afep
French Association of Large Companies

Omnibus proposal on the reduction of the administrative and reporting burden

AFEP's position
Competitive Simplification of The Sustainable Finance Framework

17 January 2025

Key points and new architecture of the sustainable finance framework

Increased global competition calls for a **rethink of the regulatory framework for sustainable finance, whose objectives AFEP strongly supports**, to make it a genuine **strategic tool for steering the green transition** and an **opportunity** to develop new products and services to conquer new markets.

The Draghi report identifies the **administrative burden as a major factor in the EU's loss of competitiveness**, particularly vis-à-vis the United States.

In the face of intensifying global competition, **European companies must not be penalised** by disproportionate requirements and standards that others would not have to bear. A **critical threshold has undeniably been crossed** between CSRD, CS3D and the EU Taxonomy.

A simplification process needs to be organised quickly at the European level, in the interests of competitiveness on the one hand and the green transition on the other hand. Indeed, these regulations provide for numerous new requirements from slightly different angles, leading to time-consuming gap analysis and **heavy reporting**, **detrimental to action**.

Consequently, the **sustainable finance framework must be organised around a new architecture**. The **cornerstone should be a streamlined CSRD** with a reduced number of data points in the ESRS standards. Legislations embedded in the sustainable finance framework must be adapted accordingly, to be consistent with CSRD, but also with each other, and to **support transition** (the Taxonomy Regulation, the CS3D, the SFDR, the EU Green Bonds Regulation and the Benchmark Regulation, etc.).

The following points are key for AFEP member companies:

- **Ensure a fair level playing field** compared to non-EU companies operating in the EU and refrain from putting EU companies in a position that weakens their capacity to compete on markets inside and outside of the EU,
- **Reinforce business secrecy and legal certainty** to protect strategically sensitive information and prevent multiple litigation against EU companies on the grounds of information they are obliged to publish (opportunities, forward-looking information, detailed investment plans, financial impacts of sustainability-related factors, remuneration…): EU companies should be exempted from the obligation to publish information detrimental to their legitimate interests. A safe harbour should be granted to companies regarding forward-looking information,
- **Focus sustainability reporting on the essentials,** so that it can be used by companies' management and investors to monitor their transition. The disproportionate amount of information required has a deleterious effect on transition. Rather than serving as a strategic compass, it becomes an exercise of pure compliance,
- **Suspend sector-specific standardisation** until the simplification of cross-sectoral standards has been achieved. Any sector-specific standard must replace rather than add complexity and should build on existing frameworks, such as SASB,

- **Take into account the practical infeasibility** for a multinational company to identify, assess, mitigate and report on impacts on its **entire value chain**: there are hundreds of thousands of players composing this chain and **going beyond tier 1 is a road fraught with pitfalls** (like the refusal of tier 1 to communicate information on its own suppliers),
- **Launch a comprehensive competitiveness assessment of the due diligence directive (CS3D)** in consultation with businesses and their business associations, to identify and address priority areas where clarification and burden reduction should be achieved. Leaving the text as it stands would force European companies to withdraw from certain regions of the world in favour of international competitors with lower sustainability standards. Non-European companies not wishing to bear the legal risks associated with CS3D will reduce their supplies to the EU, including strategic products, as some countries have already suggested. In the meantime, the application of CS3D must be postponed,
- **Streamline overlapping provisions on climate transition plans** (in CSRD, CS3D, ETS, IED) **and revise those with a proven competitive edge.** Strict reference should be made to the Paris Agreement, and the notion of 'compatibility' of each company's climate objectives with the objectives of the Agreement should be defined,
- **Reconsider digitisation requirements** taking into account the development of new technologies, in particular AI,
- **Introduce proportionality** into the framework to limit the heavy administrative burden and unnecessary costs (e.g. audit requirements should be proportionate to the nature of the data, in particular regarding qualitative data that are likely to remain unchanged during more than one reporting period). The EU standard for sustainability audit should be rapidly adopted to avoid the fragmentation of sustainability audit practices,
- **Make the EU Taxonomy voluntary**, while improving the framework and introducing the materiality principle,
- **Extend the simplification approach throughout the entire financing chain** to avoid financial institutions continuing to demand additional information from non-financial companies to meet their own reporting obligations in accordance with sectoral requirements. **Prudential requirements** applicable to financial institutions and insurance companies should **build on the sustainable regulatory framework** to ensure consistency and not add requirements. This principle should be included in the relevant legislation (CRD6 and Solvency 2).

Necessary modifications of the sustainable finance legislation

I. A streamlined CSRD as the cornerstone of the sustainable finance framework

- The disproportionate amount of information required under CSRD **obliges companies to mobilise significant resources for reporting on the green transition instead of allowing to direct those resources towards the green transition itself.** Rather than serving as the strategic compass intended by the legislator, it is becoming a heavy compliance exercise, from which it is difficult to draw conclusions in terms of steering the necessary transition.
- This burden has a **detrimental effect on the entire value chain and also impacts small and medium-sized enterprises (SMEs),** on whom it is automatically shifted through requirements imposed on business relations.
- **A strong political signal** should be sent:
  - To the **European Securities and Markets Authority (ESMA) so as not to penalise those EU companies** who are the first to implement the CSRD, which has not yet been transposed in many Member States. This first reporting exercise necessarily has room for improvement, as it is new for both the companies and their auditors. **The role of ESMA and National Competent Authorities in**

charge of the supervision of listed companies should be to support the implementation. Overly strict controls on this initial reporting would create difficulties for both the auditors and the companies, penalise those EU companies trying hard to comply with the new rules and would be contrary to the spirit of gradual implementation called for by the companies and already reflected in the CSRD and the ESRS.

- To the **European Central Bank**, the **European Banking Authority** and the **European Insurance and Occupational Pensions Authority to refrain from imposing additional requirements** on credit institutions and insurance companies that would be passed on to non-financial undertakings.

1. Reinforce the business secrecy and legal certainty

– LEVEL 1 The CSRD requires companies to **publish strategically sensitive information.** In a highly competitive world, this information may be used by competitors who will not be concerned by these transparency requirements. **The CSRD must not become a sovereignty risk for the European Union in an international trade context that is likely to become even more tense.**

Trade secrets must absolutely be preserved. The provisions of the directive allowing **derogations from the publication of sensitive information must therefore be strengthened** and amended to (i) exempt companies from the obligation to disclose information that could be seriously detrimental to their legitimate interests and (ii) remove the reference to members of the administrative, management and supervisory bodies. Furthermore, a **safe harbour should be granted to companies regarding forward-looking information**.

2. Refer to the obligations of the Paris Agreement instead of "+1.5°C" when it comes to companies' climate action and clarify the notion of "compatibility"

– LEVEL 1 The CSRD requires disclosures on plans *"to ensure that its business model and strategy are compatible with the transition to a sustainable economy and with the limiting of global warming to 1,5 °C in line with the Paris Agreement"*. This provision tends to regulate the substance instead of strictly focusing on the transparency and quality of climate disclosures. The notion of compatibility with 1.5 °C poses several severe issues:

- The Paris Agreement applies directly to Parties which are States (EU for Europe) and **not directly to companies**. Furthermore, the Paris Agreement sets the principle of Nationally Determined Contributions (NDCs) for the Parties exclusively for their greenhouse gases emissions **on their own territory (scope 1) and not on indirect emissions outside their territories**. By difference, the CSRD created an **unprecedented legislative obligation** for companies to report on climate targets **<u>outside the EU for their scope 1 emissions</u>** –even in States having their own climate regulations – and in addition, also for their scope 2 and scope 3 emissions. This goes **far beyond the obligation of the Paris Agreement** and the competitive impact of this provision has **not been tackled** properly in an impact study. Such an impact study must be performed, and lessons must be drawn if it concludes that this regulatory provision from the CSRD **puts EU companies at a disadvantage** compared to companies operating in the rest of the world and which commit under a sheer voluntary framework.
- The Paris Agreement aims to limit global warming to "**well below 2°C** and pursuing efforts to limit [it] to 1.5°C" but does not require States to assess their NDCs' compatibility with such goal. There is **no internationally agreed scenario of what such a goal would imply** (in terms of economy, policies, technology, consumer behaviour, etc.). There is **no scientific consensus** either – the IPCC takes into account no less than 97 different scenarios limiting global warming to 1.5°C with no or limited overshoot[1]. In addition, **GHG reduction pathways will necessarily vary between sectors and between geographies**. Without an authoritative scenario relating to a global warming target, the disclosure of compatibility with such a target will lack any comparability and may only lead to uncertainty and legal insecurity for companies. Compatibility with a temperature goal may only be an optional disclosure but does not seem practicable in the Directive.

[1] Cf. IPCC, "Climate change 2022 – Mitigation of Climate Change", page 1886.
https://www.ipcc.ch/report/ar6/wg3/downloads/report/IPCC_AR6_WGIII_FullReport.pdf

- In addition, the CSRD **only refers to "+ 1.5°C"** in the Paris Agreement while in its Article 2, the Agreement mentions *"Holding the increase in the global average temperature to well below 2°C above pre-industrial levels and pursuing efforts to limit the temperature increase to 1.5°C above pre-industrial levels"*. Therefore, **there is no reason to restrict in the CSRD the objective to "+1.5°C"** while this would not be the case for the Parties. It must be reminded that **experts consider that the temperature is very much likely to reach "+1.5°C" in the first years of 2030s**. In this perspective **what would be the meaning of a "+1.5°C" climate transition plan for a company?**

- Finally, **the notion of "compatibility"** mentioned above in the requirement of the CSRD **has never been defined by level 1 and 2 EU Regulation and therefore proves not to be clearly applicable**. This problem was recognized by DG FISMA during the EFRAG Sustainability Reporting Board session on 12 December 2024. **Therefore, at the very least, CSRD should be amended to define this concept in order to reduce legal certainty.**

Conclusion: At the very least, the requirements of the CSRD should be **strictly referring to the Paris Agreement's temperature goal** and the **notion of "compatibility"** between each company's climate objectives and the ambition of the Paris Agreement should be clearly defined. We understand that DG FISMA announced in mid-December 2024 the need for the Commission to bring clarity on this issue and we support this initiative.

3. Serve strategic steering of sustainability

– LEVEL 2 The **disproportionate amount** of information required under the ESRS has a **deleterious effect on the transition**. Rather than serving as a strategic compass for action, it becomes an exercise in pure compliance.

– The CSRD provides for the Commission to review the ESRS at least every three years from their date of application (1st January 2024), taking into account the opinion of EFRAG, and to amend these standards if necessary. Considering what is at stake, **the revision process needs to be triggered as early as 2025**, taking into account the lessons learned from the first reporting exercise carried out by large public interest entities on reporting year 2024.

– **Afep calls for the Commission to conduct a thorough assessment in the first half of 2025 to revise the delegated act containing the ESRS to simplify them in depth.** This assessment should involve EFRAG and preparers from financial and industrial sectors, auditors and other stakeholders such as investors.

– The information required must be **reduced and also clarified** where needed to allow sustainability reporting to serve **the strategic steering of transition policies by directors**. Also, the wording and/or translation of certain ESRS are not comprehensible. The fact that EFRAG needs to publish multiple guidelines and Q&A in attempt to clarify the reporting obligations highlights the necessity to radically simplify the standards themselves. Furthermore, their structure, which is broken down into disclosure requirements, application requirements, minimum disclosure requirements, etc. leads to confusion.

– **Some indicators, for example social indicators, are very difficult to calculate** because the data is not available on a global basis due to the lack of a global HR information system, reflecting the fact that **consolidating global HR data is generally not a relevant steering tool for the social policy** that companies are pursuing. Other indicators don't make sense, such as the ratio between the total annual remuneration of the best paid person and the median total annual remuneration of all employees. **Calculating a global ratio makes no sense** given the differences in salary levels between geographical areas. As regards **decent pay**, what should be the basis for monitoring in the absence of a common benchmark (outside the EU)? Finally, some indicators may present a **major and unjustified reputational risk,** for example the publication of the number of labour-related human rights complaints, rather than final convictions.

- LEVEL 1 & 2 The Commission should propose **an immediate freeze on sectoral standardisation until all the simplifications of cross-sectoral standards have been carried out**. Sector specific standards should simply adapt and replace agnostic standards rather than add new data requirements. The pursuit of sectoral standardisation must therefore be conditional **on the prior simplification of cross-sectoral standards and a radical change in the method and outcome,** building on existing frameworks, such as SASB. **The first two drafts** drawn up by EFRAG's SRB for the oil and gas sector on the one hand and for extractive activities on the other **are too granular** (e.g. site-by-site information) and **insufficiently interoperable with the SASB's international standards**. The **sector nomenclature** used by EFRAG is a European nomenclature, NACE, which is **poorly adapted to sustainability issues and disconnected from the ISSB's international classification**.

- LEVEL 1 **Flexibility should be introduced when data are not available:** in some cases, data are not available at the date of reporting and/or it can be technically impossible to collect data from multiple sources. Companies should not be required to publish estimates. The notion of **reasonable effort** in data collection should be recognised.

4. Exempt listed subsidiaries from the obligation to publish their own sustainability report

- LEVEL 1 The CSRD provides for two different regimes for subsidiaries within the same group: listed subsidiaries must publish their own sustainability report, while unlisted subsidiaries are exempt. It is necessary to **remove the requirement for a listed subsidiary** of a parent company subject to CSRD **to produce its own sustainability report** when it is included in the parent company's report.

5. Re-examine digitisation obligations

- LEVEL 1 **The digitisation of sustainability information will represent a significant additional burden** for companies. The digitisation of sustainability reports will have to be carried out as soon as the technical measures defining the format (XBRL) and digitisation methods (ESRS digital taxonomy) are adopted by the European Commission (first application in 2027).

- The development of new technologies and, in particular, **artificial intelligence, calls into question the relevance of digitising** sustainability reports. **Digitisation of sustainability reporting should be postponed** and a **detailed impact analysis** needs to be carried out**, including feedback on the costs and benefits of the implementation of ESEF for financial statements**.

- Furthermore, many stakeholders consider that the ESRS digital taxonomy drafted by EFRAG is too complex and burdensome to implement.

II. Postpone the application of CS3D to assess its impacts on the competitiveness of EU companies and amend the text

- LEVEL 1: **The assessment of the CS3D's competitive risks is a prerequisite to its application**. At the end of this assessment, its results should lead to the text being renegotiated. To initiate this process, the **postponement of the directive's application** should be included in the ‘Omnibus’, along with an obligation for the European Commission to carry out, within 2 years, an **assessment of the directive's (post-adoption) impact on the Union's competitiveness** and to report back to the European Parliament and the Council.

- Leaving the text as it stands will, on one side, lead EU companies to **withdraw from certain regions** of the world and to abandon these markets to international competitors who are not subject to such obligations and who often have less ambitious climate ambitions and ESG policies, and on the other side, lead some non-EU companies to leave the EU market or restructure their financial consolidation. **Non-European companies not wishing to bear the legal risks associated with CS3D will reduce their supplies to the EU**, particularly of strategic products, as some countries are already suggesting.

- The CS3D Directive, which was negotiated in haste on a highly complex subject, raises **problems of clarity and legal certainty and places excessive demands and legal risks on companies under its scope**. By way of illustration, these difficulties concern inter alia:

  - The particularly **broad definition of the chain of activities** to which the obligations of vigilance must relate which leads to an infeasible and complex exercise,

  - The **obligation to carry out meaningful engagement** with an indefinite number of internal or external stakeholders,

  - The interactions between **competition law** and the requirement to provide support to SMEs which are business partners of the company,

  - The uncertainty as to how the **transition plans** must be assessed to qualify as compatible with the Paris Agreement (see the detailed description of the difficulties linked to the notion of compatibility with 1.5 °C in point I.3. here above).

  This **penalises EU companies' competitiveness, in a geopolitical context of exacerbated competition**.

- In particular:

  - Regarding the **chain of activities**, the CS3D lays down that due diligence obligations must cover the upstream chain of activities and part of the downstream chain. This requirement is not feasible in practice. Companies can hardly carry out due diligence beyond one or two tiers, depending on their situation. Indeed, **there are no reliable and robust tools that allow the chain of activities to be traced automatically**.

    This approach will involve sending **hundreds of questionnaires** to the various business relations, who will then have to deploy them within their own business relations. **Some may even refuse to respond**, especially if they are economically more powerful than the companies placing the orders. The possibility of adopting a risk-based approach and prioritising risks will not be sufficient to rationalise the considerable workload and to reduce the legal uncertainty.

  - Regarding **engagement with stakeholders**, the particularly **broad definition** of stakeholders, which covers not only the company's own stakeholders but also those of all its partners throughout the value chain, makes the obligation of engagement **infeasible** in the light of the obligations placed on companies to:

    . **Consult stakeholders at several stages of the due diligence process** (including when deciding to terminate a business relationship) which may give rise to problems of business secrecy;

    . **Respond to requests for additional information** from the 'stakeholders consulted', it being specified that the company must respond 'within a reasonable time' and 'in an appropriate and understandable format' or justify in writing its refusal to respond to a request for additional information. **This will lead to litigation by stakeholders** who feel that they should have been consulted or that the responses given to their requests are pointless.

III. Streamline provisions on climate transition plans and revise those that jeopardize competitiveness

LEVEL 1 The European directives adopted during the last mandate create a **tangle of provisions relating to transition plans of different kinds and with different scopes, which need to be streamlined to have a clear and effective legislative architecture.** The provisions in question relate to:

- The Corporate Sustainability Reporting Directive (CSRD), which refers to "climate transition plans" at group level,

- The European Emissions Trading Directive (ETS Directive), which refers to "climate neutrality plans" at plant level,

- The Industrial Emissions Directive (IED), which encourages "transformation plans" at facility level; and finally,
- The Corporate Sustainability Due Diligence Directive (CS3D), Article 22 of which requires **the adoption and implementation of a transition plan for climate change mitigation**, and which provides that companies that declare a plan under the CSRD are deemed to have complied with the obligation to adopt a plan under the CS3D, with the proviso that it must be implemented and updated every 12 months. More generally, the CS3D, which was hastily adopted at the end of the mandate, not only **lacks the legitimately expected clarity and is therefore a source of considerable legal uncertainty**, but above all presents clear risks for the continent's competitiveness and its energy supply security,
- The Capital Requirements Directive (CRD), recently amended to include the **requirement for banks** to develop **plans to monitor financial risks** arising from ESG factors and in particular the **objective to achieve climate neutrality**.

Consequently, to avoid the superposition of different legislations, there is an **urgent need to:**

- The **CSRD should be the only legislation defining the requirements regarding the climate transition plans.**
- **Delete unnecessary constraints on conditional allocations under the EU ETS:** There is no reason for the previous amendment of the EU ETS Directive (Article 10a (1)) to have introduced a conditional cancellation of free allocations by 20% for the installations with emissions above the 80th percentile of their benchmarks. Indeed, the core principle of the EU ETS is to reduce greenhouse gas emissions at the least expensive costs through a price signal, wherever the reduction takes place, as those emissions create global pollution, not local pollution. Therefore, **there is no justification to impose an additional restriction on allocations (-20% of free allocations) at the installation level through a regulatory approach**, as the existing price signal already forces the low-performing installations to buy costly allowances. It must be reminded that the regulation approach at the installation level is dedicated to local pollutants, not to global ones. As a result, **the provision imposing this restriction of -20% of free allowance on these low-performing installations must be deleted**. Consequently, **the climate neutrality plans at the installation level, which have been conceived to enable those installations to regain those 20 % allocations, are therefore pointless under the EU ETS. They must be deleted.**

  In addition, AFEP considers the conditional free allocations depending on energy efficiency efforts at installation level (up to -20% of free allocations) should be removed from the EU ETS (article 10a (1)), as it is a topic dealt with by the Energy Efficiency Directive.
- LEVEL 1 **Remove from the Industrial Emissions Directive** (IED) the integration of greenhouse gases as a part of the transformation plans at the installation level, **as climate action plans are set up at group level, not at the installation level**.

IV. Make the EU Taxonomy voluntary

- The **purpose and usefulness of the Taxonomy Regulation need to be reassessed** taking into account the disclosures required by CSRD.
- Furthermore, **the EU Taxonomy is not fit for purpose considering the following points**:
  - The EU taxonomy covers only part of the EU economy and for eligible activities, **the alignment based on the revenue, CapEx or OpEx KPis is still low**. The investment universe is therefore very small;
  - Generally speaking, the EU Taxonomy is a **too complex tool**, and its usability needs to be improved;

- The **criteria used to determine alignment need to be amended** in particular to better support transition. For instance, the Do No Significant Harm (DNSH) test is not properly designed regarding the objective of pollution reduction and prevention. This situation results in a disproportionate burden to prove that the test is passed or the exclusion of many activities;

- The Taxonomy reporting requirements raise many issues and are too burdensome. The OpEx indicator appears to be of little relevance but requires considerable efforts to collect the necessary data and disclose the indicator. The definition and the implementation methods of the Green Asset Ratio (GAR) needs to be revised and simplified to make it applicable.

– LEVEL 1 Moving forward, AFEP considers that the **Taxonomy Regulation should be amended to address the issues mentioned above and made voluntary.** The **materiality principle should also be introduced** in the Regulation. Companies seeking for instance public sector financing for their projects or issuing EU Green Bonds could use the EU Taxonomy to demonstrate the alignment of their activities. All references to the EU Taxonomy in other legislations (SFDR, ESG Ratings, MiFID/MiFIR and Pillar 3 ESG) should be amended accordingly to take into account the would-be voluntary nature of the Taxonomy.

V. Amend the SFDR

Some of the administrative burden from CSRD has been designed to ensure the availability of data for the financial sector's ability to comply with SFDR. SFDR should also be streamlined to avoid that it imposes more disclosures to sectors using financial services.

– LEVEL 1 To ensure that the disclosure requirements are fit for purpose and consistent with the Corporate Sustainability Reporting Directive (CSRD), the materiality principle should be introduced in the SFDR meaning that all PAI indicators should be subject to a materiality test.

– Furthermore, the number of PAI indicators should be reduced and their content based on the disclosures required by the ESRS. Requirements applicable to financial market participants should be amended accordingly.

About Afep:

Founded in 1982, AFEP brings together 117 of the largest French companies, which represent 15% of France's commercial GDP, employ 13% of the private sector workforce, and account for 20% of the mandatory corporate contributions in France. AFEP member companies employ 8.5 million people and are key players in the French, European, and global economies across all sectors of activity. Among the 60 largest European companies, a third is a member of AFEP.

Its mission is to contribute to the creation of an environment conducive to the development of economic activity and to make the voice of large French companies heard by policymakers in Paris and Brussels. They are fully committed to the green and digital transition, innovation, and the pursuit of better governance.

AFEP is involved in drafting cross-sectoral legislation, at French and European level, in the following areas: economy, taxation, company law and corporate governance, corporate finance and financial markets, competition, intellectual property, digital and consumer affairs, labour law and social protection, environment and energy, corporate social responsibility and trade.

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Transparency Register identification number: 953933297-85