Advice to ESMA

SMSG advice to ESMA on its Consultation on the Draft Guidelines on Enforcement of Sustainability Information (GLESI)

1 Executive Summary

The SMSG has in this report limited its response to certain questions rather than providing specific comments to each of the questions in the consultation paper.

The SMSG supports the approach set out in the CSRD to place sustainability information at a comparable level to that of financial information and to align enforcement of financial and sustainability information as much as possible.

Sustainable finance as a topic, as well as the regulatory framework surrounding it, has developed fast and to some extent on different tracks. As a result, market participants as well as regulators spend significant resources and time on tracking and striving to comply with new rules. Against this background the SMSG notes that guidelines applicable to this area may also have to be continuously updated and developed.

The SMSG agrees with ESMA that as the requirements relating to the sustainability information framework is newer than the corresponding framework for financial information, all parties will be on a steep learning curve in the first years of reporting. This will be especially true for first time preparers. The SMSG therefore stresses the importance of flexibility and proportionality in the application and enforcement of the regulatory framework, throughout the whole reporting chain.

As enforcers will have to prepare their GLESI compliance notifications to ESMA for 2025 on an ex-ante basis, before they have full experience with applying and enforcing the new requirements, the SMSG recommends that ESMA has a continuous dialogue with NCAs in the Sustainability Reporting Working Group (SRWG) to share experiences and approaches in this regard.

The SMSG notes that ESRS will be applied both by entities supervised by ESMA and NCAs and by corporates that may fall outside the scope of such supervision, outside the realm of the Prospectus Regulation and the Transparency Directive. The SMSG recommends ESMA and NCAs to monitor and clarify the application of the rules by non-supervised entities, as well as non-EU corporates, and points to the potential risk of an unlevel playing field between unsupervised and supervised entities.

The SMSG in its report also notes the challenges following from differences in (AI-generated) texts in different languages, highlights some unclarities of definitions in GLESI and presents
proposals on how these may be clarified by ESMA, and highlights the role auditors will play in the field of sustainable finance, which is new for them as for everyone else.

Finally, the SMSG proposes, considering the role enforcers will play in accompanying issuers in the implementation process, that ESMA, EBA and EIOPA take the initiative to establish an annual Sustainable Finance Day, corresponding to the popular and useful JC Consumer Protection Day¹ where practical aspects of sustainable finance can be discussed.

2 Background

1. ESMA, on 15 December 2023, published a consultation paper (the Consultation) on Draft Guidelines on Enforcement of Sustainability Information (GLESI) with 25 detailed consultation questions, see appendix.

2. The SMSG considered whether it should provide specific comments to each of the questions but decided to limit its response to the general comments set out below.

3. The Corporate Sustainability Reporting Directive (CSRD) was published in the Official Journal on 16 December 2022. It replaces the current Non-Financial Reporting Directive (NFRD) and introduces several changes to what is presently referred to as non-financial reporting rules which will in future be referred to as sustainability reporting rules.

4. CSRD is to be transposed by Member States into national legislation by 6 July 2024, with a phased application of CSRD and the European Sustainability Reporting Standards (ESRS) commencing on 1 January 2025.

5. The first undertakings will have to start publishing sustainability statements on 1 January 2025, covering the financial year 2024.

3 Guidelines on Enforcement of Sustainability Information (GLESI)

6. The legal mandate for GLESI is set out in Art 28d of the Transparency Directive (TD) which obliges ESMA to issue guidelines on the supervision of sustainability reporting by national competent authorities (NCAs) in accordance with Article 16 of the ESMA Regulation.

7. The guidelines apply to the supervision of undertakings whose securities are admitted to trading on a regulated market in the EU (listed issuers). The guidelines will not be applied

¹ 10th Joint ESAs Consumer Protection Day (europa.eu)
to unlisted companies or micro undertakings. NCAs may however choose to apply GLESI also to such other issuers by way of national “gold plating” rules.

8. The SMSG notes that the scope of GLESI to listed issuers does not cover all entities that have to provide sustainability information under the Accounting Directive and the Taxonomy Regulation. Neither the enforcement of large unlisted undertakings nor listed micro-undertakings are in scope. ESMA notes, however, that enforcers (as well as other entities) may use GLESI on a voluntary basis.

4 ESMA’s approach to GLESI

9. CSRD aims to place sustainability information at a comparable level to that of financial information. ESMA notes in the Consultation that it considers the enforcement of sustainability information by NCAs to play an important role in reaching this goal. ESMA also notes the importance of ensuring a consistent supervisory approach across the annual financial report which will encompass both the financial statements and the sustainability statement.

10. ESMA is basing the draft GLESI on its Guidelines on Enforcement of Financial Information (GLEFI) as they have been in place, with updates, since 2014. ESMA seeks to align GLESI as closely as possible to GLEFI, to ensure that enforcement of financial and sustainability information is aligned. ESMA notes that it has also made some changes to align GLESI also with ESMA’s updated templates for guidelines.

11. The SMSG supports the approach set out in the CSRD and described by ESMA in the Consultation, to align enforcement of financial and sustainability information as much as possible. It also understands that certain changes have been made to align GLESI with ESMA’s updated templates for guidelines and would in this regard question if not also GLEFI should be updated as regards format and terminology (rather than substance) in line with the same templates.

5 Sustainable finance is an area that develops fast

12. Sustainable finance as a topic, as well as the regulatory framework surrounding it, has developed fast and to some extent on different tracks. Market participants including issuers, banks, and investment firms, as well as regulators, spend significant resources and time on tracking and striving to comply with new rules. This means that guidelines applicable to this area may also have to be continuously updated and developed.

13. Against this background, the SMSG agrees with ESMA’s statement, that as the requirements relating to the sustainability information framework is newer than the corresponding framework for financial information, there may be a steep learning curve for
all parties in the first years of reporting. This will be especially true in the case for first time preparers.

14. It is thus important to retain a certain degree of flexibility regarding the enforcement model, meaning e.g. that NCAs would be free to apply an integrated model in which the enforcement of financial information and sustainability information is done in one process and at the same time. Enforcement of ESRS should be made with a good sense of proportion, as the ESRSs are complex, implementation must be done under significant time pressure, and considering that audit standards and usances are still under development. The SMSG further highlights that to the extent that financial intermediaries may be consumers of issuers’ reports for their own reporting purposes, a proportionate approach to enforcement will be necessary throughout the reporting chain until such time as the production of issuers’ metrics is stabilised.

15. The SMSG would in this respect want to note ESMA’s comments that enforcers will have to prepare their GLESI compliance notifications to ESMA in relation to 2025 on an ex-ante basis, before they have full experience with enforcing the new requirements. The SMSG would therefore recommend that ESMA have a continuous dialogue with NCAs to share experiences and approach in this regard. The SMSG also takes note of the fact that Guideline 15 of GLESI establishes the principle that the forum for this dialogue could be ESMA’s Sustainability Reporting Working Group (SRWG).

16. The SMSG notes the fact that ESRS will be applied both by entities supervised by ESMA and NCAs and by corporates that may fall outside the scope of such supervision, outside the realm of the Prospectus Regulation and the Transparency Directive. The SMSG would here recommend that ESMA and NCAs monitor and clarify the application of the rules by non-supervised entities and consider the potential risk for an unlevel playing field vis-à-vis supervised entities. A similar question relates to non-EU corporates and what will happen if they do not comply with EU-standards. It would in these cases be preferable to have an EU-wide standard rather than 27 national standards.

17. A particular concern has shown to be translation of ESRS into national languages. While it is difficult to read and interpret ESRS in the English language, several (AI-generated) translations into national languages (Polish, Danish etc.) have proven to be substandard, even at the time of publication in the OJ. There is thus a risk (even if corrections are made at a later stage) that different interpretations by NCAs may arise due to differences in the translations.

18. The SMSG notes and agrees with ESMA’s comment that enforcers may play a role in accompanying issuers in the implementation process. The SMSG would against this background propose that ESMA, EBA and EIOPA, take the initiative to establish an annual
Sustainable Finance Day, corresponding to the popular and useful JC Consumer Protection Day\(^2\) where practical aspects of sustainable finance can be discussed.

6 Comments on specific definitions and rules

19. The SMSG notes, in relation to the definition of “Infringement” that it is not clear in the document how ESMA will define “material omission or misstatement”. It is important that this definition is applied consistently by national enforcers. At present guidance can only be found in the proposed ISSA 5000 and ESMA will need to define how it assesses the notion of material error.

20. ESMA proposes a 'mixed selection model' for determining which issuers to check (Draft Guideline 5). This model combines a risk-based approach with sampling and rotation. The SMSG supports this approach. However, we suggest that the risk-based element of the selection model be better aligned with the CSRD concept of double materiality. This concept assigns equal importance to financial risks (financial materiality) and the impacts on people and planet (impact materiality). Draft Guideline 5, paragraph 37 states: 'Determination of risk should be based on the combination of the probability of infringements in the issuer’s sustainability information and the potential impact of an infringement on the financial markets.' Properly incorporating impact materiality would mean to also consider the risks of real-world sustainability impacts connected to an issuer's operations. This means, among other things, taking into account which issuer comes from a high-impact sector.

21. Another question relates to the reference in Guideline 5, point 37 a, to "management’s ethical standards" as this can cover many aspects, financial, social etc.

7 Audits and oversight

22. Auditors will play an important role in the field of sustainable finance. This is however a new area for auditors leading to a risk that auditors may interpret rules differently. Member states will also have to have limited assurance, but may choose to have reasonable assurance, which will add complexity to the system.

23. It is important that we, in this new field, do not add layers of gold plating but strive to the extent possible to a level playing field. It should here be kept in mind that, in comparison, non-financial information may to some extent include forward looking information while financial information is traditionally based on historical data.

\(^2\) 10th Joint ESAs Consumer Protection Day (europa.eu)
24. The SMSG here notes that ESMA in its annual report on corporate reporting enforcement has qualified as “material departures” from IFRS requirements some departures that are not so material, as they do not require for most of them a restatement of the financial statements, but rather a correction in future financial statements, and furthermore in most cases a correction of a disclosure. While this may be perceived as an issue relating to ESMA’s internal statistics methodology, it this does not convey a good image of the quality of corporate reporting in Europe. If this trend continues and is amplified in the first years of ESRS application, it could be counter-productive for European companies.

This advice will be published on the Securities and Markets Stakeholder Group section of ESMA’s website.

Adopted on 10 March 2024

[signed] [signed]

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Securities and Markets Stakeholder Group

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3 ESMA issues its 2022 Corporate Reporting Enforcement and Regulatory Activities Report (europa.eu)
Annex - List of consultation questions

1. Do you have comments on the proposed scope of the GLESI? If yes, please explain your views and provide alternative suggestions where needed.

2. Should any further legislative references be added to section 2.1 of the GLESI? If yes, please explain which ones and why.

3. Should any other abbreviations be added to section 2.2 of the GLESI? If yes, please explain which ones and why.

4. Do you agree with the definitions ESMA proposes for inclusion in section 2.3 of the GLESI? Has ESMA covered all the concepts that need to be defined? If not, please explain your concerns and propose how to address them.

5. Do you agree with the proposed purpose of the GLESI? If not, please explain why and make a proposal for what should change.

6. Do you have any remarks on the compliance and reporting obligations?

7. Do you agree with the proposed objective of the enforcement of sustainability information? If not, please explain why and provide suggestions for amendments.

8. Do you agree with the draft Guideline 2 on how enforcers should ensure that they have an effective process for enforcing sustainability information? If not, please explain why and provide suggestions for amendments.

9. Do you agree with the draft Guideline 3 on enforcement of sustainability information prepared under equivalent third country sustainability reporting requirements? If not, please explain why and provide suggestions for amendments.

10. Do you agree with the draft Guideline 4 on the independence of enforcers? If not, please explain why and provide suggestions for amendments.

11. Do you agree with the draft Guideline 5 on the mixed selection model? If not, please explain why and provide suggestions for amendments.

12. Do you agree with the draft Guideline 6 on the timing of the selection model? If not, please explain why and provide suggestions for amendments.

13. Do you agree with the proposed Guideline 7 on the selection universe? If not, please explain why and provide suggestions for amendments.

14. Do you agree with the draft Guideline 8 on the four types of examination enforcers can use when they examine sustainability information? If not, please explain why and provide suggestions for amendments.
15. Do you agree with the draft Guideline 9 which addresses the enforcer’s examination process? If not, please explain why and provide suggestions for amendments.

16. Do you agree with the draft Guideline 10 which presents the conditions which enforcers should apply when they offer their issuers pre-clearance of sustainability information? If not, please explain why and provide suggestions for amendments.

17. Do you agree with the draft Guideline 11 which requires enforcers to undertake quality reviews of their enforcement processes? If not, please explain why and provide suggestions for amendments.

18. Do you agree with the draft Guideline 12 which presents the considerations enforcers should apply when they identify an infringement in the sustainability information and have to determine which enforcement action to use? If not, please explain why and provide suggestions for amendments.

19. Do you agree with the draft Guideline 13 which clarifies the approach to materiality in the enforcement of sustainability information? If not, please explain why and provide suggestions for amendments.

20. Do you agree with the draft Guideline 14 which establishes that enforcers should check whether issuers took appropriate action when they were subject to an enforcement action? If not, please explain why and provide suggestions for amendments.

21. Do you agree with the proposed requirements for how to coordinate enforcement of sustainability information at a European level in draft Guidelines 15, 16, 17, 18, 19 and 20? If not, please explain why and provide suggestions for amendments.

22. Do you agree that it is useful to publish extracts of decisions taken by enforcers, as required by draft Guideline 21, and to report on enforcement activities at national and European level, as required by draft Guideline 22? If not, please explain why and provide suggestions for amendments.

23. Do you agree that the proposed policy option 1 is preferable from a cost-benefit perspective? If not, please explain. If yes, have you identified other benefits and costs which are not mentioned above?

24. If you advocate for a different policy option, how would it impact the benefits and costs? Please provide details.

25. Do you wish to raise any other points which ESMA should consider as it finalises the guidelines?