Policy Brief: The Corporate Sustainability Reporting Directive

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On 5 January 2023 the Corporate Sustainability Reporting Directive (CSRD) entered into force. This means that some large agencies (i.e. holding groups) will soon be required to publish detailed information on sustainability matters.
The purpose of the CSRD is to revise and strengthen the existing requirements of the Non-Financial Reporting Directive (NFRD), to ensure that companies report reliable and comparable sustainability information that investors and other stakeholders need.
The aim of the legislator is to increase a company's accountability, prevent divergent sustainability standards, and ease the transition to a sustainable economy.

I. The Corporate Sustainability Reporting Directive - FAQ

1. What companies have to apply the new rules?

- all listed companies on the EU regulated market – (listed companies are those which have shares listed on an exchange at the end of the year)
- all large companies exceeding two of the three following criteria (as per the Accounting Directive 2013/34/EU):
  - 250 employees during the financial year
  - balance sheet total EUR 20 million
  - net turnover EUR 40 million

- non-EU companies generating a net turnover of more than EUR 150 million and having a subsidiary in the EU that follow the criteria applicable to EU companies (i.e., being listed on the European market except micro or being within the large company threshold) or a branch in the EU generating more than EUR 40 million net turnover

2. What if the company is a subsidiary of a large group?

A subsidiary is exempted from the CSRD obligations if the parent undertaking produces a consolidated sustainability report that conforms with the CSRD.
Such exempted subsidiaries must include in their management report:

- the name and registered office of the parent undertaking that is reporting sustainability information at group level
- the web links to the consolidated management report
- a reference of this exemption in their own management report

3. When will those rules start applying?

- as from 1 January 2024 (first reports in 2025) for companies that are already within the scope of the Non-Financial Reporting Directive 2014/95/EU
- as from 1 January 2025 (first reports in 2026) for other large companies
- as from 1 January 2026 (first reports in 2027) for listed SMEs[1]
- as from 1 January 2028 (first reports in 2029) for non-EU companies with branches/subsidiaries

4. What is the scope of reporting requirements?

A company under the scope must report information necessary to understand the company's impacts on sustainability matters and how they affect the company's development, performance and position.

The information must contain:

- description of business model and strategy as well as opportunities and resilience to sustainability risks and transition plans
- targets and their progress status; indicators
- company sustainability governance (administrative, management and supervisory bodies and their expertise and skills to fulfil their role)
- sustainability policies
- incentives schemes linked to sustainability matters
- due diligence of sustainability matters and the process to conduct it
- company's principal and adverse impacts and actions to prevent, mitigate and remediate
- principle risks and their management
- double materiality
- information on business operations, value chain, including products and services and business relationships and its supply chain

5. Where should companies report?

Companies shall include information in the management report through a dedicated section. This means that companies must bring sustainability reporting forward to the time they publish their annual report.

6. What reporting standards are companies expected to use?

Companies must report in accordance with the European sustainability reporting standards (ESRS) adopted by the European Commission.

7. When are reporting standards expected to be adopted?

The European Commission shall adopt the European sustainability reporting standards (ESRS) via delegated acts as follows:

- by 30 June 2023 – cross-cutting standards and standards for all sustainability topics i.e., environment, social and human rights, and governance.
- by 30 June 2024:
    - sector-specific standards
    - proportionate standards for listed SMEs
    - standards for non-EU companies exceeding EU turnover thresholds

8. In what format should companies report?

Companies shall prepare their management report in the electronic reporting format and mark-up their sustainability reporting to upload them to the upcoming European Single Access Point (ESAP) (as per Delegated Regulation (EU) 2019/815 on single electronic reporting format).

II. Main differences between the NFRD and the CSRD

Main Differences NFRD & CSRD

	NFRD	CSRD
For whom?	Large public-interest entities with > 500 employees: • Listed companies • Banks and Insurance companies Approx. 11,600 companies	All large companies: • 250 employees and/or • €40M Turnover and/or • €20M Total Assets Listed companies Note: small and medium-listed companies get an extra three years to comply. Approx. 49,000 companies Covering > 75% of total EU companies' turnover
When>	FY 2018 – FY 2022	FY 2023 – FY ...
Reporting Requirements	• Environmental protection • Social responsibility and treatment of employees • Respect for human rights • Anti-corruption and bribery • Diversity on company boards (in terms of • age, gender, educational and professional background)	NFRD + Adding additional requirements on: • Double materiality concept: Reporting on both the impact the company has on society and the environment and the sustainability risk the company experiences (e.g., due to climate change and scarcity of resources) • Formulating long-term ESG objectives and policies • Due diligence on its operation and supply chain • Disclose information relating to intangibles (social, human, and intellectual capital) • Reporting in line with Sustainable Finance Disclosure Regulation (SFDR) and the EU Taxonomy Regulation • Integrated reporting and mandatory external assurance
Reporting Format/ Publication	Not set – mainly online/PDFs	European Single Electronic Format ("ESEF" / "XHTML"), data tags, database

The CSRD regulation introduces several key updates to the NFRD, aiming to eventually align sustainability reporting with financial reporting standards. These updates include:

- Expanding the scope of coverage: While the NFRD applies to large public-interest companies with more than 500 employees, covering approximately 11,000 businesses across the EU, the CSRD increases the scope to almost 50,000 companies. This includes all large companies meeting specific criteria, listed SMEs, listed companies, and qualifying non-EU companies.

-More detailed sustainability reporting: Under the CSRD, sustainability reporting will need to be provided with more detail compared to the NFRD. This includes reporting on strategy, policies, and a '**double materiality assessment.**

Double materiality assessment: Double materiality implies that businesses must report not just on how sustainability concerns may pose financial risks to the corporation (financial materiality), but also on their own impacts on people and the environment (impact materiality).
The concept of materiality analysis is twofold, considering both the impact on and of the business.

- The first component, referred to as "**outside-in**," involves identifying external risks that may affect the company's internal operations, such as reputation risks or CO2 levies.

- The second component, known as "**inside-out**," looks at the impact of the company on sustainability, whether positive or negative, such as damage to biodiversity or contributions to solving environmental issues.

Using the principle of double materiality, companies can identify significant topics based on factors such as probability, scale, recoverability, and social relevance.
The double materiality principle addresses the issue of one-sided reporting, which occurs when companies do not report negative environmental impacts that do not have a financial impact on their operations.

Previously, the Non-Financial Reporting Directive's materiality principle only considered the consequences of sustainability issues on finance and corporate activity (outside-in), which prioritizes investor and stakeholder interests.

However, double materiality broadens the scope of what is considered a significant sustainability factor by including the impact of finance and corporate activity on sustainability factors (inside-out). This approach gives **greater importance to stakeholder interests and expands the range of sustainability issues that companies must consider when reporting**.

By including both inside-out and outside-in factors, the double materiality principle ensures that companies report on all significant sustainability issues, regardless of their financial impact. This approach promotes transparency and accountability, helping to ensure that companies are responsible for their impact on the environment and society.

Double materiality provides several advantages, including the ability to focus resources on the most critical issues by offering a complete picture of the company's situation and its impact on the environment. This approach enables companies to operate efficiently and effectively. Additionally, the double materiality principle provides a clear structure for developing sustainability strategies and related reporting.
Furthermore, by making sustainability negotiable among stakeholders, the principle of double materiality enhances support for sustainability-related efforts. Ultimately, the application of double materiality offers multiple benefits for companies seeking to develop sustainable practices and achieve their environmental goals.

-Mandatory accreditation auditing: While third-party assurance of reporting was not obligatory under the NFRD, the CSRD requires a mandatory level of accredited auditing against sustainability reporting standards.

-New reporting standards: The European Financial Reporting Advisory Group (EFRAG) is developing the new standards, which are shaped to EU policies while building on global initiatives. The European Commission will consult EU bodies and Member States on the current draft standards before adopting the final standards as delegated acts in June 2023.

-Digital database reporting: The CSRD changes the way companies share their sustainability reporting information. Companies are required to submit their reports to a digital database.

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