

# Moving towards greater transparency in the disclosure of non-financial information

European accounting legislation has been amended to require certain large companies to report on social, environmental and diversity matters. This is the latest development in a series of steps taken by European legislators to move towards greater transparency in company reporting. European companies need to get ready – more onerous reporting is on the way.

## Summary

On 29 September 2014, the European Council formally adopted a directive which requires certain "large public interest" entities to disclose information on policies, risks and results relating to environmental, social, employee, human rights, anti-corruption and board diversity issues (the **Directive**). The Directive proposes to make amendments to the Accounting Directive 2013/34/EU adopted in 2013 (the **Accounting Directive**). The Directive will enter into force shortly after its publication in the Official Journal of the European Union.

## Who will be affected?

Large undertakings which are considered public-interest entities and public-interest entities which are parent undertakings of a large group, in each case, having an average number of employees in excess of 500 (on a consolidated basis for groups) (**Large Public Interest Entities**) will be required to comply with the Directive. This is likely to include companies which are of significant public relevance because of the nature of their business, their size or corporate status, such as banks and insurance companies.

A Large Public Interest Entity which is a subsidiary undertaking shall not be independently subject to the reporting obligations if it and its subsidiary undertakings are included in a consolidated annual report or a separate report of another undertaking.

Member States may exempt small and medium-sized enterprises from the reporting obligation in so far as it relates to non-financial information.

The Commission estimates that this will impact upon 6,000 large companies/groups across the European Union.

## What will be required?

The Directive inserts a new provision in the Accounting Directive which requires a Large Public Interest Entity to provide a statement in its management report on non-financial matters (at a minimum, environmental, social and employee matters, respect for human rights, anti-corruption and bribery) to the extent necessary for an understanding of a Large Public Interest Entity's development, performance and position and of the impact of its activity on such matters.

A Large Public Interest Entity should include information regarding:

- its business model;
- the policy it pursues in relation to non-financial matters and the outcome of such policies, including the implementation of any due diligence policies (such as in relation to its supply or subcontracting chain if relevant);
- the principal risks related to those matters linked to its operations including, where relevant and proportionate, its business relationships, products or services which are likely to cause adverse impacts in those areas, and how it manages those risks; and
- any non-financial key performance indicators relevant to its business.

Recital (7) of the Directive elaborates on the scope of each category of non-financial information, suggesting as follows:

- **Environmental matters**, the statement should contain details of the current and foreseeable impacts of a

Large Public Interest Entity's operations on the environment, health and safety, the use of renewable and non-renewable energy, greenhouse gas emissions, water use and air pollution;

- **Social and employee matters**, the statement may extend to details of actions taken to ensure gender equality, implementation of fundamental conventions of the International Labour Organisation (ILO), working conditions, social dialogue, respect for the right of workers to be informed and consulted, respect for trade union rights, health and safety at work and the dialogue with local communities, and/or the actions taken to ensure the protection and the development of those communities; and
- **Human rights, anti-corruption and bribery**, the statement could also include information on the prevention of human rights abuses and instruments in place in order to fight corruption.

The Directive adopts a "comply or explain" approach. If a company does not have in place any policies in relation to such non-financial matters, it must clearly explain why.

Ultimately, the Directive is not prescriptive and leaves flexibility for companies to report on non-financial matters in a manner which they consider most useful. The expectation is that such reporting should provide concise, useful information on the development, performance, position and impact of a Large Public Interest Entity's activities on the relevant matters.

### Exceptional circumstances

The Directive does provide Member States with the flexibility to allow information relating to impending developments or matters in the course of negotiation to be omitted in exceptional cases where, in the duly justified opinion of the members of the administrative, management and supervisory bodies, the disclosure of such information would be "seriously prejudicial to the commercial position of the undertaking".

### When will the Directive come into effect in a Member State?

Once the Directive enters into force, Member States will have two years to transpose the provisions into national legislation. The European Commission envisages that

companies concerned will be required to report as of their financial year 2017.

A number of EU Member States, including the United Kingdom, already have disclosure requirements in place that go beyond existing EU requirements (see our previous briefings [here](#) and [here](#)). It therefore remains to be seen how the amended Accounting Directive will work alongside the legislative regime of such Member States in order to ensure that businesses are not required to adapt to differing rules in a short timeframe.

### Guidance

The Commission must prepare non-binding guidelines on the methodology for reporting on non-financial information within two years of the entry into force of the Directive, with a view to facilitating relevant, useful and comparable disclosure of non-financial information.

Meanwhile, Large Public Interest Entities are encouraged to look to national frameworks (e.g. the UK narrative reporting regime), EU based frameworks (e.g. the Eco-Management and Audit Scheme) and international frameworks (e.g. the UN Global Compact, the Guiding Principles on Business and Human Rights, the OECD Guidelines for Multinational Enterprises and the ISO 26000) for guidance.

### The European context

The Directive represents the latest in a series of steps taken by the EU to enhance business transparency on non-financial matters in line with its objective of providing consumers with better information on "the responsibility of enterprises for their impacts on society". The Accounting Directive already requires European companies in the extractive industries and forestry to disclose in their financial statements payments made to governments (see our previous briefings [here](#) and [here](#)). The Directive further demonstrates Europe's commitment to improving the transparency and accountability of businesses.

In light of such developments, it would be prudent for companies to develop and implement appropriate internal policies and procedures in order to comply with the forthcoming requirements. Companies that are able to anticipate the proposed changes within their compliance programmes will be a step ahead.

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