes that the largest European, UK and Swiss companies with revenue between 100 million-1 billion USD have on average 4.500 tier 1 suppliers, (i.e. direct suppliers), companies with revenue between 1-5 billion USD have on average 11.000 direct suppliers, and companies with revenue of more than 5 billion USD have on average 78.000 direct suppliers. However, there is no data how many of the tier 1 suppliers are SMEs, let alone if they are European SMEs.

two most common sources of such requests were large companies to whom the SME supplies good or services (28%), and public administrations when the SME applies for public funds (24%). Only 14% of respondents have received such requests from banks. • Of all SME respondents who are in large company supply chains, 43% have received information requests from the large company buyer. For medium-sized companies who are in large company supply chains, the figures goes up to 76%. These results suggest that medium-sized companies are more likely to receive information requests than smaller companies, and that supply-chains are currently a bigger source of these requests than are client relationships with banks. An ECB survey shows that 50% of Euro area SMEs consider bank loans and credit lines to be relevant financial instruments for their businesses.[105] This would suggest that a minimum of 50% of SMEs are therefore likely to receive information requests from banks that will need to report on sustainability of their lending portfolios. 33% of Euro area SMEs receiving grants and subsidised loans are also likely to receive such request as governments are introducing sustainability conditions for grants and subsidies.	
4) Assess alternative options and mitigating measures	
The standard-setter would develop a simplified standard for voluntary use by SMEs who are not under the scope of the NFRD. The simplified nature of this standard would reflect the fact that SMEs often do not have the technical expertise nor resources necessary to prepare reports in accordance with state-of-the-art, sophisticated standards. This standard would mitigate the indirect effects on SMEs outlined in point 1 above. It would also facilitate SMEs' participation in the transition to a sustainable economy. The simplified standard would be aligned with the full standard to be applied by companies under the scope of the NFRD, and it would therefore provide a cost-effective means for SMEs to respond to additional information demands that may result from the proposed changes to the NFRD. In response to the SME Panel, 53% of SMEs supported the idea of a simplified, voluntary standard. A further 15% were in favour of a mandatory standard, while 30% opposed any standard for SMEs.	See sections 5.2.1 (Standardisation options), annex 16 (Assessment of policy options for other variables), and annex 18 (Discarded policy options)

[105] Survey on the Access to Finance of Enterprises: Small businesses report challenging outlook for their access to external financing due to COVID-19, ECB, May 2020.

Alternative options: The impact assessment considered two other options: expanding the scope to non-listed medium sized companies (package 4 of the scope options) and expanding the scope to all SMEs (option discarded at an early stage). These options were not retained on the grounds of costs, efficiency and proportionality.	

ANNEX 5: SUMMARY REPORT OF SME PANEL

1. Introduction

As part of the consultation strategy for the revision of the Non-Financial Reporting Directive (NFRD) (2014/95/EU)[106], the European Commission deployed a targeted survey to micro, small, and medium enterprises (SME) referred to as the "SME Panel Consultation" or "Panel", which was managed by the European Enterprise Network (EEN). The SME Panel was open to receive responses from 3rd March 2020 through 27th May 2020.

For purposes of this document, the Panel will be referred to as the "survey" and it comprised thirteen questions that aimed to provide a good understanding of the current views and experiences of SMEs around non-financial information processes and requirements.

In order to present the results of the survey, this document summarises the responses provided by 371 companies across the EU. The responses provided by 17 companies showed such companies to be large undertakings; likewise, the size of six respondents could not be determined. Both groups were therefore excluded from the graphs, analysis, and narrative presented here, which is meant to understand the context of SMEs only. This leaves a total of 348 respondents whose replies are analysed in this report. Section 5 provides more information on the criteria used to classify companies as micro, small or medium.

2. Demographics of the respondents

The 348 respondents to the survey are located across 20 different Member States (MS) of the European Union and the United Kingdom. 78% of the responses to the survey belong to organisations from Portugal, Romania, Bulgaria, Spain, Poland, and Italy. Other MS represented to a smaller extent are Slovakia, Hungary, Czech Republic, Ireland, Sweden, Lithuania, Latvia, and Germany, among others. The survey also received 3% of responses (i.e. 9 responses) from the United Kingdom.

The respondents to the survey were segmented by size of the company according to the Accounting Directive[107]. The survey's population is comprised as follows: micro companies (58%), small companies (27%), and medium companies (15%). Table 1 provides a detailed overview of the number of respondents to the survey classified by size.

[106] Non-Financial Reporting Directive (NFRD) (2014/95/EU) https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32014L0095
[107] See Section 5

Company size	Number of respondents	Proportion to total
Micro	203	58%
Small	95	27%
Medium	50	15%
Total	**348**	**100%**

Table 1

On 26th November 2019, the European Commission published through DG GROW the annual report on European SMEs[108] which provides, among other things, information on the number of SMEs in the European market. Figure 1 shows the distribution of SMEs that responded to the survey (blue) and the estimated distribution of SMEs in the EU28 for 2018 according to the annual report on European SMEs (orange). The observed distribution of respondents in the consultation differs from that of the market as a result of targeting the survey to larger SMEs (i.e. medium and small companies), as they are more likely to be impacted by the NFRD.

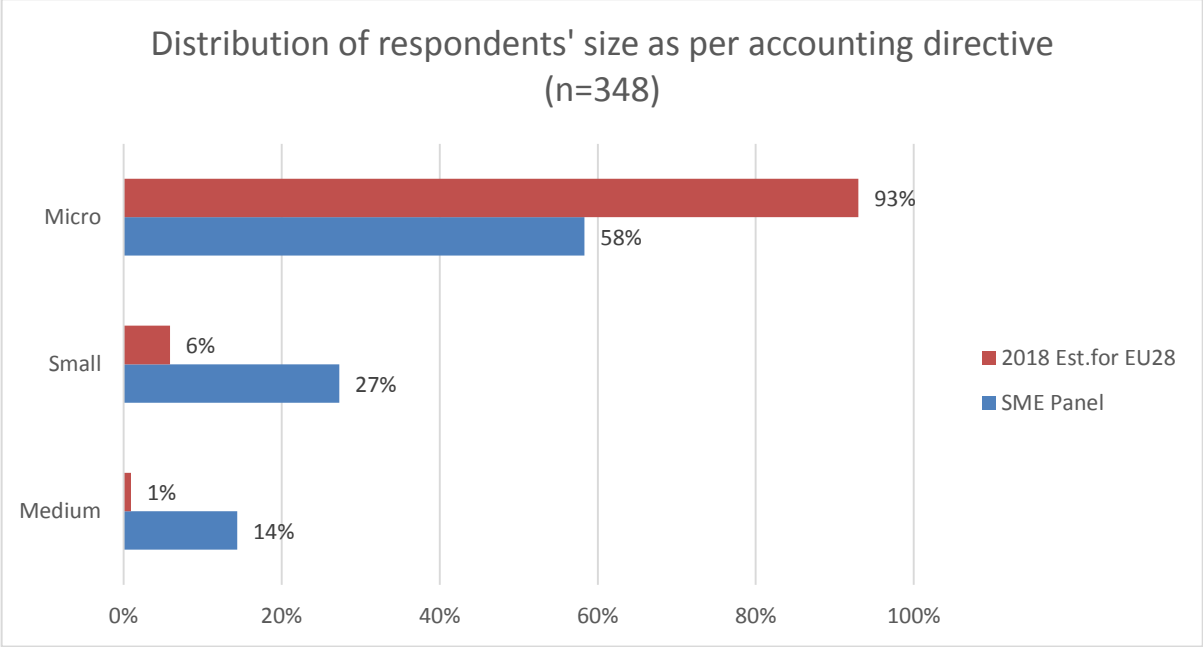


Figure 1

The survey also identified whether or not respondents are listed on regulated financial markets. 3% of the respondents identified themselves as listed, whereas 96% of the respondents declared not to be listed (Figure 2). A study carried out by CEPS shows that around 0,02% of the SMEs in the EU27 are listed on a regulated market.

[108] https://ec.europa.eu/growth/smes/business-friendly-environment/performance-review_en

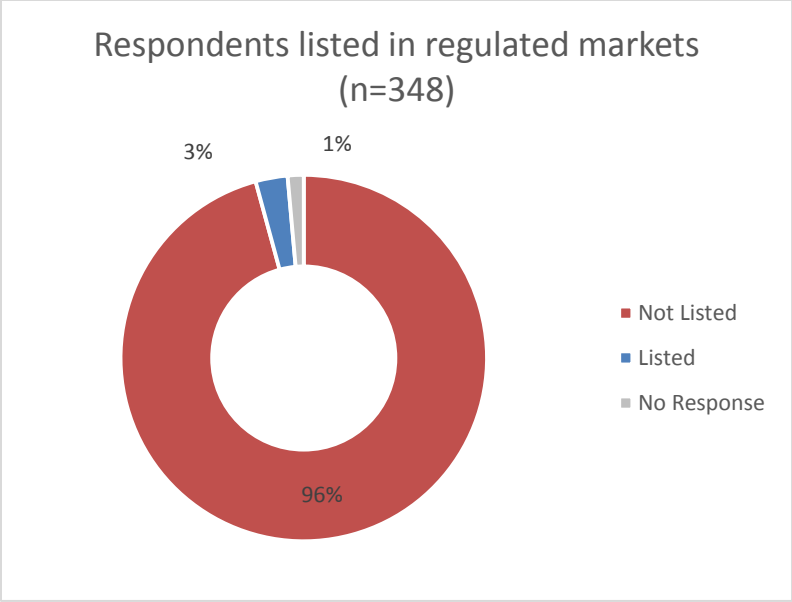


Figure 2

As observed in Figure 3, 163 SMEs (47%) responded that they are part of the supply chain of a large company while 174 SMEs (50%) are not part of the supply chain of a large company. When looking at the sizes of SMEs (Figure 4) who are part of large companies' supply chains, it may be observed that medium and small sized companies are more likely to be part of the supply chain of a large company (66% and 58% respectively) than are micro sized companies (37%).

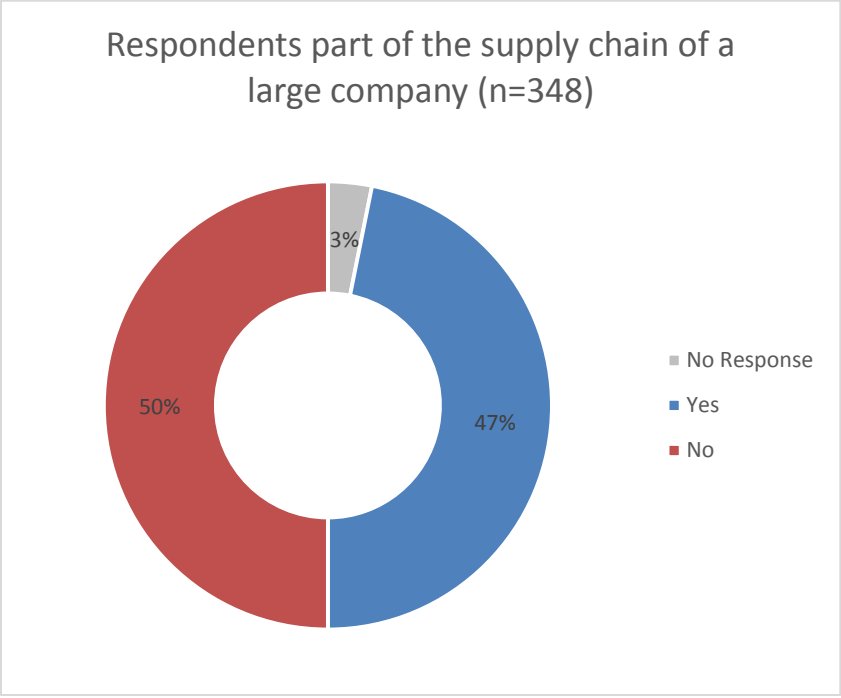


Figure 3

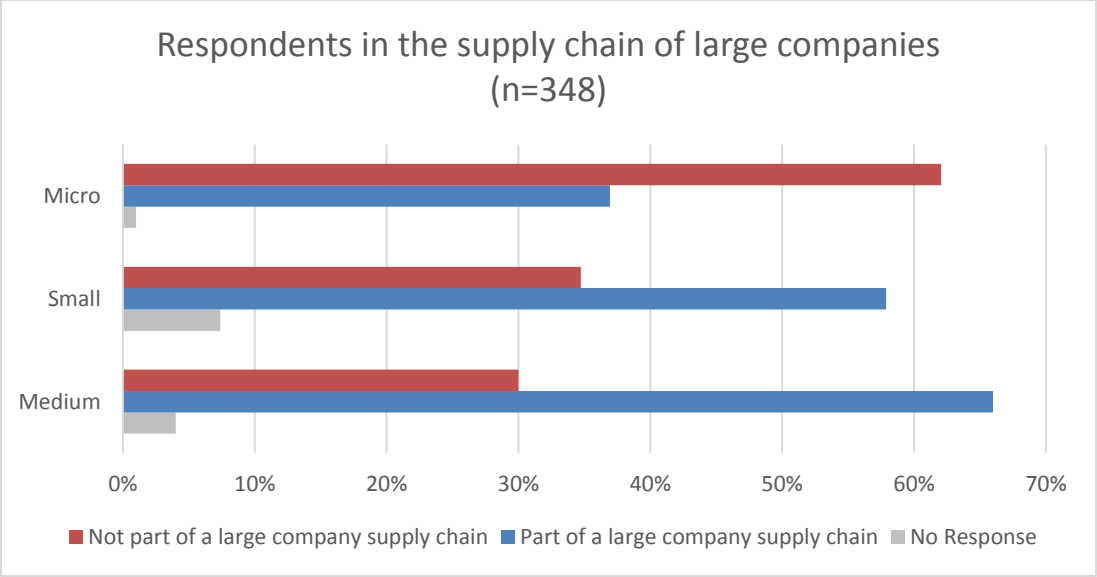


Figure 4

The respondents to the survey have business activities in different sectors as described by the NACE codes. Most respondents identified themselves to have business activities in multiple sectors simultaneously. The top 3 sectors represented in this analysis are: 1) C Manufacturing, 2) S Other service activities, and 3) M Professional, Scientific and Technical activities. Figure 5 shows the percentage of any given sector in relation to the total number of respondents. No SME described itself as being involved in sectors: "T Activities of Households as Employers […]" or "O Public Administration and Defence […]".

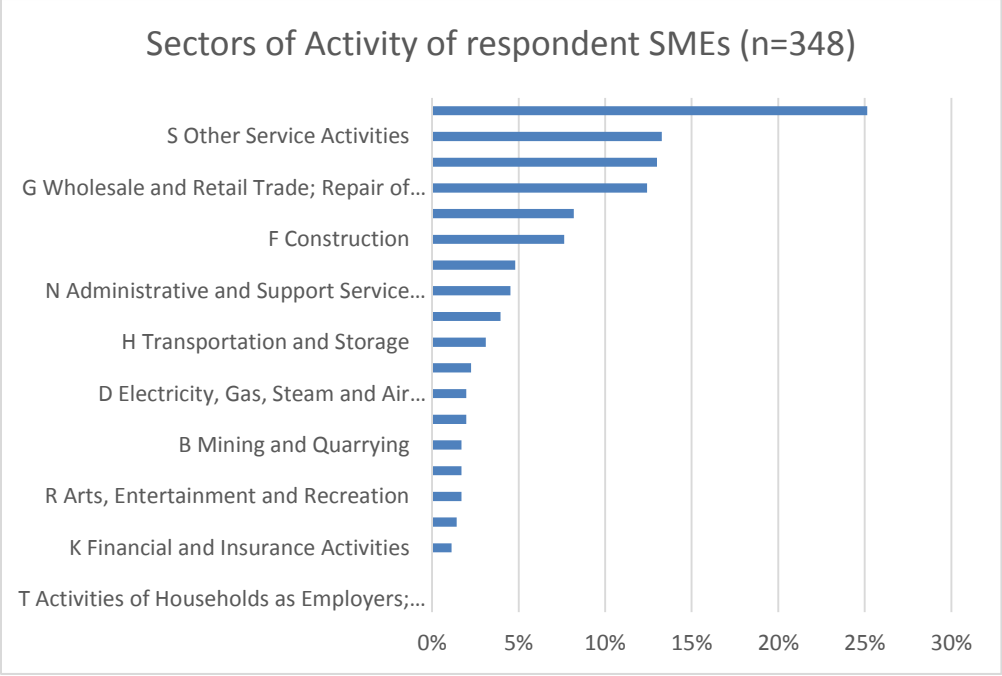


Figure 5

3. Current ESG practices and requirements

3.1 Practices on ESG data collection

From the total 348 SMEs who replied to the survey, 291 companies (i.e. 82%) declared they collect data on at least one of ten issues related to ESG matters, as proposed in the survey.[109]

The issues on which SMEs replying to the survey most commonly collect data are: employee training (64%), accidents and/or sick leave (60%), energy use (51%), water use (47%), and percentage of women and men in the workforce (46%). A small number of respondents to the survey also collect data on other matters different from the options available in the consultation; these responses include but are not limited to, data protection, worker needs and satisfaction, and nutrition. Figure 6 provides a visual representation of this distribution.

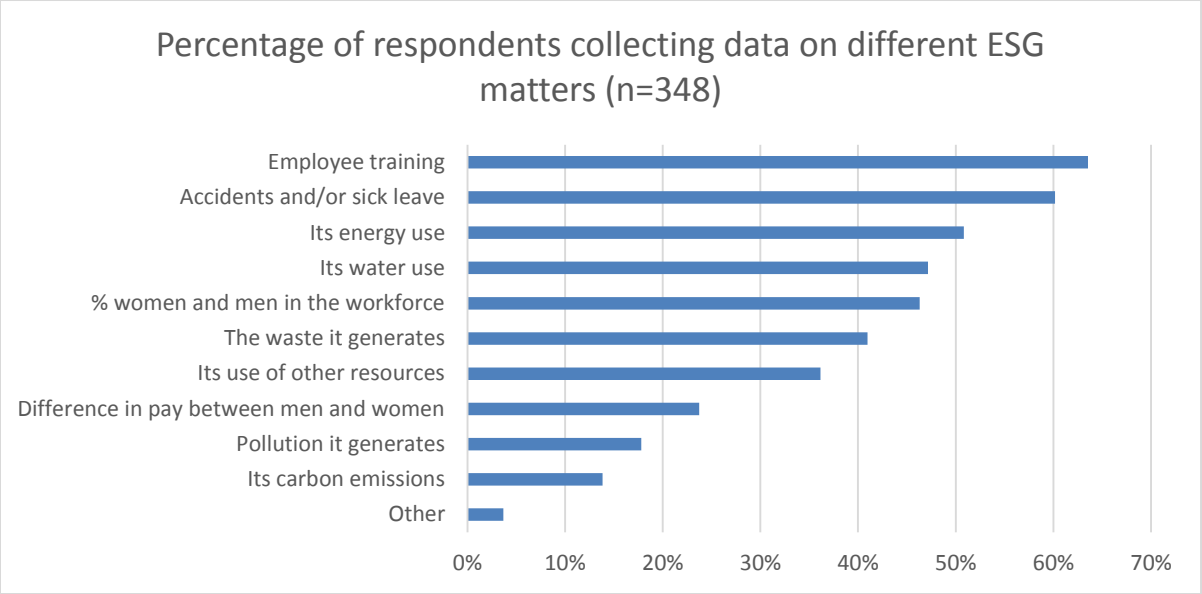


Figure 6

The respondents to the survey collect data, on average, on 4 different issues. As shown in Figure 7, 16% of the respondents do not collect data on any issue, 13% collect on 4 issues, and 11% collect data on 6 issues.

[109] This text is based on the responses to Question 5 in the survey. Which asked whether the SMES itself collects data about its own performance. It was not a question about reporting or publishing the information.

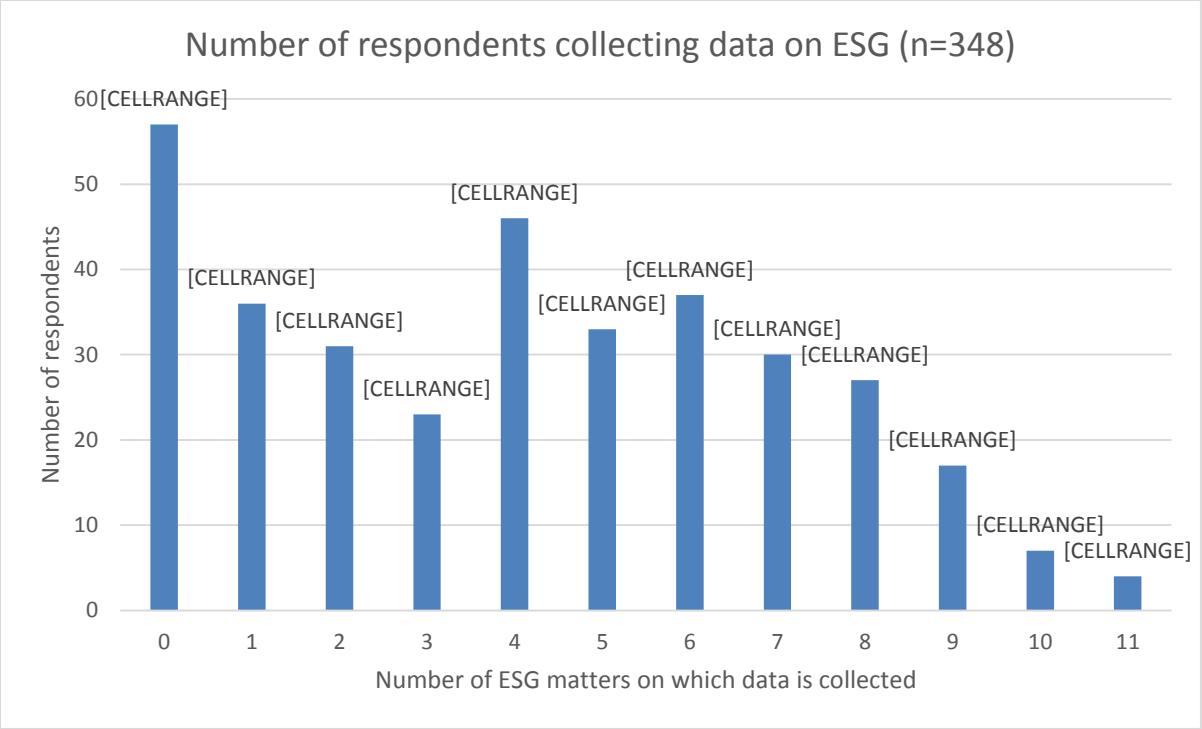


Figure 7

From the responses to the survey, it is observed that the likelihood to collect ESG information increases for medium size companies (98% collect at least some data) compared to micro companies (77%). Similarly, the number of issues on which companies collect data tends to increase with the size of the company. For instance, on average medium sized companies collect data on 6 different ESG issues whilst micro sized companies collect data on 3 issues. Table 2 provides an overview, by size, of the total number of SMEs collecting ESG issues and of the average number of issues on which data is collected for the total population.

Company size	Proportion of companies collecting data	Average number of issues for which data is collected
Micro	77%	3
Small	89%	5
Medium	98%	6

Table 2

Below, Figure 8 illustrates in further detail the individual issues of ESG information on which different size SMEs collect data[110].

[110] Figure 8 considers, yet does not display responses received as "No" or no responses.

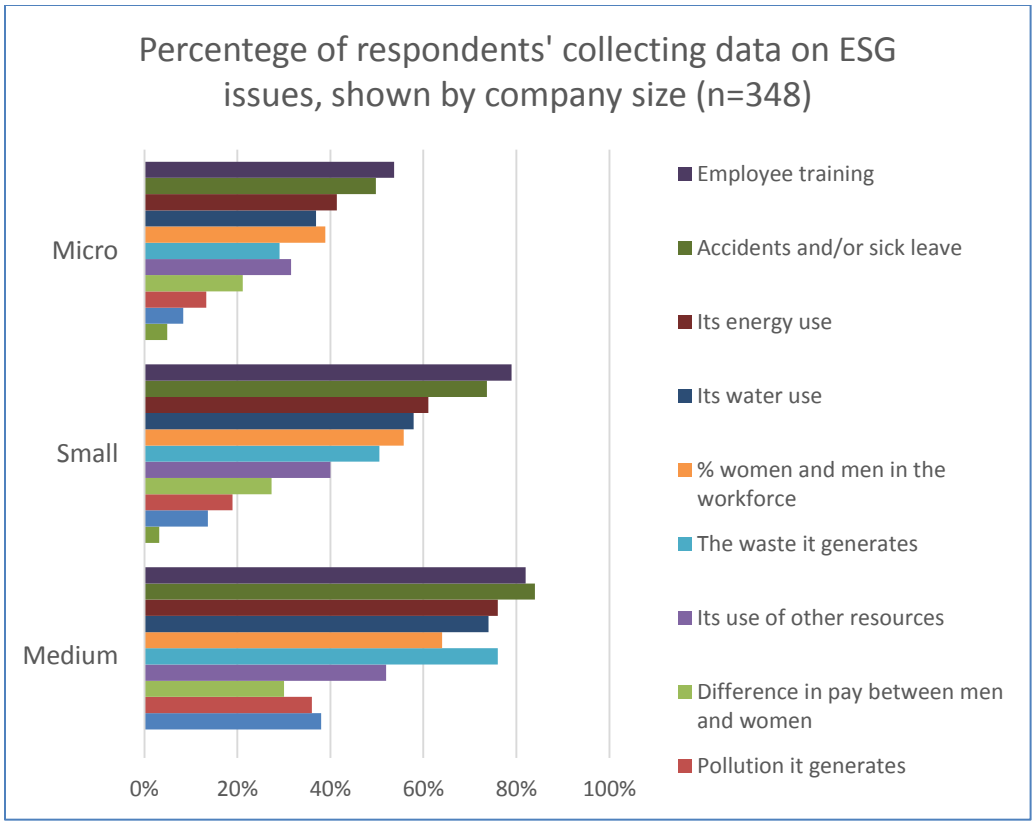


Figure 8

3.2 Publication and disclosure practices

Respondents to the survey were asked whether they make any reference to their ESG policies, performance, or commitment, if any, on their company website. Also, SMEs were asked if they ever share any ESG related information through social media.

As it is shown in Figure 9, 52% of the respondents to the survey do not make any reference to ESG policies or performance on their website. Combined, 34% of the respondents either make a general statement or publish detailed information on their ESG policies and commitments.

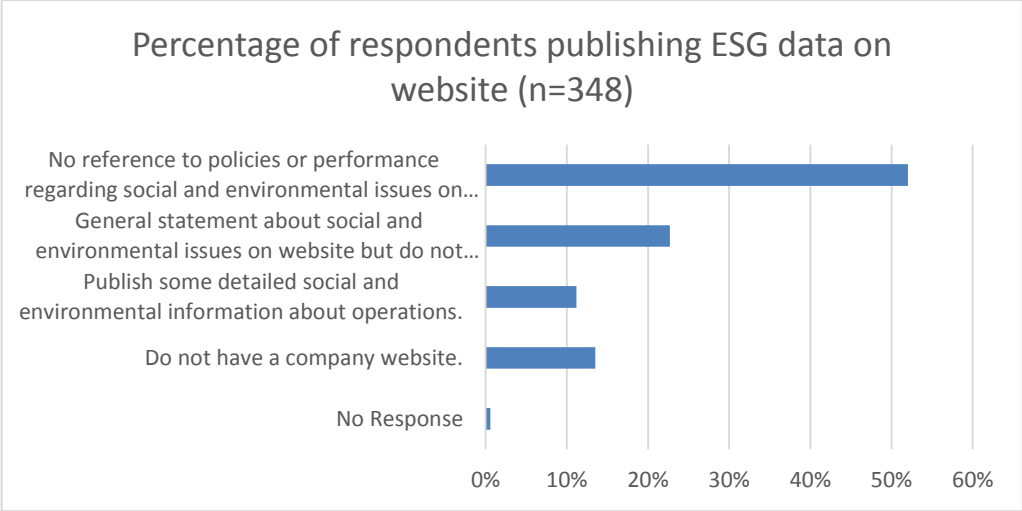


Figure 9

Medium sized companies are more likely than small and micro sized companies to either make a general statement (34%) or publish detailed ESG information (28%) in their websites. Comparably, 24% of small sized companies make general statements and 9% publish detailed ESG information in their websites, while 19% of micro companies make general statements and 8% publish detailed ESG information in their websites.

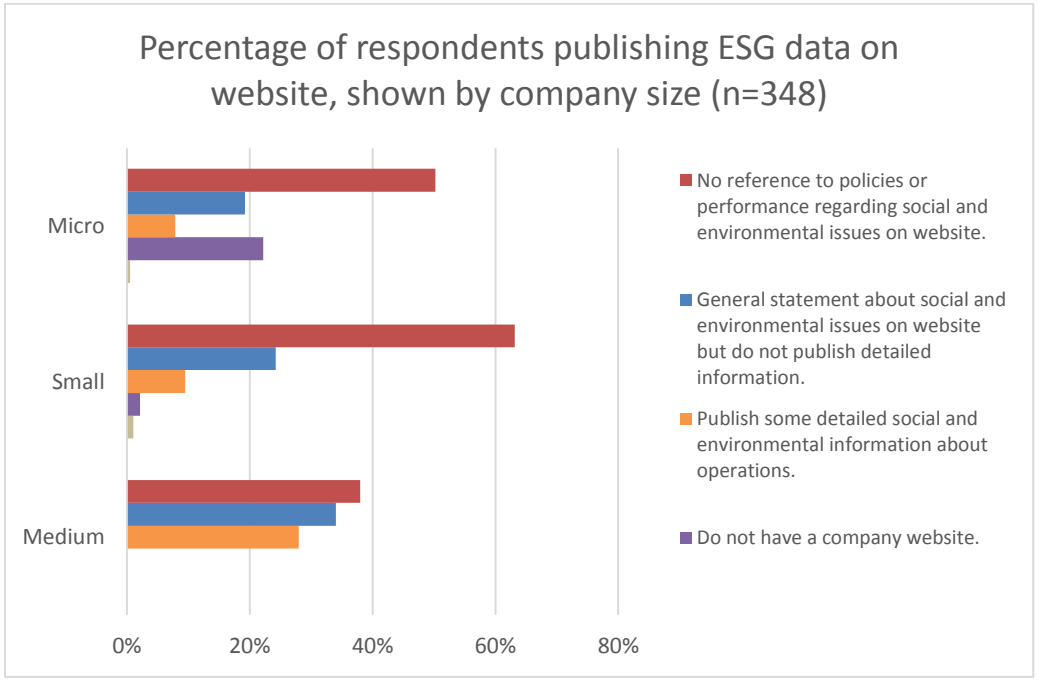


Figure 10

Regarding the practices of the respondents of sharing ESG information via social media, 59% indicated that they never share ESG data through social media, 35% share ESG information sometimes, and 6% of the respondents often share ESG information through social media. Similar to the behavior observed in the publication of ESG data on companies' websites, medium-sized companies are more likely to share ESG information through social media. However, similar percentages of micro (4%), small (7%), and medium (6%) companies often share ESG information through social media.

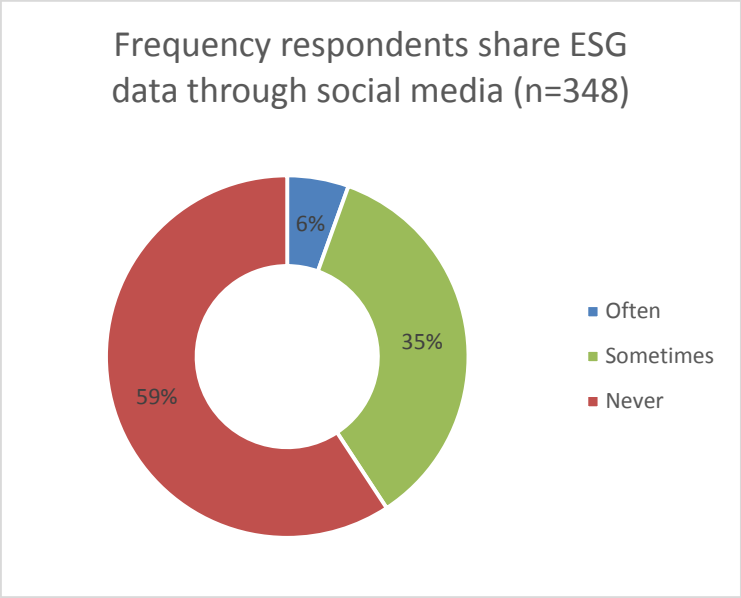


Figure 11

3.3 Requests of ESG information from stakeholders

The survey included questions to understand how different SMEs' stakeholders (e.g. SME's customers, insurance companies, banks, NGOs, etc.) interact with them regarding requests for ESG information. From the total 348 respondents, 169 companies (48%) indicated they have been requested to provide ESG data by at least one stakeholder group. Figure 12 shows the ratio of companies from the total number of respondents who receive requests for ESG information from different categories of stakeholders.

The stakeholders who most frequently require ESG data from SMEs are: companies to which SMEs provide goods or services (28% of respondents receive such requests), public administration when applying for funds (25%), and insurance companies (18%). A small number of SMEs also indicated that organisations who provide certification services and public administration for purposes other than releasing funds, also request ESG data.

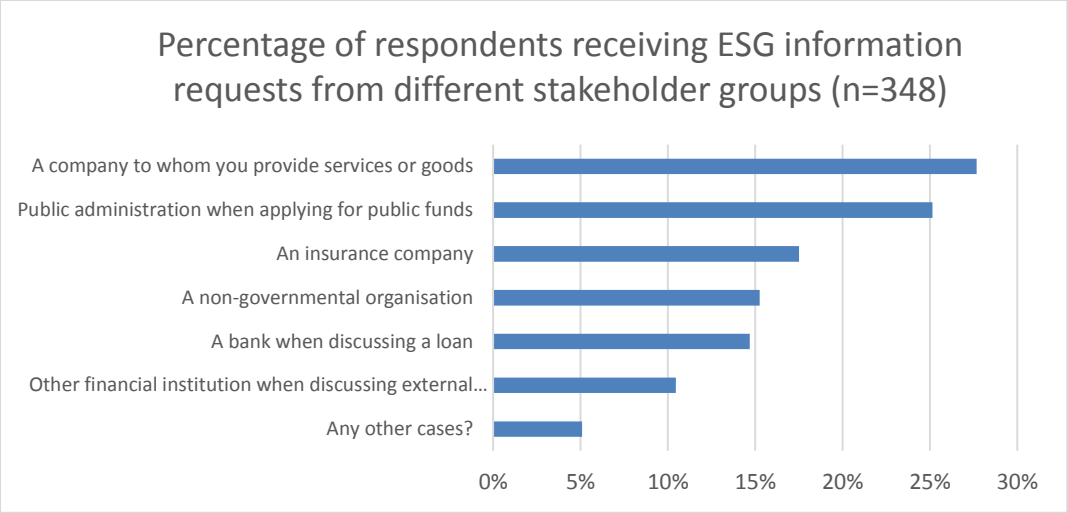


Figure 12

The respondents to the survey receive, on average, requests for ESG data from 1 stakeholder. As shown in Figure 13, 51% of the respondents (179 SMEs) do not receive any requests for ESG data from stakeholders.

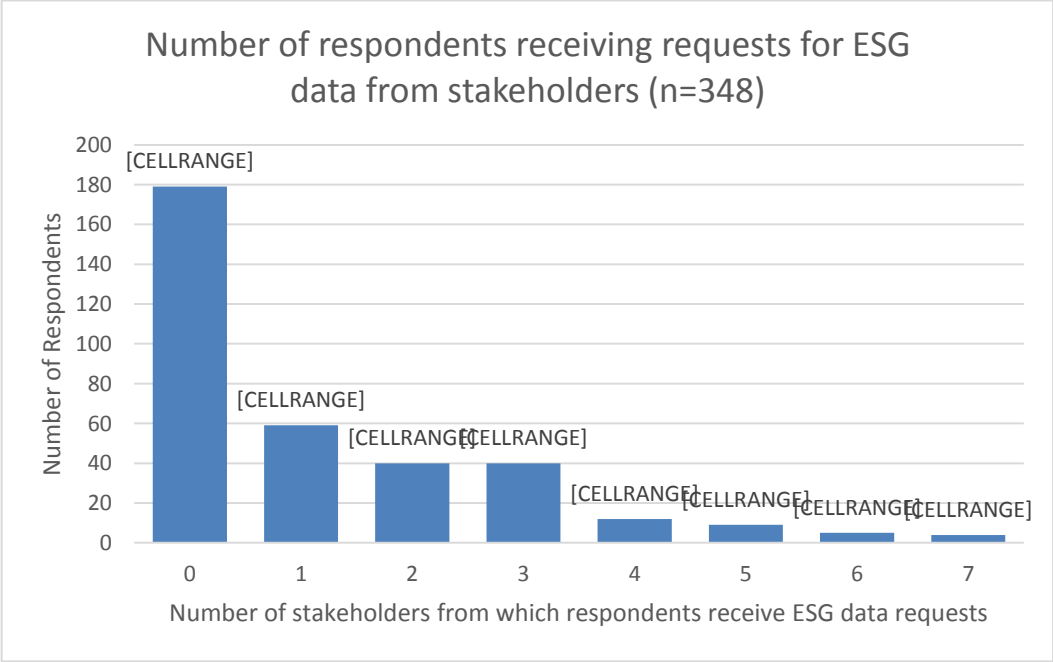


Figure 13

Similar to what was observed regarding the collection of ESG data, the size of an SME and the number of stakeholders requesting ESG data seem to be related. For instance, 80% of medium sized companies (Figure 14) receive requests to share ESG data; that percentage decreases to 45% for small sized companies (Figure 15) and 42% for micro sized companies (Figure 16). In

contrast, the average number of stakeholders who request ESG data from the SMEs does not change significantly according to the SMEs size. Table 3 illustrates an overview, by size, of the total number of respondent SMEs who receive requests to disclose ESG data and of the average number of stakeholders requesting such data.[111]

Company size	Percentage of respondents receiving at least one data request	Average number of stakeholders requesting ESG data
Micro	42%	1
Small	45%	1
Medium	80%	2

Table 3

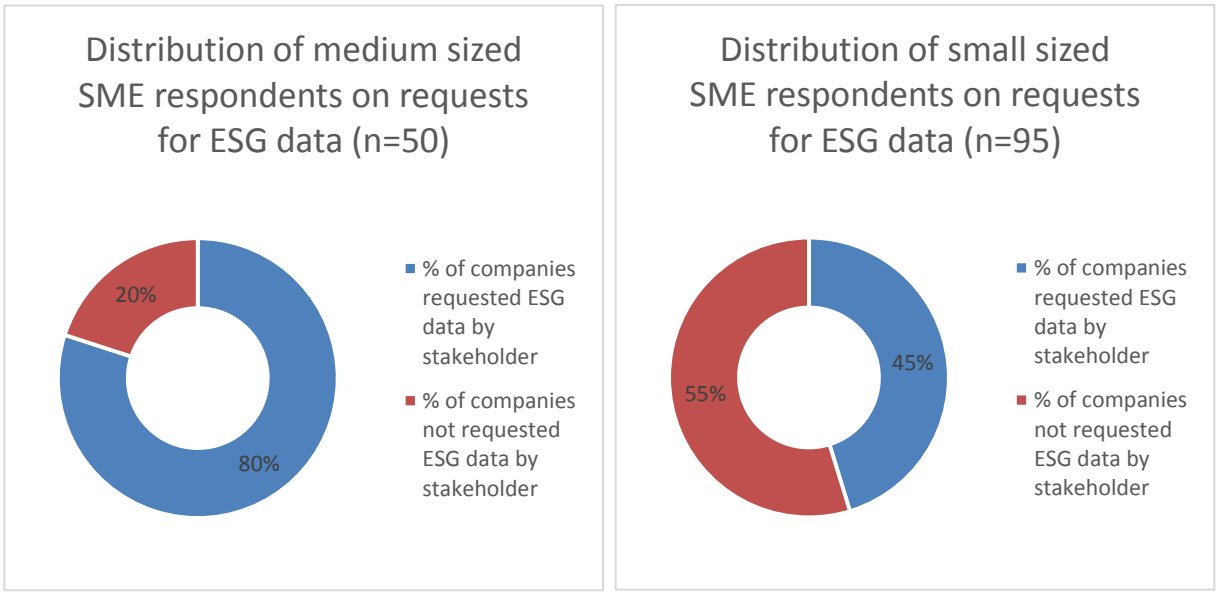


Figure 14

[111] The average is calculated considering all respondents to the survey, including those who do not receive requests from any stakeholders.

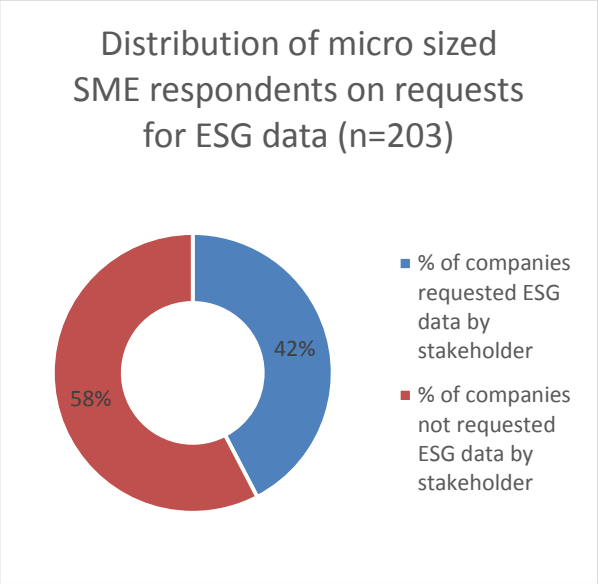


Figure 15

This section reviews the relation between SMEs who are part of the supply chain of large companies and the requests they receive from companies to whom they provide services or goods.

Regardless of their size, 43% (70 SMEs) of the respondents who are part of the supply chain of a large company indicate they receive requests to disclose ESG data from companies to which they supply goods or services. In comparison, only 15% (26 SMEs) of the respondents who are not part of the supply chain of a large company receive requests to disclose ESG data from companies that they supply. As it may be seen in Figure 18, medium SMEs in the supply chain of large companies are more likely to receive requests for ESG information from their customers. 76% of the medium sized respondents who are also part of a large company supply chain receive requests from their customers, compared to 36% and 33% for small and micro sized SMEs respectively.

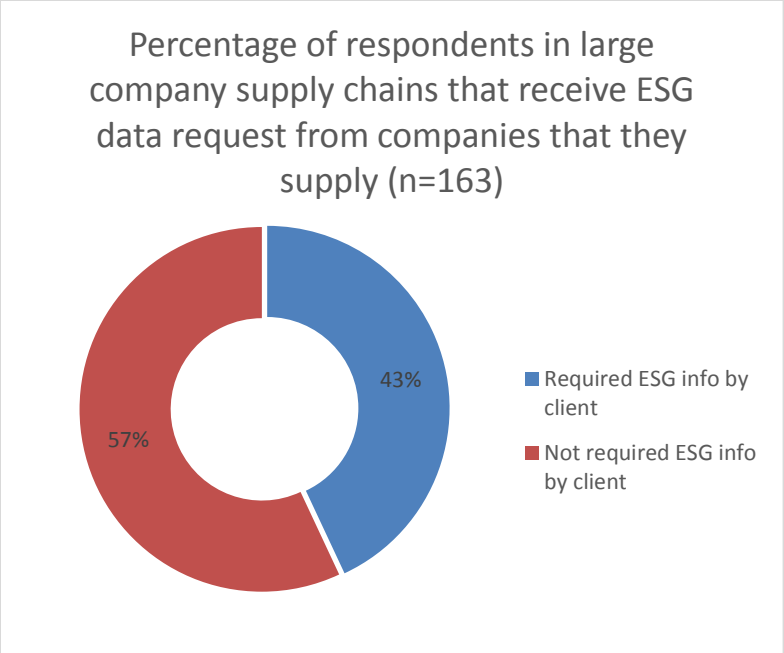


Figure 15

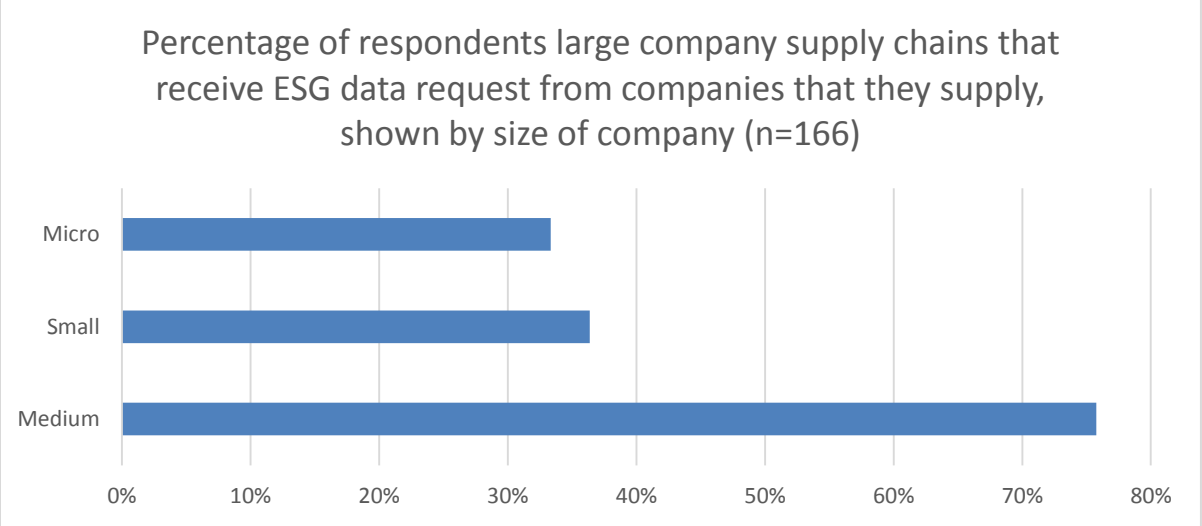


Figure 16

3.4 Time invested on ESG data processes

Respondents to the survey were asked about the estimated amount of time they spend in responding to ESG information requests or publishing such information about their operations.[112] 52% of the respondents to the survey (184) responded to this question. As observed in Figure 20, around 36% of those responding to the survey use between zero and 0.25 employee days per month for these tasks. 48% of the companies surveyed did not provide an answer because they do not publish ESG data and do not receive ESG data requests from stakeholders.

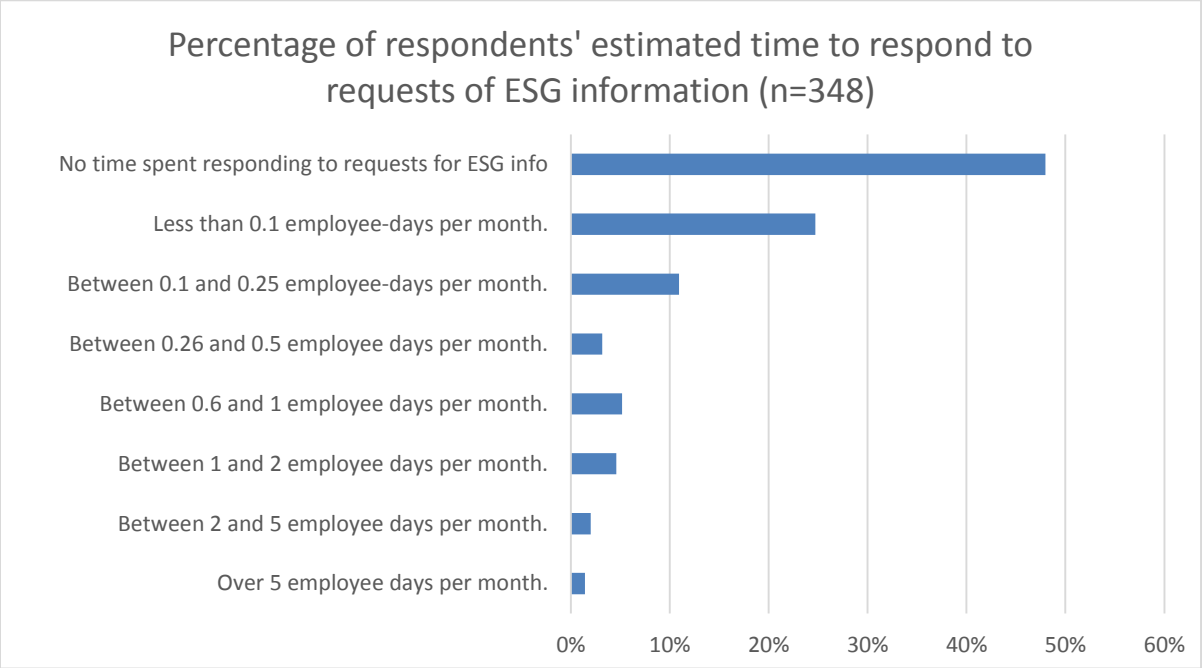


Figure 17

Figure 20 shows how the average number of issues on which ESG data is collected interacts with the monthly amount of time related to the ESG activities. It may be observed that when the number of issues on which data is collected increases, so does the amount of time used to respond to the requests.

[112] The questionnaire asked respondents that receive requests from stakeholders or that share information about operations (e.g. on the website), to include the estimated time spent by employees in collecting social and environmental information, as well in publishing it and preparing any necessary documents.

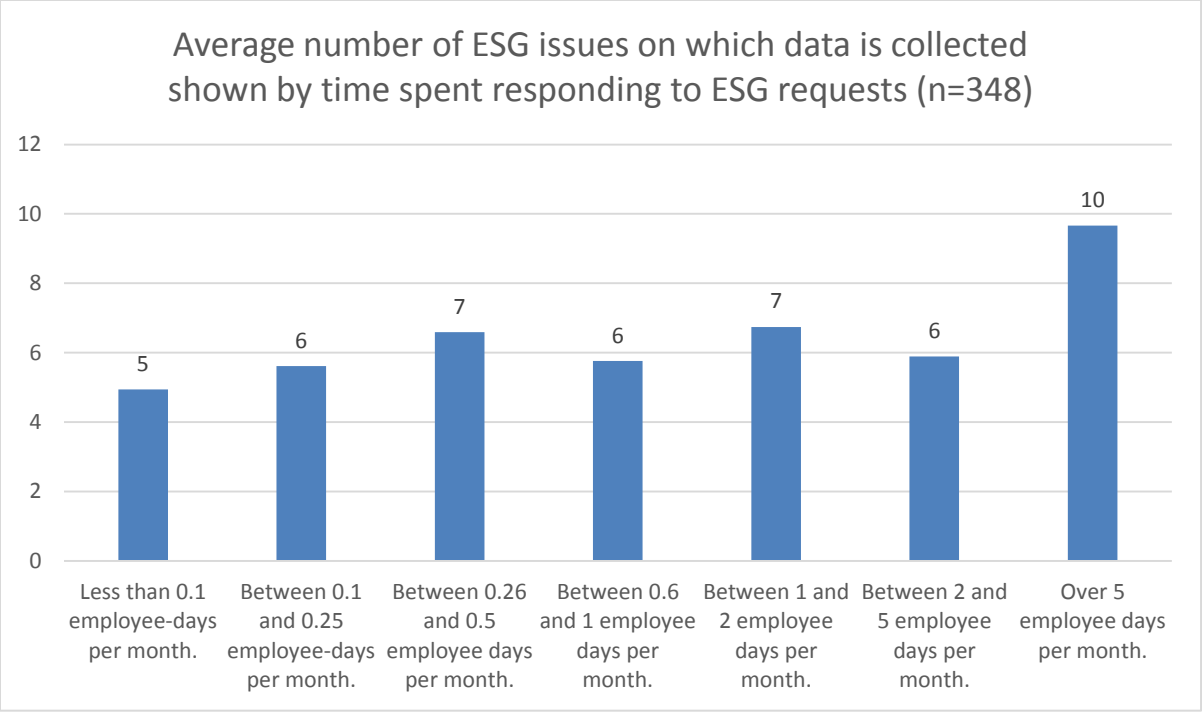


Figure 18

As part of the data collection process, some SMEs may ask their own business partners, especially suppliers, to disclose some ESG information. In general, most respondents to the survey do not ask their suppliers for ESG information (72%) and very few do request such information (16%).

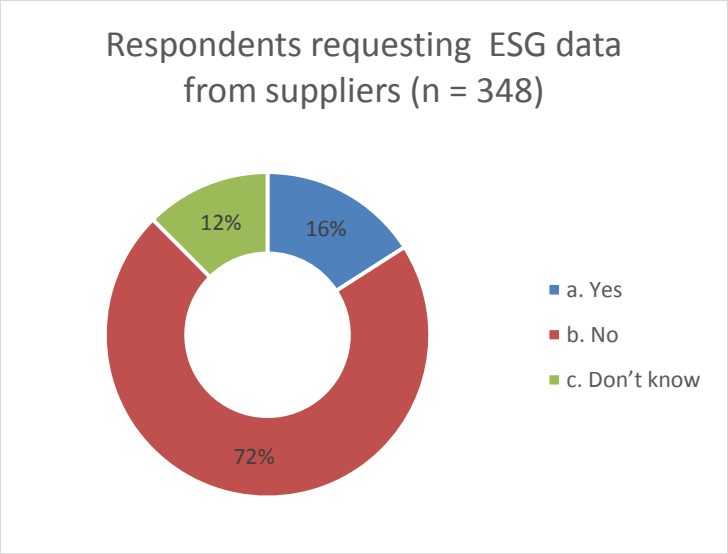


Figure 19

4. SMEs preference on development of a non-financial reporting standard for SMEs

Currently, SMEs and larger companies do not have a unique set of standards to follow. One of the questions in the survey is for SMEs to share their views on what would they would prefer regarding standards for reporting social and environmental information.

The results of the survey show most SMEs (68%) would welcome the development of a simplified standard[113] for SMEs to be used either in a voluntary basis (53%) or a mandatory basis (15%). 30% of the respondents state there is no need for a reporting standard for SMEs.

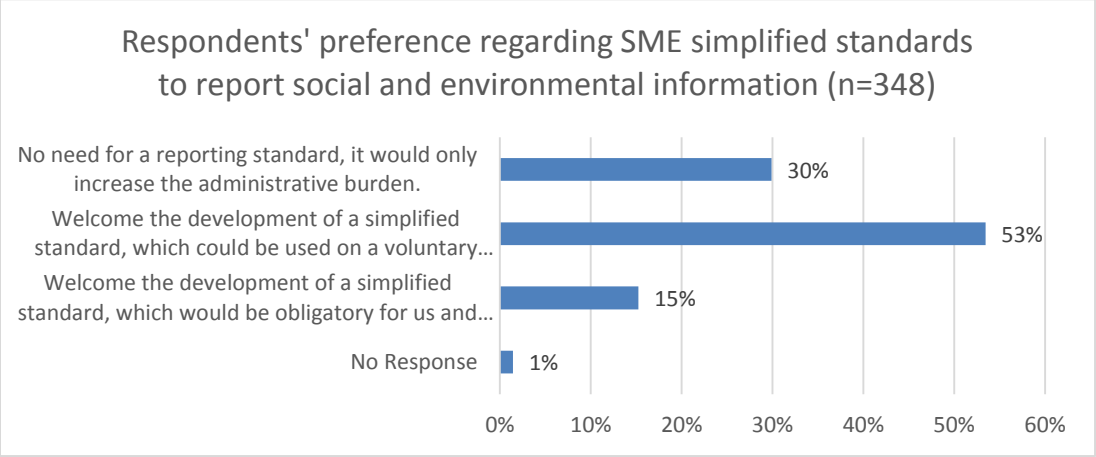


Figure 20

When looking at the respondents' size (Figure 24) it is observed that slightly more small and medium SMEs prefer either a voluntary or mandatory standard, compared to micro companies.

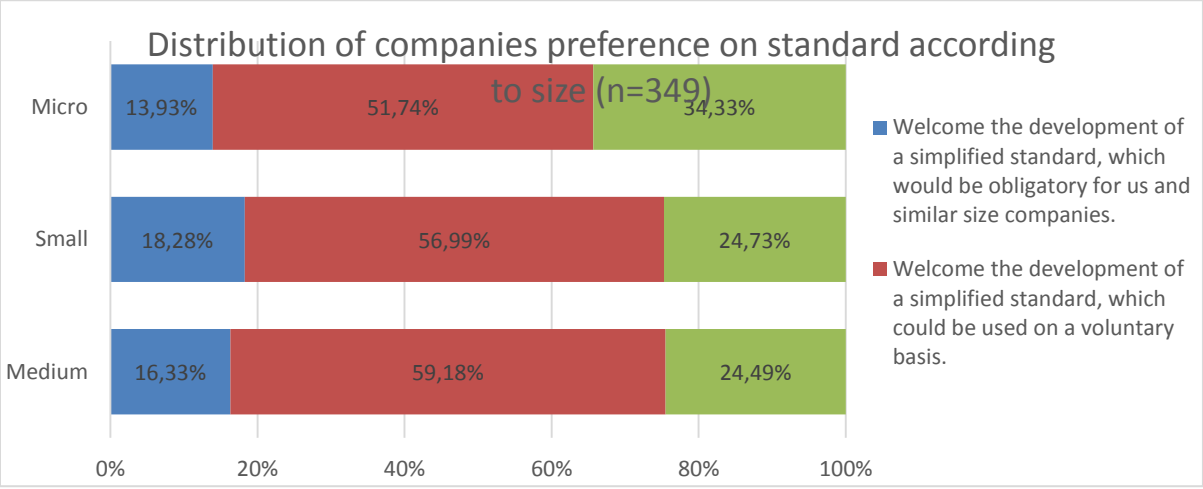


Figure 21

[113] A simplified standard for SMEs on how to report social and environmental information.

5. Methodology of Size Assessment

The size used (micro, small, and medium) in the charts of this document corresponds to the size of undertakings as described in Article 3 of the Accounting Directive (2013/34/EU)[114]. For this purpose, companies were assessed according to their responses to the following criteria:

i) the number of employees,

ii) net turnover,

iii) and balance sheet total.

Companies belong to a size category when at least two out of three of their responses to the criteria meet (or exceed) a given threshold (Examples 1 and 2). In some cases, the information provided by respondents is not sufficient to allocate them to a size category as per the Accounting Directive. Such organisations are deemed as "undetermined" (Example 3). See Table 4 for examples of such scenarios.

Scenario	No. Employees	Net Turnover	Balance sheet	Size
Example 1	Up to 10	Between 8 000 001 & 40 000 000 EUR	Between 4 000 001 & 20 000 000 EUR	Medium
Example 2	Between 11-50	Up to 700 000 EUR	Between 4 000 001 and 20 000 000 EUR	Small
Example 3	Between 51-250	No response	Up to 350 000 EUR	Undetermined

Table 4

[114] Accounting Directive (2013/34/EU) 1. […] define micro-undertakings as undertakings which on their balance sheet dates do not exceed the limits of at least two of the three following criteria: (a) balance sheet total: EUR 350 000; (b) net turnover: EUR 700 000; (c) average number of employees during the financial year: 10. 2. Small undertakings shall be undertakings which on their balance sheet dates do not exceed the limits of at least two of the three following criteria: (a) balance sheet total: EUR 4 000 000; (b) net turnover: EUR 8 000 000; (c) average number of employees during the financial year: 50. […] 3. Medium-sized undertakings shall be undertakings which are not micro-undertakings or small undertakings and which on their balance sheet dates do not exceed the limits of 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. […]. https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:02013L0034-20141211&from=EN

ANNEX 6: IMPLICATIONS OF THE COVID-19 PANDEMIC

Summary

The Covid-19 pandemic directly underlines the exposure of companies to non-financial risks. It has also lead to increased stakeholder attention to the impacts of companies, especially regarding workers and supply chains. The pandemic will therefore further accelerate the growth in demand for more and better non-financial information from companies. At the same time, the economic crisis generated by the pandemic makes it ever more important to avoid the imposition of unnecessary administrative costs on business.

Impact of Covid-19 on the problem definition

The Covid-19 pandemic directly underlines the exposure of companies to non-financial risks. This is especially the case of companies whose business models are dependent on the global movement of goods and persons. Companies can expect that investors and supervisors will now require significantly enhanced reporting about such risks. This change will materialise at the very least from the 2021 reporting cycles, and for many companies it is already a reality.

Some observers predict that the pandemic will in particular lead to a greater demand for social and worker-related information.[115] To date the investment community has tended to pay more attention to environmental information, especially climate-related information, and governance than to social information. It is notable that the European Investment Bank and the European Bank for Reconstruction and Development have published new guidelines regarding the sustainability risks of investments in the context the pandemic, and both have a strong emphasis on the social and worker-related issues, including workers in supply chains.[116]

A number of recent analyses have suggested that the pandemic will drive the growth of ESG investing. For example, a JP Morgan survey of investors found that 55% of them see the pandemic as a positive catalyst for ESG investing in the next three years, while only about a quarter (27%) expect a negative impact and 18% believe it will be neutral.[117] A study published by the European Capital Markets Institute finds that "companies integrating an ESG approach

[115] See for example Julie Moret Covid-19 has brought the 'S' in ESG back into focus published on the International Investment website July 2020: "The crisis has both intensified and highlighted a range of societal issues, such as growing inequality and the fragility of customers and employees, especially in certain segments of the economy, which have been left with little protection. […] The coronavirus pandemic has put human capital under the spotlight – issues such as employee contracts and rights have come to the forefront as investors and civil society scrutinise how businesses act during the crisis, including the way they treat their workers. The crisis has exposed the fragility of independent contractors within the gig economy and those on zero-hour contracts in sectors heavily affected by the crisis, such as entertainment and leisure."

[116] European Investment Bank Guidance note to EIB promoters On environmental and social performance in EIB-financed operations in response to the COVID-19 outbreak crisis; European Bank for Reconstruction and Development Sustainabilty and coronavirus webpage.

[117] JP Morgan *Why COVID-19 Could Prove to Be a Major Turning Point for ESG Investing* July 2020

recognised by investors and ESG funds have been more resilient in the crisis", and goes on to conclude that "investors' taste for ESG has not lessened during this crisis – quite the opposite, in fact."[118]

More generally, the pandemic may contribute to a greater awareness of the complex interactions between environmental degradation, social problems and the health of the economy.[119] One informed analyst has stated that "the pandemic and the health crisis now ravaging all continents has put the spotlight on vulnerabilities and our dependence on the natural environment. It drives home the message that markets do not operate in isolation, but instead are embedded in societies and the natural environment. This realization will fundamentally change our long-term risk perspective and the way we prepare for the looming climate crisis."[120]

If the pandemic indeed contributes to a further growth in ESG investing and to an acceleration of the paradigm shift towards a sustainable economy, then it will further accelerate the growth in demand for more and better non-financial information from companies on the part of the investors and other stakeholders.

Impact of Covid-19 on the policy options

The pandemic does not substantially alter the identification or definition of the available policy options. It does however influence the assessment of the costs and benefits of the policy options.

On the one hand, assuming that the pandemic increases the needs of users for better non-financial information, the disadvantages of non-action and the baseline scenario will increase. On the other hand, the economic crisis generated by the pandemic makes it ever more important to avoid the imposition of unnecessary administrative costs on business. In this respect, much will depend on the pace of economic recovery, since companies subject to any new reporting requirements under the revised NFRD would not have to dedicate resources to meeting those requirements until 2022 at the earliest.

[118] European Capital Markets Institute *ESG resilience during the Covid crisis: Is green the new gold?* July 2020

[119] There is some evidence that biodiversity loss and the damage to ecosystems may encourage more rapid evolutionary processes and diversification of diseases, as pathogens spread more easily to livestock and humans. See for example *Emerging Infectious Diseases of Wildlife-- Threats to Biodiversity and Human Health* Peter Daszak, Andrew A. Cunningham, Alex D. Hyatt Science 21 Jan 2000: Vol. 287, Issue 5452, pp. 443-449

[120] Covid-19 Is Accelerating ESG Investing And Corporate Sustainability Practices Georg Kell, founder of the UN Global Compact and Chair of asset manager Arabesque Partners.

ANNEX 7: DESCRIPTION OF THE NON-FINANCIAL REPORTING DIRECTIVE

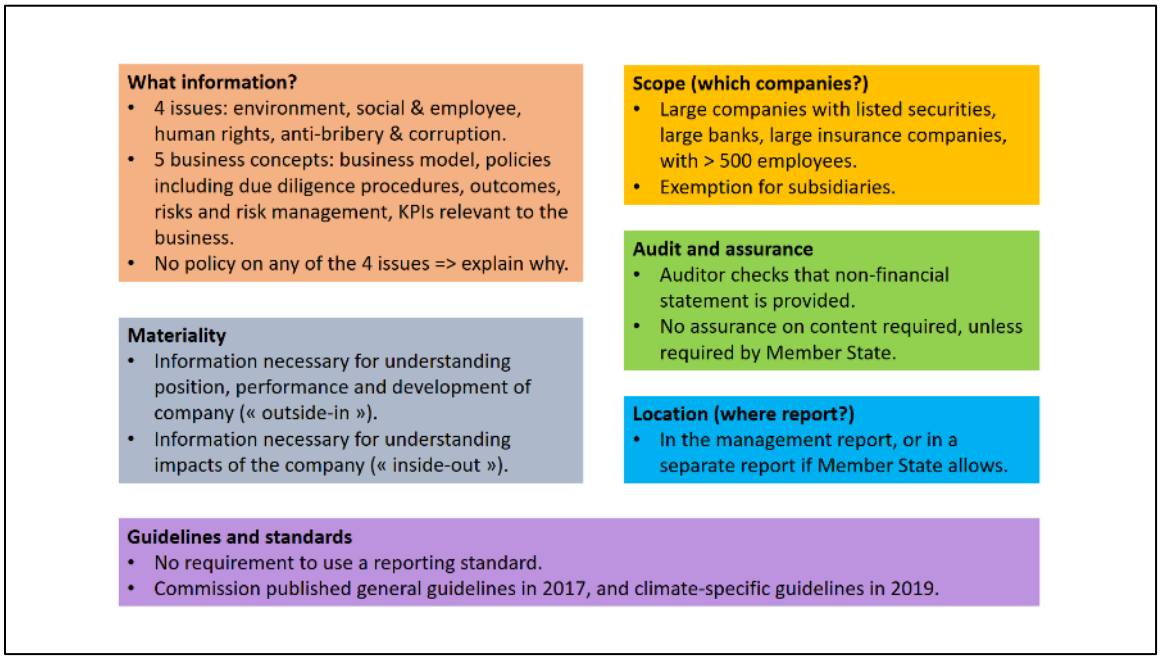
In 2003 the "Accounts Modernisation Directive" (Directive 2003/51/EC, second Accounting Directive) introduced a requirement on companies to include "information relating to environmental and employee matters" in their management reports, to the extent necessary for an understanding of the company's development, performance or position. Member States were able to exempt SMEs from this obligation.

Around the same time and in subsequent years, a number of Member States (including Denmark, France, Spain, Sweden and the UK) introduced non-financial reporting requirements at national level that went beyond the requirements of the Accounts Modernisation Directive.

In 2014 the EU agreed the Non-Financial Reporting Directive (Directive 2014/95/EU), which amended the Accounting Directive (Directive 2013/34/EU). The Non-Financial Reporting Directive (NFRD) imposed stronger non-financial reporting requirements on certain large companies.

Companies under the scope of the NFRD had to report according to its provisions for the first time in 2018, for information covering financial year 2017. Most companies have therefore now completed three reporting cycles under the NFRD.

The Non-Financial Reporting Directive at a glance



Guidelines accompanying the NFRD

As required by the NFRD, in 2017 the Commission published non-binding guidelines for companies under the scope of the Directive, to facilitate the reporting of relevant, useful and comparable non-financial information.[121] In 2019, as part of the Sustainable Finance Action Plan, the Commission published additional guidelines, specifically on reporting climate-related information.[122]

Scope (which companies)

The NFRD applies to large public interest entities with more than 500 employees, and to public interest entities that are parent companies of a large group with more than 500 employees.[123] In practice this means that it applies to large EU 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 the entity has more than 500 employees.[124] Likewise, it also applies to EU companies with securities listed in EU regulated markets, banks (whether listed or not) and insurance companies (whether listed or not) which are parents of large groups with more than 500 employees.[125]

The NFRD exempts the subsidiaries of parent companies from the reporting obligation, if the parent company itself reports the necessary information on a consolidated basis.

Taking account of how Member States have transposed the Directive, we estimate that approximately 11 700 companies are subject to the reporting requirements of the NFRD. Not taking account of national transposition, about 2 000 companies are under scope of the NFRD.

Location (where should the information be disclosed?)

The default location of the non-financial statement is in the management report, therefore as an integral part of the company's annual report. However, the NFRD allows Member States to

[121] Communication from the Commission — Guidelines on non-financial reporting (methodology for reporting non-financial information) C/2017/4234

[122] Communication from the Commission — Guidelines on non-financial reporting: Supplement on reporting climate-related information C/2019/4490

[123] Article 2 of the Accounting Directive defines "public interest entities" as being listed companies, banks, insurance companies, and other entities designed by Member States at national level because of their significant public relevance. It also applies to public interest entities that are parent companies of a large group with more than 500 employees.

[124] Article 3 of the Accounting Directive defines a "large undertaking" as an entity which on its balance sheet dates 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.

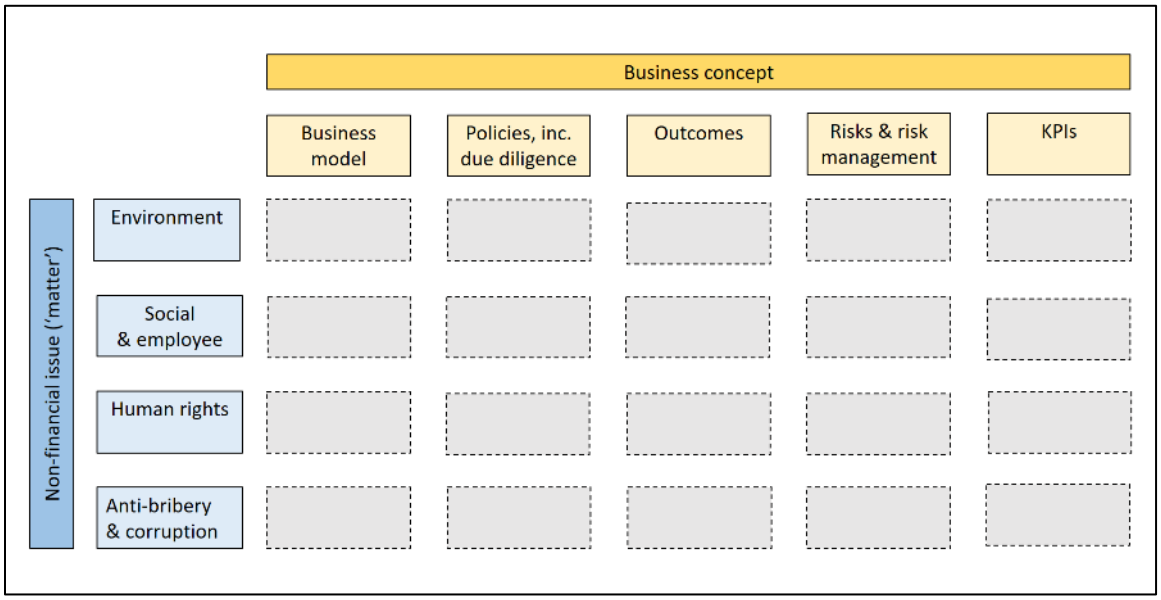
[125] Article 3 of the Accounting Directive defines a "large group" as a group consisting of parent and subsidiary undertakings to be included in a consolidation and which, on a consolidated basis, on the balance sheet date of the parent undertaking exceeds the limits of at least two of the three following 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.

allow companies to publish the necessary non-financial information in a separate report, and most Member States have used this option.

What information?

The NFRD identifies four non-financial 'matters': environment, social and employee matters, human rights, and anti-corruption and anti-bribery.[126] With regard to those four matters, the NFRD requires companies to disclose information about five business concepts: business model, policies (including due diligence processes implemented), the outcome of those policies, risks and risk management, and key performance indicators (KPIs) relevant to the business. The non-financial information that companies should disclose according to the NFRD can be visualised by cross-referencing the four non-financial issues with the five business concepts, as shown in the table below.

Graphic representation of non-financial information according to the Non-Financial Reporting Directive



If a company does not have a policy on one or more of the non-financial issues identified, it should explain why.

The reference to policies in the NFRD includes an obligation to disclose due diligence processes implemented by the company. Due diligence in this context refers to the process by which

companies identify, prevent, mitigate and account for how they address actual and potential adverse impacts in their own operations, their supply chain and other business relationships.[127]

The reference to risks specifically includes risks related to the company's business relationships. Business relationships include, but are not limited to, supply-chains. In practice, therefore, the NFRD requires companies to report relevant risks related to their supply-chains.

In the case of the financial sector, the concept of business relationships includes relationships with organisations financed by the financial sector company in question, and therefore extends to the social and environmental impacts of the activities financed.

Annex 8 provides a list of illustrative examples of the kind of information that companies could be expected to disclose under the NFRD, taken from the Commission's 2017 Guidelines on Non-Financial Reporting.

The NFRD specifies that the non-financial statement should include information on the environment, social and employee matters, human rights, and anti-corruption and anti-bribery, "*as a minimum*." In principle, therefore, companies should disclose information on other non-financial issues if they consider such information to be material (see explanation on materiality below). Information about intangible assets is an example of the kind of non-financial information that companies are not explicitly required to include in their non-financial statement. International Accounting Standard 38 defines an intangible asset as "an identifiable non-monetary asset without physical substance." Typical examples of intangible assets include intellectual property, software, customer retention, brand value and reputation, and human capital. Investments in intangible assets often do not qualify to appear in a company's financial accounts, and this is rarely compensated by adequate reporting on such assets in other parts of the annual report, including the non-financial statement.[128] Some information relating to intangible assets could coincide with the list of issues explicitly recognised in the NFRD. This is especially the case for employee matters, which will may have links with human capital as an intangible asset.[129] However, information about other intangible assets, such as customer retention, does not coincide with the list of non-financial issues explicitly recognised in the NFRD.

[127] Definition of due diligence from OECD Due Diligence Guidance for Responsible Business Conduct, 2018.

[128] Patrick de Cambourg provides a more detailed exploration of intangible assets as part of the broader concept of non-financial information in his report to the French Minister for the Economy and Finance published in May 2019: *Ensuring the relevance and reliability of non-financial corporate information: an ambition and a competitive advantage for a sustainable Europe*, Patrick de Cambourg, May 2019.

[129] For example, the Commission's 2017 guidelines suggest that companies consider disclosing their employee turnover, employee consultation processes and the hours of training per year per employee.

Materiality

A company under the scope of the NFRD is required to disclose information "to the extent necessary for an understanding of [its] development, performance, position and impact of its activity." The reference to "impact" represented a significant innovation compared to the Accounts Modernisation Directive. It introduced a double materiality perspective, whereby companies have to report information not only on how non-financial issues affect the company, but also regarding the impact of the company itself on society and the environment.[130]

The NFRD leaves very considerable flexibility to companies to judge what information is in fact necessary for an understanding of their development, performance, position and impacts. The Directive itself provides no further clarification, and few Member States have introduced further specifications when transposing the Directive. The guidelines issued by the Commission to accompany the Directive do nevertheless provide some non-binding guidance on what information to report.

Article 2 of the Accounting Directive, which the NFRD did not amend, defines "material" in relation to financial statements, with no reference to non-financial information: "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."

Provisions regarding reporting standards and frameworks

If companies use national, EU or international reporting frameworks to prepare their non-financial statement, then the NFRD requires them to specify which frameworks they have used. The NFRD does not, however, require the use of a reporting framework. The great majority of Member States have decided not to go beyond the minimum requirements of the NFRD in this regard. Spain is an example of a Member State that has gone beyond the minimum NFRD requirements: Spanish law requires companies to use a non-financial reporting standard (without specifying which), and to disclose key performance indicators that are consistent with the Global Reporting Initiative.

Audit and assurance

The NFRD requires the auditor to carry out an existence check: the auditor must verify that the company has provided a non-financial statement in the management report (or has published non-financial information in a separate report if the Member State allows that option). Some Member States (Italy, Spain and France) have introduced stronger assurance requirements than

[130] For a more in depth presentation of the double materiality perspective in the specific context of reporting climate-related information, see section 2.2 of the 2019 Commission guidelines on reporting climate-related information https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52019XC0620(01)

the existence check specified in the NFRD and require the verification of the content of the information reported by an independent assurance service provider.

Transposition

Annex 9 provides a complete overview of how Member States have transposed the NFRD. In general, most Member States have transposed most provisions by staying close to the original wording of the Directive. Only in exceptional cases have Member States further specified or strengthened the reporting requirements set out in the Directive.

ANNEX 8: EXAMPLES OF NON-FINANCIAL INFORMATION GIVEN IN THE COMMISSION'S 2017 GUIDELINES

The guidelines published by the Commission in 2017 contain examples of the kind of non-financial information that companies might report. The guidelines provide examples structured by:

- key reporting principle
- business concept
- non-financial issue

They also provide additional examples specifically relating to supply-chains and conflict.

1. Illustrative examples structured by key reporting principle

Key principle	Examples provided in 2017 guidelines
Disclose material information	A bank may consider that its own water consumption in offices and branches is not a material issue to be included in its management report. In contrast, the bank may assess that the social and environmental impacts of projects that it funds and its role in supporting the real economy of a city, a region or a country are material information. A company may consider that impacts through its upstream supply chain are relevant and material issues and report on them accordingly. Impacts may be direct or indirect. For example, a company producing mineral water may consider specific measures taken to protect the hydric resources it relies upon. A company having impacts on land use and ecosystem change (for example deforestation), directly or through its supply chain, may consider appropriate disclosures on the due diligence applied. A company which is involved in the supply chains of minerals from conflict-affected and high-risk areas may consider appropriate disclosures on the due diligence applied to ensure that it respects human rights and does not contribute to conflict.
Fair, balanced and understandable	A company disclosing certain KPIs may increase transparency by providing information on purpose and link to the company strategy; definitions and methodology; sources of information, assumptions and limitations; scope of the activities concerned; benchmarks; targets; trends; changes in methodologies (if any); and qualitative explanations of past and expected performance.

Comprehensive but concise	A company may summarise information, focus on material information, remove generic information, limit details, avoid elements that are no longer relevant, use cross-reference and signposting, etc.
Strategic and forward-looking	A company may disclose how it approaches a sustainable business strategy and how environmental, social and governance performance can help achieve its business goals. It could also disclose targets relating to KPIs reported, and explain the uncertainties and factors which may underpin forward-looking information and future prospects. A company may disclose relevant information based on the expected impact of science-based climate change scenarios on its strategies and activities. Alternatively, it may disclose targets for reducing the number of occupational accidents or diseases.
Stakeholder orientated	A company may disclose material information on its engagement with stakeholders, and explain how this influences its decisions, performance and the impact of its activities.
Consistent and coherent	A company may identify relationships and linkages between its business model and corruption and bribery aspects.

2. Illustrative examples structured by business concepts

Business concept	**Examples provided in 2017 guidelines**
Business model	A company may consider specific disclosures explaining: • the main products it makes, and how they meet the needs of consumers/customers; • how these products are made, and what makes its production approach competitive and sustainable; • the characteristics of the market where it operates, and how it may evolve.
Policies	A company may consider disclosing information on who in its organisation and governance structure is responsible for setting, implementing and monitoring a specific policy, for instance, on climate-related matters. It may also describe the role and responsibility of the board/supervisory board regarding environmental, social and human rights policies.

	A company may consider disclosures on its policies aiming at avoiding the use of hazardous chemicals, substances of very high concern or biocides in its products, operations and supply chain. It may also disclose its policies on research, development and use of safe alternatives. Companies may explain how they assess the quality, safety and environmental impact of the chemicals that they use, and how they meet legal requirements on chemical safety (e.g. REACH, CLP -classification, labelling and packaging). A company may disclose relevant information on how it identifies, assesses, and manages climate-related risks and/or natural capital A company may consider disclosing the following health and safety information: • workplace's policies; • contractual obligations negotiated with suppliers and sub-contractors; • resources allocated to risk management, information, training, monitoring, auditing, cooperation with local authorities and social partners.
Outcomes	A company may consider including specific disclosures explaining: • actual carbon emissions, carbon intensity; • use of hazardous chemicals or biocides; • natural capital impacts and dependencies; • comparison v targets, developments over time; • mitigating effects of policies implemented; • plans to reduce carbon emissions.
Risk & risk management	A company may consider including specific disclosures on: • malfunctioning products with possible effects on consumers' safety; • policies implemented to address the issue; • remediation measures addressing the needs of consumers already affected by those products. A company may consider disclosing material information on climate-related impacts on its operations and strategy, taking into account its specific circumstances and including appropriate assessments of likelihood and use of scenario analyses A company may consider disclosing material information on risks of harm related to human rights, labour and environmental protection in its supply and subcontracting chain, and on how the company manages and

	mitigates potential negative impacts.
KPIs	A company may consider appropriate disclosures on metrics and targets used to assess and manage relevant environmental and climate-related matters.

3. Illustrative examples structured by non-financial issue (or "matter")

Non-financial issue (or 'matter')	**Examples provided in 2017 guidelines**
Environment	A company may disclosure material information based on methodologies specified in specific legislation. For instance, the annexes to Commission Recommendation (EU) No 179/2013 include the Product Environmental Footprint and Organisation Environmental Footprint methods. These are life cycle assessment methods that enable companies to identify for each product or an entire organisation: (i) the most relevant impacts; and (ii) their contributing processes and emissions along the supply chain. The environmental impacts may be reported separately or as a single aggregated score. A company may consider KPIs such as: • energy performance and improvements in energy performance; • energy consumption from non-renewable sources and energy intensity; • greenhouse gas emissions in metric tonnes of CO2 equivalent and greenhouse gas intensity; • emissions of other pollutants (measured in absolute value and as intensity); • extraction of natural resources; • impacts and dependences on natural capital and biodiversity; • waste management (e.g. recycling rates).
Social & employee	A company may consider disclosing KPIs based on aspects such as: • gender diversity and other aspects of diversity; • employees entitled to parental leave, by gender; • workers who participate in activities with a high risk of specific accidents or diseases; • the number of occupational accidents, types of injury or occupational diseases; • employee turnover; • the ratio of employees working under temporary contracts, by gender;

	• average hours of training per year per employee, by gender; • employee consultation processes; • number of persons with disabilities employed.
Human rights	A company may consider disclosing material information and KPIs on: • occurrences of severe impacts on human rights relating to its activities or decisions; • the process for receiving and addressing complaints, and mitigating and providing remedies to human rights violations; • operations and suppliers at significant risk of human rights violations; • processes and measures for preventing trafficking in human beings for all forms of exploitation, forced or compulsory labour and child labour, precarious work, and unsafe working conditions, in particular as regards geographic areas at higher risk of exposure to abuse; • how accessible their facilities, documents and websites are to people with disabilities; • respect for freedom of association; • engagement with relevant stakeholders.
Anti-bribery & corruption	A company may consider disclosing material information and KPIs relating to aspects such as: • anti-corruption policies, procedures and standards; • criteria used in corruption-related risk assessments; • internal control processes and resources allocated to preventing corruption and bribery; • employees having received appropriate training; • use of whistleblowing mechanisms; • the number of pending or completed legal actions on anti-competitive behaviour.

4. Illustrative examples for additional issues (supply chains and conflict minerals)

Additional issue	**Examples provided in Non-Binding Guidelines**
Supply-chains	A company may consider disclosing material information and KPIs relating to aspects such as monitoring suppliers on: • labour practices, including child labour and forced labour, precarious work, wages, unsafe working conditions (including building safety, protective equipment, workers' health);

	• trafficking in human beings and other human rights matters; • greenhouse gas emissions and other types of water and environmental pollution; • deforestation and other biodiversity-related risks; • and monitoring the company's impact on suppliers, for instance, its payment terms and average payment periods.
Conflict minerals	Specific KPIs include: • the proportion of direct relevant suppliers having adopted and implemented a conflict minerals due diligence policy consistent with the OECD Due Diligence Guidance; • the proportion of responsibly-sourced tin, tantalum, tungsten or gold originating in conflict-affected and high-risk areas; • and the proportion of relevant customers contractually requiring conflict minerals due diligence information under the OECD Due Diligence Guidance.

ANNEX 9: OVERVIEW OF TRANSPOSITION OF THE NON-FINANCIAL REPORTING DIRECTIVE BY MEMBER STATES

Member State	Scope PIE (AD): undertakings listed in EU regulated markets, credit institutions, insurance undertakings. Large: two out of three criteria, 20m BS / 40m turnover / 250 employees.	Allowed separte report	Where should information be published?	Audit / assurance	Reporting against international standards for non-financial reporting
Austria	1. PIE (AD). 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report	Statutory auditor - Declare that the (consolidated) non-financial statement (or separate report) has been provided. Independent assurance: NO	Not required
Belgium	1. PIE (AD). Plus: settlment organisations 2. Size threshold: one of the two criteria: net turnover: over EUR 34 million; or balance sheet total: over EUR 17 million. 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report	Statutory auditor - Declare that the (consolidated) non-financial statement (or separate report) has been provided. - Declare whether the management report is consistent with the financial statements and whether it has been drawn up in accordace with the legal provisions. I statement. Independent assurance: NO	Required
Bulgaria	1. PIE (AD). Plus: pension funds and pension fund managers, investment firms, collective investment schemes, the national railways and all its subsidiaries, financial institutions under Credit Institutions Law, electricity and heat providers, natural gas providers, water and sewage companies. 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website within six months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Check that the (consolidated) non-financial statement (or separate report) has been provided. - In theory, the auditor has an obligation to check compliance with the legal requirements. Independent assurance: NO	Not required
Croatia	1. PIE (AD). Plus: UCITS, AIF, pension undertakings, factor companies, MTP operators, Central depositary clearing companies, operators of central register, settlement system operators, investors protection fund operators, companies of strategic interest for the Republic of Croatia. 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website within six months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Check that the (consolidated) non-financial statement (or separate report) has been provided. Independent assurance: NO	Not required
Cyprus	1. PIE (AD) 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website within six months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Checks "the submission" of the (consolidated) non-financial statement (or separate report). (only check? But ARC said: also check whther it has been prepared in comliance with legal requirements) Independent assurance: NO	Not required

Member State	Scope **PIE (AD): undertakings listed in EU regulated markets, credit institutions, insurance undertakings.** **Large: two out of three criteria, 20m BS / 40m turnover / 250 employees.**	Allowed separate report	Where should information be published?	Audit / assurance	Reporting against international standards for non-financial reporting
Czech Republic	1. PIE (AD). Plus: pension companies and health insurance companies 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website within six months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Declare that the (consolidated) non-financial statement (or separate report) has been provided. - If included in management report, in theory, auditor's opinion on whether the management report is consistent with the financial statements and whether it has been drawn up in accordance with the legal provisions, also extends to the non-financial statement. Independent assurance: NO	Not required
Denmark	1. Financial PIEs 2. Large 3. Employees: above 500 + All non-financial PIEs + Large non-financial undertakings	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website at the same time the management report is published, and referred to in the (consolidated) management report. Available for at least 5 years on the internet address. If the internet address is changed during the period, a direct referral from the original internet address to the new internet address should be provided.	Statutory auditor - Auditor's opinion on whether the management report is consistent with the financial statements and whether it has been drawn up in accordance with the legal provisions. - If the undertaking chooses to comply with the NFRD via another report after an international standard, the auditor must confirm that the company can use this report to comply with the NFRD, and give an opinion on whether the non-financial statement has been drawn up in accordance with the legal requirements. Independent assurance: NO	Not required
Estonia	1. PIE (AD) 2. Large 3. Employees: above 500		- (Consolidated) Management report	Statutory auditor - In theory, as part of the auditor's obligation to audit the compliance of financial and other information disclosed with the financial statements. Independent assurance: NO	Not required
Finland	1. PIE (AD) 2. Large 3. Employees: over 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website within six months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Check that the (consolidated) non-financial statement (or separate report) has been provided. - If included in management report, in theory, auditor's opinion on whether the management report is consistent with the financial statements and whether it has been drawn up in accordance with the legal provisions, also extends to the non-financial statement. If published in separate report, auditor's opinion on whether it is consistent with the financial statements. Independent assurance: NO	Not required

Member State	Scope **PIE (AD): undertakings listed in EU regulated markets, credit institutions, insurance undertakings.** **Large: two out of three criteria, 20m BS / 40m turnover / 250 employees.**	Allowed separate report	Where should information be published?	Audit / assurance	Reporting against international standards for non-financial reporting
France	1. Listed 2. Large 3. Employees: above 500 + 1. Non-listed 2. Size threshold: one of the two criteria: net turnover over EUR 100 million; balance sheet total over EUR 100 million. 3. Employees: above 500	NO	- (Consolidated) Management report	Statutory auditor - Declare that the (consolidated) non-financial statement has been provided Independent assurance: **YES when EUR 100m Balance Sheet / EUR 100m Turnover and employees above 500** (by an independent third party, can be auditors if belong to this group of accreditted by the French Accreditation Committee COFRAC). Some issues limited, some in more detail.	Not required
Germany	1. PIE (AD) 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website within **four** months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Declare that the (consolidated) non-financial statement (or separate report) has been provided. Independent assurance: NO	Not required. There is a non-financial reporting standard in Germany for group management reports: 'GAS 20 - German Accounting Standard - Group Management Report'.
Greece	1. PIE (AD) 2. Large 3. Employees: above 500	NO	- (Consolidated) Management report	Statutory auditor - Declare that the (consolidated) non-financial statement has been provided - In theory, give an opinion on non-financial statement as part of management report. Independent assurance: NO	Not required
Hungary	1. PIE (AD) 2. Size threshold: two of the three criteria- a) the balance sheet total is HUF 6.000 million (ca. EUR 16,5 million); b) annual net sales of HUF 12.000 million (ca. EUR 33 million); c) the average number of employees during the business year is 250) 2. Employees: above 500	NO	- (Consolidated) Annual report.	Statutory auditor - Declare that the (consolidated) non-financial statement has been provided - In theory, give an opinion on non-financial statement as part of management report. Independent assurance: NO	Not required. Not transposed.
Ireland	1. PIE (AD) 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website within six months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Declare that the (consolidated) non-financial statement (or separate report) has been provided. Independent assurance: NO	Not required

Member State	Scope **PIE (AD): undertakings listed in EU regulated markets, credit institutions, insurance undertakings.** **Large: two out of three criteria, 20m BS / 40m turnover / 250 employees.**	Allowed separate report	Where should information be published?	Audit / assurance	Reporting against international standards for non-financial reporting
Italy	1. PIE (AD) 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report	Statutory auditor - Check that the (consolidated) non-financial statement (or separate report) has been provided Independent assurance YES (has to be a certified auditor, statutory or not), check compliance of information reported with legal requirements	Not required
Latvia	1. PIE (AD) 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report	Statutory auditor - Check that the (consolidated) non-financial statement (or separate report) has been provided - If included in management report, in theory, auditor's view on whether the management report is consistent with the financial statements and whether it has been drawn up in accordance with the legal provisions, also extends to the non-financial statement. Independent assurance: NO	Not required
Lithuania	1. PIE (AD). Plus: brokerage firm, collective investment undertaking, pension fund, occupational pension fund, management undertaking of collective investment undertakings or (occupational) pension funds, public or private limited liability companies which are owned by the State and/or a municipality, Lithuanian Central Securities Depository and operator of regulated market, potable water supplier and wastewater manager, surface wastewater manager, energy company whose service prices are regulated by the state. 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Making it available on the undertaking's website within **three** months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Check that the (consolidated) non-financial statement (or separate report) has been provided - In theory, give an opinion on non-financial statement as part of management report. Independent assurance: NO	Not required
Luxembourg	1. PIE (AD) 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website within six months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Check that the (consolidated) non-financial statement (or separate report) has been provided Independent assurance: NO	Not required
Malta	1. PIE (AD) 2. Large 3. Employees: above 500	NO	- (Consolidated) Management report	Statutory auditor - Check that the (consolidated) non-financial statement has been provided Independent assurance: NO	Not required

Member State	Scope **PIE (AD): undertakings listed in EU regulated markets, credit institutions, insurance undertakings.** **Large: two out of three criteria, 20m BS / 40m turnover / 250 employees.**	Allowed separte report	Where should information be published?	Audit / assurance	Reporting against international standards for non-financial reporting
Netherlands	1. PIE (AD). Plus: central credit institutions 2. Large 3. Employees: above 500	NO	- (Consolidated) Management report	Statutory auditor - Opinion on whether the (consolidated) non-financial statement has been drawn up in accordace with the legal requirements and whether it is consistent with the financial statements. Independent assurance: NO	Not required
Poland	1. PIE (AD). Plus: pension funds, national payment institutions, electronic money institutions, entities intending or pending for admission to one of the EU regulated markets, certain alternative investment companies, certain entities conducting brokerage activities, entities listed on an alternative market 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Making it available on the undertaking's website within six months of the balance sheet date, and referred to in the (consolidated) management report. . In case of listed entities the separate report is a mandatory part of the Annual Financial Report which has to be published on the entity's website within 4 months of the balance sheet date (and filed within the Polish Financial Supervision Authority).	Statutory auditor - Check that the (consolidated) non-financial statement (or separate report) has been provided Independent assurance: NO	Not required. A national non-mandatory standard on non-financial reporting developed and published by the end of 2017 by the Polish Association of Reporting Standards (FSR) and the Polish Association of Issuers (SEG) is available in Poland: Standard Informacji Niefinansowych – SIN.
Portugal	1. PIE (AD). Plus: investment companies, collective investment schemes, venture capital companies, venture capital funds, securities investment companies and specialized securities investment funds, credit securitization companies and credit securitization funds, pension funds, holding companies in the field of insurances and mixed-activity insurance holding companies if majority of voting rights in credit institutions, public undertakings with certain size thresholds. 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website within six months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Check that the (consolidated) non-financial statement (or separate report) has been provided Independent assurance: NO	Not required
Romania	Financial years 2017 and 2018 (reporting years 2018 and 2019): 1. PIE (AD). Plus: national/state owned/companies, companies with full or majority state capital, self-managed public company, non-bank financial institutions, payment institutions and e-money institutions, privately managed pension funds, financial investment services companies 2. Employees : above 500 Financial year 2019 (reporting year 2020): All companies with above 500 employees	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website within six months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Check that the (consolidated) non-financial statement (or separate report) has been provided. Independent assurance: NO	Not required

Member State	Scope PIE (AD): undertakings listed in EU regulated markets, credit institutions, insurance undertakings. Large: two out of three criteria, 20m BS / 40m turnover / 250 employees.	Allowed separate report	Where should information be published?	Audit / assurance	Reporting against international standards for non-financial reporting
Slovakia	1. PIE (AD). Plus: Export-import bank, health insurance company, management company, branch of a foreign management company, a pension fund management company, supplementary pension insurance company, stock exchange, Central securities depository, securities dealers, payment institutions, electronic money institution, collective investment unit, pension funds, subsidiaries of foreign financial institutions and very large entities above certain thresholds that prepare their financial statements in accordance with IFRS/EU. 2. Employees: above 500	NO	- (Consolidated) Management report	Statutory auditor - Declare that the (consolidated) non-financial statement has been provided Independent assurance: NO	Not required
Slovenia	1. PIE (AD) 2. Large 3. Employees: above 500	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website within six months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Check that the (consolidated) non-financial statement (or separate report) has been provided Independent assurance: NO	Not required
Spain	1. PIE (AD). Plus: the concept of PIE is extended in Spain- to which companies? 2. Employees: above 500 + 1. All companies 2. Large 3. Employees: above 500 Reporting year 2021: In both cases, employee threshold lowered to 250 for consolidated reporting, SMEs excluded.	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report	Statutory auditor - Declare that the (consolidated) non-financial statement (or separate report) has been provided Independent assurance: Provided by an independent assurance service provider (possible for statutory auditor)	Required. KPIs especially recommended to be consistent with the COM guidelines and the Global Reporting Initiative.
Sweden	All Large companies	YES	- (Consolidated) Management report; or - Separate report: . Published together with the (consolidated) management report; or . Making it available on the undertaking's website within six months of the balance sheet date, and referred to in the (consolidated) management report.	Statutory auditor - Declare that the (consolidated) non-financial statement (or separate report) has been provided Independent assurance: NO	Not required

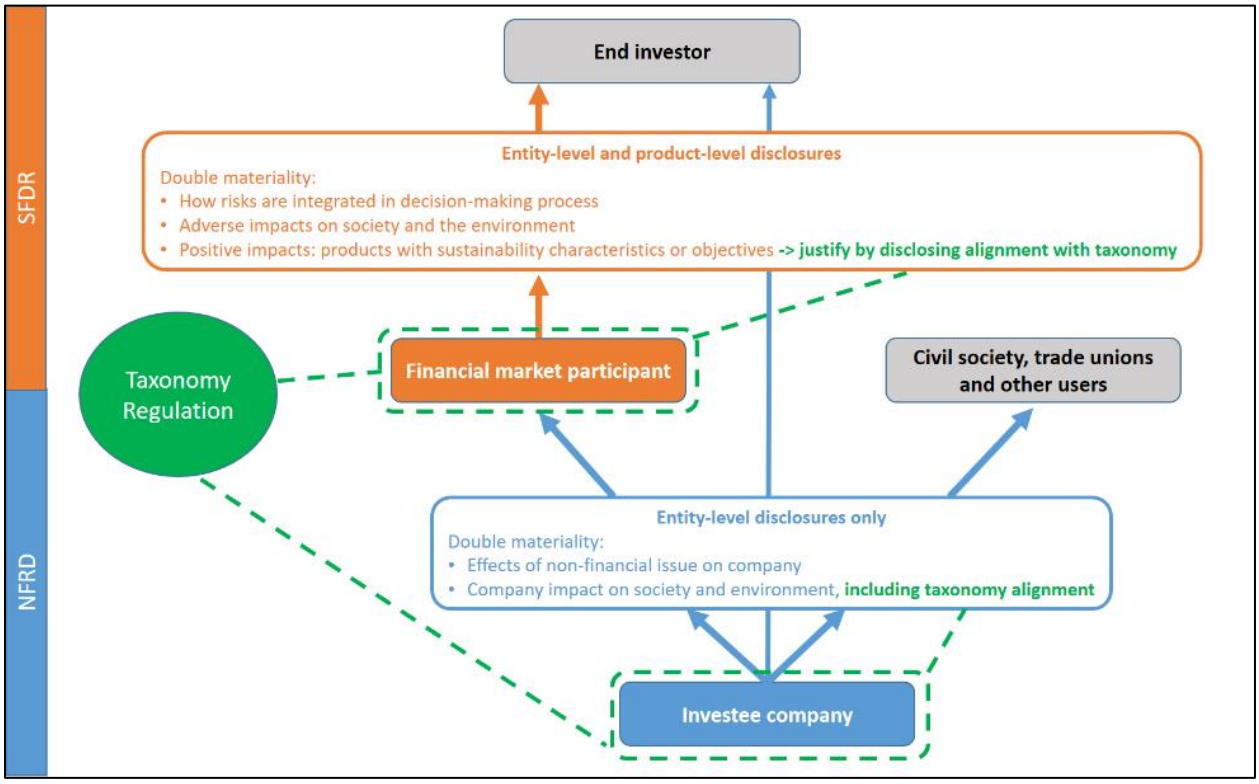
ANNEX 10: Relevant EU legislation and policy initiatives

This annex describes the most relevant existing and upcoming EU legislation and policy initiatives, and how they interact with the Non-Financial Reporting Directive. It is divided into two parts: part A addresses the interaction between the NFRD and other legislation and initiatives in the field of sustainable finance, while part B looks at interactions beyond sustainable finance.

A. Interaction between the NFRD and other legislation and initiatives in the field of sustainable finance

The Sustainable Finance Disclosure Regulation and the Taxonomy Regulation, together with the NFRD, are the central elements of the sustainability reporting regime that underpins the EU's Sustainable Finance Strategy. The figure below represents the interactions between these pieces of legislation.

Interaction between NFRD, SFDR and Taxonomy Regulation



The NFRD (represented in blue in the figure) governs reporting by companies to a variety of stakeholders, including financial market participants and end investors. As shown in the graphic sometimes the flow of non-financial information will be directly from the investee company to

the end investor. More often, however, the flow of information will be from the investee company to a financial market participant (including assets managers and financial advisers), and then from the financial market participant to the end investor.

The Sustainable Finance Disclosure Regulation (SFDR, represented in orange in the figure) governs how financial market participants should disclose sustainability information towards end investors and asset owners.

The Taxonomy Regulation (represented in green in the figure) creates a classification system of sustainable economic activities. It requires companies under the scope of the NFRD to disclose the extent to which their activities are considered environmentally sustainable according to the taxonomy. Financial market participants subject to the SFDR must also disclose the extent to which financial products marketed as sustainable are aligned with the taxonomy.

Consistency and coherence

Financial market participants will require information from investee companies in order to meet their disclosure requirements under the SFDR. Since the NFRD governs disclosures by investee companies, there is an obvious case for ensuring the consistency of the disclosure requirements between the NFRD and the SFDR. The goal is to create a consistent and coherent flow of sustainability-related information through the financial value chain.

Respondents to the open public consultation carried out in preparation for this initiative strongly endorsed the need for better alignment between different pieces of legislation on sustainability-related disclosures. 79% of financial sector respondents believed that such alignment was necessary, while only 3% of respondents believed that the alignment between the different pieces of legislation currently works well.

If reporting standards were to be developed as described in section 5.2.1 of this impact assessment, then those standards would be the vehicle for ensuring that investee companies report the information that financial market participants need to meet their own disclosure requirements under the SFDR. The revised NFRD should specify that this is as one of the necessary conditions for the adoption of non-financial reporting standards into EU law.

The SFDR disclosure requirements regarding adverse sustainability impacts will be specified in a Regulatory Technical Standard that the European Supervisory Authorities are currently developing. Consistency and alignment between that RTS and any possible standards developed under the NFRD will be especially important. The final version of the RTS will be available in the first half of 2021, which means that any organisation working on the development of European non-financial reporting standards will be in a position to ensure that such standards

fully cover the information that financial market participants need in order to comply with the RTS.

Financial market participants under the SFDR and investee companies under the NFRD are both required to disclose the extent to which their products or activities respectively are sustainable as defined by the taxonomy. The taxonomy therefore provides a common reference point that supports alignment between the SFDR and the NFRD. In response to the open consultation, a significant majority of respondents (69%) said that the legal provisions related to reporting on environmental matters should be structured according to the six objectives of the Taxonomy Regulation. The proportion of financial sector respondents who held this view as even higher (81%).

The precise content and methodology of the taxonomy-related disclosures of companies subject to the NFRD will be specified in a Delegated Act of the Taxonomy Regulation that the Commission should adopt by mid-2021. This Delegated Act will therefore also be available in good time for it to be considered appropriately in potential non-financial reporting standards that might be developed under the NFRD.

The taxonomy sets performance thresholds (referred to as 'technical screening criteria') for economic activities which: (1) make a substantive contribution to one of six environmental objectives; (2) do no significant harm (DNSH) to the other five environmental objectives; and (3) meet minimum safeguards (e.g., OECD Guidelines on Multinational Enterprises and the UN Guiding Principles on Business and Human Rights). These performance thresholds should be taken into account in any potential non-financial reporting standards developed under the NFRD, with the aim of achieving as much consistency as possible and reducing unnecessary burden on companies. The revised NFRD should specify that this is as one of the necessary conditions for the adoption of non-financial reporting standards into EU law.

The performance thresholds regarding minimum safeguards are defined in the Taxonomy Regulation itself, and are therefore already known. The performance thresholds regarding substantial contribution and DNSH are defined for two environmental objectives (climate mitigation and climate adaption) in a Commission Delegated Regulation [Publication Office: please fill in number of Regulation as per footnote].[131] They are therefore already known and can be taken into account during any standard-setting process under the NFRD.

[131] Commission Delegated Regulation (EU) …/… of XXX supplementing Regulation (EU) 2020/852 of the European Parliament and of the Council by establishing the technical screening criteria for determining the conditions under which an economic activity qualifies as contributing substantially to climate change mitigation or climate change adaptation and for determining whether that economic activity causes no significant harm to any of the other environmental objectives.

The performance thresholds regarding substantial contribution and DNSH for the other four environmental objectives identified in the taxonomy will defined in a Delegated Act that is scheduled for adoption by the end of 2021. Depending on the start date of any process to develop potential NFR standards, the preparation of this Delegated Act could run in parallel for a period time with the standard-setting process. However the Delegated Act would in any case be adopted well before any NFR standards are complete, so there should be no significant obstacles to taking account of the content of the Delegated Act in the NFR standards.

The table below summarises the different aspects of the SFDR and the Taxonomy Regulation, including Delegated Acts, that would need to be considered in potential non-financial reporting standards under the NFRD.

Level 1 legislation	Aspect	Level 2 act	Adoption date	Implications for NFR standards
SFDR	Adverse impact disclosures	Regulatory Technical Standard	Q1 2021	Available in time for consideration in NFR standards.
Taxonomy Regulation	Substantial contribution and DNSH for climate mitigation and adaptation	Delegated Act	Q1 2021	Available in time for consideration in NFR standards.
Taxonomy Regulation	Substantial contribution and DNSH for other environmental objectives	Delegated Act	Q4 2021	Development of DA and of NFR standards could run in parallel for a time, but DA will be available and adopted before any standards are completed.
Taxonomy Regulation	Minimum social safeguards	None – minimum social safeguards defined in the Regulation itself.	Not applicable.	Available in time for consideration in NFR standards.

The following arrangements have ensured and will continue to ensure adequate coordination between the possible development of NFR standards on the one hand, and the SFDR and the Taxonomy Regulation on the other hand:

- The mandate of the EFRAG Task Force on the preparation of possible NFR standards specifically required the Task Force's recommendations to be consistent with the SFDR and the Taxonomy Regulation.[132].

- The three European Supervisory Authorities responsible for drafting the Regulatory Technical Standards under the SFDR are part of the EFRAG Task Force. This ensures direct interaction between the authorities developing the RTSs for the SFDR and the

[132] EFRAG's Task Force report: https://www.efrag.org/Lab2

experts carrying out the preparatory work for possible EU non-financial reporting standards.

- The Platform on Sustainable Finance is carrying out technical work to advise the Commission on the further development of screening criteria under the Taxonomy Regulation. The chair of the Platform nominated a representative from the Platform to be a member of the EFRAG Task Force. The Chair of the EFRAG Task Force will also participate in plenary meetings of the Platform as necessary. In addition, there are already two experts who are members of both the Platform and the Task Force.

Double materiality

Both the NFRD and the SFDR apply a double materiality perspective, meaning that entities subject to either of these two pieces of legislation have to consider both the outside-in risks that sustainability issues create for the company or the investment, and inside-out sustainability impacts of the company or the investment itself. Since the taxonomy defines activities that make a substantial contribution to environmental objectives, it is highly relevant in the case of disclosing the sustainability impacts of companies and investments.

In the case of the NFRD, the double materiality perspective is expressed through the existing requirement on companies to report information "to the extent necessary for an understanding of [their] development, performance, position and impact of [their] activity." If reporting standards were to be developed as described in section 5.2.1 of this impact assessment, then those standards would further specify what information is considered material from both materiality perspectives.

By introducing the additional obligation on companies to report their alignment with activities that qualify as sustainable according to the taxonomy, the Taxonomy Regulation is consistent with and reinforces the NFRD requirement on companies to report about their impacts.

In the case of the SFDR, the double materiality perspective is expressed through the requirement on financial market participants to disclose how they integrate sustainability risks in their decision-making processes (outside-in risks) and to disclose their adverse sustainability impacts (outside-in impacts). In addition, if a financial market participant markets a financial product as having sustainability objectives or sustainability characteristics, then it must justify that claim by disclosing the alignment of the investments underlying the financial product with activities that qualify as sustainable according to the taxonomy.

Entities subject to both the NFRD and the SFDR

Some entities in the financial sector will be subject to both the NFRD and the SFDR. Typically this is the case of banks or insurance companies with more than 500 employees that also carry out asset management activities. It is also the case of a very small number of asset management companies with listed securities. The NFRD covers reporting on all activities of such entities, including lending, whereas the SFDR only covers asset management and investment-advice activities.

Currently there are approximately 300 entities that will be subject to the NFRD and SFDR. If the scope of the NFRD were to be broadened as described in section 7 (preferred option) of this impact assessment, then approximately 700 entities would be subject to the NFRD and SFDR disclosure requirements.

The burden on such entities is dependent on the extent to which the disclosure requirements of the NFRD and the entity-level disclosure requirements of the SFDR are aligned, especially with regard to individual indicators. If there is no or little alignment, then there is a risk that such entities will be obliged to disclose different information in an incoherent manner under each piece of legislation even though the underlying sustainability matters in question (environment, human rights etc.) are the same. If there is a high degree of alignment between the SFDR and the NFRD, then these entities will in principle be able to use the same underlying set of information for both disclosure exercises, thereby keeping administrative burden to a minimum. The development of EU non-financial reporting standards as described in section 5.2.1 would provide the opportunity to achieve the necessary alignment of the disclosures required under the NFRD with the Regulatory Technical Standards under the SFDR being developed by the European Supervisory Authorities.

Interaction with other sustainable finance legislation and initiatives

In addition to the SFDR and the Taxonomy Regulation, the NFRD also interacts with the Capital Requirements Regulation and with work on Green Bonds Standards, with the Eco-label for financial products, and with EU climate benchmarks.

Regarding the Capital Requirements Regulation (CRR), some banks will be subject to both the NFRD and article 449a of the. Article 449a of the CRR requires large listed banks to disclose information on ESG risks, including physical risks and transition risks.

The definition of large banks in the CRR is narrower than in the Accounting Directive/NFRD, and therefore there are currently only approximately 50 entities that will be subject to both the NFRD and the CRR ESG risks disclosure requirements. Broadening the scope of the NFRD as described in section 6.3 of this impact assessment, would not significantly affect the number of banks subject to both the NFRD and CRR ESG risks disclosure requirements.

The burden on such entities is dependent on the extent to which the disclosure requirements of the NFRD and CRR are aligned. If there is a high degree of alignment between the ESG disclosure requirements in the CRR and the NFRD, then these entities will in principle be able to use the same underlying set of information for both disclosure exercises, thereby administrative burden would be minimal. The EBA is developing a technical standard implementing Article 449a disclosure requirements. Detailed cooperation between the EBA and the possible future standards setter would ensure such alignment.

Detailed descriptions of legislation and initiatives in the field of sustainable finance

More thorough descriptions of all relevant sustainable finance legislation and initiatives are provided below.

Title	**Sustainable Finance Disclosure Regulation (Regulation EU 2019/2088 on Sustainability-related disclosure in the financial services sector) (SFDR)**
Legislative or non-legislative?	Legislative
Brief description of policy or legislation	The SFDR was adopted by co-legislators in spring 2019 and was published on 9 December in the Official Journal. It is already in force and most of the provisions apply from 10 March 2021. The SFDR together with its Regulatory Technical Standards (RTS) aim to trigger changes in investment decisions by financial market participants that produce financial products and end-investors that purchase them, and financial advisers that provide investment recommendations towards more ESG sustainable considerations by improving the quality of information from the point of view of ESG positive and negative impacts. The Regulation is expected to also have effects on business models of investee companies. The SFDR lays down rules for sustainability-related disclosures toward end-investors, for both outside-in sustainability risks and inside-out adverse sustainability impacts. It does so in relation to: • the integration of sustainability risks by financial market participants and financial advisers in all investment processes, • financial products that pursue the objective of sustainable investment or have environmental or social characteristics, and • adverse impacts on sustainability matters at entity and financial products levels, i.e. that or, in certain circumstances, whether financial market participants and financial advisers consider negative externalities on environment and social

	justice of the investment decisions/advice and, if so, how this is reflected at the product level.[133] These obligations have considerable behavioural implications. In terms of legal technique, the SFDR is a directly applicable Regulation which introduces additional disclosure requirements to the existing elements of relevant sectoral legislations (AIFMD, UCITS, Solvency II, IORP II, national pension rules, IDD and MiFID II), via a self-standing text (lex specialis) providing full harmonization, cross-sectoral consistency and regulatory neutrality as well as joint convergence by ESMA, EIOPA and EBA. Instead of amending all these existing sectoral legislations in identical way, the SFDR comes on "top" of existing rules in order to impose sustainability disclosure obligations in the same way. This way consistency and regulatory neutrality across all relevant institutional investors' sectors is ensured. The ESAs have submitted to the Commission seven Regulatory Technical Standards (RTSs) on the content, presentation and methodologies of information, including legally binding definitions. The RTS will apply as of January 2022. In addition, the Taxonomy Regulation included in the SFDR other three RTS mandates. In addition, COM is working on revision of Level 2 measures through Delegated Acts (under current empowerments in UCITS, AIFMD, MiFID II, Solvency II, IDD) to explicitly clarify how product manufacturers and financial advisers should integrate sustainability risks and consider principal adverse impact in the in investment and advisory processes (that is in the areas of organizational requirements, operating conditions, risk management and target market assessment) as part of their duties towards clients/customers/beneficiaries.
Interaction with non-financial reporting	It is important for product manufacturers (such as asset managers, institutional investors) and financial/insurance advisers to have easier access to sustainability relevant information by investee companies that are included in their portfolios/ financial products they offer to end-investors. Where non-financial information is not available, information on those companies in the portfolios of asset managers, institutional investors, nor financial advisers, will not be included in the data consolidation, product documentation or marketing information and will not be eligible for investments by financial products that pursue the objective of sustainable investment. The SFDR foresees an evaluation by December 2022 regarding the effect of the absence of reliable and comparable data coming from investee companies as regards sustainability matters.

[133] The reason is that investment decisions and financial advice might cause, contribute to or be directly linked to negative material effects on environment and society, regardless of whether the investment strategy pursues a sustainable objective or not, such as investments in assets that pollute water or devastate bio-diversity, to ensure the sustainability of investments.

Title	**Taxonomy Regulation: Regulation (EU) 2020/852 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088.**
Legislative or non-legislative?	Legislative
Brief description of policy or legislation	Regulation (EU) 2020/852, or Taxonomy Regulation (TR), establishes criteria for determining whether an economic activity qualifies as environmentally sustainable in the EU. The TR applies to: (i) measures adopted by Member States or by the Union that set out requirements for financial market participants or issuers in respect of financial products or corporate bonds that are made available as environmentally sustainable; (ii) financial market participants that make available financial products; and (iii) undertakings which are subject to the obligation to publish a non-financial statement or a consolidated non-financial statement pursuant to Article 19a or Article 29a of the NFRD. The TR is centred around six environmental objectives: climate change mitigation, climate change adaptation, sustainable use and protection of water and marine resources, transition to a circular economy, pollution prevention and control, and protection and restoration of biodiversity and ecosystems. In order to qualify for inclusion in the EU Taxonomy, economic activities will need to: (a) substantially contribute to at least one of the six environmental objectives, by complying with robust and science-based technical screening criteria; (b) do no significant harm to the remaining environmental objectives; and (c) respect minimum social safeguards. With respect to climate change mitigation, the TR recognises three different types of environmentally sustainable economic activities: (i) *low-carbon*, which in and of themselves contribute substantially to one of the six environmental objectives; (ii) *transitional*, which are consistent with EU and international environmental goals but for which there are no technologically and economically feasible low-carbon alternatives; and (iii) *enabling*, which enable other activities to make a substantial contribution to at least one of the environmental objectives and, at the same time, are environmentally sustainable themselves (according to three specific criteria). The technical screening criteria will be developed in two batches: a delegated act on the two climate-related objectives will be adopted by the Commission at the beginning of Q2 2021, whereas a delegated act on the remaining four environmental objectives will be adopted a year later. An additional delegated act complementing the TR will be adopted by June 2021 specifying the application of the requirements to publish the information that undertakings under the scope of the NFRD would have to disclose in their non-financial statements or consolidated non-financial statements.
Interaction with non-financial reporting	Article 8 of the TR will require financial and non-financial undertakings under the scope of the NFRD to include in their non-financial statements or consolidated non-financial statements information on how and to what extent their activities are associated with economic activities that qualify as environmentally sustainable. This requirement will apply from 31 December 2021. This provision will ensure consistent data streams between the information reported by entities under the NFRD

	(i.e., large listed companies, banks and insurance companies) and the taxonomy-related information that financial market participants will need to disclose. If the EU adopted EU reporting standards, these would need to be consistent with the disclosure requirements of Article 8.

Title	**Bank prudential regulation (Capital Requirements Regulation and Directive)** *Regulation (EU) No 575/2013 on prudential requirements for credit institutions* *Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions*
Legislative or non-legislative?	Legislative
Brief description of policy or legislation	The prudential requirements for credit institutions established in the EU are laid down in the Capital Requirements Regulation (CRR) and in the Capital Requirements Directive (CRD). The goal of these rules is to strengthen the resilience of the EU banking sector so that it can better absorb economic shocks, while ensuring that banks continue to finance economic activity and growth. The CRR lays down the rules on the amount of capital that credit institutions must have in order to cover potential losses, on liquidity, on leverage and on reporting and disclosure. The CRD lays down the rules on the licensing of credit institutions, on their supervision, on supervisory cooperation, on risk management, on corporate governance (including remuneration) and on capital buffers.
Interaction with non-financial reporting	Amendments to the CRR in 2019 have introduced a disclosure requirement of environmental, social and governance risks for large listed banks, which will become applicable in June 2022. The European Banking Authority is working on an Implementing Technical Standard due in 2021. A bank is considered as large under the CRR if it meets any of the following conditions: (a) it is a Global Systemically Important Institution (G-SII); (b) it has been identified as an other systemically important institution (O-SII) in accordance with Article 131(1) and (3) of Directive 2013/36/EU; (c) it is, in the Member State in which it is established, one of the three largest institutions in terms of total value of assets; (d) the total value of its assets on an individual basis or, where applicable, on the basis of its consolidated situation in accordance with this Regulation and Directive 2013/36/EU is equal to or greater than EUR 30 billion. A bank is considered as listed if it has issued securities that are admitted to trading on a regulated market of any Member State, as defined in point (21) of Article 4(1) of Directive 2014/65/EU.

Title	**Establishment of an EU Green Bond Standard**
Legislative or non-legislative?	Legislative/ non-legislative (no final decision yet, pending outcome of impact assessment)

Brief description of policy or legislation	In general, standards and labels for sustainable financial products help to protect the integrity of sustainable financial markets and allow investors to more easily identify and trust green financial products. This is why the Commission committed itself to "*Creating standards and labels for green financial products*" in the Sustainable Finance Action Plan from March 2018. As follow-up on this Action, the Technical Expert Group (TEG) on Sustainable Finance presented a report with concrete recommendations of the EU Green Bond Standard (EU GBS) in June 2019 as well as a usability guide in March 2020. The TEG recommended the creation of an official voluntary standard, building on existing market standards, with the following features: (1) Alignment of the use of proceeds of the bond with the EU Taxonomy; (2) Publication of a Green Bond Framework alongside the bond; (3) Mandatory reporting on allocation and impact; and (4) Mandatory verification of Framework and (final) allocation report. In addition, the TEG recommended that external verifiers of EU Green Bonds should be formally authorised or supervised, ideally by ESMA. It also underlined that different incentives could be attached to the EU GBS. On the basis of these recommendations, DG FISMA is currently exploring the establishment of an EU GBS. To gather further input i. a. from market participants, stakeholders and the public sector, DG FISMA has taken following measures: • Published an Inception Impact Assessment on 12 June (open until 7 August); and • Launched two consultations that refer to the EU GBS: (1) the public consultation on the Renewed Sustainable Finance Strategy (open until 15 July) and (2) a dedicated targeted consultation on the EU GBS (open until 2 October). Based on the outcome of these consultations, the Commission will put forward a proposal for a Regulation on European green bonds, as part of a renewed sustainable finance strategy. Any potential legislative proposal for an EU GBS would be foreseen for Q2 2021.
Interaction with non-financial reporting	As described above, the TEG recommends that a future EU GBS should require a certain degree of alignment of the use of proceeds of the bond with the EU Taxonomy. When applying the EU Taxonomy, Article 8 of the EU Taxonomy Regulation requires financial and non-financial undertakings under the scope of the NFRD to include in their non-financial statements or consolidated non-financial statements information on how and to what extent their activities are associated with economic activities that qualify as environmentally sustainable. In particular, these undertakings will be required to report the share of their turnover, capital expenditure, and operating expenditure that is Taxonomy-aligned.

	In the same way, issuers of future EU GBS bonds will also be required to disclose the Taxonomy-alignment of projects funded by their bond, so the two initiatives will support each other. The information disclosed according to the NFRD will provide additional information to investors, including green bond investors, allowing them to better assess the overall non-financial performance of companies.

Title	**Regulation (EC) No 66/2010 of the European Parliament and of the Council of 25 November 2009 on the EU Ecolabel**
Legislative or non-legislative?	Legislative. According to the EU Ecolabel Regulation, the criteria developed for products to be awarded the Ecolabel are adopted by a Commission Decision and have a limited validity in time (revision clause in the Commission Decision).
Brief description of policy or legislation	Established in 1992, the EU Ecolabel is a symbol of environmental excellence awarded to products and services that meet environmental standards throughout their life cycle and provides guidance to companies on environmental best practices. Minimum social, ethical, governance safeguards are also considered. In the 2018 Action Plan on Sustainable Finance, the Commission saw the potential merit in the application of the EU Ecolabel Regulation to specific financial products offered to retail investors, including Packaged Retail Investment and Insurance Products (PRIIPs). The lack of labelled financial products may in fact prevent investors from directly channelling their funds into sustainable investments. The objective of introducing the EU Ecolabel for financial products is to allow retail investors concerned with the environmental impact of their investment to rely upon a trusted and verified label to make informed investment decisions while incentivising financial markets to develop more products with reduced or positive environmental impacts. Thanks to the use of an existing framework, the EU Ecolabel Regulation, it is possible to achieve a quick establishment of an EU label for financial products and improve the currently confusing situation on the different types of green products for end-investors, contributing in this way to avoid "greenwashing". The EU Ecolabel Regulation: ✓ defines the general principles and rules, the procedures for developing/revising criteria, the labelling awarding mechanisms and promotional activities; ✓ requires Members States to designate competent bodies in charge of the verification of the product's compliance with the EU Ecolabel criteria on a regular basis; ✓ foresees a governance structure around the work on developing EU Ecolabel criteria for products and services. This includes setting up the EU Ecolabelling Board (EUEB) that has an advisory role; the involvement of stakeholders (NGOS, consumers organisations, ESAs, etc…) in criteria development process via two rounds of consultations and ad-hoc stakeholders meetings; the final vote on the criteria by the

	Regulatory Committee, composed by Members States, and their adoption via a Commission Decision. The ongoing work on the EU Ecolabel for retail financial products is co-lead by DG ENV and DG FISMA at political level. The Joint Research Centre (JRC) provides the environmental, economic analysis and scientific support to develop the criteria that financial products would have to fulfil in order to be awarded the EU Ecolabel. The JRC has analysed scientific/academic research in order to inform the philosophy and rationale for criteria structure and the comprehension of what environmental impact means for financial products. The first product group, that would be covered by the EU Ecolabel for financial products, includes UCITS/Retail AIFs/unit-linked life insurances products, having investment funds as underlying; and savings and deposits accounts. It exclusively targets products offered to retail clients. <u>Structure of the criteria proposal</u>: The current structure of the criteria proposal includes 6 criteria that have all to be fulfilled by a financial products in order to be awarded the EU Ecolabel. An important criterion relates to portfolio composition (criterion 1), for which, as opposed to the other criteria (criterion 2 to 6), distinct rules apply for different products. Criterion 1: Investment in green economic activities (as defined in the EU Taxonomy Delegated Acts) Criterion 2: Exclusions of companies/activities based on environmental aspects Criterion 3: Exclusions of companies/activities based on social and governance aspects Criterion 4: Engagement requirements Criterion 4: Engagement requirements Criterion 5: Measures taken to enhance investor impact Criterion 6 and 7: Retail investor information and information on the EU Ecolabel The strong link with the EU Taxonomy in the draft criterion 1 ensures that investments are, to an important extent, made in economic activities that are defined (by EU taxonomy) as being green. In the context of taxonomy, the EU Ecolabel will first be able to build on the definition of green activities in the areas of climate change mitigation and climate change adaptation. Green activities in the areas of pollution prevention and control, circular economy as well as in the areas of water resources and healthy ecosystems will only be defined later (the relevant delegated acts are scheduled to be adopted by the end of 2021 and to apply one year later). <u>Timeline</u>: • JRC is still working on the finalization of the draft criteria for the 1st product group financial products to be awarded the Ecolabel. • Inter Service Consultation – Q4 2020-Q1 2021 • Final vote in Regulatory Committee through a Regular Procedure with Scrutiny - summer 2021 • Adoption 4/5 months later as Decision of the Commission
Interaction with	The criteria developed to award the Ecolabel to financial products, use and

non-financial reporting	integrate the results obtained in the development of the EU taxonomy, the improvements of sustainability-related disclosure and potentially the standard for European green bond. For instance, the current lack of consistent data and reporting on the alignment of companies' activities to the EU climate change mitigation Taxonomy represents a current limitation for the development of criterion 1. The implementation of the Taxonomy Regulation will address this issue for companies falling within the scope of the Non-Financial Reporting Directive. The fact of having easier access to good quality and consistent sustainability relevant information by investee companies/underlying investments that are included in the portfolios/financial products offered to retail investors is very important for: - manufacturers, distributors and financial/insurance advisers of retail financial products that fall in the scope of the ongoing work on the EU Ecolabel for financial products and would need this information to apply for the EU Ecolabel, - for the competent bodies in charge of verifying compliance with the EU Ecolabel criteria for these financial products. Where non-financial information is not available, these entities would not be able to apply for the EU Ecolabel nor to verify compliance.

Title	**EU Climate Benchmarks: Regulation (EU) 2016/1011 as amended by Regulation (EU) 2019/2089 and the respective Delegated Regulations**
Legislative or non-legislative?	**Legislative**
Brief description of policy or legislation	Regulation (EU) 2016/1011 as amended by Regulation (EU) 2019/2089 creates two new types of EU climate benchmarks (EU Climate Transition and EU Paris-aligned benchmarks) and lays down a number of Environmental, Social and Governance (ESG) disclosure requirements for all benchmarks (with the exception of interest and foreign exchange benchmarks). The minimum standards for the construction of the EU Climate Benchmarks and the exact scope and content of the ESG disclosure requirements have been further specified in the three delegated acts that were published in the Official Journal on 3 December 2020, and which entered into application on 23 December 2020.[134] On the disclosure front, the delegated acts require benchmark administrators to

[134] Commission Delegated Regulation (EU) 2020/1816 of 17 July 2020 supplementing Regulation (EU) 2016/1011 of the European Parliament and of the Council as regards the explanation in the benchmark statement of how environmental, social and governance factors are reflected in each benchmark provided and published (OJ L 406, 3.12.2020, p. 1).
Commission Delegated Regulation (EU) 2020/1817 of 17 July 2020 supplementing Regulation (EU) 2016/1011 of the European Parliament and of the Council as regards the minimum content of the explanation on how environmental, social and governance factors are reflected in the benchmark methodology (OJ L 406, 3.12.2020, p. 12).
Commission Delegated Regulation (EU) 2020/1818 of 17 July 2020 supplementing Regulation (EU) 2016/1011 of the European Parliament and of the Council as regards minimum standards for EU Climate Transition Benchmarks and EU Paris-aligned Benchmarks (OJ L 406, 3.12.2020, p. 17).

	explain, using a set template, which ESG factors they have taken into account when designing their benchmark methodology. They shall also explain how those factors are reflected in the key elements of that methodology, including for the selection of underlying assets, weighting factors, metrics and proxies. In addition, benchmark administrators shall explain in the benchmark statement, using a standard template, how ESG factors are reflected in each benchmark or family of benchmarks they provide and publish. Finally, benchmark administrators shall disclose information on the alignment with the objectives of the Paris Agreement.
Interaction with non-financial reporting	The Delegated Regulations lay down a list of ESG factors to be disclosed by benchmark administrators, for those benchmarks that pursue ESG objectives, depending on the type of underlying assets concerned (e.g. equity, fixed income, sovereign). Information on the ESG factors should be made at an aggregated weighted value of the benchmark, not for each individual constituent (company). in order for benchmark administrators to be able to disclose such information at an aggregated weighted value, they should still be in position of the data from each of the constituent. They However, in order for benchmark administrators to be able to disclose such information at an aggregated weighted value, they should still be able to obtain data from each of the constituents. They will have to source the information directly from companies (e.g. via their annual reports) or obtain this information from external data providers. If EU non-financial reporting standards are developed, they should therefore take account of the ESG information that benchmark administrators will need. In addition, the rules for the construction of EU Climate Benchmarks contain a number of exclusions for companies involved in controversial weapon, in tobacco activities, found in violation of social norms, that significantly harm environmental objectives or which derive a percentage of their revenues from fossil fuel activities. Benchmark administrators should be in a position to obtain information on the above elements.

B. Interaction between the NFRD and other legislation and initiatives

This section describes a number of other existing and forthcoming initiatives that are relevant to the revision of the NFRD:

- Sustainable Corporate Governance Initiative
- Pay Transparency
- Green Claims Initiative
- Environmental Accounting

- Eco-management and audit scheme (EMAS)
- Emissions Trading System
- Late Payments Directive and Directive on unfair trading practices in business-to-business relationships in the agricultural and food supply chain

Title	**Sustainable Corporate Governance**
Legislative or non-legislative?	Legislative initiative, with possible secondary legislation or further guidance. The legal form and content of the initiative will be determined taking into account the results of the public consultation and the impact assessment.
Brief description of policy or legislation	The initiative aims to ensure that sustainability is further embedded into the corporate governance framework with a view to align better the long-term interests of management, shareholders, stakeholders and society. It aims at improving the framework to incentivise corporate boards to integrate properly stakeholder interests, sustainability risks, dependencies, opportunities and adverse impacts into strategies, decisions and oversight. It would serve the following specific objectives: help companies' directors to establish longer-term time horizons in corporate decision-making and withstand short-term pressures, strengthen the resilience and long-term performance of companies through sustainable business models and help reducing adverse impacts. It would create legal certainty and level playing field as to the necessary measures to be taken by companies to identify, assess and mitigate adverse impacts in the value chain. An EU level initiative could include the appropriate combination of the following corporate (company) and directors' duties with a view to requiring (still to be determined categories of) limited liability companies "not to do harm" and to empowering corporate directors to integrate wider interests into decisions, building also on existing corporate governance mechanisms: • companies to take measures to address their adverse sustainability impacts, such as climate change, environmental, human rights (including workers and child labour) harm in their own operations and in their value chain by identifying and preventing relevant risks and mitigating negative impacts (due diligence duty). Such duty could be designed by building on existing authoritative guidelines using well-established definitions as developed by the UN and later expanded by the OECD3. The performance standards could be set in line with the goals of relevant international conventions and EU goals, such as those on human rights, climate and environment including biodiversity; • company directors to take into account all stakeholders' interests which are relevant for the longterm sustainability of the firm or which belong to those affected by it (employees, environment, other stakeholders affected by the business, etc.), as part of their duty of care to promote the interests of the company and pursue its objectives; company directors to define and integrate stakeholders' interests and corporate sustainability risks, impacts and opportunities into the corporate strategy – following appropriate procedures – with measurable and time-bound, science-based targets where relevant,

	including as regards climate targets aligned to the Paris agreement, biodiversity and deforestation targets, etc. and according also to the company's size and activity, and to implement such strategy through proper risk management and impact mitigation procedures; • an appropriate facilitating, enforcement and implementation mechanism accompanying these duties, including possible remediation where necessary; • other possible corporate governance arrangements for example regarding directors remuneration etc. Depending on the scope and detail of the initiative, it would also need to be assessed to what extent legislative and to what extent non-legislative measures would be best suited to meet the objectives. In particular, it will need to be established which issues would need to be laid down in legislation and which issues would rather have their place in complementary guidance. The initiative would include proper mechanism(s) to enforce these duties and responsibilities. Adoption by the Commission is foreseen for 2021.
Interaction with non-financial reporting	The initiative on sustainable corporate governance and the review of the Non-Financial Reporting Directive would complement each other. Close cooperation will be required during the preparation of both initiatives, to ensure consistency and alignment. For companies under the scope of the revised NFRD, the NFRD should mandate all the necessary disclosures that may be necessary under the proposed sustainable corporate governance initiative. On the one hand, the sustainable corporate governance initiative would contribute to reaching the objectives of the NFRD review. Firstly, the reliability of information disclosed under the NFRD would improve as it would be underpinned by the above-detailed (enforceable) corporate and director duties. The initiative would also mitigate systemic risks in the financial sector by making investee companies themselves more sustainable. On the other hand, companies covered by the sustainable corporate governance initiative would disclose information about how they have applied sustainability in corporate governance and fulfilled their duties. Such disclosure could include in particular corporate sustainability targets and progress towards them, and the due diligence processes implemented. Reporting on these to the public would enable stakeholders to monitor director and corporate duties set out in the new initiative, thereby helping ensure that companies are accountable for how they mitigate their environmental and social impacts.
Title	**Gender pay transparency: Proposal for a Directive on strengthening the principle of equal pay between men and women through transparency (COM(2021) 93 final).**[135]
Legislative or non-legislative?	Legislative
Brief	The objective of the initiative is to enhance the application of the equal pay

[135] https://ec.europa.eu/commission/presscorner/detail/en/ip_21_881

description of policy or legislation	principle for equal work or for work of equal value between women and men regulated in Article 157 TFEU and Directive 2006/54/EC. It further aims to empower workers to enforce their rights to equal pay and reduce the space for gender bias through pay transparency measures tailored to company size, a clarification of key legal concepts relating to equal pay ensuring uniform interpretation and application as well as reinforced enforcement mechanisms. The initiative will lay down rules on pay transparency before hiring. In addition, it gives a right to information on pay and on pay setting and career progression policy upon request of workers. The initiative also foresees annual public pay reporting on the gender pay gap (for companies with at least 250 employees), and joint pay assessment - when the pay reporting demonstrates a difference of average pay between female and male workers in the organisation of at least 5 per cent in any category of workers doing the same work or work of equal value which has not been justified by objective and gender-neutral factors. Member States would have the obligation in accordance with national law and practice to ensure that the rights and obligations under the directive are discussed with social partners - without prejudice to their autonomy. Under the measures related to a better understanding and implementation of concepts on equal pay, the concepts of 'pay' and 'equal work' and 'work of equal value' are clarified based on existing CJEU case law. This is key for legislators and those involved in the enforcement of equal pay measures to have a better and common understanding of the relevant legal concepts. Under measures facilitating the enforcement of the right to equal pay, the initiative encompasses support for victims such as the strengthening of the role of equality bodies, and workers' representatives. It provides for collective claim and the alleviation of the burden of proof, as well as the collection of evidence, remedies for victims of pay discrimination and sanctions. The initiative also limits procedural barriers to enforcement (limitation periods and judicial costs), and promotes the consideration of intersectionality, i.e. situations with discrimination based on a combination of sex and any other ground or grounds of discrimination protected under EU law.
Interaction with non-financial reporting	The present initiative would require certain companies to make information regarding the gender pay gap publicly available. Some of these companies may also be covered by the forthcoming revision of Non-Financial Reporting Directive 2014/95/EU (NFRD). Both initiatives will be aligned so that any public reporting on the gender pay gap pursuant to the Pay Transparency Directive by companies subject to the NFRD would be taken into account in the future standards for non-financial reporting under the NFRD.

Title	**Green Claims initiative: Substantiating environmental claims using the Product/Organisation Environmental Footprint methods**

Legislative or non-legislative?	Legislative
Brief description of policy or legislation	The objective of the initiative is to move to a more harmonised approach for providing voluntary environmental information and ensuring the reliability and relevance of information that companies provide on a voluntary basis regarding the environmental impacts of products and organisations, thus making it easier for consumers, business and other market participants to integrate environmental considerations into their decisions. The Circular Economy Action Plan of 2020 commits that "The Commission will also propose that companies substantiate their environmental claims using Product and Organisation Environmental Footprint methods" by the end of 2020 [now scheduled for 2021]. We will examine several policy options, including a voluntary scheme and an obligation of substantiating green claims via the Environmental Footprint methods for environmental issues covered by the methods. The initiative would include claims both in business-to-consumer and business-to-business/stakeholder situations. There are two methods: one focussing on products (Product Environmental Footprint, PEF) and one for organisations (including companies, Organisation Environmental Footprint, OEF). The methods are the result of several years of common testing with businesses, business associations both in the EU and internationally; and other stakeholders including public administrations, NGOs and academia. The methods were developed by DG JRC based on existing methods, taking best practice approaches. They were subject to a Commission Recommendation on the use of common methods for measuring and communicating the life cycle environmental performance of products and organisations in 2013. A revised version based on learnings of the pilot phase will be the basis of the green claims initiative. The methods were created having in mind reliability, reproducibility and comparability of information. The methods cover impacts from the whole value chain and focus the analysis on environmental impacts and processes that are most contributing to the overall impact of a product or company. They cover 16 environmental impacts, including climate change, water use, land use, toxicity. They require the user to identify which are the environmental hotspots of the undertaking. Environmental hotspots include environmental impacts, processes (either direct or indirect, occurring upstream or downstream in the value chain) and life cycle stages. The method enables the development of product- and sector-specific environmental performance calculation rules (Product Environmental Footprint Category Rules – PEFCRs and Organisation Environmental Footprint Sector Rules – OEFRs). If such rules exist, they pre-define relevant (material) environmental impacts, life cycle stages and processes for the given product category/ sector.
Interaction with non-financial reporting	In preparing the green claims proposal, the Commission will define more clearly what can be considered a "green claim". Environmental information published in company annual reports, which is regulated by the NFRD, will not in any case fall within the definition of "green claims". Any legislation of green claims would therefore not apply to the information in company annual reports. Environmental information published in

	annual reports is mandatory, whereas companies choose to make green claims or not on a voluntary basis. The PEF and OEF methods are already referenced in the Guidelines on non-financial reporting. Particularly, OEF is relevant for company-level reporting, as a means to quantify impacts (and therefore enable target setting and tracing), to identify environmental hotspots that may pose a risk to companies (including along their supply and value chain), and to increase relevance, consistency and comparability of information. The green claims proposal will likely require companies to substantiate their green claims based on environmental performance using the PEF (for product-related claims) and OEF (for organisational related claims) methods. In some cases companies might make green claims on the basis of environmental performance information contained in their annual reports (non-financial statement). To ensure maximum consistency and coherence between the Green Claims initiative and the NFRD, any possible EU non-financial reporting standards developed as part of the NFRD revision should take account of and incorporate as appropriate the OEF methodology.

Title	**Environmental Accounting: Transparent Project –Supporting business and stakeholders in developing standardized natural capital accounting practices in the EU and internationally**
Legislative or non-legislative?	Non-legislative (supporting better implementation of legislation, including NFRD)
Brief description of policy or legislation	Of the many existing corporate environmental reporting initiatives, few focus on developing underlying management accounting methods that can produce relevant, credible, auditable, and comparable data supporting internal decision making (and external reporting). Advanced insights on how to best account for environmental impacts and dependencies were captured in the Natural Capital Protocol referenced in the NFRD guidelines. Further standardization of natural capital accounting practices and pragmatic solutions facilitating its implementation are key for its mainstreaming –an essential condition for overcoming the general shortage of relevant, credible, and comparable data on total environmental impacts and greening the economy generally. Natural capital or environmental accounting seeks to identify, quantify, and value the impacts and dependencies of an entity's activities on natural capital also (but not exclusively) in monetary terms. Hence, it allows arriving at total weighted impacts along the supply, and eventually the value chain. These impacts which generally remain unaccounted for in today's financial and non-financial statements are especially useful to management decision-making in companies or other economic entities. The Transparent project is a LIFE preparatory project responding to the EGD's call to support businesses and stakeholders developing standardized natural capital accounting practices. It supports a leading global public-private partnership in the field of natural capital accounting for the period 2020-2022, including the Value

	Balancing Alliance, the Capitals Coalition, and the World Business Council for Sustainable Development. The project's output will include the world's first standardized and widely accepted methodology to identify, measure and value environmental impacts in corporate entities. The standardized method will serve as the principal benchmark for companies establishing and using natural capital accounts and data (as well as providing assurances). It will be consistent with the NFRD's double materiality principle. Drafts for public consultation are due in 2021/Q1 with the final set due latest by 2022/Q4. Standards and guidelines will be further promoted as part of the international natural capital accounting initiative called for by the EU's recent biodiversity strategy and related initiatives, e.g. the green investment and circular economy strategies, etc.
Interaction with non-financial external reporting	The Transparent consortium is committed to also reinforce the core objectives of closely related policy initiatives and pursuing maximum synergies, notably the present revision of the NFRD. The methodology of the Transparent project and already agreed actions to further promote its application globally will help implementing the revised non-financial reporting directive and achieving its core objectives, notably by enabling companies to identify, and manage significant environmental risks related to impacts and dependencies associated with its business activities. An important aim of the Transparent project is to enhance the trust and credibility of information to that is to be relied upon for decision making by managers which can then be monitored and reported with confidence both internally and externally. The proposed method will capture the total impact and dependency for all (relevant) environmental areas (air including climate, water, land and biodiversity) covering the entire supply chain and ultimately aiming for the value chain at large. This data is likely to strengthen internal decision-making, and may also be an input to external reporting under the NFRD and any future reporting standards. The Transparent output will not serve to label activities or assets as 'green' or not green per se – an area reserved for the taxonomy, the green claims initiative, and other green product standards. It will enable companies to better identify and manage their environmental impacts and dependencies in a credible way. As such it would underpin reporting and potentially the work of auditors and assurance providers and could also play a role in sustainable corporate governance, business models, and related assurance provisions under development in the EU and globally.

Title	**Regulation (EC) No 1221/2009 of the European Parliament and of the Council of 25 November 2009 on the voluntary participation by organisations in a Community eco-management and audit scheme (EMAS)**
Legislative or non-legislative?	Legislative
Brief description of	EMAS is a management tool for organisations to evaluate, improve, and report on their environmental performance. EMAS helps organisations to implement a

policy or legislation	management framework that ensures a systematic identification and management of key environmental performance issues in order to reduce the environmental footprint and risk profile of the organisation. Established already in 1993, currently almost 4.000 organisations with over 12.000 sites in Europe and the world use the EMAS instrument. EMAS registration requires organisations to regularly produce a public environmental statement that reports on their environmental performance, thereby enhancing transparency. The credibility and recognition of EMAS and participating organisations stems from this publication of environmental information checked by an independent environmental verifier for accuracy and reliability. As an environmental management tool requiring publication of an annual, independently validated environmental statement with detailed core indicators, EMAS provides registered organisations with a high degree of transparency. EMAS registered organisations can use their environmental statements and the official EMAS logo to give their clients and customers a clear signal of their commitment to environmental performance, backed up by real data. These efforts are recognised not only by customers, but also by regulators in the Member States. Several national and local regulators accept the EMAS registration and environmental statement as proof of an organisation's legal compliance or to fulfil other reporting requirements.
Interaction with non-financial reporting	The current Directive on non-financial reporting explicitly states in its recital 9 "In providing this information, undertakings which are subject to this Directive may rely on national frameworks, Union-based frameworks such as the Eco-Management and Audit Scheme (EMAS), […]" The EU Commission also emphasizes the importance of EMAS for transparency in the Guidelines on non-financial reporting. There, environmental assessment according to Annex I of the EMAS Regulation is recognized as a methodology to perform the materiality assessment. Also, for assessing sector-specific issues, the EMAS Sectoral Reference Documents are named. Thus, also for the future updated NFRD and possible reporting standards, EMAS could be recognized as a tool to fulfil part of the reporting obligations.

Title	**EU Emission Trading System**
Legislative or non-legislative?	Legislative
Brief description of policy or legislation	Pending the outcome of the 2030 Climate Target Plan and in line with the Green Deal Communication, the Commission will review and propose to revise, if necessary to increase its ambition, the EU ETS by June 2021. The EU ETS is the key EU policy to reduce its emissions cost-effectively, meet its

	overall emission reduction targets and thus combat climate change. It is a market-based measure that caps overall emissions permissible for the installations it covers in power generation, energy-intensive industry and aviation within the EEA. Installations covered are obliged to surrender allowances against their annual emissions. Article 14 of the EU ETS Directive[136] requires the monitoring, reporting and verification of emissions of several greenhouse gases for the purposes of annual submission of verified emissions by installation operators. Eligible installations must submit an inventory of verified annual emissions each year, covering Scope 1 emissions as defined by the Greenhouse Gas Protocol[137], comprising emissions emitted directly in the execution of the activities covered. Eligible installations compile and submit this data to the Commission annually for publication.
Interaction with non-financial reporting	Currently, the legal obligations conferred on undertakings in the Non-financial Reporting Directive (NFRD) do not explicitly include the reporting of greenhouse-gas emissions in the non-financial statement. Recital (7) indicates that non-financial statements "should contain…details of…the undertaking's operations on the environment, and, as appropriate…greenhouse gas emissions". Article 1 obliges eligible undertakings to include in their non-financial statements the impact of their operations on environmental matters, the principal risks to the environment and the ways in which the undertaking is managing these risks. If no policies are in place, it must provide an explanation. There are clear grounds to expect companies to include greenhouse-gas emissions in their non-financial statements, as they impact the environment significantly. To minimise costs and administrative burden, any further specification of emissions reporting as part of the NFRD revision could, in the case of installations under the ETS, oblige the companies concerned to consolidate and submit the data for their installations in their NFRD non-financial statements. To gain a full picture of corporate emissions, emissions from the energy consumed by a company (Scope 2) and all other indirect emissions (Scope 3) would need to be accounted for separately.

Title	**Directive 2011/7/EU[138] of the European Parliament and of the Council of 16 February 2011 on combating late payment in commercial transactions (and Directive 2019/633 of the European Parliament and of the Council of 17 April 2019 on unfair trading practices in business-to-business relationships in the agricultural and food supply chain)**[139]
Legislative or non-	Legislative

[136] Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003
[137] https://ghgprotocol.org/
[138] Directive 2011/7/EU on combating late payment in commercial transactions.
[139] https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32019L0633

legislative?	
Brief description of policy or legislation	The aim of the LPD Directive is to combat late payment in commercial transactions, to ensure the proper functioning of the internal market, thereby fostering the competitiveness of undertakings and in particular of SMEs. The Directive addresses late payments in commercial transactions both between public authorities and businesses, and between businesses. The "Late Payment Expert Group[140]" was set up in 2011 to facilitate a smooth transposition and implementation by the Member States of the new late payment Directive. In the short to medium term, late payment can lead to cash flow issues, income loss, slow growth and an inability to hire new employees, which in turn has direct consequences for GDP and employment. It also affects businesses' competitiveness and profitability when the creditor needs to obtain external financing because of late payment. The risk of such negative effects strongly increases in periods of economic downturn when access to financing is more difficult. In the longer term, unsustainable cash flow threatens company survival and leads to bankruptcies. It is estimated that late payment accounts for 1 out of 4 bankruptcies in the EU. Late payment is above all an intentional practice – especially when there is an asymmetry between the debtor (large business) and the creditor (smaller business). Unfair payment practices (setting longer payment terms – often unsustainable for suppliers, refusing to pay interest, "paid when paid" clauses) are the symptoms of a bad payment culture deeply embedded in the business environment. This is why the Directive pleads for a decisive "shift" towards a payment culture where prompt payment is the new norm. Reporting on average payment periods will ultimately foster better payment practices. This is an important signal especially in moments of crisis, where disruptions in the supply chain payments further put under pressure SMEs. The LPD has been recently complemented by a Directive to combat practices that grossly deviate from good commercial conduct, that are contrary to good faith and fair dealing and that are unilaterally imposed by one trading partner on another, in the agricultural and food supply chain. It prohibits late payments for agricultural and food products, including late payments for perishable products as they impact negatively on the economic viability of the supplier, without providing off-setting benefits.
Interaction with non-financial reporting	The principle that prompt payment can avoid social consequences through the supply chain is already included in the Guidelines on non-financial reporting (methodology for reporting non-financial information) under the thematic aspect "supply chain". Reference to payment routines can also be found in existing sustainability international standards.[141] The Commission should further build on this principle in the future reporting standards if such standards are developed. The Late Payment Directive contains an Article devoted to "Transparency and awareness raising" (Article 8), which obliges Member States to ensure transparency regarding the rights and obligations stemming from this Directive. In addition, they should spread good payment practices, to foster a prompt payment culture. The LPD Directive does not go as far as imposing the regular production of a specific report, but it does encourage virtuous

[140] Late Payment Expert Group

[141] GRI 204 Procurement practices 2016 https://www.globalreporting.org/standards/gri-standards-download-center/?g=05059bfb-2058-47c3-b80b-c093d13cc976

	payment practices, and the spreading of such practices. In 2018, the Commission carried out a study[142] which explored, among other measures, the use and potential of transparency of payment practices. Indeed, a few Member States (France, Sweden, Slovenia, Spain) and the UK have established provisions setting out the mandatory communication and publication by businesses of payment practices and policies (e.g. average payment periods in France, Spain, Sweden and the United Kingdom[143], and protested bills of exchange in Slovenia). The obligations usually apply to large companies, with turnover exceeding a certain amount, or above a certain number of employees. Access to information on the payment practices of future (or existing) partners can help companies choose more reliable business partners. In addition, public access to information can be an incentive for companies to improve the way they deal with suppliers. However, where access to payment information is limited, requires payment or offers only fragmented coverage, this can prevent SMEs from systematic use of these data. Mandatory reporting of payment practices for larger operators would counteract these shortcomings. In addition, the SME Strategy published in March 2020 emphasised that, due to increased concentration and vertical integration in supply chains, the main customers of SMEs are often much larger organisations. This leads to asymmetries in bargaining power and increases the risk of small businesses being subject to unfair business practices and conditions, including late payments[144] and access to data. Better monitoring and reporting on LPD enforcement is also part of the actions of the Strategy.

[142] "Business-to-business transactions: a comparative analysis of legal measures vs. soft-law instruments for improving payment behaviour"

[143] Although it is still too early to draw comprehensive conclusions, initial data on the implementation of this measure in the UK indicates that 60% of companies reporting had not paid 95% of invoices within 60 days. This has triggered additional measures from the UK government, such as the new rule entered into force in 2018 whereby businesses that do not demonstrate proper payment performance towards their clients are excluded outright from public procurement contracts.

[144] Directive (EU) 2019/633 of the European Parliament and of the Council of 17 April 2019 on unfair trading practices in business-to-business relationships in the agricultural and food supply chain prohibits late payments for agricultural and food products, including late payments for perishable products (Art. 3.1 (a)), with a dynamic approach based on the relative size of the supplier and the buyer in terms of annual turnover, to provide better protection against unfair trading practices for those operators who need it most.

ANNEX 11: CAPITAL MARKETS UNION HIGH-LEVEL FORUM PROPOSAL FOR EUROPEAN SINGLE ACCESS POINT.

The Capital Markets Union High-Level Forum published its final report in June 2020. The report contains the following specific recommendation for the creation of an EU-wide digital access platform (EU Single Access Point, or "ESAP") to companies' public financial and non-financial information:

Recommendation
The Commission is invited to: • Propose legislation for ESMA to establish an EU-wide digital access platform (EU Single Access Point, or "ESAP") to companies' public financial and non-financial information, as well as other financial product or activity-relevant public information (hereafter referred to only as "public information"), which shall be freely accessible to the public and free of fees or license use.[145] • Ensure that companies (listed and non-listed) are required to submit all the public information only once through a single reporting channel, which may necessitate streamlining existing multiple reporting channels (considering for instance Officially Appointed Mechanisms, National Competent Authorities, European Authorities).[146] • Conduct work on harmonising the content and, if appropriate, the format of companies' public information to foster better comparability and usability of data. The use of technology as well as templates and standards should not impose additional language requirements causing significant burden. Regarding the scope of public information which could be made available through the EU Single Access Point, the Forum recommends adopting a staged approach: • In a first stage, the EU Single Access Point should: o Serve as a platform to access all public information of companies with securities listed on EU Regulated Markets. o Focus on periodic / ongoing information disclosed by companies pursuant to securities markets legislation including at least the Transparency Directive, Non-Financial Reporting Directive, Prospectus Regulation, Shareholders Rights Directive, Market Abuse Regulation, Short Selling Regulation and Take-Over Bid Directive. o Include non-financial statements disclosed by companies listed on EU regulated markets pursuant to the Non-Financial Reporting Directive. • In a second stage, it should be considered whether to expand the scope of the ESAP, once fully established, to include some, or all of the following:

[145] The exact cost model will need to be carefully thought through. Furthermore, ESMA will need to receive appropriate resources to set up and operate the ESAP so that access to the public remains free of fees.

[146] Where issuers are already allowed today to outsource submission of reporting requirements to third parties, this authorisation should also be given regarding the submission of the corresponding reporting requirements through the ESAP. As is the case today, liability regarding the accuracy of the information would remain with the issuer.

- Public information disclosed by companies on SME Growth Markets pursuant to the Prospectus and Market Abuse Regulations.
- Serve as a platform for the disclosure of documents prepared under the UCITS and 2011/61/EU AIFM Directives (such as annual financial reports and any public fund-related information documents).
- A broader range of sustainability-related companies' public information disclosed pursuant to sustainable finance legislation, such as the entity- and product-level information on sustainability risks and impacts disclosed pursuant to the Regulation (EU) 2019/2088 on sustainability-related disclosures. This would make the ESAP a repository for all current sustainability-related public information by listed companies (managed by ESMA, or in stage 3 by the relevant authority for any information beyond ESMA's remit).

- In a third stage, it should be considered whether to expand the scope of the ESAP, once fully established, to include some, or all of the following public information beyond ESMA's remits, such as:
  - market-relevant information made public pursuant to prudential or other legislation, such as Pillar 3 reports to be disclosed by credit institutions pursuant to Regulation (EU) 575/2013 on Capital Requirements (CRR), and Solvency and Financial Condition Reports (SFCR) to be disclosed by insurance undertakings pursuant to the Solvency II Directive (2009/138/EC). Appropriate arrangements should also be made with other relevant public authorities (e.g. EBA and EIOPA and corresponding authorities/bodies at national level).

In parallel to stage 1, the Commission should mandate ESMA to assess the possibility to expand the scope of the EU Single Access Point to include public information disclosed by non-listed companies including notably non-listed SMEs, on a voluntary basis[147], provided that they comply with the relevant format and content requirements. This could leverage, to the extent possible, on the Business Register Interconnection System (BRIS).

When setting up the EU Single Access Point, the Forum recommends the following steps to improve searchability of the information contained therein:

In the first stage:

- Grant ESMA powers and resources to oversee the proper collection of data and its compliance with EU standards to the extent of its jurisdiction.
- Task ESMA with developing technical standards to develop data fields and formats (XML or similar metadata) to ensure that public information is findable on the database (i.e. similar to the approach used in ESEF for annual financial reports or the Prospectus Register) which shall be used by companies when submitting the public information foreseen in the first stage described above in

[147] The operational challenges and costs of expanding the scope of the EU single access point from listed firms only (around 5000 companies across the EU) to all non-listed firms (hundreds of thousands of companies) should not be underestimated. Therefore the inclusion of non listed firms in the ESAP should be on a voluntary basis and be based on the condition that non listed firms will be voluntarily complying with all format and content requirements.

order to foster cross-border searchability.

- Such technical standards to develop data fields and formats should use appropriate entity and document identifiers (LEIs, ISINs, etc.) to ensure that public information about issuers and securities can be easily inter-linked and cross-referenced.
- Grant ESMA powers to coordinate and drive implementation with national authorities in order to ensure that the public information collected at national level is accompanied by the correct data fields and, in case of structured information (i.e. as of today, Annual Financial Reports prepared in XBRL[148] pursuant to the ESEF Regulation), that information submitted by companies complies with the applicable format requirements.

In parallel to the first stage:

- Task ESMA to assess whether it is appropriate and useful for comparability reasons and for facilitating machine-based data processing that all public information within its remits should be prepared in a machine-readable format such as XBRL or in standardised templates[149]; if so, ESMA should be tasked to develop the relevant taxonomies (for more harmonised documents, such as the Non Financial Statements) or standardised templates and should ensure that any formatting is affordable to all issuers across the EU, and do not result in significant additional burden on issuers nor costs.

In the later stages, consider to:

- Task the ESAs Joint Committee or EBA/EIOPA to perform the same assessment / develop relevant taxonomies or templates for Regulations and documents within their remit.

When setting up the EU Single Access Point, the Forum recommends the following architecture:

- The EU Single Access Point should be built in the first stage by ESMA as a hybrid structure whereby public information is submitted by companies at national level (to OAMs/NCAs in the first step, and potentially to other authorities/bodies in the future) and then it is collected, aggregated and disclosed by ESMA (and in stage 3 also by the relevant authority for any information beyond ESMA's remit) at EU level via system specifications provided by ESMA.
- OAMs or other authorities/bodies should be allowed to check the correct application of data fields entered by issuers, in line with their respective competences, and to ensure compliance with format requirements (XBRL or other) whenever applicable. ESMA shall be empowered to supervise the compliance with these requirements for information within its remit. In later phases adequate arrangements should be made with other ESAs and other national bodies if necessary.
- ESMA, under the authority of the legislative proposals from the Commission shall establish the ESAP having regard to the EU Data Strategy of March 2020, ensure that the architecture of the ESAP can be scaled up so as to prepare the grounds for stages 2 to 4, and encompass further authorities or bodies at national level and at EU level to the extent necessary.

[148] See CMU HLF recommendation fiche on listing requirements and simplification.

[149] As of today, only Annual Financial Reports including IFRS consolidated financial statements prepared pursuant to the Transparency Directive are in XBRL format

- The EU Single Access Point needs to be devised in a way that a one-click access for human users is possible, and that machine-data users can automatically download public information from the platform in order to foster "big data" applications and data reuse. The data fields should ensure that public information is searchable by criteria such as Member State of origin, sector, size, turnover range, etc.
- The IT infrastructure of the EU Single Access Point should ensure interconnectedness of the existing European and national registers, and should be devised so that in the future further repositories/ databases currently managed by other authorities or bodies (e.g. National Competent Authorities, Officially Appointed Mechanisms "OAMs", or European authorities). This would allow users, in particular investors, to have an integrated access to all relevant public information. The system should be designed with sufficient flexibility to encompass new or additional categories of public information in the future, remain up-to-date with technical developments and address evolving user needs.
- ESMA should establish the EU Single Access Point as quickly as possible leveraging on existing provisions in the Transparency Directive, while ensuring that the system is able to evolve in a flexible manner to cover a broader range of public information. For this purpose, ESMA should be provided with adequate ad hoc funds and resources.
- In order to collect, aggregate and disseminate data at EU level, the EU Single Access Point should rely on the most appropriate technology.

Issue at stake

Some of the key objectives of a true Capital Markets Union include (i) promoting market integration, and (ii) ensuring easy access to diverse sources of funding for all companies, including sustainable ones. Unfortunately, issuers often have to rely on national markets only, and investors on more developed capital markets, thereby reducing their chances of finding capital/investment opportunities. In particular, many smaller companies – including in smaller Member States – struggle to attract investors' interest. This national or home bias furthermore limits the Union's economic resilience by hindering geographical and sectoral diversification. This is partly explained by the lack of easily accessible, reliable, understandable and comparable public information that would help investors in their investment decisions and ease their diversification strategies. Setting up a European centralized access to public financial and non-financial information would boost issuers' exposure to a wider set of investors, while ensuring a better allocation of capital in the EU.

Setting up such a centralised access point will take time. A phased approach should be preferred in order to gradually develop the initiative, whilst not losing sight of the ultimate objective of free centralized access to public information.

Justification

To make investment decisions, investors in capital markets require information about issuers of securities. The availability and quality of such public information is a measure of the transparency of a capital market, which is itself a driver of investor confidence in capital markets. Suboptimal accessibility or quality of information about issuers therefore undermines investor confidence and the

development of capital markets. In addition, the fragmentation and lack of comparability of public information on a geographical/jurisdictional basis increases search costs for investors, thereby undermining their ability to scale their investment strategies across geographical/jurisdictional boundaries. This undermines the integration of capital markets. Public information therefore plays an essential role for both elements of the CMU project: 1) the development of national capital markets; and 2) the integration of capital markets across the EU.

Accessing public financial and sustainability-related information can be difficult for anyone including investors, especially as it is scattered all across the EU. Accessibility is currently undermined by the lack of consistent disclosure mechanisms and of a single point of access to such information. In addition, diverse implementation of reporting obligations at national level, lack of harmonised definitions, together with language barriers render data understanding and comparability across most EU listed and non-listed companies challenging. This is first and foremost to the detriment of smaller companies and those in smaller Member States with less-developed capital markets. These market conditions act as an impediment to a true CMU. Comparable, usable and easily accessible public information is not only essential for investors, but also for financial intermediaries (i.e. rating agencies, financial analysts, research providers, etc.) who need such data to help investors to make informed investment decisions. Hence, there is scope for improving accessibility, usability and comparability of publicly disclosed public information. The usability of public information could also potentially be enhanced by broader use of structured data which could facilitate both analysis by investors and the use of information disclosed pursuant to securities markets legislation.

Legal amendments

The Commission is invited to put forward dedicated legislative proposals for the establishment of an EU Single Access Point (ESAP) for public information. In terms of sequencing, during ESAP's stage ESMA, under the authority of the legislative proposals from the Commission should firstly set up the IT infrastructure (point 1 below). The legal changes needed to finalise the ESAP's stage 1 (point 2 below) could be proposed in parallel before proposing the legal amendments needed to implement ESAP's stages 2 and3(corresponding to points 3 and 4 below respectively).

1. During ESAP's stage 1, as a very first action, the Commission would propose new provisions in order to establish the ESAP architecture, as there is currently no legal obligation to interconnect national and European registers and databases other than the European Electronic Access Point foreseen in the Transparency Directive. When setting up this interconnection, relevant existing EU law should be taken into account (e.g. Open Data Directive, EU communication on data strategy). In addition, the Commission should define rules setting out how users can access such information (i.e. the characteristics of the ESAP for users, such as ensuring searchability by Member States of origin, sector, size, turnover range, etc.). This would allow users to already have access to all listed companies' public information via the ESAP, whatever the format of disclosure.

2. For the finalisation of the ESAP's stage 1, all pieces of EU legislation regulating the disclosure of public information shall be amended as follows:

i) The Transparency Directive and the RTS on the EEAP should be amended to reflect the amended objective, scope and organisational set-up of the European electronic access point; adequate funding for ESMA should be foreseen in the related Legislative Financial Statement

ii) In order to facilitate the analysis and comparability of public information retrieved via the ESAP, the Commission should amend the Transparency Directive (2004/109/EC), the Non Financial Reporting Directive (2014/95/EU), Prospectus Regulation (EU/1129/2017),[150] Shareholders' Rights Directive (2007/36/EC), Take-Over Bids Directive (2004/25/EC), Market Abuse Regulation (EU/596/2014) and Short Selling Regulation (EU/236/2012) to delegate powers to ESMA to define the machine-readable data fields and format (i.e. XML or similar data fields) to be applied by issuers when fulfilling each reporting obligation of public information.

iii) In order to ensure that companies' reportings comply with the EU rules on the machine-readable data fields and format, the Commission should amend the Transparency Directive (2004/109/EC), the Non Financial Reporting Directive (2014/95/EU), Prospectus Regulation (EU/1129/2017), Shareholders' Rights Directive (2007/36/EC), Take-Over Bids Directive (2004/25/EC), Market Abuse Regulation (EU/596/2014) and Short Selling Regulation (EU/236/2012) to grant the relevant competent bodies/authorities in charge of receiving the company's filings the power to conduct quality check, order resubmission and hold companies responsible for the public information that they submit and grant ESMA the power and budget to coordinate and steer such activities.

iv) In order to limit the administrative burden on companies related to disclosures, the Commission should require Member States to implement a 'file-only-once' principle for companies to disclose their public information only once through this entry point. In addition, the Commission should amend the Transparency Directive (2004/109/EC), the Non Financial Reporting Directive (2014/95/EU), Prospectus Regulation (EU/1129/2017), Shareholders' Rights Directive (2007/36/EC), Take-Over Bids Directive (2004/25/EC), Market Abuse Regulation (EU/596/2014) and Short Selling Regulation (EU/236/2012) to require companies to submit their reporting only once through the established national single entry point.

v) In order to ensure that the public information submitted into the ESAP by companies are complete and are compliant with the machine-readable data fields and formats, the Commission should amend articles 31 and 35 of the Regulation 1095/2010 establishing ESMA to broaden its powers of coordination over the collection of public information within its remit.

3. Once stage 1 of the ESAP is operational, its scope could be extended to include all public information foreseen in the ESAP's stage 2:

i) the Commission should amend the Prospectus Regulation (EU) 1129/2017 and the Market Abuse Regulation (EU) 2014/596 to require SME growth market issuers to submit their reporting of public information pursuant to these texts (i) only to the established national entry point and (ii) using the machine-readable data fields and formats developed at EU level.

ii) the Commission should amend Directive 2014/91/EU on UCITS and Directive 2011/61/EU on AIFM to require related disclosure obligations by funds (e.g. UCITS Prospectuses, annual

150 Building on the experience gathered in the context of the Prospectus register

financial reports and any other fund-related public information documents) to be carried out (i) only once through the established national entry point and disclosed through the ESAP and (ii) using the machine-readable data fields and formats developed at EU level.

iii) The Commission should amend Regulation 2019/2088 on sustainability-related disclosures in the financial services sector, as well as any future legislation on sustainability issues, in order to require market participants to fulfil their disclosure obligations (i) only through the ESAP and (ii) using the machine-readable data fields and formats developed at EU level.

iv) In parallel, the Commission should delegate powers to ESMA, EBA and EIOPA to assess whether it is appropriate to develop, and if so to develop, relevant taxonomies (in XBRL or similar formats) or standardised reporting templates for issuers to be able to fulfil their reporting obligations within the scope of the ESAP's stage 2 in a standardised and comparable manner.

4. During ESAP's stage 3, the following amendments could be considered:

i) The Commission should amend Regulation (EU) 575/2013 on Capital Requirements the Solvency II Directive (2009/138/EC) to require (i) credit institutions to submit Pillar 3 reports only to the national entry point; (ii) insurance undertakings to submit Solvency and Financial Condition Reports (SFCRs) only to the national entry point; and that both (iii) use the machine-readable data fields and formats developed at EU level.

In parallel with the ESAP's stage 1, the Commission should mandate ESMA to assess whether the scope and functionalities of the ESAP could be expanded to non-listed companies (including non-listed SMEs) willing to opt-in on a voluntary basis. Public information disclosed by non-listed companies would need to be harmonised and comparable. For instance, on the basis of ESMA's advice, the Commission could allow non-listed companies, on a voluntary basis, to either (i) comply with the same reporting obligations as listed companies, or (ii) comply with a subset of these requirements, or (iii) publish financial accounts according to alleviated IFRS standards.

Feasibility: Implementation process and possible risks

- The EU single access point is an ambitious project, which might face reluctances from Member States and national supervisors, despite its potential of being a game-changer for investors, companies and financial intermediaries. In particular, broadening the scope of the ESMA's (and potentially, in a later phase, other ESA's) powers and unlocking budget to set up and run the ESAP could prove difficult.
- The scope of public financial and sustainability-related information which could be included within the ESAP following the first phase means that proper consideration would need to be given to operational arrangements to ensure smooth coordination among the ESAs and other national databases/ registrars. For instance, sustainability-related disclosures of entities within the exclusive scope of EIOPA or EBA's remits (i.e. non listed banks or insurances), are not within ESMA's remits.
- Making the ESAP free for users will require finding appropriate budget or funding for national entry points and the ESAP set-up and running. In addition, the cost of implementing the ESAP will vary depending on how ambitious its scope will be.

Expected benefits
• Contribute to further integrating European capital markets by giving investors an easy, EU-wide view of investment options, thus enabling a more efficient allocation of capital and indirectly strengthening economic resilience through diversification • Promote companies' visibility to potential investors and financial intermediaries • Enable big data and IA based services through the increased use of structured data • Contribute to the harmonisation and standardisation of publicly disclosed information of companies, both financial and non-financial, to allow its findability • Facilitate the findability of SME data, thus tackling an important barrier to more SME investment.
Delivery timetable
• The Commission should put forward a legislative proposal by mid-2021 to task ESMA with setting up the ESAP IT structure and providing ESMA with adequate ad hoc funds and resources to deliver on this project. • ESMA should identify the most suitable IT structure for the ESAP by mid-2022. • ESMA should roll out the ESAP's first stage by Q2 2023. • Following stages should be assessed after phase 1 is fully operational. Stage 2 should ideally follow by 2025. • The Commission should empower other relevant authorities to deploy stage 3 by Q2 2028.

ANNEX 12: PROBLEM DEFINITION

This annex provides a full description of the problem definition, to complement the overview given in section 2.1.

It is useful to make a distinction between problems for users of non-financial information disclosed in company annual reports, and problems for preparers of that information (that is to say, reporting companies).

1. Problems and consequences from the perspective of users of non-financial information

a. Specific problems from a user perspective

The specific problems from the perspective of users of non-financial information are:

i. Some companies from which users want non-financial information do not report such information.
ii. Many companies that do report non-financial information nevertheless do not report all relevant information that users need or want.
iii. Reported information is not sufficiently comparable.
iv. Reported information is not sufficiently reliable.
v. It is hard for users to find and exploit the information they are looking for even when that information is reported.

Each of these specific problems is described in more detail below.

i. Specific problem: Some companies from which users want non-financial information do not report such information.

NGOs and other organisations that wish to hold companies accountable for their social and environmental impacts argue that some companies do not disclose adequate non-financial information even though their impacts may be significant. For example, large non-listed companies, with the exception of banks and insurance companies, are not subject to the disclosure requirements of the NFRD even though they may have significant social and environmental impacts.[151] A very high proportion (87%) of social and environmental organisations responding to the 2020 public consultation believed that the scope of the NFRD should be expanded to include all large non-listed companies.

[151] According to estimates based on CEPS study only around 25% of other categories of large companies and 5% of SMEs publish non-financial information on a voluntary basis.

Some investors/financial market participants argue that they need information from a larger number of companies than those subject to the NFRD. For example, they may need non-financial information from smaller listed companies (not under the scope of the NFRD), to be able to assess and compare risks between listed companies. They will also need some non-financial information from companies that do not currently disclose such information in order to meet their own reporting requirements under the SFDR and Taxonomy Regulation. 70% of financial sector respondents to the open consultation believed that all listed companies should be required to disclose non-financial information, regardless of their size.

The subsidiaries of parent companies are not obliged to disclose non-financial information if the parent company does so according to the NFRD provisions on a consolidated basis. Information at the subsidiary level may nevertheless be of interest to users, either for civil society organisations who wish to know more about the impacts of a group at individual country level, or for investors considering investments in the subsidiary.

Box 1

Examples of evidence that some companies from which users want non-financial information do not report such information

- "Large private companies have considerable societal and environmental impacts. They also operate in high-risk sectors and areas of the world […] In light of this reality, there is therefore no justification for excluding privately-owned companies from these reporting obligations." *European Coalition for Corporate Justice, response to 2018 public consultation on EU framework for public corporate reporting.*

- "The scope of the NFRD is too limited, as it fails to include medium-sized companies from these reporting obligations. Increasing the pool of companies that shall do sustainability reporting will give the public and investors a broader and more adequate picture of how the market stands […]." *World Wildlife Fund, response to 2018 public consultation on EU framework for public corporate reporting.*

- "The EU rules on non-financial reporting should apply to all listed companies given the application of the taxonomy to all financial investments in the capital/financial market. Companies from sectors with a high transition risk (for example mining, carbon, smaller utilities), should also comply with reporting obligations for material risks (e.g. climate only), regardless of the size of the company." *European Banking Federation, comments on Inception Impact Assessment for review of the Non-Financial Reporting Directive, February 2020.*

ii. Specific problem: Many companies that do report non-financial information nevertheless do not report all relevant information that users need or want.

There is a large amount of evidence that many companies fail to disclose the non-financial information that users find necessary and relevant. This evidence comes from a variety of different sources, including investors, non-governmental organisations, and national supervisors and enforcement authorities.[152] In summary, the principal disclosure gaps are:

- Failure to report non-financial information that is sufficiently specific and detailed to meet user needs. The information reported is in many cases generic and summary in nature, and does not address particular issues or risks faced by the company. For example, few companies provide adequate information about their dependencies on natural capital and the implications of such dependencies for their business model and risks.

- Weaknesses in reporting of specific non-financial matters. There is evidence of gaps in reporting of relevant information on all the non-financial matters identified in the NFRD: environment (including climate), social and employee issues, human rights, and bribery and corruption. There is also evidence of gaps in reporting on risk management, on supply-chain risks, and on due diligence processes.

- In addition, it is widely recognised that information on intangible assets is underreported.[153] Investments in intangible assets often do not qualify to appear in a company's financial accounts, and this is rarely compensated by adequate reporting on such assets in other parts of the annual report, including the non-financial statement. 59% of users who replied to the consultation stated that companies should be required to disclose non-financial information on intangible assets.

- Failure to report about negative impacts and positive impacts in a balanced way, with a tendency to emphasise the positive impacts and under-report negative impacts.

[152] Examples include: *"Undue short-term pressure on corporations"*, European Securities and Markets Authority (ESMA), December 2019; *"2019 Research Report: An analysis of the sustainability reports of 1000 companies pursuant to the EU Non-Financial Reporting Directive"*, Alliance for Corporate Transparency, 2020; *"In Balance 2019 - Survey of value creation and follow-up to the Non-Financial Information (Disclosure) Decree"*, Dutch Authority for the Financial Markets (AFM), December 2019; *"Compliance by Belgian listed companies with the requirement to publish a non-financial statement"*, Belgian Financial Services and Markets Authority, March 2019; *"Integration of Sustainability into Corporate Governance: A survey of financial firms' public sustainability information"*, Finansinspektionen (Swedish Financial Supervisor), November 2018; *Ensuring the relevance and reliability of non-financial corporate information: an ambition and a competitive advantage for a sustainable Europe*, Patrick de Cambourg, May 2019.

[153] See for example: "Investment in intangible assets in the euro area" in *ECB Economic Bulletin, Issue 7/2018*, European Central Bank, 2018.

- Failure to report adequate information on the outcomes of company policies on the non-financial issues identified in the NFRD (environment, social and employee issues, human rights, and bribery and corruption). This can be linked to imprecise descriptions of company policies, which often lack measureable targets.

- Failure to link key performance indicators to the company's policies, targets or outcomes. This reduces the relevance of the reported KPIs for investment analysts and other stakeholders.

- Failure to explain potential links between non-financial and financial information, including the impacts of non-financial issues on the company. This problem tends to be exacerbated in the case of companies that publish non-financial information separately from their management report.

- The lack of adequate forward-looking information, which many users value especially highly in comparison to backward-looking, historical performance data.

- Failure to comply with the requirement in the NFRD to provide an explanation in the case that the company does not have a policy on any of the sustainability matters identified in the NFRD.

- Failure to disclose how the company has decided what information is material to its particular circumstances and should therefore be reported. 83% of users responding to the open consultation think companies reporting under the NFRD should be required to disclose their materiality assessment process.

Responses to the open public consultation show that the 72% of users consider companies do not disclose all relevant non-financial information. This problem will intensify further when the SFDR comes into force. This is because financial market participants will need investee companies to report certain specific information in order to be able to meet their own disclosure requirements under the SFDR. Of financial sector respondents to the public consultation, only 25% believed the current reporting requirements of the NFRD would ensure that investee companies report the information that financial market participants will require once the SFDR comes into force.

While users generally believe that companies fail to disclose significant amount of relevant information, companies themselves generally believe that they are at least complying with legal requirements. In the CEPS survey of companies currently under the scope of the NFRD, nearly all the surveyed companies stated that they report on their business model, environmental, social,

human rights, anti-corruption and bribery matters as required under the NFRD. Around half of surveyed companies stated that they report on all required matters to the full extent and nearly one-third of the companies stated that they report on all the matters to a high extent. Only a marginal share of companies (1%–3%) stated that they do not report at all on one of the five matters.

Companies that only publish non-financial information in reports that are separate from the management report are less likely to explain the connections between the financial and non-financial information that they are reporting. The separate publication of financial and non-financial information therefore prevents investors from receiving an integrated and coherent overview of the risks facing the company. At the same time, the strategic importance of synergies between financial and non-financial information is growing rapidly, as the interactions between sustainability and company value become ever more evident. Companies that publish financial and non-financial information together in the same report are more likely to provide users with relevant information about how non-financial risks and performance might influence the future value of the company.

Whether a company reports against a recognised reporting standard, is a useful proxy for assessing the relevance reported information. Based on CEPS study, we estimate that only around 20% of large limited liability companies in the EU comprehensively apply recognised reporting standards.

Box 2

Examples of evidence that companies do not report all information that users consider relevant

- "Some companies create links between the information provided in their non-financial statement and that included in other parts of the annual financial statement, thereby making the latter more consistent and logical. Too few such links have, however, been established to date between financial and nonfinancial information. *"Compliance by Belgian listed companies with the requirement to publish a non-financial statement"*, Belgian Financial Services and Markets Authority, March 2019.

- A report on human rights reporting by French companies found that 18 out of 20 companies analysed did not identify their salient human rights issues (i.e. the human rights at risk of the most severe negative impact through the company's activities and business relationships). *Human Rights Reporting in France, Shift, 2018.*

- 60% of institutional investors responding to an EY survey believed that companies do not disclose ESG risks that could affect their business and that they should disclose them more fully. This represented an increase of 21 percentage points on the previous survey. *EY survey of institutional investors, EY, 2017*

iii. Specific problem: Reported information is not sufficiently comparable.

One of the most frequent complaints from users of non-financial information is that reported information is not easily comparable between companies. Respondents to the 2018 Fitness Check public consultation were significantly less optimistic about the impacts of the NFRD on the comparability of non-financial information compared to its impacts on other characteristics of that information (e.g. material, timely). Similarly, respondents to the 2020 public consultation believed that limited comparability was a bigger problem that the limited reliability of reported information or than the non-reporting of relevant information. The great majority of users (84%) believed that the limited comparability of information is a problem, and only 3% of users believed is *not* a problem.

Comparability is critical in certain circumstances, especially when comparing the risks of different investments. Without comparable information from different companies, the value of information from any one company is greatly reduced. Comparability is especially important between companies in the same economic sectors.

The problem of comparability manifests itself in different ways. It may arise when one company reports a certain piece of information but another company does not disclose that same information. It may result from differences in the methodologies used by different companies to report data on the same issue (e.g. different methodologies to report a KPI on environmental impact). In addition, differences in presentation of data can hamper comparability.

Box 3

Examples of evidence that reported information is not sufficiently comparable

- 48% of a sample of 100 European investors from France, Germany, Italy, Spain, and the U.K say that obtaining consistent and comparable historical data is a big challenge. *"The Sustainability Imperative: Business and Investor Outlook 2018"*, Bloomberg Sustainable Business & Finance Survey.

- An analysis found 20 different ways companies report their employee health and safety data, and showed that these inconsistencies lead to significantly different conclusions when looking at the same group of companies. *"Four Things No One Will Tell You About ESG Data"*, Journal of Applied Corporate Finance 31 (2), Spring 2019, pages 50-58. Sakis Kotsantonis and George Serafeim.

- "The lack of consistent methodologies and reporting standards, and mixed evidence of performance make it challenging for investors to incorporate ESG principles into their investment process." *October 2019 Global Financial Stability Report (GFSR)*, International Monetary Fund.

iv. Specific problem: Reported information is not sufficiently reliable

The value of non-financial reporting is closely linked to the extent to which users trust the information reported. While users generally have confidence in the accuracy of financial information reported by companies, they tend to have less confidence in reported non-financial information. A number of analyses have pointed to the limited reliability of non-financial information as one of the reasons why such information often fails to meet the needs of the intended users.[154]

The publication of non-financial information in a separate report, instead of in the management report, can impact negatively on the perceived reliability of the information if it gives the impression that the company board attaches less importance to non-financial reporting.

73% of users who responded to the open public consultation believe that the limited reliability of non-financial reported information is a problem. Moreover, 69% of users responding to the consultation believe the existing differences between financial and non-financial information are not at all justifiable or are justifiable only to small extent, compared to 34% of respondents believe differences are justifiable.

Based on CEPS study, we estimate that only around 30% of large limited liability companies in the EU publish non-financial information that has been assured to a minimum level.

Box 4

Examples of evidence that reported information is not sufficiently reliable

- "One implication of our study is that policy-makers need to consider whether existing NFD requirements will lead to the provision of information of sufficient quality. To enhance quality, policy makers could require companies to undertake external assurance of the information disclosed. The importance of rigorous independent verification processes, designed to reassure stakeholders about the credibility, completeness and materiality of the social information reported, has been stressed in various previous studies […]" *"Mandatory Non-financial Disclosure and Its Influence on CSR: An International Comparison", Jackson, G., Bartosch, J., Avetisyan, E. et al. Journal of Business Ethics (2019)*

- "[… N]ow that there are legal requirements for financial market participants to disclose the ESG risks and factors of their financial products based on data sourced from issuers of the instruments underlying the financial products, mandatory third-party assurance around such data would be critical. It would help enhance the quality and credibility of the non-financial information reported by issuers and consequently by financial product manufacturers and distributors. As a result, this would help decrease the risk of mis-selling and greenwashing for investors."

[154] For example: *"Undue short-term pressure on corporations",* European Securities and Markets Authority (ESMA), December 2019; *"Social and environmental value creation",* Association of Chartered Certified Accountants, 2019.

Association for Financial Markets in Europe (AFME), response to 2020 open public consultation on the revision of the NFRD.

- "Bringing assurance as to the quality of the non-financial information reported is essential. As a consequence, external control of non-financial information by third-party verification providers should be mandatory throughout the EU and those third-party verification providers should certify the information." *Finance Watch, response to 2020 open public consultation on the revision of the NFRD*

v. Specific problem: It is hard for users to find and exploit the information they are looking for even when that information is reported.

There are a number of reasons why users often experience difficulties in finding the non-financial information they are looking for even when that information has been reported. Firstly, many reporting companies disclose significant amounts of information that users consider not to be relevant alongside the information that they do consider relevant. Typical examples of less relevant information are descriptions of the company's philanthropic activity, or performance indicators that are not critical to understanding the company's principal impacts or risks (e.g. a bank reporting on its paper consumption). The reporting of such information increases the overall volume of reports, meaning that users must spend more time and resources finding the information that they do consider relevant. 59% of users who replied to the open public consultation face difficulties finding the reported information.

Secondly, non-financial information is not sufficiently digitalised, which hinders users' access to and the usability of the reported information. There is no widely accepted IT taxonomy for non-financial information that would enable digital tagging.[155] This in turn limits the extent to which non-financial information machine-readable. In addition there is no single data space that provides easy access to all non-financial information reported by companies. The limited digitalisation of non-financial information exacerbates the other problems that users experience in terms of finding and exploiting reported non-financial information. According to the results of the open publication, 77% of users agree that it would be useful to require the tagging of reports containing non-financial information and 79% of users agree that non-financial information should be available through a single access point.

Thirdly, companies present their non-financial information in different formats rather than according to a standard format. For example, while some companies present a summary list of

[155] 'Taxonomy' is the technical term used for IT systems (categorisation system). It does not refer to the new taxonomy of sustainable economic activities established by the Taxonomy Regulation.

KPIs in one place, many present KPIs throughout their report with no summary list.[156] The greater the variety between companies in terms of structuring their non-financial information, the greater the difficulty for users in finding and using the information they need.

Finally, companies often divide their non-financial information between different publications, meaning that some users may have difficulty in finding all the information they are looking for in one place. This may be the case when companies publish some non-financial information in the management report, and also publish a separate sustainability or corporate social responsibility report. According to the public consultation, a substantial majority of users (58%) say that non-financial information published in a separate report is hard to find.

In addition, the exemption of subsidiaries from the reporting obligations of the NFRD if the parent company is subject to the NFRD provisions on consolidated reporting, makes it difficult for users to identify the reporting parent company and to find the non-financial information it publishes.

b. How do the problems of NFR reporting vary across the EU?

According to the 2019 report by the Alliance for Corporate Transparency, the quality of non-financial reporting by companies from the Eastern European region was worse than that of companies from other regions on most criteria. The reporting of companies from the Eastern European region was especially weak with regard to climate and human rights.

This statement is consistent with the research conducted by Polish Institute for Human Rights and Business as part of the Valuing Respect Project led by Shift. According to the latter, information provided and the way it is presented make it also rather doubtful that the company is using it in a strategic way to inform its further actions. At times, the user is also not sure if the company is actually measuring anything that would be useful to advance it on its quest to be better. Finally very low number of companies actually reports on risks in a specific way. With few exceptions amongst the 107 reports examined, even those companies reporting on risks approached this issue as risks to company and not risks to people.

The key points from PIHRB research in 2017 into the current use of metrics regarding human rights in NFR are: 1) Company reporting is focused on input, activity and output data with 79% of all information falling into these indicator categories. Detailed information about inputs and activities is rarely provided. 2) With regard to outputs, which are the dominant category of indicators, about 88% of these are reported in numerical form. They are often presented as a

[156] "Only 21.9% of companies provide their KPIs in summarised statements. The absence among four fifths of all companies of such a summary significantly undermines the practical usability of their reports." – *"2019 Research Report: An analysis of the sustainability reports of 1000 companies pursuant to the EU Non-Financial Reporting Directive"*, Alliance for Corporate Transparency, 2020.

snap-shot for the reporting period, without a narrative of what the company concluded or did as a result of that data. PIHRB considers that this might reflect that data included in monitoring and reporting is driven more by external requirements than by the perceived value of the data for business decision making.

The CEPS study carried out in preparation of this impact found that companies in central and Eastern European Member States were more likely to perceive non-financial reporting as a communication exercise than as a strategic document reflecting the company's approach to sustainability. They were also less likely to understand the concept of the 'double materiality perspective' (the obligation to report information on how non-financial issues effect the company and the impact of the company itself on society and the environment).

According to the 2019 report by the Alliance for Corporate Transparency , the key trend is that in most categories Nordic companies tend to be among regions that report more specific information than others, whereas Eastern European companies lag behind. The exception is a very low rate of disclosure of integration of ESG criteria in executive remuneration in the Nordic region. Since this is not in line with any other data, it is likely a result of specific corporate governance or disclosure traditions.

According to the same report, in some countries such as France, in addition to the NFR Directive, companies are subject to more detailed requirements on climate change disclosures. So that, in general, French companies provide noticeably information on their strategy and they also often describe how they integrate ESG criteria in the executive remuneration. This suggests that clear reporting requirements result in the disclosure of relevant data

It is worthy to mention the 2019 Spanish report by the Alliance for Corporate Transparency and Sustentia which analyse sustainability reports of 67 Spanish companies. According to the latter, Spanish companies present better results in several indicators than European companies in most cases, however this information is formal and not very material. In other words, there are significantly more Spanish companies that report on their commitments on climate change, use of natural resources, respect for human rights or anti-corruption. However, the percentages are similar to those in Europe when we focus only on those companies that report on the key aspects and objectives of these policies.

Something similar occurs with the information on the results of the policies where only 10% of Spanish and European companies provide results that allow understanding the degree of compliance with the objectives and goals established by the policies. However, it is important to note that regarding certain indicators that are specified by the national Law, there are many more Spanish than European companies that provide data, for example the wage gap between men and women (Spain 72%, average European 24%). As in the case of France, a clear reporting requirements result in the disclosure of relevant data.

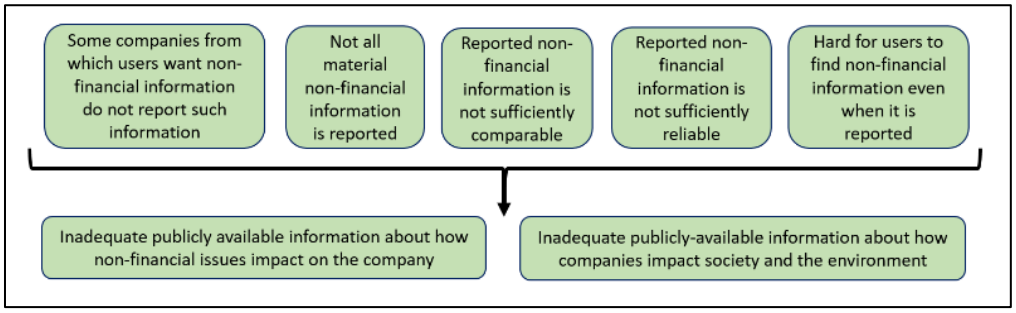
c. General problems from a user perspective

The specific problems described in point (a) above create the following general problem from the user perspective: users do not have access to adequate information about how non-financial issues, and sustainability issues in particular, might impact companies, or about how the company itself impacts society and the environment:

- General problem: Users do not have access to adequate publicly-available information about how non-financial issues, and sustainability issues in particular, might impact companies. This information is of most interest to investors / financial market participants, who wish to understand and compare the financial risks of different companies.

- General problem: Users do not have access to adequate publicly-available information about the potential and actual impacts of companies on society and the environment. This information is of interest both to NGOs and to investors/financial market participants. NGOs and other organisations want to have such information in order to hold companies accountable for their social and environmental impacts. Investors/financial market participants may want this information either to fulfil their own legal requirements under the Sustainable Finance Disclosure Regulation (SFDR) and the Taxonomy Regulation; and/or because they are marketing a 'sustainable' financial product and therefore need information about the social and environmental impacts of companies financed by that product.

The specific and general problems from a user perspective



Overall, "there is a growing expectation gap between users and providers of ESG information."[157] The investor demand for sustainability and other non-financial information has

[157] *Undue short-term pressure on corporations*, ESMA, December 2019

been growing fast and is predicted to increase further.[158] These specific problems are therefore highly likely to intensify (see section 2.3 "How will the problems evolve?").

Added to the increasing demands for non-financial information from investors is accompanied by other legislative requirements that companies must comply with, such as the SFDR for financial market participants, or the Taxonomy Regulation. Under this context, 69% of the financial sector respondents to the public consultation believe the current NFRD requirements do not ensure, or to a small extent, that investee companies report the information required by the financial sector to meet the new disclosure regulations.

d. Consequences of problems from a user perspective

The specific and general problems from a user perspective have a number of consequences, which vary depending on the potential users of the information.

i. Consequences of inadequate information for investors.

The lack of adequate non-financial information means that investors are unable to take sufficient account of sustainability-related and other non-financial risks and opportunities in their investment decisions. This has the potential to create systemic risks that threaten financial stability. It is for this reason that central banks, in the G20's Financial Stability Board, launched the Task Force on Climate Related Financial Disclosures (TCFD) in 2018. Their aim was to improve reporting by companies on the financial implications of climate change and thereby reduce systemic risk.

Analysis by the European Central Bank shows that climate change-related risks have the potential to become systemic for the euro area, in particular if markets are not pricing the risks correctly.[159] The Network of Central Banks and Supervisors for Greening the Financial System (NGFS) has recognised that there is "a strong risk that climate-related financial risks are not fully reflected in asset valuations."[160] To help address this risk, the NGFS endorses the TCFD disclosure framework, and recommends that policy-makers and supervisors support the development of an internationally consistent environmental disclosure framework.

In November 2020 the Financial Stability Board published a report on the implications of climate change for financial stability.[161] The report states that "the breadth and magnitude of climate-

[158] See for example *Stakeholder Perceptions of Non-Financial Reporting*, UK Department for Business, Energy and Industrial Strategy, 2019: "There was also a consensus that non-financial reporting is becoming and will be increasingly important in the future as investors become more engaged with non-financial risks."
[159] "Climate change and financial stability" in *Financial Stability Review*, European Central Bank, May 2019.
[160] *A call for action Climate change as a source of financial risk*, Network for Greening the Financial System, April 2019.
[161] *The Implications of Climate Change for Financial Stability*, Financial Stability Board, November 2020.

related risks" might make the effects of these risks "more pernicious than in the case of other economic risks", and that "the interaction of climate-related risks with other macroeconomic vulnerabilities could increase risks to financial stability". The report goes on to point out that, "even where individual financial firms take actions to mitigate risks, climate-related risks to financial stability might be sustained by a lack of disclosure by financial firms of their own financial exposures to climate-related risks and risk management processes."

The financial risks at stake from sustainability issues are considerable, and are by no means limited to climate change. The Netherlands National Bank estimates that the Dutch financial sector's exposure to the most water-scarce regions in the world is EUR 97 billion, and highlights significant financial risks arising from human rights issues and biodiversity loss.[162] The World Economic Forum has concluded that USD 44 trillion of economic value generation (over half of global GDP) "is moderately or highly dependent on nature and its services and is therefore exposed to nature loss".[163]

Building on the experience of the TCFD in the climate field, the creation of Taskforce for Nature-related Financial Disclosures (TNFD) is now being considered, with the aim of creating a framework for the reporting of financial risks that result from biodiversity loss and from companies' dependencies on natural capital.[164] The fact that a number of major banks and asset managers have joined the TNFD is further evidence that the demand from financial markets for better information extends beyond just climate-related risks to encompass the broader sustainability agenda. In a speech to the One Planet Summit in December 2020, the chair of the NGFS indicated that the network will increasingly consider the implications of biodiversity loss in its future work.[165]

The evidence shows that most individual companies fail to report adequately on their sustainability-related risks, including on their dependencies on natural capital (see section (a) above, "Specific problems from a user perspective"). This means that individual investment decisions cannot take such risks into account. The potential for systemic risks across the financial system is accentuated by the accumulation of individual investments that are made without adequate regard for sustainability-related financial risks. The lack of adequate information on intangible assets further limits the ability of investors to make judgements about risks and opportunities. According the European Financial Reporting Advisory Group (EFRAG) this lack of information can have adverse economic impacts in terms of: the level of information asymmetry concerning a firm (volatility of share prices and insider trading); the accountability of

[162] *Values at risk: Sustainability risks and goals in the Dutch financial sector*, De Nederlandsche Bank (Dutch National Bank), 2019
[163] *Nature Risk Rising: Why the Crisis Engulfing Nature Matters for Business and the Economy*, World Economic Forum, 2020
[164] https://tnfd.info/
[165] Source "Environmental Finance", subscription required.

management for actions/decisions in managing the firm's resources; and the lack of data for analysis and rational external resource allocation and investment decisions.[166] Investment in intangible assets currently represents the majority of investment carried out by the private sector in advanced economies.[167] Intangible assets to some extent help to explain the widely recognised gap between the accounting book value of many companies and their market valuation. In many sectors of the economy, for example information technologies, this gap is widening.[168] Since traditional financial accounting cannot adequately reflect all intangible assets, it becomes ever more important that companies include information about intangible assets in their non-financial reporting.

In addition to contributing to systemic financial risks, the lack of adequate non-financial information from companies hinders the ability of the financial system to channel more financial resources to companies and economic activities that address and do not exacerbate social and environmental problems.[169] If investors do not have adequate information about the social and environmental impacts of investee companies then by definition they cannot make decisions that take such impacts into account. Recently agreed legislation, in particular the SFDR and the Taxonomy Regulation, aims to address this problem, but depends for its success on more and better non-financial information from companies.

The overall consequence is that the financial system cannot play the positive role that it needs to play in the urgent transition to a sustainable economic system. The lack of adequate non-financial information from investee companies contributes to a misallocation of capital: too many resources flow to economic activities that have negative social and environmental impacts, while too few resources flow to activities that have positive impacts. This will significantly constrain the ability of the EU as a whole to meet the objectives of the European Green Deal, including a just transition, and to achieve the UN Sustainable Development Goals.

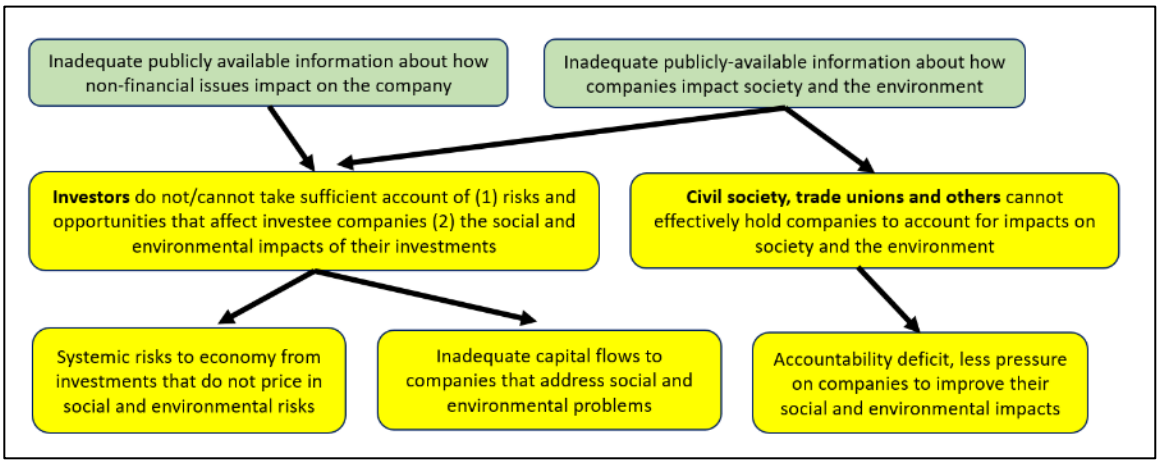
ii. Consequences of inadequate information for NGOs, trade unions and others.

Civil society organisations and trade unions want non-financial information from companies to be able to better hold companies accountable for their impacts on society and the environment. Inadequate transparency from companies can therefore create an accountability deficit. It reduces the pressure on companies to identify, prevent and mitigate any negative impacts they have,

[166] *Academic Report: a Literature Review on the Reporting of Intangibles*, EFRAG, February 2020
[167] *Productivity and secular stagnation in the intangible economy*, Jonathan Haskel, Stian Westlake, 31 May 2018
[168] *Ensuring the relevance and reliability of non-financial corporate information: an ambition and a competitive advantage for a sustainable Europe*, Patrick de Cambourg, May 2019
[169] The High Level Group on Sustainable Finance (2018) identified two imperatives for sustainable finance: "The first is to improve the contribution of finance to sustainable and inclusive growth as well as the mitigation of climate change. The second is to strengthen financial stability by incorporating environmental, social and governance (ESG) factors into investment decision-making."

since the reputational risks of such impacts are less. The accountability deficit created by inadequate transparency may also undermine citizen trust in business, especially in larger companies. In this sense, it may be a contributory factor in the weakening of the social contract between business and citizens, with effects on the efficient functioning of the social market economy.

Consequences of problems from a user perspective



e. Implications of Covid-19 pandemic for the problem definition

The Covid-19 pandemic directly underlines the exposure of companies to non-financial risks. This is especially the case of companies who business models are dependent on the global movement of goods and persons. Companies can expect that investors and supervisors will now require significantly enhanced reporting about such risks. This change will materialise at the very least from the 2021 reporting cycles, and for many companies it is already a reality.

Some observers predict that the pandemic will in particular lead to a greater demand for social and worker-related information. To date the investment community has tended to pay more attention to environmental information, and especially climate-related information, than to social information. It is notable that the European Investment Bank and the European Bank for Reconstruction and Development have published new guidelines regarding the sustainability risks of investments in the context the pandemic, and both have a strong emphasis on the social and worker-related issues, including workers in supply chains.

A number of recent analyses have suggested that the pandemic will drive the growth of ESG investing. For example, a JP Morgan survey of investors found that 55% see the pandemic as a positive catalyst for ESG investing in the next three years, while only about a quarter (27%) expect a negative impact and 18% believe it will be neutral. A study published by the European Capital Markets Institute finds that "companies integrating an ESG approach recognised by

investors and ESG funds have been more resilient in the crisis", and goes on to conclude that "investors' taste for ESG has not lessened during this crisis – quite the opposite, in fact."

More generally, the pandemic may contribute to a greater awareness of the complex interactions between environmental degradation, social problems and the health of the economy. One informed analyst has stated that "the pandemic and the health crisis now ravaging all continents has put the spotlight on vulnerabilities and our dependence on the natural environment. It drives home the message that markets do not operate in isolation, but instead are embedded in societies and the natural environment. This realization will fundamentally change our long-term risk perspective and the way we prepare for the looming climate crisis."

If the pandemic indeed contributes to a further growth in ESG investing and to an acceleration of the paradigm shift towards a sustainable economy, then it will further accelerate the growth in demand for more and better non-financial information from companies on the part of the investors and other stakeholders.

2. Problems and consequences from the perspective of preparers (reporting companies)

a. Problems from a preparer perspective

The problems from a preparer perspective are:

i. Preparers face difficulty and complexity when deciding what information to report.
ii. Preparers find it difficult to get the non-financial information they need from suppliers, clients and investee companies to report adequately.
iii. Preparers receive information requests from stakeholders in addition to the information they report to fulfil their legal requirements.

These specific problems are described in more detail below.

i. Specific problem: Preparers face difficulty and complexity when deciding what information to report.

Companies frequently state that they find it difficult to decide what information they should report. The reporting requirements of the NFRD, as transposed into national law, remain high level and principles-based, meaning that companies must decide what information to report in their particular circumstances. Companies invest considerable time and resources in consulting multiple different standards and sets of guidance, and have to make difficult judgements about whether and to what extent they should use each one. Many companies pay consultants to assist with this task.

The CEPS survey of companies under the scope of the NFRD found that for about half of the companies, the selection of material information to disclose does not pose any particular difficulty, and for about 20% of the companies, choosing the information to disclose is easy (easy and very easy). For one-third it is considered difficult (difficult and very difficult). In response to the open public consultation, 38% of preparers said that they face uncertainty and complexity when deciding what non-financial information to report.

This problem appears to be more problematic for smaller companies under the scope of the NFRD, which have relatively less internal capacity and expertise in the field of non-financial reporting. In the CEPS survey, the share of smaller listed companies having difficulties in choosing information was almost twice as high as that of bigger listed companies. The CEPS study also found that as companies gain more years of experience in non-financial reporting, fewer of them experience difficulties in choosing what information to report.

This problem appears to have worsened in recent years, as users and supervisors pay more attention to the content of non-financial reports, and as the number of existing standards, frameworks and other guidelines has grown.

At the same time, many companies state that they appreciate the flexibility of the reporting requirements in the NFRD. They support the fact that the NFRD does not impose a detailed "one-size-fits-all" reporting obligation on all companies regardless of their particular circumstances. They stress the importance of only being obliged to report material information, and they defend the principle that reporting companies themselves should make the initial judgement about what information is or is not material.

These problems were observed in the responses of the open public consultation where 69% of preparers of non-financial information indicate that there is a need to streamline different pieces of legislation, 44% indicate there are gaps and 22% indicate there is an overlap between different legislations.

Examples of evidence that preparers face difficulty and complexity when deciding what information to report.

- A survey of 55 listed Polish companies showed that 55% find it rather difficult or very difficult to decide what non-financial information to report. *Results of survey conducted by the Polish Association of Listed Companies, data gathered and analysed by the Foundation for Reporting Standards, September 2019, Author: Piotr Biernacki*

- "Companies struggle to provide consistent, comparable and reliable non-financial information as hundreds of frameworks have emerged and none of them covers the full width of non-financial reporting. Many of the frameworks overlap and it remains unclear how meaningful

the differences between the frameworks are. This poses a major challenge for companies that want to report nonfinancial information." "*Green paper: Towards a global standard setter for non-financial reporting", EUMEDION (Dutch Corporate Governance Forum), October 2019.*

- One of the principle conclusions of an extensive consultation process carried out by the World Economic Forum concerns the complexity and burden of ESG reporting, in particular that companies face hurdles in navigating reporting standards. *"Seeking Return on ESG Advancing the Reporting Ecosystem to Unlock Impact for Business and Society", World Economic Forum, 2019.*

ii. Preparers find it difficult to get the non-financial information they need from suppliers, clients and investee companies to report adequately.

To adequately report on their material risks and impacts, many companies need corresponding information from other companies with whom they do business. For example, a food retailer might need information from its suppliers about the social conditions and environmental impacts of the agricultural production. Banks and other investors might need information about the impacts of the companies and activities they finance.

The CEPS survey of companies under the scope of the NFRD found that just over one third of companies requested additional information from their suppliers and/or clients as a result of the NFRD disclosure obligations.

The extent to which a company's business partners (suppliers, clients, investee companies) do or do not collect and publish relevant non-financial information therefore has a significant impact on the costs and burden of non-financial reporting. In response to the open public consultation, about half of preparers stated that they experienced significant difficulties in finding relevant information from business partners. Only 2% of preparers responding to the consultation stated that this was not at all a problem.

iii. Preparers receive information requests from stakeholders in addition to the information they report to fulfil their legal requirements.

European companies often have to dedicate significant time and resources to answering specific request for non-financial information, independently of any information they may disclose as a result of obligations under the NFRD.[170] These requests come principally from those sustainability rating agencies, data providers and research providers who do not exclusively rely

[170] These requests may come in the form of questionnaires, requests for feedback or formalised engagement (meetings/calls). Many data providers have formal systems set up for companies to share updates, or point out inaccuracies in their data.

on public data,[171] who then usually sell this information on to investors.[172] Some requests also come from civil society organisations and platforms. Companies that do not respond to such requests run the risk of exclusion from certain indices or ratings, or research, with possible consequences in terms of access to capital. They also run the risk of being rated poorly, or labelled as not sustainable and/or not transparent.[173]

The number and complexity of these additional information requests has grown considerably in recent years. Anecdotal evidence from one business association suggests that responding to the most demanding questionnaire from one sustainability rating agency can take up to 100 days for a full-time employee. Some sustainability rating agencies send pre-filled questionnaires, reducing burden on the companies. However, the format and precise nature of the data requested by each request tends to vary, meaning that companies must respond to each one individually, which further adds to the burden.[174] Companies have also problems understanding which requests come from the sustainability rating agencies and which come from other entities.

Responses to the open public consultation indicate that 64% of preparers of non-financial information agree that they are under pressure to respond to individual demands for non-financial information from different stakeholders (including sustainability rating agencies, data providers, and civil society organisations).

Evidence that preparers receive many information requests from stakeholders in addition to the information they report.

- Listed European companies "are confronted with numerous questionnaires and ratings, based on different methodologies and definitions." *EuropeanIssuers, feedback to Inception Impact Assessment, February 2020*

- "Issuers need to devote considerable time and expense to providing responsive data for these surveys [from sustainability rating agencies and data providers], checking for accuracy and follow-up." *Towards a Common language for Sustainable Investing", BlackRock, January 2020*

[171] Preliminary results of SustainAbility study show that only two notable data providers do not engage with companies. Research by Environmental Finance states that "companies complain about the growing number of questionnaires they are being asked to respond", June 2019.

[172] Investors in its broader sense, includes as well asset managers. In particular, asset managers who actively manage portfolios need data from companies rather than from intermediaries, as it allows them to better understand the specificities of companies and carry out their own analysis. It is crucial that they have access to reliable, comparable and granular data published by companies as active managers lead the changes in the capital allocation and therefore (SustainAbility study).

[173] As larger companies have larger resources, this leads to the assumption that larger companies have an advantage in providing more or better ESG data. This is strengthened by research that shows that large-cap companies have significantly higher ESG disclosure scores than mid-cap companies, *Drempetic, S., Klein, C. & Zwergel, B. The Influence of Firm Size on the ESG Score: Corporate Sustainability Ratings Under Review. J Bus Ethics (2019).*

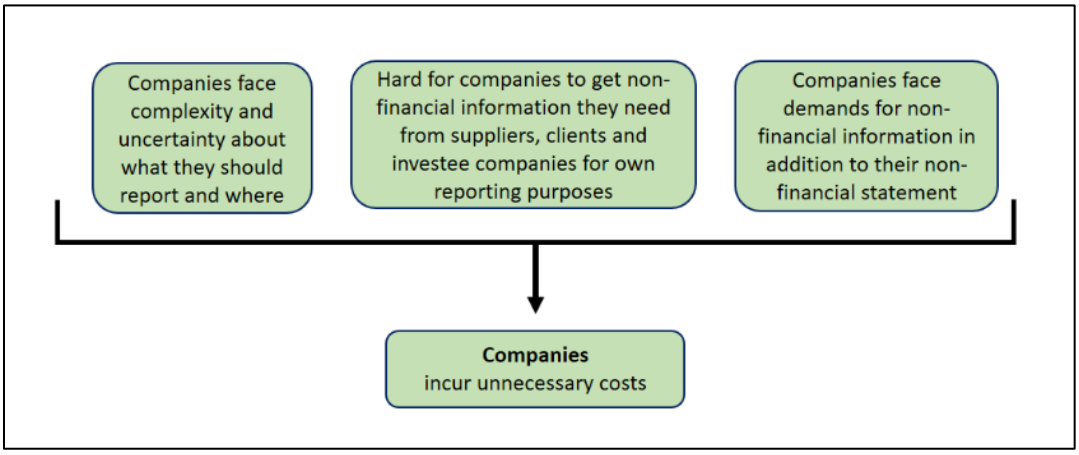
[174] Estimated costs from filling in these questionnaires amount to EUR 170 – 290 million per year for the current NFRD population (including national transposition), EUR 25 000 per company per year. This calculations are based on the replies to the survey carried out by SustainAbility. See annex 17 for a detailed cost analysis.

- A survey found that 46 out of 55 listed Polish companies received direct requests for non-financial information in addition to any information they published further to their obligations under the NFRD. *Results of survey conducted by the Polish Association of Listed Companies, data gathered and analysed by the Foundation for Reporting Standards, September 2019, Author: Piotr Biernacki*

b. Consequences of problems from a preparer perspective

The consequence of the problems from a preparer perspective described in section (a) above is that companies face unnecessary costs.

Problems from a preparer perspective



ANNEX 13: DESCRIPTION OF PRINCIPAL PRIVATE INTERNATIONAL NON-FINANCIAL REPORTING FRAMEWORKS AND STANDARDS

This annex presents some of the most used standards or frameworks to report ESG matters. It includes a detailed description of: the Global Reporting Initiative (GRI); the Sustainability Accounting Standards Board (SASB); the International Integrated Reporting Council (IIRC); the CDP (formerly Carbon Disclosure Project); and the Task Force of Climate-related Financial Disclosures (TCFD). In 2020, the IIRC and SASB announced their intention to merge, creating a new body that will be called the Value Reporting Foundation.

Other important initiatives not described in detail in this annex include the Climate Disclosure Standards Board (CDSB) and the UN Guiding Principles Reporting Framework (for the UN Guiding Principles on Business and Human Rights). Examples of national standards include the Standard Informacji Niefinansowych (SIN), which is widely used by listed companies in Poland, and the Sustainability Code of the German Council for Sustainable Development (RNE).

The domain of non-financial reporting standards and frameworks is dynamic, and new initiatives continue to emerge. For example, in January 2020 the World Economic Forum launched a consultation to develop a common, core set of metrics and recommended disclosures. In March 2021 the IFRS (International Financial Reporting Standards) Foundation, further to the results of a public consultation, announced its intention to establish a sustainability standards board (SSB). The plans of the IFRS Foundation are supported by the Financial Stability Board and by the International Organisation of Securities Commissions (IOSCO), amongst others. The initial focus of the SSB is expected to be on climate reporting from a financial materiality perspective, building on the recommendations of the TCFD.

The GRI, SASB, IIRC, CDP and CDSB have sought to enhance their cooperation through the publication in September 2020 of a shared vision for a comprehensive corporate reporting system. In December 2020 they published a prototype climate-related financial disclosure standard that illustrates this shared vision could be applied in practice to climate reporting.

This annex is structured in a way to show an overall description of the standard/framework (including general information on establishment, location, objective, etc.); their scope (e.g. what issues each covers); the materiality and their target audience; and the estimated number of users. Figure a. shows a summary of the main attributes each of the frameworks and standards that are reviewed in this annex has, facilitating a comparison among them. A similar table containing a more extensive list of reporting initiatives and different attributes was developed by the TCFD

and may be found under the Appendix 4 of the Recommendations of the Task Force on Climate-related Financial Disclosures.[175]

[175] "Recommendations of the Task Force on Climate-related Financial Disclosures." 54. Task Force on Climate-related Financial Disclosures. 2017.

Figure 1 - Summary of Frameworks

Framework/Standard / Attribute	**GRI Standards**	**IIRC Framework**	**TFCD Recommendations**	**CDP System**	**SASB Standards**
Target reporter	Any company, organisation, or public authority.	Public listed companies.	Any company (specially owning public debt/equity).	Any company, organisation, or public authority.	Any company.
Target Audience	Investors, customers, governments, other providers of financial capital, and NGOs.	Providers of financial capital. Also addresses the preparers of information.	Institutional Investors, lenders, insurance underwriters, and preparers of information.	Financial, business, academic, and policy communities and civil society.	Investors and consumers
Materiality	Mainly social & Environmental (inside-out)	Financial (outside-in) and some elements of Social & Environmental materiality	Financial (outside-in)	Financial (outside-in) and Environmental (inside-out)	Financial (outside-in)
ESG Scope	ESG	ESG topics and other non-financial information (e.g. manufactured, social, intellectual capitals)	Climate	Environmental (Climate change, water issues, and deforestation)	ESG issues (Industry specific)
Estimated percentage of users in CEPS study survey*	64%	11%	15%	29%	3%

**The CEPS survey was addressed to all companies under the scope of the NFRD. 188 companies responded to the survey. The percentage shown in this table is the percentage of respondents who said they used the standard or framework in question to a full or to a high extent.*

As it may be observed in Figure a., the five most used initiatives to report non-financial information vary regarding the target audience they are trying to reach. Additionally, the materiality concept for each initiative is not always the same and none of the five initiatives, standing-alone, fully applies a *double-materiality persepctive*. Lastly, the scope these five initiatives have regarding sustainability and non-financial topics varies largely: from the most narrow and specific (TCFD and CDP) covering a limited set of environmental issues, to a framework (IIRC) that widens the scope of non-financial issues to include social and relationship, manufactured, and intellectual capitals.

1. Global Reporting Initiative (GRI) Standards

1.1 Description of framework

The GRI is a private initiative organisation formed in 1997 in Boston, USA and was part of the Coalition for Environmentally Responsible Economies (CERES). In 2001, the GRI was formed into a separate, independent non-profit organisation. In 2002, the GRI relocated to Amsterdam and since then has served a growing international audience. In the past 13 years, the GRI was "eager to start establishing a regional presence in key territories […]" and opened "Focal Points" (i.e. regional offices) in Brazil, Australia, China, India, USA, South Africa, and Colombia.[176][177] The objective of these Focal Points is to facilitate and promote the active engagement of local organisations and to make sustainability reporting regionally and globally a standard practice.

The main objective of the GRI is to help "businesses and governments worldwide understand and communicate their impact on critical sustainability issues such as climate change, human rights, governance and social well-being."[178] The GRI identified 4 main focus areas to reach such objective, being: 1) creating standards and guidance to advance sustainability development, 2) harmonise the sustainability landscape, 3) lead efficient and effective sustainability reporting, and 4) drive effective use of sustainability information to improve performance.[179] Also through a common set of standards, the GRI enhances the global comparability and quality of the impacts companies have on ESG topics across regions.

From year 2000 through 2013 the GRI has published 4 generations of guidelines (G1, G2, G3, and G4). Subsequently, in 2016, the GRI "launched the first global standard for sustainability reporting".[180]

[176] GRI . 2020. *GRI'S History.*
[177] GRI. 2020. *About GRI*..
[178] Ibid.
[179] Ibid.
[180] GRI . 2020. *GRI'S History*.

1.2 Scope in content

The GRI standards are grouped into four series: one universal series including foundations, general disclosures, and management approach; and three separate and specific standards series, including i) economic, ii) environmental, and iii) social topics. In total, the GRI has developed 37 individual standards intended to work together to help organisations prepare a sustainability report based on the GRI's reporting principles for material topics.[181]

By having a standardised and comparable way of reporting material topics, the GRI aims to allow comparison between companies from different sectors (e.g. biodiversity, human rights, occupational safety, etc.).

1.3 Materiality and target audience

The GRI standards are intended for organisations to report about their impacts on environment, society, and/or the economy,[182] i.e. social and environmental materiality. The GRI standards do not directly consider financial materiality (i.e. the impact the environment, economic, or social matters may have on the financial performance of the organisation). The GRI acknowledges, however, that social and environmental impacts may already be financially material at the time of reporting, or may become financially material over time.[183]

The target audience of the GRI reports is deliberately wide, and includes investors, customers and consumers, governments, other providers of financial capital, and NGOs.

1.4 Number of users

According to the survey of companies under the scope of the NFRD carried out by CEPS as part of its study, it was determined that of 188 respondents, 64% use the GRI to the full or a high extent, while 19% either use GRI to a limited extent or do not use GRI at all.

In 2017, KMPG estimated that 89% of the largest 250 companies in the world report sustainability using some guidance from the GRI (either guidelines or standards)[184][185]. According to Accountancy Europe companies in some countries of the EU (Belgium, Italy, and Spain), use the GRI standards as the preferred framework to report sustainability information as required by the NFRD transposition in their local legislations.[186]

[181] "GRI 101: FOUNDATION 2016." 3. GRI Standards. 2018.
[182] Ibid., 10.
[183] https://www.globalreporting.org/information/news-and-press-center/Pages/Promoting-clarity-and-compatibility-in-the-sustainability-landscape.aspx
[184] "The KPMG Survey of Corporate Responsibility Reporting 2017." 28. KPMG. 2017.
[185] "Global Standards Media." 3. GRI. 2018.
[186] "Towards Reliable Non-financial Information Accross Europe." Accountancy Europe. 2020.

The GRI discloses in its database that 2.171 organisations in Europe (not just the EU) disclosed 2.192 reports using the GRI standards in 2017.[187]

2 International Integrated Reporting Council (IIRC) – Framework

2.1 Description

The IIRC was founded in 2010 as a non-profit organisation formed by "global coalition of regulators, investors, companies, standard setters, the accounting profession, academia and NGOs." [188] In its constitution, the IIRC declared its main objectives to be: "1) improve communication about value creation, 2) advance the evolution of corporate reporting, and 3) make lasting contributions to financial stability and sustainability reporting."[189] The IIRC was established and continues to be based in London.

According to the Constitution of the IIRC, its mission is to "establish integrated reporting and thinking within mainstream business practice as the norm in the public and private sectors." [190] Also in the Constitution of the IIRC Part II Article 46.1(b), it is stated that the objective is "To create a globally accepted integrated reporting framework which brings together financial, environmental, social and governance information in a clear, concise, consistent and comparable format with the aim of helping with the development of more comprehensive and comprehensible information about organizations, prospective as well as retrospective, to meet the needs of a more sustainable, global economy."[191]

"Integrated Reporting" (<IR>) intends to improve the quality of information supplied from organisations to providers of financial capital through the production of integrated reports.[192]

In 2013 the IIRC released the <IR> Framework, which is the structure organisations use when preparing integrated reports. The IIRC conducted international consultation and testing prior the publication of the Framework.[193]

2.2 Scope in content

The <IR> Framework proposes "that disclosures should include information about the business model, strategy and resource allocation, performance and governance."[194] The Framework establishes Guiding Principles and Content Elements that govern the overall content of an integrated report. The focus on value creation takes into consideration the

[187] Sustainability Disclosure Database. GRI. 2020.
[188] The IIRC. International Integrated Reporting Council. n.d.
[189] "Constitution of the International Integrated Reporting Council." 3. International Integrated Reporting Council. 2015.
[190] Ibid., 1.
[191] Ibid., 34.
[192] Why the need for change? International Integrated Reporting Council. n.d.
[193] Frequently Asked Questions. International Integrated Reporting Council. n.d.
[194] Frequently Asked Questions. International Integrated Reporting Council. n.d.

resources and relationships used and affected by an organisation, which are categorised in six types of capitals: financial, manufactured, intellectual, human, social and relationship, and environmental.[195]

As the name indicates, the <IR> Framework gives organisations the layout and concepts to prepare integrated reporting. It acknowledges the individuality of different organisations and aims to remain as flexible as possible while ensuring a sufficient degree of comparability across organisations based on the interactions between the capitals. The six capitals, as defined by the Framework, cover the basic sustainability topics (i.e. environment, social and governance) and other non-financial information subjects not explicitly covered by other initiatives reviewed in this annex (e.g. manufactured, intellectual, or social and relationship capitals).

The <IR> Framework intends that organisations disclose any material interactions, activities, and relationships that may influence their creation of value over time, through the integrated report. This includes accounting to what extent the capitals are externalised and the positive or negative impact externalities may have in the organisation's ability to create value by itself.[196] Additionally, the report should be detailed enough to allow understanding of an organisation's strategy, governance, performance and prospects while remaining concise and avoiding less relevant information.[197]

2.3 Materiality and target audience

The <IR> Framework states that "a matter is material if it could substantively affect the organization's ability to create value in the short, medium or long term."[198] This points mainly towards financial materiality, but can also be considered to integrate social and environmental materiality, to the extent that the creation of value refers to value for all company stakeholders, not just shareholders.

The principal target audience of IIRS reports is the community of providers of financial capital (including investors).

The Framework has a secondary target audience: reporting companies. The <IR> proposes the reporting companies to incorporate "Integrated Thinking" (i.e. the ability for organisations to consider the relationships between their operating and functional units and the capitals the organisation affects.)[199] For reporting organisations, the aim of adopting integrated thinking is to increase cohesion and efficiency in their reporting

[195] "The International <IR> Framework." 10-12. International Integrated Reporting Council. 2013.
[196] Loc. cit.
[197] Ibid., 21.
[198] "Materiality in <IR>: Guidance for the preparation of integrated reports." November 2015. 4. International Integrated Reporting Council. 2015.
[199] Frequently Asked Questions. International Integrated Reporting Council. n.d.

processes to reduce organisational segregation and focus on value creation; consequently contributing towards a more financially stable economy.[200]

2.4 Number of users

Responses to survey of companies under the scope of NFRD carried out by CEPS as part of its study, it was determined that of 188 respondents, 11% use the IIRC framework to the full or a high extent, and 66% do not use IIRC at all.

3 Task Force on Climate-related Financial Disclosure (TCFD) - Recommendations

3.1 Description

The TCFD was established by the Financial Stability Board (FSB) in December 2015 to develop a set of voluntary and consistent disclosure recommendations related to organisations' climate-related financial risks.[201] Through the creation of the Task Force, the FSB intended to coordinate an overwhelming amount of climate-related disclosure provisions (over 400)[202] that affect companies disclosing such information.

Part of the mission of the TCFD is to develop recommendations that "will help companies understand what financial markets want from disclosure in order to measure and respond to climate change risks, and encourage firms to align their disclosures with investors' needs."[203]

The 31 members of the Task Force are elected by the FSB and come from different industries (preparers of climate disclosures) and countries in order to define a set of recommendations for financial reporting reflecting what is relevant to evaluate financial risks of climate impact and bringing "the challenges and opportunities surrounding climate reporting […] in the spotlight."[204]

3.2 Scope in content

The TCFD published its recommendations in June 2017 after public engagement and consultation. These recommendations included 11 key climate-related financial disclosures (also known as recommended disclosures) grouped around four areas: 1) governance around climate-related risks and opportunities; 2) strategy and financial planning aligned to actual and potential climate-related risks; 3) risk management to identify, assess, and manage climate-related risks; and 4) metrics and targets, used to assess and manage relevant climate-related risks and opportunities.[205] These

[200] International <IR> Framework. International Integrated Reporting Council. 2013.
[201] TCFD report finds encouraging progress on climate-related financial disclosure, but also need for further progress to consider financial risks. FSB. 2019.
[202] Everything you need to know about the Task Force on Climate-related Financial Disclosures. CDSB. 2016.
[203] About the Task Force. Task Force on Climate-related Financial Disclosures. n.d.
[204] Everything you need to know about the Task Force on Climate-related Financial Disclosures. CDSB. 2016.
[205] Everything you need to know about the Task Force on Climate-related Financial Disclosures. CDSB. 2016.

recommendations aim to promote better decision-making, enhanced market resilience and more sustainable economic growth.[206]

The TCFD focuses on climate-related information only. The TCFD recognises that industries and organisations' have different needs and are affected differently by climate change, therefore the TCFD developed supplemental guidance for financial and non-financial sectors. These guidelines provide more clarity for organisations to know which recommended disclosures better suit their operations, if any, depending on their activity sector.[207] The TCFD recommends that organisations holding public debt or equity should adopt its recommendations. It also recommends to include the climate-related disclosure within the public financial filings.

3.3 Materiality and target audience

As stated in the TCFD's mission, the recommendations are made on the disclosure of financial risks related to climate change. They therefore consider the outside-in impact (i.e. financial materiality).

The primary target audience of reports issues according to the TCFD recommendations are providers of financial capital (institutional investors lenders, and insurance underwriters).[208]

3.4 Number of users

According to the survey of companies under the scope of the NFRD carried out by CEPS as part of its study, the proportion of respondents that use the TCFD to the full or a high extent is of 16%. 10% uses TCFD to a limited extent, and 55% do not use the TCFD at all.

By February 2020, the TCFD had received the support from over 1.027 organisations.[209]

4 CDP – Environmental Disclosure System

4.1 Description

The CDP was founded in 2000, formerly known as the "Carbon Disclosure Project". The CDP is an international non-profit organisation[210] that runs a global environmental disclosure system; it supports companies and governments to complete environmental

[206] *How the new EU guidelines on reporting climate-related information will impact your business webinar*. Corporate Disclosure Standards Board. 2019.
[207] "Recommendations of the Task Force on Climate-related Financial Disclosures." 15. Task Force on Climate-related Financial Disclosures. 2017.
[208] TCFD report finds encouraging progress on climate-related financial disclosure, but also need for further progress to consider financial risks. FSB. 2019.
[209] TCFD Supporters
[210] Who we are. CDP. n.d.

disclosure, managing their risks and opportunities on environmental issues. The "CDP was the first platform to link environmental integrity and fiduciary duty." [211]

The CDP's mission and vision is "to see a thriving economy that works for people and planet in the long term. We focus investors, companies and cities on taking action to build a truly sustainable economy by measuring and understanding their environmental impact."[212] CDP's strategy to reach this includes a scoring system for companies and cities, through which "CDP aims to incentivise and guide them […] towards becoming a leader on environmental transparency and action."[213]

With presence in more than 50 countries, the CDP has become "the world's largest, most comprehensive dataset on environmental action", and it, "empowers investors, companies, cities, and national and regional governments to make the right choices today to build a thriving economy that works for people and planet in the long term."[214] In order to reach this stage, CDP has established regional offices and local partners in countries including India, China, Japan, Taiwan, USA, Turkey, South Africa, Brazil, Germany, Belgium, and Switzerland.

4.2 Scope in content

The CDP system focuses on organisations' disclosure of environmental issues that are divided in three sub-categories: climate change, water security, and forest security. Other environmental, social and governance issues are not considered under CDP.

The CDP system takes into consideration not only the direct impact a given organisation may have, but also the whole extent of its business model. For instance, the CDP guidelines recommend companies to disclose their scope 3 emissions,[215] therefore including the organisations' whole value chain (upstream and downstream).

The CDP helps organisations disclose some of their environmental risks and opportunities through recommendations and Key Performance Indicators (KPIs). The CDP scores companies using a letter-grade system resulting from the answers they provide to a detailed online questionnaire.

For companies, the reporting process through CDP begins with the requests for environmental information from investors and customers. Companies then collect such data and use the CDP's questionnaire to report, assess, and find areas of opportunity about environmental risks. The resulting data and CDP findings are provided to investors

[211] *About us: What we do.* CDP. n.d.
[212] Who we are. CDP. n.d.
[213] CDP Scores. CDP. 2020.
[214] Ibid.
[215] CDP, Mirjam Wolfrum, and Nico Fettes. 2019. The new EU guidelines on non-financial reporting: Setting the scene for a review of the EU corporate reporting framework. 06 27. https://www.cdp.net/en/articles/governments/the-new-eu-guidelines-on-non-financial-reporting.

for them to take informed decisions, as well as published to the market via reports, analysis, and company score.[216]

4.3 Materiality and target audience

The CDP system allows companies to disclose environmental information on a double materiality basis. For instance, the CDP system takes into consideration the impact organisations have towards climate-change, water issues, or deforestation (i.e. environmental materiality). Likewise, the CDP system requests companies to disclose environmental information that may affect their ability to create value (i.e. financial materiality).[217]

The CDP's results are targeted principally towards the financial, business, academic, and policy communities as well as to civil society.[218]

4.4 Number of users

Results of the survey to companies under the scope of the NFRD carried out by CEPS show that of 188 respondents, 29% follow the CDP standard fully or to a great extent, 16% follow CDP to some extent, and 45% do not apply the CDP standards at all.

CDP's 2019 annual report[219] shows over 1 800 European companies (representing 75% of Europe's market capitalisation) used the CDP to respond to inquiries made by investors. More than 8 400 companies worldwide used the CDP. Additionally, in Europe, more than 200 cities, states, and regions used the CDP to disclose environmental information.

5 **Sustainability Accounting Standards Board (SASB) - Standards**

5.1 Description

The SASB Foundation is an independent non-profit organisation established in the USA in 2011. It aims to "enable corporations and investors to assess key risks and opportunities that materially contribute to an organization's sustained success […]", and recognises that disclosures of ESG in corporate reports are inconsistent from company to company and there is a need for, "integration of sustainability metrics into standardized disclosure."[220]

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[216] CDP. 2020. How to disclose as a company. https://www.cdp.net/en/companies-discloser/how-to-disclose-as-a-company.
[217] CDP. 2018. "CDP Disclosure." 11. https://6fefcbb86e61af1b2fc4-c70d8ead6ced550b4d987d7c03fcdd1d.ssl.cf3.rackcdn.com/comfy/cms/files/files/000/002/942/original/CSC-Benefits-Slides-Nov-2019.zip.
[218] Ibid., 31.
[219] "CDP." *CDP Europe Annual Report 2018-2019.* CDP. 2019.
[220] "Industry Working Group Orientation Materials." 10. Sustainability Accounting Standards Board. 2014.

SASB has the mission "to establish industry-specific disclosure standards across environmental, social, and governance topics that facilitate communication between companies and investors about financially material, decision-useful information. Such information should be relevant, reliable and comparable across companies on a global basis."[221]

To achieve this mission, the SASB Foundation created an independent standard-setting arm named Sustainability Accounting Standards Board (SASB).

The Standards Board is accountable for the due process, outcomes, and ratification of the SASB standards (industry-specific sustainability disclosure standards tied to the concept of materiality to investors).[222]

5.2 Scope in content

SASB Standards were first made public in 2018, after over six years of research and continuous consultation. The Standard covers 77 industry-specific standards (grouped in 11 sectors) that help companies identify environmental, social and governance (ESG) topics that may affect their value creation through time. Each of the industry-specific standards identify a minimal set of financially material sustainability topics and their associated metrics for a typical company in an industry.[223] SASB has a unique tool called the SASB Materiality Map® [224]that allows users to identify "sustainability issues that are likely to affect the financial condition or operating performance of companies within an industry,"[225] in a visual way.

5.3 Materiality and target audience

As described in the SASB Foundation mission, the SASB Standards focus on financial materiality and do not directly consider social and environmental materiality.[226] They "identify the subset of sustainability-related risks and opportunities most likely to affect a company's financial condition (e.g., its balance sheet), operating performance (e.g., its income statement) or risk profile (e.g., its market valuation and cost of capital)".[227]

The main target audience of the SASB Standards are investors.

5.4 Number of users

[221] SASB Governance. Sustainability Accounting Standards Board. 2018.
[222] Standards Board. Sustainability Accounting Standards Board. 2018.
[223] Standards Overview. Sustainability Accounting Standards Board. 2018.
[224] SASB Materiality Map®
[225] SASB Materiality Map. The SASB Foundation. 2018.
[226] "Industry Working Group Orientation Materials." 10. Sustainability Accounting Standards Board. 2014.
[227] https://www.sasb.org/blog/promoting-clarity-and-compatibility-in-the-sustainability-landscape-gri-and-sasb-announce-collaboration/

According to the results provided from the survey to companies under the scope of the NFRD conducted by CEPS, from 187 respondents, 3% applies the SASB standard to its full or to a high extent and 79% do not apply SASB at all.

According to figures published in the SASB website, "Hundreds of companies around the world and across every sector are using SASB standards". According to SASB figures, 45% of companies reporting ESG performance to investors that use SASB standards are domiciled outside the USA.[228]

[228] https://www.sasb.org/blog/dispelling-the-top-11-sasb-myths/

ANNEX 14: NON-FINANCIAL REPORTING REQUIREMENTS IN OTHER JURISDICTIONS

This description of non-financial reporting requirements from different jurisdictions is taken from the 2020 annual report of the International Platform on Sustainable Finance (IPSF).[229] Its primary focus in on environmental disclosures.

The US is not a member of the IPSF, and the US is therefore not covered in this description. US policy and regulation in this area is expected to evolve significantly under the new administration, at least covering climate disclosures and possibly extending to other non-financial issues.

The United Kingdom has joined the IPSF since the publication of the 2020 annual report, and the UK is therefore also not covered in this description. In November 2020 the UK announced its intention to mandate climate risk disclosure using TCFD recommendations across the UK economy by 2025.

Extracts from the International Platform on Sustainable Finance 200 annual report

The majority of IPSF members have already set mandatory environmental-related disclosure requirements. These requirements apply to various types of companies. A group of jurisdictions (Argentina, China, EU, India, and Singapore) addresses disclosure obligations to listed companies, with some specificities. In the EU, for instance, large public-interest entities with more than 500 employees are required to disclose under the rules of the Non-Financial Reporting Directive (NFRD). In India, disclosure rules apply to the top 1000 companies based on market capitalisation. In China companies subject to mandatory disclosures are defined as listed companies that heavily discharge key pollutants with other listed companies falling under a "comply or explain" regime. In Argentina, the Securities and Exchange Board (CNV) only requires listed (non-financial companies) to disclose sustainability information. In Singapore, the Singapore Stock Exchange requires all listed companies to disclose five components of their non-financial information on a comply or explain basis .

Morocco issued disclosure rules for issuers of securities. In Chile, the financial market authority has issued rules for issuers of securities to disclose sustainability-related information and for all listed corporations to disclose information on their corporate governance practices on a "comply or explain" basis. In Canada, provincial securities legislation requires reporting issuers to disclose the material risks affecting their business and, where practicable, the financial impacts of such risks in certain prescribed continuous disclosure documents (e.g. Annual Information Form), including climate-related risks, if applicable .

Switzerland and New Zealand have not yet set mandatory disclosure obligations. Swiss financial and non-financial companies can voluntarily disclose sustainability-related information based on the Six-exchange regulation (soft law). In practice, Swiss companies have widely adopted GRI reporting and TCFD recommendations. In New

[229] https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/international-platform-sustainable-finance_en

Zealand, the Stock Exchange, which is privately owned, issued rules for listed companies regarding the disclosure of non-financial information on a "comply or explain" basis. It is worth noting that the Swiss Government is assessing the need to set mandatory disclosure obligations for companies, while in New Zealand the Government has recently announced that it will introduce a mandatory climate-related financial disclosure in line with TCFD recommendations.

International reporting standards and frameworks are also widely adopted in IPSF jurisdictions with mandatory disclosure rules. In Chile and India, companies generally disclose against the Global Reporting Initiative (GRI) standards or the framework of the International Integrated Reporting Council (IIRC). In Singapore and Morocco, the competent authority either recommends or requires companies to adopt recognized international standards and frameworks including, where appropriate, the TCFD recommendations, GRI, Climate Disclosure Standards Board (CDSB) or Sustainability Accounting Standards Board (SASB). In the EU, companies falling under the scope of the NFRD should state which recognised standards or frameworks they have used when this is the case. The European Commission's guidelines on climate reporting that supports the NFRD incorporate the TCFD recommendations. In Norway, there is an expectation for large companies to adhere to international standards such as the TCFD recommendations. In Canada, the federal Government encourages the adoption of the TCFD disclosure standards by federal Crown corporations where appropriate and relevant to their business activities.

International reporting standards and frameworks help ensure cross-border consistency and contribute to global convergence. They serve different purposes. The Sustainability Accounting Standards Board (SASB) standards, for instance, are designed to provide investors with information about sustainability factors that have an impact on financial performance. The Global Reporting Initiative (GRI) focuses more on the impact organisations have on the environment and society, and targets a wider variety of stakeholders. The Taskforce on Climate-related Financial Disclosures (TCFD) recommendations are designed to encourage financial institutions and non-financial companies to disclose information on climate-related risks and opportunities. The TCFD recommendations are widely recognised as authoritative guidance on the reporting of financially material climate-related information.

Furthermore, beyond the spectrum of international reporting standards and frameworks, international organisations such as the OECD have issued recommendations to help companies identify, assess and manage sustainability risks and adverse impacts on society and the environment.

As regards content, companies are required to provide disclosure on environmental, social and governance aspects (the E, S, and G). The most comprehensive approaches have been adopted in the EU, India, Morocco, Norway, and Singapore where disclosure requirements address the three dimensions of sustainability: environmental, social, and governance. In India, disclosure requirements cover social and environmental protection issues related to products and services (incorporation of social concerns, mechanisms to recycle products and waste, respect of resource use etc.) as well as possible action taken

by companies to protect and restore the environment. In China, the disclosure obligations relate to environmental impacts caused by dischargers of key pollutants. Their key performance indicators focus on, inter alia, construction and operation, environmental impact assessment of projects and administrative permits with respect to environmental protection, contingency plans for unexpected environmental incidents, as well as self-monitoring plans for environmental information. In contrast, in Chile, issuers of securities are required to report on social-related issues such as diversity and gender salary gap. Under a separate regime, listed companies in Chile should report, as part of their corporate governance disclosure, on how the board of directors incorporates into the risk management and control process economic, social and environmental risks faced by the entity. Finally, it is also worth noting that many IPSF jurisdictions are currently revising their rules and guidelines to further strengthen sustainability-related disclosure obligations. This is the case, for instance, in the EU with the ongoing NFRD revision but also in Chile, China and Singapore.

The materiality lens of information is also a key element of the approach to disclosure obligations. Within the IPSF membership, sustainability disclosure rules in the EU, China, Morocco, Norway and Singapore have a double materiality perspective. The NFRD approach, in the EU, is a typical example of double materiality approach, which implies that companies have to disclose not only on how sustainability issues may affect the company (financial materiality) but also on how the company's activities affect the environment (environmental materiality). The TCFD recommendations are an example of single materiality, focused on the financial implications of climate change (i.e. how companies' financial performance is affected by sustainability risks and opportunities).

Overview of environmental-related disclosure approaches in IPSF members

Key Characteristics	Argentina	Canada	Chile	China	European Union	India
Mandatory vs voluntary	Mandatory (corporates) and voluntary (banks)	Mandatory for material risks	Mandatory (issuers of securities) and "comply or explain" (listed corporations)	Mandatory	Mandatory	Mandatory
Undertakings affected	Public listed companies	Reporting issuers	Listed corporations	Listed companies and Key Pollutant Discharging Enterprises	Large publi-interest entities with +500 employees)	Top 1000 companies based on market capitalization (incl. banks)
Reporting against International standards & frameworks	GRI (banks on a voluntary basis)	Voluntary use of recognized reporting standards and frameworks (e.g. TCFD)	ISO 26000:2010, GRI or IIRC	NA	Voluntary use	Voluntary use by top 500 listed entities by market capitalization of IIRC
Location of disclosures	Annual report or other public report (eg. Corporate governance report)	Annual Information Form; Management Discussion & Analysis	Annual report or special report (eg. Corporate governance practices)	Annual and semi annual report	Annual report or separate report	Annual report
Information assured	NA	NA	NA	Third party verifiers	NA (ie. Statutory auditor or audit firm only checks existence of information)	Optional third party verification
Materially lens (financial and/or environmental materiality)	Financial materiality	Financial materiality	Environmental materiality	Double materiality	Double materiality	Environmental and social materiality

Key Characteristics	Morocco	New Zealand	Norway	Singapore	Switzerland
Mandatory vs voluntary	Mandatory (for companies issuing securities on the market)	Voluntary	Mandatory	Mandatory	Voluntary
Undertakings affected	issuers of securities on the market (both financial and non-financial issuers)	Listed companies	Large companies	Listed companies	Voluntary for Financial and non-financial companies
Reporting against International standards and frameworks	Required use of an internationally recognized standard	Recommended use of GRI and IIRC	Voluntary use (e.g. TCFD)	Voluntary use (e.g. GRI, IIRC, SASB, TCFD, CDSB)	Voluntary use of SIX Exchange Regulation (eg. GRI and TCFD)
Location of disclosures	Annual report	Annual report	Annual report or other public document	Annual report or special report (sustainability report)	Sustainability report in accordance with International Standard
Information assured	Voluntary external assurance by independent professional bodies	NA	NA	Voluntary external assurance by independent professional bodies	NA
Materially lens (financial and/or environmental materiality)	Double materiality	Double materiality	Double materiality	Double materiality	Financial materiality

ANNEX 15. LEGAL BASIS

In this Impact Assessment we cumulatively consider two Articles of the TFEU as legal basis for the proposed initiative.

Firstly, Article 50 TFEU is the traditional legal basis for company law legislation, mandates the European Parliament and the Council to act by means of directives to ensure freedom of establishment as regards a particular activity. The Accounting Directive and its amending Non-financial Reporting Directive are based on this article. They set out reporting rules, as diverging approaches taken at Member State level could have potentially undermined the right of establishment across the Internal Market. This is also the case of the Audit Directive, which might also need to be amended to implement the preferred policy option.

In addition, certain changes to the Transparency Directive 2004/109/EC might be needed. Article 114 TFEU together with Article 50 is the legal basis of the Transparency Directive 2004/109/EC. This Directive is closely linked to the reporting requirements of the Accounting Directive, as it sets out additional reporting requirements for issuers with securities listed on EU regulated markets. Article 50 only refers to "companies or firms" as defined by Article 54 TFEU, i.e. companies or firms "incorporated in the EU", and the Transparency Directive also imposes disclosure obligations on third country issuers. This is the reason why although Article 50 is a *lex specialis*, the residual legal basis of article 114, *lex generalis* applies as well with the objective of establishing or ensuring the functioning of the internal market – in this case, with reference to ensuring the free movement of capital.

Therefore, this Impact Assessment considers changes to the Accounting Directive 2013/34/EU (as amended by the NFRD), the Audit Directive and the Transparency Directive 2004/109/EC on the basis of Articles 50 and 114 TFEU.

ANNEX 16: ASSESSMENT OF PROPOSED POLICY OPTIONS FOR OTHER VARIABLES

Table 1. Overview of other variables for policy options and specific objectives

		Policy options					
		Digital	Supervision	Intangibles	Location	Materiality	Subsidiaries
Specific objectives	Companies from which users need information report that information		x				x
	Companies report all relevant information		x	x	x	x	x
	Reported information is comparable	x			x		
	Reported information is reliable		x		x		
	Reported information is easy to find and exploit	x			x		
	Companies have clarity about what to report		x	x		x	x
	Companies have better information from supplies, clients and investees	x		x		x	x
	Reduction of the burden created by additional demands for information	x				x	x

1. Digitalisation

1.1 Baseline

The requirements in the NFRD would remain the same. The EU would not develop an EU taxonomy and companies would not be required to tag their reports accordingly.[230]

1.2 Proposed change: Develop EU digital taxonomy and require companies to tag reports

The EU would develop a taxonomy accompanying the reporting standards[231] in order to allow companies to tag the information reported. The standards setter described in

[230] 'Taxonomy' is the technical term used for IT systems (categorisation system). It does not refer to the new taxonomy of sustainable economic activities established by the Taxonomy Regulation.

section 5.2.1. i) or the EU body deemed most appropriate, would develop this taxonomy and set up a process to ensure its yearly maintenance.

Companies would be required to tag their reports according to this taxonomy,[232] which would allow the information to be machine-readable. This policy option would feed into the work on digitalisation announced by the Commission in its Communication "A European Strategy for Data" where it already explains its plans for "common European data spaces".[233]

Any company that claims to use the EU standards on a voluntary basis (including simplified SME standards), would need to tag its report.

1.3 Impacts of the proposed change: Develop EU digital taxonomy and require companies to tag reports

Effectiveness. The requirement to tag reports according to a digital EU taxonomy would largely contribute to making concrete reported matters easier to find and compare. Accessibility, usability and comparability of publicly disclosed public information would improve, facilitating both analysis by users and reporting by financial market participants and other companies subject to different EU disclosure requirements. The length of the reports themselves would no longer represent a problem for users looking for information, as this would be machine readable.[234]

The estimated total annual ***costs for preparers*** subject to the current requirements of the NFRD for tagging reports according to this taxonomy would be approximately EUR 20 million. One-off costs would amount to EUR 100 million. If the scope was broadened according to the preferred policy option described in section 6.3.6, these costs would increase to EUR 80 million and EUR 500 million respectively. The Transparency Directive already requires companies listed on EU regulated markets to tag their consolidated financial statements using a single electronic format (ESEF Regulation). One possible way forward would be to extend these tagging requirements to non-financial information. In this case, companies already required to report against ESEF would face lower increase in costs and the actual incremental costs of this policy option

[231] This policy option is only feasible if reporting against EU non-financial standards was mandatory (preferred policy option for standardisation variable).

[232] The EU has introduced a taxonomy, 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 be tagged using iXBRL elements specified in the ESEF taxonomy. One possible way forward would be to extent these tagging requirements to non-financial information.

[233] The Commission is exploring opportunities to establish a single access point for public corporate information, including non-financial information that would improve accessibility of the reported information. The High-level Forum on CMU has formulated recommendations on this topic from the Capital Markets angle (see annex 11): (https://ec.europa.eu/info/sites/info/files/business_economy_euro/growth_and_investment/documents/200610-cmu-high-level-forum-final-report_en.pdf).

[234] Improved accessibility to public corporate information, including non-financial information, would be addressed by a different EU initiative. See annex 11.

would be lower than the costs estimates presented. The body in charge of developing the taxonomy would be tasked with performing a detailed cost-benefit analysis for preparers.

The costs associated with meeting multiple different users' demands would be reduced in the medium term, as information would be easier to find by users. Preparers would be able to cope with the expected growth in users' demands through public reporting (even if initially the costs incurred might be higher).

Costs for users of non-financial information would be significantly reduced. Tagging of reports would make publicly available information machine readable and therefore easier to use.

49% of respondents to the public consultation believe that the costs of tagging reports according to a taxonomy would be proportionate to the benefits, while 22% do not.

Costs for the EU. One-off costs of developing a taxonomy to accompany the reporting standards would be approximately EUR 550 000. Annual maintenance costs would amount to EUR 80 000.

Annual ***costs for member states*** from filing the reports in the electric format would be approximately EUR 5 million, considering the work of both officially appointed mechanisms and business registers with regard to reporting of listed and non-listed companies respectively. Implementation one-off costs would ascend to approximately EUR 35,5 million in total. Some synergies could be created in the case of OAMs, as they already have experience with financial reporting (*ESEF Regulation).*[235]

Economic, environmental, social and fundamental rights impacts

- Greater speed, reliability and accuracy of data handling would enable improving its analysis, allowing for better quality of information and decision-making.
- Companies would be held more accountable for their impacts on society and the environment, as tagging of reports against a taxonomy would allow users to search and assess the reported non-financial information more easily.
- Better usability of publically available information by policy makers, environmental authorities and other public authorities, to inform policy actions that could lead to environmental, social and fundamental rights impacts.
- Competitive advantage. Front runners in terms of transparency and in terms of performance regarding sustainability issues would be more easily identifiable, which could give them a competitive advantage, for example in terms of reputation, or to attract capital in the context of the Sustainable Finance agenda.

[235] This policy option is only feasible if reporting against EU non-financial standards was mandatory (preferred policy option for standardisation variable). The costs for the EU of developing a taxonomy that would accompany reporting against voluntary standards would not be justifiable.

1.4 Proposed changes compared to baseline

The proposed changes in the area of digitalisation are effective in contributing to meeting the objectives of making concrete reported matters easier to search and use. Improved usability of information can only granted by this option, as only by tagging reports according to a taxonomy can we facilitate machine readability of the information. This option is not too costly for the EU either, as work would build on the processes and framework developed under the ESEF Regulation, and recurring costs would be marginal to the costs of this initiative. Although there would be immediate costs for prepares, these would also experience costs savings and other positive impacts in the medium term. Therefore, this proposed change is sufficiently efficient and coherent with the rest of EU initiatives in the field of digitalisation (ESEF Regulation and upcoming CMU Strategy-European Single Access Point for corporate information).

2. Sanctioning regime and enforcement

2.1 Baseline

Sanctioning regime and enforcement of corporate reporting by listed companies

The enforcement of corporate reporting by companies with securities listed in EU regulated markets is carried out by national supervisors, according to the Transparency Directive. However, in its mandate to national competent authorities to supervise reporting of companies, the Directive lacks an explicit reference to the non-financial statement.[236]

The majority of member states have designated authorities to supervise this reporting. However, national competent authorities of some member states consider there is no legal mandate to supervise non-financial reporting, if this is published in a separate report, outside of the annual financial reports (management report).[237]

Additionally, in some member states the designated national authority that supervises non-financial reporting is not the same as the one that supervises financial reporting as mandated under the Transparency Directive. The consequence of this is that ESMA has no power to ensure supervisory convergence among these other national supervisors.

[236] Articles 7, 24(4)h, 24(4b), 28, 28a, 28b, 28c and 29 of the Transparency Directive.

[237] Member States have transposed Articles 19a and 29a of the Accounting Directive with some differences. As a result, a limited number of enforcers can supervise and enforce non-financial information only if it is set out within the management report or published together with it or only have the power to check the existence of the non-financial information as opposed to the content or do not have any supervisory powers on non-financial information at all. For this reason, the priorities presented in Section 2 may be addressed differently by, or may not apply to, these enforcers. European common enforcement priorities for 2020 annual financial reports, ESMA October 2020.

Sanctioning regime and enforcement of corporate reporting by not listed companies

The enforcement of corporate reporting by companies not listed in EU regulated markets is carried out by Member States, according to the Accounting Directive.[238] The Directive however does not specify how the sanctioning powers should be exercised, nor imposes specific types of sanctions (it only requires that sanctions are proportionate, dissuasive and effective).

2.2 Proposed changes: Clarify and strengthen supervisory regime of non-financial reporting

Sanctioning regime and enforcement of corporate reporting by listed companies

The mandate to national competent authorities to supervise non-financial reporting of companies with securities listed in EU regulated markets would be clarified in legislation. The Transparency Directive would be amended to explicitly include non-financial information as part of regulated information,[239] clarifying that national competent authorities should supervise it.

National competent authorities exercise sanctioning powers specified in the Transparency Directive applicable to breaches of the corresponding provisions by companies listed in EU regulated markets. With the mentioned amendment to the Transparency Directive this sanctioning regime would also apply to infringements of the non-financial reporting provisions.

Additionally, ESMA would be tasked to issue guidelines for national competent authorities to promote supervisory convergence of non-financial reporting.

Sanctioning regime and enforcement of corporate reporting by not listed companies

The sanctioning regime of the Accounting Directive (as amended by the NFRD) would be strengthened to ensure adequate non-financial reporting by non-listed companies in the EU. Member States would have the ability to impose equivalent sanctions and administrative measures, than those specified in the sanctioning regime of the Transparency Directive for listed companies.

[238] Article 51 of the Accounting Directive – Penalties.

[239] The Transparency Directive (Directive 2004/109/EC), sets out the publication requirements of the annual financial reports and mandates Member States to designate national competent authorities to supervise its legal obligations. The reference to the content of the management report, and where necessary to the separately reported non-financial information would be clarified in article 4 of the directive. This is the same amendment by which third country issuers would be included under the scope of the reporting requirements as described in section 5.3.3 iii).

2.3 Impacts of the proposed changes: Clarify and strengthen supervisory regime of non-financial reporting

Effectiveness. This policy option would contribute to ensuring that all companies under the scope of the NFRD report all information that users find relevant. Additionally users would trust more the reported information.

Costs for the EU. ESMA would incur in some costs for the issuance of guidelines for national competent authorities.

Costs for national authorities for supervising non-financial reporting by listed companies that were not supervised before due to lack of coordination between the legal provisions of the Accounting Directive and the Transparency Directive, would be marginal. Also, no relevant costs are expected from strengthening the sanctioning regime of the Accounting Directive, in particular with regard to non-financial reporting by non-listed companies.

Cost for users would be reduced if due to the trust in the publically available information they need to send less ad hoc request for information or hire third party providers.

2.4 Proposed changes compared to baseline

The proposed changes in the area of supervision are effective in ensuring that all companies under the scope of the NFRD report all required information appropriately, and in improving the reliability of the reported information.[240] This option is not costly for preparers and it would bring costs savings for users at the same time. Costs for the EU and national authorities would not be significant, and therefore it can be considered a very efficient alternative, as it would bring many benefits without negatively impacting any stakeholder group. This proposed change would as well approximate the supervision regimes of listed and non-listed companies to a certain extent, improving the overall coherence of the legal requirements in Company Law.

3. Reporting on intangibles

3.1 Baseline

The minimum list of non-financial matters identified in the NFRD provisions would remain the same. No mention to information on intangibles would be included in the Accounting Directive, in addition to the existing requirement to indicate in the management report the company's activities in the field of research and development.[241]

[240] The preferred option of requiring reporting against EU standards presented in section 6.2.1.i), facilitates supervisory activities, which in turn would also contribute to ensuring the comparability of the information disclosed.
[241] Article 20(2)b of the Accounting Directive.

It is widely recognised that information on intangible assets is underreported. Investments in intangible assets often do not qualify to appear in a company's financial accounts, and this is rarely compensated by adequate reporting on such information in other parts of the annual report, including the non-financial statement. This would difficult the majority of investment decisions carried out by the private sector in advanced economies and fail to explain the increasing gap between the accounting book value of many companies and their market valuation, in many sectors of the economy, for example information technologies. Some financial authorities point out that intangibles provide essential information about an issuer's value creation potential and the lack of disclosure creates an information gap between issuers and investors.

3.2 Proposed change: Require reporting on intangibles

In light of the importance of intangibles in the economy, in addition to the current disclosure requirements on other non-financial matters, undertakings would be required to disclose non-financial information on intangibles (e.g. intellectual property, software, customer retention, human capital, etc.), apart from activities in the field of research and development and intangible assets in financial statements. 50% of respondents to the public consultation believe that reporting on intangibles is needed, this view is stronger among only users of non-financial information (59%).

2.3 Impacts of the proposed change: Require reporting on intangibles

Effectiveness. More information relevant to users would be disclosed.

Costs for preparers for reporting according to the reporting standards described in section 7 (preferred option), specifically on intangibles, would be marginal in relation to reporting on the other non-financial matters of the NFRD.

Additionally, the costs associated with meeting ad hoc users' demands for information on intangibles would be reduced in the medium term, as information would be publically available for users. Preparers would be able to cope with the expected growth in users' demands through public reporting (even if initially the costs incurred might be higher).

Costs for users of non-financial information, specifically of information on intangibles, would be reduced. Publicly available information on intangibles would make it easier for users to find and use such information.

Economic, environmental, social and fundamental rights impacts

- Facilitate investments in companies with real value.

2.4 Proposed changes compared to baseline

The proposed change is effective because it ensures that all companies under the scope of the NFRD are reporting information on intangibles appropriately.[242] Even if additional disclosure requirements could create greater administrative costs for companies in the short term, ad hoc demands from investors would decrease in the medium term. Therefore, considering expected costs saving in the medium term, the overall costs for companies from reporting against intangibles are considered marginal compared to the benefits, and the proposed change is an efficient option.

4. Where to publish non-financial information?

4.1 Baseline

The requirements in the NFRD would remain the same. Disclosure of non-financial information would be required by default in the management report, but Member States could decide to allow companies to report in a separate report subject to the criteria set out in the current legal provisions.[243]

The availability of relevant information that connects financial and non-financial information would not be improved. Information would not be easier to find by users, especially investors, who are interested both in financial and non-financial information. In some cases, possible different publication times would continue to exacerbate this problem. According to the public consultation, 58% of users of non-financial information believe having separate reports for non-financial information creates problems to find it.

4.2 Proposed changes: Do not allow reporting in separate report

Companies would be required to report the information in the management report. The primary intention would be to ensure better connectivity between financial and non-financial reporting and to avoid the impression that non-financial information belongs to a category of less relevant information to the board of the company. Secondly, it would reduce the time spent by users of non-financial information searching such information in separate reports.

[242] The preferred option of requiring reporting against EU standards presented in section 6.2.1. i), would contribute to ensuring the comparability of the information disclosed on intangibles.

[243] Article 19a(4) of the Accounting Directive *"Where an undertaking prepares a separate report corresponding to the same financial year […] covering the information required for the non- financial statement […] Member States may exempt that undertaking from the obligation to prepare the non-financial statement […] provided that such separate report: (a) is published together with the management report in accordance with Article 30; or (b) is made publicly available within a reasonable period of time, not exceeding six months after the balance sheet date, on the undertaking's website, and is referred to in the management report."*

4.3 Impacts of the proposed changes: Where to publish non-financial information

Effectiveness. This policy option contributes to meeting several of the objectives defined in section 4.2:

- Improvement of the availability of relevant information to the extent that this information would be linked to other financial information. This is especially relevant for investors, who want to know how non-financial companies affect the final performance of companies (outside-in) and any link between non-financial and financial reporting.
- Information would be considered more reliable by users, as it would be disclosed in the annual financial reports of companies.
- Information would be easier to find, and at the same time as financial information. The timely availability of information is very important to investors.
- Information would be more comparable if it is easier to find, and if it can be found at the same time in all companies reporting according to the NFRD.

55% of respondents to the open public consultation consider that companies should be required to disclose all necessary non-financial information in the management report (61% of users, 47% of preparers), while 32% preferred to keep the option of separate reports. Among users, financial sector companies' opinion is divided with the same number of respondents arguing for each approach, while the majority of civil society organisations think information should be disclosed in the management report (79%). Opinions from preparers of reports are very balanced. 48% of users and 38% of preparers, do not believe that publication in separate reports provides an effective communication with users of the reports.

Costs for prepares as a result of EU intervention would be zero. Companies surveyed in CEPS study that reported non-financial information in the management report, incurred significantly lower average incremental costs than those that disclosed it in a separate report. However, this difference could also be the result of other factors, such as the complexity of the business model of the company or the sector in which it operates, and therefore we cannot draw up definitive conclusions with regard to differences in costs between reporting in management report and separate report..

Costs for users from looking for non-financial information would be reduced. These includes costs from looking for information in different public reports, form sending ad hoc demands to companies or from paying third party data providers.

Economic, environmental, social and fundamental rights impacts

- Raise the profile of non-financial information, both internally for the management and board members of the company and externally for stakeholders. Reporting non-financial information in the management report avoids the impression that

this information belongs to a category of less relevant information, both internally for the board members of the company and externally for stakeholders. 61% of respondents to the public consultation, and 70% of users, believe that publishing non-financial information in separate reports creates a perception that the information is of secondary importance.

4.4 Proposed changes compared to baseline

The proposed change is effective in contributing to the objectives of the initiative. It ensures that all companies under the scope of the NFRD report information in the management report, as part of the annual financial report. This entails cost savings for users of information, while not increasing the burden on companies. It is clearly a very efficient option that brings a lot of benefits while having no significant negative impacts. Additionally greater coherence with the financial reporting framework would be ensured, especially in terms of publication requirements, supervision, board responsibility on the reported information, etc.

5. Materiality concept in non-financial reporting

5.1 Baseline

The requirements in the NFRD would remain the same. The double materiality concept would derive from the current drafting of the law: companies are required to report information "to the extent necessary for an understanding of [its] development, performance, position and impact". Companies would retain the current degree of flexibility to judge what information is in fact necessary for an understanding of their development, performance, position and impacts. Some stakeholders would continue to interpret the legal text as requiring disclosure of information only when it is relevant from both perspectives at the same time.

5.2 Proposed change: Clarify in law when is information material

The legal requirements would specify in more detail when companies should consider non-financial information material (double materiality). With a clearer approach to the double materiality concept, companies would be given less discretion to judge what information is in fact necessary for an understanding of their development, performance, position and impacts.[244]

[244] This could build on the materiality guidance included in the Commission's guidelines (2017) and in the Commission's guidelines on climate related-reporting (2019). It could as well consider the definition of material information proposed by the Corporate Reporting Dialogue: "any information which is reasonably capable of making a difference to the conclusions stakeholders may draw when reviewing the related information".

5.3 Impacts of the proposed change: Clarify materiality concept

Effectiveness. According to his policy option, the legal text would re-affirm and clarify the double materiality perspective, contributing to the objective of ensuring that companies report relevant information, both on the risks that sustainability and other non-financial issues pose to the company, and the impacts of the company itself on society and the environment.

69% of respondents to the consultation agree the current definition of materiality is relevant to determine a company's development, performance and position, only 46% believe the same definition of materiality is relevant to determine a company's impacts on society and the environment. This reflects the current unclarity in the understanding of the legal requirements.

Costs for prepares. Companies would have greater clarity about what kind of information to report, reducing any inefficient investment in time or resources in trying to understand how best to comply with EU legislation.

Costs for users. It would be clear for users that reported information is relevant from either of both of the materiality perspectives, especially important for meeting FMP's needs for information due to their own disclosure obligations under the SFDR

Economic, environmental, social and fundamental rights impacts

- Behavioural implications. Clearly obliging companies to look at information from both perspectives during their reporting exercise would help companies assessing the risks to the company's performance stemming from non-financial matters, and also make it more aware of its impacts to the environment and society.
- No risks to the single market from companies interpreting the requirement in different ways in different member states.

5.4 Proposed change compared to baseline

The proposed change is effective in contributing to the objectives of the initiative of increasing the availability of relevant information for users. It ensures that all companies under the scope of the NFRD report both information that is relevant to understand the risks on the company that could stem form sustainability matters, and the impacts of the company on society and the environment. This entails cost savings for both prepares and users of information. The former, would gain clarity about the reporting requirements. The latter, would get information from both materiality perspectives. It is clearly a very efficient option that brings a lot of benefits while having no negative impacts.

6 Exemption of subsidiaries

6.1 Baseline

Subsidiary companies are exempted from the reporting obligations of the NFRD if the parent company itself reports according to the NFRD provisions. Additionally, the NFRD requires parent companies to publish a consolidated non-financial statement at group level.

The current requirements might not be clear enough, and might not ensure that users have access to particularly relevant information of subsidiary companies.

6.2 Proposed changes: Clarify in law the exemption of subsidiaries

Subsidiary companies would only be exempted from the reporting obligations of the NFRD if the parent company is subject to the NFRD provisions on consolidated reporting.[245] In addition, exempted subsidiaries would be required to publish the consolidated management report of their parent company containing sustainability information, and to refer to it in their individual management report. This would ensure that any company operating in the EU via subsidiaries reports on non-financial information either at subsidiary level or at consolidated level.

Additionally, as indicated in section 5.2.1, the non-financial reporting standards described under the preferred policy option for the standardisation variable, would consider the particularities of consolidated reporting. In this respect, they would ensure that information about subsidiaries is appropriately included in consolidated reporting in order to meet users' needs. The standards setter would explore the best ways to disaggregate subsidiaries' information, to ensure useful, efficient reporting.[246]

Therefore, information about subsidiaries would be included as necessary in consolidated reporting, which would be identifiable via a reference in the subsidiary's management report.

6.3 Impacts of the proposed change: Clarify in law the exemption of subsidiaries

Effectiveness. By clarifying how the exemption of subsidiaries work, this policy option contributes to ensuring that users of information have access to adequate information. In this case either via individual reporting or via consolidated reporting of parent companies.

[245] According to the preferred option, third country issuers would be subject to the NFRD provisions. Hence subsidiaries of such companies would be exempted from the reporting obligation.
[246] The disaggregation of subsidiaries' information could be done at different levels (geographical, product based…). Specific information from certain categories of subsidiaries could be required.

A majority of respondents to the open public consultation think there is no need for removing this exemption (43% vs. 32%). Specifically 60% of respondents in the financial sector, find there is no need for removing this exemption, versus 19% that think there is. Likewise, 54% of prepares do not agree to the need to remove the exemption (vs. 24% that do). On the contrary, 65% of social and environmental organisations and trade unions find the exemption to subsidiaries should be removed (vs. 9% that do not).

Costs for prepares. Companies would have greater clarity about which reporting obligations apply to them or not. Both subsidiaries and parent companies will have clarity about when reporting can be done only at consolidated level by the parent company. This would reduce time inefficiently invested in trying to understand how best to comply with EU legislation. The costs of referring to the parent company's consolidated report are considered insignificant.

Costs for users. It would be clearer for users which companies are reporting which information. With clear references to parent company consolidated reports in subsidiaries' management reports, users would be able to find relevant information that concerns the specific subsidiary.

Economic, environmental, social and fundamental rights impacts

- Competitiveness of EU companies. Non-EU companies with activities in the EU would report on these via subsidiary reporting (or, if third country issuers were brought into scope as indicated under the preferred policy option, via their consolidated report).
- No risks to the single market from companies interpreting the requirement in different ways in different member states.

6.4 Proposed changes compared to baseline

The proposed change is effective in contributing to the objectives of the initiative. It brings clarity about the personal scope of the NFRD and ensures users get all relevant information form companies they are interested in. It benefits both preparers and users without increasing the burden on neither of them. Preparers would still benefit from the exemption for reporting at subsidiary level (a removal of the exemption would translate in approximately a 60% increase in the number of reporting companies according to the proposed scope extension presented in section 6.3); and users would have clarity about where to find the information needed.

ANNEX 17: COSTS ANALYSIS

The purpose of the cost analysis is to assess the costs incurred by companies and other parties in undertaking the actions necessary to comply with the new regulatory requirements. The NFRD sets out reporting and assurance requirements for companies, hence the main cost items analysed are administrative costs and costs of assurance for the preparers of the non-financial statement. In addition, public authorities would also face costs in relation to standard setting and digitalisation of the reports.

Since the core of the NFRD is a public reporting obligation of companies, the most important cost element is the **administrative cost** of providing the required information by the businesses. As is customary in assessing administrative costs, the analysis follows the logic of the EU Standard Cost Model (SCM). Even though **assurance costs** qualify as external costs, their analysis followed the same methodology in many respects.

Evidence-base

The Commission contracted a study with CEPS and worked closely to get very granular information about the number of companies under the scope of the NFRD and the different scope options, about existing reporting and assurance patterns among different groups of companies, and about the costs of reporting and assurance according to the current provisions of the NFRD and of applying different private reporting standards and frameworks.[247]

First, CEPS built a database to estimate the number of companies currently subject to the NFRD requirements, and the number of companies that would be brought into the scope under the different scenarios. Secondly, CEPS surveyed companies subject to the NFRD in order to collect cost-related information among other information. Over 200 large companies responded to the survey. CEPS checked the quality of the responses systematically and engaged with company representatives to verify the results at different stages. In addition, the Commission facilitated an exchange between CEPS, Business Europe and company representatives, to discuss the costs information obtained from the survey. The results were also broadly consistent with the replies to the Commission's open public consultation.

In close cooperation with the Commission, CEPS set out criteria for what can be considered as reporting against detailed standards, i.e. the extent to which a company applied one or more existing standards, and the Commission used this costs estimate for calculating costs of reporting against future EU standards. CEPS also collected information about the current reporting practices of different groups of companies (NFRD reporters, national transposition companies, other large companies, and SMEs).

[247] CEPS Study on the Non-Financial Reporting Directive, publication expected in Q1 2021.

The Commission has performed a thorough research for alternative sources of information to allow the triangulation of CEPS's data, but virtually no such data was identified. In any case, on the Commission's request, CEPS has performed the comparison between the results of its own data collection, and some information sources available, such as Eurostat company data, or earlier Commission impact assessments.[248] The Commission used all literature (sources of data) available for the estimation of other supplementary costs, such as costs of digitalisation or various cost savings.

Methodology

General

The basic approach in the cost analysis is to take the number of companies under the different scope options, and multiply it by the estimated unit costs to arrive at the total cost of different options/packages.

Population of stakeholders

The companies under the scope of the NFRD, preparers of non-financial statements, can be classified into three main groups. Firstly, there are companies that already fall under the scope of the NFRD requirements. Secondly, the national transposition of the NFRD by the Member States in certain countries not only added certain requirements (such as requiring assurance), but also widened its scope to additional companies. Finally, the different scope options considered in the current IA also extend the scope of the NFRD to new groups of companies.

The CEPS Study allowed the Commission to assess as precisely as possible the companies in the different scope options in terms of their number, turnover, and market capitalisation. This assessment followed the rules of the current (and potential future) NFRD, in particular as regards consolidated reporting and the exemption of subsidiaries from the reporting obligation.[249] For the cost analysis, the number and turnover of companies added by each option is of a particular importance:

[248] Such as the 2013 Commission impact assessment accompanying the NFRD proposal or the 2011 Commission Impact Assessment accompanying the Proposal for a Directive on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings.

[249] In particular, the statistics on the number of companies take the number of companies actually reporting (i.e. excluding exempted subsidiaries), while the turnover figures include the total turnover of the companies that are covered by the report (i.e. it is calculated on a consolidated basis, including turnover of subsidiaries).

Population of companies under the different scope options			
Company groups	Number of companies	Total turnover (EUR million)	Average turnover per company (EUR million)
Current NFRD	1,956	7,565,886	3,868
National transposition extra	9,697	5,715,659	589
Option 1 - Large PIEs below 500 employees	1,157	246,138	213
Option 2 - Large non-EU undertakings listed in the EU	86	979,471	11,389
Option 2 - Large non-listed EU undertakings.	35,184	7,702,874	219
Option 3 - Small and medium SMEs listed in the EU	1,059	12,209	12
Option 4 - Non-listed medium SMEs	160,205	2,606,297	16
Total	**209,344**	**24,828,536**	**119**

The population of companies is heterogeneous as per their size (e.g. average turnover, number of employees), but also as per several other factors, such as their sector or the Member States in which they operate. This represents a challenge for the cost calculation, and justifies certain segmentation in the analysis (see below).

It is notable that by adding the different scope options to the current NFRD scope, some companies which are currently covered due to national transposition will also be covered by the new NFRD scope.[250] It was decided to deduct these "overlaps" from the new scope options (i.e. not considering them additional in the new scope) to better reflect the true additional costs as they arise by extending the scope of the NFRD.

Cost inputs

Administrative and assurance cost

Administrative costs and costs of assurance were quantified in the CEPS Study on the basis of a survey on a sample of companies under the current scope of NFRD.[251] The survey design and CEPS's cost calculations followed the EU Standard Cost Model.[252] The administrative and assurance costs were calculated by CEPS for various groups of companies across several dimensions, such as sectors, company sizes, country of the company headquarters, use of frameworks, the level of assurance, etc.

CEPS Study confirmed that the cost of reporting (and assurance) is influenced by many factors such as the size of the company, the sector(s) in which it operates, its location(s), the number of material topics, the availability of resources and experience, the depth of reporting chosen, and in general the complexity of the business. Even though CEPS surveyed only large companies under the scope of the NFRD,[253] the results have

[250] An implicit assumption here was that the new scope options are added *ceteris paribus*, i.e. existing national transposition rules remain the same as they currently are.
[251] CEPS invited almost all companies under the current scope of the NFRD to fill out the questionnaire. Companies responded on a voluntary basis resulting in self-selection bias.
[252] See the CEPS Study for more details on their own methodology and limitations.
[253] Notable that while all respondents of the survey were large as per the definition of the Accounting Directive, the sample represented companies with a turnover between 27 million EUR and 170 billion EUR, a more than 6 000-fold difference.

confirmed the wide dispersion of costs. For instance, the average cost of reporting according to standards was 106 000 EUR in the study sample, but the responses were ranging between 437 EUR and 800 000 EUR with a median of 61 000 EUR, and an interquartile range (range between the first and third quartile) of 25 000 EUR and 138 000 EUR.[254]

Since the limited number of observations in the survey[255] did not allow accounting for all the factors affecting the costs,[256] it was decided to address the heterogeneity of the companies by a stratified (segmented) approach along the most important factors of complexity of reporting/level of assurance and size of the company.

First, the survey sample was grouped into two reporting categories: companies 1) reporting against a standard, 2) reporting without following a standard.[257] Along the line of assurance, the sample was grouped into three categories: companies with 1) existence check by the auditor only (no assurance), 2) limited assurance, and 3) reasonable assurance.

Second, the survey sample was divided into two groups, with companies above and below the median turnover, and average costs were calculated both for the entire sample, and the resulting "smaller" sample separately. In the subsequent cost calculations, according to the comparable average turnover of different company groups in the various scope options, the average costs (both administrative and assurance costs) for the entire survey sample were applied to the current NFRD companies, while the average costs for the "smaller" sample were applied for the national transposition extra companies, and for companies in scope options 1 and 2.[258]

SMEs represent yet another scale jump in company size, hence for the estimation of SME costs another method was chosen.[259] Namely, the CEPS survey provided cost estimates

[254] Because extreme values or outliers in the distribution do not affect the median, it is sometimes preferred to the mean. The median tells us the centre of the data set, but says nothing about how the data on either side of its value is spread or dispersed. That is where the quartile helps. The quartile measures the spread of values above and below the median by dividing the distribution into four groups. Quartiles are used to calculate the interquartile range, which is a measure of variability around the median. The interquartile range is simply calculated as the difference between the first and third quartile: Q3 – Q1. In effect, it is the range of the middle 50% of the data that shows how spread out the data is. Finally, the minimum and maximum values tell us about the extreme values in the data set.

[255] 211 questionnaires were submitted to CEPS, furthermore, the number of observations could be lower depending on the response rate of particular questions.

[256] The knowledge about the characteristics of the company population in the future scopes was also limited, which would have limited the usability of further segmentation anyway.

[257] The CEPS survey addressed only companies under the scope of the NFRD, hence all of them were reporting non-financial information one way or another. See CEPS Study for the rules to qualify as standard reporting, as agreed with the Commission services. Any other level of reporting was qualified as non-standard reporting.

[258] While the average turnover in the entire sample was around 8 billion EUR, companies in the "smaller" sample had an average turnover of EUR 658 million, substantially closer to the average turnover of these company groups (see table above on the Population of companies under the different scope options). It is noticeable that the average turnover of both the entire and "smaller" samples is still higher than that of the target groups. Insofar as larger companies have higher costs, this could be considered a conservative approach leading to the overestimation of costs.

[259] Other information sources, such as the open public consultation, or the SME Panel did not result in reliable cost estimates, mostly due to very limited number of observations, but also as currently hardly any SME performs standard

both as averages of absolute costs, which is equivalent of assuming that all costs are fixed, and as averages of costs as a percentage of turnover, which is equivalent of assuming that all costs are variable.[260] Companies also gave their response as regards the share of individual activities in the total admin costs. These individual activities were than analysed in a qualitative manner to provide estimates of the fixed-variable cost part of each activity,[261] which was then weighted up to an aggregated fixed-variable split estimate of the total costs. The fixed-variable cost estimates applied were as follows:

Fixed - variable cost distribution			
Activities	Share in total costs	Fixed	Variable
Retrieve data	24%	10%	90%
Analyse information	22%	10%	90%
Report information	32%	30%	70%
Other costs	22%	30%	70%
Total	**100%**	**21%**	**79%**

Subsequently, the average administrative costs of SMEs were estimated based on these ratios, the average absolute and turnover based costs (of the entire sample), and the average turnover of SMEs in option groups 3 and 4:[262]

SME administrative cost estimation (EUR)						
Type of reporting	Fixed share	Fixed cost (absolute average based)	Variable share	Variable cost (% of turnover based)	Total SME admin cost (fixed+variable)	Ratio between SME/All sample admin costs
NFRD non-standard	21%	10,371	79%	613	10,983	22.03%
NFRD Standard	21%	21,980	79%	727	22,707	21.49%

Option 4 assesses the incremental costs of requiring a simplified standard reporting for all non-listed medium SMEs. No specific cost estimate was made for such "simplified standard", instead it was assumed that its cost would be equal to the estimated cost of non-standard reporting for SMEs.

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reporting. Similarly, SME representatives confirmed the extreme rarity of SMEs that currently assure non-financial reports.

[260] A fixed cost is a cost that does not change with an increase or decrease in the amount of goods or services produced or sold (this is the assumption when applying the same average cost for all companies, irrespective of their size). A variable cost is a cost that changes in proportion to production output (i.e. by the size of the company, in our case measured by turnover). Variable costs increase or decrease depending on a company's production volume; they rise as production increases and fall as production decreases. In general, companies can have two types of costs, fixed costs or variable costs, which together result in their total costs.

[261] By considering what kind of activities lie behind the data retrieval, data analysis, and data reporting, for instance:
- All companies need at least one software license (fixed), however it may be that software license is charged by the number of workstations, e.g. when there are different subsidiaries, each has to have one (variable).
- All companies need to print the report (fixed), but some reports may be longer, costing more to print (variable). The same goes for translation, editing, etc.
- Retrieving data may depend mostly on how many locations the company has (each has at least one location).
- All companies need someone to spend some minimum amount of time on analysing the data and prepare the report (fixed), but if the data were more complex, more people, or more working hours would be needed (variable).

[262] The assurance costs for SMEs were estimated by multiplying the assurance cost averages of the entire sample with the ratio between the estimated SME administrative costs and entire sample average administrative costs (last column of table). In other words, it was assumed that SME assurance costs are also proportionally lower than large company assurance costs, as it was the case with their administrative costs.

The estimated recurring costs per company used in the cost analysis as per the stratified approach were the following:[263]

Recurring administrative costs per company (EUR)			
Type of reporting	All sample mean	Smaller sample mean	SMEs
NFRD non-standard	49,860	31,340	10,983
NFRD Standard	105,673	63,497	22,707

Assurance cost per company (EUR)									
Type of reporting	All sample mean			Smaller sample mean			SMEs		
	Existence check	Limited assurance	Reasonable assurance	Existence check	Limited assurance	Reasonable assurance	Existence check	Limited assurance	Reasonable assurance
NFRD non standard	1,206	56,253	95,842	1,206	20,930	32,296	na	12,392	21,113
NFRD Standard	1,206	75,181	125,046	1,206	36,939	57,000	na	16,155	26,870

One-off administrative costs

The EU SCM requires distinguishing between one-off and recurring obligations/costs. Administrative and incremental costs may vary across time and usually are higher in the first year of compliance, when addressees have to perform both one-off and recurring actions. For instance the cost of familiarising with information obligations, certain investments, training of staff, etc. typically concentrate on the first year of compliance, while other costs, such as the cost of retrieving, analysing and reporting data occur on a recurring basis.[264] The CEPS survey took account of this issue, and collected separate cost data for the first and the following years of compliance.

The cost analysis considered one-off costs as the difference between the first year and following year costs. Hence, companies under the different scope options would incur the sum of one-off costs and recurring costs in the first year, while in the following years only the recurring costs would occur. The estimated one-off administrative costs per company used in the cost analysis as per the stratified approach were the following:[265]

One-off administrative costs per company (EUR)			
Type of reporting	All sample mean	Smaller sample mean	SMEs
NFRD non-standard	24,817	19,851	5,467
NFRD Standard	43,431	22,739	9,333

[263] Cost estimates for the "Smaller" sample non-standard reporting reasonable assurance from CEPS were unreasonably low (lower than corresponding limited assurance cost estimates – likely due to very low number of observations), hence were replaced by an estimate based on the ratio between the limited and reasonable assurance costs for standard reporting in the "smaller" sample.

[264] Due to certain economies, the cost of recurring actions might decrease over time, for instance as a result of economies of learning, relying on information already collected before, or as certain characteristics of the companies (e.g. business model, risks) typically do not change much from one year to another. This is partly reflected in the CEPS study results, as some of the respondents have already been reporting for some years. Nevertheless, the current NFRD reporting requirements are still relatively new; hence, there could be further grounds for such economies in the future. In this sense, the current estimation of recurring costs can be considered conservative (overestimating costs).

[265] The one-off administrative costs for SMEs were estimated by multiplying the one-off administrative cost averages of the entire sample with the ratio between the estimated SME administrative costs and entire sample average administrative costs.

The one-off costs calculations were based on the following further assumptions:

- One-off costs of assurance were assumed zero. There is no reason to assume that the first year cost of assurance would be much different from the cost in the following years, and hence no such question was asked to the respondents of the CEPS survey.
- In the cost calculations, there are two corresponding columns. "Total one-off costs" is what all companies under the respective scope will have to pay extra in the first year of their reporting, regardless of which is this "first year". Some of them pay it only after the entry into application of the new requirements, some have paid it (or part of it) already, if they had started some reporting before ("Total one-off costs" is therefore partly backward looking). "Incremental one-off costs" shows only the true additional burden of the companies under the scope in the first year of the application of the new rules (only forward looking).
- Those companies that currently do not report non-financial information pay full one-off cost of the standard reporting, non-standard reporters pay the difference between one-off costs of standard and non-standard, and already standard reporters pay no one-off cost. This is in line with how recurring costs were treated.[266]

Costs of digitalisation (tagging)

Preparers of the non-financial report would need to digitally tag the non-financial information in order to facilitate its searchability and usability. The only available information on costs that is comparable was found in an ESMA study from 2016 dealing with structured electronic reporting of financial statements (ESEF).[267] According to this study, costs for companies starting digital reporting from scratch were for the first year minimum: EUR 2 700; maximum: EUR 40 000; mean: EUR 13 000; median: EUR 11 500, and for subsequent years (including software maintenance) minimum: EUR 200; maximum: EUR 18 250; mean: EUR 4 600; median: EUR 1 700.[268] For the cost calculation, it was decided to take the median results as benchmarks, also considering the heterogeneity of the companies under the different scope options. Hence, the costs for tagging were estimated at **EUR 1 700 recurring** costs, and **EUR 9 800 one-off** costs (that would only occur in the first year) per company.

In the tagging cost estimation for preparers, the following considerations were made:

[266] The analysis recognised the synergies created by previous reporting activities, and therefore full one-off costs of standard reporting were not applied for all reporters equally.
[267] Feedback Statement on the Consultation Paper on the Regulatory Technical Standard on the European Single Electronic Format (ESEF), ESMA, 2016
https://www.esma.europa.eu/sites/default/files/library/2016-1668_esma_feedback_statement_on_the_rts_on_esef_0.pdf
[268] Page 96 of ESMA report.

- Tagging non-financial reports is new to everyone, hence there are no current costs, and all future costs will be incremental.
- Some companies already deal with tagging as regards their financial statements; hence one could consider certain synergies for certain types of companies. However, due to that 1) it was not straightforward which companies and to what extent would have been affected as such, and that 2) the number of companies that could have been potentially affected is not significant for the costs calculation, it was decided not to apply any reduced cost estimates on this account. This could be considered as a conservative approach.
- For the same reason of uncertainty of information, it was decided not to follow the stratified approach as regards costs of tagging; all company groups' tagging costs were estimated based on the same unit costs for tagging.

The costs for other stakeholder groups stemming from this requirement, were estimated based on the same ESMA study, taking the ESEF cost estimates as benchmark.[269] The entities concerned are (1) the EU body that will be responsible for developing and maintaining the IT taxonomy for the tagging of reports, (2) Officially Appointed Mechanisms (OAMs) per Member State (altogether 27), responsible for developing digital ad hoc processes for the filing of reports by listed companies and for maintaining and updating the digital registers, and (3) Business Registers per Member State (altogether 27), responsible for developing digital ad hoc processes for the filing of reports by non-listed companies and for maintaining and updating the digital registers.

A cost reduction factor was added to the cost estimation of two of these bodies to take account for certain synergies with the already existing ESEF system. Namely, ESEF cost estimates were reduced by 10% in the calculation of costs for the EU body that will be responsible for developing and maintaining the IT taxonomy for non-financial reporting, and by 80% for OAMs, who are already responsible for maintaining and updating the digital registers for financial reports of certain listed companies, and will be responsible to do so for non-financial reports of listed companies according to the new provision of the NFRD as well. No reduction was applied for Business Registers, as these would only start developing digital ad hoc processes for the filing of reports by non-listed companies as a consequence of this new requirement for non-financial statements.[270]

The resulting cost estimates for third parties are the following:[271]

[269] Similarly to the ESEF cost estimates, it was assumed that the costs for each body do not depend on the number of reporting companies (at least on a reasonably short term all costs are fixed), hence the different scope options do not modify the costs.
[270] These cost reductions were applied to both one-off costs and recurring costs.
[271] Cost of taxonomy development and implementation qualify as one-off costs, while cost of maintenance qualifies as recurring cost.

Costs of tagging for third parties(EUR)				
	ESEF cost estimate per entity	Cost reduction factor	NFRD cost estimate per entity	Total NFRD cost estimate (27 MSs)
EU body / standard setter	**690,000**	**10%**	**621,000**	**621,000**
Development of taxonomy and implementation	*600,000*		*540,000*	*540,000*
Annual maintenance	*90,000*		*81,000*	*81,000*
OAMs	**1,250,000**	**80%**	**250,000**	**6,750,000**
Implementation	*1,100,000*		*220,000*	*5,940,000*
Annual maintenance	*150,000*		*30,000*	*810,000*
Business Registers	**1,250,000**	**0%**	**1,250,000**	**33,750,000**
Implementation	*1,100,000*		*1,100,000*	*29,700,000*
Annual maintenance	*150,000*		*150,000*	*4,050,000*

Cost savings of preparers

It is reasonable to assume that preparers' costs of dealing with multiple ad hoc sustainability information requests would be reduced in the medium term by the mandatory application of EU reporting standards. A recent study has inquired companies about the time they spend on responding to sustainability ratings and ranking providers, including time completing questionnaires and correcting data or reports.[272] The 47 respondents indicated 90 (median) to 155 (average) person days.[273] On this basis it can be estimated that EU companies incur costs between EUR 24 200 and 41 700 annually on the account of responding to questionnaires or correcting ratings reports[274]. On the assumption that the new reporting requirements on the basis of mandatory EU standards completely eliminate the need for such ad hoc requests, this translates into potential savings of up to around EUR 280 - 490 million for the current NFRD population (including national transposition).[275]

It is also reasonable to assume that the enhanced clarity of the reporting obligations as a result of new comprehensive reporting standards, would lead to cost savings as well. The CEPS study shows that companies that find it easy to decide which information should be included in the non-financial statement usually incur around 25% lower cost of reporting than those companies that find the decision on the materiality of information

[272] Study on sustainability ratings and research, by SustainAbility (https://op.europa.eu/en/publication-detail/-/publication/d7d85036-509c-11eb-b59f-01aa75ed71a1/language-en/format-PDF/source-183474104).

[273] This is broadly in line with the findings of other studies indicating approximately half a full-time post for the same. See, Clementino, E., Perkins, R. How Do Companies Respond to Environmental, Social and Governance (ESG) ratings? Evidence from Italy. J Bus Ethics (2020). https://doi.org/10.1007/s10551-020-04441-4 and Häßler, Rolf. (2013). The Impact of SRI – An Empirical Analysis of the Impact of Socially Responsible Investments on Companies by oekom research

[274] EUR 26.9 was used as hourly labour cost average for EU27 in accordance with "Labour cost levels by NACE Rev. 2 activity" available at Eurostat (reference year 2018): https://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=lc_lci_lev&lang=en. In line with the SCM methodology (and the CEPS Study), the indicated EUR 26.9 labour cost was incremented by 25% to account for overheads, resulting in EUR 33.625 hourly cost.

[275] This could be extrapolated to potential savings of around EUR 1 200 – 2 000 million for the companies under Package 3. However, it is uncertain whether these companies already have such a high burden of ad hoc sustainability information requests, in particular given that most of them are smaller in size or not listed (lower interest from investors and as a result sustainability ratings and ranking providers).

more difficult (neutral or difficult).[276] Assuming that as a result of the obligation to report against standards, all companies would find "easy" the decision about what information to disclose, the estimated total reporting costs would be reduced by around 20% or around EUR 600 million under the preferred option.[277] These estimates however must be treated with appropriate caution, as the requirement to report against standards may not alone completely ease the decision about what information to disclose. The complexity of the business might still play a role in deciding what information to disclose.[278] Furthermore, the decision on what information to disclose is only one cost driver of many, e.g. in the costs of collecting and analysing the relevant information, the nature and complexity of the business appears to be decisive.

Business-as-usual factor

The rationale behind splitting compliance costs of new legal obligations into business-as-usual (BAU) cost and incremental cost components, is that while companies already carry out certain activities on a voluntary basis, the regulator should only focus on the consequences of its own actions by identifying the true additional burden of the regulation when performing its cost-benefit analysis. Hence, the BAU part of the compliance cost is considered only as background information when comparing the different options. In the field of administrative costs, the part of the costs that occur solely because of the new legal obligations is referred to as "administrative burden", but the same concept is equally valid for any other type of compliance costs.

In order to identify the incremental cost component of the new measures, it was necessary to establish the current reporting and assurance patterns of companies under the current NFRD scope, of extra national transposition companies, and of companies under the different future scope options. The reporting and assurance patterns of companies subject to the current NFRD scope were established by CEPS on the basis of its NFRD survey results. Reporting patterns were differentiated according to three categories: 1) reporting under a standard, 2) reporting without following a standard, and 3) no reporting.[279] Assurance patterns were differentiated according to three categories as well: 1) existence check only (or no assurance), 2) limited assurance, and 3) reasonable assurance.

CEPS carried out desk research regarding the reporting patterns of random samples of companies in line with the Commission's request,[280] namely among extra national

[276] See Figure 5.32 in the CEPS report.
[277] The average cost data included those companies that already find this decision easy.
[278] It is also uncertain how representative CEPS's sample was in this respect for the current and in particular for the future NFRD reporting population.
[279] See CEPS Study for the criteria to qualify as standard reporting, as agreed with the Commission. Any other reporting was qualified as non-standard reporting.
[280] It was possible to identify reporting patterns through a desk research, but assurance patterns could only have been established through directly asking the companies themselves. See CEPS Study for more details.

transposition companies, large PIEs under 500 employees (Option 1), large non-listed companies (Option 2), and listed SMEs[281] (Options 3).[282]

Finally, the combined reporting and assurance statistics for the company groups other than the current NFRD scope were calculated based on the following assumptions:

- If there is no non-financial reporting, there is no assurance of it either;
- within non-standard reporting, assurance patterns follow the NFRD survey assurance patterns for non-standard reporting companies;
- within standard reporting, assurance patterns follow the NFRD survey assurance patterns for standard reporting companies;
- based on mandatory assurance requirements of national transposition in two countries, the overall national transposition assurance statistics were combining assumptions for these two countries[283] with the above two assumptions;
- the current NFRD sets an existence check as a minimum requirement. For the new scope company groups no assurance was assumed for this assurance type.

The resulting combined reporting and assurance patterns for the different company groups were as follows:

NFRD	No assurance (Existence check)	Limited assurance	Reasonable assurance	Total
No reporting	0%	0%	0%	0%
Non-standard	17%	15%	6%	38%
Standard	12%	39%	11%	62%
Total	29%	53%	18%	*100%*

National transposition	No assurance (Existence check)	Limited assurance	Reasonable assurance	Total
No reporting	0%	0%	0%	0%
Non-standard	10%	37%	8%	54%
Standard	8%	31%	7%	46%
Total	18%	68%	15%	*100%*

Option 1	No assurance (Existence check)	Limited assurance	Reasonable assurance	Total
No reporting	78%	0%	0%	78%
Non-standard	7%	6%	2%	15%
Standard	1%	5%	1%	8%
Total	86%	10%	4%	*100%*

[281] Excluding micro enterprises.

[282] In the calculations it was further assumed that 1) non-EU large companies listed in the EU follow the patterns of non-listed large EU companies (both in Option 2); and 2) medium SMEs follow the patterns of the sampled small and medium listed SMEs (Option 4 follows Option 3)

[283] In France and Spain, the national transposition requires assurance. In these two countries, it was assumed that 90% of companies under the NFRD applies limited assurance, 10% of companies applies reasonable assurance.

Option 2	No assurance (Existence check)	Limited assurance	Reasonable assurance	Total
No reporting	76%	0%	0%	76%
Non-standard	4%	4%	2%	10%
Standard	3%	9%	3%	14%
Total	83%	12%	4%	*100%*

Option 3-4	No assurance (Existence check)	Limited assurance	Reasonable assurance	Total
No reporting	95%	0%	0%	95%
Non-standard	1%	1%	0%	2%
Standard	1%	2%	1%	4%
Total	96%	3%	1%	*100%*

In general, the incremental costs of the different options were calculated as the difference between the estimated future costs of the different company groups, and the current costs of the different company groups as estimated based on the above reporting and assurance patterns.

Limitations

Since the vast majority of the input data is sourced from the CEPS Study, all methodological limitations therein are equally affecting the results of this cost calculation (e.g. representativeness of the sample, company estimates instead of hard data, some missing information).[284] Furthermore, a number of assumptions and estimations were used in the cost calculations (all of which were described above in detail).

Finally, it is important to emphasize that while CEPS's survey results permitted to estimate the relative magnitude of administrative and assurance costs across different alternative scope options, the per company costs should not be considered as a reliable estimate of administrative and assurance costs for any particular company, which, as mentioned above, is influenced by several factors.

[284] The same can be said as regards the limitations of other data sources used.

Cost calculations

The administrative and assurance cost calculations under the stratified approach are presented below:

ANNUAL ADMINISTRATIVE COSTS (EUR)		ACTUAL CURRENT COSTS						FUTURE COSTS	
NFRD scope	Number of companies	No reporting	Non standard	Standard	Non-standard reporting cost	Standard reporting cost	Total reporting cost	Total future reporting cost (all standard)	Incremental cost
Baseline (current NFRD)	**11,653**	**-**	**6,000**	**5,653**	**201,929,713**	**409,802,878**	**611,732,591**		**0**
Baseline NFRD	*1,956*	*-*	*751*	*1,205*	*37,438,775*	*127,348,759*	*164,787,534*		
Baseline NT	*9,697*	*-*	*5,249*	*4,448*	*164,490,938*	*282,454,119*	*446,945,057*		
PACKAGE 0 (Option 0 Standard)	**11,653**	**-**	**6,000**	**5,653**	**201,929,713**	**409,802,878**	**611,732,591**	**822,422,895**	**210,690,304**
Package 0 NFRD	*1,956*	*-*	*751*	*1,205*	*37,438,775*	*127,348,759*	*164,787,534*	*206,696,832*	*41,909,298*
Package 0 NT	*9,697*	*-*	*5,249*	*4,448*	*164,490,938*	*282,454,119*	*446,945,057*	*615,726,063*	*168,781,006*
Option 1 (Standard)	1,157	*897*	*174*	*87*	*5,438,987*	*5,509,913*	*10,948,900*	*73,465,510*	*62,516,611*
Option 2 (Standard)	35,270	*26,948*	*3,435*	*4,888*	*107,636,833*	*310,345,937*	*417,982,770*	*2,239,523,383*	*1,821,540,613*
Option 3 (Standard)	1,059	*1,001*	*21*	*37*	*232,630*	*841,638*	*1,074,268*	*24,046,794*	*22,972,526*
Option 4 (Simplified Standard)	160,205	*151,394*	*3,204*	*5,607*	*35,192,109*	*127,322,551*	*162,514,660*	*1,825,341,827*	*1,662,827,167*
PACKAGE 1 (OPTION 1 Standard)	**12,810**	**897**	**6,173**	**5,740**	**207,368,700**	**415,312,791**	**622,681,491**	**895,888,406**	**273,206,915**
Package 1 NFRD	*3,113*	*897*	*924*	*1,292*	*42,877,762*	*132,858,672*	*175,736,434*	*280,162,343*	*104,425,909*
Package 1 NT	*9,697*	*-*	*5,249*	*4,448*	*164,490,938*	*282,454,119*	*446,945,057*	*615,726,063*	*168,781,006*
PACKAGE 2 (OPTION 2 Standard)	**48,080**	**27,845**	**9,608**	**10,628**	**315,005,532**	**725,658,728**	**1,040,664,260**	**3,135,411,788**	**2,094,747,528**
Package 2 NFRD	*38,383*	*27,845*	*4,359*	*6,179*	*150,514,594*	*443,204,609*	*593,719,204*	*2,519,685,725*	*1,925,966,522*
Package 2 NT	*9,697*	*-*	*5,249*	*4,448*	*164,490,938*	*282,454,119*	*446,945,057*	*615,726,063*	*168,781,006*
PACKAGE 3 (OPTION 3 Standard)	**49,139**	**28,845**	**9,629**	**10,665**	**315,238,162**	**726,500,366**	**1,041,738,528**	**3,159,458,582**	**2,117,720,055**
Package 3 NFRD	*39,442*	*28,845*	*4,380*	*6,217*	*150,747,224*	*444,046,247*	*594,793,471*	*2,543,732,519*	*1,948,939,048*
Package 3 NT	*9,697*	*-*	*5,249*	*4,448.34*	*164,490,938*	*282,454,119*	*446,945,057*	*615,726,063*	*168,781,006*
PACKAGE 4 (OPTION 4 Simpl. Stan.)	**209,344**	**180,239**	**12,833**	**16,272**	**350,430,271**	**853,822,917**	**1,204,253,188**	**4,984,800,410**	**3,780,547,222**
Package 3 NFRD	*199,647*	*180,239*	*7,584*	*11,824*	*185,939,333*	*571,368,798*	*757,308,131*	*4,369,074,347*	*3,611,766,215*
Package 3 NT	*9,697*	*-*	*5,249*	*4,448.34*	*164,490,938*	*282,454,119*	*446,945,057*	*615,726,063*	*168,781,006*

ONE-OFF ADMINISTRATIVE COSTS (EUR)		ALREADY SUNK ONE-OFF COSTS						FUTURE COSTS	
NFRD scope	Number of companies	No reporting	Non standard	Standard	Non-standard one-off cost	Standard one-off cost	Total sunk one-off cost	Total one-off cost (all standard)	Incremental one-off cost
Baseline (current NFRD)	**11,653**	**-**	**6,000**	**5,653**	**122,825,999**	**153,492,802**	**276,318,800**		**0**
Baseline NFRD	*1,956*	*-*	*751*	*1,205*	*18,634,615*	*52,339,911*	*70,974,527*		
Baseline NT	*9,697*	*-*	*5,249*	*4,448*	*104,191,383*	*101,152,891*	*205,344,274*		
PACKAGE 0 (Option 0 Standard)	**11,653**	**-**	**6,000**	**5,653**	**122,825,999**	**153,492,802**	**276,318,800**	**305,456,439**	**29,137,639**
Package 0 NFRD	*1,956*	*-*	*751*	*1,205*	*18,634,615*	*52,339,911*	*70,974,527*	*84,951,702*	*13,977,176*
Package 0 NT	*9,697*	*-*	*5,249*	*4,448*	*104,191,383*	*101,152,891*	*205,344,274*	*220,504,737*	*15,160,463*
Option 1 (Standard)	1,157	*897*	*174*	*87*	*3,445,147*	*1,973,218*	*5,418,366*	*26,309,578*	*20,891,213*
Option 2 (Standard)	35,270	*26,948*	*3,435*	*4,888*	*68,179,017*	*111,141,550*	*179,320,567*	*802,021,457*	*622,700,890*
Option 3 (Standard)	1,059	*1,001*	*21*	*37*	*115,788*	*345,910*	*461,698*	*9,883,151*	*9,421,453*
Option 4 (Simplified Standard)	160,205	*151,394*	*3,204*	*5,607*	*17,516,370*	*52,329,140*	*69,845,509*	*897,493,969*	*827,648,459*
PACKAGE 1 (OPTION 1 Standard)	**12,810**	**897**	**6,173**	**5,740**	**126,271,146**	**155,466,020**	**281,737,166**	**331,766,017**	**50,028,851**
Package 1 NFRD	*3,113*	*897*	*924*	*1,292*	*22,079,763*	*54,313,130*	*76,392,892*	*111,261,280*	*34,868,388*
Package 1 NT	*9,697*	*-*	*5,249*	*4,448*	*104,191,383*	*101,152,891*	*205,344,274*	*220,504,737*	*15,160,463*
PACKAGE 2 (OPTION 2 Standard)	**48,080**	**27,845**	**9,608**	**10,628**	**194,450,163**	**266,607,571**	**461,057,734**	**1,133,787,475**	**672,729,741**
Package 2 NFRD	*38,383*	*27,845*	*4,359*	*6,179*	*90,258,780*	*165,454,680*	*255,713,460*	*913,282,738*	*657,569,278*
Package 2 NT	*9,697*	*-*	*5,249*	*4,448*	*104,191,383*	*101,152,891*	*205,344,274*	*220,504,737*	*15,160,463*
PACKAGE 3 (OPTION 3 Standard)	**49,139**	**28,845**	**9,629**	**10,665**	**194,565,951**	**266,953,481**	**461,519,432**	**1,143,670,626**	**682,151,194**
Package 3 NFRD	*39,442*	*28,845*	*4,380*	*6,217*	*90,374,568*	*165,800,590*	*256,175,158*	*923,165,889*	*666,990,731*
Package 3 NT	*9,697*	*-*	*5,249*	*4,448*	*104,191,383*	*101,152,891*	*205,344,274*	*220,504,737*	*15,160,463*
PACKAGE 4 (OPTION 4 Simpl. Stan.)	**209,344**	**180,239**	**12,833**	**16,272**	**212,082,321**	**319,282,621**	**531,364,941**	**2,041,164,595**	**1,509,799,653**
Package 3 NFRD	*199,647*	*180,239*	*7,584*	*11,824*	*107,890,937*	*218,129,730*	*326,020,667*	*1,820,659,858*	*1,494,639,190*
Package 3 NT	*9,697*	*-*	*5,249*	*4,448*	*104,191,383*	*101,152,891*	*205,344,274*	*220,504,737*	*15,160,463*

ANNUAL ASSURANCE COSTS (EUR)		ACTUAL CURRENT COSTS							FUTURE COSTS (LIMITED ASSURANCE)					
NFRD scope	Number of companies	No reporting	Non standard	Standard	Existence check costs	Limited assurance cost	Reasonable assurance cost	Total assurance cost	Standard	No assurance costs	Limited assurance cost	Reasonable assurance cost	Total assurance cost	Incremental cost
PACKAGE 0 (Option 0 Standard)	**11,653**	**0**	**6,000**	**5,653**	**2,766,817**	**258,102,094**	**101,388,877**	**362,257,788**	**11,653**	**0**	**426,930,453**	**123,974,481**	**550,904,934**	**188,647,146**
Package 0 NFRD	*1,956*	*0*	*751*	*1,205*	*687,661*	*72,827,890*	*39,457,583*	*112,973,135*	*1,956*	*0*	*121,164,237*	*43,062,320*	*164,226,557*	*51,253,422*
Package 0 NT	*9,697*	*0*	*5,249*	*4,448*	*2,079,155*	*185,274,204*	*61,931,294*	*249,284,653*	*9,697*	*0*	*305,766,216*	*80,912,161*	*386,678,377*	*137,393,724*
Option 1 (Standard)	1,157	897	174	87	0	3,396,629	1,828,166	5,224,795	1,157	0	41,097,493	2,532,938	43,630,431	38,405,636
Option 2 (Standard)	35,270	26,948	3,435	4,888	0	140,413,002	69,309,190	209,722,192	35,270	0	1,248,900,540	83,256,544	1,332,157,084	1,122,434,892
Option 3 (Standard)	1,059	1,001	21	37	0	474,909	256,095	731,004	1,059	0	16,942,069	276,140	17,218,209	16,487,205
Option 4 (Simplified Standard)	160,205	151,394	3,204	5,607	0	71,844,002	38,741,987	110,585,989	160,205	0	1,983,205,584	38,741,987	2,021,947,571	1,911,361,582
PACKAGE 1 (OPTION 1 Standard)	**12,810**	**897**	**6,173**	**5,740**	**2,766,817**	**261,498,724**	**103,217,043**	**367,482,584**	**12,810**	**0**	**468,027,946**	**126,507,420**	**594,535,366**	**227,052,782**
Package 1 NFRD	*3,113*	*897*	*924*	*1,292*	*687,661*	*76,224,520*	*41,285,750*	*118,197,930*	3,113	*0*	*162,261,730*	*45,595,258*	207,856,988	*89,659,058*
Package 1 NT	*9,697*	*0*	*5,249*	*4,448*	*2,079,155*	*185,274,204*	*61,931,294*	*249,284,653*	9,697	*0*	*305,766,216*	*80,912,161*	386,678,377	*137,393,724*
PACKAGE 2 (OPTION 2 Standard)	**48,080**	**27,845**	**9,608**	**10,628**	**2,766,817**	**401,911,725**	**172,526,233**	**577,204,775**	**48,080**	**0**	**1,716,928,486**	**209,763,964**	**1,926,692,450**	**1,349,487,674**
Package 2 NFRD	*38,383*	*27,845*	*4,359*	*6,179*	*687,661*	*216,637,521*	*110,594,940*	*327,920,122*	*38,383*	*0*	*1,411,162,270*	*128,851,803*	*1,540,014,072*	*1,212,093,950*
Package 2 NT	*9,697*	*0*	*5,249*	*4,448*	*2,079,155*	*185,274,204*	*61,931,294*	*249,284,653*	*9,697*	*0*	*305,766,216*	*80,912,161*	*386,678,377*	*137,393,724*
PACKAGE 3 (OPTION 3 Standard)	**49,139**	**28,845**	**9,629**	**10,665**	**2,766,817**	**402,386,634**	**172,782,329**	**577,935,780**	**49,139**	**0**	**1,733,870,555**	**210,040,104**	**1,943,910,659**	**1,365,974,879**
Package 3 NFRD	*39,442*	*28,845*	*4,380*	*6,217*	*687,661*	*217,112,430*	*110,851,035*	*328,651,126*	*39,442*	*0*	*1,428,104,339*	*129,127,942*	*1,557,232,281*	*1,228,581,155*
Package 3 NT	*9,697*	*0*	*5,249*	*4,448*	*2,079,155*	*185,274,204*	*61,931,294*	*249,284,653*	*9,697*	*0*	*305,766,216*	*80,912,161*	*386,678,377*	*137,393,724*
PACKAGE 4 (OPTION 4 Simpl. Stan.)	**209,344**	**180,239**	**12,833**	**16,272**	**2,766,817**	**474,230,636**	**211,524,316**	**688,521,769**	**209,344**	**0**	**3,717,076,139**	**248,782,091**	**3,965,858,230**	**3,277,336,461**
Package 3 NFRD	*199,647*	*180,239*	*7,584*	*11,824*	*687,661*	*288,956,432*	*149,593,022*	*439,237,115*	*199,647*	*0*	*3,411,309,923*	*167,869,930*	*3,579,179,853*	*3,139,942,737*
Package 3 NT	*9,697*	*0*	*5,249*	*4,448*	*2,079,155*	*185,274,204*	*61,931,294*	*249,284,653*	*9,697*	*0*	*305,766,216*	*80,912,161*	*386,678,377*	*137,393,724*

The summary of the cost calculations for preparers is presented below.

Package cost estimates (million EUR)										
				Stratified recurring costs				Stratified one-off costs		
	Total number of companies	Number of companies new to reporting/ assurance /tagging	Number of companies with non-standard reporting before/ with assurance that needs to be elevated	Current costs	Future costs	Incremental costs	Increase vs previous package	Total one-off costs	Incremental one-off costs	Increase vs previous package
Baseline	**11,653**			**974**				**276**		
administrative costs	*11,653*			*612*				*276*		
assurance costs	*11,653*			*362*				*0*		
Subtotal admin+assur.	**11,653**			**974**				**276**		
tagging costs	*11,653*			*0*				*0*		
Package 0	**11,653**			**974**	**1,393**	**419**	**419**	**420**	**143**	**143**
administrative costs	*11,653*	*0*	*6,000*	*612*	*822*	*211*	*211*	*305*	*29*	*29*
assurance costs	*11,653*	*2,295*	*3,835*	*362*	*551*	*189*	*189*	*0*	*0*	*0*
Subtotal admin+assur.	**11,653**			**974**	**1,373**	**399**	**399**	**305**	**29**	**29**
tagging costs	*11,653*	*11,653*		*0*	*20*	*20*	*20*	*114*	*114*	*114*
Package 1	**12,810**			**990**	**1,512**	**522**	**103**	**457**	**176**	**32**
administrative costs	*12,810*	*897*	*6,173*	*623*	*896*	*273*	*63*	*332*	*50*	*21*
assurance costs	*12,810*	*3,287*	*3,901*	*367*	*595*	*227*	*38*	*0*	*0*	*0*
Subtotal admin+assur.	**12,810**			**990**	**1,490**	**500**	**101**	**332**	**50**	**21**
tagging costs	*12,810*	*12,810*		*0*	*22*	*22*	*2*	*126*	*126*	*11*
Package 2	**48,080**			**1,618**	**5,144**	**3,526**	**3,004**	**1,605**	**1,144**	**968**
administrative costs	*48,080*	*27,845*	*9,608*	*1,041*	*3,135*	*2,095*	*1,822*	*1,134*	*673*	*623*
assurance costs	*48,080*	*32,724*	*5,219*	*577*	*1,927*	*1,349*	*1,122*	*0*	*0*	*0*
Subtotal admin+assur.	**48,080**			**1,618**	**5,062**	**3,444**	**2,944**	**1,134**	**673**	**623**
tagging costs	*48,080*	*48,080*		*0*	*82*	*82*	*60*	*471*	*471*	*346*
Package 3	**49,139**			**1,620**	**5,187**	**3,567**	**41**	**1,625**	**1,164**	**20**
administrative costs	*49,139*	*28,845*	*9,629*	*1,042*	*3,159*	*2,118*	*23*	*1,144*	*682*	*9*
assurance costs	*49,139*	*33,742*	*5,227*	*578*	*1,944*	*1,366*	*16*	*0*	*0*	*0*
Subtotal admin+assur.	**49,139**			**1,620**	**5,103**	**3,484**	**39**	**1,144**	**682**	**9**
tagging costs	*49,139*	*49,139*		*0*	*84*	*84*	*2*	*482*	*482*	*10*
Package 4	**209,344**			**1,893**	**9,307**	**7,414**	**3,847**	**4,093**	**3,561**	**2,398**
administrative costs	*209,344*	*180,239*	*12,833*	*1,204*	*4,985*	*3,781*	*1,663*	*2,041*	*1,510*	*828*
assurance costs	*209,344*	*187,658*	*6,456*	*689*	*3,966*	*3,277*	*1,911*	*0*	*0*	*0*
Subtotal admin+assur.	**209,344**			**1,893**	**8,951**	**7,058**	**3,574**	**2,041**	**1,510**	**828**
tagging costs	*209,344*	*209,344*		*0*	*356*	*356*	*272*	*2,052*	*2,052*	*1,570*

ANNEX 18: DISCARDED POLICY OPTIONS

The following options have been considered but discarded at an early stage:

1) General: European Transparency Benchmark.
2) Standardisation: Additional non-binding guidelines issued by the Commission.
3) Standardisation: Endorsement of an international standard.
4) Scope: Expanding the scope to include all SMEs.

This annexes describes each of these options and the reasons for discarding them at an early stage.

1) General: European Transparency Benchmark

Description of option:

The Commission could propose the establishment of a European transparency benchmark which publicly rates the non-financial reporting of companies, with the aim of creating an incentive for companies to improve the quality of such reporting. This could be modelled on the Netherlands Transparency Benchmark that the Dutch government has supported since 2004.[285] The Netherlands Transparency benchmark aims to enable companies to compare their own non-financial reporting with other companies, to provide a starting point for dialogue between the company and its stakeholders on transparency, and to identify trends in non-financial reporting.

Reasons for discarding this option:

In spite of its experience with the Transparency Benchmark, the Dutch regulatory supervisor has identified many of the same deficiencies in non-financial reporting in the Netherlands that exist in other Member States of the European Union.[286] There is therefore significant doubt about whether such a scheme at European level would adequately resolve the identified problems.

The management of a transparency benchmark at European level, in particular the comparison between companies across all Member States, would be complex and costly. Whereas the Dutch transparency benchmark in 2019 looked at 240 companies using one language, a European scheme would need to compare several thousands of companies reporting in many different languages.

2) Standardisation: Additional non-binding guidelines issued by the Commission

Description of option:

The Commission issued general non-binding guidelines on non-financial reporting in 2017, as required by the NFRD. In 2019 the Commission issued supplementary

[285] https://www.transparantiebenchmark.nl/en
[286] *In Balance 2019 - Survey of value creation and follow-up to the Non-Financial Information (Disclosure) Decree*, Dutch Authority for the Financial Markets (AFM), December 2019

guidelines on how to report climate-related information. The Commission could issue additional non-binding guidelines on other specific topics on which corporate reporting is considered to be inadequate. Some stakeholders have suggested this option, including some business associations and individual companies in their comments on the Inception Impact Assessment for this initiative.

Reasons for discarding this option:

There is insufficient evidence that the existing non-binding guidelines have had a significant impact on the quality of non-financial reporting by companies under the scope of the NFRD. The problems identified in chapter 2 all exist in spite of the non-binding guidelines issued by the Commission in 2017.

In response to the 2018 public consultation, 36% of respondents who expressed an opinion thought the guidelines contributed to improve the quality of disclosures, while 33% disagreed. Many respondents considered that the guidelines were most useful for companies that had never previously reported non-financial information.

An analysis by the Carbon Disclosures Standards Board and CDP found "no direct evidence from companies that the Commission's guidelines accompanying the Directive were being used or having a positive effect on NFRD […] disclosures".[287] A survey of 55 Polish listed companies under the scope of the NFRD found that only 16% had used the guidelines.[288] The CEPS survey of companies under the scope of the NFRD indicates a somewhat higher proportion of respondents (44%) who say that they apply the 2017 guidelines to a full extent or to a high extent. The proportion of respondents that say they have applied the 2019 guidelines on climate reporting to a full or to a high extent is 11%, while 58% of the respondents did not apply the 2019 guidelines at all.

The guidelines are comprehensive in the sense that they cover the broad range of non-financial issues envisaged by the NFRD. However, they are not detailed enough to address the specific problems identified in this impact assessment, in particular the specific problems for users regarding comparability and relevance. For example, they do not define KPIs in any significant detail, they do not define the methodology behind KPIs and they do not define the non-financial issues that may be relevant to particular sectors. The guidelines are significantly less detailed than the principal existing private standards and frameworks used in the market, such as the standards of the Global Reporting Initiative or the Sustainability Accounting Standards Board.

The voluntary nature of the guidelines means that companies are free to apply them or not as they see fit. They therefore cannot on their own resolve the problems related to the comparability of information between companies or the non-disclosure of information

[287] "First Steps: corporate climate and environmental disclosure under the EU Non-Financial Reporting Directive", Carbon Disclosure Standards Board and CDP, November 2018

[288] Results of survey conducted at a conference on non-financial reporting organized by the Polish Association of Listed Companies, data gathered and analysed by the Foundation for Reporting Standards, September 2019. Author: PioMBiernacki.

that users believe is relevant. In this respect, the non-binding guidelines may even exacerbate the complexity faced by preparers if they are perceived as additional to the various private non-financial standards and frameworks in the market, without removing the pressure on preparers to consider each of those standards and frameworks individually and to respond in any case to additional information requests from stakeholders.

In addition, the non-binding guidelines themselves have explicitly indicated that they should not be used as basis for expressing conformity with the requirements of the NFRD. They do not therefore significantly contribute to resolving problems related to enforcement of the reporting requirements or the reliability of disclosed information.

If it is considered that companies require more detailed guidance, then this is best achieved by means of non-financial reporting standards, developed by a standard-setter through a recognised standard-setting process, rather than by means of additional non-binding guidelines issued by the Commission. Compared to additional guidelines from the Commission, standards are more likely to achieve a level of granularity that will successfully address the identified problems. A formal standard-setting process also provides a more effective means of incorporating the views and expertise of users, reporting companies and other relevant stakeholders.

3) *Standardisation: first developing voluntary EU standards before moving to a mandatory approach*

Description of option:

The Commission could propose the development of EU reporting standards for use on a voluntary basis for an initial period of time, and then introduce a requirement on companies to use those standards at a later date.

Reasons for discarding this option:

So long as reporting standards are voluntary, they will not resolve the critical issues of relevance and comparability identified in the problem definition. Voluntary standards, as opposed to mandatory standards, would also seriously undermine the effectiveness of the preferred options with regard to other variables analysed in this impact assessment, especially assurance, digitalisation, and supervision. Overall, any period during which EU standards were voluntary would simply delay the achievement of the policy objectives identified in this impact assessment.

4) *Standardisation: Endorsement of an international non-financial reporting standard*

Description of option:

The Commission could endorse an *international* non-financial reporting standard. Endorsement could take the form of a Commission recommendation, or it could mean a mandatory obligation on companies to use such an international standard. Additionally,

this option could either comprise endorsement of an *existing* international non-financial reporting standard (such as the Global Reporting Initiative or the standards of the Sustainability Accounting Standards Board); or it could comprise endorsement of *new* international non-financial reporting standards that would have to be developed in the future, such as the standards that may be developed under the auspices of the IFRS Foundation.

Reasons for discarding this option:

The principal reason for discarding this option is that an international standard could not meet the specific needs of the European context. The information reported by companies in the EU will need to align with the information that financial market participants will need to meet their own legal requirements under the Sustainable Finance Disclosure Regulation (SFDR) and its accompanying Regulatory Standards where relevant. In addition, information specified in non-financial reporting standards for use by EU companies will have to align to the extent possible with the EU taxonomy on sustainable economic activities. It will also need to be consistent with relevant EU legislation, including, for example, possible future legislation on due diligence and sustainable corporate governance. It is not reasonable to expect that any existing or future international standard could do that at the necessary level of specificity.

Secondly, no existing international standard adequately covers the two materiality perspectives that companies under the scope of the NFRD are already required to consider. The two most comprehensive private international standards in existence each cover one materiality perspective. The SASB standards consider financial materiality but not necessarily the impact of the company on society and the environment. Providers of capital are the target audience of TCFD reporting. The initial plans of the IFRS Foundation are to focus on climate reporting and from a financial materiality perspective only. The GRI standards, on the other hand, focus on the social and environmental impacts of the company but not on the risks to the reporting company arising from sustainability and other non-financial issues. The target audience of GRI reports is deliberately wide, and includes investors, customers and consumers, governments, other providers of financial capital, and NGOs.[289]

If comprising the endorsement of *new* international non-financial reporting standards, this option has also been discarded on the grounds that there would be little prospect of reaching global agreement on new international non-financial reporting standards that cover the full range of sustainability topics within the necessary timelines. Negotiations could be expected to take several years, considering the different starting-points and the divergence of views between different jurisdictions on critical issues such as climate and human rights. However, the financial market participants in the EU will already need information from investee companies that is aligned with the Sustainable Finance Disclosure Regulation and its accompanying Regulatory Standards from March 2021.

[289] Annex 13 provides a description of the main existing international non-financial reporting standards and frameworks.

A further consideration is the need for adequate political and democratic oversight of the content of any non-financial reporting standard that the EU might endorse or require. Given the political nature of many of the issues that such a standard would cover (e.g. human rights, environmental issues including climate), this kind of oversight is increasingly important. It is probably not feasible to ensure the necessary degree of political and democratic oversight in the case of an international standard.

The open public consultation carried out in preparation for this initiative asked respondents to what extent they believed that GRI, SASB or the framework of the International Integrated Reporting Council (IIRC), would, if applied on their own, resolve the current problems of reporting under the NFRD. Respondents had more confidence that the GRI standards could, on their own, resolve the identified problems compared to the SASB standards and the IIRC framework. However, even in the case of the GRI standards, only a fifth of respondents believed that they would resolve the current problems "to a very great extent."

5) *Scope: expand scope to all SMEs*

Description of option:

The Commission could propose to expand non-financial reporting requirements to all SMEs. This compares to package 3 (analysed in section 6.3.4) which would expand the scope to include all SMEs with securities listed on EU regulated markets, and to package 4 (analysed in section 6.3.5) which would expand the scope of the NFRD to all *medium-sized* companies whether listed or not. The specificity of this discarded option is therefore the expansion of scope to non-listed small and micro-enterprises.

Reasons for discarding this option:

This option was discarded at an early stage for reasons of proportionality. The evidence shows that user demand for non-information decreases with the size of the company. According to the SME Panel carried out in preparation for this initiative, 80% of medium-sized companies had received at least one request for some kind of non-financial information, compared to 45% of small companies.

In response to the open public consultation, the option of expanding the scope of the NFRD to all limited liability companies regardless of their size was by a considerable margin the least favoured of the different scope options. Of respondents who identified themselves as users of non-financial information, only 25% "mostly" or "totally" agreed with this option. In contrast, 45% of users explicitly opposed this option. When looking at responses from the financial sector, only 16% favoured this option and 60% explicitly opposed it.

Given the very large number of micro- and small-sized limited liability companies in the EU (over 13 million), the total estimated yearly incremental costs of requiring such companies to report non-financial information in annual reports would be of EUR 145

billion. Since users are also less interested in non-financial information from these companies, we concluded that this option should be discarded.