

# ENNHRI Response to ESMA's Consultation Paper: Draft Guidelines on Enforcement of Sustainability Information

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## 1. Context and general comments

The European Network of National Human Rights Institutions (ENNHRI) welcomes the opportunity to respond to ESMA's Consultation Paper and the Draft Guidelines on Enforcement of Sustainability Information (GLES).

ENNHRI supports the preparation of guidelines to streamline the enforcement of the Corporate Sustainability Reporting Directive (CSRD) and the Taxonomy Regulation by Member States' competent authorities. Adequate supervision and enforcement are indeed crucial to transparency and ensure meaningful sustainability reporting in practice. Such transparency can allow investors to access necessary data informing investment decisions in support of sustainability as well as other stakeholders to pursue accountability for negative impacts on people and the environment by companies. Furthermore, they are a precondition for better-informed decisions by businesses, consumers, and other stakeholders that strive to promote responsible business conduct, including respect for human rights.

The recommendations put forward by ENNHRI aim to highlight the significance of human rights in the implementation of the directives, notably CSRD, as well as in the international frameworks upon which these directives are founded. The integration of human rights considerations into sustainability reporting, as outlined in these documents, warrants greater attention.

Specifically, we find the existing emphasis on human rights within the guidelines to be inadequate, particularly evident in the objectives section. We argue that augmenting the guideline with a stronger focus on human rights is imperative, given that implementation guidelines are instrumental to a successful implementation of the Directives.

ENNHRI has already submitted and published several submissions and a statement on the evolving EU legal framework on sustainable finance and corporate sustainability. This includes the [Submission for the public consultation on revision of the Non-Financial Reporting Directive 2014/95/EU](#) (2020), the statement [Welcoming a social taxonomy in support of human rights](#) (2021), and the [ENNHRI submission on the Platform for Sustainable Finance's report on minimum safeguards](#) (2022).

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

No answer suggested

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

No answer suggested

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

No answer suggested

Question 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.

ENNHRI answer: Given the focus area of the GLESI, the list of definitions should be extended to include key terms set out in the European Sustainability Reporting Standards (ESRS), most importantly "double materiality", "impact materiality", and "financial materiality". Adding these terms to the list of definitions would enhance consistency in interpretations of key concepts across enforcing entities and underline the particularities of sustainability reporting as opposed to financial reporting.

Furthermore, the definitions of the terms "Infringement" and "Immaterial departure" call for reconsideration. Both terms are defined by reference to "material" or "immaterial" omissions or misstatements in reporting. In the context of sustainability reporting however, this choice of terminology poses a risk of causing conceptual confusion because the ESRS equally apply the term "material" in the context of the materiality assessment, i.e. the process of determining what information must be provided in a company's sustainability statement. Therefore, the GLESI should either resort to different terminology or clarify how materiality in the context of enforcers determining the gravity of non-compliance relates to the double materiality assessment of companies determining what information must be disclosed (see also response to question 19).

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

ENNHRI answer: ENNHRI recognises the *immediate* objective of the guidelines to establish consistent, efficient and effective supervisory practices with a view to ensure common, uniform and consistent enforcement of sustainability information as required under the CSRD, the ESRS and the Taxonomy Regulation. What is missing from the purpose statement, however, is the *intermediate* and *ultimate* objectives of the sustainability information framework and therefore the enforcement of it.

The recitals of the CSRD importantly recall relevant international and European frameworks defining sustainability goals, including the Green Deal, the Action Plan on Financing Sustainable Growth, the UN 2030 Agenda for Sustainable Development, the Paris Agreement, and the UN Convention on Biological Diversity (CSRD Recitals 1, 2, 6, 9, 11 and 14). Contributing to the realisation of these frameworks is the ultimate objective of the EUs sustainability information framework. The recitals also clarify that reporting requirements should specify information to be disclosed as it relates to the European Social Pillar, the International Bill of Human Rights and other core UN human rights conventions, including the UN Convention on the Rights of Persons with Disabilities, the UN Declaration on the Rights of Indigenous Peoples, the UN Convention on the Rights of the Child, the ILO Declaration on Fundamental Principles and Rights at Work, the fundamental conventions of the ILO, the European Convention for the Protection of Human Rights and Fundamental Freedoms, the European Social Charter, and the Charter of Fundamental Rights of the European Union (CSRD Recital 49).

The mechanisms for achieving these goals and furthering corporate respect for human rights form the intermediate objectives of sustainability reporting. They include putting investors in a position to understand the risks and opportunities of sustainability issues and the impacts of investments on environmental, social and governance concerns (CSRD Recital 9). In addition, sustainability information facilitates civil society organisations and others to hold companies to account for their negative impacts on people and the environment (CSRD Recital 9). ENNHRI recommends that the purpose section is adjusted to include references to the intermediate and ultimate objectives that should equally guide enforcement efforts by national competent authorities.

Concretely, ENNHRI proposes to add the purpose of ensuring that the enforcement of sustainability information facilitates meaningful sustainability disclosures across EU Member States putting investors, consumers, policymakers, civil society actors, and other stakeholders in a

position to evaluate companies' sustainability performance as it relates to the objectives set out *inter alia* in the Green Deal, the Action Plan on Financing Sustainable Growth, the UN 2030 Agenda for Sustainable Development, the Paris Agreement, and the UN Convention on Biological Diversity. This should include information relating to companies' adverse impacts on human rights and their management thereof.

In addition, the draft GLESI stipulate the objective of making sure that the enforcement of sustainability information closely resembles the enforcement of financial information. While recognising the connectivity between financial and sustainability information (CSRD Recitals 57 and 61), there remain crucial differences between the two regimes when it comes to the type of information disclosed, the time horizon, the users of information and the purpose. Bringing sustainability information on par with financial information may require some expanding on the interlinkages with the Guidelines on Enforcement of Financial Information (GLEFI). However, the guidelines should not disregard the differences between financial and sustainability reporting and their implications in the context of enforcement. Therefore, ENNHRI recommends that the purpose section specifies in detail which principles of GLEFI find application in the GLESI and why. Further, the text should explicitly recognise that while sustainability and financial information interrelate, attention must be paid by enforcers to the particularities of the sustainability information framework.

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

No answer suggested

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

ENNHRI answer: The section on the objective of enforcement merits further clarification. First, the differences between the work of an enforcer and the tasks of auditors or independent assurance service providers should be spelled out more clearly. While the text describes the different modalities of each task (scope, objective and status of sustainability information), it does not explain how the actual examinations compare or contrast. The section would particularly benefit from references to the types of examination that enforcers can perform and the elaborations on the examination process in draft Guideline 9. Second, the draft Guideline should elaborate on what qualifies as "topics for further examination" and what criteria determine their selection. ENNHRI recommends that the Guideline specifies how 'topics for further examination' and the selection criteria relates to the ESRS topical standards and to the double materiality perspective of

the reporting requirements, including to ensure that topics related to impact materiality are prioritised.

Question 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.

The section rightly demands sufficient human and financial resources to guarantee effective enforcement procedures. In this context, it is particularly important that the responsible staff has the necessary skills, experiences, and abilities. However, the present draft only requires experience with the “sustainability information framework”, meaning the specific Articles under the CSRD along with the ESRS and the Taxonomy Regulation requiring sustainability disclosures. These reporting rules alone, however, can only be properly assessed and enforced if the responsible staff possess knowledge and experience on the *substance*, i.e. on environmental, social and governance issues. Therefore, the draft Guideline 2 should be amended to require that enforcement personnel have knowledge and experience on environmental, social and governance, i.e. sustainability impacts of businesses. This also includes proficient expertise on relevant international and regional frameworks, international treaties, and other laws, standards defining responsible business conduct (e.g. the UN Guiding Principles on Business and Human Rights, the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct, etc.).

Question 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.

No answer suggested

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

Draft Guideline 4 introduces several requirements that ensure the independence of enforcers from undue interference in their work. ENNHRI welcomes the provisions on codes of ethics, cooling off periods, assurance of staff independence, and safeguards for the composition of boards preventing that representatives of issuers, audit firms and independent assurance services providers assume a majority. Nevertheless, additional requirements are deemed appropriate to guarantee the independence of enforcers. The processes for nominating the leadership of the competent authorities, for instance, should follow an open nomination process based on clear

selection criteria. Furthermore, the enforcer should have robust policies and processes, not only for avoiding, but also for managing potential conflicts of interest when they evolve.

Question 11:

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

The combination of risk-based, rotational, and random modes of selection in the GLESI is deemed useful and well-balanced overall. Particularly welcome is that risk-based selections should account for at a minimum half of the assessments. However, draft Guideline 5 requires modification when it comes to the determination of risk that would underpin the risk-based approach. Paragraph 37 of the GLESI defines the criteria of a risk-based selection, namely (i.) the probability of infringements in the issuer's sustainability information and (ii.) the potential impact of an infringement on the financial markets. These criteria were adopted from paragraph 55 of the Guidelines on Enforcement of Financial Information (GLEFI), though without adjusting for the characteristics of sustainability reporting, namely the principle of double materiality, the associated distinction between risks and impacts and the different users of sustainability information under the CSRD and ESRS.

A key innovation of the EU sustainability information framework is the duty to report under the double materiality principle. This principle requires not only disclosures on how companies are affected by sustainability issues (*financial materiality*) for the purpose of informing the financial markets, but *also* on how companies impact people and the environment (*impact materiality*) for the purpose of informing the general public. In other words, not only the potential impacts of an infringement on investors decisions are relevant, but also the potential impacts of an infringement on other users of sustainability information. These other recipients include a company's business partners, trade unions and social partners, civil society and non-governmental organisations, governments, analysts and academics (see ESRS 1, paragraph 22 b). The CSRD similarly underlines the diversity of recipients of sustainability information and explicitly refers to civil society organisations seeking to hold companies accountable for negative impacts, for instance, on human rights or the environment (CSRD Recital 9). The determination of risk for the purpose of selecting companies for assessment under the GLESI must take these characteristics into account rather than replicate the GLEFI approach 1:1 as this is a key substantive difference from the enforcement of financial information.

ENNHRI recommends that for the determination of risk, enforcers should additionally consider the potential impact of an infringement on the ability of 'other users' to consider the sustainability information. An indication of this additional risk criterion is information about corporate misconduct and handling thereof, such as in relation to alleged involvement in human rights abuses or environmental degradation incidents. These cases particularly demand the attention of other users of sustainability information, including rightsholders and civil society organisations seeking to hold a company accountable for adverse impacts or gain access to remedy. It is recommended that this is reflected in the 'risk profile' of the issuer (para 37), which should be expanded to include 'severity of issuer's potential or actual impacts on sustainability matters'. High-risk sector affiliation, operations in high-risk countries or conflict territories as well as credible third-party reports about the involvement of an in-scope company in negative sustainability impacts could in this connection trigger a selection of the related sustainability information for examination – *independent* of whether these negative impacts have implications for the financial markets.

Question 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.

No answer suggested

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

No answer suggested

Question 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.

No answer suggested

Question 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.

Draft Guideline 9 stipulates the objectives of the examination process to be undertaken by enforcers, namely determining (i.) compliance with the sustainability information framework and (ii.) consistency with information provided elsewhere in the annual financial statement. What is missing under (i.), however, are more details on the actual assessment of compliance, as reporting

in compliance with the sustainability information framework involves adequate materiality assessment processes. Without further specifications, the GLESI risk incentivising a tick-box approach, where enforcers confine themselves to the assessment of formal compliance rather than substantial examinations, for example, around whether a company has undertaken an adequate materiality assessment and disclosed sufficient corresponding information taking into account credible third party reports concerning its involvement in adverse impacts on human rights or the environment or potential severe impacts associated with its activities in high risk sectors or geographies. To mitigate this risk, it is recommended that Guideline 9 describes the essential steps of the examination process and the type of information that enforcers shall consider in the examination process to evaluate the adequacy of the reporting.

Question 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.

No answer suggested

Question 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.*

ENNHRI welcomes that the GLESI foresees quality reviews to ensure robust enforcement procedures and conclusions. Similar to the recommendations in the response to Question 8, however, the staff responsible for quality reviews should not only have experience and expertise regarding the sustainability information framework, but also on environmental, social and governance impacts by businesses and associated standards set out in international and regional frameworks (e.g. the UN Guiding Principles on Business and Human Rights, the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct, etc.), international treaties, and other documents defining responsible business conduct. Furthermore, attention must be paid to ensure that the personnel undertaking the quality reviews is sufficiently independent, details on how this is to be ensured is to be included in Guideline 11. Finally, the draft Guideline 11 should specify further what the review shall focus on. Considering the purpose of sustainability disclosures, the focus of the review should include evaluating whether current enforcement practices facilitate meaningful sustainability reporting by putting investors, consumers, policymakers, civil society actors, and other stakeholders in a position to evaluate companies' sustainability performance and effectiveness of the measures companies are undertaking to detect, prevent, and address impacts, and, where necessary, to hold them to account amidst the



objectives set out inter alia in the Green Deal, the Action Plan on Financing Sustainable Growth, the UN 2030 Agenda for Sustainable Development, the Paris Agreement, and the UN Convention on Biological Diversity.

Question 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.

No answer suggested

Question 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.

The use of the term *materiality* in draft Guideline 13 to distinguish between light and severe forms of misstatements and omissions of sustainability information is not sufficiently clear. The guideline links the task of determining the materiality of a misstatement or omission to the double materiality assessment companies must undertake to determine what information must be provided in a sustainability statement under the ESRS, where relevant, but does not clarify how to relate the two dimensions. Considering the different roles of enforcers and reporting entities, using the same terminology poses a risk of misconception. Therefore, the GLESI should either resort to different terminology or explain in detail how materiality in the context of enforcers determining the gravity of non-compliance relates to the double materiality assessment of companies determining what information must be disclosed. Finally, Guideline 13 should elaborate on the criteria enforcers should apply to distinguish light from severe misstatements and omissions.

Question 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.

ENNHRI welcomes Guideline 14 and recommends it is further specified what 'a timely basis' for publication of corrected information can be. When doing so it is recommended that the severity of the infringements is considered to ensure the prioritisation of quick publication of corrected information in cases of severe infringements, including where inadequate reporting relates to material impacts on people and planet.

Question 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.

ENNHRI welcomes Guidelines 15, 16, 17, 18, 19, and 20 and their role in supporting crucial coordination at the European level.

Question 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.

ENNHRI welcomes Guidelines 21 and 22 and notes their importance in making available relevant information of use to ESMA, different national level enforcer authorities, preparers as well as users of information around enforcement activities at country levels, including as these will differ across Member States. Such information can also be useful to civil society organisations, representatives of affected stakeholders and other groups involved seeking access to remedy or hold companies accountable as it relates to their sustainability impacts as well as academics and researchers considering the effectiveness of sustainability reporting regulation. ENNHRI recommends that the guidelines are adjusted to ensure that selection criteria do not inadvertently make publication of decisions the exception to the rule. Rather publication of as many decisions as possible should be the aspiration unless there is legitimate reason to refrain. In addition, it is recommended that the Guidelines further specify that reporting on enforcement activities, in addition to disclosing information around enforcement policies and concrete decisions (para 94), also includes disclosing qualitative and quantitative information substantiating how the enforcer carries out its enforcement activities in practice such as number of assessments in the last year as well as details that clarify how assessments are implemented in practice.

Question 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?

No answer suggested

