



## **EU publishes exposure drafts of sustainability standards for consultation**

Proposals cover all aspects of environmental, social and governance (ESG) reporting

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- What companies would be impacted?
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# EU publishes exposure drafts of sustainability standards for consultation

The European Union (EU) has issued a set of 13 [exposure drafts](#) of European Sustainability Reporting Standards (ESRSs) for companies located in EU member states. These standards would introduce extensive new disclosure requirements and would apply to most listed and large companies located in the EU, including 'large' (as defined) European subsidiaries of foreign parent companies.

Legislative procedures are still in process but current proposals aim for initial application for reports published on or after 1 January 2025, with a requirement for limited assurance initially and reasonable assurance after six years.

“The EU is joining the ISSB and SEC by publishing exposure drafts for sustainability reporting. By aiming to deliver public policy objectives in addition to serving the information needs of capital markets, these latest drafts go beyond the scope of the other standard setters.”



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## What are European Sustainability Reporting Standards?

In April 2021, the European Commission adopted the proposal for a Corporate Sustainability Reporting Directive (CSRD). One of the proposals in the CSRD is to introduce the requirement for companies to report sustainability information based on European Sustainability Reporting Standards (ESRSs). ESRSs are to be developed by the European Financial Reporting Advisory Group (EFRAG) and adopted by the European Commission.

The CSRD, if adopted as proposed, requires EFRAG to draft, and the European Commission to finalise, an initial set of ESRSs by 31 October 2022 and further sector-specific standards by 31 October 2023.

In response, EFRAG set up various working groups to do the ground work on the draft standards. These have now been issued formally by the newly created EFRAG Sustainability Reporting Board as exposure drafts for public consultation.

## What companies would be impacted?

Under the most recent CSRD proposal, companies that are currently obliged to report under the Non-Financial Reporting Directive (NFRD) – i.e. large public-interest companies with more than 500 employees – would be required to report in accordance with ESRSs in reports published on or after 1 January 2025 (e.g. those covering reporting periods ending on 31 December 2024). This scope is then set to expand to ultimately cover all large and most listed companies (in reports published on or after 1 January 2027). Large companies are defined as those that meet two of the following criteria:

- over 250 employees;
- over €40 million net revenue; and
- over €20 million total assets.

## What has been proposed?

The 13 proposed ESRs cover:

- one standard on general principles for sustainability reporting;
- one standard on overarching disclosure requirements; and
- specific disclosure requirements focused on eleven ESG topics.

Under the proposals, companies would have to publish separate sustainability statements as part of their management reports containing sector-agnostic, sector-specific and company-specific disclosures.

The exposure drafts organise the sustainability statements as follows.

<p><b>Disclosure topics</b></p>	<p>Exposure drafts were issued for the sub-topics:</p> <p><b>(a) Environmental matters:</b></p> <ul style="list-style-type: none"> <li>▪ Climate change;</li> <li>▪ Pollution;</li> <li>▪ Water and marine resources;</li> <li>▪ Biodiversity and ecosystems; and</li> <li>▪ Resource use and the circular economy.</li> </ul> <p><b>(b) Social matters:</b></p> <ul style="list-style-type: none"> <li>▪ Own workforce;</li> <li>▪ Workers in the value chain;</li> <li>▪ Affected communities; and</li> <li>▪ Consumers and end users.</li> </ul> <p><b>(c) Governance matters:</b></p> <ul style="list-style-type: none"> <li>▪ Governance, risk management and internal controls; and</li> <li>▪ Business conduct.</li> </ul>
<p><b>Areas of disclosure for all topics</b></p>	<ul style="list-style-type: none"> <li>▪ Strategy and business model, governance and organisation, and impacts, risks and opportunities</li> <li>▪ Implementation measures covering policies, targets, actions and action plans, and allocation of resources.</li> <li>▪ Performance measurement.</li> </ul>
<p><b>Conceptual guidelines in preparing sustainability reporting</b></p>	<ul style="list-style-type: none"> <li>▪ Characteristics of information quality such as relevance, faithful representation, comparability, verifiability and understandability.</li> <li>▪ The double materiality concept, which includes the concepts of <i>impact materiality</i> and <i>financial materiality</i> in the preparation of the sustainability report. These concepts are defined differently from the (<i>financial</i>) <i>materiality</i> that is used in the preparation of the financial statements.</li> <li>▪ Reporting boundaries and consideration of the value chain both upstream and downstream, and the level of disaggregation.</li> <li>▪ The time horizons used for reporting on sustainability matters (such as short-, medium- and long-term).</li> </ul>

Sector-specific standards would be developed by EFRAG for adoption by the European Commission in 2023.

## How would ESRs interact with international standards?

By adopting double materiality principles, the proposed ESRs consider a wider range of stakeholders than IFRS® Sustainability Disclosure Standards or the US Securities and Exchange Commission (SEC) [published proposal](#). They aim to meet public policy objectives as well as meet the needs of capital markets.

It is the International Sustainability Standards Board's (ISSB™) [aim](#) to create a global baseline for sustainability reporting standards that allows local standard setters to add additional requirements (building blocks), rather than face a coexistence of multiple separate frameworks. EFRAG has published a comparison against the ISSB Board's proposals and committed to join an ISSB Board working group to drive global alignment. However, in the short term, companies and investors may potentially have to deal with three sets of sustainability reporting standards in setting up their reporting processes, controls and governance.

### *Key differences*

- The proposed ESRs list detailed disclosure requirements for all ESG topics. The proposed IFRS Sustainability Disclosure Standards would also require disclosure in relation to all relevant ESG topics, but the ISSB Board has to date only prepared a detailed exposure draft on climate, asking preparers to consider general requirements and other sources of information to report on other sustainability topics. The SEC focused on climate in its recent proposal.
- The proposed ESRs are more prescriptive and the number of disclosure requirements significantly exceeds those in the proposed IFRS Sustainability Disclosure Standards.
- While the proposed IFRS Sustainability Disclosure Standards are intended to focus on the information needs of capital markets, ESRs also aim to address policy objectives of the EU by addressing wider stakeholder needs.

Appendices to the cover letter of the exposure drafts contain a comparison of disclosure requirements – where applicable – in the proposed ESRs and

- the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD); and
- the proposed IFRS Sustainability Disclosure Standards.

## What does this mean for you?

Companies should start thinking about the effects that the standards would have on processes and systems of internal controls to ensure that sustainability information is equivalent in terms of quality as financial information and could be audited initially with limited and later reasonable assurance.

Have your say on the exposure drafts by sharing your comments with EFRAG by the comment letter deadline of 8 August 2022.



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