# "Sustainability: the importance of transparency" Spanish Issuers' Conference

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Thank you, Javier.

It is a pleasure to participate in a **Spanish Issuers' conference**. This is the first time I have been here, but the CNMV has always been present, in one way or another, and I am very pleased to continue this practice which is, after all, a reflection of the ongoing and constructive dialogue we have always maintained.

Today you have discussed two relevant regulatory developments: the Preliminary Draft Law to ensure the protection of whistleblowers and the proposed Directive on Due Diligence of governance bodies on sustainability.

Both initiatives, but especially the second one, are an example of how the organisational requirements and the information and reporting obligations faced by companies are progressively increasing, especially in the area of sustainability, and will continue to do so in the future.

This is understandable, given the European agenda to transform the economic model and finance a sustainable economy. But it is also true that the transition is not without its difficulties. Hence the importance that the regulation and the different initiatives that we are adopting also incorporate the costs and take into account the timescales that entities need to adapt and adjust their current structures, resources and procedures to the new requirements that these scenarios demand.

Please do not get me wrong. I do not want this to sound unsustainable. Nothing could be further from the truth. The fight against climate change is one of the main challenges we face as a society: we are facing a climate emergency and it is urgent to act in a determined and coordinated manner.

The question is how we do it, what steps we take and at what pace, so that we move forward decisively and achieve an orderly and just transition. It must take into account social and employment aspects, it must also address current inequalities, and it must make it easier for us to move together towards a low-carbon economy.

In my opinion, the answer is not obvious, but I think we are starting from a solid base.

We know that in order to move towards a zero net emissions economy by 2050 we need the impetus of public intervention, of regulation, because in these cases, self-regulation by the market is not enough. We are (to use economists' jargon) facing one of the biggest market failures and therefore need policies to internalise costs in asset prices and protect the environment as a public good.

We also know that financing the transition will require large volumes of finance, both public and private, and for that we have to rely on investors and the financial markets in general (some 250 trillion euros cumulatively over the next 30 years[1]).

And finally, we have an increasingly aware society and a growing demand for sustainable companies that respect the environment and their surroundings, that contribute to the improvement of society and the achievement of sustainable development objectives.

All of the above has prompted many legislative initiatives in recent years, with which you are well acquainted.

- The Regulation on the taxonomy for the classification of environmentally sustainable activities[2], which has yet to develop the economic activities linked to four of the six environmental objectives it sets out.
- The Sustainable Finance Disclosure Regulation (SFDR), which obliges them to communicate how sustainability risks are integrated into their investment strategies and increases transparency requirements in the provision of investment services. It refers to socially or environmentally sustainable objectives, although the taxonomy of which activities are to be considered as socially sustainable remains to be developed.
- The proposed Corporate Sustainability Reporting Directive (CSRD), which will regulate the content of companies' "sustainability reporting".
- The proposal on Due Diligence, which you have discussed today, to promote sustainable and responsible business behaviour throughout the supply chain.
- Or the proposal for a regulation on an EU green bond standard, among other initiatives.

All of them aim at solving incentive problems. This means integrating ESG risks (and opportunities) and promoting a long-term view, as well as addressing the issues of consistency, availability and reliability of information that investors need to be able to consider sustainability factors when making investment decisions. Especially in a context of proliferating code and standards initiatives that have emerged over the years.

So, what are the difficulties? I would highlight two such problems:

[1] See "*The Net Zero transition: what it would cost, what it could bring*", McKinsey Global Institute, February 2022.

[2] Through climate change mitigation and adaptation, circular economy, water and marine resources, pollution prevention and control and biodiversity.

On the one hand, we are faced with an avalanche of regulation, as we have just seen with the various initiatives underway, which may impose non-negligible costs for companies to comply with, especially for smaller ones.

And on the other hand, in some areas there may be a lack of temporal consistency in regulation: by establishing transparency requirements when we do not yet have, for example, a homogeneous framework of standards on which to report, or regulatory developments that detail the technical criteria for certain environmental objectives. This can lead to inconsistencies in the application of the rules, difficulties of interpretation and lack of homogeneity between jurisdictions.

Let me just say a word about the proposal for a **Directive on Corporate Sustainability Due Diligence** that you have discussed today. This directive, when adopted, will go a step further. It involves moving from the realm of principles, recommendations or guidelines to establishing legally binding obligations and requirements for companies in the field of human rights or the environment. This is not without some complexity.

There is no doubt that it can be a challenge for many companies to obtain all the information they need to control the risks of the various players in their entire value chain, such as clients and suppliers, to the extent that they have stable relationships with them. The proportionality criterion also needs to be fine-tuned. And it will probably require a sufficient transitional period to allow companies to adapt their internal procedures to the new requirements. This can be complex and costly for some companies.

But it is also true that there are precedents in other jurisdictions, such as France and the Netherlands, and that, at the end of the day, it is about highlighting the importance of companies of a certain size being aware of the potential risks of causing significant negative human rights or environmental impacts.

It is therefore essential that companies prepare themselves and have adequate internal policies and controls in place to be able to identify, monitor and manage climate risks and ensure respect for human rights in the value chain.

The challenges I have mentioned are common in regulating new policy areas and we supervisors are well aware of them. In this context, we can adjust priorities and be flexible in certain areas, and we have communicated this publicly, but as long as this does not undermine the ultimate objective or reduce confidence in the information and data being published.

## Transparency and sustainability reporting

In view of this forthcoming regulatory framework, today I would like to emphasise the importance of transparency as an essential tool for promoting the development of a sustainable economy.

This is an area, sustainability reporting, where, in my opinion, companies have come a long way in recent years. As you know, at the CNMV we annually review the sustainability reports of listed companies[3].

And this year, we are also monitoring in particular the new reporting requirements for Ibex companies on environmentally sustainable activities[4]. That is, what percentage of their economic activity - based on annual total revenue, capital expenditure (CapEx) or operational expenditures (OpEx) - is eligible under the taxonomy to mitigate and adapt to climate change.

What do the data tell us? What assessment can we make?

For the Ibex35 companies, we observe the following data:

- Firstly, companies with electricity generation activities show higher ratios of activities eligible for climate change mitigation and adaptation targets than other sectors. This is understandable, as they are largely increasing the weight of their activities in the areas of generation and marketing of renewable energies.
- Secondly, we also note that four Ibex entities have anticipated the regulation and voluntarily provided not only the percentage of eligible activities but also the ratios related to the degree of alignment, which are more demanding requirements and therefore a subset of the former.
- Finally, we note that credit institutions show a ratio of total assets to exposures to eligible economic activities ranging from 41% to 55% (Green Asset Ratio (GAR)).

These are preliminary data, and we lack comparisons, but I would venture to say that they are a good starting point and will tend to improve progressively. In any case, they are valuable information for investors, as they allow them to quantify the extent to which companies' activities contribute to climate change mitigation and adaptation, and their evolution over time will also be an important indicator.

On the other hand, as you know, we at the CNMV review the **sustainability information of listed companies** and publish a report on the annual review[5] with conclusions and recommendations. This year is the first time we are publishing it separately.

Overall, year on year we see an improvement in the reporting and quality of company information. But, as a good supervisor, there are always areas for

[3] In Spain, all companies with more than 250 employees, which also meet other requirements, are obliged, from 2021, to publish information on sustainability and this must be verified by a third party.

[4] Since the beginning of this year, and in relation to the 2021 financial year, companies with an obligation to prepare an NFS under EU law (public interest companies with more than 500 employees) have to detail how and to what extent their activities are eligible and can be associated with environmentally sustainable activities. Commission Delegated Regulation (EU) 2021/2178, of 6 July 2021, specifies the content and presentation of the information to be disclosed in accordance with Article 8 of the Taxonomy Regulation in respect of environmentally sustainable economic activities, and the specification of the methodology for complying with the disclosure obligation.

[5] https://www.cnmv.es/DocPortal/Publicaciones/Informes/EINF_2020.pdf

improvement. From the review of the 2020 financial year, I would like to draw your attention to the following three areas:

- On greenhouse gas emissions, there is room for improvement in the description of the methodology, the sources used in their calculation and the scope. A further breakdown by areas of activity and geographical areas is also needed. Many companies report greenhouse gas emissions, but they do so in a "limited" way, without integrating the emissions of all parties in the value chain[6].
- Regarding the pay gap, companies should improve their reporting by specifying the type of remuneration considered in the calculation, the methodology used, and by further segmenting the information to allow for a more reasonable comparison. If we cannot compare, data is of little use.
- Finally, the breakdowns concerning the entities' complaints channel should also be improved, an aspect that is of particular relevance in today's event. The CNMV recommends that more information be provided on the entire management procedure, as well as on the number of complaints received in each area.

I was saying that the effort on the part of the entities to improve reporting is remarkable, but it is also true that they still do not have a homogeneous reporting framework, which makes their task more difficult.

This is where the proposed **Corporate Sustainability Reporting Directive or CSRD**, which I mentioned earlier, comes into play and which will regulate sustainability reporting, broadening the breakdown and scope of companies subject to its scope.

Negotiations in Europe are well advanced. We expect it to apply for tax years from 2024 onwards, following the agreement to delay its entry into force by one year. The proposal itself includes a mandate to EFRAG to develop sustainability standards at European level. In fact, at the end of last week, EFRAG published its first proposal for standards for public consultation, which I would encourage you to participate in. The CNMV, through its participation in ESMA, will actively contribute to this consultation.

But as we live in a globalised world, it is very important that these standards are compatible with the international standards being developed by the ISSB, as the international standard setter for sustainability. To this end, the ISSB has designed a building block model, with a common global baseline as its core, from which other building blocks could be added, made up of more advanced standards such as those of the EU, which include the concept of dual materiality.

## Final reflections

Most of the initiatives I have detailed are mainly concerned with transparency, i.e., the provision of consistent and quality information to investors and citizens. For me, this is one of the main areas where we need to concentrate our efforts.

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6 Including only the business travel of its employees via external means and excluding emissions from the value chain, such as from the manufacture of purchased materials or the use of goods and services sold by the company.

Without information, without data, market participants cannot identify or quantify risks, nor take them into consideration for the purposes of price formation or investment decisions.

Transparency is one of the most important tools we have to discourage inappropriate behaviour and to encourage sustainable investment. And it answers precisely one of the questions I raised at the beginning, on how to address the challenge of sustainability.

The discipline of transparency also operates in the area of **corporate governance**, through the obligation to report on the extent to which the recommendations of the code of good governance are being followed, to ensure that ESG factors are integrated into day-to-day management and to promote a long-term vision.

In Spain, in 2020 we updated the Code of Good Governance so that, among other measures, elements related to sustainability would be strengthened.

We are also working on a **code of investor and manager engagement**, generally referred to as stewardship codes, and expect to launch the consultation in the coming months, before the summer. This code aims to encourage long-term orientation of investors and managers, which will also help to promote this approach in the companies in which they invest.

In short, transparency and information are a very powerful tool that, when properly regulated, can ensure the proper functioning of the markets. In situations where transparency is not sufficient, other more restrictive or limiting measures are justified. Let us focus on boosting transparency and providing companies, investors and citizens in general with the information they need to adapt their consumption habits and investment decisions towards a sustainable economy that respects human rights.