Setting Standards for Sustainability

WHAT THE EU DIRECTIVE FOR MANDATORY SUSTAINABILITY REPORTING MEANS FOR YOUR COMPANY

EU Directive on diversity and non-financial information

Directive 2014/95/EU sets out rules regarding mandatory disclosures to be included in consolidated non-financial statements by certain large undertakings and groups.

The Directive was adopted on 29 September 2014 and came into force on 22 October 2014.

Key objectives:

1. increase transparency and increase relevance, consistency and comparability of non-financial information
2. increase diversity in boards of companies
3. increase the company's accountability and performance

Legal elements of the Directive:

To amend Directive 2013/34/EU on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings and in particular to:

1. insert articles 19a and 29a
2. amend article 20

The proposal is based on article 50(1) of the Treaty which is the legal basis for adopting EU measures.

What must be covered?

Those subject to the Directive will be required to produce a non-financial statement containing information to the extent necessary for an understanding of the:

- development,
- performance,
- position, and
- impact of a reporting company's activity, relating to the following matters:
    - environmental
    - social
    - employee
    - respect for human rights
    - anti-corruption and bribery

The statement will include:

- a brief description of the organisation's business model;
- a description of the policies pursued in relation to the abovementioned matters, including due diligence processes implemented;
- the outcome of those policies;
- the principal non-financial risks listed above which are linked to the reporting company's operations including, where relevant and proportionate a reference to:
    - business relationships,
    - products or services which are likely to cause adverse impacts in those areas, and
    - how those risks are managed
- non-financial key performance indicators relevant to the particular business

Where companies do not pursue policies in relation to ONE or more of these matters, it must provide a "clear and reasoned" explanation for not doing so.

Companies can rely on UN Global Compact, UN Guiding Principles on Business and Human Rights, OECD guidelines for MEs, ISO26000, and disclose which framework they have relied on.

The implication, therefore, is that companies will have to set up a policy and procedures that meet the requirements of at least one of these frameworks.

Diversity requirements

Companies subject to the Directive are also required to provide a description of their diversity policy, including, for example, aspects concerning age, gender, geographical diversity and educational and professional background. This information must be included in the corporate governance statement. Where companies do not have a diversity policy they will be obliged to explain why this is the case.

What companies are covered by the obligations?

The obligations apply only to large undertakings:

1. with over 500 employees AND
2. who are public interest entities

The requirements outlined in article 19(a) also apply to public interest entities which are parent undertakings of a large group, “exceeding on its balance sheet dates, on a consolidated basis, the criterion of the average number of 500 employees during the financial year” (inserted as article 29(a)).

Some 6000 companies are expected to fall subject to the Directive’s requirements.

What is a Public Interest Entity?

A press release issued by the Council on 29 September 2014 defines public interest entities as “companies, such as:

- listed undertakings,
- banks,
- insurance companies, or
- undertakings which are of significant public relevance because of the nature of their business, their size or their corporate status.”[1]

What about third party verification?

It will be mandatory for auditors to check that the non-financial statement has been provided. It is up to Member States whether to “require that the information included in the non-financial statement or in the separate report be verified by an independent assurance services provider.”

When will the Directive become effective at national level?

Member States have until 6 December 2016 to transpose the Directive into national legislation. Organisations falling subject to the legislation will only start reporting and need to be in compliance as of their financial year 2017.

[1] http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/intm/144945.pdf

How does it differ from the current UK Standards on non- financial reporting?

The UK Companies Act 2006 (Strategic Report and Directors) Regulations 2013 requires listed, large and medium sized companies to report on their non-financial information. Only listed companies have to provide KPIs.

There is therefore a possibility that more large companies will be caught by the provisions of the EU proposal.

For more information on the regulatory requirements for UK Companies see our guide available for download at *www.clt-envirolaw.com*

Key issues to consider:

Questions to ask:

1. Does the organisation in question have more than 500 employees?
2. Does the organisation in question constitute a large undertaking that is a public-interest entity?
3. What policies does the organisation in question have in place to address environmental, social, human rights and bribery issues?
4. Does the organisation in question have a diversity policy?
5. Have you considered how to get the report audited?