



Need to know

European Commission consults on delegated regulation for European Sustainability Reporting Standards

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This *Need to know* outlines the **consultation** launched by the European Commission (EC) on 9 June 2023 on the draft delegated regulation that supplements the Accounting Directive (Directive 2013/34/EU of the European Parliament and of the Council) for sustainability reporting standards.

- The EC is consulting on a draft regulation to specify the text of European Sustainability Reporting Standards (ESRS) which are to be mandatory for entities, as specified in the Corporate Sustainability Reporting Directive (CSRD)
- The EC has modified the draft ESRS submitted by EFRAG in November 2022 to include:
 - Changes to the materiality approach
 - Further phasing-in of certain requirements
 - The conversion of certain requirements into voluntary datapoints
 - Flexibility in relation to how certain disclosure requirements can be met
 - Technical adjustments to ensure coherence with the EU's legal framework
 - Changes aimed at further interoperability with global standard-setting initiatives
- The draft regulation indicates that ESRS would apply for financial years beginning on or after 1 January 2024 for entities already subject to the Non-financial Reporting Directive (NFRD)
- The draft regulation is open for feedback until 7 July 2023

Background

The EU Accounting Directive (as amended by the Corporate Sustainability Reporting Directive (CSRD)) requires certain entities to include in a dedicated section of their management report the information necessary to understand the entity's impacts on sustainability matters and how sustainability matters affect the entity's development, performance and position.

For more information please see the following websites:

www.ukaccountingplus.co.uk

www.deloitte.co.uk

The CSRD specifies which entities are in scope and the financial year in which they are first required to provide sustainability information. The scope of the CSRD is wide and includes both EU and certain non-EU entities.

For further detail on scope and effective dates, see our [Need to know—Worldwide reach of the Corporate Sustainability Reporting Directive—final text published in Official Journal](#).

The EC is required to adopt sustainability reporting standards specifying the information that entities are to report in accordance with the CSRD. **Draft European Sustainability Reporting Standards (ESRS)** have been developed by EFRAG and were submitted to the EC in the form of technical advice in November 2022. The EC consulted with various European agencies and other stakeholders and made further amendments to these draft ESRS before publishing the draft regulation.

Observation

The EC indicates that consultations undertaken confirmed that the draft ESRS broadly meet the mandate of the CSRD and would achieve the intended policy goals in the context of the European Green Deal. At the same time, some respondents drew attention to the challenging nature of many of the disclosure requirements for many entities, and in particular for entities that have not previously been subject to legal requirements to report sustainability information.

In addition, as part of the EC's request to the European Supervisory Authorities (ESAs) to provide an opinion on the draft ESRS, the European Insurance and Occupational Pensions Authority (EIOPA) underlined the importance of avoiding fragmentation of sustainability reporting requirements across jurisdictions. To this end, they stated that compatibility between ESRS and IFRS Sustainability Disclosure Standards should be ensured so that European entities reporting according to ESRS are automatically considered to be compliant with IFRS Sustainability Disclosure Standards.

Implication for UK companies

The CSRD will directly affect UK companies if they have securities (shares or debt) listed on EU regulated markets or if they generate more than EUR 150 million net turnover in the EU (for each of the last two consecutive financial years) **and** have at least one EU subsidiary (large or listed on an EU regulated market) or EU branch (more than EUR 40 million net turnover in the preceding financial year). It will also apply directly to EU subsidiaries of UK companies. This may be as soon as periods commencing on or after 1 January 2024 for UK companies with securities listed on an EU regulated market and that have more than 500 employees.

In April 2023, the UK government published a new policy paper, **Green Finance Strategy—Mobilising Green Investment** (“the 2023 Strategy”), building on the previous Green Finance Strategy which was published in July 2019. The 2023 Strategy re-emphasises the government's commitment to the sustainability disclosure requirements (SDR) set out in its **Greening Finance: Roadmap to Sustainable Investing**, published in October 2021, including its support for UK adoption of the standards being finalised by the ISSB and the development of an endorsement mechanism. The UK has already taken a number of steps in developing the SDR, including the Financial Conduct Authority (FCA)'s Listing Rule for premium and standard listed companies to make disclosures consistent with the TCFD Recommendations, and government legislation to require certain AIM listed and unlisted companies and LLPs to include climate-related financial disclosures in their annual report.

The UK government aims to introduce the SDR in a way that complements the UK's wider non-financial reporting framework, minimises duplication with other forms of corporate reporting and gives businesses enough time to implement the new requirements. However, where the requirements of the CSRD go beyond the reporting requirements in the UK, additional disclosures will need to be made by UK companies in scope of the CSRD to comply with EU requirements. The additional disclosures could be significant, particularly for companies required to apply full ESRS. Furthermore, the disclosure will be subject to mandatory assurance.

Determining whether a company or its subsidiary is in scope and if so, at what level it is required to report, which sustainability reporting standards apply (ESRS, standards for third country undertakings, simplified standards for SMEs, or standards deemed equivalent to ESRS), and from what date, is complex. Given the extensive disclosure requirements, UK companies should consider how the CSRD may impact them early. This extends to consideration of other EU Regulations, such as the EU Taxonomy Regulation which introduces disclosures for companies in scope of the CSRD. Under the EU Taxonomy Regulation, non-financial undertakings must disclose “green” turnover, capex and opex indicators and financial undertakings need to disclose ratios relevant to their industry that relate to the proportion of environmentally sustainable economic activities in their financial activities, such as lending, investment and insurance. Determining what activities are “green” according to the specific technical screening criteria associated with the EU Taxonomy Regulation is not straightforward and will require careful consideration.

For further information, please see:

- [Need to know](#) discussing the final text of the CSRD
- [Need to know](#) discussing the UK Government's Green Finance Strategy—Mobilising Green Investment

The draft regulation

To ensure entities disclose relevant, comparable and reliable information on all major sustainability-related topics, the CSRD requires entities within its scope to use ESRS that specify the information to report and, where relevant, specify the structure in which that information should be reported. The draft regulation applies to the first set of sector-agnostic ESRS developed by EFRAG. The additional standards to be developed by EFRAG (i.e. sector-specific standards, standards for listed SMEs and a standard for third-country undertakings) will be adopted through additional delegated acts.

The draft regulation includes the text of the ESRS in two annexes to the draft regulation. Annex I to the draft regulation includes the text of the ESRS, while Annex II includes acronyms and definitions.

The regulation would enter into force four months after the date of adoption. The regulation, and therefore the ESRS, are applicable for financial years beginning on or after 1 January 2024 in line with the requirements in the CSRD. The regulation would be binding in its entirety and directly applicable in all Member States.

The draft regulation is open for feedback until 7 July 2023. Feedback will be taken into account for finalising the draft regulation.

Observation

After the feedback period ends, it is expected that the regulation will be agreed by the EC before the end of August 2023. The scrutiny period by the European Parliament and the European Council would then begin and last for two months (with another possible two-month extension). It is necessary that this timeline is adhered to for ESRS to become effective from 1 January 2024.

Changes to draft ESRS submitted to the EC by EFRAG

To facilitate the correct application of the standards by entities, the EC has introduced modifications to EFRAG's technical advice in the following areas.

Materiality

The draft ESRS submitted to the EC by EFRAG required that, irrespective of the outcome of the materiality assessment, all information required by ESRS 2 *General disclosures* and ESRS E1 *Climate change* should be disclosed, together with certain requirements in ESRS S1 *Own workforce* for certain entities, and datapoints in cross-cutting and topical standards that are required by EU law which stem from other EU legislation.

The EC has changed this in the draft regulation, so that all disclosure requirements and datapoints within each standard will be subject to materiality assessment, except for the disclosure requirements specified in ESRS 2. The EC expects that this measure will lead to a significant reduction in the reporting burden for entities.

Observation

The essential objective of the standards referred to in ESRS 1 *General requirements* continues to be to “specify the information that an undertaking shall disclose about its material impacts, risks and opportunities in relation to environmental, social, and governance sustainability matters”. In addition, the double materiality perspective is retained.

Phasing-in of certain requirements

In addition to the phasing-in of certain requirements proposed by EFRAG, the EC has provided for further phasing-in for all entities in scope with extra reliefs available for entities with less than 750 employees. These are as follows:

	In the first year an entity applies ESRS	In the first two years an entity applies ESRS
Information all entities may omit	Anticipated financial effects related to non-climate environmental issues (pollution, water, biodiversity, and resource use)	
	Certain datapoints related to own workforce (social protection, persons with disabilities, work-related ill-health, and work-life balance)	
Information entities with fewer than 750 employees may omit	Scope 3 GHG emissions data as specified in ESRS E1	The disclosure requirements in ESRS E4 <i>Biodiversity and ecosystems</i> , ESRS S2 <i>Workers in the value chain</i> , ESRS S3 <i>Affected communities</i> and ESRS S4 <i>Consumers and end-users</i>
	The disclosure requirements in ESRS S1	

Making certain disclosures voluntary

Each disclosure requirement in ESRS consists of one or more distinct datapoints. The term “datapoint” can also refer to a narrative sub-element of a disclosure requirement.

The draft standards submitted by EFRAG already included many voluntary datapoints. In addition to those, the EC has made voluntary several mandatory datapoints proposed by EFRAG. This includes, for example:

- Biodiversity transition plans
- Certain indicators about “non-employees” in the entity’s own workforce
- An explanation of why the entity may consider a particular sustainability topic not to be material

Further flexibilities in certain disclosures

The EC has also introduced additional flexibility with regard to how to meet some requirements. For example, in the following areas:

- Disclosure requirement on financial effects arising from sustainability risks
- Disclosure requirement on engagement with stakeholders
- Methodology to use for the materiality assessment process

Furthermore, the EC has modified datapoints regarding corruption and bribery, and the protection of whistle-blowers.

Coherence with EU legal framework

The EC made technical modifications to ensure better alignment with other provisions in the Accounting Directive and with other relevant parts of EU legislation, for example on the Pay Transparency Directive and the European Pollutant Release and Transfer Register.

Interoperability with global standard-setting initiatives

The EC and EFRAG have continued to engage closely with the International Sustainability Standards Board (ISSB) and the Global Reporting Initiative (GRI) to enhance interoperability with ESRS, and further modifications to the draft ESRS have been made because of that engagement.

Observation

The EC made changes aimed at facilitating interoperability of ESRS with IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* and IFRS S2 *Climate-related Disclosures*, which the ISSB expects to publish on 26 June 2023. The objective of these changes is to avoid creating a double reporting burden for entities that apply ESRS at the same time as IFRS S1 and IFRS S2.

Editorial and presentational modifications

The EC has made editorial and presentational changes to improve the clarity, usability, and coherence of the standards. This includes, for example, the introduction of a drafting convention to clearly identify all terms for which ESRS includes a precise definition.

Further information

If you have any questions about the draft regulation, please speak to your usual Deloitte contact.

The Deloitte Accounting Research Tool (DART) is a comprehensive online library of accounting and financial disclosures literature.

GAAP in the UK on DART allows access to the full IFRS Standards and UK GAAP, linking to and from:

- Deloitte’s authoritative, up-to-date, GAAP in the UK manuals which provide guidance for reporting under IFRS Standards and UK GAAP
- Model financial statements for entities reporting under IFRS Standards and UK GAAP

In addition, our **sustainability reporting** volume of GAAP in the UK provides guidance on disclosure requirements and recommendations which businesses must consider in light of the broader environmental, social and governance matters which can significantly drive the value of an entity.

To apply for a subscription to GAAP in the UK on DART, click [here](#) to start the application process and select the GAAP in the UK package.

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