Future of ESG Reporting

June 2023

KPMG South Africa

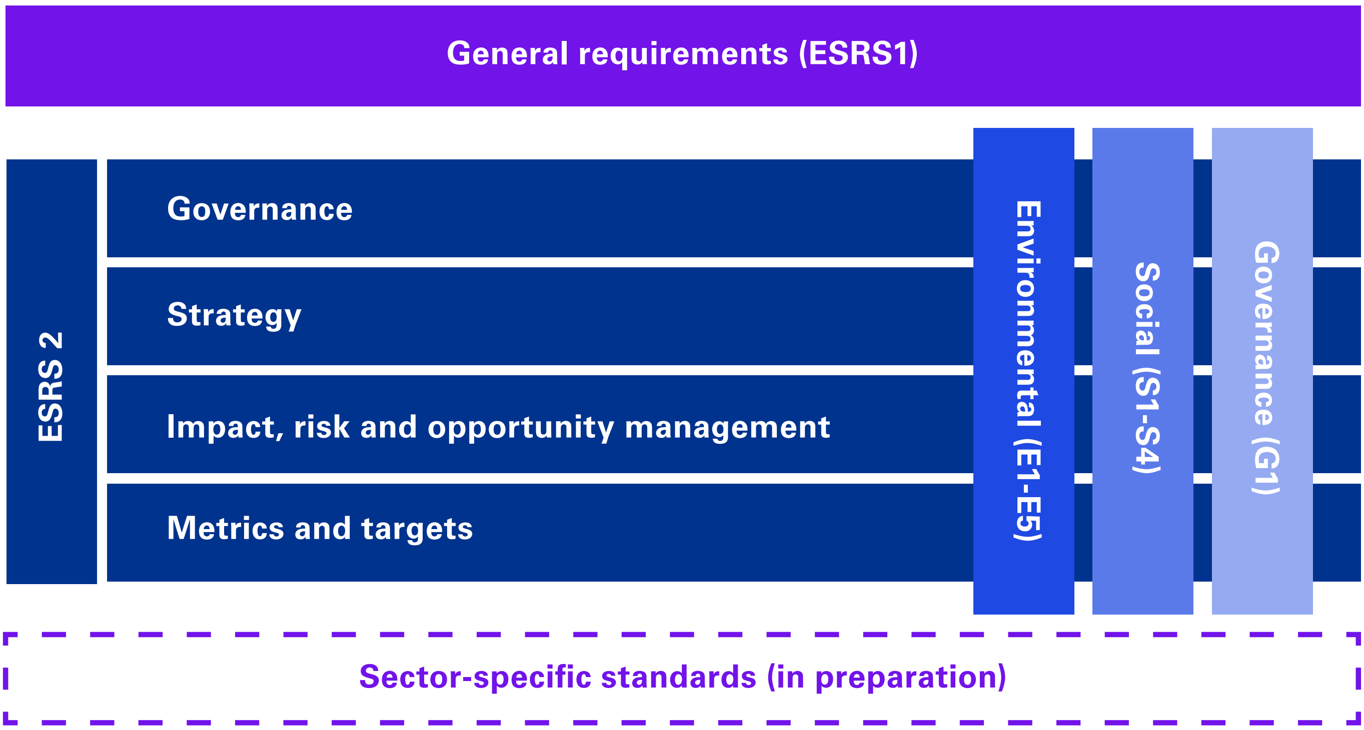
The European Union (EU) Corporate Sustainability Reporting Directive (CSRD) – through the lens of a South African company

With the ESG reporting landscape being in a state of flux, it is imperative for companies to be aware of changes that may impact their reporting processes and responsibilities. As a trusted advisor, KPMG offers insights and support to enable and enhance compliance and meet stakeholder expectations. It is especially important that insights are contextualised for the South African market.

Following the European Parliament and European Commission's approval and adoption of the proposal for Corporate Sustainability Reporting Directive (CSRD), draft European Sustainability Reporting Standards (ESRS) have been published. ESRS will apply for years beginning on or after 1 January 2024. Phase in-measures would apply, where the ESRS include specific reliefs that companies could apply in the early years of adoption to support them in transitioning from existing methodologies or reporting frameworks.

The objective is to significantly expand the existing EU requirements for sustainability reporting for large organisations operating in the EU. Ten topic specific standards have been released providing topic specific application guidance on governance, Strategy and impact, risk and opportunity management. In addition, two cross-cutting standards have been released that provide disclosure requirements applicable for all topics, provide principles of disclosure and presentation structure, establish transitional provision and explain fundamental concepts from the CSRD. Additional sector-specific standards are being developed for later adoption.

Overview of the standards



In-scope companies will be required to report on how their activities and value chain affect the environment and people, as well as how sustainability matters affect their cash flows, financial position and financial performance. It is estimated that about 50,000 companies in the EU will be affected.

General scoping

The following EU companies are in-scope for CSRD reporting:

- Companies with listed securities in the EU other than 'micro-undertakings'. A micro-undertaking meets at least two of the following (including ≤ 10 employees; ≤ €700,000 net turnover; ≤ €350,000 total assets).
- Public interest entities with more than 500 employees.
- Non-capital market oriented companies (including all their subsidiaries on a consolidated level) that meet at least two of the following:
  - > 250 employees;
  - > €40M net turnover (revenue); and
  - > €20M total assets.

South African companies with listed debt or equities in EU markets will be scoped in (unless they are micro-undertakings).

Non-EU parent company scoping

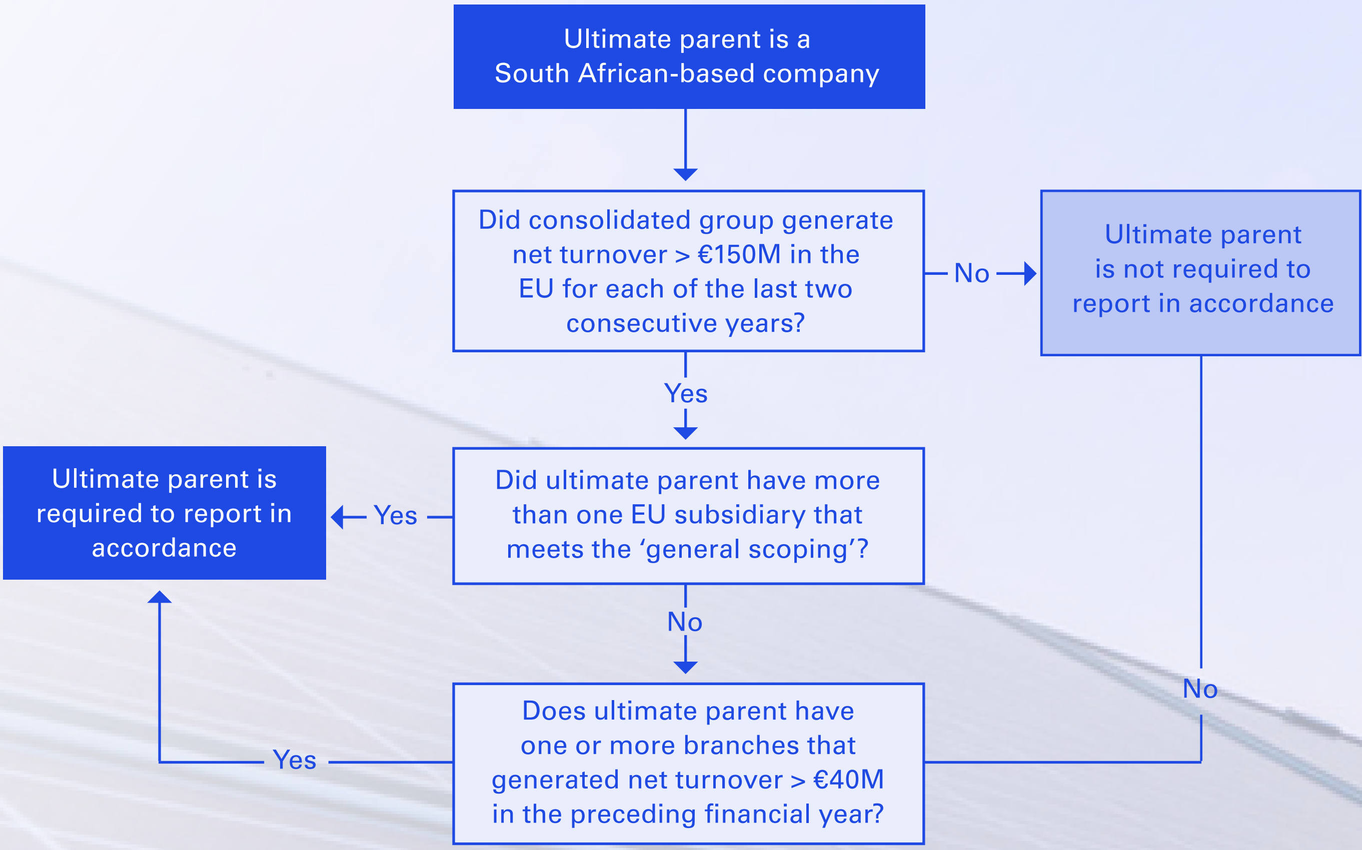
An ultimate non-EU parent company would be subject to CSRD reporting if it has:

- Substantial activity in the EU - i.e. net revenue > €150 million (EU) for two years.

At least:

- One subsidiary that meets the general scoping of the CSRD; or
- One branch: net revenue > €40 million in the preceding year.

Scoping decision tree for a South African parent company



Impact on South African companies

In the short-term, South African subsidiaries of scoped-in EU groups would likely have expanded internal ESG reporting requirements for the EU parent to report on relevant group-wide disclosures. This reporting may also need to be assured to provide comfort to the ultimate reporting entity and satisfy the requirements of the standards.

South African parents with scoped-in EU subsidiaries would need to closely monitor their requirements under the non-EU parent reporting standard being developed by the EFRAG. This is a specific disclosure standard for non-EU parent companies (subject to certain reporting exemptions).

Importantly, South African suppliers and customers of scoped-in EU companies may have expanded data and reporting demands from EU companies in order for them to report required ESG information in their value chain, such as ethical sourcing in their supply chain and reporting Scope 3 GHG emissions from upstream and downstream activities.

Over the medium to long term, investors and other stakeholders may become accustomed to, and make decisions based on, the ESRS reporting requirements. These stakeholders may expect, or require, the same level of reporting (and assurance) for prospective investees outside of the EU. In this way, reporting information in terms of ESRS could in the future be seen by capital markets as best practice, serve as a catalyst beyond local reporting requirements, and promote foreign direct investment.

Timelines

FY24
Reporting in 2025
Large public interest entities with > 500 employees

FY25
Reporting in 2026
Other large companies

FY26
Reporting in 2027
Listed small and medium-sized companies (excluding micro-companies) have option to opt out for two years

FY28
Reporting in 2029
South African parent companies

FY28
Reporting in 2029
Listed small and medium-sized companies (excluding micro-companies)

Assurance

CSRD would require assurance across all topics starting with limited assurance from date of initial reporting; with the ambition to move to reasonable assurance at a future date.

Member states may choose to allow assurance over sustainability reporting to be separate from the financial statement audit (i.e. by a separate auditor or independent assurance provider).

In the absence of an assurance opinion, the company would need to issue a statement indicating this.

Clearly, developments in the EU are making waves at a global level!

KPMG is dedicated to being a trusted partner in helping our clients navigate the constantly changing landscape of ESG Reporting and Assurance.

Comparison of standards

In August 2021, the Value Reporting Foundation (which oversaw the Sustainability Accounting Standards Board (SASB) standards) consolidated into the International Financial Reporting Standards Foundation (IFRS Foundation), thereby establishing the International Sustainability Standards Board (ISSB). The objective of the ISSB is to provide a comprehensive global baseline of sustainability disclosures focused on the needs of investors and the financial markets. As such, it is expected that when the ISSB standards have been finalised they might have a considerable impact on the capital markets of South Africa, much like the ESRS.

	Standards	Standards
Summary	Proposed standards for mandatory sustainability reporting for in-scope companies with significant interests in the EU.	ISSB IFRS Sustainability Disclosure Standards are investor-focused general principles, including proposed requirements to report across all significant sustainability-related risks and opportunities, however, to date, only climate related detailed guidance is available.
Framework/ standards structure	Applicable across sustainability matters for the reporting areas Governance, Strategy, Impact, risk and opportunity management and Metrics and targets, in line TCFD recommendations.	General principles including proposed requirement to report across all significant sustainability-related risks and opportunities. Will build on the industry-based SASB Standards and embed SASB's industry-based approach to standards development. Climate proposal includes industry specific disclosures.
Prescribed reporting format	In scope companies mandated to disclose material sustainability matters in the management report.	Sustainability information and performance metrics that are "financially material" should be incorporated into a reporting company's scheduled disclosures in line with other applicable reporting requirements
Materiality approach	Double materiality	Financial materiality
Materiality assessment required?	Yes – Materiality assessment is necessary for the undertaking to identify the material impacts, risks and opportunities to be reported. However, organizations are requested to provide their Scope 1 and Scope 2 GHG emissions independent of materiality assessment, and, if appropriate, Scope 3 GHG emissions and the related risks.	Yes - ISSB uses the same definition of 'material' that is used in IFRS Accounting Standards – information is material if omitting, obscuring or misstating it could be reasonably expected to influence investor decisions.
Assurance requirements	Limited assurance initially, moving to reasonable assurance over time.	No mandate to require assurance, instead information is designed to be verifiable. Jurisdictions may choose to require either limited or reasonable assurance.

With the SASB standards now under the oversight of the ISSB, the industry-based standards are foundational input in the development of the Board's IFRS Sustainability Disclosure Standards. Companies that are currently reporting in alignment with SASB standards are encouraged to continue to do so, and those that intend to align with ISSB standards are encouraged to use SASB standards, as this would be good preparation for the implementation of ISSB standards.

Visit our global page where we compare ESRS, ISSB and the SEC climate proposal.

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