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EBF response to the Inception Impact Assessment on the Non-Financial Reporting Directive

General comments

A European approach, case for an EU Regulation

A European initiative to improve the disclosure of non-financial information makes better sense and will be more effective than measures taken by individual member states. The current non-financial disclosures legislation comes in the form of an EU Directive that is subject to national implementations, using a number of national discretions that may differ in several ways and hamper an efficient implementation of a standardized, digital reporting ecosystem across Member States. Large companies most often operate in multiple EU Member States with multiple banking relationships. Harmonized disclosure requirements would benefit both companies and banks and decrease administrative burdens. The NFRD should therefore take the form of a Regulation, not a Directive.

Cost vs usefulness of the information

Balance between the desired level of transparency and the costs to the businesses should be found. Additional reporting requirements can only be justified if there is clear evidence that the information will deliver additional benefits. The importance of the materiality principle should be recognised. Detailed information should only be required if they are relevant with respect to the identified risk and strategy.

When seeking to find the right balance between costs and benefits, best practices in the current use of the standards, possible gaps in the regime as well as where existing requirements could be simplified or removed if not useful should be examined more closely before extending and strengthening the provisions of the NFRD. Availability of relevant data should be part of such an assessment.

Functional and coherent approach

A well-designed framework that balances the notion of materiality with a right level of details to drive consistency and coherence of the reported information is needed.

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Consistency across existing and future frameworks must be ensured, avoiding incoherence and overlaps. The Taxonomy and Disclosure Regulations but also CRR II (Article 449a) of CRD IV (Article 98), EBA Guidelines on Loans origination and monitoring and the NFRD (and KPIs in guidelines) et al. should constitute a coherent regime.

Harmonized format and structure

The harmonization of companies' ESG reporting should be part of the objectives of the upcoming review of the Non-financial Reporting Directive. While ideally the ESG reporting should be developed globally and at all levels of economy to fulfill the data gap, we support the EU to take a lead role and to start the work of standardizing the format and the structuring of companies' ESG reporting.

We suggest that the EU creates a single ESG reporting framework, building on the existing market tested models and practices. This framework does not need to be developed from scratch but could comprise of a combination of the leading existing reporting frameworks, which are compatible and could be matched with each other.

An EU minimum reporting standard could reflect best practices from companies' ESG reporting point of view and another would ensure financial materiality of ESG issues from investors' point of view. This could save the EU authorities the time needed for the development of a completely new reporting model and it would save companies the time and resources that currently are spent on fulfilling several differing ESG-reports and questionnaires, depending on who's asking.

We suggest building the EU minimum reporting standard on the key data points and KPIs that are necessary to apply the taxonomy and the sustainability disclosures regulation, and more specifically to demonstrate the investment's environmental impact.

Public EU ESG Data register

The biggest challenges regarding ESG data at the moment are the lack of comparability, the high costs of ESG data and the subsequent unaffordability of the data to smaller investors. A more harmonized and comparable information of companies' ESG performance would facilitate the collection of raw ESG data from companies that could be done via a single EU data register that could be opened, under specific conditions, to financial market participants.

Specific comments

Alignment with the taxonomy, usability of the data

The dependency on corporate disclosure is not adequately recognized by the Taxonomy Regulation. Given the current gaps in data availability and reporting, the legislative text proposes to shift the burden of data collection towards financial market participants by proposing individual engagement with companies or to buy data from third party providers. There is an unrealistic expectation and wrong assumption that only in exceptional cases, information will not be available justifying the shift of the data collection burden towards financial markets participants. In addition, the lack of data availability impacts all stakeholders, including data providers.

The application of the current NFRD does not provide banks with sufficient information to fulfil their current and forthcoming disclosure requirements (Regulation xx and the Guidelines on NFRD regarding climate related information). The current reporting is largely qualitative, non-standardized, and difficult to compile and analyse across companies/industries. Further harmonisation regarding the metrics and KPIs used (a common methodology), in order to make the information comparable, is crucial.

The data is also necessary for the successful implementation of the taxonomy, ideally in a most automated way. Manual assessment, data collection and processes represent a major obstacle to acceleration of the sustainability agenda. The NFRD requirements should therefore be closely aligned with the requirements of the Taxonomy and its screening criteria. Codification of the taxonomy and the ability for banks and other stakeholders to be able to process environment-related reporting data automatically is key to ensuring a successful implementation of the objectives of the Sustainable Finance Action Plan.¹

Broadening of the NFRD scope

Taking into account the new provisions for non-financial reporting under article 4 delta of the Taxonomy regulation, the legal act should:

1) Modify the scope in a proportionate way, to add certain categories of companies not currently covered by the NFRD as follows

A) 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.

B) 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. Information on climate risk is essential for TCFD reporting as integrated into the EU Non-financial reporting guidelines.

C) A simplified minimum reporting framework or Guidelines could be considered for the remaining companies taking into account materiality, proportionality and possible gradual implementation.

Inclusion of SMEs, whose lack of data poses a problem for banks should be considered based on a minimum and possibly simplified set of information that could be provided by SMEs in a structured manner consistent with EU standards, given due considerations to proportionality and materiality. This will further

¹ For alignment of the environmental classifications that are also part the data requirements of the System of Environmental Economic Accounts (SEEA) that EU member states use for their environmental economic accounts with the taxonomy, please refer to the following links:

<https://www.ebf.eu/wp-content/uploads/2019/03/Sustainable-Finance-Enviromental-Taxonomies-in-Europe-EBF-feedback-and-proposals.pdf>

<https://ec.europa.eu/jrc/en/publication/joint-jrc-eba-workshop-banking-regulation-and-sustainability>

facilitate bank's support to businesses and development of new sustainable products and services. In a first stage, only SMEs from sectors with a high transition risk.

Broadening of the scope may require a gradual approach and a development of training schemes at European level on criteria and norms on which sustainability activities thresholds for mitigation are defined and that could help specific financial actors and non- financial enterprises to build a common understanding of the taxonomy and disclosure requirements. Local authorities and public sector could also provide tools to calculate the carbon footprint etc.

2) **Specify in more detail what non-financial information companies should report, namely a common minimum set of key performance indicators; these KPIs must be aligned with the**

- The list of Taxonomy-compliant activities and products they produce. Companies could follow the reference to metrics in the taxonomy and indicate where they stand compared to the threshold.
- The environmental characteristics of the respective activities and products (including process and product certifications, environmental product claims or declarations – EPD - and life cycle analysis declarations - LCA) or the products' environmental applications, and
- Gradually, companies should be requested to report the associated revenues and expenses of eligible products or activities (as a percentage of the total) and the associated sustainable assets (as a percentage of the total).

Article 4 delta of the Taxonomy Regulation should align the reporting obligations with the NFRD.

Strengthening the provisions regarding the assurance of non-financial information.

Data must be sufficiently validated and assured in order to minimize risks of green washing and to allow banks and other users to rely on those data without further validation. Third-party limited assurance should be carried out according to the ISAE 3000 standard to ensure comparability for companies.

Third-party assurance would also help companies improving non-financial reporting by identifying areas for improvement. However, the burden on small companies should be taken into account e.g. by exempting group C from the validation an assurance in the short term.

Publication of the information

We acknowledge the possibility to integrate the non-financial information in the management report, keeping them separate from the financial report. It is crucial that the non-financial information remain separate from the financial information both in order to be informative and to retain the integrity of the financial information.

Nevertheless, it should still be possible to be published as a stand alone document.; i.e. a sustainability report or similiar published on company website at the same time as the Annual report.

Digital data format from a central data register

The EU should open up its databases that collect environmental reporting data and make those re-usable for finance providers. Data should be collected in a central EU repository and made available digitally to financial market participants in order to ensure that data are widely accessible across MS in an open source format. The public sector (national banks, local authorities, utility companies, ...) could publish their data (energy efficiency, air pollution, ...) on a statistical basis, protecting the private information for individuals².

We are therefore proposing that the EU Commission put in place or support infrastructures to collect periodically, with the help of new reading technologies, existing climate change mitigation and adaptation data of companies that published non-financial statements under the NFRD and other available relevant information or, at least, identify the sources. A centralized database would facilitate building of ESG disclosures and the access to relevant and reliable data at the EU level. The register could be administered by Eurostat.

The EU Commission could further launch a project to identify the information gaps of relevant climate change mitigation and adaptation information. Digital information and central repository will also facilitate identification of the information gaps and identify sources of additional information etc

Enforcement regime and supervisory convergence

As regards supervision, the regime must be harmonised. This is especially important in markets, activities and finance which are increasingly cross-border in character. Thus, there are strong arguments to be made for a distinctly harmonised framework. Excessive flexibility for Member States and national supervisors is more likely to create friction on the market.

ESMA should be charged with ensuring the consistent application of the rules just as it is for prospectuses and annual reports.

² Ensuring secure processing with adequate confidentiality and clarifying the responsibilities of the parties involved will thus be essential for a well-functioning regime and practices to evolve