

JULY 2021

FEEDBACK TO THE CORPORATE SUSTAINABILITY REPORTING ADOPTED ACT

INTRODUCTION

The Danish Institute for Human Rights (DIHR) welcomes the recognition by the European Commission of the vital role that non-financial reporting plays in encouraging responsible business conduct and efforts to reform the Non-Financial Reporting Directive (NFRD) to address the existing gap between the sustainability information reported by companies and the information needs of users. As we have noted previously in our [submission](#) to the public consultation on revision of the NFRD, there is a need for greater clarity of the obligations of reporting entities in relation to human rights, including with respect to application of the ‘double materiality’ principle and for the NFRD to align with other reforms, including those as part of the Sustainable Finance and Sustainable Corporate Governance Initiatives. The legislative proposal for a Corporate Sustainability Reporting Directive (CSRD) contains significant improvements on the NFRD, and the DIHR in particular welcomes the extension of the personal scope of the CSRD to apply to a larger pool of companies, the development of sustainability reporting standards and the intention to clarify the principle of double materiality. However, there remain a number of points requiring attention which are set out below.

CLARIFYING CONCEPTS

In the Explanatory Memorandum accompanying the CSRD, the Commission acknowledges the lack of precision in current reporting requirements, an issue which is sought to be addressed in the CSRD. To achieve this aim, the CSRD should aim to the greatest extent possible to clarify the concepts that companies are required to have regard to when reporting. However, in the view of the DIHR, there are a number of key concepts in the CSRD which would benefit from greater clarity.

For example, one of the key aspects of the CSRD is that it aims to clarify the principle of “double materiality” and remove any ambiguity about the fact that companies should report information

necessary to understand how sustainability matters affect them, and information necessary to understand the impact they have on people and the environment. The concept of “double materiality” as set out in Article 19a (2)(a)(iv) and 29a (2)(a)(iv) states that an undertaking shall report a brief description of the undertaking’s business model and strategy, including “how the undertaking’s business model and strategy take account of the interests of the undertaking’s stakeholders and of the impacts of the undertaking on sustainability matters”.

The intention stated in the Explanatory Memorandum is that this provision requires undertakings to report both on how various sustainability matters affect the undertaking, and on the impacts of the activities of the undertaking on people and the environment. However, this provision requires an undertaking to report on how the undertaking “takes into account” the interests of stakeholders, not how the undertaking actually or potentially impacts on people and planet. Accordingly, the double materiality requirement may not be immediately clear to reporting undertakings and they may omit required information. The provision would benefit from greater clarity, specifying that an undertaking should report on how it impacts on the enjoyment of the human rights of rightsholders and on the planet.

Further, Articles 19a(3) and 29a(3) of the CSRD state that an undertaking “shall include information about the group’s value chain, including its own operations, its products and services, its business relationships and its supply chain, where appropriate”. The concept of “appropriateness” is somewhat ambiguous which could lead to undertakings interpreting this requirement narrowly, and thereby omitting critical information in their sustainability reporting. Given that Commission has recognised the need for undertakings to report on their whole value chain, the DIHR suggests that the CSRD clarify this requirement.

In addition, the CSRD requires reporting on “intangibles” including information on intellectual, human and social and relationship capital. However, the CSRD should further clarify what “intangibles” is intended to capture, and how this aligns with the sustainability factors that undertakings are required to report on.

NEED FOR REGULATORY ALIGNMENT

The DIHR welcomes the Commission’s recognition of the need to ensure consistency with international instruments such as the UN Guiding Principles on Business and Human Rights

(UNGPs) and the OECD Due Diligence Guidance for Responsible Business Conduct. As we have noted in our previous submission on the revision of the NFRD, there is a need for regulatory alignment, in particular with the reforms currently under consideration under the Sustainable Finance and Sustainable Corporate Governance Initiatives. Regarding the UNGPs and OECD Guidance as critical touchstones for the development of each of these regulatory reforms is a practical means of facilitating regulatory alignment. However, there remain points of potential misalignment between the CSRD and other reforms, such as the development of mandatory human rights and environmental due diligence (mHREDD). For example, the personal scope of the CSRD applies to larger undertakings and listed SMEs, whereas the text adopted by the European Parliament by resolution of 10 March 2021 with recommendations to the Commission on corporate due diligence and corporate accountability extends the personal scope of the due diligence requirement to large undertakings, listed SMEs and, critically, high risk SMEs. The DIHR suggests that the CSRD should extend to high risk SMEs to ensure alignment and encourage SMEs in this category to reflect on their risks and impacts through the reporting process, reinforce the need to identify and address their risks through mHREDD and assist SMEs in this category to prepare for mHREDD regulation.

FRAMING OF HUMAN RIGHTS

Article 19a(2)(b) and 29a(2)(b) of the CSRD requires undertakings to make certain disclosures about social factors. Human rights are considered as a subset of “social” and are considered separately from equal opportunity and certain issues related to labour. However, this carries the risk of conceptual confusion which may drive reporting on ‘social impact contributions’ rather than on respect for human rights, including labour rights. Equal opportunities, working conditions and other areas that the EU wishes to highlight are ultimately included within human rights and should be considered as part of an overarching obligation to reporting on the undertaking’s human rights impacts. Accordingly, the DIHR suggests that human rights, including labour rights be the principal reporting category under the social factors section. The DIHR also suggests that the CSRD might usefully reflect on the suggestion from the EFRAG task force and the Platform on Sustainable Finance to organise social reporting by way of affected stakeholder groups, i.e. workers including across value chains, communities, as well as end-users and consumers. Social factors are ultimately about people and hence organising reporting by the groups of people most commonly affected by business activities can provide an intuitive and simple structure.

PARENT-SUBSIDIARY REPORTING

The proposal suggests that all subsidiary undertakings be exempted from the obligation to report non-financial information where such undertakings and their subsidiary undertakings are included in the consolidated management report of their parent undertaking, provided this includes the required non-financial information. As recalled by recital 21 it is important to ensure that sustainability information is easily accessible for users and to foster transparency. For large corporate groups with subsidiaries in numerous countries covering different business segments and activities there is a risk that aggregate reporting at the group level will not deliver meaningful disclosure. Impacts on sustainability factors, including human rights, play out at the local level and for one corporate group the risks and impacts are likely to differ significantly across country presences and hence across subsidiaries, and even more so for different types of business activities. As a result, the DIHR recommends that the proposal and subsequent standards clarify that group level reporting shall include information necessary to understand the undertaking's impacts on sustainability matters, including the impacts of subsidiaries. Articles 19a and 29a could usefully clarify the need to ensure that reported information give users information about impacts at aggregate and disaggregate levels.