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October 2019

# Europe pushes companies one step further towards sustainable investments

*The European Commission has underlined the importance for companies to publish sufficient, reliable and comparable sustainability-related information to effectively direct capital towards sustainable investments.*

*Although disclosure of climate-related information by reporting companies has improved, the Commission finds that there are still significant gaps and that further improvement in the quantity, quality and comparability of disclosures is required.*

## The Commission's guidelines on the disclosure of climate-related information

In March 2018, the Commission published the Action Plan on Financing Sustainable Growth. One of the three major aims was to reorient capital towards sustainable investment. As part of this objective, the Commission has published on 20 June 2019 new **guidelines on the disclosure of climate-related information by companies**. The Guidelines were adopted to meet the objectives set out in the 2015 Paris Agreement on Climate Change, the United Nations' Sustainable Development Goals and the Special Report of the Intergovernmental Panel on Climate Change and are line with the Recommendations of the **Task Force on Climate-related Financial Disclosures** (**TCFD**) of 2017.

The Guidelines supplement the following instruments:

1. Directive 2014/95/EU regarding disclosure of non-financial and diversity information by certain large undertakings and groups (the "**Non-Financial Reporting Directive**");
2. the applicable national regulation transposing the Non-Financial Reporting Directive;
3. the previous Guidelines on Non-Financial Reporting, published by the Commission in June 2017 which contain 6 key principles for good non-financial reporting, namely that disclosed information should be: (1) material; (2) fair, balanced and understandable; (3) comprehensive but concise; (4) strategic and forward-looking; (5) stakeholder-oriented; and (6) consistent and coherent ; and
4. the recommendations of the TCFD and, if necessary, the supplementary.

## Companies in scope

The Non-Financial Reporting Directive is applicable to large undertakings which are public-interest entities with a balance sheet total of at least euro 20 million or a net turnover of euro 40 million and over 500 employees in average (and on a consolidated basis in case of a group). A definition of a public-interest entity is provided by Article 2(13) of the Statutory Audit Directive 2006/43/EC. Public-interest entities are listed companies whose securities are admitted to trading on a regulated market of the EU, credit institutions, insurance undertakings and entities which are designated as public-interest entities by a Member State, for instance entities that are of significant public relevance because of the nature of their business, their size or the number of their employees.

## Materiality and type of risks

Climate-related information must be disclosed if it is necessary for an understanding of the external impacts of the company from an environmental and social perspective or if affecting the financial value of the company whereas TCFD has a financial materiality perspective only. The Commission has taken a broad interpretation of materiality compared to the 2017 Guidelines which incorporate the definition of the EU Accounting Directive 2013/34 ("*information where its omission or misstatement could reasonably be expected to influence decisions that users make on the basis of the financial statements*").

The result of such a broad definition is that most of the reporting companies will have to disclose climate-related information. Companies that conclude that climate is not a material issue are advised by the Guidelines to make a statement to that effect explaining how that conclusion has been reached.

Under the Non-Financial Reporting Directive, risks should be understood both as negative impacts on the climate (emission of greenhouse gases, use of fossil fuels, GHG emissions, etc.) and negative impacts on the company. A company might be impacted by transition risks (risks of litigation, reputational risks...) and by physical risks (weather-related events such as storms, fires, etc. or chronic physical risks such as temperature changes, rising sea level, etc.).

## Content of the information

The recommended disclosure relates to the reporting areas listed in the Non-Financial Reporting Directive: business model, policies and due diligence processes, policy outcomes, principal risks and their management, and key performance indicators.

**Disclosure on business model**

1. the impact of climate-related risks and opportunities on the company's business model, strategy and financial planning;
2. the ways in which the company's business model can impact the climate, both positively and negatively; and

3. the resilience of the company's business model and strategy, taking into consideration different climate-related scenarios over different time horizons.

The aim of this disclosure is to make sure that stakeholders understand the company's view of how climate change impacts its business model and strategy, and how its activities can affect the climate over the short, medium and long term.

**Disclosure on policies and due diligence processes**

1. any company policies related to climate, including any climate change mitigation or adaption policy;
2. any climate-related targets the company has set as part of its policies especially any GHG emissions targets, and how company targets relate to national and international targets and to the Paris Agreement in particular;
3. the board's oversight of climate-related risks and opportunities; and
4. the management's role in assessing and managing climate-related risks and opportunities and explain the rationale for the approach.

Information on the involvement of the board and management in relation to climate change informs stakeholders on the level of the company's awareness of climate-related issues. A company's policies and any associated targets that demonstrate its commitment to climate change mitigation and adaption may also be interesting for stakeholders. It will help stakeholders understanding the company's ability to manage its business to minimise climate-related risk, limit negative impacts on climate and maximise positive impacts throughout the value chain.

**Disclosure on policy outcomes**

1. the outcomes of the company's policy on climate change, including the performance of the company against the indicators used and targets set to manage climate-related risks and opportunities; and
2. the development of GHG emissions against the targets set and the related risks over time.

**Disclosure on principal risks and their management**

1. the company's processes for identifying and assessing climate-related risks over the short, medium and long term and disclose how the company defines short, medium, and long term;
2. the principal climate-related risks the company has identified over the short, medium, and long term throughout the value chain, and any assumptions that have been made when identifying these risks;
3. the processes for managing climate-related risks, and how the company is managing the particular climate-related risk that it has identified;
4. how processes for identifying, assessing, and managing climate-related risks are integrated into the company's overall risk management.

**Disclosure on key performance indicators**

Key performance indicators are measures that analyse the performance of a company and its activities. In particular, the company should disclose indicators and targets used by the company to assess climate-related risks and opportunities in line with their strategy and risk management processes. The indicators should either be integrated with other disclosures or in an additional table that presents all indicators.

## Banks and insurance companies

The Action Plan on Financing Sustainable Growth insists on the systemic importance of banks and insurance companies in the transition to a low-carbon and climate-resilient economy. The Non-Financial Reporting Directive imposes the same requirements on all companies under its scope, regardless of the sector in which they operate. Hence, it does not impose additional requirements on banks and insurance companies compared to other companies. Banks and insurance companies should look at the aforementioned disclosures from the particular perspective of their business activities, including lending, investing, insurance underwriting, and asset management activities. Therefore, banks and insurance companies should disclosure certain sector-specific information. For example, it could be useful to include information about an investment, lending and insurance underwriting portfolio that contributes to climate change mitigation and adaptation, and any relevant target in this respect. The sector-specific disclosures do not apply to other financial sector companies, such as asset management companies or pension funds since those companies do not fall within the scope of the Non-Financial Reporting Directive.

## Non-binding

The Guidelines are non-binding, which means that the companies falling in their scope may choose alternative approaches to the reporting of climate-related information provided they meet legal requirements. The content of climate-related disclosures may also vary between companies according to certain factors, such as the sector of activity and the geographical location.

## Concluding remarks

The new Guidelines on the Disclosure of Climate-Related Information aim to increase transparency and provide for standardisation in relation to a company's impact on the environment. Most of the reporting entities should consider that climate is material to them according to the Guidelines and adapt their reporting format to include climate-related information.

The standardisation of the format and content of climate-related disclosure is needed to enable comparisons between the reporting companies, from both a financial point of view and a social and environmental point of view. The new Guidelines set out precisely which climate-related information should be disclosed. However, the fact that Guidelines on the Disclosure of Climate-Related Information are non-binding may impede the level of standardisation that the Commission aims to reach.

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