EU legislative tsunami

- Lela Mélon -
1. Corporations
2. Corporate Sustainability Reporting Directive
3. Corporate Sustainability Due Diligence Directive
4. Recap
1. Corporations
Corporate Knights - 100 most powerful economies in the world
The size of corporations
The influence of corporation
The focus on regulating corporate behaviour in the EU
2. Corporate Sustainability Reporting Directive
CSRD context

1. **NFRD and taxonomy**
   - Companies will report their business contribution to sustainability

2. **SFDR and taxonomy**
   - Investors will use this information to calculate their contribution to sustainability. They will also report on their approach to sustainability

3. **Taxonomy and MiFID suitability**
   - Advisors will assess which products fit their sustainability policy. They will also ask clients if they prefer sustainable products

4. **More money for sustainable investments**
   - Investors will see which managers best integrate sustainability. They will choose advisors who have a sustainability stance
From NFRD to CSRD

NFRD EVOLUTION

2013
Accounting directive (2013/34/EU) – ensure clarity & comparability of financial statements

2014
NFRD Draft (2014/95/EU) Accounting Directive amended to include non-financial reporting in annual reporting

2016
EU Green Deal

2017
NFRD Becomes Law

2018
Action Plan for Financing Sustainable Growth

2019
Additional guidelines for disclosure of complete related information being published

2020
Consultation to identify revisions to NFRD

2021
EC Proposal for Corporate Sustainability Reporting Directive

2022
EU ESAs guidance for Taxonomy-Aligned Disclosure under NFRD

2023
Companies would apply the standards set by the CSRD for the first time to reports published in 2024, covering financial year 2023

EFRAF to publish Sustainability Reporting Standards by 6/2022 that will align with CSRD

Proposals for Sustainability Reporting Standard-Setting
The Corporate Sustainability Reporting Directive (CSRD) requires companies to report on the impact of corporate activities on the environment and society, and requires the audit (assurance) of reported information.

<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Which companies are concerned?</strong></td>
<td>Large &quot;public interest entities&quot; with more than 500 employees</td>
</tr>
<tr>
<td>All large companies meeting at least 2 out of 3 criteria:</td>
<td>• Listed companies</td>
</tr>
<tr>
<td>• 250 employees and/or</td>
<td>• Banks and insurance companies</td>
</tr>
<tr>
<td>• EUR 40M Turnover and/or</td>
<td></td>
</tr>
<tr>
<td>• EUR 20M Total Assets</td>
<td></td>
</tr>
<tr>
<td>Listed companies on EU regulated markets (SMEs get 3+ years to comply)</td>
<td></td>
</tr>
<tr>
<td>• Except listed micro-companies (less than 10 employees or below EUR 20M in turnover)</td>
<td></td>
</tr>
<tr>
<td><strong>Timeline</strong></td>
<td>In application since 2018</td>
</tr>
<tr>
<td>Application on 1st January 2024 for the 2023 financial year (SMEs 2027)</td>
<td></td>
</tr>
<tr>
<td>• Concerned companies will have to submit their report in compliance with the CSRD by 2023</td>
<td></td>
</tr>
<tr>
<td>• For SMEs more detailed reporting requirements and delayed timelines are available</td>
<td></td>
</tr>
<tr>
<td><strong>Different phases:</strong></td>
<td></td>
</tr>
<tr>
<td>• 2023: the first set of Sustainability Reporting Standards (draft standards open mid-2022)</td>
<td></td>
</tr>
<tr>
<td>• 2024: the second set of Sustainability Reporting Standards</td>
<td></td>
</tr>
<tr>
<td>Adoption of the EU Directive in MS legislation: 1st December 2022</td>
<td></td>
</tr>
<tr>
<td><strong>No of companies concerned</strong></td>
<td>11,600</td>
</tr>
<tr>
<td>49,000 (75% of total EU’s companies turnover)</td>
<td></td>
</tr>
</tbody>
</table>
The Corporate Sustainability Reporting Directive (CSRD) requires companies to report on the impact of corporate activities on the environment and society, and requires the audit (assurance) of reported information.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Additional requirements on:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Double materiality concept:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sustainability risk: including</td>
<td></td>
<td></td>
</tr>
<tr>
<td>climate change, affecting</td>
<td></td>
<td></td>
</tr>
<tr>
<td>the company</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Companies’ impact on society</td>
<td></td>
<td></td>
</tr>
<tr>
<td>and environment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Process to select material</td>
<td></td>
<td></td>
</tr>
<tr>
<td>topics for stakeholders</td>
<td></td>
<td></td>
</tr>
<tr>
<td>More forward-looking information,</td>
<td></td>
<td></td>
</tr>
<tr>
<td>including targets and progress</td>
<td></td>
<td></td>
</tr>
<tr>
<td>therein</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Disclose information relating</td>
<td></td>
<td></td>
</tr>
<tr>
<td>to intangibles (social, human</td>
<td></td>
<td></td>
</tr>
<tr>
<td>and intellectual capital)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reporting in line with</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sustainable Finance Disclosure</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Regulation (SFD) and the EU</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxonomy Regulation</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reliability of reporting (Third</td>
<td>Mandatory (planned end of 2022)</td>
<td>Non-mandatory</td>
</tr>
<tr>
<td>party assurance)</td>
<td>Reporting must include:</td>
<td></td>
</tr>
<tr>
<td>Integration in auditor’s report</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Involvement of key audit</td>
<td></td>
<td></td>
</tr>
<tr>
<td>partner</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Scope to include EU Taxonomy</td>
<td></td>
<td></td>
</tr>
<tr>
<td>and process to identify key</td>
<td></td>
<td></td>
</tr>
<tr>
<td>relevant information</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Where to report
- Included in the Management Report
- A single report in a “digital machine-readable format”

Non-mandatory
- Included in the Annual Report
- The sustainability report can be disclosed separately with a clear reference to the financial report and management report.
The Corporate Sustainability Reporting Directive (CSRD) requires companies to report on the impact of corporate activities on the environment and society, and requires the audit (assurance) of reported information.

<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Reporting format</strong></td>
<td>Electronic format (in XHTML format in accordance with ESEF regulation)</td>
</tr>
<tr>
<td><strong>Alignment with other EU legislation</strong></td>
<td><strong>EU Taxonomy</strong>: all companies concerned by the CSRD will have to report on their alignment with the EU Taxonomy</td>
</tr>
<tr>
<td></td>
<td><strong>SFRD</strong>: the indicators of the standards will be aligned with the reporting of the CSRD</td>
</tr>
<tr>
<td></td>
<td><strong>It takes into consideration other frameworks</strong> (TCDR, GRI, SASB)</td>
</tr>
</tbody>
</table>
## The Top Five Sustainability Frameworks You Should Know

<table>
<thead>
<tr>
<th>STANDARD</th>
<th>FOCUS</th>
<th>WHY REPORT</th>
<th>SCORING</th>
<th>WHO REPORTS</th>
<th>REPORTING PERIOD</th>
</tr>
</thead>
<tbody>
<tr>
<td>CDP</td>
<td>GHG emissions as well as governance actions and business strategies to mitigate climate change and deforestation and promote water security.</td>
<td>CDP holds the largest repository of GHG emissions and energy use data in the world. In 2021, more than 9,900 investors with over US$11 trillion in assets requested companies disclose through CDP. CDP’s transparent scoring methodology helps respondents understand exactly what's expected of them.</td>
<td>Companies are scored based on four criteria: Disclosure, Awareness, Management, and Leadership. CDP recognizes top scoring companies in the Carbon Disclosure Leadership Index (CDLI).</td>
<td>Cities and companies</td>
<td>For companies, CDP’s online reporting system opens in early April and responses are due in late July.</td>
</tr>
<tr>
<td>GRI</td>
<td>Corporate social responsibility with an equal weight on environmental, social, and governance factors. Heavy on stakeholder engagement to determine materiality.</td>
<td>GRI was announced as the official reporting standard of the UN Global Compact, making it the default reporting framework for the compact's more than 5,800 associated companies. It's among the oldest, most widely adopted and most widely respected reporting methodologies in the world. Its thorough focus on social and governance aspects of ESG is unparalleled.</td>
<td>The GRI Standards – A constantly updated set of guidelines focusing on transparency and accountability rather than a set score. Designed to give a high level look as well as a more detailed breakdown depending on your organization’s material topics.</td>
<td>The 2,500 largest public companies in the world.</td>
<td>April 6 - July 13</td>
</tr>
<tr>
<td>GRESB</td>
<td>Environmental, social and governance performance in the global commercial real estate sector only. Includes asset- and entity-level disclosures.</td>
<td>GRESB’s annual survey looks at GRESB’s annual survey the barometer of sustainability performance in the commercial real estate industry. Its niche target audience allows it to give deeper and more accurate insights into industry performance and reveal “investment grade” results.</td>
<td>Private and public institutional investors look at GRESB’s annual survey as the barometer of sustainability performance in the commercial real estate industry. Its niche target audience allows it to give deeper and more accurate insights into industry performance and reveal “investment grade” results.</td>
<td>Anytime, but typically integrated into a company’s traditional annual report</td>
<td>April 1 - June 30</td>
</tr>
<tr>
<td>SASB</td>
<td>Industry-specific standards focus on material aspects of an organization's sustainability performance.</td>
<td>SASB offers disclosure standards for more than 150 industries to ensure information disclosed is most relevant to the financial performance of an organization’s industry. The standards focus on financially material aspects so that the disclosure can help drive business and investment decisions.</td>
<td>SASB Standards offer material information to report and can be used in conjunction with other frameworks.</td>
<td>Any corporation can use SASB to guide its disclosure.</td>
<td>No specific reporting period, but this framework may be complemented by other organizational disclosures.</td>
</tr>
</tbody>
</table>
**EFRAG and European Sustainability Reporting Standards**

- On April 29, 2022, the European Financial Reporting Advisory Group (EFRAG) issued the first draft of sustainability reporting standards for public comment.

- The new rules are part of Europe’s proposed Corporate Sustainability Reporting Directive (CSRD).

- **EFRAG** was established in 2001 by the European Union (EU) and the private sector to provide technical advice to the European Commission on accounting matters.

- Charged with providing input into the development of IFRS sustainability standards.

- **Mission:** to serve the European public interest by developing and promoting European views in financial and sustainability reporting.

- **April 2021:** CSRD proposal, which appointed EFRAG as the technical advisor to the Commission responsible for developing the European Sustainability Reporting Standards (ESRS).

The European Sustainability Reporting Standards (ESRS) were released as a set of exposure drafts that outline reporting requirements across 13 EGS issues, categorized into four areas:

1. **Cross-cutting:** General principles, general, strategy, governance, and materiality assessment.

2. **Environment:** Climate change, pollution, water and marine resources, biodiversity, resource use and circular economy.

3. **Social:** own workforce, workers in the value chain, affected communities, consumers, and end-users.

4. **Governance:** governance, risk management, internal control, and business conduct.
Companies will have to disclose how **sustainability is embedded across the business** and how material ESG impacts, risks, and opportunities are identified and managed.

- This includes policies, targets, action plans, and performance measurement metrics. More details on what will be required are available in EFRAG’s “Appendix I – Navigating the ESRS.”

**A few key features of the ESRS to be aware of include:**

- They may change before being adopted into the final CSRD, pending ongoing legislative negotiations.
- They take existing European law and initiatives into account such as the March 2018 EU action plan financing sustainable growth, SFDR, EU Taxonomy Article 8, the Benchmark Regulation, the GHG allowance Directive, Corporate Sustainability Due Diligence, and more.
- Lessons learned and best practices from European and other international standards and frameworks were considered during development, including those from NFRD, GRI, IFRS, SEC, TCFD, and more.
- They are designed to ensure that sustainability information is reported in accordance with CSRD, can be easily navigated, and has maximum comparability across sectors while allowing flexibility for sector-specific information.
- Audited assurance of reported information will be required.
- Companies will have to prepare the information in a digital format that is machine readable and tagged, so it can be fed into the EU single access point envisioned in the capital markets union action plan.
ESRS Climate Change

Proposed ESRS E1: Climate Change

To enable users of sustainability statements to understand the company’s risks, opportunities, impacts associated with climate change, mitigation efforts aligned with the Paris Agreement, and business plans or actions taken to prevent, mitigate, or remediate adverse impacts.

- General, strategy, governance and materiality assessment — Transition plan for climate change.
- Policies, targets and action plans and resources — Policies to manage climate change, targets for mitigation and adaptation, and associated action plans and resources.
- Performance management — Energy metrics, GHG metrics, taxonomy regulation for climate change mitigation and adaptation, and potential financial effects of material physical and transition risks and opportunities.

Environmental

- Proposed ESRS E2: Pollution
- Proposed ESRS E3: Water and Marine Resources
- Proposed ESRS E4: Biodiversity and Ecosystems
- Proposed ESRS E5: Resource Use and Circular Economy

Cross-Cutting

- Proposed ESRS 1: General Principles
- Proposed ESRS 2: General, Strategy, Governance and Materiality Assessment

Social

- Proposed ESRS S1: Own Workforce
- Proposed ESRS S2: Workers in the Value Chain
- Proposed ESRS S3: Affected Communities
- Proposed ESRS S4: Consumers and End-Users

Governance

- Proposed ESRS G1: Governance, Risk Management and Internal Control
- Proposed ESRS G2: Business Conduct
The image is a diagram illustrating regulatory frameworks and standards for financial and ESG (Environmental, Social, and Governance) reporting across different regions and jurisdictions. It outlines the roles of regulatory bodies such as the SEC and EC, the involvement of the IFRS Foundation and other organizations like IOSCO, and the alignment of voluntary reporting frameworks such as TCFD, GHG Protocol, and SASB. The diagram emphasizes the mandate and mandate-supplemented processes in the regulatory landscape, ensuring compatibility and alignment across various standards and reporting requirements. This infographic is crucial for understanding the complex landscape of financial and sustainability reporting regulations globally.
3. Corporate Sustainability Due Diligence Directive
Due diligence
CSDD Directive

Article 4

Directives

- Bring actual adverse impact to an end
  - Neutralise the identified adverse impact or minimise its extent by developing and implementing a corrective action plan with defined timeline

Due diligence integration

- Embed due diligence requirements on human rights and environment

Adverse impacts identification

- Implement appropriate measures to identify actual or potential adverse impacts on human rights and environment for their own operations or those of their subsidiaries

Prevention of potential adverse impacts

- Take appropriate measures to prevent or adequately mitigate potential adverse impacts on human rights and environment (i.e. prevention action plan development)

Communication

- Publicly communicate on due diligence on 30 April each year - specifications information on the expected description will be clarified in delegated acts.

Monitoring

- Carry out periodic assessment of companies operations or those of their subsidiaries to monitor effectiveness of identification, prevention, mitigation, ending or minimisation of the extent of the human rights and environment adverse impacts.

Complaints procedure

- Provide the possibility for persons or companies to submit complaints with appropriate follow up and competent instances.
Figure 1– EU countries’ national corporate due diligence legislation

Source: Unpacking the upcoming EU law to stop corporate abuse. Press kit, joint NGOs, November 2021
Organisations within the scope of the Proposed Directive will be required to identify, prevent, mitigate and account for their “adverse impacts” on human rights and the environment.

- Adverse impacts as violations of prohibitions, obligations and rights enshrined in the international conventions listed in the Annex to the Proposed Directive.

The Proposed Directive is intended to complement those international conventions and other existing and proposed EU laws and policies on human rights issues. These include:

- forced labour,
- child labour,
- inadequate workplace health and safety, and
- exploitation of workers.

They also extend to environmental issues such as:

- greenhouse gas emissions,
- pollution,
- biodiversity loss and
- ecosystem degradation.
Scope of the Proposed Directive

- The Proposed Directive will apply to the following categories of companies, which is broadly defined and includes regulated financial undertakings (In Scope Companies):

Large companies
- EU companies having more than 500 employees, including part-time and temporary agency workers, and a net worldwide turnover of greater than €150 million in the last financial year for which annual financial statements have been prepared
- Non-EU companies which generated a net turnover of more than €150 million in the EU in the financial year preceding the last financial year

Designated sector companies
- EU companies with more than 250 employees and a net worldwide turnover of greater than €40 million in the last financial year for which annual financial statements have been prepared, provided that at least 50% of that net turnover was generated in one or more of a specified list of high-impact sectors (Designated Sectors)
- Non-EU companies which generated a net turnover of more than €40 million but not more than €150 million in the EU in the financial year preceding the last financial year, provided at least 50% of its net worldwide turnover was generated in one or more Designated Sectors
Obligations
Corporate policies
- In Scope Companies will be required to integrate due diligence into their corporate policies and to adopt a due diligence policy, including a code of conduct for employees and subsidiaries. They must keep it under review and up to date.

Adverse impacts
- In Scope Companies will be required to take “appropriate measures” to (i) identify, (ii) prevent and mitigate and (iii) bring to an end all adverse impacts arising from their own operations, those of their subsidiaries and those of the entities:
  - In their “value chains” ie carrying on activities related to the production of goods or the provision of services, and
  - With which they have an “established business relationship” ie a relationship which is or is expected to be lasting in view of its intensity or duration and is not a negligible or ancillary part of the value chain
- “Appropriate measures” will vary on a case-by-case basis having regard to the severity and likelihood of the adverse impact. However, they can be far-reaching and may result in significant expense and administrative burden for an In Scope Company. They may include, for example, a requirement for an In Scope Company to:
  - Develop and implement prevention and/or corrective action plans
  - Seek contractual assurances from the business partners with which it has an established business relationship to ensure compliance with the In Scope Company’s code of conduct and any prevention and/or corrective action plans. They must also monitor compliance with those contractual assurances.
  - Make necessary investments, for example into management or production processes and infrastructures
  - Provide targeted and proportionate support to SMEs with which it has an established business relationship where compliance by the SME with the In Scope Company’s code of conduct and any prevention and/or corrective action plans would jeopardise the viability of the SME
- In the case of identified actual adverse impacts, pay damages and financial compensation to affected persons and communities, and
- Suspend or terminate relevant business relationships where adverse impacts are severe and have not been prevented, adequately mitigated or brought to an end by other measures
4. Recap
HOW THE EU CSDD AND CSRD INTERACT

**CSDD**
- Mandatory due diligence
- Companies must implement regarding human rights and environmental impacts along their supply chains

**EU**
- UN Guiding Principles on Business and Human Rights (UNGPs)
- the OECD Guidelines for Multinational Enterprises (OECD Guidelines)

**CSRD**
- Reporting vehicle by which companies will report their relevant sustainability activities
Keep in touch

www.lelamelon.eu
lela.melon@upf.edu;
lela.melon@esci.upf.edu
LinkedIn: Lela Mélon
Twitter: @melonlela
Thank you