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THE ESG COMPLIANCE MAZE

The issue of ESG compliance fosters respect for individual businesses. Given that businesses confront a number of substantial risks associated with their ESG compliance duties, respect is due.

Risks from non-compliance vary depending on the industry, company size, and geographic location, but include the following key areas:

1. Regulatory and Legal Risks
- Non-compliance can lead to legal sanctions, fines, and even litigation.
- Struggling to keep up with constantly evolving requirements can result in unintentional non-compliance and subsequent penalties.

2. Financial Risks
- Implementing and maintaining ESG compliance can be costly (investments in technology, expertise, reporting, and auditing), especially for smaller companies.
- Investors and financial institutions increasingly consider ESG factors in their investment decisions. Poor ESG practices can limit a company's access to capital.

3. Investment Risks
- Rating agencies are increasingly evaluating companies based on ESG criteria. A low ESG rating can negatively impact a company's market value.

4. Reputational Risks
- Companies that claim environmental or social responsibility but fail to align with those claims risk accusations of 'greenwashing,' which can severely damage their reputation and erode customer and investor trust.
- Failure to adequately address ESG issues, such as labor conditions or environmental damage, can lead to negative publicity and harm the company's brand.

5. Operational Risks
- Many companies lack adequate systems for tracking, collecting, and analyzing ESG data. Incomplete or inaccurate reporting increases the risk of non-compliance.
- Companies are increasingly held accountable for the ESG practices of their suppliers. Poor practices within the supply chain can create indirect risks that affect the company's overall ESG profile.

6. Market and Competitive Risks
- Companies that do not implement robust ESG strategies risk falling behind their competitors.
- Growing consumer sensitivity to sustainability and ethical issues may lead to reduced demand for the products and services of companies that do not meet ESG standards.

7. Physical and Climate Risks
- Companies are exposed to risks associated with climate change, such as extreme weather events, floods, or droughts, which can disrupt operations and supply chains.
- Increasing pressure to reduce carbon emissions can lead to higher operational costs.

Thus, what should be done and how should the company responsibly prepare in order to ensure that these risks and threats—which involve not only not meeting regulatory requirements but also strategically managing business operations—are identified early on and adequately addressed?

The following questions require answers:
- Do you fall within the jurisdiction of the CSRD?
- If yes, when should you commence reporting?
- Which ESRS should be used?
- Is a consolidated or individual sustainability report to be prepared?
- Does your organization possess sufficient human and financial resources?
- Under whose responsibility will sustainability information be prepared?

PLATFORM FOR GATHERING DATA

Selecting the platform for data collection is one of the most critical decisions a company must make. Numerous software solutions now offer advanced materiality testing, centralized data collection, and conversion tools in multiple languages, tailored for different holdings or enterprises. These platforms are regularly updated to reflect the latest regulations, providing clarifications, instructions, and even allowing direct data input and seamless data migration.

While using Excel spreadsheets for data collection may seem cost-effective at first, the time-consuming process—along with the risk of errors during recalculations, data transfers, and handling across entities—can quickly become overwhelming and lead to many of the risks mentioned earlier.

Therefore, this is an issue of significant importance.

ENOUGH TIME TO GATHER DATA

Waiting until the year of disclosure to start data collection is too late. It's essential not to underestimate the importance of planning; ideally, data collection should begin a year in advance. This allows sufficient time to evaluate the volume and quality of the data, implement any necessary changes, and provide staff with the required training. As the classic quote by Sun Tzu goes: "Preparation is the key to victory. Therefore, the more prepared you are, the more likely you are to succeed."

WHO DOES IT CONCERN?

Source: Smarthead

Type of company	1st reporting period	Applicable standards	Additional notes
Large PIE with 500+ employees	2024	ESRS	Companies previously in the scope of NFRD
Large company *	2025	ESRS	Companies which meet 2 out of 3 criteria: • 50 mil. EUR revenue • 25 mil. EUR total assets • 250 employees
Parent company * /subsidiary of a large group	2024 or 2025	ESRS	• Parent company prepares a consolidated report • Subsidiary will need to report to group • Identical size criteria as those for large companies applied to the consolidated data
Listed SME	2026	ESRS for listed SME	Option to extend reporting by 2 years to 2028 Also applies to: • Small and no-complex credit institutions • Captive insurance undertakings
Business partner to a CSRD reporter	Various	Voluntary ESRS	Exact timing and scope depend on business partners in the value chain • Scope is limited to ESRS for listed SME • Option to report voluntary
Company from a 3rd country	2028	ESRS for 3rd country companies	Company established in 3rd country with 150+ mil. EUR revenue in the EU and: • at least 1 subsidiary in the scope of CSRD • at least 1 branch generating 40+mil. EUR revenues

* exemptions are available for subsidiaries of parent companies that are subsidiaries