Non-financial CSR reporting: too much or not enough?

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In September 2014, a directive amending Directive 2013/34/EU was adopted. Its main purpose is to ensure a higher level of corporate transparency by introducing the mandatory disclosure of certain non-financial information by large undertakings and groups in the EU regarding the impacts of their activities on society. Even though the reporting will be mandatory, the real impact might be viewed as questionable.

Is the new CSR mandatory notification requirement a step forward?

After many lengthy and complicated discussions, the final wording of the directive regarding the disclosure of non-financial information was approved. It can be considered another small step towards a sustainable global economy combining long-term profitability with social justice and environmental protection. From a corporate social responsibility point of view, this directive may be considered a step forward for several reasons. First of all, it should enable a broader group of people, including potential investors, creditors, employees, suppliers, customers, consumers and public representatives to better understand the impacts of a company´s activities on society. Secondly, the new directive may indirectly force large undertakings and groups to pay closer attention to the impacts of their activities on society, either because they will have to disclose them or because of the potential threat of bad publicity connected with such disclosure.

Who will be affected?

In general, the obligation to disclose non-financial information will affect large undertakings which are public-interest entities as defined by EU or national legislation and which have an average of more than 500 employees during the financial year. A similar obligation will apply to public-interest entities which are the parent undertakings of a large group which has an average of more than 500 employees during its financial year. Public-interest entities include banks, insurance companies, listed companies and health insurance companies. It is expected that approximately 6,000 companies in the EU could be affected by the new directive.

What must be reported?

The new directive defines the scope of non-financial information which large undertakings and groups will need to disclose. In particular, the large undertakings concerned will be required to disclose non-financial information relating to environmental, social and employee issues, human rights, and anticorruption and bribery issues, including (a) a brief description of the undertaking's business model, (b) a description of the policies pursued by the undertaking in relation to these issues, including due diligence processes implemented, (c) the outcome of these policies, (d) the principal risks related to these issues connected to the undertaking's operations including, where relevant and proportionate, its business relationships, products or services which are likely to cause adverse impacts in these areas, and how the undertakings manages these risks, (e) non-financial key performance indicators relevant to the particular business. Affected large groups will also be required to report such information.

The directive indicates which details should be disclosed. As regards environmental matters, statements should contain information regarding the current and foreseeable impact on the environment of the undertaking´s activity, information regarding the use of renewable and non-renewable energy and relating to greenhouse gas emissions, water or air pollution. As regards social and employee issues, the undertaking´s statements should include information regarding measures relating to gender equality, working conditions, social dialogue, health and safety at work and a number of other issues. Finally, with regards to human rights and anticorruption measures, the non-financial statement should include information on the prevention of human rights abuses and on measures in place to prevent corruption and bribery.

How will it be reported?

Large undertakings and groups must include the above-stated non-financial statement in management reports or consolidated management reports on an annual basis. The directive undertakes EU Member States to permit large undertakings and groups to rely on national, EU-based or international frameworks, and if they do so, to specify which frameworks they have relied upon.

However, where a large undertaking or group does not pursue policies in relation to one or more of these issues, the non-financial statement must provide a clear and reasoned explanation for not doing so.

It is explicitly stated in the directive that the European Commission will prepare non-binding guidelines and methodology for reporting non-financial information, including non-financial key performance indicators, general and sectoral, with a view to facilitating relevant, useful and comparable disclosure.

Will the directive work in practice?

Although the directive introduces mandatory non-financial reporting for certain companies, it is questionable whether the main purpose of the directive will be fully achieved. One potential problem is the introduction of the "complain or explain" approach which opens the door for undertakings and groups to avoid disclosing certain sensitive facts, provided they are able to explain why they were not disclosed. There are no sanctions or requirements with regard to not providing a proper explanation. Another potential problem is that the directive allows the use of multiple international or national standards or frameworks for reporting, which may lead to the disclosure of a differing amount of information by different undertakings and groups. This problem should be addressed to some extent by the issuance of reporting guidelines and methodology by the European Commission. Another potential problem is that the directive does not contain any controlling or sanction mechanisms in the event that undertakings and groups do not properly disclose the required non-financial information. Therefore, even though the non-financial reporting will be mandatory, undertakings and groups will still have plenty of room to avoid reporting.

Even though there are many undertakings and groups which pay attention to responsible corporate social conduct of their activities, there are also many which do not. Therefore, a change from a voluntary to a mandatory approach may be considered a step forward. On the other hand, given the specific wording and content of this directive, it is difficult to predict its real final impacts.