BETTER FINANCE
The European Federation of Investors and Financial Services Users
Fédération Européenne des Épargnants et Usagers des Services Financiers

Ref: Corporate Sustainability Reporting

Link to consultation: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12129-Corporate-Sustainability-Reporting_en

BETTER FINANCE feedback on Corporate Sustainability reporting

About BETTER FINANCE

BETTER FINANCE, the European Federation of Investors and Financial Services Users, is the public interest non-governmental organisation advocating and defending the interests of European citizens as financial services users at the European level to lawmakers and the public in order to promote research, information and training on investments, savings and personal finances. It is the one and only European-level organisation solely dedicated to the representation of individual investors, savers and other financial services users.

BETTER FINANCE acts as an independent financial expertise and advocacy centre to the direct benefit of European financial services users. Since the BETTER FINANCE constituency includes individual and small shareholders, fund and retail investors, savers, pension fund participants, life insurance policy holders, borrowers, and other stakeholders who are independent from the financial industry, it has the best interests of all European citizens at heart. As such its activities are supported by the European Union since 2012.

Introduction

In May 2018, The European Parliament called for further developments of reporting requirements in the framework of the Non-Financial Reporting Directive (NFRD). In December 2020, a resolution on Sustainable Corporate Governance has been launched including the commitment to review the NFRD and increase its scope to additional categories of companies.

In April 2021, the European Commission has published the proposal for a directive to amend the existing rules on non-financial reporting standards. The review follows a series of consultations and the establishment of the European Corporate Reporting Lab under the European Financial Reporting Advisory Group (EFRAG).

The primary users of the information on the sustainability of the company are mostly investors, NGOs, social partners and other stakeholders. Among investors there are not only asset managers but also individual investors who are interested in the sustainability of the companies they want to invest in.

The main changes to the EC's proposal for the NFRD are:

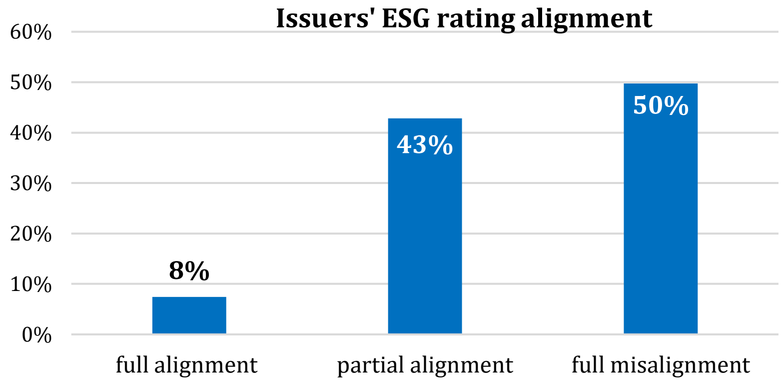
- The extend the scope of reporting requirements to a larger group of companies which includes all large companies and listed companies with the exception of listed micro companies.
- To require assurance of sustainability information
- More specifications on what to disclose regarding sustainability information and requirements in line with the EU sustainability reporting standards.
- Information disclosed as part of the companies' management reports, disclosed in a digital

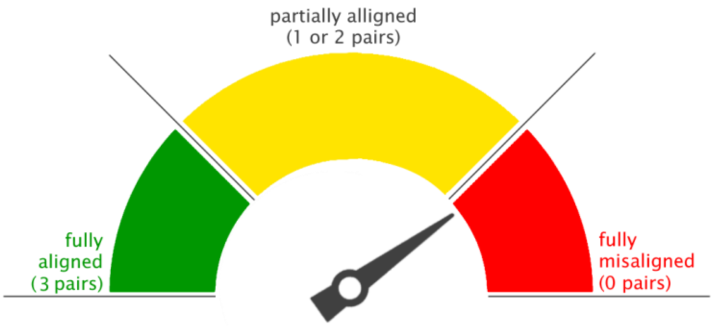
machine-readable format.

BETTER FINANCE Feedback

BETTER FINANCE welcomes the new changes and the scope of the Non-financial Reporting Directive. Individual investors are in dire need of comparable and accessible information that can help them to make an informed decision regarding their investments, in particular regarding the long-term risks in terms of sustainability that affect the company they want to invest in. In addition, in order to reach the EU climate objectives and targets set in the EU Green Deal, it is necessary to obtain robust data on environmental, climate, social/community impact and governance issues that companies are facing.

In our research on sustainable investments funds, we look at ESG rating for issuers. ESG scores, rankings or ratings provided by ESG rating providers. The research team collected the ESG ratings for the ten largest holdings of the funds in a sub-sample from three rating providers, totalling 1,079 companies. The findings are quite concerning of these 1,079, 149 (14%) did not have any publicly available ESG-rating, 138 (13%) only had one rating available, and for the rest (73%) we could find either 2 or three ESG ratings. We compared the ESG-ratings and found that 43% are potentially either fully or partially aligned, while the rest (50%) were inconsistently rated by rating providers.





The reason for this high degree of misalignment is due to two different factors:

- Lack of available and reliable data provided by companies/issues. (And this can be tackled by the review of the non-financial reporting).
- Different methodologies used by ESG rating providers which determine different results in terms of ratings and sustainability of the companies. For this reason, it is also important to have a common understanding and approach in the definition and evaluation of sustainability risks. It is necessary to align practices on the assessment of sustainability criteria. Otherwise, divergent and

contradicting ESG ratings/scores would mislead financial services users in their investment choice.

Review, definition and improvement on sustainability reporting is an essential step towards addressing EU climate targets and shift to more veritable green investments, as stated by the Executive Vice-President Vladis Dombrovskis in the EU Commission communication on 21 April 2021: "*Europe was an early leader in reforming the financial system to support investments for climate change. Today, we are taking a leap forward with the first-ever climate taxonomy which will help companies and investors to know whether their investments and activities are really green. This will be essential if we are to mobilise private investment in sustainable activities and make Europe climate-neutral by 2050. This is a ground-breaking step for which we have consulted far and wide. We left no stone unturned in seeking a balanced, **science-based outcome**. We are also proposing improved rules on sustainability reporting by companies. By developing European standards, we will build on and contribute to international initiatives.*"[1]

Scope

We believe that the changes in the scope by including listed and non-listed companies is an important step forward in terms of coverage of the directive. However, we would have expected that also non-EU companies active in the EU would fall under the directive. This exclusion of non-EU countries could generate unequal treatment, and unfair competition. The review should enable a strong alignment with the taxonomy regulation and its technical standards which include thresholds and metrics. It is also essential to ensure that not only companies' policies are disclosed but also the impact of these policies. In addition, as already advocated by BETTER FINANCE, non-financial information should be also disclosed on the **Summary Prospectus of listed companies**.

Requirements

We welcome the inclusion forward looking indicators in line with the Paris Agreement limiting global warming to 1.5C. These indicators are also extremely relevant to monitor whether companies are taking the necessary initiatives to reduce CO2 emissions. However, the information on human rights policies is not clear. We believe that the NFRD should give equal importance to environmental/climate and social issues.

Intangibles

We are strongly support the inclusion of intangibles in the Non-Financial Reporting. So far intangibles were not reflected through financial reporting even though they are key to the development of the business and the value creation. Intangibles bring an added value in terms of non-financial reporting in particular regarding the assessment of the sustainability of the company. Specific rules and recommendations on how to assess and measure intangibles are necessary in order to streamline the information disclosure of these companies' assets. This is particularly relevant with the rise of big tech companies which rely mostly on intangible assets as brand value, consumer list, consumer satisfaction, loyalty, etc.[2]

[1] https://ec.europa.eu/commission/presscorner/detail/en/ip_21_1804

[2] For additional information on intangibles please see our survey response: https://betterfinance.eu/wp-content/uploads/BETTER-FINANCE-response-to-the-survey-on-Intangibles-Final.pdf

Assurance

BETTER FINANCE believes that one of the main issues is the lack of understanding on the reporting of sustainability. Due to the divergent practices, it is extremely important to harmonise and standardise the assurances approaches based on the review of rules in the Non-Financial Reporting Directive. This should include metrics, standards and thresholds. Nevertheless, the requirement for auditing non-financial aspects should reach the same standards of financial aspects.

Even if, the limited insurance seems to be a step forward, we should reach a higher level of assurance (such as reasonable assurance) equal to what is already achieved for financial information.

Digitalisation

We welcome the digitalisation of the information which can generate benefits, such as comparability and accessibility. However, it is crucial to ensure that the digital tagging process does not undermine the whole process and will facilitate the analysis of sustainability risks of the companies. The tagging of non-financial information would only be possible if reporting is compliant with standards. Therefore, coordination and harmonization with the taxonomy is crucial on this aspect. The centralization of information via a single access point would facilitate the accessibility of the information for investors.