Political agreement on the CSRD: New sustainability reporting obligations in the EU start with the 2024 financial year

In April 2021, the European Commission published its proposal for a Corporate Sustainability Reporting Directive (CSRD) for a comprehensive revision of sustainability reporting in the EU. The political negotiations with the Member States and the European Parliament (the so-called trilogue) on the CSRD, which have been ongoing for months, were concluded on 21 June 2022, so that the CSRD can be officially adopted by the European Parliament and the Council before the end of 2022. The key points of the agreement were announced in press releases of the Council of the European Union and the European Parliament.

More detailed and more standardised reporting requirements

- With the CSRD, the existing sustainability matters of environmental, social and governance reporting will be expanded and standardised. A major contributing factor is the clarification of the principle of double materiality. This principle requires that the reporting covers information necessary for an understanding of how sustainability matters affect the undertaking's development, performance and position, as well as information necessary for an understanding of the undertaking's impacts on sustainability matters.
- There is also a standardisation of content which is to be achieved through mandatory reporting standards following technical advice from EFRAG. It is expected that this will eliminate the existing "patchwork" of different voluntarily applicable sustainability frameworks and standards. The first drafts of the standards, the European Sustainability Reporting Standards (ESRS), were issued for public consultation by EFRAG at the end of April 2022 and show how challenging the new reporting requirements are in terms of depth and breadth.

Extension of scope

- The CSRD will significantly expand the scope of sustainability reporting at both the individual entity and group level. On the one hand, all large undertakings, whether listed or not, as well as all parent undertakings of a large group will be subject to the new reporting requirements. The determination of the size criteria for large undertakings and large groups follows the EU Accounting Directive, i.e. large undertakings are those which exceed two of the three criteria i) € 20 million balance sheet total, ii) € 40 million net turnover, iii) average number of 250 employees during the financial year in two consecutive financial years. On the other hand, the scope of application also includes small and medium-sized entities (SMEs), provided they are listed on regulated markets, but with the possibility of postponing the first-time application by two years ("opt-out") and on the basis of their own reporting standards.(ie set of SMEs specific standards).
- What is fundamentally new compared with the Commission proposal is that the scope of application also includes companies outside the EU if they generate a net turnover in the EU of more than € 150 million and have at least one subsidiary or branch in the EU. Details on the implementation of this aspect are not yet known, because there are different scenarios envisaged.

There is a possibility that there could be changes to the exemption options for subsidiaries by inclusion in the consolidated sustainability report of a parent undertaking. Listed subsidiaries may no longer benefit from this exemption option. In addition, certain disclosures and metrics have to be broken down at the subsidiary level in the parent undertaking's report, possibly under the condition that the subsidiary has a different risk profile than the group as a whole.

Timing: First-time application

The first-time application will be staggered as follows:

- For undertakings that are already subject to reporting under the Non-Financial Reporting Directive (NFRD): First-time application for financial years beginning on or after 1.1.2024;
- For large undertakings (as defined) or parent undertakings of a large group that are not yet covered by the NFRD: First-time application for financial years beginning on or after 1 January 2025;
- For listed SMEs, certain small and non-complex credit institutions and so-called captive insurance undertakings: first-time application for financial years beginning on or after 1 January 2026. Listed SMEs have the possibility to opt-out of the application of the CSRD until the financial year 2028.

Where to report and external assurance obligation

Unlike in the past, the only permissible reporting format will be the (group) management report. The sustainability report will form a separate section within the (group) management report.

Sustainability reporting will be subject to an external assurance obligation (initially with only limited assurance being required). The (statutory) auditor of the financial statements will be allowed to perform these assurance engagements.

It may take several weeks for the final text of the Directive to be available and only then it will be possible for detailed questions to be answered. Both the Parliament and the Council still have to formally adopt the text. Therefore, until that happens, there could always be changes to the final text.