Provisional agreement reached by European legislative bodies, and further reporting clarity for non-EU companies.

**Source and applicability**

- Proposal for a Corporate Sustainability Reporting Directive (CSRD)
- Companies with listed securities in the EU, some non-EU parents (including US companies) of EU subsidiaries, and non-EU subsidiaries of EU parents that meet the scoping requirements.

**Fast facts, impacts, actions**

The CSRD would amend and significantly expand the existing EU requirements for sustainability reporting. In June 2022, the European legislative bodies reached provisional agreement on the CSRD, which brings it one step closer to finalization. Notwithstanding that the CSRD is an EU Directive, there are considerable ESG reporting implications for US and other non-EU based companies.

The following overview – based on the latest status of the CSRD as it works its way through the legislative process – highlights the potential impact on a US (or other non-EU) parent of an EU subsidiary.

- The CSRD includes different scoping requirements for non-EU parent companies, which would be based on a combination of physical presence in the EU (e.g. a subsidiary) and net turnover (revenue) generated in the EU.
- There would be a separate disclosure standard for non-EU parent companies in the scope of the CSRD; such reporting would cover the parent’s consolidated group – i.e. not just its EU subsidiaries.
- Reporting exemptions would reduce – but not eliminate – the reporting obligations of non-EU parent companies.

For US and other non-EU based companies that had been waiting for further clarity on the scope and reporting requirements under the CSRD, much of that clarity has been provided. Get started by analyzing your group structure to identify potential reporting obligations.
Background

The existing EU requirements to publish nonfinancial statements stem from the Non-Financial Reporting Directive (NFRD) – EU Directive (2014/95/EU). The NFRD currently applies to large ‘public interest entities’ with more than 500 employees.

The CSRD would amend and significantly expand the existing EU requirements for sustainability reporting – both in terms of the number of companies in scope and the nature of the sustainability reporting. It is estimated that the scope would extend from less than 12,000 to nearly 50,000 companies just in the EU. The European Commission originally proposed the CSRD in April 2021. After various counter-proposals, the European legislative bodies reached provisional agreement on the CSRD in June 2022.

One of the provisions in the CSRD would introduce the requirement for companies in scope to report sustainability information based on European Sustainability Reporting Standards (ESRSs). Further, it would require the European Commission to adopt an initial set of ESRSs (drafted by the European Financial Reporting Advisory Group, or EFRAG) by June 30, 2023 and additional standards in following years.

In April 2022, the newly created EFRAG Sustainability Reporting Board issued its first set of draft ESRSs for public comment; the comment period ended in August. To understand the ESRS exposure drafts, see our talk book on the Top 10 Q&A, and read our comment letter. There would be a separate standard for reporting by an ultimate non-EU parent company that is in scope of the CSRD, and an exposure draft is expected in the first half of 2023.

The CSRD is just one component of a number of sustainability-related regulations under the European Green Deal that include reporting obligations – e.g. EU Taxonomy disclosures. For additional information, see Resources.

Scoping requirements

The provisional CSRD includes different scoping requirements for EU versus non-EU based companies – referred to in this Defining Issues as ‘general’ vs ‘non-EU parent’ scoping. Whereas the general scoping would depend on listing status or size, the non-EU scoping would be based on a combination of physical presence in the EU and net turnover (revenue) generated in the EU. This interplay of requirements, plus related reporting exemptions, can make the scoping analysis complex.

General scoping

The CSRD would apply to all companies operating in the EU and their subsidiaries (EU-based companies) that meet the following general scoping requirements.

- Large companies or large groups (i.e. a company including all its subsidiaries on a consolidated level) that meet at least two of the following:
  - > 250 employees;
  - > €40M net turnover (revenue);
  - > €20M total assets.

- Companies with listed securities in the EU other than ‘micro-companies’. A micro-company meets at least two of the following: < 10 employees; ≤ €2M net turnover; ≤ €2M total assets.

The general scoping would include large subsidiaries of non-EU parents – i.e. all EU companies would be subject to testing under the above criteria regardless of the origins or domicile of their ownership.
Non-EU parent scoping

Irrespective of the general scoping described above, an ultimate non-EU parent company would be subject to the CSRD if it has:

- substantial activity in the EU – i.e. it generated net turnover greater than €150M in the EU for each of the last two consecutive years; and
- at least:
  - one subsidiary that meets the general scoping of the CSRD; or
  - one branch (in general, a physical presence) that generated net turnover greater than €40M in the preceding year.

The following decision tree summarizes application of the non-EU parent scoping.

For an ultimate non-EU parent company that is subject to the CSRD, reporting would cover the entire group – i.e. from the perspective of the parent. However, there would be a separate disclosure standard. The disclosure requirements under the non-EU parent scoping are expected to be slightly reduced compared to those under the general scoping for which the first set of exposure drafts has been issued.

Further, any subsidiary that meets the general scoping would nonetheless be in the scope of the related disclosures that apply to EU-based companies.

Reporting exemptions

There would be three exemptions available under the CSRD.

- **The group exemption.** If a parent makes available a CSRD-compliant sustainability report that includes the entire group, all in-scope subsidiaries would be exempt from preparing their own sustainability reports. However, this exemption would not apply to subsidiaries under the general scoping that are large public interest entities. Therefore, these subsidiaries would still be required to prepare a stand-alone CSRD-compliant report.
It is not yet clear whether the group exemption would apply to:

- reports that comply with the full set of ESRs under the general scoping and reports prepared by an ultimate non-EU parent company under the non-EU parent scoping; or
- only CSRD reports that comply with the full set of ESRs.

- **The ultimate non-EU parent exemption.** If a non-EU parent has multiple subsidiaries in the EU that meet the general scoping, for the first seven years one of the largest EU subsidiaries would be allowed to prepare a consolidated sustainability report that includes only those subsidiaries that fall under the general scoping. This report would need to follow the reporting requirements specific to the general scoping.

- **The equivalency exemption.** The European Commission has the power to designate individual sustainability reporting frameworks or reporting regimes as ‘equivalent’ to reporting under the CSRD. See Use of other sustainability reporting frameworks.

**Examples**

The following examples highlight the proposed requirements for US and other non-EU based companies.

**Example 1: EU activity is not substantial**

The EU subsidiary (not a public interest entity) had average net turnover of €60M in each of the past two years and has total assets of €30M. Neither the US parent nor the other subsidiaries generate turnover in the EU.

**Analysis**

- The EU subsidiary would be required to prepare a stand-alone CSRD-compliant report under the general scoping.
- The US parent would not be subject to the CSRD because it does not meet the non-EU parent scoping – i.e. US consolidated group did not generate net turnover of €150M in the EU in each of the past two years.

**Example 2: EU activity is substantial**

The same as Example 1 except that the group had net turnover generated in the EU of €175M in each of the past two years. (It is this difference in revenue – rather than the different group structure – that drives the different analysis below.)

**Analysis**

- Like Example 1, the consolidated EU subsidiary (i.e. including the Australian subsidiary) would be required to prepare a stand-alone CSRD-compliant report under the general scoping.
- Unlike Example 1, the US parent would be subject to the CSRD because it meets the non-EU parent scoping – i.e. the US consolidated group generated net turnover of
**Application to public interest entities**

Both the NFRD and the CSRD refer to ‘public interest entities’ as part of their respective scopes, but the application would not be the same. The following table summarizes the differences in the context of the above discussion.

<table>
<thead>
<tr>
<th>PIEs in NFRD scope?</th>
<th>Public interest entities (PIEs) include:</th>
<th>PIEs in CSRD scope?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes, if &gt; 500 employees</td>
<td>An entity whose transferrable securities are admitted to trading on regulated markets governed by the law of a member state of the EU (companies with listed securities in the EU)</td>
<td>Yes; but group exemption(^1) would not apply to large public interest entities</td>
</tr>
<tr>
<td></td>
<td>A bank or insurance company</td>
<td>Yes, if large; group exemption(^1) would apply</td>
</tr>
<tr>
<td></td>
<td>Any other company designated as such by a member state of the EU</td>
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Note 1: See [insight](#) on the form of the report in applying the group exemption.

**Use of other sustainability reporting frameworks**

A non-EU company could fulfill its reporting requirements by applying either:

- the CSRD as drawn up (i.e. applying ERSRs); or
- a similar sustainability reporting framework that is considered ‘equivalent’ by the European Commission.

Although the Commission has not yet determined what would be considered an equivalent sustainability reporting framework, it will likely use the following criteria:

- whether the other framework requires companies to disclose information on environmental, social and governance matters; and
- whether the other framework requires companies to disclose information necessary to understand the company’s impacts on sustainability matters, and how sustainability matters affect the company’s development, performance and position (so-called double materiality).

**Effective dates**

Large public interest entities with more than 500 employees that are also large under the general scoping would need to apply ERSRs for 2024 year-ends (reporting in 2025); other companies, including small and medium-sized companies with listed securities in the EU, would follow in a phased application. An ultimate non-EU parent company under the non-EU parent scoping would need to apply the applicable...
ESRSs for its 2028 year-end (reporting in 2029). Limited assurance over the entire CSRD-compliant report – under both the general and non-EU parent scoping – would be required initially, with the intent of moving to reasonable assurance in time.

Next steps

The following are next steps for the items discussed in this Defining Issues.

- **CSRD approval.** The CSRD will not become effective until it is formally approved. It is planned to be brought to the European Parliament in November 2022. After publication in the Official Journal of the EU plus 20 days, member states (which will also enforce the CSRD) have 18 months to transpose it into national law.

- **ESRSs under the general scoping.**
  - **First set of ESRs.** Following redeliberation of the exposure drafts, EFRAG will deliver its technical recommendations (‘advice’) to the European Commission, which will then have to adopt the ESRs for them to become effective. These ESRs are expected to be adopted by the Commission by June 30, 2023.
  - **Additional sets of ESRs.** Exposure drafts of additional standards have not yet been released. They are expected to contain sector-specific proposals, and proposals for small and medium-sized entities. ESRs for small and medium-sized entities and for the first high-priority sectors are expected to be adopted by the Commission by June 30, 2024.

- **ESRS under the non-EU parent scoping.** An exposure draft relevant to the non-EU parent scoping is expected in the first half of 2023, and is expected to be adopted by the Commission by June 30, 2024.

Resources

For further guidance on the CSRD and related developments, we recommend the following KPMG resources as a starting point.

- Talk book with Top 10 Q&A, Get ready for European Sustainability Reporting Standards
- Talk book with Top 10 Q&A, Comparing ESG reporting proposals (from the International Sustainability Standards Board, EFRAG and the SEC)
- Report, European Green Deal Policy Guide (focus on the ‘Fit for 55 package’).