EUROPEAN COMMISSION

SEC(2021) 164

7.10.2020

REGULATORY SCRUTINY BOARD OPINION

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 sustainable corporate sustainability reporting

{COM(2021)189}
{SWD(2021)150}
{SWD(2021)151}

Brussels,
RSB

Opinion

Title: Impact assessment / Revision of the non-financial reporting Directive

Overall opinion: POSITIVE WITH RESERVATIONS

(A) Policy context

The Directive on non-financial reporting (NFRD) requires certain large companies to report on non-financial issues. These issues concern social, employee and environmental matters, human rights, bribery and corruption. Currently, companies find it difficult to know what to report. The information reported may not meet the needs of users (investors, civil society). It may be incomplete or not sufficiently reliable.

The EU is developing a range of sustainable finance legislation. In this context, user demand for non-financial information is expected to increase. The lack of adequate information creates risks for investors. It inhibits allocation of funds to activities that target the climate, environmental and social issues.

The objective of this initiative is that companies report information that investors and civil society need. It aims to avoid excessive reporting requirements. The ongoing fitness check on the reporting obligations for companies also looks at the effectiveness and burden of such reporting.

(B) Summary of findings

The Board notes the useful additional information provided in advance of the meeting and commitments to make changes to the report.

However, the report still contains significant shortcomings. The Board gives a positive opinion with reservations because it expects the DG to rectify the following aspects:

(1) The report does not sufficiently explain the coherence with other initiatives.

(2) The problem description does not clarify where it follows the conclusions of the draft fitness check and where it goes further. It does not show clearly how users' information needs increased significantly.

(3) The report is not sufficiently clear on the content of the options.

(4) The comparison of options is not sufficiently consistent and substantiated.

This opinion concerns a draft impact assessment which may differ from the final version.

(C) What to improve

(1) The report should better explain the coherence with related initiatives, such as the sustainable finance disclosure Directive and the taxonomy Regulation. It should clarify how it would ensure coherence with linked initiatives with a different timing, such as the green claims initiative.

(2) The problem definition should better clarify where it follows the findings of the draft fitness check and where it builds on additional evidence. It should better justify the need for standardisation of non-financial reporting. It should better clarify to what extent reporting standards require complementary methodologies to measure impacts or materiality. The report should better substantiate with evidence the evolution of non-financial risks and users' information needs, and better describe related drivers.

(3) The report should clarify what changes it intends to make to the NFRD and what will be left to implementing legislation, in particular on standardisation. It should also distinguish more clearly between the content of the revision of the NFRD and how the European Financial Reporting Advisory Group could support the standard development process. The report should better justify why it focusses only on some of the problems and treats others in the annex. The report should describe in more detail how interest groups are expected to hold companies accountable to environmental, social and governance standards. The report should explain why it did not include a gradual approach to EU standards, starting with voluntary use and then, after review, possible mandatory use.

(4) The report should better justify the scores given in the comparison of options. The effectiveness scores should better reflect the size of the change in scope of each option. The report should better explain the efficiency concept and justify the scores. It should clarify why it considers that there are no net costs for any stakeholder group for any of the options.

(5) The report should better elaborate the benefits for listed SMEs to be subject to the same information requirements as other listed companies. It should also clarify that non-listed SMEs can access other types of trading platforms that are not subject to NFRD reporting (such as SME growth markets).

(6) The report should be more explicit about overall costs and benefits of the preferred option. It should take into account also the options discussed in annex, to show the full expected impact of the preferred option.

The Board notes the estimated costs and benefits of the preferred option in this initiative, as summarised in the attached quantification tables.

Some more technical comments have been sent directly to the author DG.

<u>(D) Conclusion</u> **The DG may proceed with the initiative.** **The DG must revise the report in accordance with the Board's findings before launching the interservice consultation.** **If there are any changes in the choice or design of the preferred option in the final version of the report, the DG may need to further adjust the attached quantification tables to reflect this.**	
Full title	Revision of the Non-Financial Reporting Directive (NFRD)
Reference number	PLAN/2019/6123
Submitted to RSB on	10 September 2020
Date of RSB meeting	7 October 2020

ANNEX: Quantification tables extracted from the draft impact assessment report

The following tables contain information on the costs and benefits of the initiative on which the Board has given its opinion, as presented above.

If the draft report has been revised in line with the Board's recommendations, the content of these tables may be different from those in the final version of the impact assessment report, as published by the Commission.

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;[1] • reduction of costs for preparers from addressing investors ad hoc requests for information;[23] • 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;[87]	Stakeholders who benefit: reporting companies (preparers)

[1] CEPS study shows that companies that find it more difficult to decide which information should be included in the nonfinancial 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).

[2] 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 20 for a detailed cost analysis.

[3] % 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%).

Requiring limited assurance on reported information	• public availability of reliable information; • ensure all companies under the scope of the NFRD are reporting appropriately; • reduction of expectation gap from users perspective, brining clarity and a common level of assurance to all information reported;	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)
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;[4]	Stakeholders who benefit: • investors • reporting companies (in their capacity of users of information: from suppliers, clients and investee companies)

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

<table>
<tr>
<td>Requiring disclosure in management report</td>
<td>• 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 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;</td>
<td>Stakeholders who benefit:

• investors
• civil society organisations and trade unions
• policy makers
• national supervisors
• reporting companies (in their capacity of users of information: from suppliers, clients and investee companies)</td>
</tr>
<tr>
<td>Strengthening of supervision regime of non-listed companies</td>
<td>• ensure all companies under the scope of the NFRD are reporting appropriately;
• increase trust in reported information;
• improve quality of reporting;</td>
<td rowspan="3">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)</td>
</tr>
<tr>
<td>Tasking ESMA with issuance of guidelines</td>
<td>• ensure supervisory convergence, ensuring consistent information across the single market;
• costs savings for supervisors due to clarity about how to supervise non-financial reporting</td>
</tr>
<tr>
<td>Tasking ESMA with issuance of report on supervisory challenges</td>
<td>• better overview of supervisory challenges
• ensure continuous improvement in supervision and application of the reporting standards;</td>
</tr>
<tr>
<td rowspan="2">Clarification in law of double materiality concept</td>
<td> clarity that reported information is relevant from either of both of the materiality perspectives</td>
<td>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)</td>
</tr>
<tr>
<td> clarity about what information is required to be reported, costs savings for prepares</td>
<td>Stakeholders who benefit:
 reporting companies (preparers)</td>
</tr>
</table>

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 nonEU 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 would translate into a competitive advantage for more sustainable companies (will be more easily identifiable);	Stakeholders who benefit: reporting companies (preparers)
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)

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
Admin costs: Tagging reports against digital taxonomy	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 (nonlisted 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 audit services
	Indirect costs	NA	NA	NA	NA	NA	NA