



EU REPORTING - CSRD REQUIREMENTS FINALISED AND FIRST BATCH OF ESRS DELIVERED TO THE EUROPEAN COMMISSION

INTERNATIONAL SUSTAINABILITY REPORTING BULLETIN

2022/07



INTRODUCTION

In April 2021, the European Commission published a proposed new Corporate Sustainability Reporting Directive (CSRD). The proposals were designed 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.

As part of the legislative process, the European Commission's proposals were subject to review by the European Parliament and the European Council (which is made up of representatives from each EU Member State). Both the Parliament and the Council proposed amendments to the Commission's proposals.

In the second quarter of 2022, the so-called Trilogue discussions took place. These are discussions among the European Parliament, the European Council and the European Commission at which a compromise is sought, in order to finalise the text which will form the basis of the requirements of the new legislation.

The European Parliament has now published its [final text of the CSRD](#). The EU Council is expected to adopt the CSRD by the end of November 2022, after which it will be published in the Official Journal. The CSRD will then enter into force 20 days after publication. EU members states then have 18 months to incorporate the CSRD into their national law.

Separately, on 22 November 2022, EFRAG delivered the [first batch of European Sustainability Reporting Standards](#) to the European Commission.

This publication sets out an overview of key changes that will be introduced by the CSRD in comparison to the existing Non-Financial Reporting Directive (NFRD), based on the Parliament's final text, together with a more detailed explanation of the very significantly expanded scope, a summary of what companies need to prepare for, and when. It also includes an overview of the ESRS that were delivered to the European Commission and how (and the extent to which) the CSRD links these to IFRS Sustainability Disclosure Standards that are being developed by the ISSB at the IFRS Foundation.

EXECUTIVE SUMMARY

The Corporate Sustainability Reporting Directive significantly expands both the scope of the existing NFRD (including to non-EU undertakings) and the sustainability reporting requirements, which will be in accordance with European Sustainability Reporting Standards. Entities will also need to obtain assurance over the disclosures.



KEY CHANGES INTRODUCED BY THE CSRD

Requirement	NFRD	CSRD
Companies that are required to report	<p>Large public interest entities (both single entities and consolidated groups) with more than 500 employees</p> <p>Public interest entities are:</p> <ul style="list-style-type: none"> Companies listed on an EU regulated market (EU and non-EU companies) EU banks and insurance companies 	<p>Listed companies (except for listed micro entities)</p> <p>All large companies, defined as those meeting two out of the following three criteria:</p> <ul style="list-style-type: none"> More than 250 employees More than EUR 40m turnover More than EUR 20m total assets <p>This includes subsidiaries of non-EU groups.</p> <p>Insurance undertakings and credit institutions regardless of their legal form</p> <p>Non-EU groups which generate more than EUR 150m turnover in the EU and which have a subsidiary or branch in the EU (if a subsidiary, either a large - as defined above - or a listed entity and, if a branch, one which generates more than EUR 40m turnover).</p>
When do the requirements apply?	Years ended 31 December 2018 onwards	<p>Year ending 31 December 2024</p> <ul style="list-style-type: none"> Entities currently within the scope of the NFRD <p>Year ending 31 December 2025</p> <ul style="list-style-type: none"> All other large entities <p>Year ending 31 December 2026</p> <ul style="list-style-type: none"> Listed SMEs*, small and non-complex credit institutions and captive insurance undertakings <p>Year ending 31 December 2028</p> <ul style="list-style-type: none"> Non-EU undertakings (except those currently within the scope of the NFRD)
How many EU companies will need to comply with the requirements?	11,600	49,000
Scope of the requirements	<ul style="list-style-type: none"> Environmental protection Social responsibility and treatment of employees Human rights Anti-corruption and bribery Diversity on company boards 	<p>NFRD requirements plus:</p> <ul style="list-style-type: none"> Disclosure of information about intangibles (including social, human and intellectual capital) Additional forward looking information Reporting that is consistent with the Sustainable Finance Disclosure Regulation and the EU Taxonomy Double materiality concept, which expands the consideration of sustainability beyond an entity's capital market value, to include the entity's wider effects on society and the environment
Assurance	Not required	<p>Mandatory</p> <ul style="list-style-type: none"> Initially limited assurance, to be expanded to reasonable (audit) assurance in future.

*Listed SMEs can defer application of the reporting requirements to years ending 31 December 2028 if a statement is included in their management report of why the sustainability information was not provided.

SCOPE

The scope of the CSRD is considerably wider than the existing NFRD, and extends to cover all entities listed on regulated markets (except listed micro entities) and all large entities. There are also linked, additional reporting requirements; if an entity falls within the scope of the CSRD, then it is also required to report in accordance with Article 8 of the Taxonomy regulation. This requires disclosures about the extent to which an entity's operations are associated with environmentally sustainable economic activities (with reference to the related amounts of turnover, operating expenditure and capital expenditure).

Although listed SMEs will be required to report in accordance with the CSRD, they will be permitted to apply simplified sustainability reporting standards which are proportionate to the capacities and resources of SMEs, and relevant to the scale and complexity of their activities. These simplified sustainability reporting standards have not yet been developed and will form part of the second batch of sustainability standards that are required to be adopted by the European Commission by 30 June 2024.

Non-EU entities which have significant activity in the EU will also be required to publish sustainability reports. These are non-EU entities which have at least one subsidiary or branch in the EU and generate EUR 150 million net revenue or more in the EU as a whole in each of the last two consecutive financial years. To ensure proportionality, a subsidiary needs to be large or listed (except for listed micro entities), and there is an additional threshold for branches of net turnover of EUR 40 million or more. The sustainability reports are required to cover the consolidated group of the ultimate non-EU parent, with the responsibility for publication in the EU being with the subsidiary or branch. They will need to be prepared in accordance with sustainability standards that are applicable to EU entities, or in accordance with sustainability standards which are deemed to be equivalent by the European Commission.

BDO's Insight

The scope of the CSRD is such that certain entities that are not domiciled in the EU will be required to provide sustainability disclosures.

The European Commission is required to adopt sustainability reporting standards that specify the information to be included in reports prepared by non-EU entities by 30 June 2024.

A non-EU parent may have multiple subsidiaries in the EU that are within the scope of the CSRD. As a transitional provision, for the first seven years in which the CSRD is in force, one of those EU subsidiaries will prepare a consolidated sustainability report that includes all EU subsidiaries that are within the scope of the CSRD. The EU subsidiary

which prepares the sustainability report will be one of the subsidiaries that generated the greatest amount of turnover in the EU in at least one of the preceding five years, on a consolidated basis where applicable. The same approach applies to information which is required to be disclosed by the Taxonomy regulation.

There are some exemptions to the application of the CSRD, although these do not apply to large Public Interest Entities. An unlisted subsidiary will be exempt if it is included in a consolidated group sustainability report prepared by its ultimate parent company that complies with the CSRD (or other standards that are recognised as equivalent). A similar exemption applies to a subsidiary that is itself a parent entity. However, additional disclosures will be required in the consolidated group report to provide an adequate understanding if the circumstances (that is, the sustainability risks or effects) of the group and the subsidiary are significantly different (or the circumstances of subsidiaries in different geographies are significantly different). The sustainability report of the parent will also have to be subject to assurance (either limited or reasonable) in the same way assurance would be required if the parent was an EU entity. If the parent does not report in accordance with the CSRD, and the EU has not granted equivalence to the sustainability reporting framework adopted by the parent, the subsidiary will have to prepare a report in accordance with the CSRD.

If an unlisted subsidiary of a non-EU parent does qualify for and take advantage of the exemption, it will need to include in its management report the name and registered office of the parent entity that is reporting consolidated sustainability information at group level and related website links, together with a statement that the subsidiary is exempt from reporting sustainability information. There is a member state option to require the consolidated sustainability report to be translated into any language that they accept.

The exemption for sustainability reporting has criteria which are different from those applicable to financial reporting consolidation exemption. Consequently, it is possible that an entity could qualify for the financial reporting consolidation exemption, but not for the sustainability reporting exemption, and vice versa.

For the purposes of equivalence, the European Commission will be able to establish a mechanism for sustainability reporting standards applied by non-EU entities. This will be similar to the existing regulation which sets out the criteria for the equivalence of accounting standards applied by non-EU entities.

However, the European Commission will use specified criteria when assessing the equivalence of sustainability reporting standards that are applied by non-EU entities which are that they at least ensure:

- That the sustainability reporting standards require disclosure of information on environmental, social and governance factors; and
- That the sustainability reporting standards require the disclosure of information which is necessary to understand the entity's impacts on sustainability matters, and to understand how sustainability matters affect their development, performance and position (that is, a 'double materiality' approach - see the sustainability reporting standards section below).

KEY AREAS OF REPORTING

Entities will be required to report information which is necessary to understand their impacts on sustainability matters, and information necessary to understand how sustainability matters affect their development, performance and position. The information will need to be disclosed in a clearly defined section of the management report, and include:

- A brief description of the business model and strategy
- A description of time bound targets related to sustainability matters, including (where appropriate) absolute greenhouse gas emission reduction targets for at least 2030 and 2050, together with a description of the progress made in achieving those targets and a statement of whether the targets related to environmental targets are based on conclusive scientific evidence
- A description of the role of the administrative, management and supervisory bodies with regard to sustainability matters, and of their expertise and skills in relation to fulfilling that role or the access they have to such expertise and skills
- A description of the entity's policies in relation to sustainability matters
- Information about the existence of incentive schemes offered to members of the administrative, management and supervisory bodies which are linked to sustainability matters
- The due diligence process implemented with regard to sustainability matters, the principal actual or potential adverse effects connected with an entity's own operations and value chain, and any actions taken (and the result of those actions) to prevent, mitigate, remediate or bring an end to actual or potential adverse effects.
- Principal risks to the entity associated with sustainability matters, including dependencies, and how such risks are managed

- The process carried out to identify the information included in the sustainability report, including information related to short, medium and long-term time horizons as applicable
- Turnover, capex and opex in accordance with the Taxonomy Regulation

SUSTAINABILITY REPORTING STANDARDS

Proposals for the first batch of European Sustainability Reporting Standards (ESRS) were developed by a Project Task Force at the European Financial Reporting Advisory Group (EFRAG). Exposure drafts were published in April 2022 with a comment deadline of early August 2022. Final standards, approved by the EFRAG Sustainability Reporting Board, supported by the EFRAG Sustainability Reporting Technical Expert Group (TEG), were delivered by EFRAG to the European Commission on 22 November 2022. This first set of ESRS is required to be adopted by the European Commission no later than 30 June 2023.

12 standards were delivered to the European Commission (although there were 13 exposure drafts, one of the proposed governance standards has been merged into ESRS 2), and cover the following topics:

Cross cutting

- ESRS 1 General requirements
- ESRS 2 General disclosures

Topical standards - 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

Topical standards - social

- ESRS S1 Own workforce
- ESRS S2 Workers in the value chain
- ESRS S3 Affected communities
- ESRS S4 Consumers and end-users

Topical standards - governance

- ESRS G1 Business conduct

Although the number of overall disclosure requirements in the final ESRS have been significantly reduced in comparison with the exposure drafts (from 128 to fewer than 100), they remain complex and detailed with around 1,100 data points. Of these, around 400 are required by EU legislation and will always need to be disclosed; the remaining 700 are required subject to a materiality assessment.

Key changes in comparison with the exposure drafts include:

- The three pillar structure that was proposed in the exposure drafts has been changed to align with the four pillars in the TCFD (governance, strategy, risk management, metrics and targets) which form the foundation of the ISSB's proposals. However there are some differences for risk

management due to the ESRS using double materiality (see below), and the way in which ESRS incorporate metrics and targets in the form of policies, actions, targets and performance metrics although, in accordance with the CSRD, the remit of the EFRAG SRB has been to align with the ISSB to the fullest extent possible.

- In a number of key respects, the ESRS have been aligned with ISSB proposals, including the terminology for qualitative characteristics, financial stakeholders (investors, lenders and creditors), and financial materiality. However, the financial materiality alignment is with the ISSB exposure draft, and the ISSB has since tentatively decided to amend its definition to eliminate the reference to enterprise value.
- The rebuttable presumption that disclosures included in the ESRS are material has been eliminated. However, disclosures in two of the ESRS (ESRS 2 General disclosures and ESRS E1 Climate change) will always be mandatory because the disclosure requirements in those ESRS come from EU legislation (for ESRS 2, the CSRD and for ESRS E1 the Sustainable Finance Disclosure Regulation, or SFDR).
- The references to time horizons (short - up to one year, medium - up to five years, long - more than five years) has been retained, but is structured more as guidance than a specific requirement.
- The application guidance had become mandatory application requirements, which form an integral part of each ESRS.

The ESRS incorporate the so-called double materiality concept, which expands the consideration of sustainability beyond an entity's enterprise (or capital market) value, to include the entity's wider effects on society and the environment. Views differ about the extent to which double materiality differs from enterprise value materiality; some consider that there are significant differences, while others consider that the differences are relatively small (for example, because an entity's employment of slave labour would be likely to affect its reputation in the marketplace and, in consequence its future sales and profits).

Additional sets of sector specific standards will also be developed as will standards for SMEs, with the first additional set to be adopted by the European Commission no later than 30 June 2024.

As part of the process to ensure that the ESRS take account of the views of EU Member States, the European Commission will need to consult the Member State Expert Group on Sustainable Finance and the Accounting Regulatory Committee (note that consultation with this Committee is also part of the process for the EU endorsement of IFRS Accounting Standards). The European Securities and Markets Authority (ESMA), European Banking Authority (EBA) and the European Insurance and Occupational Pensions Authority (EIOPA) will be required to give an opinion on EFRAG's technical advice to the European Commission. These organisations will have a period of two months to respond from the date of receipt of the request from the European Commission.

The European Commission will also be required to consult the European Environment Agency, the European Union Agency for Fundamental Rights, the European Central Bank, the Committee of European Auditing Oversight Bodies and the Platform on Sustainable Finance, with those organisations being given two months from the date of being consulted to submit any comments or opinions if they wish to do so.

Information about a company's value chain will be required. However, for the first three years after the application of the CSRD, if the necessary information is not available, companies do not need to publish value chain information. However, in that case, they are required to provide an explanation of the efforts made to obtain that information, and set out the reasons why the information could not be obtained together with plans about how the information will be obtained in future.

Companies will need to report more widely about key intangible resources on which the business model depends. The potential scope of reporting is wide; examples are information about employees' skills, competencies, experience, loyalty to the entity and motivation for improving processes, goods and services. Information about the quality of relationships between the entity and its stakeholders, including customers, suppliers and communities affected by an entity's activities that is relevant to social or governance matters could also be viewed as being information about intangible resources.

There will also be a requirement to disclose plans about the business model and strategy that are linked to the transition to a sustainable economy, and with the objective of limiting global warming to 1.5°C above pre-industrial levels in accordance with the Paris Agreement.

The European Commission is required to undertake a review of the standards, including those for SMEs, every three years to take account of relevant developments, including the development of international standards.

RELATIONSHIP WITH INTERNATIONAL SUSTAINABILITY REPORTING STANDARDS

The exposure drafts of ESRS were developed by EFRAG during a period in which there were also significant international developments, including the formation of the International Sustainability Standards Board at the IFRS Foundation. The final text of the CSRD includes references to the need for the ESRS to take account of both existing standards (including the GRI, SASB, IIRC, IASB, TCFD, CDSB and CDP) as well as any sustainability reporting standards developed under the IFRS Foundation. Recital 43 notes that:

'Sustainability reporting standard should be proportionate and should not impose an unnecessary administrative burden on companies required to use them. In order to minimise disruption for undertakings that already report sustainability information, sustainability reporting standards should take account of existing standards and frameworks for sustainability reporting and accounting where appropriate. Such existing standards and frameworks include the Global Reporting Initiative and Sustainability Accounting Standards Board, the International Integrated Reporting Council, the International Accounting Standards Board, the Task-force on Climate-related Financial Disclosures, the Carbon Disclosure Standards Board, and CDP, formerly known as the Carbon Disclosure Project. Union standards should take account of any sustainability reporting standards developed under the auspices of the International Financial Reporting Standards Foundation. To avoid unnecessary regulatory fragmentation that could have negative consequences for undertakings operating globally, Union sustainability reporting standards should contribute to the process of convergence of sustainability reporting standards at global level, by supporting the work of the International Sustainability Standards Board (ISSB). Union sustainability reporting standards should reduce the risk of inconsistent reporting requirements for undertakings to operate globally by integrating the content of global baseline standards to be developed by the ISSB, to the extent that the content of those baseline standards is consistent with the Union's legal framework and the objectives of the Green Deal.'

Recitals to EU law are not themselves legally binding in the way that the operative provisions (the Articles) are. However, Article 29b(2) states that

...The sustainability reporting standards shall ensure the quality of reported information, by requiring that it is understandable, relevant, verifiable, comparable and represented in a faithful manner. The sustainability reporting standards shall avoid imposing a disproportionate administrative burden on undertakings, including by taking account, to the greatest extent possible, of the work of global standard-setting initiatives for sustainability reporting..'

In addition, Article 29b(5) requires that:

When adopting delegated acts pursuant to paragraph 1, the Commission shall, to the greatest extent possible, take account of:

- (a) the work of global standard-setting initiatives for sustainability reporting, and existing standards and frameworks for natural capital accounting and for greenhouse gas accounting, responsible business conduct, corporate social responsibility, and sustainable development;
- (b) ...
- (c) ...

ASSURANCE

The CSRD introduces requirements for the assurance of sustainability reports. The European Commission is to adopt assurance standards for limited assurance by October 2026, with assurance standards for reasonable assurance following by October 2028 (subject to an assessment of whether reasonable assurance is feasible for auditors and for entities).

Although the European Commission is required to adopt assurance standards, during the period before these standards are adopted, national assurance standards are permitted to continue to apply. Since EU Member States have differing requirements, diversity in the requirements may arise before the European Commission adopts EU-wide assurance standards.

When an entity is required by EU legislation to have some elements of its sustainability reporting assured, the assurance report is to be made available either as an annex to the management report or by some other publicly accessible means. Where the same statutory auditor carries out the statutory audit of the financial statements and the assurance of sustainability reporting, Member States can require the assurance report on sustainability reporting to be included as a separate section of the audit report.

ASSURANCE PROVIDERS

The statutory auditor will be able to provide an opinion on sustainability reporting.

In addition, Member States are to be given two options. These are:

- to allow a statutory auditor other than the one(s) carrying out the statutory audit to express an opinion on sustainability reporting, and
- to accredit Independent Assurance Service Providers (IASPs) which are assurance providers that are not statutory auditors.

However, if a Member State accredits IASPs, it is then also required to allow a statutory auditor other than the one(s) carrying out the statutory audit to express an opinion on sustainability reporting.

In order to provide a level playing field among all persons and firms permitted by Member States to provide an assurance opinion on sustainability reporting, IASPs will be subject to requirements that are equivalent to those applicable to statutory auditors, while being adapted to the characteristics of IASPs that do not carry out statutory audits. This includes training and examination, continuing education, quality assurance systems, professional ethics, independence, objectivity, confidentiality and professional secrecy, appointment and dismissal, the organisation of the work of IASPs, investigations and sanctions, and the reporting of irregularities. However, IASPs that have, prior to implementation of the CSRD, already been accredited by a Member State for the assurance of sustainability information will be permitted to continue to do so, subject to compliance with the new accreditation requirements within a period of two years from the date of application of those new requirements.

If the assurance of sustainability reporting is carried out by an audit firm, Member States are required to ensure that the audit firm designates at least one key sustainability partner, who may also be (one of) the key audit partner(s). The key audit partner(s) will be required to be actively involved in the work in carrying out the assurance of sustainability reporting.

The CSRD also prohibits any restriction on the choice of auditor by the general meeting of shareholders or members of the audited entity to certain lists of statutory auditors or audit firms for the statutory audit and, where applicable, the assurance of sustainability reporting, with any such clauses being null and void. There is also a prohibition on the dismissal of statutory auditors or audit firms except where there are proper grounds. The CSRD notes that divergence of opinions on accounting treatments, audit procedures or, where applicable, on sustainability reporting or assurance procedures are not proper grounds for dismissal.



This publication has been carefully prepared, but it has been written in general terms and should be seen as broad guidance only. The publication cannot be relied upon to cover specific situations and you should not act, or refrain from acting, upon the information contained therein without obtaining specific professional advice. Neither BDO IFR Advisory Limited, and/or any other entity of BDO network, nor their respective partners, employees and/or agents accept or assume any liability or duty of care for any loss arising from any action taken or not taken by anyone in reliance on the information in this publication or for any decision based on it.

The BDO network (referred to as the 'BDO network' or the 'Network') is an international network of independent public accounting, tax and advisory firms which are members of BDO International Limited and perform professional services under the name and style of BDO (hereafter 'BDO member firms'). BDO International Limited is a UK company limited by guarantee. It is the governing entity of the BDO network.

Service provision within the BDO network in connection with corporate reporting and IFRS Accounting Standards (comprising International Financial Reporting Standards, International Accounting Standards, and Interpretations developed by the IFRS Interpretations Committee and the former Standing Interpretations Committee), and other documents, as issued by the International Accounting Standards Board and IFRS Sustainability Disclosure Standards as issued by the International Sustainability Standards Board, is provided by BDO IFR Advisory Limited, a UK registered company limited by guarantee. Service provision within the BDO network is coordinated by Brussels Worldwide Services BV, a limited liability company incorporated in Belgium.

Each of BDO International Limited, Brussels Worldwide Services BV, BDO IFR Advisory Limited and the BDO member firms is a separate legal entity and has no liability for another entity's acts or omissions. Nothing in the arrangements or rules of the BDO network shall constitute or imply an agency relationship or a partnership between BDO International Limited, Brussels Worldwide Services BV, BDO IFR Advisory Limited and/or the BDO member firms. Neither BDO International Limited nor any other central entities of the BDO network provide services to clients.

BDO is the brand name for the BDO network and for each of the BDO member firms.

© 2022 BDO IFR Advisory Limited, a UK registered company limited by guarantee. All rights reserved.