

First Assessment of the Proposal for a directive, as regards corporate sustainability reporting. COM(2021) 189 final

Key messages

- CSRD will neither benefit SMEs nor their direct stakeholders
- Uncertainty on 'SME standard': Listed SME one or real SME (micro) standard?
- In absence of timely 'SME-standard' market will impose big industry one
- SMEs will have in practice no transposition period (contrary to Listed SMEs – 3 years)
- No guarantee that 'SME standard' will be accepted by non-SME clients
- Risk of gold-plating by Member States
- No 'one in/one' out compensation
- Estimated costs for SMEs: between 10 and 200 billion euro.
- Lack of budget for SME support.

Introduction

This paper contains feedback of the SMEUnited secretariat on the proposal on corporate sustainability reporting¹ adopted by the European Commission. A final position paper of SMEUnited will follow after the summer break.

Assessment of the proposal

The actual proposal of the Commission has serious shortcomings which will negatively impact SMEs. While SMEUnited has always stressed that both financial as non-financial reporting should be in the first place be a management tool for the entrepreneur, this objective is completely lacking in the proposal. Moreover as the objective of the SME standard apparently does not seem to report on their own performance but rather to fulfill the information needs of the large companies, the CSRD will neither benefit SMEs nor their own direct stakeholders, which have other interests.

Reasons for and objectives of the proposal

The Explanatory memorandum justifies the proposal for different reasons:

- “The revision of the NFRD will contribute to the objective of building an economy that works for people. It will strengthen the EU’s social market economy, helping to ensure that it is future-ready and that it delivers stability, jobs, growth and investment. These goals are especially important considering the socio-economic damage caused by the COVID-19 pandemic and the need for a sustainable, inclusive and fair recovery.” (p. 1-2)

Although these are all laudable objectives which SMEUnited fully supports, nowhere in the Explanatory Memorandum any argument, let alone any proof, is given of this possible contribution.

- “The current situation is also problematic for companies that have to report. The lack of precision in the current requirements, and the large number of private standards and frameworks in existence, make it difficult for companies to know exactly what information they should report. They often experience difficulties in getting the information they themselves need from suppliers, clients and investee companies. Many companies receive requests for sustainability information from stakeholders in addition

¹ Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending directive 2013/34/EU, Directive 2004/109/EC, Directive 2006/43/EC and Regulation (EU) No 537/2014, as regards corporate sustainability reporting; COM(2021) 189 final, 21.4.2021.

to the information they report to comply with current legal requirements. All of this generates unnecessary business costs."

SMEUnited welcomes the fact that the Commission recognises the described problem, however these problems are not solved for SMEs with the actual proposal, on the contrary. While the actual situation entails already now unnecessary business cost, the proposal does not explain how it solves these encountered problems. The Memorandum continues with: "The objective of this proposal is therefore to improve sustainability reporting at the least possible cost, in order to better harness the potential of the European single market to contribute to the transition towards a fully sustainable and inclusive economic and financial system in accordance with the European Green Deal and the UN Sustainable Development Goals."

"The proposal aims to reduce unnecessary costs of sustainability reporting for companies, and to enable them to meet the growing demand for sustainability information in an efficient manner."

A lot of emphasis is rightly put by the Commission on the (reduction of) costs of sustainability reporting. However there is nor an indication or proof on how to achieve this reduction neither how the proposal will improve the situation.² According to our assessment the costs for SMEs will dramatically increase. In addition, it has to be noted that the Commission proposal and the Impact Assessment does not contain any data on the actual costs for SMEs.

- "It will bring clarity and certainty on what sustainability information to report, and make it easier for preparers to get the information they need for reporting purposes from their own business partners (suppliers, clients and investee companies). It should also reduce the number of demands companies receive for sustainability information in addition to the information they publish in their annual reports."

Maybe the proposal will lead to a reduction of different demands for some large enterprises but for the majority of SMEs they will increase. The actual proposal will also not lead to more clarity for SMEs, as we will further explain, as they will depend on the different demands from their big suppliers. The different ecosystems SMEs are active in is not taken into account.

² We would like to refer to the similar comments of the Scrutiny board on the initial Impact Assessment : "The report does not present a consistent set of objectives, nor does it illustrate how policy action would deliver desired outcomes. The analysis is too often limited to presenting the delivery of corporate reporting, without verifying that it contributed to the objectives." p 104.

SMEUnited notes that in this part of the Explanatory Memorandum, “Reasons for and objectives of the proposal”, no reference at all is made to SMEs. Even more, according to the preparatory documents there is more attention for the so-called difficulties, burdens and costs that large companies, investors and some outsiders encounter, than the consequences of the proposal for self-employed and other SMEs.

SMEUnited regrets that in the proposal, when elaborating on the consistency with other Union policies, no reference is made to or no explanation is given on the consistency with the better regulation strategy. The Commission should come up urgently with concrete proposals to apply the “one in-one out” rule as this is the main promise of the Von der Leyen Commission to reduce administrative burdens.

Proposed SME Standard

SMEUnited welcomes that the Commission proposes³ separate, proportionate standards for SMEs which they can use voluntarily.

However, a careful reading of the proposal and the other preparatory documents, leads us to the conclusion that the legal text of article 19c is not that clear as it deals at the same time with a standard for SMEs and a standard for Listed SMEs.

The voluntary SME standard should be a self-standing standard adapted to the particularities and capacities of the majority of SMEs namely micro and small enterprises and not one that is adapted to Listed SMEs, which will be too complex for non-listed micro and small enterprises. Indeed the text of article 19 a sums up on what large undertakings as well as listed SMEs will have to report on. There is no distinction made on content between large enterprises and the listed SMEs. We do not see who a “simpler” standard that has to respect the requirements of art 19a2 can reduce substantial the burden for SMEs (be it listed or not). Moreover the Commission's power to adopt delegated acts is subject to strict limits: the delegated act cannot

³ Today's proposal revises and strengthens the existing rules introduced by the Non-Financial Reporting Directive (NFRD). It aims to create a set of rules that will – over time – bring sustainability reporting on a par with financial reporting. It will extend the EU's sustainability reporting requirements to all large companies and all listed companies. This means that nearly 50,000 companies in the EU will now need to follow detailed EU sustainability reporting standards, an increase from the 11,000 companies that are subject to the existing requirements. The Commission proposes the development of standards for large companies and separate, proportionate standards for SMEs, which non-listed SMEs can use voluntarily. Press Release 21 April 2021 see:

https://ec.europa.eu/commission/presscorner/detail/en/ip_21_1804

change the essential elements of the law⁴. So we wonder if the Commission can limit by delegated act the informations required by article 19a.

A possible solution would be the following amendment to Article 19c: Sustainability reporting standards for SMEs:

“The Commission shall adopt delegated acts in accordance with Article 49 to provide for sustainability reporting standards proportionate to the capacities and characteristics of small and medium-sized undertakings. ~~Those sustainability reporting standards shall specify which information referred to in Articles 19a and 29a small and medium-sized undertakings referred to in Article 2, point (1)(a) shall report. They shall take into account the criteria set out in Article 19b, paragraphs 2 and 3. They shall also, where relevant, specify the structure in which that information shall be reported.~~

The Commission shall adopt those delegated acts at the latest by 31 October 2023.”

A new article 19cbis could then deal if necessary with the requirements for Listed SMEs. It has to be noted that in the Explanatory Memorandum no justification is given why Listed SMEs (with the exception of micro's) are in the scope of the Directive.

An additional problem is that there is no guarantee at all that the “SME standard” will be accepted by the market. Listed SMEs will be certainly obliged, when they are in the supply chain of a large enterprise, to report according the large enterprise standard. For non listed SMEs there is the same risk due to the “trickle down” effect. The Commission is aware of this danger as it is even mentioned in the Impact Assessment, but fails to solve this major problem.

Moreover, as SMEs are often part of different supply chains and have different stakeholders and clients they will continue to be subject to different reporting demands with diverging information demands due to their unbalanced negotiating power. In addition, it has to be taken into account that SME information systems are ill-equipped to collate data. The SMEs themselves will also encounter problems to obtain information from the companies down in their supply chain due to a lack of bargaining power.

Therefore SMEUnited request that it should be **prohibited that (large) enterprises ask the SMEs in their supply chain to report according the large enterprise standard.**

The ambitious time schedule is also challenging and should be reconsidered in favor of practical implementability. The final version of the EU Sustainability Reporting Standards (SRS) needs to be published by 31.10.2022 and applied just two months later. New reporting companies in particular need sufficient time after the final standards have been adopted by the EC in order

⁴ https://ec.europa.eu/info/law/law-making-process/adopting-eu-law/implementing-and-delegated-acts_en

to carry out high-quality implementation. Two months is too little time for this. In the actual proposal non listed SMEs are treated less favourable than listed SMEs. Indeed while listed SMEs will have 3 years to adapt, non-listed SMEs in the supply chain will be obliged by the market to report from day one on.

We fully agree with the Commission when it states that “*Significant differences in requirements for sustainability reporting and assurance between Member States create additional costs and complexity for companies operating across borders. This is detrimental to the single market.*” However this proposal does not solve this problem as there is still the risk of distortions of competition within the EU, due to differences in the future implementation by the Member States.

Concerning the scope of the proposal SMEUnited supports the extension to EU subsidiaries of non-EU companies as well as all non-EU companies with transferable securities listed on a regulated EU market to ensure a "level playing field".

SMEUnited regrets the absence of a proper Impact assessment and SME test. On the basis of existing data, we estimate very conservatively the costs for SMEs between 10 billion and 200 billion euro.

The proposal states that it does not have any budgetary implications as “*Existing budgetary resources will be used for expenditure to fund the development of EU sustainability reporting standards.*” However we are not aware that the experts that are requested to do the preparatory work in the PTF are paid for the work that they do in the public interest.

The fact that there is no budget foreseen for SMEs and their organisations will certainly not help to foster sustainable reporting amongst SMEs. As SMEUnited had already requested in the past⁵, SMEs need support, accompanying measures, and adapted proportional tools in order to be able to comply non-financial reporting if they want or need to. Due to the fact that no support was given in the past, SMEs suffer from a relative lack of knowledge on how to report.

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⁵ - UEAPME Position Paper on Disclosure of Non-Financial Information by Companies, July 2012.