EUROPEAN COMMISSION

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Dear President,

The Commission would like to thank the Bundesrat for its Opinion on the proposal for a Corporate Sustainability Reporting Directive {COM (2021) 189 final} (the CSRD proposal).

This proposal forms part of a broader package of ambitious measures designed to enable finance to play its full part in the green transition. The European Green Deal aims to make the EU climate-neutral by 2050, by supporting green jobs, green growth and green investment. In its Communication on the European Green Deal, the Commission committed to reviewing the provisions introduced in 2014 by the Non-Financial Reporting Directive, as part of its strategy to strengthen the foundations for sustainable investment. In this respect, the proposal for a Corporate Sustainability Reporting Directive is part of efforts to scale up sustainable finance by improving transparency.

The CSRD proposal will revise and strengthen the sustainability reporting rules for certain categories of companies according to the information needs of market participants and other stakeholders. We need a consistent flow of reliable, comparable and relevant information on sustainability risks, opportunities and impacts from companies, to asset managers and analysts, to investors. The current situation of multiple standards is costly and confusing. Companies face uncertainty and complexity when deciding what sustainability information to report. The development of EU sustainability reporting standards, which is the centrepiece of the CSRD proposal, should provide a rational and cost-effective solution for reporting companies.

The Commission welcomes the Bundesrat's broad support for the aims of the proposal. It is pleased to have this opportunity to provide a number of clarifications regarding its proposal and trusts that these will allay the Bundesrat's concerns.

The points made above are based on the initial proposal presented by the Commission, which is currently in the legislative process involving both the European Parliament and the Council. The Commission remains hopeful that an agreement on the final text will be reached by the middle of 2022.

Mr Bodo RAMELOW
President of the Bundesrat
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The Bundesrat's Opinion has been made available to the Commission's representatives involved in the ongoing negotiations between the co-legislators and will inform these discussions.

In response to the more technical comments in the Opinion, the Commission would like to refer to the attached annex.

The Commission hopes that the clarifications provided in this reply address the issues raised by the Bundesrat and looks forward to continuing the political dialogue with the Bundesrat in the future.

Yours faithfully,

Maroš Šefčovič
Vice-President

Mairead McGuinness
Member of the Commission

<u>Annex</u>

The Commission has carefully considered the issues raised by the Bundesrat in its Opinion and would like to offer the following observations, grouped by topic.

Sustainability reporting standards

As far as the global coherence of sustainability reporting standards is concerned, the Commission strongly welcomes efforts to create more alignment at global level. The Commission sees the International Financial Reporting Standards (IFRS) Foundation initiative as a baseline. EU standards should build on what exists, while also meeting Europe's specific needs. Cooperation between global and regional standard-setters is key to ensuing coherence and interoperability between frameworks. The European Financial Reporting Advisory Group (EFRAG) Project Task Force has signed Statements of Cooperation with the Global Reporting Initiative, which has developed the standards that are currently most widely used by European companies, and with Shift, one of the leading authorities on the United Nations Guiding Principles on Business and Human Rights. In particular, EFRAG is also cooperating as closely as possible with the Technical Readiness Working Group established by the IFRS Foundation to prepare work on the/a? global climate standard prior to the operational establishment of the International Sustainability Standards Board (ISSB). There is already a lot of common ground. For example, the Commission has integrated in the CSRD proposal all the key concepts of the recommendations from the Task Force on Climate-related Financial Disclosures, which will be a key element of future ISSB standards.

The Commission aims to give companies the tools to better integrate sustainability in their activities and to report on what they are doing. The Commission shares the view that the focus should be on simple, easy to implement and effective measures. Mandatory EU sustainability reporting standards should provide a rational solution for reporting companies. Over time, EU standards should help to limit further cost increases for companies resulting from expectations to use multiple overlapping and inconsistent standards and frameworks, and having to respond to numerous additional information demands from stakeholders. EU standards should provide clarity and certainty for reporting companies. They should be proportionate, and should not impose unnecessary administrative burdens on companies. At the same time, standards must be consistent with the rest of the EU's agreed sustainable finance framework, in particular the Taxonomy Regulation and the Sustainable Finance Disclosure Regulation. If EU standards were not consistent with these and other pieces of EU legislation, reporting companies would face unnecessary administrative burden and additional information demands from stakeholders, in particular from investors and financial institutions. According to the CSRD proposal, EFRAG should carry out cost-benefit analyses on the draft standards that it produces to ensure that standards are practical and feasible for preparers. The Commission fully supports the involvement of preparers in the standard-setting process, alongside other stakeholders.

Scope and SMEs

On the scope, we estimate that this proposal would extend mandatory reporting requirements from 11.000 to some 50.000 companies, essentially all large companies established in the EU and all listed companies in EU regulated markets. The proposed scope covers those companies from whom investors and others need sustainability information most, and is therefore proportionate.

The proposal foresees a simpler reporting regime for listed SMEs, of which there are currently about 1.000 in the EU. Listed micro-enterprises are excluded from the scopeentirely. Other listed SMEs would have the option of reporting according to simpler, proportionate reporting standards, instead of using the full standards. In addition, they would only have to start reporting three years after large companies. This strikesa balance between the risk of administrative burden for listed SMEs and protecting access to capital for SMEs. If listed SMEs did not report the sustainability information needed by investors and other financial market participants, they could run the risk of being excluded from investment portfolios.

The CSRD proposal does not impose any new requirements on the vast majority of SMEs. They may however choose to use the proportionate SME reporting standards on a voluntary basis. These standards should help non-listed SMEs to respond to banks and large company clients that increasingly demand sustainability information. The SME standards should set a reference for companies that are under the scope of the Directive regarding the level of sustainability information that they could reasonably request from SME suppliers and clients in their value chains.

Demand for sustainability information from all companies, including SMEs, is increasing rapidly. This is an inevitable consequence of the transition to a sustainable economy, and the demand would increase even if the EU were not to introduce stronger sustainability reporting requirements on large companies and listed companies as foreseen in the CSRD proposal. The proportionate SME standards proposed by the Commission are the best way to help non-listed SMEs to cope with this demand, so that they can play a full part in the transition to a sustainable economy and benefit from the business opportunities that the transition creates.

Delegated Acts, and the balance between the Directive and the proposed standards

The empowerment of the Commission to adopt sustainability reporting standards in EU law needs to balance two different requirements. On the one hand, the empowerment must lay out the essential requirements of the future sustainability reporting framework, and be sufficiently clear and circumscribed. It should provide the necessary guarantees that the adopted standards would meet the objectives defined in the Directive by the co-legislators, and not extend beyond those objectives. One the other hand, there must be a sufficient degree of flexibility in the way that the CSRD proposal itself frames the content of the standards. This flexibility is necessary because, amongst other things, the needs of users will evolve, as well as the end content of related EU legislation and the content of proposed global standards. There is a recognised need to ensure as much consistency *and interoperability as possible between European reporting standards and global standards. The more detail is introduced in the Directive itself, the harder it becomes to ensure consistency with global initiatives when adopting sustainability reporting standards. Overall, standards need to be able to remain up to date and incorporate relevant elements to the required disclosures, without going through the heavier procedure of revising the Accounting Directive on every occasion. A similar approach applies and is accepted in the field of financial reporting. The CSRD proposal presents a balanced approach between providing for the needed flexibility in the adoption of standards and sufficiently framing the empowerment and the exercise of the delegation of powers by the Commission.*

Digitalisation and the European Single Electronic Format* (*ESEF)

The CSRD proposal anticipates the increasing digitalisation of sustainability information. The digitalisation of reporting is an inevitable trend, and it is expected to bring significant advantages and cost savings to reporting companies and to users of reported information over the medium and long term. These advantages, and the advantages of the proposed European Single Access Point, will be realised if companies report information in a single electronic format and "tag" the information to make it machine-readable.

Timetable

The Commission acknowledges that the timetable in the CSRD proposal is ambitious. This timetable is consistent with the urgent need to address the climate and broader sustainability objectives, such as the Paris Agreement, the EU Green Deal and the EU's climate strategy. It is also necessary to ensure as soon as possible the coherence of the EU legislative framework. In particular, there is an urgent need to ensure that financial market participants can access the information they need from other companies to meet their own reporting requirements under the Sustainable Finance Disclosure Regulation. Any delay compared to the timetable proposed in the CSRD would therefore have knock-on effects for the rest of the EU's sustainable finance agenda, including the EU's Sustainable Finance Disclosure Regulation and Taxonomy Regulation.

Good cooperation with existing standard-setting initiatives such as the GRI and the IFRS Foundation is enabling EFRAG to move fast in developing draft standards. In addition, companies will have a good insight into the probable content of standards once EFRAG launches its public consultation in the first months of 2022. This means companies can begin to prepare well before the Commission formally adopts any reporting standards.