

New rules on European corporate sustainability reporting

On the 19 of November 2022, the European Parliament has on 10 November 2022 adopted the Corporate Sustainability Reporting Directive (CSRD) proposed by the European Commission (EC) in April 2021. The proposal amends the 2014 non-financial reporting directive by introducing more detailed reporting requirements while capturing additional companies that will be required to report on sustainability issues such as environmental rights, social rights, human rights, and governance factors.

The proposal aims to fill the gaps in the existing rules on non-financial information. Sustainability reporting could attract additional investments and funding to facilitate the transition to a sustainable economy as described in the Green Deal. For example, companies would need to provide better information on the sustainability risks to which they are exposed and on their impact on people and the environment.

The CSRD introduces a certification requirement for sustainability reporting as well as improved accessibility of information mainly by requiring its publication in a dedicated section of company management reports. The European Financial Reporting Advisory Group (EFRAG) will be responsible for drafting the European reporting standards on which the reporting requirements will be based on. Thereafter, the European Commission is expected to adopt the corresponding Delegated Acts that will contain these reporting standards.

The text of the CSRD adopted by the EU Parliament can be found [here](#).

Background

EU law requires certain large companies to disclose information on the way they operate and manage social and environmental challenges. This helps investors, organisations, and other stakeholders to evaluate the non-financial performance of large companies and encourages these companies to develop a more responsible business approach.

The Non-Financial Reporting Directive (NFRD)¹ lays down the rules on the disclosure of non-financial and diverse information by certain large companies. Under the NFRD large public-interest companies with more than 500 employees must publish information related to environmental and social matters, anti-corruption and bribery information and diversity on company boards.

The European Commission has published respectively 2017 and 2019, guidelines to help companies disclose environmental and social information and guidelines on reporting climate-related information.

¹ Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups

Proposal for a Corporate Sustainability Reporting Directive (CSRD)

On 21 April 2021, the European Commission adopted a proposal for a Corporate Sustainability Reporting Directive (CSRD)² which would amend the existing reporting requirements of the NFRD. The proposal:

- extends the scope to all large companies and all companies listed on regulated markets (except listed micro-enterprises)
- requires the audit (assurance) of reported information
- introduces more detailed reporting requirements, and a requirement to report according to mandatory EU sustainability reporting standards
- requires companies to digitally 'tag' the reported information, so it is machine-readable and feeds into the European single access point envisaged in the capital markets union action plan³

Expansion of the scope

Mandatory taxonomy reporting applies to companies in scope with NFRD, from now on CSRD, and voluntarily by any entity. With the CSRD regulation, there is an expansion of the companies in scope. From roughly 11,000 companies in scope to 49,000. This list includes:

- All large companies and all companies listed on regulated markets. These companies are also responsible for assessing the information at the level of their subsidiaries.
- Non-EU companies: provide a sustainability report that applies to all companies generating a net turnover of €150 million in the EU and which have at least one subsidiary or branch in the EU (subsidiaries and branches with a minimum 40 million net turnover).
- Listed SMEs included with opt-out until 2028 and companies making use of it only have to provide a brief declaration about why they don't comply.

On the inclusion of extra-EU companies. These will have to only report on EU-based representatives (subsidiaries and branches with a minimum of 40 million net turnovers) and report at the EU level or individual level based on the EU standards or, in the future, possibly at the group level on the basis of equivalent international standards (equivalence depending on Commission decision).

² Sustainable finance package ([europa.eu](#))

³ Capital markets union 2020 action plan (europa.eu)

Audit

The NFRD regulation did not require a statutory audit or audit firm to assess the inclusion of the non-financial statement in a report. The review of the NFRD identified this as a problem with the effectiveness of the directive. The review also identified problems with the limited reliability of sustainability information.

The CSRD introduces the requirement for reporting to be certified by an accredited independent auditor or certifier. The independent auditor or certifier must ensure that the sustainability information complies with the certification standards that have been adopted by the EU. The reporting of non-European companies should also be certified, either by a European auditor or by one established in a third country.

The audit will be a requirement for limited assurance at the beginning of the application of the CSRD. The aim is to move towards reasonable assurance. The proposal would allow Member States to open up the market for sustainability assurance services to independent assurance services providers. Member states will be obligated to set out requirements ensuring the quality of the assurance carried out by independent assurance services providers and ensure consistent outcomes in the assurance of sustainability reporting.

Member states will set out requirements for examination, quality assurance systems, and other requirements for auditors. Member states will be given the possibility to apply national assurance standards and procedures as long as the Commission has not adopted an assurance standard covering the same subject matter. The Commission is planning to adopt assurance standards for limited assurance before the 1st of October 2026.

Sustainability reporting standards

The Commission's proposal for a Corporate Sustainability Reporting Directive (CSRD) envisages the adoption of EU sustainability reporting standards. The draft standards would be developed by the European Financial Reporting Advisory Group (EFRAG). The first set of standards would be adopted by October 2022⁴.

The sustainability reporting standards will consider:

- a. specify the information that undertakings are to disclose about environmental factors, including information about:
 - i. climate change mitigation
 - ii. climate change adaptation
 - iii. water and marine resources
 - iv. resource use and circular economy

⁴ [Reports on development of EU sustainability reporting standards \(europa.eu\)](https://european-council.europa.eu/media/en/press-summaries/Pages/12122.aspx)

- v. pollution
 - vi. biodiversity and ecosystems
- b. specify the information that undertakings are to disclose about social factors, including information about:
- i. equal opportunities for all, including gender equality and equal pay for equal work, training and skills development, and employment and inclusion of people with disabilities
 - ii. working conditions, including secure and adaptable employment, wages, social dialogue, collective bargaining and the involvement of workers, work-life balance, and a healthy, safe work environment
 - iii. respect for human rights, fundamental freedoms, and democratic principles
- c. specify the information that undertakings are to disclose about governance factors, including information about:
- i. the role of the undertaking's administrative, management and supervisory bodies, including sustainability matters, and their composition
 - ii. business ethics and corporate culture, including anti-corruption and anti-bribery
 - iii. political engagements of the undertaking, including its lobbying activities
 - iv. the management and quality of relationships with business partners, including payment practices
 - v. the undertaking's internal control and risk management systems, including the undertaking's reporting process

CROSS-CUTTING STANDARDS	ESRS 1 General Principles		ESRS 2 General, strategy, governance and materiality assessment disclosure requirements		
ENVIRONMENT	ESRS E1 Climate Change	ESRS E2 Pollution	ESRS E3 Water and Marine resources	ESRS E4 Biodiversity and ecosystems	ESRS E5 Resource use and circular economy
SOCIAL	ESRS S1 Own workforce	ESRS S2 Workers in the value chain	ESRS S3 Affected communities	ESRS S4 Consumers and end-users	
GOVERNANCE	ESRS G1 Governance, risk management and internal controls		ESRS G2 Business Conduct		

Table 1 Reporting elements and standards

Reporting requirement

Undertakings within the scope of the CSRD are required to include in their management report:

1. Information on environmental, social and governance matters
2. Information necessary to understand:
 - The undertaking's impacts on sustainability matters
 - How sustainability matters affect the undertaking's development, performance, and position

The CSRD proposal builds on the EU Accounting Directive, which requires undertakings to report both on the impacts of the activities of the undertaking on people and the environment, and on how various sustainability matters affect the undertaking. That is referred to as the double-materiality perspective. Consequently, companies will have to disclose their adverse impact or performance on a wide range of environmental and social factors and the extent to which their activities and operations qualify as environmentally sustainable according to the EU Taxonomy.

The information should be disclosed in a clearly identifiable dedicated section of the management report.

Example of information to be disclosed⁵

Large undertakings and, as of 1 January 2026, small and medium-sized undertakings shall include in the management report information necessary to understand the undertaking's impacts on sustainability matters, and information necessary to understand how sustainability matters affect the undertaking's development, performance, and position.

The information shall contain in particular:

- a. a brief description of the undertaking's business model and strategy, including:
 - i. the resilience of the undertaking's business model and strategy to risks related to sustainability matters.
 - ii. the opportunities for the undertaking related to sustainability matters.
 - iii. the plans of the undertaking 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.
 - iv. how the undertaking's business model and strategy take account of the interests of the undertaking's stakeholders and of the impacts of the undertaking on sustainability matters.
 - v. how the undertaking's strategy has been implemented in sustainability matters.
- b. a description of the targets related to sustainability matters set by the undertaking and of the progress, the undertaking has made towards achieving those targets.
- c. a description of the role of the administrative, management and supervisory bodies in sustainability matters.

⁵ According to Article 19a page 42

- d. a description of the undertaking's policies about sustainability matters.
- e. a description of:
 - i. the due diligence process implemented about sustainability matters.
 - ii. the principal actual or potential adverse impacts connected with the undertaking's value chain, including its operations, its products and services, its business relationships and its supply chain.
 - iii. any actions taken, and the result of such actions, to prevent, mitigate or remediate actual or potential adverse impacts.
- f. a description of the principal risks to the undertaking related to sustainability matters, including the undertaking's principal dependencies on such matters, and how the undertaking manages those risks.
- g. indicators relevant to the disclosures listed above.

Challenges

The major challenge of the CSRD, along with specific and demanding disclosure, is the timing. To be able to be fully prepared for 2024 is important for companies to start working now.

Suggested actions:

- Identify if the company is included in the scope and by when
- Focus on what you need to prepare
- Perform a complete diagnosis of new qualitative and quantitative information to be produced and disclosed
- Monitor EFRAG developments for example sector-specific standards

Timing and calendar

How are the sustainability obligation evolving during the coming years?

The application of the CSRD would take place in three stages:

- 1 January 2024 for companies already subject to the non-financial reporting directive (reporting in 2025 for the financial year 2024).
- 1 January 2025 for large companies that are not presently subject to the non-financial reporting directive (reporting in 2026 for the financial year 2025).
- 1 January 2026 for listed SMEs, small and non-complex credit institutions and captive insurance undertakings (reporting in 2027 for the financial year 2026).

An extensive review by 2028 and every three years thereafter, with European Commission to put forward appropriate legislative proposals. The assessment is to include, among other aspects:

- achievement of the CSRD goals and convergence of reporting practices between member states
- number of SMEs using voluntary reporting

- extension of the scope, regarding SMEs and third-country companies
- accessibility
- whether and how to ensure accessibility for people with disabilities to sustainability reports
- sustainability assurance

Next steps

By November 2022, EFRAG is expected to deliver the first set of standards to the European Commission as its technical advice. The Commission will consider the EFRAG's technical advice, consult with other entities (as determined in the text of the CSRD) and adopt a Delegated Act covering such standards. The objective of the Commission is to adopt the Delegated Act by June 2023 – entry into force is expected as of 2024. The adoption of the second set of standards including SMEs and sector-specific standards is expected on 30 June 2024.

The final text of the CSRD has also set timelines for when the Commission should adopt further delegated acts on reporting standards.

By the 30th of June 2023, the Commission should adopt delegated acts specifying the information that undertakings will be required to report.

By the 30th of June 2024, the Commission should adopt delegated acts specifying:

- complementary information that undertakings shall report.
- information that undertakings shall report that is specific to the sector in which they operate.

Useful links:

Alexander Bassen. "A first Draft to discuss – What can we expect from the new European Reporting Rules?" Research Group Sustainable Finance, University of Hamburg

Commission proposal for a directive on corporate sustainability reporting (21 April 2021) <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52021PC0189&from=FR>

Corporate Sustainability Reporting Directive [Corporate Sustainability Reporting Directive \(pwc.be\)](#)

Directive of the European Parliament and the Council as regards corporate sustainability reporting (CSRD) <https://www.consilium.europa.eu/media/57644/st10835-xx22.pdf>

Draft European Sustainability Reporting Standards [Public consultation on the first set of Draft ESRS - EFRAG](#)

General approach – proposal for a directive on corporate sustainability reporting <https://data.consilium.europa.eu/doc/document/ST-6292-2022-INIT/en/pdf>