Corporate Sustainability Reporting Directive

New reporting requirements for undertakings in the EU

16 January 2023

The Corporate Sustainability Reporting Directive ("CSRD")[1] entered into force on 5 January 2023. The CSRD must be transposed into the national laws of EU member states by 6 July 2024.

Summary of key points:

- the CSRD **amends and strengthens the existing rules on reporting sustainability information**, creating new uniform and more detailed sustainability reporting standards in the EU;
- the new reporting rules **significantly expand the categories of undertakings** which are subject to reporting requirements;
- reporting will need to be **certified by an accredited independent auditor or certifier**;
- the sustainability report will be **published in a dedicated section of company management reports**, disclosed in a digital, machine-readable format;
- the **application of the CSRD will take place in four stages**. The first reporting will need to be done in 2025 for the financial year 2024.

The CSRD significantly extends the scope of sustainability reporting requirements and the number of undertakings that are subject to these reporting requirements as compared to the currently applicable Non-Financial Reporting Directive ("**NFRD**")[2].

Its goal is to increase business accountability, enhance transparency and comparability of sustainability information, prevent divergent sustainability reporting standards and "greenwashing", and to facilitate the transition to a sustainable economy.

Thorough sustainability reporting can help undertakings to identify and manage their own risks and opportunities related to sustainability and can improve access to financial capital.

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[1] Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022 amending Regulation (EU) No 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting.

[2] The NFRD currently applies to large public-interest entities with an average number of employees in excess of 500, and to public-interest entities that are parent undertakings of such undertakings. Approximately 11,700 companies are subject to the reporting requirements of the NFRD.

1 Undertakings covered by the CSRD

The following categories of undertakings are subject to sustainability reporting obligations under the CSRD, in addition to public-interest entities:

(1) Undertakings whose securities are admitted to trading on a regulated market in the EU (except micro undertakings[3]);

(2) Large undertakings - either an EU undertaking or an EU subsidiary of a non-EU undertaking, which exceeds at least two of the following criteria:

(i) balance sheet total exceeding EUR 20 million,

(ii) a net turnover exceeding EUR 40 million; and

(iii) more than 250 employees on average during the financial year;

(3) Third-country undertakings with significant activity in the territory of the EU (net turnover of more than EUR 150 million in the EU at consolidated level) and which have at least one subsidiary (large or listed) or a branch in the territory of the EU exceeding certain net turnover thresholds.

Exemption for Subsidiary Undertakings

A subsidiary undertaking will be exempt from reporting if that undertaking and its subsidiary undertaking are included in a consolidated management report of their parent undertaking, provided that the parent's report is compliant with the CSRD or if a non-EU parent's sustainability disclosures were determined to be "equivalent" to EU sustainability reporting standards. The Commission will adopt necessary decisions on the equivalence of sustainability reporting standards and measures that aim to establish general equivalence criteria regarding sustainability reporting standards to issuers of more than one country.

2 When does the CSRD apply?

The application of the new reporting rules will take place in four stages (for financial years starting on or after):

As of 1 January 2024	- Large undertakings (with over 500 employees) which are already subject to the NFRD.
As of 1 January 2025	- Large undertakings which are not currently subject to the NFRD, and exceed two of the following size criteria: a. 250 employees on an annual average; b. balance sheet total of more than EUR 20 million; c. revenue of more than EUR 40 million.

[3] In order to qualify as a micro undertaking, an undertaking must remain below at least two of the following: (i) have fewer than 10 employees over the financial year on average; (ii) a net turnover of EUR 0.7 million; and (iii) a balance sheet total of EUR 0.35 million.

As of 1 January 2026	- All listed small and medium-sized enterprises (**SMEs**), including third-country undertakings whose securities are admitted to trading on a regulated market in the EU. **SMEs can opt-out from sustainability reporting requirements until 2028.**
As of 1 January 2028	- Third-country undertakings with: a. an annual net revenue at the consolidated or individual level in the EU of more than EUR 150 million for each of the last two consecutive financial years, and b. at least one subsidiary undertaking (which is either a large EU undertaking or an SME) or a branch in the EU which generated an annual net revenue in excess of EUR 40 million in the preceding financial year.

To meet these reporting obligations, undertakings must start collecting the relevant data in the previous year, which means that the companies which must report after 1 January 2024, must start collecting the relevant data from 1 January 2023.

3 What are the obligations under the CSRD?

An undertaking must report forward-looking, retrospective, qualitative and quantitative information necessary to understand (i) the undertaking's impacts on sustainability matters and (ii) the impact of sustainability matters on the undertaking's development, performance, and position ("**double materiality**" reporting).

The principle of double materiality requires that undertakings look inward (to evaluate how sustainability issues affect the undertaking) and outward to understand how the undertaking impacts people and the environment, considering short-, medium- and long-term time horizons.

In order to ensure the quality and reliability of reporting, the sustainability reports of third-country undertakings should be accompanied by an assurance opinion expressed by a person or firm authorised to give an opinion on the assurance of sustainability reporting. If no assurance opinion is provided, the subsidiary undertaking or branch must issue a statement indicating that the third-country undertaking did not make the necessary assurance opinion available.

The sustainability report should be made accessible free of charge to the public through the central, commercial or companies registers of the Member States, or alternatively on the website of the subsidiary undertaking or the branch of the third-country undertaking.

3.1 Provide additional disclosures

Undertakings are required to report on the following list of sustainability matters:

(1) **Strategy and business model** (including the resilience of their business model and strategy to risks related to sustainability matters; their opportunities related to sustainability matters; their plans (*including implementing actions and related financial and investment plans*) to ensure that their business model and strategy are compatible with the transition to a sustainable economy and in line with the Paris Agreement and the objective of achieving climate neutrality by 2050; how their business model and strategy take account of the interests of their stakeholders and of their impact on sustainability matters; and how their strategy has been implemented with regard to sustainability matters.)

(2) Established sustainability targets and the progress made towards achieving them;

(3) Governance - the role of the administrative, management and supervisory bodies regarding sustainability matters;

(4) Policies in relation to sustainability matters;

(5) Existence of incentive schemes linked to sustainability matters which are offered to members of the administrative, management and supervisory bodies;

(6) Due diligence process implemented regarding sustainability matters;

(7) Impacts - principal (actual or potential) adverse impacts connected with the undertaking's value chain, including its own operations, its products and services, its business relationships and its supply chain;

(8) Remedial Actions taken, and the result of such actions, to prevent, mitigate or remediate actual or potential adverse impacts;

(9) 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; and

(10) Indicators relevant to the disclosures referred to in points (1) to (9).

Value Chain Reporting

Where appropriate, an undertaking will also have to disclose information about its own operations and about its value chain, including its products and services, business relationships and supply chain.

For the first three years of the application of the reporting obligations and in the event that not all the necessary information regarding its value chain is available, the undertaking will have to explain the efforts made to obtain the necessary information about its value chain, the reasons why not all of the necessary information could be obtained, and its plans to obtain the necessary information in the future.

Key Intangible Resources

Undertakings will also need to report information on the key intangible resources[4] and explain how the business model of the undertaking fundamentally depends on such resources and how such resources are a source of value creation for the undertaking.

[4] The CSRD defines the "key intangible resources" as resources without physical substance on which the business model of the undertaking fundamentally depends and which are a source of value creation for the undertaking.

3.2 Report in accordance with new European Sustainability Reporting Standards

Disclosures will need to be reported in accordance with the European Sustainability Reporting Standards (**ESRS**) which are to be developed by the European Financial Reporting Advisory Group (**EFRAG**), a public-private partnership tasked to advise the European Commission on the adoption of international financial reporting standards into EU law. The EFRAG delivered the first set of draft ESRS[5] to the European Commission on 23 November 2022, and the European Commission must adopt the first set of standards by 30 June 2023.

To respect the principle of proportionality, the European Commission will adopt mandatory sustainability reporting standards for large undertakings and separate, proportionate standards for SMEs, for third country undertakings, and additional sector-specific standards, which are particularly important for sectors associated with high sustainability risks and/or impacts on the environment, human rights and governance[6].

Further standards must be adopted by 30 June 2024.

3.3 Use Digital Tagging

Under the NFRD, undertakings may currently choose where to file their non-financial statements - either in their management report or, under certain conditions, in a separate report. Under the CSRD, undertakings will have to disclose sustainability information in their management report. Financial statements and management reports will need to be prepared in a single electronic reporting format, and sustainability information will have to be marked-up as and when specified in the ESEF Regulation[7].

3.4 Additional Role of Audit Committees and Assurance Providers

Audit committees will have enhanced responsibilities under the CSRD. Along with monitoring the undertaking's sustainability reporting process and submitting recommendations to ensure the integrity of the sustainability information, they will need to (i) monitor the effectiveness of the undertaking's internal quality control and risk management systems and its internal audit functions; (ii) monitor the assurance of annual and consolidated sustainability reporting; (iii) inform the undertaking's administrative or supervisory body of the outcome of the assurance of sustainability reporting; and (iv) review and monitor the independence of the assurance providers.

The CSRD introduces a general EU-wide audit assurance requirement for reported sustainability information in order to prevent greenwashing. The European Commission will adopt legislation to provide for a "**limited assurance**" requirement by 1 October 2026, and subsequently adopt further legislation to provide for a higher "**reasonable assurance**" requirement by 1 October 2028.

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[5] The first set of 12 draft ESRS is composed of two (2) Cross-cutting Standards and ten (10) topical standards – five (5) covering environment, four (4) social and one (1) governance.

[6] EFRAG announced on 23 November 2022 that in the next months it will focus on set 2 of draft ESRS which are draft sector specific standards: (i) five (5) sectors covered by global reporting standards (GRI): agriculture, coal mining, mining, oil+gas (upstream), oil+gas (mid-to downstream) and five (5) high-impact sectors: energy production, road transport, motor vehicle production, food/beverages, and textiles.

[7] Commission Delegated Regulation (EU) 2018/815 of 17 December 2018 supplementing Directive 2004/109/EC of the European Parliament and of the Council with regard to regulatory technical standards on the specification of a single electronic reporting format.

3.5 Rights of Shareholders

Shareholders or members of large undertakings subject to sustainability reporting requirements and which represent more than 5 % of the voting rights or 5 % of the capital of the undertaking, acting individually or collectively, have the right to table a draft resolution to be adopted in the general meeting of shareholders or members, requiring that an accredited third-party that does not belong to the same audit firm or network as the statutory auditor or audit firm carrying out the statutory audit prepare a report on certain elements of the sustainability reporting and that such report be made available to the general meeting of shareholders or members.

3.6 Penalties

The CSRD does not contain provisions on uniform penalties for companies that should report under the CSRD but fail to do so, nor does it provide for sanctions for improper conduct by authorised auditors. Penalties and procedures related to infringements will be enacted by the Member States.

4 Key Takeaways

The CSRD significantly extends the scope of the sustainability reporting requirements and the number of undertakings subject to such reporting requirements. It is important that the undertakings to which the CSRD applies start compiling and developing standards and procedures to make sure that the sustainability information is available and accurate.

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