A quick guide for corporates

The EU Taxonomy and the Corporate Sustainability Reporting Directive (CSRD)

April 2022
The foundations for sustainable finance in EU

In the context of EU’s policy, sustainable finance is understood as finance to support economic growth while reducing pressures on the environment and taking social and governance aspects into account. Sustainable finance is an essential part of the European Green Deal. The EU sustainable finance action plan contains a list of actions to ensure businesses to have access to new sources of funding through global capital markets and the financial sector worldwide.

1. EU Taxonomy
   A common classification of economic activities substantially contributing to environmental objectives, using science-based criteria.
   — Taxonomy Regulation adopted on June 18, 2020

2. Disclosures
   Comprehensive disclosure regime for both non-financial and financial institutions to provide investors with the information necessary to make sustainable investment choices.
   — Sustainable Finance Disclosure Regulation (SFDR) applies since March 10, 2021
   — Corporate Sustainability Reporting Directive (CSRD) proposed by the Commission in April 2021
   — Sustainability Preferences (MiFID II) adopted by the Commission in April 2021

3. Tools
   Broad toolbox for companies, market participants and financial intermediaries to develop sustainable investment solutions, while preventing ‘greenwashing’.
   — EU Climate Benchmark Regulation applies since April 2020
   — European green bond standard (EUGBS) proposed by the Commission in July 2021

Adapted from the European Commission, Goldman Sachs Global Investment Research
# How the EU sustainable finance framework affects disclosures

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<tbody>
<tr>
<td><strong>Scope</strong></td>
<td>Asset Managers</td>
<td>Corporates</td>
<td>Asset Managers</td>
<td>Corporates &amp; Asset Managers</td>
</tr>
<tr>
<td></td>
<td>Financial market participants offering investment products and financial advisers</td>
<td>All large EU companies and all listed in the EU companies (except listed micro enterprises), around 49,000 corporates (potentially including private companies)</td>
<td>Financial market participants; investment advisors, asset managers, etc.</td>
<td>Financial market participants; all companies subject to CSRD</td>
</tr>
<tr>
<td><strong>Disclosure</strong></td>
<td>Entity and product level disclosure on sustainability risks and Principal Adverse Impacts (PAIs)</td>
<td>Report on the basis of formal reporting standards and subject to external audit</td>
<td>Suitability disclosure rule for financial institutions to raise awareness and promote transparency of ESG products to clients</td>
<td>Turnover, capital and operating expenditures in the reporting year regarding products or activities associated with Taxonomy</td>
</tr>
<tr>
<td><strong>Status</strong></td>
<td>Effective as of March 10, 2021</td>
<td>Under negotiation; expected to apply from 2023</td>
<td>Applies one year after being officially published (Q4, 2022)</td>
<td>Applies from January 2022</td>
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</table>
The EU Taxonomy regulation for corporates at a glance

The EU Taxonomy came into force on July 12, 2020, offering a classification system for companies and investors to determine whether an economic activity is ‘green’ or not.

For the reporting year 2021, companies will have to present the proportion of Taxonomy-eligible and Taxonomy non-eligible activities in their total CAPEX, OPEX and turnover. For the reporting year 2022 and onwards, companies will have to disclose their taxonomy alignment on CAPEX, OPEX and turnover.

**Timeline**

- **April 2021**: Corporate Sustainability Reporting Directive (CSRD) communicated by the EU Commission
- **Q1 2022**: Disclosures for activities related to climate change mitigation and adaptation
- **2022**: Publication of remaining four delegated acts
- **Q1 2023**: Disclosures for activities related to all six environmental objectives
Disclosures for activities related to climate change mitigation and adaptation

**Who should disclose?**

All companies that are required to provide a non-financial statement under the Non-Financial Reporting Directive (NFRD)*

*Currently this includes large PIES of 500+ employees. The CSRD will replace the NFRD and will include all large companies (meeting at a minimum two criteria of 250+ employees, EUR 40 mln turnover, EUR 20 mln assets) and will come into effect as of reporting year 2023.

**How and what to disclose?**

- Identify eligible activities against the classification system
- Test for alignment based on the Technical Screening Criteria, DNSH criteria, and compliance with minimum social safeguards

**For eligible and aligned activities**

- Turnover %
- CAPEX %
- OPEX %

**Did you know...**

- Additional screening criteria for No Significant Impact (NSI) and Significant Harm (SH) are to be developed
- Additional granularity within screening criteria ‘Shades of Green’ might be added (e.g. levels of performance vs ‘in-or-out thresholds’)
- Additional delegated acts on social aspects are expected: From compulsory dictionary for ‘E’ to dictionary for ‘E+S’ ‘social taxonomy’
Key implementation challenges

Operational impact
What will the administrative burden be for the company and how well equipped are our systems?

Reporting alignment
How can we integrate EU Taxonomy reporting into existing processes and align it with other frameworks, such as TCFD?

Change story
How can we use the EU Taxonomy as a tool to further shape and support our change story?

Data availability
How easy is it to retrieve the required data and what changes are needed to our systems over time?

CAPEX, OPEX and turnover definition
How will we apply the definitions to our data and ensure they align with our current financial reporting?

Strategic steering
How will the EU Taxonomy shape our strategic decisions, e.g. regarding investments and how do we communicate on this topic?
KPMG can support you with your EU Taxonomy challenges

<table>
<thead>
<tr>
<th>VALUE FOR YOU</th>
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<tbody>
<tr>
<td><strong>KPMG has a standardized EU Taxonomy approach based on conversations with many clients</strong></td>
</tr>
<tr>
<td>As experienced providers of advisory and assurance services, KPMG has been one of the first organizations to help companies map their activities for EU Taxonomy alignment, support disclosure and reporting, and provide assurance on EU Taxonomy information in reports. Based on the numerous (international) client conversations and engagements, KPMG has developed a standardized approach that addresses the key questions clients pose. The approach can be tailored to best address a specific ask.</td>
</tr>
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| KPMG professionals can bring in and leverage practical knowledge from previous engagements |

| **KPMG has in-depth sector expertise** |
| KPMG professionals have extensive experience working in various sectors, ranging from energy & natural resources to manufacturing, logistics and agri-food. They understand the developments that are relevant to your sector, seek to understand your business and know the stakeholder landscape well. |

| KPMG professionals can work efficiently as they understand your sector and can help you benefit from existing insights |

| **KPMG is at the forefront of new developments through the EU Taxonomy Hub** |
| KPMG is closely connected to relevant developments at the EU level through the KPMG office in Brussels and the international EU Taxonomy Committee. In addition, through participation in a number of leading business networks, KPMG is well aware of the discussions around certain topics and the direction to which these discussions are leading. |

| KPMG professionals can provide first-hand access to relevant insights regarding future developments and their impact on your business |

| **Interconnected, hands-on teams** |
| Across KPMG, the EU Taxonomy focus teams combine relevant aspects to help achieve a successful delivery. Combining EU Taxonomy expertise, extensive sustainability and accounting know-how, and in-depth sector knowledge. |

| KPMG’s professionals can provide relevant expertise to help successfully and efficiently deliver the project based on years of practical experience |
CSRD at a glance

EU law requires certain large companies to disclose information on the way they operate and manage social and environmental challenges. On April 21, 2021, the Commission adopted a proposal for a Corporate Sustainability Reporting Directive (CSRD), which will amend the existing reporting requirements of the Non-Financial Reporting Directive (NFRD).

### Trends in reporting
- Increased awareness that climate change will have severe consequences when not actively addressed
- Societal stability requires more focus on equal treatment of people, including a more equal distribution of income and financial capital
- Allocating capital to companies with successful long-term value creation requires more comprehensive insights in non-financial value factors
- Recognition that large corporate institutions have a much broader role than primarily serving shareholders

### Policy response
- Policy makers such as the EC address these trends through comprehensive legislation, focusing on directly addressing issues as well as indirectly, through corporate disclosures to support investors decision making

### New regulation
- The EU Corporate Sustainability Reporting Directive (CSRD)

#### Companies to be affected
- **All [listed or non-listed] large companies** (2 of 3 criteria met):
  - > 250 employees;
  - EUR 40 mln turnover;
  - EUR 20 mln total assets.
- **All other (small/medium) listed companies** get an extra 3 years to comply

#### Limited assurance mandatory (subject to Member States)
**If statutory auditor:**
- Integration in auditor’s report;
- Involvement of key audit partner;
- EU Taxonomy and materiality assessment in scope.
Timeline and multi-cluster pipeline

This timeline for undertakings implementing the CSRD by FY 2023 is based on the European Commission proposal dated April 2021.

Proposal Corporate Sustainability Reporting Directive, implementation by FY 2023
First set of Sustainability Reporting Standards (EFRAG), implementation by FY 2023
Second set of Sustainability Reporting Standards (EFRAG), implementation by FY 2024

However, in February 2022 the Council of the European Union proposed a delay of the implementation timeline. The revised proposal will be discussed with the EU Parliament this spring.

Reporting entities already subject to the NFRD report in 2025 on 2024 data
Large reporting entities not currently subject to the NFRD report in 2026 on 2025 data
Listed SMEs, small and non-complex credit institutions and captive insurance entities report in 2027 on 2026 data

Overview of the reporting of requirements of the CSRD

<table>
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<tr>
<th>Overall requirements</th>
<th>General disclosures</th>
<th>Topic-specific disclosures</th>
</tr>
</thead>
<tbody>
<tr>
<td>— Inclusion in the annual report</td>
<td>— Business model, strategy and policies</td>
<td>— Environmental (incl. EU Taxonomy)</td>
</tr>
<tr>
<td>— External (limited) assurance (as from FY 2023)</td>
<td>— KPIs and targets (forward looking information)</td>
<td>— Social</td>
</tr>
<tr>
<td>— Reporting principles</td>
<td>— Company and sustainability governance</td>
<td>— Governance (for topics)</td>
</tr>
<tr>
<td>— Format and timing</td>
<td>— Double materiality assessment and due diligence</td>
<td>— Diversity</td>
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<tr>
<td></td>
<td>— Risk and opportunity management</td>
<td>— Sector-specific standards</td>
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## How to deal with CSRD: requirements and approach

### Detailed overview of the reporting requirements of the CSRD

#### Overall requirements

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<thead>
<tr>
<th>Category</th>
<th>CSRD requirement</th>
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</thead>
<tbody>
<tr>
<td><strong>Inclusion in the annual report</strong></td>
<td>— The required information should be included in the management section of the annual report.</td>
</tr>
<tr>
<td><strong>External (limited) assurance</strong></td>
<td>— Limited assurance on reporting against EU standards.</td>
</tr>
<tr>
<td><strong>Reporting principles</strong></td>
<td>— Strategy and targets, due diligence, risk and materiality assessment should include short-, medium- and long-term time horizons.</td>
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<tr>
<td></td>
<td>— Information should:</td>
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<tr>
<td></td>
<td>• be forward-looking and retrospective, and qualitative and quantitative;</td>
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<td></td>
<td>• cover a value chain where appropriate;</td>
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<tr>
<td></td>
<td>• be understandable, relevant, representative, verifiable, comparable, in a faithful manner.</td>
</tr>
<tr>
<td></td>
<td>— Link to other information in annual report where appropriate.</td>
</tr>
<tr>
<td></td>
<td>— Information that may be seriously prejudicial to the commercial position of the company may be omitted in certain exceptional cases.</td>
</tr>
<tr>
<td><strong>Format and timing</strong></td>
<td>— Report should be published within 12 months after the balance sheet date.</td>
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<td>— Prepare the report in a Single Electronic Reporting Format and sustainability information mar-up.</td>
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#### General disclosures

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<thead>
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<th>Category</th>
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</thead>
<tbody>
<tr>
<td><strong>Business model, strategy and policies</strong></td>
<td>— Strategy and business model description.</td>
</tr>
<tr>
<td></td>
<td>— Sustainability strategy description.</td>
</tr>
<tr>
<td></td>
<td>— Sustainability policies description.</td>
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<tr>
<td></td>
<td>— Plans to ensure compatibility with the transition to a sustainable economy and 1.5C pathway.</td>
</tr>
<tr>
<td><strong>KPIs and targets</strong></td>
<td>— Description of targets including progress made and plans to achieve these targets.</td>
</tr>
<tr>
<td></td>
<td>— Indicators for all general disclosures.</td>
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<tr>
<td></td>
<td>— Intangibles (other than those in the balance sheet), incl. intellectual, human, social and relationship capital.</td>
</tr>
<tr>
<td><strong>Role of management</strong></td>
<td>— Role of management and supervisory board in sustainability.</td>
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<tr>
<td><strong>Double materiality assessment and due diligence</strong></td>
<td>— Consideration of the financial interests of stakeholders and the impact of the company on sustainability matters.</td>
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<tr>
<td></td>
<td>— Actual or potential adverse impacts throughout the value chain.</td>
</tr>
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<td>— Due-diligence process disclosure.</td>
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<td></td>
<td>— Risks and opportunities from sustainability matters, including dependencies, and how those are managed.</td>
</tr>
<tr>
<td><strong>Risk and opportunity management</strong></td>
<td>— Actions to prevent, mitigate, remediate actual or potential adverse impacts.</td>
</tr>
<tr>
<td></td>
<td>— Resilience to sustainability risks, including how risks are managed.</td>
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<tr>
<td></td>
<td>— Opportunities related to sustainability.</td>
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### Topic-specific disclosures

<table>
<thead>
<tr>
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<th>CSRD requirement</th>
</tr>
</thead>
</table>
| **Environmental** | — Climate change mitigation.  
— Climate change adaptation.  
— Water and marine resources.  
— Use of resources, and circular economy.  
— Pollution.  
— Biodiversity and ecosystems. |
| **Social** | — Equal opportunities for all.  
— Working conditions.  
— Respect for human rights. |
| **Governance** | — Role and composition of administrative, management and supervisory bodies, incl. on sustainability matters.  
— Business ethics and corporate culture, incl. anti-corruption and anti-bribery.  
— Political engagements of the undertaking, incl. its lobbying activities.  
— Management and quality of relationships with business partners, incl. payment practices.  
— Internal control and risk management systems, incl. those in relation to the undertaking’s reporting process. |
| **Diversity** | — Diversity related to management and supervisory board, policy and implementation, objectives, and results. |

### A potential way forward to become CSRD ready

This timeline for reporting entities implementing the CSRD by FY 2023 is based on the European Commission proposal dated April 2021. Alternative proposal drafted by the Council of the European Union suggests delay in implementation (see page 9 for details), which if adopted will affect a potential way forward outlined below.

- **2021**
  - Double materiality assessment
  - Set KPIs and targets
  - Develop plans to achieve targets
  - Establish reporting process and governance

- **2022**
  - Collect data over FY21
  - Set up a control framework
  - Evidence and audit trail in place
  - Compare KPIs against the first set of EU standards
  - Conduct a pre-assurance review

- **2023**
  - Collect data over FY22
  - Establish XBRL tagging
  - Prepare to integrate sustainability information into the annual report
  - Compare KPIs against the second set of EU standards
  - Conduct assurance

- **2024**
  - CSRD-compliant to the annual report over FY23
  - Assurance over sustainability KPIs
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