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BANKING AND FINANCE

Targeted consultation on the update of the non-binding guidelines on non-financial reporting

Fields marked with * are mandatory.

Introduction

Disclaimer:

Nothing in this document commits the European Commission or prejudices any decision by the Commission regarding the update of the the non-binding guidelines on non-financial reporting.

The non-financial reporting Directive (2014/95/EU) requires large public interest entities with over 500 employees (listed companies, banks, and insurance companies) to disclose certain non-financial information. As required by the directive, the Commission has published non-binding guidelines to help companies disclose relevant non-financial information in a more consistent and more comparable manner.

In March 2018 the Commission published the action plan on financing for sustainable growth, with the aim of reorienting capital towards sustainable investment, managing financial risks that arise from climate change and other environmental and social problems, and fostering transparency and long-termism in financial and economic activity.

As part of that action plan the Commission committed to updating the non-binding guidelines on non-financial reporting, specifically with regard to the reporting of climate-related information. In practice, it is expected that the update will consist of a new supplement to the existing guidelines. The Commission expects to publish the new supplement on the reporting of climate-related information in June 2019.

In June 2018, the European Commission set up a technical expert group on sustainable finance (TEG) to assist in four key areas of the action plan through the development of

1. a unified classification system for sustainable economic activities (taxonomy),
2. an EU green bond standard,
3. benchmarks for low-carbon investment strategies,
4. new guidelines on the reporting of climate-related information.

In January 2019 the TEG published its report on climate-related disclosures. The TEG invited feedback on its report by 1 February 2019, and approximately 70 organisations and individuals submitted comments. The TEG has published a summary of these comments.

The Commission has taken into account the TEG report and the feedback received from stakeholders on that report and is now consulting stakeholders on the update of the non-binding guidelines before their planned adoption in June 2019. Stakeholders are invited to provide written comments by 20 March.

The consultation document takes account of the TEG report and of stakeholder feedback on that report. This document has been drafted by the services of the European Commission to facilitate a targeted consultation with interested stakeholders on the possible content of the new supplement to the non-binding guidelines. Comments on this document should be submitted by the end of Wednesday 20 March 2019, through this online facility created for this purpose. Comments submitted after that date, and comments not submitted through the online facility, will not necessarily be taken into consideration.

Nothing in this document commits the European Commission or prejudices any decision by the Commission regarding the update of the the non-binding guidelines on non-financial reporting.

More information:

- consultation document on the update of the non-binding guidelines on non-financial reporting
- on this consultation
- on the protection of personal data regime for this consultation

1. Information about you

*Are you replying as:

- [ ] a private individual
- [x] an organisation or a company

- ○ a public authority or an international organisation

* Name of your organisation:

Deloitte

Contact email address:

The information you provide here is for administrative purposes only and will not be published

chcunningham@deloitte.com

* Is your organisation included in the Transparency Register?
(If your organisation is not registered, we invite you to register here, although it is not compulsory to be registered to reply to this consultation. Why a transparency register?)

- ◉ Yes
- ○ No

* If so, please indicate your Register ID number:

53994278504-37

* Type of organisation:

- ○ Academic institution
- ○ Company, SME, micro-enterprise, sole trader
- ◉ Consultancy, law firm
- ○ Consumer organisation
- ○ Industry association
- ○ Media
- ○ Non-governmental organisation
- ○ Think tank
- ○ Trade union
- ○ Other

* Where are you based and/or where do you carry out your activity?

Other country

* Please specify your country:

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* Field of activity or sector (*if applicable*):

at least 1 choice(s)

- ☑ Accounting
- ☑ Auditing
- ☐ Banking
- ☐ Credit rating agencies

- [ ] Insurance
- [ ] Pension provision
- [ ] Investment management (e.g. hedge funds, private equity funds, venture capital funds, money market funds, securities)
- [ ] Market infrastructure operation (e.g. CCPs, CSDs, Stock exchanges)
- [ ] Social entrepreneurship
- [ ] Other
- [ ] Not applicable

Important notice on the publication of responses

*Contributions received are intended for publication on the Commission's website. Do you agree to your contribution being published?
(see specific privacy statement)

- (●) Yes, I agree to my response being published under the name I indicate (*name of your organisation /company/public authority or your name if your reply as an individual*)
- ( ) No, I do not want my response to be published

2. Your opinion

1. Do you have any comments on Chapter 2 "How to use these guidelines" of the report?

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We agree with including the two aspects of materiality, i.e. both a) the effect of non-financial matters on a company's development, performance and position (dependencies); and b) the external impact of the company's activities. As identified in the document, these are not distinct from each other. There is circularity as the impact that a company has externally may translate into opportunities/risks that are financially material. The terms 'financial materiality' and 'environmental and social materiality' which are used in Figure 1 and throughout the document are however confusing, as materiality is usually considered from the perspective of the user, not the subject matter, so all information within the management report, for example, should be reported using a consistent materiality. We consider that investors should indeed be a key stakeholder and form part of the primary audience.

We support that the Commission is not encouraging stand-alone climate reporting and consider that the disclosures should sit within the management report. Where matters are of importance to the understanding of a company's long-term viability, risks and opportunities, they need to be given appropriate prominence to stakeholders, and investors in particular.

We welcome the fact that the Commission encourages companies to implement the FSB's Task Force on Climate-related Financial Disclosures (TCFD) recommendations and that the EU guidelines incorporate them. This is important, including so as to support convergence and comparability for stakeholders. A cross-reference approach between the Non-Financial Reporting Directive (NFRD) and the TCFD could help to address the slight tension re. one materiality but two types of disclosure. The differing types of disclosure (1 vs. 2) may require some finessing, to ensure that the differences are understood and make sense across the jurisdictions (e.g. GHG disclosures are cited as type 2, but are mandatory in places). Ultimately, the goal is to encourage better disclosures - flexibility and proportionality may be key to achieving that.

We also welcome the Commission's approach in taking account of other existing standards and frameworks. We are seeing real momentum in regulatory developments around the world in respect of TCFD disclosures, for example in Australia and Japan recently, and it is good to see action at EU level. Furthermore, as countries progress with legislation to implement the Paris Agreement, companies will develop greater awareness of what is expected of them and be better able to design and measure against their scenario planning and analyses.

We are supportive of the Commission's approach and view that methodologies and best practice are evolving fast in this space and that organisations are encouraged to innovate and further improve beyond the content of the guidelines; they are not an end in of themselves.

2. Do you have any comments on Chapter 3.1 "Business Model" of the report?

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We are supportive of the comments around the need for longer-term perspectives and of the general approach.

3. Do you have any comments on Chapter 3.2 "Policies and Due Diligence Processes" of the report?

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4. Do you have any comments on Chapter 3.3 “Outcomes” of the report?

3000 character(s) maximum

5. Do you have any comments on Chapter 3.4 “Principal Risks and Their Management” of the report?

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6. Do you have any comments on Chapter 3.5 “KPIs” of the report?

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We would suggest the following refinements to Table 5:
- For scope 1 emissions, companies are required to estimate emissions where full data is not available, but for scope 2 they are only asked to state where scope 2 emissions could not be calculated or estimated. We would suggest changing “If necessary, companies should […state where…] GHG emissions could not be calculated or estimated” to “If GHG emissions could not be calculated or estimated, companies should state what options they considered for estimating the emissions, and why the options were rejected”.
- The measurement of Scope 3 emissions is in its early stages, and evolving rapidly. Without knowing the method used, it will be hard to compare reported results across companies. We suggest that companies should explain the method that they have used to measure scope 3 emissions.
- Regarding the GHG emissions target, absolute and intensity reporting are both required metrics. For example, rapidly growing companies will likely demonstrate an increasing absolute GHG emissions total, whereas declining large companies may demonstrate declining absolute emissions even if their emissions intensity is increasing. To align with the intention of the guidelines, investors need both metrics so they can judge the whole picture. We would suggest either requiring the reporting of absolute and intensity reporting or changing the wording from “in the case of an intensity target, companies should disclose the estimated change in absolute emissions for each scope (%) as a result of the intensity target” to “in the case of an intensity target, companies should also disclose the estimated change in absolute emissions for each scope across the company”.

We would suggest the following refinement to Table 6:
- Regarding “Total energy consumption and/or production (excluding feedstock) from renewable and non-renewable sources” – while agriculture causes significant emissions, the types (e.g. arable versus dairy) have materially different emission levels. We would suggest removing ‘(excluding feedstock)’ from the KPI wording.

We are supportive that the proposed supplementary guidelines recommend that companies consider indicators on related environmental issues, in addition to GHG emissions.

7. Do you have any comments on Annex I “Proposed disclosures for Banks and Insurance companies to the report?

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The requirements to disclose and describe potential risks and potential impacts with regard to insurance underwriting activity in sub-section 1, Business Model, appear to be duplicative, unless the guidelines expand upon the different reporting objectives.

The metric reference to net written premium related to energy efficiency and low carbon technology in sub-section 2, Policies and Due Diligence Processes, presents two issues:
- The premium is the measure of the risk price that the policyholder pays to transfer the risk to the insurance company. If energy efficiency and low carbon technology are to be encouraged, the insurer would charge those policyholders that have adopted them less, and may charge more to those who do not. This could be proven by loss ratios which combine the analysis of premium and claims incurred showing that those policyholders with energy efficient and low carbon technology have a lower loss ratio. The use of the premium alone is unlikely to be informative.
- The use of written premiums in financial reporting will cease with the adoption of IFRS 17. The new metrics emerging from the adoption of IFRS 17 should be considered in the evolution of these guidelines as the EU approaches the adoption of IFRS 17 e.g. the guidelines could replace net written premium with net insurance revenue.

Annex 1 appears to be comprehensive, albeit we have some suggestions:
- Listing the number of climate-related risks or % of products incorporating climate-related risks does not inform the debate, nor give comfort that they have been priced correctly to reflect the risk. We would suggest either requiring the publication of scenario analysis or, for more advanced companies, full risk distributions.
Regarding the requirement for “weighted average carbon intensity of each portfolio, where data are available or can be reasonably estimated” - to make the numbers meaningful to investors, banks and insurers should report exposure to at least all high-carbon intensive sectors – and would suggest: “weighted average carbon intensity of each portfolio, to include at least all exposure to high-carbon intensive sectors A, B, C, D, E, F, H (NACE classification) using reasonable estimates where necessary. Where estimates have been made, these should be stated.”
- Regarding the “Maximum Expected Loss from natural catastrophes caused by climate change (life / non-life / reinsurance)”, we consider that it might be more useful to ask for the increased risk above the base, as a result of future climate expectations.
- The Maximum Expected Loss is not a concept that is defined globally and the EU would need to make sure that a definition for consistent application within the EU is agreed after consultation with EIOPA.

Finally, we would reiterate the importance of considering climate-related risks in the context of - and in relation to - a broader set of risks, in order to avoid an isolated approach to the former.

8. Do you have any comments on Annex II “Mapping of NFRD requirements and TCFD recommended disclosures” to the report?

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As we mentioned in our letter re. the TEG Report, we caution that only incorporating parts of the TCFD might hinder global comparability, which should remain an important principle going forward.

We are supportive that, as the consultation document states, “if a company subject to the NFRD wants to meet the recommendations of the TCFD regarding the location of its climate-related disclosures, it should publish these disclosures in the management report”. This is consistent with the TCFD’s idea of including it in mainstream filings and highlights that these risks are important to - and managed by - directors and management.

9. Do you have any additional comments on the report as a whole?

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(i) Independent assurance/verification and investor needs:

We note the lack of reference to assurance/verification in the Report (other than indication of the third-party verification/assurance status that applies to companies' reported Scope 1, 2 and 3 GHG emissions).
We are however aware of both confusion among investors as to which of the information sources they use have been independently audited or assured, and increasing market appetite for assurance over non-financial information.
By way of note with regards to ongoing initiatives and developments:
- This is not an entirely recent shift: a Forbes Insight study from 2014 (conducted at the request of the Global Public Policy Committee (GPPC) of the six largest global audit networks, to explore the future role of audit) found that there were "two areas of management-supplied information where different levels of assurance are already being provided in some jurisdictions: corporate social responsibility and remuneration reports. Some stakeholders considered that "Sustainability reporting is nowhere near the level of accuracy that financial reporting is, and I think that's going to be the next horizon."
- A US academic study last year found that "sustainability assurance efforts more than pay for themselves in a majority of companies". There is also a noted increase in the US sustainability-linked loan market, with banks offering credit lines / revolver deals that link a company's interest rate to sustainability targets.
- The IAASB is currently consulting on Extended External Reporting. This is relevant to integrated and sustainability reporting as well as other reporting by entities about ESG matters.
- The Sustainability Accounting Standards Board (SASB) recently published its first set of industry-specific sustainability accounting standards covering financially material issues. SASB standards support robust, investor-grade reporting; can be used alongside other sustainability frameworks; are already being used by investors.

(ii) General:

Deloitte Global leaders are signatories in support of the TCFD's voluntary recommendations. We welcome the Commission's efforts to support the improvement of climate-related disclosures and are supportive of companies using internationally accepted standards and frameworks for non-financial reporting as this helps to establish and maintain the level playing field. We consider the existing guidelines and the update (supplement) to be a useful step towards improving climate-related reporting.
We consider that awareness-raising is also critical and that the Commission has an important role to play in this regard; to help companies understand the requirements that apply to them and how the various frameworks dovetail and integrate.

Useful links

More on the Transparency register (http://ec.europa.eu/transparencyregister/public/homePage.do?locale=en)

More on this consultation (https://ec.europa.eu/info/consultations/finance-2019-non-financial-reporting-guidelines_en)

Specific privacy statement (https://ec.europa.eu/info/files/2019-non-financial-reporting-guidelines-specific-privacy statement_en)

Consultation document (https://ec.europa.eu/info/files/2019-non-financial-reporting-guidelines-consultation-document_en)

Contact

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