

EUROCHAMBRES position on the proposal for a Corporate Sustainable Reporting Directive

European SMEs need a regulatory framework that allows them to look at their business models and develop practical capacities to report sustainability, without jeopardising the access to supply chains nor burdening them with onerous and unnecessary red tape.

EUROCHAMBRES believes it is crucial to guarantee proportionality by adopting a voluntary and simplified sustainability reporting standards for SMEs, creating incentives for more responsible business conduct, and providing tailored guidance for small businesses to report more and better¹.

In April 2021, the European Commission published a proposal for a new Corporate Sustainability Reporting Directive (CSRD) which revises and strengthens rules introduced by the Non-Financial Reporting Directive (NFRD), extends the NFRD's scope and aims to ensure that companies report reliable and comparable ESG information.

EUROCHAMBRES overall welcomes the Commission's push to streamline parallel legislative initiatives, especially in connection with sustainable finance and sustainable corporate governance, and the proposal's objective to align existing reporting requirements under harmonised EU reporting standards. This is important step towards encouraging European companies to adopt more sustainable processes and integrate ESG information into their corporate reporting cycles.

However, the proposed obligations more than quadruples – and in some countries increases by 30 times – the number of companies that will need to report substantially more and should offer the necessary support for SMEs to quickly gather knowledge and expertise in sustainability reporting. The proposal needs to guarantee the level-playing field for smaller, unlisted businesses involved in large undertakings' supply chains who might be forced to report according to top-down cascade standards ill-suited to their size. Furthermore, the proposal does not cover large non-listed, non-EU companies that most likely adhere to less stringent disclosure requirements on social and environmental standards. This does not lead to the desired level-playing field but to competition and market distortions.

Additional gold-plating at the Member States' level at the expense of businesses should also be averted at all costs. The goal must be to achieve a coherent, efficient regulatory framework that places as little burdens as possible on entrepreneurs overall.

According to the Commission's "**One In, One Out**" approach, an increase of administrative burdens must go hand in hand with an equivalent reporting relief. Consequently, Chambers invite EU decision-makers to reassess key provisions anchored in the "**Think Small First**" principle with the overall goal of achieving proportionality.

¹ Due to the parameters of its mandate DIHK abstains from expressing an opinion on the topic addressed in this paper.

1. SCOPE.

The 500 employees' threshold of the non-financial reporting requirements brought in by the NFRD was intended to strike a balance between the costs and benefits of non-financial reporting requirements, despite some Member States adopting a lower threshold of 250 employees. It is also important to remember in this context that corporate structures as well as the size of companies vary between member states and that companies have started to report according to the NFRD for the first time only in 2018.

The extension of the scope to listed SMEs also poses problems, first and foremost to those already listed in regulated markets, which may feel encouraged to transfer to other trading venues or even to delist. Secondly, since the obligations for listed SMEs are higher than for non-listed SMEs, the proposal promotes an uneven level-playing field solely based on the funding source, contributing to the debt-equity bias.

EUROCHAMBRES also believes that change in the scope would entail a seismic shift for many non-listed companies across the EU, many of them family businesses, especially those in Member States that implemented the 500-employee threshold.

In addition, EU decision-makers need to be aware for the financial situation and difficult financing conditions with which European SMEs are currently confronted due to COVID-19. Many companies with less than 500 employees are not only facing the prospects of insolvency but also the lifting of banks' moratoria on the repayment of loans. European companies are expected to struggle in the medium/long-term and will not be able to cope with the inconvenience of reallocating financial resources to report sustainability as demanded by Article 19a, when in fact they are struggling for their survival.

In order to ensure regulatory stability, EUROCHAMBRES suggests:

- 1.1. Maintaining the NFRD's scope limited to companies with more than 500 employees.**
- 1.2. Upholding the extension of the scope to EU subsidiaries of non-EU companies as well as non-EU companies with transferable securities listed on a regulated EU market.**
- 1.3. The extension of the scope to large non-listed, non-EU companies.**

2. SUSTAINABILITY REPORTING STANDARD AND REPORTING AREAS

First, Chambers would like to point out that existing climate-related reporting standards and frameworks such as GRI have helped a wide range of stakeholders such as companies, investors and NGOs to handle ESG information in a flexible manner. ISO also provides useful voluntary, consensus-based standards on ESG that are internationally recognised and accredited by independent parties from 165 countries. However, we acknowledge that different standards have also contributed to non-financial reporting divergences that may have hindered comparability sought by investors.

EUROCHAMBRES welcomes the proposal's efforts towards conceiving EU-wide sustainability reporting standards that harmonises concepts, metrics, procedures, and

existing standards, allowing businesses to identify and monitor the ESG risks to which they might be exposed, and implement adequate measures to address them.

Within this harmonisation exercise, it is important to highlight that creating a uniform set of standards to measure and compare non-financial risks across vastly different companies operating in different industries, across various jurisdictions, and therefore facing remarkably diverse non-financial challenges may be difficult to attain. The diversity of "*non-financial*" issues faced by different companies makes it necessary to have purely sectoral elements. It would be therefore useful that the Commission indicates as precisely as possible the information to be published by the different sectors. EUROCHAMBRES believes that the Commission should set a clearly defined harmonised reporting framework, adapted to specific sectorial needs as some international non-financial reporting frameworks like GRI or SASB already do. This would also contribute to align the CSRD with the recently taken ecosystem approach of the [updated EU Industrial Strategy](#).

In order to guarantee a smoother transition, non-mandatory application of the new standards during an initial phase could be envisaged, during which the configuration of reports, the double materiality principles and other important information could be calibrated.

From the perspective of internationally active companies, the European legislator should closely monitor any developments at the global level linked to sustainability reporting e.g., on-going discussions to adopt an IFRS standard, and strive for the highest possible level of harmonisation from the outset to avoid or minimise any additional sustainability reporting obligations for internationally oriented companies. For companies whose activities do not require such an adaptation to international sustainability standards, however, such an approximation of the standards could lead to additional, unnecessary requirements.

In the case of smaller companies, reporting sustainability should be exclusively voluntary as the scarcity of relevant information reported by smaller players is overwhelmingly linked to high costs and difficulties when it comes to illustrating ESG risks, scale breadth and complexity. Furthermore, important administrative burdens risk to slow down decision-making processes in companies, eventually damaging their competitiveness vis-à-vis non-EU companies.

EUROCHAMBRES agrees with having simplified reporting standards applied to SMEs. As such, the Commission needs to put in place provisions to mitigate the reporting pressure on SMEs and shield them from complying with larger undertakings' standards. Failing to guarantee proportionality will result in supply chains' disruptions and affect Europe's competitiveness, at a time where major industrial ecosystems are struggling to recover.

Despite being less acquainted with ESG reporting, SMEs are contributing to the best of their ability. EU decision-makers need to carefully assess the risks of putting a strain on the resources of SMEs and research more on the specific needs of investors. We should avoid information overload for both the investor, and for the company.

Chambers support companies adoption, social and environmentally responsible actions, for example by advising companies, offering further training, conducting events and drafting guidelines. The companies are accompanied in their voluntary CSR commitments, the know-how transfer between companies is promoted and best-practice examples are highlighted. Hence, companies perceive CSR as competitive advantage which is the most sustainable incentive for the sustainable transformation currently being pursued. Against that background we plead for tailor-made guidance, that facilitate a market based process towards sustainability. EU programmes such as the InvestEU and the Enterprise Europe Network could provide de-risking mechanisms and extra advisory services on sustainability, but only if additional budgetary resources are allocated to that end.

- 2.1. During an initial phase, non-mandatory application of the new reporting standards could be envisaged, allowing all businesses to calibrate the reporting narrative.**
- 2.2. Guidelines to ensure that specific aspects of given sectors are included in the information reported by the company would be desirable.**
- 2.3. Simplified reporting standards for listed and unlisted SMEs should remain voluntary.**
- 2.4. Mitigate the pressure on SME suppliers involved in large companies' supply chains by ordering the use of the simplified standard.**

Furthermore, the Commission should avoid exacerbating competitive disadvantages by clarifying what it means by reporting on “supply chain and other business relationships”. The small business community especially need assurances, in the sense that not only the simplified reporting standards remains voluntary for SMEs, but also larger undertakings accept them as part of a well-performing and trusting supply chain relationship management. The use of templates, estimates, and other tools prepared by the Commission should not be underestimated.

Caution must be exercised when obliging companies to include the impact of their suppliers within their sustainability disclosures. Since a considerable number of suppliers could be smaller in size, they would likely be exempt from reporting on such matters, and so are unlikely to have the required information at hand. This could add an additional burden for companies within the scope of the proposal to access and present that information, while also burdening micro and small companies disproportionately in adhering to their clients' request for information.

The disruptive changes brought by the proposal require a strong “comply or explain” approach and enough flexibility for companies to identify which topics are most material for them to report. EUROCHAMBRES believes that companies should be given room for manoeuvre in case they do not pursue policies vis-à-vis the new reporting categories stated in Article 1(3) of the proposal, allowing them to provide a clear and reasoned explanation on how this conclusion was reached.

There is also a risk that the publication of sensitive data could lead to false conclusions being drawn about the business model, technical developments. or process innovations of companies. The need to report about political engagements of the undertaking, including its lobbying activities, is also too far-reaching as simple business outreach campaigns or interviews given to media outlets could be considered as a political move,

according to some stakeholders. It is important to recall that according to the GDPR companies are not allowed to ask their employees about their political affiliation. Consequently, the management/board should also not be forced to do so.

Chambers reiterate the need to:

- 2.4. Reinstate the “comply or explain” provision to avoid box-ticking.**
- 2.5. Carefully assess the impact on SME suppliers linked to reporting about business relationships across the value chain.**
- 2.6. Ensure that sensitive business information on e.g., innovation processes, intellectual property, and other intangible assets, should not have to be reported.**
- 2.7. Abstain from obliging undertakings to report about their political engagement and lobbying activities.**

EUROCHAMBRES respects EFRAG’s prominent role in developing EU sustainability reporting standards. Chambers invite EFRAG to regularly exchange views not only with the European Securities and Markets Authority (ESMA) and the European Supervisory Authorities (ESAs) but especially with corporates’ representatives to build a more business-friendly interconnectivity between sustainability and financial reporting. Special outreach sessions to different regions in the EU proved to be particularly effective and should be continued. However, the input from the International Accounting Standards Board (IASB) should be carefully considered, as European listed SMEs largely rely on local GAAP and should not be obliged to follow potentially unsuitable IFRS-led sustainability standards.

Furthermore, subsidiary companies are exempted from the reporting obligations 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. EUROCHAMBRES believes that the reporting at group level granted under the NFRD should be upheld, as requested by most respondents to the public consultation. Even though subsidiaries do not have to draft their own report to date, they are faced with the efforts of providing the necessary information to their parent companies, which should not be under-estimated.

Lastly, and as a general remark, it is key to work towards greater coordination and interoperability between different administrations as means to reduce the information requirements requested to companies. Promoting these collaborations will have positive effects both in terms of certainty and transparency, as well as in the reduction of administrative costs borne by companies.

- 2.8. EFRAG should regularly consult with business representatives during the drafting of the sustainability reporting standards.**
- 2.9. Exempt subsidiaries from reporting in case the parent company already abides by the sustainability reporting obligations.**

3. LOCATION OF THE REPORT

The proposal removes the possibility for Member States to allow companies to publish the required information in a separate report that is not part of the management report. EUROCHAMBRES disagrees with this removal because well-established processes, such as the use of cross-references, have not caused any inconvenience for corporates nor investors.

Including an obligation to report on sustainability matters in the management report takes away important flexibility for companies in terms of when and where to publish sustainability information, such as the flexibility to report separately to investors and stakeholders. In addition, timing is important to companies. Financial information is far easier to collect, whereas non-financial information may take longer to gather, making it difficult to ensure synchronised releases of such information.

The principle of sustainability reporting is based on the premise that key stakeholders who are impacted by the actions of a company can see how they are affected through the disclosed sustainability information. A standalone sustainability report presents a better opportunity to those stakeholders to extract the required information, rather than having it buried in an extensive management report. Obliging the inclusion of sustainability information in the management report takes away from a company's ability to sufficiently place the information in context.

3.1. Companies that wish to report in the management report should not be precluded from doing so, but this should remain optional.

4. DIGITAL FORMAT

The proposal obliges preparers of the sustainability report to digitally tag the non-financial information in a standardised machine-readable format, developed under the ESEF Regulation, to facilitate its searchability and usability by investors and other stakeholders.

EUROCHAMBRES reiterates that common data formats such as MS Word, MS Excel, RTF, or PDF are inexpensive, readily available, and easy to access by civil society. The XBRL reporting system is complex, extremely costly when compared with other online tools, and that XHTML markup language is largely unsuited for non-listed undertakings. SMEs also do not have in-house knowledge on financial reporting and expertise, which means they would have to rely on external consultants from third party providers – an often-costly exercise.

Flexible solutions must be offered so that companies can report sustainability in the format they are more acquainted with.

4.1. ESEF tagging of information should not be mandatory for non-listed companies, especially SMEs.
4.2. The submission of the report should be allowed in a standard data format.

5. ASSURANCE AND PENALTIES

Sustainability information must not be treated in the same way as financial information due to its largely qualitative and context-based nature. EU decision makers should realise that mandatory assurance of very long and detailed reports leads to disproportionate burdens and costs, especially for first-time preparers. Companies will require a large number of in-house staff and those experiencing financial constraints – a large majority in the current situation – will not be able to allocate enough resources for assurance services, nor engage a third party that performs such service.

In this context, the ownership of the assurance must also be considered. Clarity needs to be provided on whether those providing assurance on sustainability reports can provide other consultancy services, or whether it is sufficient for firms to provide reporting and assurance services if consultancy and assurance teams are kept separate and independent. Additionally, businesses feel uncertainty about the depth of the audit, how the process takes place, how time consuming it is, and the level of additional documentation needed.

It remains unclear whether auditors will have the necessary expertise to move to assurance of sustainability information within the timeline envisaged for implementation of the Directive. The availability of such resources to meet the new demand and to the right levels of expertise, would need to be nurtured through a coordinated effort with educational and regulatory institutions, with the input of stakeholders, to ensure that warranted professionals are available to adequately deliver such services to companies, as necessary. It is not an exaggeration to say that such a process may likely need years to develop.

EUROCHAMBRES is also against any penalties or punitive excesses with regard to any violation of reporting obligations. If a penalty provision is unavoidable, the principle of “advice instead of punishment” could be implemented in the law. This could generate a risk of frivolous litigation instead of having concrete and positive impacts on companies.

- 5.1. The external audit requirement to sustainability information should be reconsidered due to the additional costs and burdens.**
- 5.2. The Commission should launch a campaign with educational and regulatory institutions and the participation of stakeholders, to ensure that audit professionals can deliver such services.**
- 5.3. Avoid a punitive approach, focusing instead on self-responsibility.**

6. TRANSPOSITION AND IMPLEMENTATION

EUROCHAMBRES feels that the timeline for developing the standards is far too ambitious and could result in a lack of alignment due to it running in parallel to the institutional negotiation on the proposal. Quality should be prioritised over speed and the development of standards should commence once political agreement on the proposal is reached.

The first set of reporting standards needs to be adopted by 31 October 2022, transposed, and applied just two months later. Companies reporting sustainability according to the

new Directive, especially first-time preparers, need additional time after the final standards have been adopted by the Commission to build-up their capacity, carry out high-quality disclosure assessments on highly detailed and prescriptive information, and create better reports.

It is proposed that a transition period is implemented whereby reporting will be voluntary for a pre-determined amount of time, allowing companies to be able to build the required capacity. This would ensure upholding the required standard of reporting until such a time that reporting becomes an obligation. The Commission should also consider the fact that educational campaigns will need to be held at an intense pace at national level on the subject, which will take time of its own right, hence the need for lengthening the timeline.

Furthermore, any delay in the adoption and publication of the reporting standards must automatically trigger a delay in their application. The situation where the Commission requires level 1 compliance, but companies are practically unable to comply due to the lack of Level 2 (and Level 3), needs to be avoided. These concerns also relate to the application of Art. 8 Taxonomy Regulation.

6.1. Extend the timeline for the development, transposition and application of the standards, allowing businesses to correctly deliver sustainability information and avoid potentially costly mistakes.

EUROCHAMBRES – The Association of European Chambers of Commerce and Industry represents over 20 million enterprises in Europe – 98% of which are SMEs – through 45 members and a European network of 1700 regional and local Chambers.

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