London Stock Exchange Group (LSEG) response to the European Commission consultation on non-financial reporting Guidelines

Executive Summary

London Stock Exchange Group (LSEG) welcomes the opportunity to respond to the European Commission ("the Commission") consultation on non-financial reporting Guidelines. As a stock exchange, we have a unique position, acting as a natural link between the issuers and investors. We promote fair and transparent market and sustainable investment. We believe that high quality non-financial reporting, including on ESG (environmental, social and governance-related) enhances corporate transparency, performance and ultimately facilitates the development of the EU Single market.

- We believe that the guidance on the reporting companies needs to be properly calibrated, taking into account the "emerging" status of standards in the area of ESG reporting.
- We consider that the guidance should strike a balance between encouraging supply of consistent, easily comparable and reliable data and the need to avoid overly prescriptive requirements, particularly where global consensus has not been yet reached.
- We encourage the Commission to take into account the ongoing international work streams in the area of non-financial reporting, particularly by the UN Sustainable Stock Exchange (UN SSE[1]) Group.
- The ESG data that are material for a company to report will vary depending on the sectors and locations in which such company operates. Therefore, outside of a few indicators that may be universally relevant, the reporting standards should avoid a one-size fits all approach, so that the costs don't outweigh the benefits.

[1] In 2013 LSEG became a member of the UN SSE. The initiative is aimed at exploring how exchanges can work together with investors, regulators, and companies to enhance corporate transparency, and ultimately performance, on ESG (environmental, social and corporate governance) issues and encourage responsible long-term approaches to investment. Following membership of the UN SSE, LSEG was invited to chair a working group alongside other exchanges, investors and issuers to develop "Model Guidance" on sustainability reporting. The aim of this group was to provide a framework and a basis for exchanges to develop their own guidance on (voluntary) best practice reporting for their issuers. The final guidance was launched in September 2015.

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I. General principles and key attributes of the non-financial information

Q1. What aspects of disclosure of non-financial information do you think that should be addressed by the GUIDELINES? Please, order in terms of importance (1 least important, 9 most important)	
Materiality/Relevance	9
Usefulness	3
Comparability	7
Avoiding undue administrative burden	5
Comprehensiveness	6
Fairness and balance	1
Understandability	2
Reliability	8
Other – Timely and regular	4
Many of the concepts listed above are of equal and high importance. In terms of “relevance”, it is worth noting that what is deemed relevant by the company may be different from the investor’s point of view and vice versa. In terms of “fairness”, we question what can be assessed as “unfair” data.	

Q2. Who should be considered in your opinion the main audience of the non-financial statement? Choose one.	
The shareholders	
The investment community in a broad sense	X
Users of information with an economic interest, such as suppliers, customers, employees, etc.	
All users of information (including consumers, local communities, NGOs, etc.)	
Other	

Q2.1 Could you please provide a brief explanation on your answer regarding who should be considered the main audience of the non-financial statement?
The investment chain is a complex set of actors that is not fully and adequately captured by the term “shareholders”. Such chain includes all those that may influence investment strategy, asset allocation, investment decision making and the interactions between investors and investee companies. Actors right through the investment chain need to access this ESG information and data since they are also the best equipped with the appropriate set of skills

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and knowledge to understand how ESG issues may affect future companies' evaluation and performances.

The Guidelines should be investor-focused and "demand-driven". It is worth noting that the reading and evaluation of reports will frequently take place among data and research intermediaries who provide the data through to their clients such as portfolio managers through research platforms.

Q3. ***In your opinion, what features make a piece of information relevant (or material) for the purposes of the non-financial statement? Please, order in terms of importance (1 least important, 7 most important)***	
Useful for the management/directors of the company	3
Relevant for shareholders or investors' decision-making	7
Relevant for stakeholders in general	1
Necessary to understand the impacts of the company's activity	2
Necessary to understand the company's development, performance and position	4
Necessary to understand how the company manages non-financial risk	6
Other – Necessary to understand the long term business/ investment perspective.	5

Q3.1 ***Could you please provide a brief explanation on your answer regarding the features which make a piece of information relevant (or material) for the purposes of the non-financial statement?***

The survey LSEG ran with investors on ESG issues demonstrated that investors are increasingly integrating ESG evaluations in their investment process. Therefore, we believe that in trying to understand the company's development, performance and competitive position, investors will review the non-financial statement alongside the financial reports.

Further, we believe that it is necessary to acknowledge and understand the so called "non-financial" risks, as it is directly related to and can turn into financial risks, therefore impacting the profitability and price performance of the shares.

II. Content of the non-binding Guidelines

Q4. Do you think that the GUIDELINES will be more useful for companies and users if they set out general principles and key ideas or if they put forward solutions in a detailed manner, including on specific sectoral issues? **Please, indicate on a scale from 1 to 5 (1 geared towards general principles, 5 high level of detail/prescription)**	3

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***Q5**. Please, provide a brief description of how you think that the following matters should be treated in the GUIDELINES, including as appropriate how they should be defined and described:*	
a. Business model:	The companies' business models should include clarifications on how the model and plans inter-relate with a company's wider operating environment, including global trends and risks such as climate change, water scarcity or cyber security. In particular, the Guidelines should ask companies to explain the relevance of specific ESG factors and their impact on the firm's long-term profitability, risk management and competitive position.
b. Policies:	Companies should be encouraged to publish all their relevant policies on their website and the reports should reference them. We believe that updates on a continuous basis would reflect better the reality and improve the overall quality of the information available. For certain of their policies, the companies may need to involve external stakeholders - both when designing the policies and when getting feedback on their actual implementation. The Guidelines could suggest this.
c. Due diligence process:	We consider due diligence on reported information and data very important. It is critical that the data is reliable and robust, also by means of an effective internal due diligence process, as investors will be using these to design their investment models and make decisions.
d. Business relationships:	We believe that the Guidelines should take business relationships into account, in the cases where such information is relevant for investors. For some industries this will include relationships with suppliers or customers. For example in industries such as in fast moving consumer goods labour standards in supplier companies can have reputational impacts, or in food producers the nutritional and health impact on consumers would be a material issue.
e. Key performance indicators –KPIs:	The survey LSEG ran with investors on ESG issues demonstrated the need to identify a minimum set of key indicators that would support

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	investors' evaluation of companies. Therefore, we believe that there is a case to identify quantitative metrics for companies to report non-financial information in order to allow investors to better measure the progresses made by these companies on material ESG area. These quantitative metrics should enhance the comparability across enterprises and industries. We believe that this could result in hard measurable and verifiable data. At London Stock Exchange Group, our index and data analytics company FTSE Russell has been working, since 2001, on developing ESG measures and metrics. FTSE Russell has developed an ESG model that applies certain ESG metrics depending on the industrial sectors and countries in which a company operates. For example, water use metrics become relevant if a company operates in industrial sectors where water usage is higher and in countries where there are greater water scarcity challenges. FTSE Russell has aimed to draw from the most accepted international standards and frameworks in each ESG area. We therefore believe that the Guidelines should be cautious in providing many "one-size fits all" specific KPIs or parameters, since it would be very difficult to set *a priori* a reporting model that could fit all sectoral issues and companies. Instead, in order to help companies under the scope of the Directive to choose KPIs and report non-financial and diversity information, the Guidelines should reference the relevant international standards and Guidelines (*e.g.* the GHG Protocol, the Global Reporting Initiative, ISO26000, OECD Guidelines for multinational enterprises *etc*.) We also recommend that the Guidelines support the companies in self identifying the most relevant KPIs to their specific sector and corporate strategy. This approach would allow the development of best practices among different industries. This can also allow a more detailed and specific implementation, at a later stage, once clearer industry specific standards are agreed. This has happened in the past with corporate governance standards.
f. Outcome of policies:	There should be some reporting of how key policies (i.e. those relating to the most material/pertinent ESG issues) are implemented and how well they related to performance. The guidelines could encourage an open dialogue between companies and investors, which would provide companies with a structured feedback, encouraging further standardization of KPIs and measurability of results.
g. Principal risks:	The Guidelines should provide a broad distinction and encourage companies to distinguish in their management reports between

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	environmental, social, governance and diversity related risks. However, we believe that the Guidelines should not provide a pre-determined list of risks since they may vary greatly depending on each company's specific industry issues.
h. Impact of the activity:	The Guidelines should precise that the ESG policies and information should be published alongside a clear explanation that will help investors understand and assess the activity of the company.
i. Adverse impacts:	We believe that the Guidelines should clarify that the integrated financial-non financial reports shall not only address the positive outcomes of ESG policies but also their challenges. The Guidelines should encourage companies to transparently report on all significant issues, rather than focusing on the areas where it has performed well. Therefore, we believe that the Guidelines should underline that ESG policy disclosure shall not be seen as a form of "marketing tool" but as a useful tool for assessing and evaluating companies' prospects and financial performances.
j. Information omitted in exceptional cases where disclosure would be seriously prejudicial:	No comments.

Q6. How do you think that the GUIDELINES should approach the disclosure of key performance indicators (KPIs)? ***Choose best and second best option***	
The GUIDELINES should highlight key principles on how to disclose relevant KPIs and complementariness with narrative and/or financial information as applicable	1
The GUIDELINES should make reference to KPIs proposed by other frameworks where addressing concrete matters or issues	2
The GUIDELINES should include a comprehensive list of KPIs, general and sectoral	
The GUIDELINES should provide flexibility for companies to exercise judgement in deciding what KPIs should be included in their disclosures	
Other	

Q6.1 Could you please provide a brief explanation on your answer regarding how you think the GUIDELINES should approach the disclosure of key performance indicators (KPIs)?	

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We believe that the Guidelines should aim at promoting a cultural change among businesses. We suggest that KPIs contain two components: (a) the definition of indicators and (b) their application to particular companies. We believe that the (a) definitions should be precise and unified based on existing international standards and frameworks and of use to investors. They should evolve, become ever tighter and more sector specific over time. However, the (b) application should be proportionate, allow flexibility and serve as a tool (set of methodologies) when companies design their ESG policies and prepare their integrated reports. This is to avoid an undue burden, particularly on smaller players – and avoid any "tick-the-box" approach to ESG issues. Such KPIs need to help drive harmonisation rather than add to a myriad of similar, but slightly differing, reporting requirements.	

<u>Q7</u>. Do you think that the GUIDELINES should include guidance on specific sectoral issues such as responsible supply chain management of conflict minerals? Please, indicate on a scale from 1 to 5 (1 geared towards general principles, 5 high level of detail/prescription)	3

<u>Q7.1</u> Could you please provide a brief explanation on your answer regarding whether the GUIDELINES should include guidance on specific sectoral issues such as responsible supply chain management of conflict minerals?	
For certain companies these will be among their most pertinent/material ESG risks, while for others it will not be very relevant. This is why a one-size fits all approach to reporting is not satisfactory. The Guidelines should be cautious in addressing sectoral issues because there is a very wide spectrum of different industries that will be under the scope of the Directive. Some sectors will have well established global KPI standards whilst others will be at a more embryonic stage. Highly detailed prescriptions related to sectoral-issue' might have negative side effects as there are no globally accepted KPIs yet. Instead, a flexible reporting tool could evolve over time and be adaptable enough to include new indicators and parameters. Also, it would leave room for a company to refer to existing ESG international Guidelines relevant for its industry or sector.	

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III. Interaction with other frameworks and other aspects

<u>Q8</u>. How do you think that the GUIDELINES should relate to existing national, international or other EU-based frameworks (such as UN Global Compact, the UN Guiding Principles on Business and Human Rights, OECD Guidelines for multinational enterprises, the ILO Tripartite Declaration of principles concerning multinational enterprises and social policy, EMAS, etc.)? Please, order in line with your views (1 least in line, 6 most in line)	
The GUIDELINES should include detailed solutions and be an exhaustive document in a way that could make unnecessary for companies the use of other Guidelines	2
The GUIDELINES should be complementary to other frameworks	5
The GUIDELINES should make reference to other frameworks where addressing concrete matters or specific issues	6
The GUIDELINES should get general inspiration from other frameworks	3
The GUIDELINES should explain how content produced in the context of other frameworks could be used in the non-financial statement	4
Other	

<u>Q8.1</u> Could you please provide a brief explanation on your answer regarding how you think the GUIDELINES should relate to existing national, international or other EU-based frameworks?

The Guidelines should reference the national, international or other EU-based frameworks, complement them and provide guidance to how to assess them. Where such other frameworks are referenced, the Guidelines should avoid "reinventing the wheel". However frameworks which are purely national should be considered only where there is a strong likelihood that they will become the basis for the most international accepted KPI, or alternatively, in markets that are at a different stage of development (materially different approach to ESG matters).

The reference to national, international or other EU-based frameworks needs to be led by the investment industry to ensure that investors are getting the data they need. Hence, in the long term, a clear and comprehensive framework of KPIs reflecting global standards is required. The development of such framework will emerge from increased global consensus between investors and companies.

We believe that a good example is the UN SSE Model Guidance on sustainability reporting[2] which provides a good basis for this.

[2] In 2013 LSEG became a member of the UN SSE. The initiative is aimed at exploring how exchanges can work together with investors, regulators, and companies to enhance corporate transparency, and ultimately performance, on ESG (environmental, social and corporate governance) issues and encourage responsible long-term approaches to investment.

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<u>Q9</u>. Do you think that when preparing the GUIDELINES only the companies included in the scope of the DIRECTIVE should be considered, or that the interests, characteristics and/or requirements of other companies that prepare management reports should be taken into account as well? **Please, check the box of the alternative that you consider most appropriate**	
Specific to the requirements of the companies under scope of the DIRECTIVE	
Consider all large companies	
Consider all companies	
Focus on the requirements of the companies under the scope of the DIRECTIVE, but also propose best practice for other companies that prepare management reports	X

<u>Q9.1</u> Accordingly, do you think that the content of the Guidelines should be different according to the targeted companies? Could you please provide a brief explanation?	If the Guidelines are designed to set out general key principles and criteria applicable to each company, they do not need to accommodate the proportionality aspect (criteria to differ according to the size or the sector of the company). On the other hand, if the Guidelines become more prescriptive, the proportionality element needs to be taken into account. Only the companies in scope of the Directive shall comply, but the Guidelines should provide key principles and criteria that may be used and followed voluntarily by other companies, creating a level playing field between listed and unlisted companies. The key principles and criteria may also be used by those small and medium companies on a voluntary basis. We believe that the Guidelines should adopt a progressive approach, as in the future there may be an increasing demand for mandatory ESG reporting also for SMEs. While keeping high standards, the Guidelines should avoid creating unnecessary barriers to foreign companies that may be using different reporting practices and may be in an early stage adopting higher standards.

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Q10.* Does your company disclose annually relevant non-financial information?** ***Y / N / Don't know	*Y*

IV. Disclosures related to board diversity policy

Q11*. Should the GUIDELINES provide more clarity on what companies should disclose as regards their board diversity?** ***Y / N / Don't know	*Y*

***Q11.1* Could you please provide a brief explanation on your answer regarding whether the GUIDELINES should provide more clarity on what companies should disclose as regards their board diversity policy?**	Currently there are a number of different standards and codes in place across markets. We believe that this is an opportunity to have a consistent approach and that the Guidelines should provide specific indicators, benefiting from and building upon existing national legal frameworks around board diversity. We suggest that the guidelines provide clarity for companies to report on: gender diversity on the company board and among company executives, which we define by Executive Committee members plus direct reports or Management Board; and further reporting on board diversity policy and executive diversity policy (if any), alternatively on plans and progress for implementing these policies. We believe this to be consistent with the European Commission overall thinking and support these initiatives.

About London Stock Exchange Group

London Stock Exchange Group (LSE.L) ("the Group") is a diversified international market infrastructure and capital markets business sitting at the heart of the world's financial community. The Group can trace its history back to 1698.

The Group operates a broad range of international equity, bond and derivatives markets, including London Stock Exchange; Borsa Italiana; MTS, Europe's leading fixed income market; and Turquoise, pan-European equities MTF. It is also home to one of the world's leading growth markets for SMEs, AIM. Through its platforms, the Group offers international business and investors unrivalled access to Europe's capital markets.

Post trade and risk management services are a significant part of the Group's business operations. In addition to majority ownership of multi-asset global CCP operator, LCH.Clearnet Group, LSEG operates CC&G, the Italian clearinghouse; Monte Titoli, the T2S-ready European settlement business; and globeSettle, the Group's newly established CSD based in Luxembourg.

The Group is a global leader in indexing and analytic solutions. FTSE Russell offers thousands of indexes that measure and benchmark markets around the world. The Group also provides customers with an extensive range of real time and reference data products, including SEDOL, UnaVista, and RNS.

London Stock Exchange Group is a leading developer of high performance trading platforms and capital markets software for customers around the world.

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