HOW IS THE CSR REPORTING OBLIGATION HAVING AN EFFECT?

The EU Non-Financial Reporting Directive (NFRD), also known as CSR law, has been in force for more than two years. Across Europe, some 6,500 companies are affected. But what has the law achieved? An in-depth three-country study commissioned by software specialist iPoint provides answers. The conclusion is mixed: Although reporting on gender equality is relatively high, there is often a lack of transparency, especially with regard to human rights in supply chains.

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Child labor, environmental pollution, consumer deception — the list of corporate misconduct is long. Although many companies work within legal boundaries, black sheep cast a shadow over corporate responsibility. This is why the state has long ceased to rely solely on voluntarism. Increasingly, laws and ordinances are creating binding frameworks. These are supplemented by voluntary commitments and industry standards — a "smart policy mix" as it is referred to by the UN.

One example of such a binding framework is the Non-Financial Reporting Directive of the European Union. The Directive states that non-financial information is "vital for managing change towards a sustainable global economy by combining long-term profitability with social justice and environmental protection." (See Recital 3, Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014.) Indeed, "disclosure of non-financial information helps the measuring, monitoring and managing of undertakings' performance and their impact on society." (Ibid) It consequently decrees that capital market-oriented corporations as well as banks and insurance companies with more than 500 employees have non-financial reporting obligations on matters including environmental, employee and social issues, respect for human rights, and the fight against corruption and bribery.

Important baseline determination

In a recent study commissioned by iPoint, the nonprofit research organization Development International has, for the first time, systematically investigated the degree of non-financial transparency of 516 companies from Germany, 590 from Sweden, and 75 from Austria. To this end, the annual or sustainability reports of these companies were assessed against 60 key performance indicators from the Global Reporting Initiative, the German Sustainability Code, and the UN Global Compact.

On average, disclosure transparency was highest with regard to gender distribution, anti-corruption measures, and employee rights. Many companies tended to report less on environmental issues, and even less on human rights issues. In this regard, each individual company was assigned a "transparency score," which reflects whether the information was disclosed or not. Osram Licht AG turned out to be the transparency leader in Germany (with a transparency score of 30), and Husqvarna AB in Sweden (with a transparency score of 37).

Climate protection: Talking is silver, acting is gold

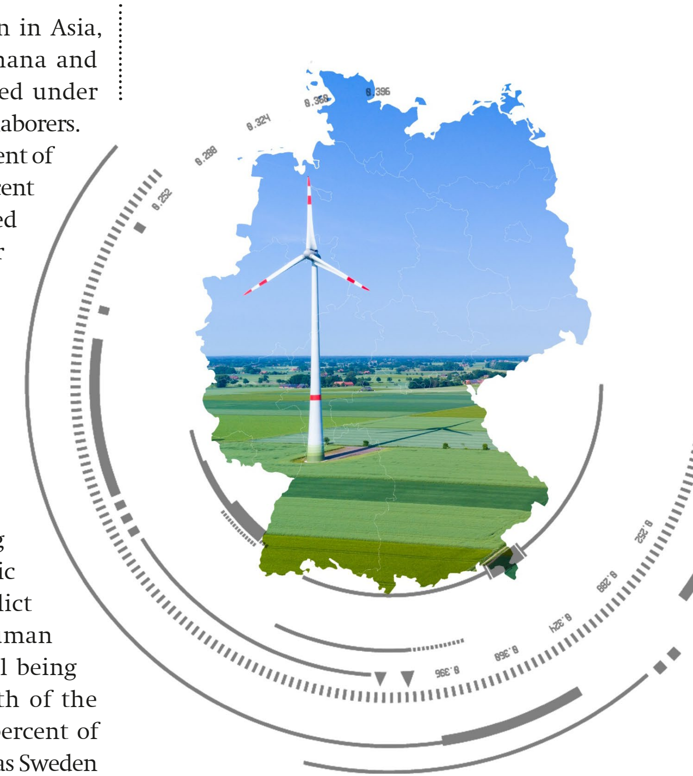
The example of climate protection shows where the wheat is separated from the chaff. Although 75 percent of the German companies and 83 percent of the Swedish companies surveyed reported on the issue of greenhouse gases, not everyone could back up their statements with figures. With respect to Scope 1, for example, which refers to direct greenhouse gas emissions originating from sources owned or controlled by the company, just under a third (32.9 percent) of German companies and 41.6 percent of Swedish companies were able to report the same.

There is also a lot of work ahead in the area of climate management. Only 17.3 percent of the German companies and 38.8 percent of the Swedish companies surveyed have their own climate and emission targets. According to the study, Hamburger Hafen und Logistik AG is one such company: It has set itself the clear goal of reducing emissions for every container loaded by 30 percent by 2020 compared with the reference year 2008. The Swedish company Hennes & Mauritz AB has set a goal to be "climate positive" by 2040, that is, to remove more carbon from the air than it emits.

Yet, sustainable corporate management is not only limited to measuring and managing performance within the group, it also involves taking a further step and addressing potentially negative environmental impacts in its supply chains. Only one company in Germany, Merck KGaA, provided such disclosure. It is a pharmaceutical, chemical, and life science company that identified two suppliers with potential negative impacts on air emissions and improper waste management with the risk of soil contamination. In response, the company developed an action plan and was reportedly monitoring each of these suppliers. By contrast, 43 (17.6 percent) Swedish companies under study reported having taken action on 134 occasions to remediate negative environmental impacts in their supply chains.

Human rights: Monitoring suppliers

In supply chains, not only are tasks outsourced, but risks as well. There are a number of countries and raw materials that are associated with an increased risk of modern slavery and human trafficking: fish from Thailand, cotton from Uzbekistan, and textiles sewn in Asia, for example. Cocoa from Ghana and Côte d'Ivoire is often obtained under hazardous conditions for child laborers. According to the study, 58 percent of German companies and 38 percent of Swedish companies surveyed have child labor on their radar and report on it. For forced labor and modern slavery, the figure is only 34 percent in Germany and 32 percent in Sweden.



With respect to raw materials such as tin, tungsten, tantalum, and gold originating from the Democratic Republic of Congo (the so-called conflict minerals associated with human rights violations that are still being perpetuated in the aftermath of the country's civil war), only 6 percent of companies in Germany as well as Sweden have addressed the issue. However, a new EU regulation (2017/821) due to come into force in 2021 has introduced a duty of care for companies importing those four raw materials. A positive example of active measures is the automotive supplier Schaeffler, which, according to its report, already installed a monitoring process in 2013 that also asks about the origins of materials. Schaeffler does not mince words when describing the issue: The acquisition of 3TG (tin, tantalum, and gold) contributes "in some countries to the financing of armed conflicts and human rights violations."

Supplier standards beyond quality management are still not on the agendas of many German companies, but they are on the agendas of many Swedish companies. Whereas only 31.3 percent of German companies had issued a code of conduct for their suppliers, 82.9 percent had done so in Sweden. On a positive note, however, German companies with a corresponding Code of Conduct are investigating new suppliers in almost 70 percent of cases, and almost 85 percent of cases in Sweden. In this way, the supplier base is rendered more sustainable in the long term. Technotrans AG, for example, reports that new suppliers must undergo a standardized process and are only commissioned if they meet the necessary criteria, including labor practices. One hundred percent of Com Hem Holding AB's new suppliers were screened for human rights in 2017.

Conclusion

Providing an in-the-trenches perspective, iPoint CEO Joerg Walden observes: "Behind and in front of the scenes, we are witnessing bona fide ESG campaigns. But to what extent are companies willing and able to comprehensively disclose their non-financial fundamentals through established reporting frameworks? Everyone is asking this question, and this study provides answers."

Dr. Chris Bayer, principal investigator of the study, concludes the studies on a positive note: "In summary, it can be said that some, but not all of the companies surveyed use the EU Non-Financial Reporting Directive as an opportunity to prove that they deserve a social — and not only a financial — license to operate. ■