Climate Disclosure Standards Board

The state of environmental disclosure in Romania in 2020

In our new report 'The state of EU environmental disclosure in 2020'[1] the Climate Disclosure Standards Board (CDSB) has taken a deep dive into the environmental disclosures of the largest listed companies in the EU. Third in the series, we pick up where our previous report 'Falling Short?'[2] left off, comparing where we were then and what progress has been made. Supported by the LIFE programme of the European Union, CDSB reviewed the 2020 environmental disclosures of 50 of Europe's largest listed companies, with a combined market capitalisation of US$3.5 trillion, under the EU Non-Financial Reporting Directive (NFRD) and the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD).

Of the 50 companies sampled, none were situated within Romania. As a result, for this briefing we have used the 15 Romanian companies examined by the Alliance for Corporate Transparency (ACT) in their analysis of EU companies' performance under the NFRD[3] compared to 303 companies across Europe. We will look to reach a conclusion on how Romania is performing relative to the average level in the EU as also identified in ACT's sample. ACT's methodology in analysing its larger data set was similar to that of CDSB's, by focussing on performance against the core content elements of the NFRD.

All data used when referring to Romanian companies and the European average is that of ACT's analysis unless otherwise explicitly stated.

The current state of play: CDSB's analysis

Our latest review of 50 of Europe's largest listed companies, none of which were situated in Romania, shows signs of improvement in the completeness and quality of aspects of environmental disclosure. However, the core challenges identified in our previous research, relating to TCFD adoption, risk disclosures and the application of materiality, must still be addressed to provide investors with the consistent, coherent and comparable disclosure needed.

Key Findings from CDSB dataset

- **Business model:** 52% of companies fully disclosed the relevant environmental aspects of their business;
- **Policies and due diligence:** All companies disclosed environmental policies, but 30% did not clarify board and management level due diligence;
- **Outcomes:** 26% did not use targets to monitor environmental performance and 16% failed to link progress updates clearly to policies;
- **Principal risks:** 74% considered both physical and transition risks, but just 4% companies clearly disclosed their risks over different time horizons;
- **Key performance indicators:** All companies provided GHG emissions disclosure, but only 10% disclosed metrics on biodiversity;
- **TCFD:** 68% referenced TCFD in their disclosure, but only 18% adequately disclosed their resilience to different climate scenarios;
- **Materiality:** 38% applied the double materiality perspective to their environmental disclosures; and
- **Disclosure location and format:** 82% included their non-financial statement in the mainstream report, but disclosures grew by 36% compared to 2019.

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[1] CDSB (2020) The state of EU environmental disclosure in 2020. [PDF]. Available from: https://www.cdsb.net/nfrd2020

[2] CDSB (2020) Falling Short? Why environmental and climate-related disclosures under the EU Non-Financial Reporting Directive must improve. [PDF]. Available from: https://www.cdsb.net/falling-short.

[3] Alliance for Corporate Transparency (2020), Database for Non-Financial Reporting Directive Review [Online], Available at: https://www.allianceforcorporatetransparency.org/database/2020.html

Romania: Overview of ACT's analysis

Overall summary from ACT dataset

The review of the 15 Romanian companies' non-financial reporting results by ACT revealed an overall below average level of compliance with NFRD requirements when compared to the rest of the EU in their own dataset.

Business model

Romanian companies performed slightly below the EU average when it came to disclosing business models:

- They were less likely to make references to environmental matters within their business models than the EU average and none were able to display climate change, as displayed in the chart below.

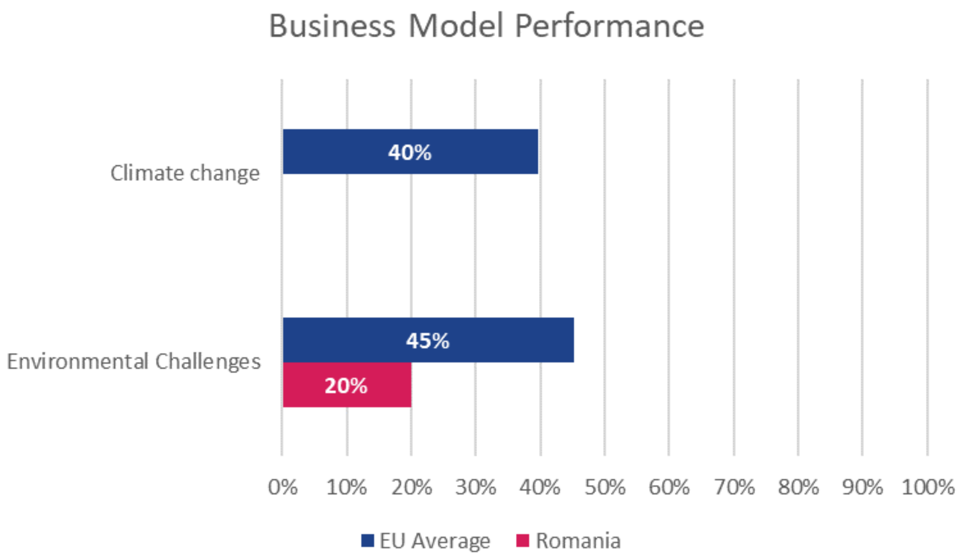

Figure 1: Romania vs EU business model disclosure comparison

Policies and due diligence

Well-articulated corporate policies provide the basis to inform and structure a company's environmental and climate-related disclosure. Romanian companies performed generally below the EU average:

- A third of Romanian companies failed to disclose their polices related to climate change (33.3%) against a European average of 23.1%; and
- No organisation described how executive compensation is affected by their performance against ESG criteria, against a European average of 8.9%.

Policy outcomes

Beyond relevant policies the company put in place, reported outcomes enable investors to understand how companies are progressing against them and, ultimately, whether they are aligning their activities with these ambition statements. Romanian companies were able to perform above the European average regarding climate change in the following areas:

- Romanian companies were more likely to provide relevant data or KPIs for their outcomes when compared to Europe (60% vs 44.9%);
- They were also more likely to offer some form of description relating to their policy outcomes (60% vs 53.8%); and
- Less companies were able to disclose in a clear, detailed and logical manner the outcomes of their climate and biodiversity policies (20% and 0% for Romania vs 25.4% and 12.9% in Europe, for climate and biodiversity respectively).

KPIs

KPIs are a useful tool to assess the progress of a company against previously set policies. Romanian companies generally performed below the EU average.

- Romanian companies underperformed against the European average for disclosing of GHG emissions; 33.3% disclosed Scope 1 (EU 61.7%), 26.7% disclosed Scope 2 (EU 51.5%) and 6.7% disclosed Scope 3 (EU 25.7%); and
- No Romanian company disclosed its performance regarding deforestation, as opposed to 5.6% of the European average.

Risks and TCFD implementation

The environmental and climate-related risks which businesses face should play an important role in informing their business model, policies and KPIs. This is also a key emphasis of the TCFD recommendations. Overall Romania had a mixed performance when comparing against the EU average in each of the different recommendation areas.

When it comes to TCFD recommendations:

- **Governance:** 20% of companies indicated how sustainability is integrated into corporate governance arrangements compared to a European average of 35.3%;
- **Strategy:** 6.7% of Romanian companies provided adequate disclosure on strategic resilience using scenario analysis (EU average 6.6%);
- **Risk Management:** Only 6.8% of Romanian companies were able to disclose clear management approach for identified risks and impacts, compared to a European average of 17.8%; and
- **Metrics and Targets:** Generally a below average area of performance for Romanian companies when compared to the European average (see KPIs for previous analysis).

CDSB's key recommendations for Romanian policymakers and regulators

The following policy recommendations are taken from CDSB's overall policy briefing[4] and were formulated based on CDSB's own dataset. Of these, we have chosen the three recommendations we believe to be the most applicable to Romanian policymakers and regulators.

1. Explicitly embed the TCFD recommendations into the Directive, as non-binding guidelines are not driving uptake at the necessary pace and scale to support investor decision-making and improving disclosure of principal climate risks.

Whilst 68% of companies referenced or provided some disclosure aligned to TCFD in 2020 in their reports, adoption of the recommendations was found to be inconsistent and incomplete. The vast majority have still only partially adopted the recommended disclosures, with just 4% clearly defining risks over short, medium and long-term time horizons, and 18% providing clear disclosure on their resilience to different climate scenarios.

Given the TCFD recommendations were integrated into the Directive's 2019 Guidelines on reporting climate-related information, it could have been expected that TCFD disclosures would have seen greater improvement in 2020 reports. The continued challenges in the quality and completeness of disclosures however indicates that voluntary adoption of the TCFD by Europe's largest companies, through its inclusion in non-binding guidelines, is not achieving the levels of disclosure required to fully inform investor decision-making. It is therefore evident that the TCFD recommendations must be embedded into the revision of the Directive itself.

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[4] Climate Disclosure Standards Board (2020), Summary for policymakers: The state of EU environmental disclosure in 2020 [PDF] available at:
https://www.cdsb.net/sites/default/files/cdsb_summary_for_policymakers_the_state_of_eu_environmental_disclosure_in_2020.pdf

2. **Emphasise in the revision of the Directive the importance of ensuring that the different content elements provide a connected overall view on how companies ensure sustainable long-term value creation.**

Whilst disclosure of information under individual content categories of the Directive has shown some improvement, such as business models and KPIs, coherent and connectedness across environmental disclosures is critical to ensuring it is decision-useful for investors. Our 2020 review found that information across content categories was not always well linked. For example, 14% disclosed policy outcomes that did not clearly relate to their stated policies, and 36% did not indicate any explicit management actions being taken to address their principal risks.

To drive disclosure that provides a complete and consistent picture on the organisation's overall approach to sustainable long-term value creation, it is therefore key that the revision of the Directive places greater emphasis on ensuring companies' disclosure across content categories tells a clear overall story regarding its approach to environment, social and governance issues.

3. **Incentivise companies to do more to tackle environmental and climate issues, through ambitious policies and rigorous due diligence processes, by ensuring policy coherence between the NFRD review and the upcoming EU initiative on corporate governance.**

Whilst due diligence disclosures under the NFRD are expected to provide information on board and management level responsibilities of relevance from a corporate governance perspective, 30% of companies did not provide this information relating to environmental matters in their 2020 reports. Additionally, where governance information was provided, the level of detail and specificity it included on how environmental risks were managed, and in particular climate risk as requested under the TCFD recommendations, was often limited. The revision of the NFRD therefore presents a timely opportunity to ensure that companies disclose information on their internal processes and responsibilities over environmental issues, while the EU also takes legislative action to boost responsible business conduct through the upcoming initiative on sustainable corporate governance.

For questions relating to this, please contact our Policy and External Affairs Director, Michael Zimonyi
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