Mandatory ESG reporting is progressing, bringing new responsibilities for audit committees

Mandatory ESG reporting is progressing, and audit committees will be pivotal to compliance

By Dave Power and Michael Ort

Mandatory ESG reporting requirements are in effect for many organizations operating in Europe and are being finalized in other jurisdictions, including Canada. Now is the time for organizations to develop detailed written plans, assess the need for external resources and prepare for compliance with new reporting requirements. Audit committees are an integral part of the reporting process and are well placed to ensure their organization is prepared to comply in advance of the effective dates.

Similarly, new government regulations are also putting pressures on organizations to curb greenwashing. For example, under the anti-greenwashing amendments to the Competition Act (Bill C-59), organizations must now prove their environmental claims regarding their products and services with proper tests and follow international standards for operational-related claims, including net-zero commitments. This applies to both Canadian companies making statements in Canada or other countries, and foreign companies making statements in Canada. Failure to do so can result in severe financial penalties and reputational harm. Importantly, the Competition Bureau has also signalled that ESG content in securities disclosures constitute "promotion" for the purposes of the Competition Act as amended by Bill C-59.

The need to be prepared for mandatory ESG reporting cannot be overstated. Audit committees have an opportunity to take a lead role by challenging management to prepare for timely compliance with the new requirements.

Final standards have been released

In 2023, the EU's Corporate Sustainability Reporting Directive (CSRD) came into force,

> It is crucial to be prepared for new and evolving reporting requirements. Audit committees have an opportunity to proactively challenge management to ensure compliance with the requirements in a timely manner.

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meaning that certain EU and non-EU companies with ties to the EU will be required to report on multi-stakeholder focused sustainability topics, according to the European Sustainability Reporting Standards (ESRS). Under the ESRS reporting framework, large and listed EU-based organizations must report on ESRS in the management report at the level of the legal entity, or on a consolidated basis, depending on a variety of factors. Parent companies of EU-based entities scoped in by CSRD will need to report on reduced non-EU parent standards (standards to be published in 2026) at the global group level. Non-EU small- and medium-sized businesses (SMBs) which are listed on the EU exchanges will be required to report in the management report on a specific, simplified set of standards at the level of the legal entity.

The Canadian Sustainability Standards Board (CSSB) released its first two Canadian Sustainability Disclosure Standards (CSDS) in December 2024. The standards are available for use in reporting on a voluntary basis for periods beginning on or after January 1, 2025.

The Canadian Securities Administrators (CSA) will ultimately decide whether the standards (in part or entirely) should be mandated and, if so, who will need to apply the standards and over what time frame. A statement issued by the CSA in March 2024 noted they anticipate initially adopting only those provisions of the sustainability standards that are necessary to support climate-related disclosures.

Management should have a roadmap to compliance

Uncertainty around the timing of formal ESG reporting requirements, combined with the need to prioritize resources for other business initiatives, has led some organizations in Canada to delay their preparations. However, organizations in other jurisdictions that commenced their reporting readiness process years in advance have still faced significant challenges in meeting deadlines. Preparing for mandatory ESG reporting is a substantial undertaking, requiring comprehensive data collection across multiple domains, rigorous analysis of that data and the development of robust reporting systems to meet the evolving expectations of regulators, investors and other stakeholders.

To ensure successful implementation of the standards, audit committees should encourage management to create a detailed written roadmap to meet the deadlines for compliance. A successful roadmap will have five stages: establish, assess, design, implement and sustain. The process begins with establishing the regulations that are applicable to the organization in all jurisdictions in which it operates and determining the material topics that must be addressed. Next, the organization must assess where it currently stands on ESG reporting and whether it has the proper operating model,

> Organizations cannot leave mandatory ESG reporting preparedness to the last minute. We've learned from other jurisdictions that companies that successfully migrate to mandatory reporting start years ahead. Audit committees should ensure management has a roadmap in place to meet the new reporting requirements.

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Questions audit committees should be asking:

- Are we clear on the ESG requirements for the organization?
- What have we done to date to prepare for ESG reporting and assurance?
- Does the organization have a roadmap for implementation? If not, when will this be ready?
- Does management have sufficient expertise to evaluate the reporting requirements? If not, how do we get it?

including the right people, processes, technology and controls in place. Management should update the audit committee regularly on their progress to achieve the roadmap.

Organizations can benefit from identifying needed resources and securing them early. Organizations that discover they lack the internal resources required will find it easier to secure limited and highly sought-after external resources if they start early. Audit committees should inquire of management about their efforts to promptly identify and secure the required resources.

The design and implementation stages of the roadmap propel the organization through necessary changes required to be compliant with the standards, identifying what adjustments and amendments are needed to existing reporting processes to meet future regulatory requirements. Even companies that are already voluntarily reporting ESG information may need to implement significant changes as a result of the adoption of mandatory standards.

Lastly, sustaining and maintaining a new operational model could entail an annual assurance process. It will also mean keeping abreast of evolving regulatory changes. To date, standards have primarily been focused on climate, but global standard setters have intentions of drafting future standards for biodiversity, water and social issues, as a starting point. Audit committees will want to ensure that management is keeping up to date with emerging standards.

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