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Disclosure of Environmental Information in Companies' Annual Reports under EU Law Provisions

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1. INTRODUCTION

Companies and other forms of organisations are increasingly aware of the need for socially responsible behaviour. Social responsibility should lead to sustainable development. Effects upon the society and the environment have become the key part of assessing overall success of an organisation and its capacity for further effective functioning. This is a consequence of increasing need to assure healthy ecosystems, social equality and good management of organisations. Furthermore, organisations are increasingly supervised by various groups. Consequently, a widespread opinion is that business entities must go beyond bare financial reporting and disclose comprehensive and credible information on a variety of environmental

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and social indicators. There is also a significant demand in the financial markets for non-financial information.

Accounting standards are at the core of the reform at the EU and global level[2] that respond to the recent economic crisis with the aim of increasing transparency and market confidence. This is also an opportunity for recognising a stronger role of sustainable reporting, as in the context of the crisis companies often pay less attention to social and environmental standards. In this respect more concrete rules are needed most notably in relation to social and restructuring reporting, which has made considerably weaker progress in the last decade as compared to the environmental reporting, that being so despite the fact that employees present the key stakeholder group in any business organisation. The economic crisis must thus be used to establish stable foundations for socially more responsible business entities.

This article deals with legal aspects of sustainable reporting in the EU. It firstly explores the state of affairs in sustainability reporting regulation and points out recent increased support for integrated reporting. In the second part of the chapter, EU rules in this field are briefly discussed – first of all, the article deliberates EU rules on financial reporting, which is important as development in this field offers several lessons for future regulation of non-financial reporting and since it is anticipated that financial and non-financial reporting will be additionally integrated in the future. In respect of non-financial reporting both, current state of affairs is presented, particularly the new Directive 2014/95/EU, as well as legal alternatives for more effective regulation are discussed.

2. FROM NON-FINANCIAL TO INTEGRATED REPORTING

2.1.General observations

For many years annual reports were the document in which companies presented their financial results, recent achievements and vision for the future. In the past years, however, the degree of interest for environmental, social and ethical achievements of companies by various interest groups has grown significantly. For this reason, in recent years companies increasingly include matters of corporate responsibility in such reports. The rationale behind this is that financial accounts can only partially show risks and potential value of the company, which derive from intangible factors, such as strategies, product innovativeness, trademarks, reputation, energy effectiveness, decrease of commercial, environmental and social risks etc.

Non-financial reporting, also known as sustainable reporting,[3] enables the companies to disclose such non-financial aspects of their business activities. Sustainable reporting thus marks practice of measuring and disclosing as well as responsibility to the internal and external interest groups for conducting business towards the goal of sustainable development and social responsibility *(i.e. Corporate Social Responsibility)*.[4] The latter stands for predominantly voluntary bond by companies to act ethically and to contribute to the economic development in parallel to improvement of quality of life of the employees and their families, while at the same

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[2] Most notably of the Financial Stability Board initiatives.

[3] Other terms in use include: Corporate Social Responsibility (CSR) Reporting, Environmental Social Governance (ESG) Reporting, Triple Bottom Line (TBL) Reporting etc.

[4] Non-financial reporting, <http://www.ey.com/Publication/vwLUAssets/Non-financial_reporting/$FILE/Climate%20change_Non%20financial%20reporting.pdf> (8.1.2012).

time contribute to the local and wider community.[5] The goal of socially responsible companies is therefore better society and cleaner environment.

Companies use non-financial reporting to increase reputation of the company in society. This form of transparency makes them appear more responsible and thus less risky. This means that the main advantage of non-financial reporting is the transparency of the companies that disclose non-financial information. It increases competitive advantage and reputation of the companies, as well as enhances the capacity to keep workers, shareholders and clients. It is improving the quality of information available to employees. Investors have more reliable information for comprehensive evaluation of the companies, what increases trust of the investors and leads to better allocation of capital. It also increases trust of owners, donators, sponsors and financial institutions and benefits for their branding. Consequently, non-financial reporting increases long-term competitiveness, facilitates access to capital and reduces reputational risks. Better disclosure of non-financial information increases the image of an accountable enterprise and encourages positive relationship with other companies, state authorities, media, suppliers and the community in which the company works, as well as to the environment as it might lead to increased sustainability. Furthermore, Business in the Community, a British business-community charity promoting responsible business, has conducted research, which reveals a significant link between effective management and governance of environmental and social issues and financial performance.[6] The results revealed that those companies which actively managed and measured social and environmental issues outperformed their FTSE 350 peers on total shareholder return by between 3.3% and 7.7%.[7] For all these reasons, despite the predominantly voluntary nature of sustainable reporting, it has become almost the rule among large multi-national companies.

Increasingly widespread non-financial reporting affects annual reports – the latter are less extensive than they used to be, while on the other hand they include more information on initiatives that are considered under CSR. Furthermore, many companies issue separate reports on social responsibility.[8] Also ways the reports are published are changing, since the importance of the social responsibility initiatives for strengthening public image of companies is making it important that annual reports, including results of social responsibility, reach consumers and investors. For this reason companies use various media to widespread the results of their annual reports, including social networks, such as Facebook and Twitter. The reports increasingly often include statements of reliability that are given to the reports by independent external sources with the aim of increasing the level of trust in the disclosed information. Development of CSR thus considerably influences accounting practices in general. In this respect the main challenge for the future is to develop measurable frameworks of sustainable reporting, harmonisation of

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[5] Definition of the World Business Council for Sustainable Development (2000), Corporate Social Responsibility: Making good business sense, p. 9, <http://www.wbcsd.org/web/publications/csr2000.pdf> (8.1.2012).

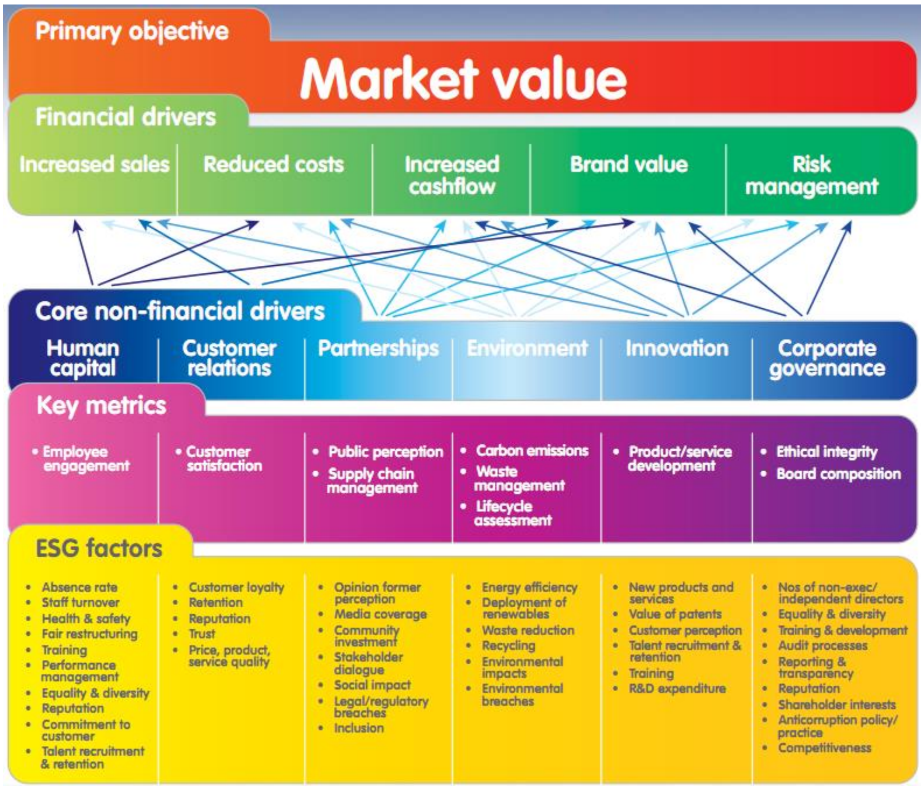
[6] The report examines the relationship between total shareholder return, dividend yield and share volatility and the management of non-financial issues in the 33 UK companies listed on the London Stock Exchange (index FTSE 350).

[7] Laboratory on Valuing Non-Financial Performance: A European framework for company and investor dialogue, <http://investorvalue.org/sourceDocuments.htm> (8.1.2012).

[8] See the Methodologie, Annual Review of Corporate Reports, A review of 2010 Fortune 100 corporate reports, 2011, p. 2, which serve as a barometer of modern reporting practices - <http://methodologie.com/images/Methodologie_2011_Annual_Review_of_Corp_Reports.pdf> (8.1.2012).

definitions and more comparable use of such reports. The way to achieve it is to bring the national and supranational legislation and other rules in the field closer together.[9]

Picture 1: Financial and non-financial drivers of the market value



Source: Valuing non-financial performance: A European framework for company and investor dialogue, <http://ec.europa.eu/enterprise/newsroom/cf/_getdocument.cfm?doc_id=5310>, p. 2.

2.2.International standards of non-financial reporting

Despite its voluntary character non-financial reporting does not avoid legal provisions. At the global level a series of actors has developed individual principles and standards of non-financial reporting – e.g. Global Reporting Initiative (GRI), UN Global Compact, ISO 26000, OECD guidelines, ILO conventions, IASB commentary, initiatives of the Financial Stability Board (IASB), that was established by the G20 group. None of these is currently truly globally accepted in the same sense as in respect with financial reporting, nevertheless, GRI standards come very close to this[10] and are for this reason presented into more detail.

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[9] Synchronisation of voluntary standards on non-financial reporting with compulsory national and supranational requirements is supported by the recent initiative of the Global Reporting Initiative and the World Intellectual Capital Initiative, to develop XBLR taxonomies for non-financial information, considering that also the new US Securities and Exchange Commission requires financial reports in XBLR format.

[10] See also Expert Group on Disclosure, Background non-paper in view of 11 July kick-off meeting.

GRI develops standards of sustainable reporting that are predominantly used across the world.[11] GRI was established in 1997 by the Coalition of environmentally responsible economies (Ceres) with the assistance of the environmental programme of the United Nations. In 1999 GRI published draft version of *Sustainability Reporting Guidelines* and in 2000 the first complete version was published. GRI is a permanent institution of international law with its secretariat in Amsterdam. It is independent even though it cooperates with the environmental programme of the UN and with the initiative UN Global Compact.

GRI endeavours for sustainable reporting to become a regular feature of all organisations as this stands for financial reporting. Its standards are being used by large corporations, public companies, small companies, non-governmental organisations etc. GRI standards are a framework of reporting on issues, such as human rights, position of workers, environment, corruption etc. They are considered as the most credible, considering that they are developed through a consensus-seeking, multi-stakeholder process – participants are drawn from global business, civil society, labour, academic and professional institutions.

GRI is trying to gradually improve standards of sustainable reporting. Today the third generation of GRI standards is in force (GRI-G3) that was published in October 2006 at a large international conference. GRI-G3 standards are composed of principles and items and the latter are composed of several performance indicators. The principles of sustainable reporting help to define:

a) report ***content:*** principles of materiality, stakeholder inclusiveness, sustainability context, and completeness;

b) report ***quality:*** principles of balance, comparability, accuracy, timeliness, reliability, and clarity; and

c) report ***boundary:*** in preparing a sustainability report, a reporting organisation needs to set a “boundary” that defines which entities are included in a report (e.g. parent company and its subsidiaries), and which are excluded (e.g. joint ventures).[12]

Sustainable reporting performance indicators include disclosure of individual management aspects. Items (or factors) concern aspects such as:

- **environment**: materials, water, biodiversity, emissions etc.,
- **human rights**: clauses incorporating human rights concerns in investment and public procurement contracts, prohibition of discrimination, freedom of association and collective bargaining, child labour, forced labour etc.,
- **decent work**: statistics of employees – total workforce by employment type, employment contract, region, gender, return to work and retention after parental leave,

[11] In 2009 over 1.400 organisations from 60 states were using their standards when preparing sustainability reports and eleven states referred to the GRI standards in their national rules – see GRI, Year in Review, 2009/2010, http://www.globalreporting.org/NR/rdonlyres/FDEBC79B-24C3-495B-8297-8F217F3CAC12/0/GRIYearInReview2010.pdf (2.8.2011). Considering the GRI search engine in 2010 sustainability reports were formed by nearly 2000 companies - Sustainability Disclosure Database, <http://database.globalreporting.org/search> (8.1.2012). Additionally, the international research shows that sustainable reporting is considerably better developed in Europe than in the USA – e.g. in 2010 only 251 companies from Northern America formed sustainability reports as opposed to 843 European companies.

[12] See GRI Boundary Protocol, 2005, <https://www.globalreporting.org/resourcelibrary/GRI-Boundary-Protocol.pdf> (8.1.2012).

number of employees included in the collective bargaining, work safety, education and training, equal pay for equal work etc.,

- **society**: impact of the company business for the local society, corruption, breaches of free competition, penalties for breaching legislation etc.
- **product responsibility**: consumer protection, labelling etc.

GRI-G3 standards are the basis for sustainable reporting. Other components of the Framework include Sector Supplements (unique indicators for industry sectors) and National Annexes (unique country-level information). The whole reporting framework (including GRI-G3 standards) is free public good. It is worth mentioning that the fourth generation of sustainable reporting standards is being prepared (GRI-G4), which is about to be published in 2013.[13]

2.3.Integrated reporting

Since the outbreak of the recent financial crisis certain initiatives promoting integrated reporting have arisen from the considerations of sustainable reporting. In this respect the Prince of Wales' Accounting for Sustainability project introduced the Connected Reporting Framework in 2007. The aim of the project was to produce a series of case studies that document the ways in which connecting financial and sustainability information can improve organisational processes and actions.[14] As the crisis has demonstrated the need for capital market decision-making to reflect long-term considerations, the Project started to collaborate with the International Federation of Accountants (IFAC) and the Global Reporting Initiative (GRI) with the purpose of establishing an International Integrated Reporting Committee (IIRC), recently renamed into the Council.

The role of the IIRC, which was established in August 2010, is to help develop a new internationally accepted approach to reporting the result of which will be reports that not only provide financial information, but information about an organisation's governance, social and environmental performance in an integrated manner, which reflects that all these elements (financial, governance, social and environmental) are closely related and inter-dependent.[15] As explained by the IIRC *"Integrated Reporting demonstrates the linkages between an organization's strategy, governance and financial performance and the social, environmental and economic context within which it operates"*, emphasising that *"Integrated Reporting can help business to take more sustainable decisions and enable investors and other stakeholders to understand how an organization is really performing."*[16]

[13] Considering that the new generation of standards is also developed by way of international consultations and workshops with a broad spectrum of interest groups, GRI is appealing to the interested stakeholders to cooperate. See: http://www.globalreporting.org/CurrentPriorities/G4Developments/ (2.8.2011).

[14] The Prince's Accounting for Sustainability Project, Accounting for Sustainability: Practical Insights Book, <http://www.accountingforsustainability.org/embedding-sustainability/accounting-for-sustainability-practical-insights-book> (8.1.2012). Companies reporting using this framework, which links sustainability performance reporting with financial reporting and strategic direction in a connected way, include Aviva, BT and HSBC – see: Hopwood, A., Unerman, J., Fries, J., Accounting for Sustainability: Practical Insights, Earthscan, UK, 2010.

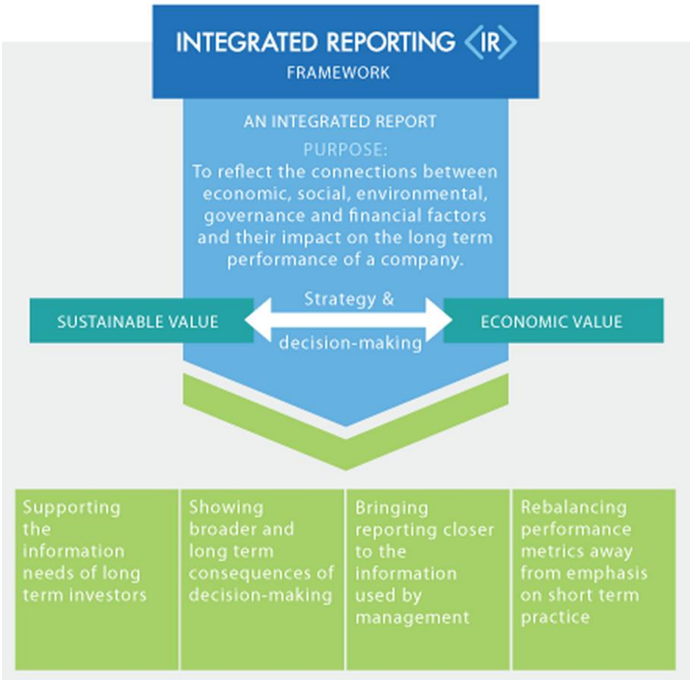
[15] <http://iirc.newsweaver.co.uk/newsletter/1ja775usz5leq5jjkzjymy> (8.1.2012). The IIRC published an Integrated Reporting Discussion Paper for public consultation in mid-2011 and launched a Pilot Programme for Integrated Reporting in October 2011.

[16] IIRC, About integrated reporting, <http://www.theiirc.org/about/>, (8.1.2012).

An integrated report should be a single report which is the organization's primary report – in most jurisdictions the Annual Report or equivalent. By addressing the material issues for an organisation, an integrated report should demonstrate in a clear and concise manner an organization's ability to create and sustain value in the short, medium and longer term.[17]

Considering the increased orientation towards more sustainable development and the lessons learnt in the last economic crisis it is reasonable to expect that integrated reporting will provide an important step for organisations facing the challenges of the 21st century. EU should in this respect lead the way by adopting clear and effective rules, which will assure reliable integrated reports, as well as by encouraging its trade partners to adopt comparable rules.

Picture 2: IIRC integrated reporting framework



Source: IIRC, About integrated reporting, <http://www.theiirc.org/about/>, (8.1.2012).

3. REGULATING CORPORATE REPORTING IN THE EU

This chapter first makes an overview over the regulation of financial reporting in the EU and then continues with initiatives already present and rules already adopted concerning sustainable reporting.

[17] Corporate reporting on financial and non-financial information in a single document has grown as socially responsible investing (SRI) has grown faster than the investment industry overall. As more assets are managed with SRI frameworks, more investors are going beyond financial information to consider non-financial, extra-financial or environmental, social and governance (ESG) information in investment decisions. Companies that already produce integrated reports include BASF, Philips, Novo Nordisk and United Technologies Corporation (UTC).

3.1. Overview of the financial reporting regulation

Accountancy is the business discipline of collecting and analysing critical financial information about a business entity that are relevant for internal decision-making (so-called management accounting) as well as for the external entities (e.g. shareholders, creditors, financial analysts and government agencies – so-called financial accounting).[18] The latter is much more structured than the former as it needs to respond to various needs of the users outside the business entity and is therefore subject to different accounting principles at national, regional and international level. The need for reliable financial statements was accentuated after the 2001 series of financial information frauds involving Enron Corporation and some other well-known corporations, in which management manipulated the figures shown in financial reports to indicate a better economic performance. These problems highlighted the need to review the effectiveness of accounting standards, auditing regulations and corporate governance principles. The Enron scandal has led to developing new regulations to improve the reliability of financial reporting across the globe, including the EU.

The accountancy framework of the EU has been adopted more than thirty years ago. In 1978 the Council adopted the **Fourth company law directive** on the annual accounts of companies.[19] In 1983 the second important accountancy directive followed – i.e. the **Seventh company law directive** on consolidated accounts.[20] These directives regulate issues on formation, adoption and publication of (consolidated) annual accounts and have increased the quality of accounting reporting and enabled comparability and mutual recognition of reports across the EU.[21] Nevertheless, at the beginning of the 1990's this accounting-law framework started to cause increasing problems to the corporations in the EU, that have been searching for capital on the international market. The existing accountancy directives have not enabled comparability of the accounts of public companies at the international level, what was detrimental for the holders of securities and prevented effective control over the financial reporting. These disadvantages reflected the fact that the aim of the directives (in accordance with their legal nature) was solely to harmonise accounting regulations of the Member States and not to achieve complete standardisation of the accounting rules. The reports, drafted on the basis of the directives and corresponding national implementing legislation, did not fulfil international (foremost US) legal requirements in the field. The result of this was that large European companies (so-called global players), that wanted to participate on the international capital market (foremost on the New York Stock Exchange), needed to form double accountancy reports. This was not only expensive but has also led to confusion, both within the companies as well as on the capital markets, as it often happened that reports for the same company showed both profit and loss, depending on the accountancy rules that were applied when preparing the reports.

[18] Elliot, B., Elliot, J., Financial accounting and reporting, Prentice Hall, London 2004, p. 3.

[19] Fourth Council Directive 78/660/EEC of 25 July 1978 on the annual accounts of certain types of companies, OJ L222, 14.8.1978, p. 11.

[20] Seventh Council Directive 83/349/EEC of 13 June 1983 on consolidated accounts, OJ L193, 18.7.1983, p. 1. See also Directive 86/635/EEC and Directive 91/674/EEC of 19 December 1991 on the annual accounts and consolidated accounts of insurance undertakings, OJ L374, 31.12.1991, p. 7.

[21] It is also worth mentioning the Eight Council Directive 84/253/EEC of 10 April 1984 on the approval of persons responsible for carrying out the statutory audits of accounting documents, OJ L 126, 12.5.1984, p. 20.

In order to help large European companies the Commission issued **a new accounting strategy** in 1995[22] with the objective of forming accounting standards, which will be recognised on all world capital markets. In this respect the Commission proposed that the new approach should be oriented towards the International Accounting Standards,[23] that present *»exhaustive and conceptually strong set of reporting standards that are intended for business public«.*[24] IASs have been adopted by the *International Accounting Standards Committee* in London for over thirty years.[25] Since 1983 the Committee comprises of professional accounting organisations that are members of the International Accounting Association, what gives the IASs recognition of being well-devised and internationally recognised accounting standards that have also been recognised by the *International Organisation of Securities Commission – IOSCO*. On the basis of this strategy in 2001 a proposal for a Regulation on the application of the international accounting standards was made.[26] The Commission explained in the proposal that the *internal market approach* to the accounting in the EU is based on political goal of establishing complete and effective capital market. In this respect minimum requirements on financial reporting were no longer sufficient and measures to achieve *»considerably higher level of comparability of business accounts across the internal market«*[27] were needed. On the basis of this proposal a **Regulation 1606/2002 on application of international accounting standards** was adopted in 2002.[28] It is one of the most important acts of the EU accounting law and serves as a basis for endorsement and application of the International Accounting Standards (IASs)/ International Financial Reporting Standards (IFRS)[29] in the EU (Article 1 of the Regulation 1606/2002). The Regulation provides that *»for each financial year starting on or after 1 January 2005, companies governed by the law of a Member State shall prepare their consolidated accounts in conformity with the international accounting standards adopted in accordance with the (special endorsement) procedure (...) if, at their balance sheet date, their securities are admitted to trading on a regulated market of any Member State (...)"* (Article 4).

Table 1: Application of IASs by the EU companies

	Consolidated accounts	Annual reports
Public limited companies	Obliged to use IASs	Member States may apply* IASs

[22] Communication from the Commission, Accounting Harmonisation: A New Strategy vis-à-vis International Harmonisation, COM 95 (508).

[23] It is interesting to note that the Commission did not even consider the possibility of adopting US standards (US GAAP). The reason for this was that the American standards had been established for the American market only. Also political influences on this decision may not be disregarded, considering that EU had no word in establishing US GAAP – in contrast to the IAS.

[24] See Commission, <www.europa.eu.int/comm/internal_market/en/company/account> (14.4.2005).

[25] Structure of the Committee was changed in April 2001, so that it was replaced by the IAS Board.

[26] Commission Proposal for a Regulation of the European Parliament and of the Council on the application of international accounting standards, COM (2001) 80 final.

[27] Ibidem, Explanatory Memorandum, p. 3.

[28] Regulation EC No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards, OJ L243, 11.9.2002, p. 1.

[29] IFRS are issued by the International Accounting Standards Board (IASB); IASs were issued by the IASC, predecessor of IASB till 2000. As many of the standards forming part of IFRS are known by the older name of IASs, the latter term is used in this chapter, also as the Regulation 1606/2002 is known as the IAS Regulation.

Other limited companies	Member States may apply* IASs	Member States may apply* IASs

*Member States may *permit or require* application of the IASs

The Regulation also served as the legal basis for establishment of a special *Accounting Regulatory Committee.* The Committee is composed of the national representatives of the Member States under the Commission's presidency. The purpose of the Committee is to give opinions in relation to the Commission's proposals to endorse IASs. The latter cannot directly apply in the EU,[30] as the EU cannot authorise a private law organisation, upon which it has not direct influence, to form standards binding in the EU.[31] For this reason a special *endorsement mechanism* was needed, upon which the Commission drafts a proposal to endorse an individual or a group of IASs into the EU law and the before-mentioned Committee either approves or rejects the adoption of a specific proposal. This mechanism assures that in the EU only those IASs apply that do not contravene the EU policy, while at the same time increasing legal certainty, as specific regulations clearly indicate, which IASs bind European companies.

Although the Regulation on IASs was adopted the EU accounting directives stayed in force. They are binding for a large group of business entities that are not bound by the Regulation on IASs. In order to assure equal treatment of the entities that are bound by the IASs and those that continue to apply national accounting law of the Member States *(so-called level playing field),* the Commission adopted proposals to amend the existing accounting directives (e.g. principle of prudence was replaced by the fair value principle). Additional amendments were needed for reasons of general development in the accountancy profession in the last twenty-five years related to the technological development (e.g. recognition and valuation of intangible assets). The first important amendment of the accounting directives was adopted by the Directive 2001/65/EC that has changed the valuation rules.[32] Other amendments were adopted in the regular five-year directive on euro amounts.[33] Third group of amendments of the accounting directives were adopted by the Directive 2003/51/EC (known as *"the modernisation directive"*),[34] which concluded the harmonisation of the accounting directives with the IASs. Furthermore, Directive 2009/49/EC[35] was enacted as a response to the 11 Fast Track Actions (FTA),[36] adopted by the Commission with the aim of cutting administrative costs. In this respect

[30] IASs normally do not directly apply; their compulsory nature is recognised only in some states, including Croatia, Macedonia, Serbia, Armenia, Cyprus, Estonia and few others.

[31] Financial Reporting: The IAS Regulation – FAQ, MEMO/01/40, 13.03.2001.

[32] Directive 2001/65/EC of the European Parliament and of the Council of 27 September 2001 amending Directives 78/660/EEC, 83/349/EEC and 86/635/EEC as regards the valuation rules for the annual and consolidated accounts of certain types of companies as well as of banks and other financial institutions, OJ UL L 283, 27.10.2001, str. 28–32.

[33] Council Directive 2003/38/EC of 13 May 2003 amending Directive 78/660/EEC on the annual accounts of certain types of companies as regards amounts expressed in euro, OJ L 120/22.

[34] Directive 2003/51/EC of the European Parliament and of the Council of 18 June 2003 amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC on the annual and consolidated accounts of certain types of companies, banks and other financial institutions and insurance undertaking, OJ L 178/16.

[35] Directive 2009/49/EC of the European Parliament and of the Council of 18 June 2009 amending Council Directives 78/660/EEC and 83/349/EEC as regards certain disclosure requirements for medium-sized companies and the obligation to draw up consolidated accounts – OJ L164.

[36] Smart regulation, Action programme for reducing administrative burdens in the EU,

the Directive 2009/49/EC includes a possibility for Member States to exempt medium-sized entities, which often focus on only one business activity from the obligations to disclose unnecessary information in the notes to the annual accounts.

When the recent financial crisis escalated numerous international accounting rules were severely criticised. The European Commission is now endeavouring to achieve a global agreement on a single system of accounting standards to assure greater financial transparency. This is in line with the latest publication of stricter requirements for disclosure of risk related to financial instruments by the International Accounting Standards Board (IASB), whereas it is also envisioned to adopt stricter requirements in relation to disclosure of off-balance-sheet items. Furthermore, the Commission recently proposed simplification of accounting rules for SMEs and reducing burdensome reporting obligations for listed companies, including SMEs, adding further to cost savings.[37]

3.2.Regulating non-financial reporting

As regards regulation on non-financial reporting achievements of EU are considerably lower than in the field of financial reporting.

3.2.1. Recommendation on disclosure of environmental issues

The EU's commitment to the sustainability reporting was first demonstrated in 1992, when the Commission published its fifth action programme on the environment "Towards sustainability".[38] Among a range of proposals in the area of environmental protection, it provides for a Community initiative in the area of accounting. The Amsterdam Treaty recognised that a key element for promoting sustainable development (Article 6 of the EC Treaty) is the principle of the integration of environmental requirements into other policies and in 2001 the Commission adopted a communication concerning the sixth action plan for the environment.[39] Despite this the Commission found that:

»the lack of explicit rules has contributed to a situation where different stakeholders, including regulatory authorities, investors, financial analysts and the public in general may consider the environmental information disclosed by companies to be either inadequate or unreliable. Investors need to know how companies deal with environmental issues. Regulatory authorities have an interest in monitoring the application of environmental regulations and the associated costs. Nonetheless, voluntary disclosure of environmental data in the annual accounts and annual reports of companies is still running at low levels, even though it is often perceived that enterprises face increasing environmental costs for pollution prevention and clean-up

<http://ec.europa.eu/enterprise/policies/smart-regulation/administrative-burdens/action-programme/index_en.htm#h2-3> (9.11.2011).

[37] Proposal for a directive on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, COM(2011) 684 final. See also Financial reporting obligations for limited liability companies – frequently asked questions, MEMO/11/732, 25.10.2011.

[38] Towards Sustainability, A European Community programme of policy and action in relation to the environment and sustainable development, COM (1992) 23.

[39] Proposal for a Decision of the European Parliament and of the Council Laying down the Community Environment Action Programme 2001-2010, COM (2001) 31 final.

equipment and for waste clean-up and monitoring systems, in particular those enterprises operating in sectors that have significant impacts on the environment.«[40]

The first step in solving these problems was that on 30 May 2001 the Commission adopted a Recommendation on the recognition, measurement and disclosure of environmental issues in the annual accounts and reports of companies.[41] The Recommendation clarifies the accounting rules and indicates how the quality, transparency and comparability of environmental data given in companies' annual accounts and annual reports can be improved. It founds that the absence of a common set of rules for disclosing matters relating to the environment in financial information makes it very difficult to undertake valid comparisons between companies. The Recommendation encourages companies to improve the environmental information provided to the regulatory authorities, investors, financial analysts and the public in general. It applies to the accounting directives concerning certain forms of companies (Fourth and Seventh Company Law Directives) as well as banks and insurance companies. It also takes account of the provisions requiring listed companies to apply the international accounting standards (IAS) as from 2005. As the recommendation is not binding (Article 288 TFEU) its practical effect is dependent upon the persuasive power of the Commission, which called for the Member States to take account of the recommendation and report to the Commission on the measures taken in this respect.

3.2.1. EU accounting directives

Since the adoption of the modernisation directive in 2003 non-financial reporting also became a subject-matter of EU legislation. It is hence a subject-matter of the **Fourth Company Law Directive**. Article 46 (1)(b) of the modernised directive stipulates that to the extent necessary for an understanding of the company's development, performance or position, the analysis shall include both financial and, where appropriate, non-financial key performance indicators relevant to the particular business, including information relating to environmental and employee matters. Similar provision as in Article 46 of the Fourth directive is also included in Article 36(1) of the **Seventh Company Law Directive**, which regulates the content of consolidated annual reports. Both provisions are further emphasised by **the Transparency Directive**,[42] which in Article 4(5) stipulates that *"(t)he management report shall be drawn up in accordance with Article 46 of Directive 78/660/EEC and, if the issuer is required to prepare consolidated accounts, in accordance with Article 36 of Directive 83/349/EEC."*

In comparison to the provisions on financial reporting, which are very precise and comprehensive, provisions on non-financial reporting can be assessed at most as unpretentious and modest. Considering the importance of sustainable development and CSR for future development of the European economy and society, the present EU regulation on non-financial reporting cannot be perceived as satisfactory as it lacks sufficient legal obligation. Non-financial reporting is voluntary as the directives support it only *"to the extent necessary"*. As

[40] Recommendation on the recognition, measurement and disclosure of environmental issues in the annual accounts and reports of companies, OJ L 156, 13.6.2001, para. 4.

[41] Ibidem.

[42] Directive 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market, OJ L 390, 31.12.2004, p. 38-57.

was found by the Commission's public consultation[43] respondents made criticism that this makes it difficult for shareholders and investors to make reasonable assessments of CSR related activities and some even stated that the voluntary regime is only a way to enhance company reputation, rather than adhering to the larger objectives of CSR reporting. In this respect ETUC recently emphasised that *"it is not enough to "invite" companies to act responsibly; more concrete/binding measures are needed"*.[44]

A further problem is that companies are considerably differently treated across EU Member States. As directives are harmonisation (rather than unification) instruments certain Member States (United Kingdom, France, Netherlands, Sweden and Denmark) have adopted rules that exceed requirements from the directives – e.g. Denmark has adopted the UN Global Compact as reference, whereas the French law developed a national frame of reference. Furthermore, while some Member States provide for compulsory non-financial reporting, the other adopted the *»comply or explain«* system. This situation hinders the single market and creates difficulties in benchmarking between companies in different jurisdictions. Moreover, Member States may exempt small and medium sized companies from the obligation of reporting these matters, which additionally diminishes the importance of non-financial reporting.

Considering that the provisions on sustainable reporting has only recently (that is in 2005, when the importance of CSR has already been widely acknowledged) been introduced into the accounting directives it is surprising that the matter has not been regulated into more details. The reasons for the voluntary approach of the Commission may be found in the preamble of the Directive 2003/51/EC, which states that:

"(9) The annual report and the consolidated annual report are important elements of financial reporting. (...) The information should not be restricted to the financial aspects of the company's business. It is expected that, where appropriate, this should lead to an analysis of environmental and social aspects necessary for an understanding of the company's development, performance or position. (...) However, taking into account the evolving nature of this area of financial reporting and having regard to the potential burden placed on undertakings below certain sizes, Member States may choose to waive the obligation to provide non-financial information in the case of the annual report of such undertakings."

It is to be hoped that the crisis has taught the decision-makers that long-term sustainability is an aim, which deserves supporting all instruments available to this end – after all, hardly any legal field can be described as "non-evolving" and should we wait for the legal evolution to end before adopting any binding legislation hardly any relations in the society would be regulated. Additionally, since 2001 when the Commission proposed the modernisation directive principles on non-financial reporting have certainly gained considerably wider recognition and support than they had before.

4. TOWARDS MORE EFFICIENT REGULATION OF NON-FINANCIAL REPORTING IN THE EU

[43] DG Internal Market and Services, Summary Report of the Responses Received to the Public Consultation on Disclosure of Non-Financial Information by Companies, April 2011 (henceforth: Report of the responses), <http://ec.europa.eu/internal_market/consultations/docs/2010/non-financial_reporting/summary_report_en.pdf> (8.1.2012).

[44] ETUC resolution on a renewed EU strategy 2011-2014 for Corporate Social Responsibility (CSR), 7-8 December 2011, para. 17.

4.1. Setting the floor for action

Considering the before-mentioned differences among the EU Member States in respect of their requirements in relation to sustainability reporting and under the pressures of developing CSR the demands for improved comparability, reliability and relevancy of the disclosed information by the companies have strengthened recently. As a consequence of this, the Commission is showing its commitment to more effective rules on sustainability reporting. Several of its initiatives give signs that we can expect more detailed requirements on sustainability reporting in the future.

In this respect the EU's Growth Strategy (Europe 2020)[45] promotes the renewal of CSR. On the basis of this in the Single Market Act, adopted in April 2011, the Commission again stressed that reforms envisioned should *"contribute to sustainable development, based on a highly competitive social market economy"* and that the internal market is based on a *"highly competitive social market economy"*, which reflects the trend towards inclusive, socially fairer and environmentally sustainable growth. Most importantly, amongst the twelve levers to boost growth and strengthen confidence it sets out an initiative to redefine the role of business in today's economy, focusing on improving transparency, particularly in the areas of environment, human rights and sustainable development. The Commission emphasised that new business models are being used, in which these societal concerns are taking precedence over the exclusive objective of financial profit and announced that it will present a legislative proposal on the transparency of the social and environmental information provided by companies in all sectors.

Within a new package on more responsible businesses, which was published in October 2011, the Commission adopted a new communication,[46] in which it put forward a simpler definition of CSR as *"the responsibility of enterprises for their impacts on society"* and outlined what companies should do to meet that responsibility. In relation to this one of the EU's cornerstone policies is to improve company disclosure of social and environmental information, once again confirming the Commission's intention to bring forward a new legislative proposal on this issue.

More concrete Commission's activities to improve regulation on non-financial reporting began in 2009, when the Commission started its discussions with various interest groups by way of organising a series of workshops throughout 2010 and in November 2010 it launched a public consultation on disclosure of non-financial information, which ended in January 2011. In this respect the Commission reports[47] that half of the respondents described the current regime on sustainability reporting applicable in their respective jurisdiction as poor or very poor. In the process of improving current EU rules on non-financial reporting the Commission has commissioned the Centre for Strategy and Evaluation Services (CSES) a specific study aiming at providing some qualitative analysis of current reporting practices in the EU and at providing a cost/benefit analysis of non-financial reporting by companies. Furthermore, the commission

[45] Europe 2020, A strategy for smart, sustainable and inclusive growth, COM (2010) 2020 final.

[46] Communication from the Commission, A renewed EU strategy 2011-14 for Corporate Social Responsibility, COM (2011) 681 final. The Communication was endorsed by the ETUC – see ETUC resolution on a renewed EU strategy 2011-2014 for Corporate Social Responsibility (CSR), 7-8 December 2011.

[47] Report of the responses, ref. supra.

established an Expert/Steering Group on Disclosure of Non-financial information, with the specific mandate to provide expert advice to the Commission.[48]

4.2.Regulatory alternatives for more efficient non-financial reporting in the EU

When deciding about future approaches towards non-financial reporting the Commission will have to choose between several alternatives available, even though they can often be accumulated. These alternatives vary from a number of non-binding (soft-law) instruments at one hand to stringent unified binding legislation on the other hand.

Non-binding instruments to wide-spread non-financial reporting foremost include sharing of best practices, better guidance and creating more incentives for companies within a voluntary regime (e.g. awards for exemplary sustainability reports), industry self-assessment and benchmarks. Furthermore, EU could encourage voluntary reporting and promote existing international frameworks for non-financial reporting. In this respect the Commission could issue a recommendation or guidelines on social reporting, as it has done in relation to environmental reporting, and this way emphasise benefits of sustainability reporting for companies' reputation and competitiveness. According to their non-binding nature all these instruments enable flexibility for the companies/preparers of the reports, on the other hand, however, this mostly means further keeping of fragmented *status quo*, in which certain Member States keep high standards in the field, whereas others do not and where companies that perform well in respect of sustainability prepare the reports, while the others do not, or just emphasise those aspects of sustainability that are worth disclosing, whereas other aspects stay unrevealed – namely, if a company performs well in respect of environmental sustainability it does not necessarily mean that it is also performing well in respect of social sustainability.

In order to assure clear disclosure requirements and hence a level playing field, coherence and comparability across the EU **a change in the existing EU legal regime** for corporate reporting would be needed. As mentioned before, in this respect the Commission announced a legislative proposal on the transparency of the social and environmental information at several occasions. Two options in respect of the legislative instrument are available – a directive and a regulation. In the field of financial reporting both forms of legislative instruments are used – directives when certain differences in regulation between the Member States are tolerable and regulations when completely unified approach is needed in terms of international comparability of the European companies' reports. In respect of the latter, a regulation in the field of non-financial reporting would be an appropriate instrument, should the Commission decide to give a binding nature to one set of international standards on sustainability reporting (e.g. GRI standards), as this has been done in relation to IAS in the field of financial reporting. Since these standards on sustainability reporting are adopted by private entities and do not bind the EU, such regulation could regulate their legal status within the EU and at the same time establish a special Committee that would assess individual standards' suitability for the EU companies and endorse them into the EU legal order, which would give the EU control over the standards that bind EU companies. Despite these advantages of having a regulation in the field of non-financial reporting, at the present state of development of non-financial reporting in the EU it is hard to expect political support for such an act of unification, especially considering that even in the field of financial reporting the Regulation 1606/2002 only binds certain groups of companies (public listed companies) and for certain reports only (consolidated accounts). This

[48] Expert Group on Disclosure of Non-Financial information by EU Companies – Minutes of the Expert Group's first meeting: <http://ec.europa.eu/internal_market/accounting/docs/11072011_minutes_en.pdf> (8.1.2012).

suggests that when considering future legislation in the field of non-financial reporting, it is more realistic to expect a directive than a regulation.

In respect of a directive on non-financial reporting two alternatives were available: one was to amend existing EU accounting directives (Fourth and Seventh Company Law Directive) and possibly also the Transparency Directive, which refers to the former two directives in respect of non-financial reporting. The other alternative was to adopt a new directive all together entirely dedicated to the issues of non-financial reporting. Although both alternatives were acceptable, the advantage of the former was that integration of the rules on non-financial reporting in single legislative acts on corporate reporting might show stronger support of the EU to the developing concept of integrated reporting and make it easier to require integrated reports on both financial and non-financial matters. On the other hand, a separate directive on non-financial reporting could have perhaps more effectively emphasise the importance of sustainability reports, although this would probably mean continuous practice of preparing two separate reports, one for financial and the other for non-financial matters.

4.3.Content of the report

4.3.1. What information should European companies be required to disclose?

Two main options existed in respect of the content of such legislation: a principle-based-approach and approach supporting more detailed disclosure of information. **Principle-based-approach** means a requirement to reveal whether or not companies have a CSR policy, if they do how they implement it, to identify the principal business risks and opportunities arising from social and environmental issues etc. On the other hand, a more ambitious EU legislation would provide more concrete reporting requirements in terms of disclosure of key information (so-called **key performance indicators – KPIs**) regarding issues such as employee engagement, customer satisfaction, and public perception of the company, environmental policies and innovation.[49]

In any event, the Commission should have determine some mandatory principles on non-financial reporting, on which KPIs should be based. The Expert Group has in this respect agreed that non-financial information should be material, comparable, accurate, timely, reliable, clear, verifiable, forward-looking as well as retrospective.[50] As regards more precise content of the report the Commission could have either determine some general topics to report on and/or form a detailed list of KPIs. In relation to the former, the Expert Group agreed that non-financial disclosure should cover at least issues related to human rights, freedom of association, non-discrimination, diversity, equal remuneration, materials and waste, climate change, air quality, energy use and strategy, innovation and anti-corruption.[51] As regards a list of key performance indicators, the Commission could have either determined a specific list of reporting requirements or it can refer to one or more existing frameworks. Respondents to the Commission's public consultation generally suggested that appropriate reference to existing international standards and institutions should be made (e.g. to the GRI, UN Global Compact,

[49] Report of the responses, ref. supra.

[50] Expert Group on Disclosure of Non-Financial information by EU Companies, Meeting Report, 20 Sept. 2011, p. 2.

[51] Ibidem, p. 3.

ISO 26000, OECD Guidelines for Multinational Enterprises etc.), and argued against developing new EU-specific frameworks. Should the Commission comply with this prevailing opinion it should nevertheless decide, whether to select (one or more sets of) international standards, which should be respected by EU companies when reporting on non-financial matters or whether the companies themselves should select relevant indicators – supposedly together with their investors and other stakeholders and disclose information according to such indicators, depending on the use that different stakeholders would make of such information.

It was a generally accepted position that should the Commission make a selection of an appropriate set of standards, preference should be given to those standards that are already accepted world-wide, that are more comprehensive and which are both general (relevant and common to all companies) and sensitive for sectors' specifics. Although none of the international frameworks on non-financial reporting covered all reporting requirements that could potentially be considered, the Commission should have made such a selection in order to achieve comparability that is needed and to enable benchmarking. While it is true, as found by the Expert Group, that in comparison with reporting on financial information there is currently no truly globally accepted standard-setter for non-financial information, it must be admitted that GRI come very close to this.[52] It was also expected that should the Commission give preference to one set of international standards (e.g. GRI) on sustainability reporting many other jurisdictions would follow the EU's choice. Furthermore, most of the organisations that set international standards are open for external suggestions on KPIs and EU should in this respect assure its place in the organisation, whose standards would be endorsed in the EU legislation and significantly influence the content of the standards in the future (such position should after all be a reward for EU's support and promotion of the selected standards). Considerably more important than the question which set of standards might be promoted by the Commission, however, was the question what will the companies' obligations in that respect be – i.e. will the Commission adopt a *"comply or explain"* approach or will it introduce mandatory reporting requirements. This was a choice between flexibility and true commitment to sustainability. It was the choice that had to be made by the EU institutions alone, considering that there are irreconcilable difference between the main stakeholders – companies and other stakeholders in the companies, the former advocating the flexibility and voluntariness, whereas representatives of social and environmental interests justly emphasise that sustainability reporting should no longer be voluntary, much the same as financial reporting is not.

4.4. Other issues on non-financial reporting to be decided

4.4.1. What companies should be required to disclose non-financial information?

One of the most important questions of the reform of corporate reporting concerned the issue what companies should be required to disclose non-financial information. This is primarily, but not exclusively, a question of size. Considering the impact on the economy and local communities as well as for reason of leading business trends, the prevailing opinion was that **large companies** should be bound to report on non-financial aspects of their respective business. As far as **SMEs** are concerned, however, opinions varied to great extent.[53] Respondents to the Commission's public consultation suggested a phase-in approach, whereby

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[52] Expert Group on Disclosure, Background non-paper in view of 11 July kick-off meeting.

[53] For definition of large, medium-sized and small companies see the Fourth Company Law Directive.

the introduction of a new reporting requirement could apply first only to large companies, and later, following evaluation, to medium-sized companies, whereas a significant majority of respondents agreed that small enterprises should not be subject to any mandatory requirement, considering administrative burden this would entail. Contrary to this was argumentation that, although not individually, SMEs collectively have a large impact on society and the environment, and should for this reason be included in the reporting of non-financial information. This is also in line with integrated reporting principles, where small companies are required to report, but under less stringent rules – should the EU support integrated reporting a coordinated approach towards financial and non-financial reporting will be needed.

A specific issue was whether **institutional investors** (e.g. pension funds) should be subject to specific or additional disclosure requirements, e.g. how environmental and social issues affect their investment decisions. This would be important in order to enhance the long-term investment performance, while at the same time increasing transparency to their clients and stakeholders and would thus encourage the former towards more sustainable action. In this respect also one of the UN Principles for Responsible Investment (UN PRI) – Principle No. 3 proclaims: *"We will seek appropriate disclosure on ESG issues by the entities in which we invest."* As possible actions under this principle the initiative emphasises:

- ask for standardised reporting on ESG issues (using tools such as the Global Reporting Initiative);
- ask for ESG issues to be integrated within annual financial reports;
- ask for information from companies regarding adoption of/adherence to relevant norms, standards, codes of conduct or international initiatives (such as the UN Global Compact);
- support shareholder initiatives and resolutions promoting ESG disclosure.[54]

Finally, in relation to the addressees of the disclosure requirements, the issue of **reporting boundary** had to be settled in legislation on sustainability reporting. This required a provision whether a report should include information at group level (the parent company and its subsidiaries) or should these requirements go beyond group level (i.e. including undertakings within the sphere of influence of the reporting company). In this respect the first alternative should have probably been sufficient to get adequate information on the companies' sustainability aspects, while on the other hand assuring legal certainty and not straining the administrative burden upon the preparers of the reports.

4.4.2. External assurance/auditing

Further key issue to be observed by the announced EU legislation concerned the question whether disclosed non-financial information should be audited by external auditors or at least get some sort of external assurance. It is beyond doubt that there is value in getting the non-financial reports assessed by independent experts in order to improve accuracy, completeness and comparability and enhance confidence amongst the stakeholders.[55] Although this is at the same time causing cost for companies, such cost should not be considered undue considering the limited importance of unverified reports. Furthermore, although it is true that external

[54] See <http://www.unpri.org/principles/> (8.1.2012).

[55] See Report of the responses, ref. supra.

assurance on non-financial information involves activities and qualifications significantly different than those required for auditing financial statements, this does not justify legislative approval of reports that are not externally assured. In line with the principle of proportionality SMEs should perhaps be allowed to provide assurance opinions only rather than full audits, which would significantly limit the costs while nonetheless force the companies to prepare truthful reports. Additionally, the Commission should have considered putting the companies under obligation of online publication of non-financial information. As emphasised by the Commission's Expert Group *"reports published online are de facto exposed to "public verification""*.[56] This would directly enable all the stakeholders (employees, consumers etc.) to verify the reports, although the internal stakeholders of the companies should be engaged already in preparation of sustainability reports and not just be informed on the content of the final version. As stressed by the ETCU *"the presence of trade unions is the most effective monitoring system and mechanism for addressing grievances"*.[57]

5. DIRECTIVE 2014/95/EU ON DISCLOSURE OF NON-FINANCIAL INFORMATION

In line with these policy choices the Commission finally proposed a directive that was recently adopted by the European Parliament and the Council.[58] The Directive entered into force on 6 December 2014. EU Member States now have two years to transpose it into national legislation.

The Directive 2014/95/EU amends the EU Accounting Directive 2013/34/EU. It requires companies concerned to disclose in their management report, information on policies, risks and outcomes as regards environmental matters, social and employee aspects, respect for human rights, anticorruption and bribery issues, and diversity in their board of directors. This should provide investors and other stakeholders with a more comprehensive picture of a company's performance.

In its preamble the directive states that *»in order to enhance the consistency and comparability of non-financial information disclosed throughout the Union, certain large undertakings should prepare a non-financial statement containing information relating to at least environmental matters, social and employee-related matters, respect for human rights, anti-corruption and bribery matters.«*[59] It is further stated that *»where undertakings are required to prepare a non-financial statement, that statement should contain,* ***as regards environmental matters****, details of the current and foreseeable impacts of the undertaking's operations on the environment, and, as appropriate, on health and safety, the use of renewable and/or non-renewable energy, greenhouse gas emissions, water use and air pollution.«*[60]

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56 Expert Group on Disclosure of Non-Financial Information, 11. July, 2011, p. 3.

57 ETUC resolution on a renewed EU strategy 2011-2014 for Corporate Social Responsibility (CSR), 7-8 December 2011, para. 19.

58 Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups, OJ L 330, 15.11.2014, p. 1–9.

59 Directive 2014/95/EU, preamble rec. 6.

60 Ibidem, rec. 7, emphasis added.

The new rules will only apply to some large companies with more than 500 employees. This includes listed companies as well as other public-interest entities, such as banks, insurance companies, and other companies that are so designated by Member States because of their activities, size or number of employees. The scope includes approx. 6 000 large companies and groups across the EU. The scope of the Directive is in line with the European Council's conclusions of 24 and 25 March 2011, which called for the overall regulatory burden, in particular for small and medium-sized enterprises ('SMEs'), to be reduced at both European and national levels. Thus, in accordance with the 'think small first' principle, the new disclosure requirements should apply only to certain large undertakings and groups.[61] In relation to the groups of companies the Directive states that *"Consolidated management reports should be drawn up so that the information concerning such groups of undertakings may be conveyed to members and third parties. National law governing consolidated management reports should therefore be coordinated in order to achieve the objectives of comparability and consistency of the information which undertakings should publish within the Union."*[62]

The Directive leaves significant flexibility for companies to disclose relevant information in the way that they consider most useful, or in a separate report. Companies may rely on national frameworks, Union-based frameworks such as the Eco-Management and Audit Scheme (EMAS), or international frameworks such as the United Nations (UN) Global Compact, the Guiding Principles on Business and Human Rights implementing the UN 'Protect, Respect and Remedy' Framework, the Organisation for Economic Co-operation and Development (OECD) Guidelines for Multinational Enterprises, the International Organisation for Standardisation's ISO 26000, the International Labour Organisation's Tripartite Declaration of principles concerning multinational enterprises and social policy, the Global Reporting Initiative, or other recognised international frameworks.

With a view to facilitating the disclosure of non-financial information by undertakings, the Commission should prepare non-binding guidelines, including general and sectoral non-financial key performance indicators. In this respect it is specifically stated that when referring to environmental aspects, the Commission should cover at least land use, water use, greenhouse gas emissions and the use of materials.[63]

Statutory auditors and audit firms should only check that the non-financial statement or the separate report has been provided. In addition, Member States may require that the information included in the non-financial statement or in the separate report are verified by an independent assurance services provider.

The Directive bounds the Member States to ensure that effective national procedures are in place to enforce compliance with the obligations laid down by this Directive, and that those procedures are available to all persons and legal entities having a legitimate interest, in accordance with national law, in ensuring that the provisions of this Directive are respected.

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[61] Ibidem, rec. 13.

[62] Ibidem, rec. 15.

[63] Ibidem, rec. 17.

6. CONCLUSION

Short-term and environmentally as well as socially irresponsible decision-making in majority of economic organisations has created a crisis that is disproportionally harming those that have not caused it. To bring EU economy out of the crisis and to prevent its repeat, a fully engaged orientation towards sustainable development is needed. Sustainable reporting is an important instrument to achieve this objective, considering that disclosure of certain aspects of business activities stimulates companies to actually perform better in the fields they report on. In order that EU in fact achieves these objectives it needed to establish solid legal foundations for effective sustainable reporting that will establish a level playing field across the internal market. The legislation should bind all or vast majority of business entities, who should be required to report on all the important environmental, social and other non-financial aspects of their respective business that affect sustainable development of the society. Such information should be clear, precise, verifiable and should enable comparisons across the EU.

It is understandable and necessary that in the process of proposing and adopting legislation on sustainable reporting EU institutions balance various costs that imposition of sustainable reporting will have on European companies – in form of increased administrative burden and costs in form of data collection, staff training, third party evaluation and assurance etc. Nevertheless, the fear of cost should not lead to such legislation that would prevent any serious achievements in the field of sustainability reporting and jeopardise sustainable development in general. Leaving disclosure of non-financial information voluntary or limiting this obligation to large companies only or to general non-financial information that needed not to be externally verified would reflect that EU is not seriously dedicated to sustainability. On the other hand, however, costs of high standards on non-financial reporting can be alleviated considering that publishing costs can be reduced if templates are offered and considering that after the first year the costs of maintaining the reporting activities are not substantial any more. Companies should, furthermore, access the sustainability reporting as something that may benefit themselves, much the same as financial reporting does, and see the benefits of data collected for better risk control, cost management and better overall definition of corporate strategies. Consequently, although flexibility is an important aspect to be considered when preparing any legislation, within the sustainability reporting legislation it should not be promoted to the level that sustainability itself would be at stake.

Furthermore, it makes sense to support integrated reporting as this could contribute significantly to “mainstreaming” environmental and social issues and raise awareness about the links between financial and non-financial information thus giving a holistic view about a company's activity and helping stakeholders realise that the financial results of a company were only one part of its impacts. The EU should also work in close co-operation with the International Integrated Reporting Council (IIRC) and in the future potentially endorse standards on integrated reporting that will be adopted by the IIRC.

As found by the Commission’s Expert Group, *“better disclosure of social and environmental information could enhance the accountability of enterprises, and consequently contribute to greater public trust in business”.* In order to stabilise EU economy such public trust is an imperative.