Federation of European Accountants
Fédération des Experts comptables Européens

FEE Position on ESG Disclosure

General

(1) FEE (The Federation of European Accountants) has participated in the EC workshops on ESG (Environmental, Social and Governance) disclosures as organised by DG Enterprise. FEE appreciates having the opportunity to submit its thoughts on the issue as a contribution to the final workshop scheduled for 25 February 2010 in which FEE will be represented by Paul Druckman, Chair of FEE's Sustainability Group and Nancy Kamp-Roelands, Vice-Chair of FEE's Sustainability Group. FEE commends the EC for taking the initiative to enhance the discussions on ESG disclosures.

(2) FEE supports the objective of the EC workshops being the promotion of better and more widespread disclosure of ESG information. Through its work in the sustainability area notably through the FEE Discussion Paper "Sustainability Information in Annual Reports-Building on the Implementation of the Modernisation Directive", published in December 2008; the FEE Policy Statement on Non-Financial Information of January 2009; the joint Roundtable of FEE and Eurosif hosted by the European Parliament on "Sustainable Disclosure" of 29 April 2009; and the related Joint FEE and Eurosif Call for Action on "Sustainability Disclosures in Financial Information can be improved" as published in July 2009, FEE has demonstrated its interest in proper ESG disclosures and contributed to the debate.

(3) FEE believes that there is a clear business case, as well as a wider social imperative, for organisations of all kinds and all sizes, to ensure that their information systems embrace performance indicators which reflect the urgent challenge of sustainability. This information, whenever material, should be embedded as a core part of strategy and decision-making. Changes in corporate culture are needed and will be facilitated by giving visibility and prominence to relevant measurements. Non-financial key performance indicators (KPIs) provide useful information about the way the company is managed and should be understood and connected to the company's performance by stakeholders. Responsible companies should provide an appropriate level of sustainability disclosures as a matter of course to ensure maximum transparency and accountability, regardless of whether such disclosures are mandatory or not.

Summarised Recommendations

(4) In summary FEE would:

- Support exploring the case for a combined approach to corporate reporting as one of the levers to embed sustainability in corporate strategy and management practices;
- Support a debate over the advantages and disadvantages of moving towards more mandatory regulatory approach to ESG reporting at the European level for large and listed companies;

- o Consider that there is no ESG reporting framework presently fully meeting the needs of capital markets actors (namely companies and investors);
- o Acknowledge the fact that the time has come to unite the efforts of the scattered European initiatives on ESG disclosure and reporting, taking into account a global context;
- o Urge the EC to contribute to the global debate and initiatives in this area such as those of GRI and ensure that any European requirements or guidance are compatible with these international developments.

Context

(5) Greater transparency can play a role in helping to restore trust in business. Better information is critical in facilitating well informed decision-making that takes account of risk and other factors. Increasingly investors are demanding more developed and sophisticated reporting on non-financial issues.

(6) As indicated above, information is only relevant if it is used in decision-making and, from an ESG perspective, changes decisions taken towards more sustainable outcomes. A key question is therefore who is the information being reported for and what decisions are taken as a result? Answering this question influences the form and type of disclosure and reporting that would be required:

- o Ensuring that reporting provides the information set to enable stakeholders to assess a company's contribution (positive and negative) towards the achievement of a sustainable economy and society;
- o Providing the information set that enables an assessment of a company's value now and in the future.

(7) There is an overlap between these two different perspectives – if the economy and society are not sustainable into the future, many companies will also not be sustainable and their value will be negatively impacted. This is of particular relevance to universal owners such as pension funds and insurance companies who are exposed to longer-term trends within the economy as a whole, rather than the performance of individual companies. In this sense, there is an incentive for these classes of investors to ensure that companies are taking the steps necessary to transition towards a sustainable economy and rewarding those companies that do so.

(8) The primary objective is to transition to a sustainable society, however, part of that transition has to be to enable economic actors to better price-in the risks and opportunities associated with sustainability trends through better and more comparable disclosure and reporting. The answer is not to add more data to the reporting regimes in existence, it has to be about refocusing on what matters to the target user group and how they use the information.

(9) Although developing a common set of indicators is not the whole answer, improving standardisation and therefore comparability for core metrics (at international, EU, national and sector levels) is a fundamental enabler for ESG factors to be taken into account in investor decision-making and therefore part of the step-change that needs to happen.

Discussion of recommendations

Combined approach to corporate reporting

(10) Non-financial information helps put historical performance into context and portrays the risks, opportunities and prospects for future growth. Non-financial information including sustainability information plays an important role in mitigating short-termism that until recently dominated financial analysis and valuation. Therefore, FEE would favour a combined approach to corporate reporting as one of the levers to embed sustainability in corporate strategy and management practices.

Support a debate over the advantages and disadvantages of moving towards more mandatory regulatory approach to ESG disclosure and reporting at the European level

(11) We acknowledge that the EC recognised the need for non-financial information to complement financial information already back in 2003 when it amended Article 46 of the Fourth Directive through the Modernisation Directive to require the inclusion in the annual report, to the extent necessary for an understanding of the company's development, performance or position, the analysis of the company's business, and where appropriate of non-financial KPIs relevant to the particular business, including social and environmental impacts.

(12) Because ESG disclosure and reporting is still in infancy, any further European regulatory approach should combine the requirements with further guidance. However, fixing a deadline for defining a generally accepted framework for the content of ESG disclosure and reporting is key. We feel that the existing requirements in Article 46 of the Fourth Directive and in Article 36 of the Seventh Directive best be completed by a recommendation which would:

- Design the reporting principles that should be followed to achieve an effective ESG reporting framework (relevance of ESG issues, comparability, reliability, etc.);
- Define the process to be followed to design the report content for ESG reporting;
- Decide on a deadline by which a first set of cross-sector and industry indicators should be agreed upon by the stakeholder community;
- Support the whole process by a strong communication campaign, supporting explanatory tools and 'good practices';
- Fit within global initiatives such as GRI but also the management commentary guidance of the IASB.

(13) Making further basic, specific disclosures mandatory should be investigated, for example as part of the Directives or as part of corporate governance codes. Disclosures may include disclosures on strategy, key business challenges and responses, governance and responsibilities, and risk management. Companies can then build on such disclosures. A "comply or explain" approach could be applied in that companies explain why they are not providing the basic disclosures. In a phased approach that could be further investigated; mandatory reporting should primarily apply to listed companies in a first step and large companies as a second step.

(14) The issue of assurance needs to be addressed. Assurance may help ensuring the quality and credibility of all management information, financial and nonfinancial, thus contributing to ensure that this information is useful to business decision-making in line with strategic objectives and good governance based on a sustainability framework. Further,

recommendations on good practice and good practice examples should entail information that is verifiable and therefore not include disclosures that are judgemental or subjective in nature. Accountants within organisations as well as those providing assurance services are in a key position to help organisations move to a connected reporting culture which encompasses non-financial as well as financial information.

ESG reporting framework

(15) In the field of financial and non-financial KPIs, there is no unanimously recognised framework as of today. It will need to be established through a convergence process of the different existing European initiatives taking into account the global developments.

(16) One of the key messages in the FEE Discussion Paper of 2008 is that corporate entities might be helped by further guidance as to how to report on ESG matters in the annual report, including the selection of the relevant KPIs for example in the form of good practice examples, since current practices differ widely. A general framework identifying topics that are relevant to include in the annual report and linking financial with non-financial KPIs may be helpful in increasing transparency on sustainability in the annual report. In addition, it could be considered for entities to use a "comply or explain" model and explain why environmental or sustainability issues are not relevant to them in that case, so that they need not to be addressed in the annual report.

(17) Entities should describe sustainability KPIs relevant to their business. The annual report is prepared from a financial perspective. However, addressing sustainability issues may introduce a different context and perception of relevance and materiality compared to the financial perspective by taking a larger time horizon and different boundaries and looking beyond the financial impact to the impacts on a wider group of stakeholders. An entity needs to indicate how it selected (and determined the significance of) its KPIs (selection criteria).

Need to unite efforts of the scattered European initiatives on ESG disclosure and reporting

(18) The challenge is building consensus between the different interested parties. Given the fact that different stakeholders have different interests and therefore different requirements in terms of disclosure content and format, we suggest the EC:

- To create a high level working Group composed of representatives of the major stakeholders within the categories implicitly defined by the EU ESG Disclosure Workshops;
- To investigate the use of Information Technology, such as WIKI or XBRL to facilitate different reports for different purposes/stakeholder groups using the same primary data;
- To fix a deadline by which the disclosure and reporting framework should be agreed upon between the stakeholders.

Compatibility with international developments

(19) Guidance on particular measures, especially for external reporting, is evolving and is increasingly well established – amongst the best known is that issued by GRI. Leading edge practice also depends on embedding company specific indicators into decision-making processes to support corporate strategy. It is important to have a globally understood language that enables stakeholders to assess how companies are performing and how risks or opportunities are addressed. The discussion on how to make such sustainability disclosures measurable needs to continue. The EC can make a contribution to this discussion.

FEE, 17 February 2010

About FEE

FEE (Fédération des Experts-comptables Européens – Federation of European Accountants) represents 43 professional institutes of accountants and auditors from 32 European countries, including all 27 EU Member States.

In representing the profession, FEE recognises the public interest. FEE has a combined membership of more than 500.000 professional accountants working in different capacities in public practice, small and larger firms, business, public sector and education, who all contribute to a more efficient, transparent, and sustainable European economy.