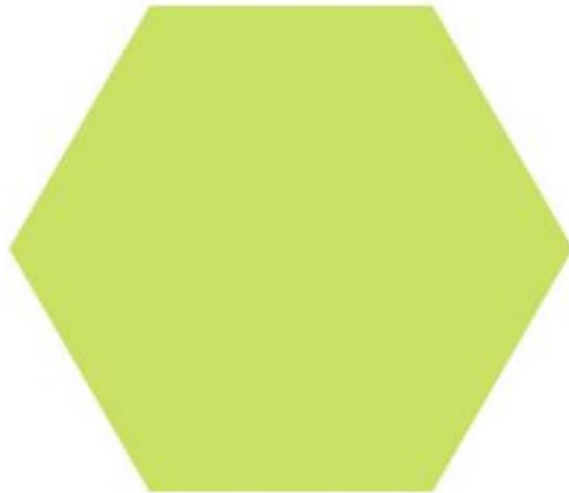


**EUROPEAN LAB**  
**CONSULTATION ON**  
**FUTURE PROJECTS**  
July 2019

**CONSULTATION ENDING**  
**30 SEPTEMBER 2019**





## Foreword



With the first project of the European Lab on good practices on climate-related reporting well on its way and aiming for publication of the results by the end of the year, it is now time to consider the future activities of the European Lab in the area of corporate reporting and start planning for the next projects.

We are confident that the European Lab can provide a valuable and important contribution to the European Commission agenda for sustainable and inclusive growth in Europe, and the wider global debate on corporate reporting. We need to make sure that we focus on the right issues.

With the rapid changes in the world around us and the resulting challenges to economies and businesses, the extended scope of corporate reporting requires new and innovative solutions. We want the European Lab to play a pivotal role in this respect by providing practical insights on good reporting practices

Your input on the European Lab future projects will help to ensure that these future projects stimulate innovation in the field of corporate reporting in Europe by identifying and sharing good reporting practices. This is an objective that we are sure is shared by all our stakeholders – reporting companies, users and all other parties with an interest in better corporate reporting and sustainability.



### **Jean-Paul Gauzès**

*European Lab Steering Group Chairman and  
EFRAG Board President*

### **Alain Deckers**

*European Commission DG FISMA Head  
of the Corporate Reporting, Audit and  
Credit Rating Agencies Unit, and  
European Lab Steering Group Vice-  
Chairman*

## Objective of the European Lab future projects agenda consultation

1. The European Corporate Reporting Lab @EFRAG (European Lab) was established by EFRAG, following a call by the European Commission in its March 2018 Action Plan on *Financing Sustainable Growth* (EC Action Plan). The European Lab serves the European public interest and its objective is to stimulate innovation in the field of corporate reporting in Europe by identifying and sharing good reporting practices through:
  - (a) Facilitating dialogue between reporting companies, users and other relevant stakeholders and organisations; and
  - (b) Documenting the content and outcomes of this dialogue in reports and other means, for making them available in the public domain.
2. Corporate reporting issues are part of a wider debate of communication to the markets and other stakeholders of sustainability and corporate social responsibility information, and there is an interplay with various external factors, initiatives and discussions. The European Lab supports and contributes to the implementation of the EC Action Plan in areas within its competence.
3. More information on the governance and operation of the European Lab can be found on the [EFRAG website](#).
4. The first project of the European Lab, currently in progress, is on climate-related reporting. The project is assessing the current state of play for climate-related reporting by European companies, and the current and potential use of climate-related information by investors and other users. The primary focus is on the *Task Force on Climate-related Financial Disclosures (TCFD) recommendations* with consideration of other reporting frameworks as appropriate, while also taking account of the European Commission's non-binding *Guidelines on non-financial reporting* issued in July 2017 and their supplement *Guidelines on reporting climate-related information* issued in June 2019. Focus areas are climate-related disclosures and scenario analysis.
5. The decision to add a project to the European Lab agenda is made by the European Lab Steering Group, taking into consideration input from stakeholders in a public consultation.
6. This public consultation seeks views on European Lab future project topics and their prioritisation. We also seek your input on any possible alternative project that in your view would be more important and urgent for the European Lab to undertake than the three projects proposed in the public consultation. We welcome views on any of the points addressed by 30 September 2019.

## Input required from stakeholders

7. In paragraphs 12 to 36 below, the European Lab outlines three potential topics identified by the European Lab Steering Group to be considered as future projects of the European Lab.
8. The questions to stakeholders are found in paragraphs 37 to 40.
9. Replies are requested by **30 September 2019**:
  - (a) electronically through a web survey available [here](#); or
  - (b) sending an email to [europeanlab@efrag.org](mailto:europeanlab@efrag.org).
10. All replies received will be placed on public record, unless confidentiality is requested.
11. For any queries contact [europeanlab@efrag.org](mailto:europeanlab@efrag.org).

## Proposed topics for future projects of the European Lab

12. The European Lab Steering Group has identified three possible future project topics:
  - (a) Reporting of social matters and human rights.
  - (b) Reporting of non-financial risks and opportunities, and linkage to the business model.
  - (c) Reporting on the materiality assessment process and outcomes for Environment, Social and Governance (ESG) matters
13. This document presents a brief description for each of the proposed topics.

### Project 1 – Reporting of social matters and human rights

14. The Directive 2014/95/EU on non-financial information reporting (NFRD) requires large European companies to report, amongst other things, on social matters and human rights. This area also forms an integral part of the United Nations Sustainable Development Goals (SDGs) which are increasingly integrated into companies' business strategies. Social and human rights play an important role in strategies relevant to SDGs, and regulations on corporate responsibility towards respecting social engagement and human rights is increasingly being enacted. However, with attention concentrating mainly on the environment including climate change and due to difficulties in quantification of social matters, the reporting of relevant information and its linkage to business models and long-term value creation is generally limited or even missing from corporate reports. The need for improved reporting on social matters and human rights was highlighted in a 2018 Alliance for Corporate Transparency report and through the European Securities Market Authority (ESMA) 2018 report on enforcement priorities.
15. At the same time, there is no commonly accepted definition or consensus on what topics fall under "social matters". For example, a 2018 World Bank report on incorporating ESG factors into investments highlights that different organisations have different topics under their definition of "social matters". Hence, a project that focuses on "social matters" may be too broad if it was to address all potential topics and there is need to focus on specific topics. For this reason, a European Lab project on this topic would aim at identifying good reporting practices on the use of relevant metrics and other disclosure of social matters and human rights in one of the specific focus areas to be selected as outlined below.
16. *Need for a focus on sectors that have higher impact on human rights:* Human rights is a cross-cutting issue across the specific focus areas considered below. Hence, as part of the analysis of good reporting practices, it will likely be necessary to focus on the sectors that have higher impact on human rights.

#### *Focus area 1 – Reporting on social matters and human rights in the supply chain*

17. Supply chains can be a significant driver for companies success, through value creation and innovation.
18. The complexity added to supply chains by the involvement of multiple countries, tiers, structures and interdependencies has a critical impact on business operations, reputations and investment performance.
19. As supply chains often fall outside of companies core operations and control, they may expose them to significant risks typically driven by ESG factors, such as human rights abuses, corruption, social issues within the work force and labour standards, fair operating and trade practices by and with suppliers, natural resources depletion, community engagement and development.

20. Public awareness of supply chain issues continues to grow, and companies are increasingly under scrutiny in respect of their action on major human right issues among their suppliers.
21. This focus area would primarily be on reporting human rights associated with supply chains. However other 'social' matters, as enumerated in paragraph 19 above, could also be considered.
22. Furthermore, companies are increasingly expected to understand and prevent or mitigate human rights risks that may occur in their supply chain as well as to manage their exposure to such risks. In support of meeting their responsibility to respect human rights and their reputation, and to ensure the resilience and sustainability of their business model, companies are called to include in their corporate reports information on indirect (third party suppliers) or internal (supply chain management) related risks and opportunities), together with their associated due diligence processes, and provide evidence on the effective management of these risks.

*Focus area 2 –Reporting on human capital management*

23. Human capital has been defined by a number of organisations as the knowledge, skills and attributes of the workforce and others across the value chain. Human capital management forms a significant part of business processes for enhancing business performance and value creation. Companies are therefore expected to include information on human capital management in their corporate reports in relation to the resilience and sustainability of their business model. Hence, this focus area would primarily be on good practices in the reporting of human capital management.
24. In addition to reporting on human capital management, and to the extent that the scope does not become too broad, this focus area may be extended to the way that companies report on how they manage issues related to social capital. Social capital often being defined as the value added to society by companies' products, services and activities, as well as the relationships within and between communities, groups of stakeholders and other networks. Depending on particular business models, different factors impact on social capital including but not limited to: community relations; customer data security; transparent information, fair advice and pricing; and measures to ensure product safety. Hence, this focus area could include examples of reporting on factors that impact on social capital.

*Focus area 3 – Reporting on human capital and social capital impacts of climate adaptation and mitigation policies*

25. Climate change impacts are systematic in nature. As such, climate adaptation and mitigation measures are prevalent across a variety of sectors. These measures can not only have internal impacts within companies but can also have broader impacts at a societal level. As highlighted in the recently published EC *Guidelines on reporting climate-related information*, many companies are dependent on human capital, such as the skills and motivation of employees for the purposes of climate adaptation and mitigation. For example, employees can be critical to the development of innovative low-carbon products and services or jobs can be eliminated due to new processes and technologies. In this respect, human capital management can be interrelated with companies' climate adaptation and mitigation measures.
26. Furthermore, as noted in the EC guidelines, climate mitigation and adaptation can also impact on companies' social capital including on the level of trust companies' enjoy amongst external stakeholders. Under the *UN Guiding Principles on Business and Human Rights*, companies are expected to address the human rights implications of climate change.



27. One example of how climate adaptation and mitigation policies are considered in relation to social matters and human rights is the extent to which Metals & Mining and Oil & Gas exploration and production companies with climate risk exposure consider the security and land rights of indigenous peoples in their operations and measures taken to mitigate climate risk. For example, whether an Oil & Gas company that is changing its energy mix towards renewable sources, does so while managing adverse social impacts that would arise if the human rights of affected parties were ignored. There are other examples of impacts on social capital that occur depending on particular business models, location of companies' operations and climate risk mitigation strategies. Hence, this focus area would be on good practices around how companies integrate information about impacts on human capital and social capital in the reporting of their climate-related adaptation and mitigation strategies.

### **Project 2 – Reporting of non-financial risks and opportunities, and linkage to the business model**

28. Stakeholders need to better understand the business model of companies and the impact of non-financial considerations on their strategy and activities. The NFRD requires reporting on the business model, policies pursued by the group, outcomes of those policies, principal risks linked to the group's operations and non-financial Key Performance Indicators (KPIs). Apart from the NFRD requirements, reporting on the nature, position, performance and development of the business, together with the principal risks are included in Directive 2013/34/EU (the Accounting Directive) and through the International Accounting Standards Board (IASB) Management Commentary Practice Statement which provides voluntary guidance for IFRS reporting companies. Notwithstanding the multiple sources of guidance, a number of reviews of both EU and global companies' reporting practices have shown that there is scope for improvement in the linkage between the business model description and non-financial information including the related risks and opportunities.
29. For instance, a 2018 Climate Disclosure Standards Board (CDSB) report based on a review of 80 EU companies found that frequent failures in linking non-financial information such as climate risk with the business model description. Another study<sup>1</sup> that reviewed the disclosures of 15 Oil & Gas companies found that many of these companies disclosed greenhouse gas emissions in terms of performance and future goals, but explanations of discussions about how targets related to the business model and strategy were rare. Similarly, a 2018 Alliance for Corporate Transparency report assessed the extent to which companies disclose their business strategies and products or services for pursuing opportunities connected with a sustainable economy. Based on the analysis of reporting by a sample of 105 companies, the report highlights that there is room for improvement enhancement in the information provided on strategies relating to social and environmental areas including information on related KPIs, targets, revenue and investments.
30. A robust description of the business model that conveys the sources of competitive advantage, risks, opportunities and the sustainability of the business model over time is a core input of users' assessment of companies' competitive position in comparison to peers. Furthermore, in the absence of a robust business model description, users can have difficulty in identifying the link between the business model and changes over time in companies' reported risk tolerance and principal risks including non-financial risks.

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<sup>1</sup> Eccles, R.G. and Krzus, M.P. 2019, *Implementing the Task Force on Climate-related Financial Disclosures Recommendations: An Assessment of Corporate Readiness*. Schmalenbach Business Review, Edition 71, Pages 287-293.

31. This project would focus on examples of companies' business model reporting and linkage to non-financial risks and related opportunities. Whereas non-financial risks that arise from the external operating environment could negatively affect the prospects, performance and risk exposure of companies, there can also be opportunities for enhancing profitability for companies that adapt their business models in response to the non-financial risks. For example, a company could improve profitability through the launch of new, high-demand products certified to environmental and/or social standards or through energy-efficiency driven cost savings or through steps that impact on companies' sustainability reputation and social license to operate. The project could consider the reporting of economic impacts of risks and opportunities and the positive or negative social or environmental impacts of companies' related strategies.

**Project 3 – Reporting on the materiality assessment process and outcomes for Environment, Social and Governance (ESG) matters**

32. Materiality is one of the fundamental principles of the non-financial reporting introduced by the NFRD. However, despite its relationship to the principle of materiality for financial reporting, it is widely considered to be more challenging because of (i) the higher level of subjectivity stemming from the typically less prescriptive nature of non-financial reporting requirements, (ii) the longer time-horizon, and (iii) the consideration of the information needs of, and the effects on, a wider range of stakeholders.
33. Complexity is also increased by the existence of multiple definitions and frameworks, and many organisations find it challenging to navigate the range of materiality definitions across reporting regulations, standards and frameworks. The project would provide insights for both users and preparers by identifying good practices in relation to reporting on companies' materiality assessment processes and outcomes in relation to Environmental, Social and Governance information. The reporting of the materiality assessment can be an input to users' assessment of the relevance of any disclosed ESG KPIs and targets, and to their understanding of which of the ESG factors have the greatest impact on a company's risks and opportunities.
34. The project would consider the dual perspective of materiality in relation to ESG information. That is, the project would consider the material impacts a company has on the environment and society, as well as material impacts the environment and society have on the organisation, including, but not limited to, the following:
  - (a) Reporting about the materiality assessment process including the links with the organisation's strategy, governance, policies and risk management;
  - (b) Reporting about the level of engagement with providers of financial capital and other stakeholders; and
  - (c) Reporting about the outcomes of the materiality assessment process.
35. In carrying out this project, the European Lab would consider existing frameworks and definitions of materiality but would keep a 'neutral' approach by not giving precedence or prominence to any specific framework.
36. It should also be noted that, as in all the projects of the European Lab, because the frameworks regarding materiality for non-financial information are either recently applied by companies or are evolving, what is considered to be good reporting practices today is likely to evolve once companies get to a more mature stage of implementation.

## Questions to stakeholders

### General information about the respondent

37. Please provide the following details:

(a) Your name:

Elisa Bevilacqua

(b) Your contact e-mail address:

Elisa.bevilacqua@eacb.coop

(c) Your job title/role:

Head of Department, Sustainable Finance

(d) Name of the organisation on behalf of which you are responding:

EACB

(e) Country of operation:

Belgium

(f) Which type of respondent are you representing?

- Reporting company  User  Accountancy profession  Academic  
 Financial institution  Civil society  Other (please specify)

European Trade Association

(g) Short description of activity/industry:

The European Association of Co-operative Banks (EACB) is the voice of Co-operative Banks in Europe. With 67,000 outlets and 2,900 banks, co-operative play a major role in the financial and economic system. Co-operative banks have a long tradition in serving 209 million customers, mainly consumers, retailers and SMEs. They have also developed a strong foothold in the corporate market providing services to large international groups. Quantitatively co-operative banks in Europe represent about 81 million members, 720,000 employees with a total average market share of about 20%.

(h) If you are responding on behalf of a reporting company, are you directly involved in the preparation of corporate reports?

- Yes  No  **Not applicable**



**Information required on proposed projects**

38. Please rank the proposed project topics outlined in paragraphs 12 to 36 above by order of priority, and explain your selection with details of the distinct added value you would expect of a potential European Lab project on each topic:

	<b>Priority</b>	<b>Reasoning for your selection and ranking</b>
<b>Project 1.1</b> – Reporting on human rights and other social matters in the supply chain	Highest Medium <b>X Lower</b>	We consider these projects as lower priority because many of the elements in project 1.1, 1.2 and to some extent 1.3. would be covered projects 2 and 3.
<b>Project 1.2</b> – Reporting on human capital management	Highest Medium <b>X Lower</b>	We consider these projects as lower priority because many of the elements in project 1.1, 1.2 and to some extent 1.3. would be covered in projects 2 and 3.
<b>Project 1.3</b> – Reporting on human capital and social capital impacts of climate adaptation and mitigation	Highest <b>X Medium</b> Lower	
<b>Project 2</b> – Reporting of non-financial risks and opportunities, and linkage to the business model	<b>X Highest</b> Medium Lower	This project is considered of highest importance by EACB Members. It would provide tools for the implementation of the new Non-Binding Guidelines of the NFRD. The proportionality principle should be taken into account.
<b>Project 3</b> – Reporting on the materiality assessment process and outcomes for Environment, Social and Governance (ESG) matters	Highest <b>X Medium</b> Lower	Being addressed to the companies of the real economy, this project could provide EACB Member banks an indication on topics that matter especially from a risk assessment point of view.

39. Are there other topics that you advise the European Lab to add to its agenda? If so, please provide a description of the topic and the priority you would assign to it:

The EACB Members encourage the Lab to focus on NFRD implementation and materiality of ESG matters.

*2019 European Lab future projects agenda consultation*

40. Please provide any details of interaction you may be aware of with the work of other initiatives, in respect of the topic you rank as highest priority:

41. Thank you for responding to our consultation! Your views are very important to us.



EFRAG receives financial support of the European Union - DG Financial Stability, Financial Services and Capital Markets Union. The content of this document is the sole responsibility of EFRAG and can under no circumstances be regarded as reflecting the position of the European Union.



**EFRAG**

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