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ESG Essentials

Your Guide to EU Reporting

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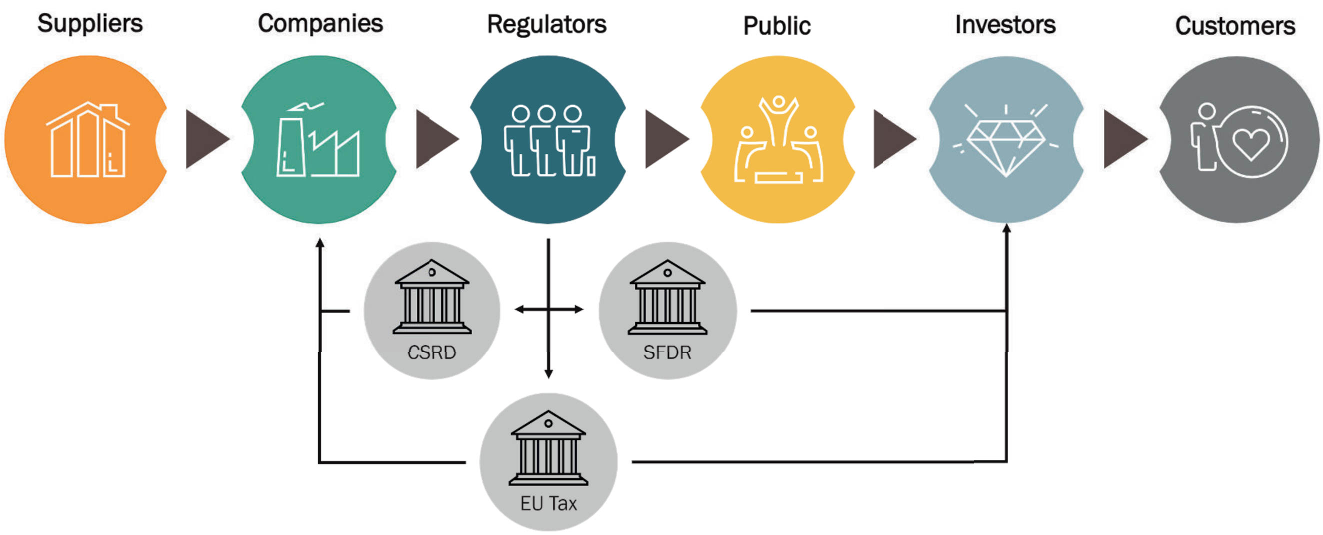
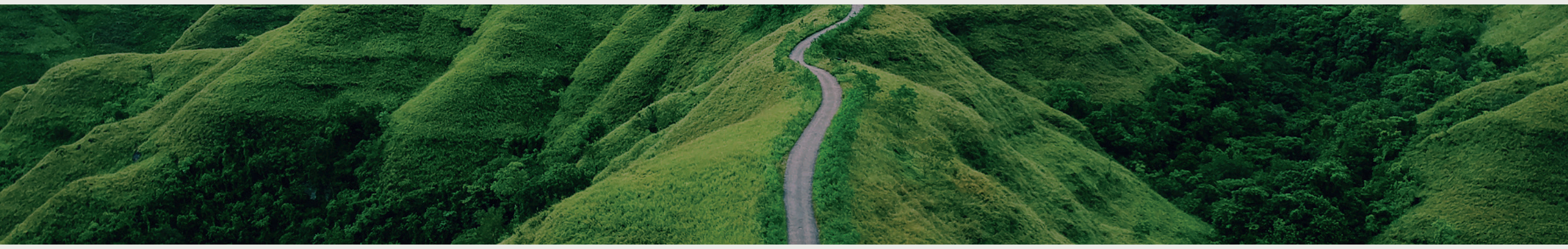
The preparation of a report on the financial situation of a company as a balance sheet or income statement is a standard process. However, ESG reporting obligations present a different challenge: Although figures also play a role here, the focus is primarily on non-financial performance information. In contrast to traditional accounting, the know-how of managers and staff is limited. Companies across Europe and the European Union are increasingly recognizing the need to change this, as corporate ESG reporting is about to be standardized. Capital market-oriented companies are in the lead with regards to ESG reporting. In this whitepaper, you will learn to understand the new ESG reporting obligations, who must comply, and how they can be implemented.

ESG Reporting: An Introduction

Because Progress in the field of ESG (Environment, Social and Governance) must be made measurable and transparent, companies already had to document some of their efforts in the past. To ensure comparable reporting within the EU, the European Union has created the **Corporate ESG Reporting Directive (CSRD)** as a central building block. This directive is part of the European strategy to create a sustainable economic and financial system and presents disclosure obligations for ESG information. The binding **European ESG Reporting Standards (ESRS)** regulate what exactly must be reported. Internationally active companies still use the **Global Reporting Initiative (GRI)** which can be the guiding source for reporting in accordance with the CSRD.



ESG-regulations lead to an exchange of information throughout the value chain. Besides the above mentioned further are applied/upcoming.



Since 2017, capital market-oriented companies with more than 500 employees have been obliged to include a non-financial statement on the impact of their business activities in their management reports. The comprehensive CSRD reporting obligation is a response to the business sector's relevance to the UN's 17 Sustainable Development Goals and the Paris Climate Agreement. Additionally, extended and more precise transparency requirements like the planned European Corporate **Sustainability Due Diligence Directive (CSDDD)** bring fair market conditions for ESG further within reach. However, based on the Green Deal there are further reportings relevant to companies like the **EU Taxonomy,** which will be discussed here as well. In addition, some companies are already urged to comply and report on the **Carbon Border Adjustment Mechanism (CBAM)** and **Sustainable Finance Disclosure Regulation (SFDR)**, which is a binding obligation for financial institutions.

ESG reporting is a comprehensive and regularly recurring process. It offers the opportunity to highlight topics that are closely linked to the development of the company and its future viability and goes beyond purely financial reporting. In the long run, the ESG report will be part of the annual management report as an integrated report.

CSRD is a central obligation

CSRD is not a simple undertaking. The aim of the CSRD is, among other things, to publish sufficient ESG-related information for all stakeholders so that they have a solid information basis for their decision-making on the capital market. A certain degree of comparability and reliability of non-financial reporting is essential for this. For this reason, overarching and technical standards have been defined in the ESRS. On the reporting level, the information needed results in a high effort in recording the necessary data.

Who must report?

Whether the ESG report is at the top of the agenda, is being planned or has already been prepared voluntarily - the European Union has set the timetable but not all companies are immediately obliged to prepare an ESG report. Initially, mainly large capital market-oriented companies are subject to this obligation, but in future many more companies will have to meet the EU`s ESG reporting requirements. From a current point of view the CSRD will affect 15,000 companies in the EU. Small and medium-sized companies should be warned as they may be required to do so earlier, especially if they are a supplier or service provider in the supply chain of a large enterprise that is required to report in the near future. The implemen-

tation of the regulations and thus the reporting obligation in accordance with the CSRD will be rolled-out over several years and, will affect approx. more than 15,000 companies in Germany alone by 2028.

Integrating ESG Management in your Organization

Even if companies have different organizational structures and processes, responsibilities must be clearly defined, whether ESG management is the responsibility of the management, a business unit or an individual. So far, there is no one-size-fits-all approach or a single organizational form, as can be seen in the variety of positions and organizational structures that exist in companies. The different ways in which ESG is implemented in the company also go hand in hand with different definitions of the basic competencies that are required. However, possible areas of responsibility include the management & board, an independent ESG department, a cross-functional ESG committee, a project team, the workforce or external advisory boards.

The choice of implementation allows conclusions to be drawn about the firm's ambitions and motivations, for example concerning whether ESG is established as a strategic core element. In this context, questions about the planned resources and the available and required competencies are crucial.

Regardless of the organizational implementation, the topic requires strong cross-functional integration. Interdisciplinary work is needed, ideally with support from the management level.

Materiality Analysis as a Milestone

The materiality analysis plays a crucial role in determining which topics are important and are to be reported. It is therefore a key component of the ESG report. Its aim is to identify and evaluate various ESG topics and determine their relevance for the company and its stakeholders. The impacts, opportunities and risks are examined in more detail. At the end of the materiality analysis, there is a list or matrix of the key ESG topics that the company should report on.

The Double Role of Financials

Even when non-financial performance information needs to be reported, the financial perspective is not completely ignored. In the European context, the dual materiality is often discussed in connection with materiality analysis. The ESRS divides materiality into a financial perspective and a social and environmental impact perspective.

From a financial perspective, it is important to examine the impact that climate change or resource scarcity, for example, have on the companies success and future cash flows. Anything that influences the value of the company should be considered material.

On the other hand, transparent communication and progress give companies access to more favorable conditions on the capital market. Investors such as banks are also obliged to report on ESG within the framework of the EU. These players must evaluate their assets in terms of ESG, which motivates them to have as many "sustainable" assets as possible on their balance sheets.

EU Taxonomy as a Guardrail

With the **Taxonomy Regulation**, the EU has created another key building block for the transformation of the economy towards a sustainable future. This regulation provides a standardized system for determining whether an economic activity can be classified as environmentally sustainable. For this, an economic activity such as an investment must make a significant contribution to one of six environmental objectives and at the same time not compromise one or more of these objectives. The transition to a circular economy, for example, is aimed at avoiding waste and recycling. The focus here is on resource and energy efficiency as well as the durability and reparability of products.

Outlook

Creating an ESG report requires the cooperation of an entire company and all stakeholders. Information and knowledge about ESG issues can be found in all areas and departments. This is a long-term process, not a sprint: the preparation of a first ESG report usually takes over a year from preparation to completion. Soon, this process will become an annual obligation for all companies, requiring preparation and organization. Once the foundation has been laid and the awareness of ESG is anchored in the company, reporting can become a standard process over time. At cbs, we support you on this path. Together with you, we derive strategic goals and translate the requirements from the departments into a technological basis. We use your existing organization and strategy as a starting point. We transform the requirements into processes and tools and implement the necessary solutions. In this way, we accompany you on your way to ESG reporting.

Do you want to learn how you can embed ESG in your technological architecture? Book a slot for our Awareness Workshop to discuss with one of our experts.

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