

Implications of ESRs implementations in sustainability consulting practice

Marija Bajica *, Andreja Pavlović *

* Oikon – Institute of Applied Ecology, Zagreb, Croatia
Mbajica@oikon.hr

Abstract — Climate change is a pressing global challenge that drives sustainability legislation development and enforcement, making sustainability reporting mandatory in addressing it. EC adopted CSRD in 12.2022 and ESRs in 06.2023. 12 ESRs cover general principles for sustainability reporting, overarching disclosure requirements, and specific disclosure requirements focused on 10 environmental (ESRS E1–E5), social (ESRS S1–S4), and governance (ESRS G1) topics. This paper has used case study in the context of sustainability consulting practice to explore the impact the adoption of ESRs has on existing corporate data harvesting and reporting processes and project-related sustainability assessment tools. The way forward to achieve compliance with EU regulations is further outlined.

Keywords - ESRs; CSRD; sustainability reporting; project related sustainability assessment

I. INTRODUCTION

Concerns about sustainability and the impact of human activities on the environment have a long history, but the modern concept of sustainability, as we understand it today, began to take shape in the 20th century. One of the earliest and most significant milestones was the publication of Rachel Carson's 'Silent Spring' [1] in 1962 which raised awareness about the environmental impact of pesticides and is often credited with sparking the modern environmental movement. However, the concept of sustainability in its broader sense, encompassing not just environmental concerns but also social and economic dimensions, gained significant international attention with the UN Conference on the Human Environment in Stockholm in 1972. This was the first major international conference focused on environmental issues and marked a turning point in the development of international environmental politics.

The term 'sustainable development' itself was popularized by the Brundtland Commission in its 1987 report 'Our Common Future' [2]. The Commission, formally known as the World Commission on Environment and Development (WCED), was chaired by Gro Harlem Brundtland, a former Prime Minister of Norway. The report defined sustainable development as 'development that meets the needs of the present without compromising the ability of future generations to meet their own needs.'

Since then, the concept of sustainability has continued to evolve and expand, influencing global policies and practices across various sectors. The United Nations' adoption of the Sustainable Development Goals (SDGs) in 2015 further marked a global commitment to addressing major sustainability challenges, including poverty,

inequality, climate change, environmental degradation, peace, and justice.

The EU's key response to the adoption of the SDGs was the European Consensus on Development (2017), representing a shared vision and framework for development cooperation for the EU and its Member States. It aligned European development policy with the 2030 Agenda for Sustainable Development. The European Green Deal (2019) that followed provided a comprehensive plan to make the EU's economy sustainable by turning climate and environmental challenges into opportunities. A set of financial and non-financial regulations followed, with the 12 European Sustainability Reporting Standards (ESRS) issued on 31 July 2023 being the latest addition to the EU legislative framework. The ESRs fully apply the requirements of Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector (SFDR).

The EU sustainability legislation is driven by a range of environmental, social, and economic challenges that are both global and region-specific. One of the most pressing issues is the need to mitigate climate change which includes reducing greenhouse gas emissions, transitioning to renewable energy sources, and adapting to climate change impacts.

The unsustainable use of natural resources by overfishing, deforestation, and the overuse of water and mineral resources is leading to depletion and environmental degradation. Addressing various forms of pollution, including air, water, and soil pollution, is crucial. This encompasses challenges like reducing plastic waste, managing chemical pollutants, and improving air quality.

The loss of biodiversity due to habitat destruction, pollution, climate change, and other factors is also a critical issue. Protecting ecosystems and wildlife is essential for maintaining environmental balance. Sustainable economic growth, reduction of the environmental footprint of cities, sustainable transportation, the transition to more sustainable energy systems, focus on energy efficiency, and the development of renewable energy sources are economic and environmental imperatives that require a legal framework for timely and successful results.

A. Chronology of building EU alignment of financial and non-financial into sustainability legislation

EU sustainability legislation aims to address these issues effectively, ensuring a more sustainable future for all EU member states.

Several parallel processes were underway, some of which had a significant impact on companies obliged to publish non-financial statements as of January 1, 2022. The Non-Financial Reporting Directive (2014/95/EU) together with the Sustainable Finance Disclosure Regulation the Taxonomy Regulation (2020/852) and the Corporate Reporting Directive proposal (2021/0104) are the central components of sustainability reporting requirements underpinning the EU's sustainable finance strategy. The purpose of that legal framework was to enable a coordinated and coherent flow of sustainability information through the financial value chain.

In line with the Commission's Sustainable Finance Action Plan (COM (2018) 097 final), the EU has taken a few actions to enable the financial sector to play a significant role in achieving the objectives of the European Green Deal. The successful implementation of the European Green Deal and the Sustainable Finance Action Plan requires better data on sustainability risks and opportunities and their impact on people and the environment. As is the case with financial reporting, common standards are needed for the information provided to be comparable and relevant. In December 2019, in its conclusions on the Capital Markets Union, the EU Council stressed the importance of reliable, comparable, and relevant information on sustainability risks and opportunities and sustainability impacts.

Common reporting standards are expected to greatly facilitate the digitalization, verification, and enforcement of sustainability reporting. At the end of November 2022, the European Sustainability Reporting Standards (ESRSs) prepared by the European Financial Reporting Advisory Group (EFRAG) were published based on the Corporate Sustainability Reporting Directive proposal. The Corporate Sustainability Reporting Directive (CSRD) amends the 2014 Non-Financial Reporting Directive. It introduces more detailed reporting requirements and ensures that all large, medium, and small enterprises must publish information relating to sustainability issues concerning environmental, social, human rights and corporate governance. The CSRD also introduces a requirement to audit (verify) published sustainability information, as well as better access to information by requiring it to be published in a separate management report.

The latest addition to EU sustainability legislation was the set of 12 Sustainability Reporting Standards (ESRSs) defining a comprehensive list of metrics and data points to be used in corporate reporting for companies complying with the Corporate Sustainability Reporting Directive (CSRD). The ESRSs were published by the European Regulatory Financial Reporting Group (EFRAG) in October 2023. ESRS standards are divided into four thematic areas: general comprehensive and cross-sectoral standards and thematic standards concerning the environment, society, and governance.

In summary, the new EU sustainability regulations (CSRD with ESRSs) increase corporate responsibility, prevent the existence of different national standards, and facilitate the transition to a sustainable economy. Member States had the obligation to transpose them into national legislation by 1 December 2022.

II. SUSTAINABILITY ASSESSMENT AND REPORTING ON CORPORATE LEVEL

Good sustainability reporting goes beyond mere legal requirements. Companies need to continuously adapt their business models and strategies considering increasing environmental and social challenges - how they create and distribute value for businesses and stakeholders. The EU reform policies relating to sustainability have a significant impact on mandatory business reporting on a corporate level. Only ESRS standards contain 84 requests for publication with 1144 pieces of information (data points) within the publications requested.

The complexity of requirements requires active management comprising:

- I. Alignment with the EU taxonomy by applying technical screening criteria to determine the conditions under which economic activity is deemed to contribute significantly to climate change mitigation or adaptation and whether that economic activity is causing significant damage to any other environmental objective (Delegated Regulation on the EU Taxonomy of Climate Sustainable Activities 2021/2139 came in effect from 1 January 2022):
 - (a) The determination of the share of taxonomically eligible and ineligible economic activities in total revenues and capital and operational expenditure and the publication of qualitative information defined in Chapter 1.2. Specification of publications accompanying the key performance indicators of non-financial undertakings referred to in Annex I to the Delegated Regulation on disclosures (2021/2178).
 - (b) The publication of information on key performance indicators from 1 January 2023, including any supporting information following Annexes I and II. Delegated Regulation on Disclosures (2021/2178).
 - (c) The publication of key indicator information for the remaining four environmental targets under a Delegated Regulation adopted at the end of 2022.
- II. The application of the CSRD Directive, which replaced the Non-Financial Reporting Directive (NFRD) in a package with the European Sustainability Reporting Standards (ESRSs), substantially improves the quality of sustainability reporting, in terms of comparability and transparency. It also ensures compliance with the Sustainable Financial Disclosure Regulation (SFDR) and the Taxonomy Regulation, as well as other EU sustainable finance initiatives.

Following these new EU regulatory requirements, in addition to existing comprehensive financial reporting, companies need to establish data collection and prepare the delivery of data required by the Taxonomy Regulation, the CSRD, and the ESRSs.

A. *The implications of ESRSs implementation on corporate data harvesting*

In the last two years, our consulting practice has used Global Reporting Initiative (GRI) standards to assist our clients in reporting on their non-financial performance. The GRI standards are structured as a set of modular, interrelated standards. There are three universal standards (GRI 101: Foundation, GRI 102: General Disclosures, and GRI 103: Management Approach) that apply to every organization, and topic-specific standards covering economic, environmental, and social topics. They are designed to apply to companies of any size, type, sector, or location.

With the introduction of the European Sustainability Reporting Standards (ESRSs), we must acquire knowledge and expertise to keep on advising and assisting our clients on how to apply these new rules in their new sustainability reporting.

GRI has been actively involved in developing the ESRS in cooperation with the European Financial Reporting Advisory Group (EFRAG), focusing on ensuring interoperability between the two standards and minimizing reporting burdens for companies. EFRAG also provides implementation guidance for these data points. This list, current as of January 2024, is still to be finalized with further industry-specific metrics to be added in the coming years.

There is a high level of interoperability between GRI and ESRSs, meaning that companies already reporting with GRI Standards can integrate ESRS requirements into their existing processes, however, that transition needs time and effort. The Global Reporting Initiative (GRI) and the European Sustainability Reporting Standards (ESRS) both serve as frameworks for sustainability reporting, but they have distinct differences in their requirements and approaches that need to be overcome. To speed up the process, we identified a few differences that must be understood and considered in implementing ESRSs requirements:

- **Mandatory vs. voluntary reporting**
The GRI Standards are globally applied and are voluntary. Companies are not legally obliged to report following GRI Standards. ESRS-based reporting is legally binding for certain companies in the EU starting in 2024. This means that companies operating in the EU will have to comply with ESRSs requirements as part of their systematic reporting routines.
- **Materiality Approach**
GRI Standards focus primarily on impact materiality, identifying material topics as those representing the company's most significant impacts on the environment and people, including human rights. The ESRSs require a double materiality assessment, which includes both the impact and financial perspective. This means that companies need to assess how sustainability topics affect their financial performance (financial materiality) and how their operations impact the environment and society (impact materiality).

- **Reporting scope and granularity**
GRI recommends analysis at the thematic level and may require quantitative disclosures on certain topics whereas ESRSs might require narrative disclosures. ESRSs reporting is more prescriptive regarding the requirements for the reporting format, including materiality on various levels like topics, sub-topics, and impacts.
- **Failure to Disclose Information**
ESRS allows withholding disclosure only if it would undermine the business position, whereas GRI includes various reasons like legal prohibitions or confidentiality constraints.

These differences (for example, ESRS 1 is mandatory for all eligible companies, and most ESRS 2 is a requirement, regardless of materiality assessments) indicate that, while both GRI and ESRS aim to enhance sustainability reporting, they differ in their approach, with ESRS being more prescriptive and legally binding in the EU context, and GRI focusing more on global applicability and voluntary reporting with a focus on impact materiality.

III. SUSTAINABILITY ASSESSMENT AND REPORTING ON PROJECT LEVEL

For this study, the definition and the concept of project sustainability were used from the Project Management Institute (PMI) Project Management Body of Knowledge (PMBOK) standard [3]. PMI is the leading global association for the project management profession. Our PMPs, certified project managers, and consultants have been applying PMI best practice principles for years within our environmental, nature protection, and natural resource management consulting practice.

Project sustainability in the context of project management refers to an approach that encompasses balancing the environmental, social, and economic aspects of project-based work. It involves ensuring that the deliverables, outcomes, and benefits of a project are sustainable throughout its life cycle, including its creation, disposal, and decommissioning. This concept of sustainability is integral across all areas of project-based work and requires both individual and organizational responsibility. The aim is to embed sustainability into the vision of the project from the outset, ensuring it is a fundamental component throughout the project's lifecycle.

Assessing project sustainability involves the selection of a range of indicators that reflect the environmental, social, and economic aspects of the project. These indicators are tailored to the specific context and objectives of the project to enable evaluation of how well the project adheres to sustainability goals.

The key environmental indicators, identified in Oikon's consulting practice that need to be managed on the project level, focus on environmental compliance (checks adherence to environmental regulations and standards), carbon footprint (measures greenhouse gas emissions caused by the project), or pollution control (monitors the levels of pollutants released into the air, water, and soil),

energy efficiency (monitors the amount of energy used per unit of output), water usage (quantifies the volume of water used and the efficiency of its use), waste management (assesses waste production and recycling rates), biodiversity impact (evaluates the effect of the project on local flora and fauna) and resource utilization (tracks the use of renewable and non-renewable resources).

The key social indicators focus on: community engagement (measures the level of community involvement and feedback), job creation (tracks the number and quality of jobs created by the project), employee well-being (assesses working conditions, health, and safety measures), equity and inclusion (evaluates policies and practices promoting diversity and equality), stakeholder satisfaction (evaluates the satisfaction levels of stakeholders), local economic impact (assesses the project's impact on the local economy) and human rights compliance (monitors adherence to human rights principles and labor laws).

The key economic indicators focus on cost-benefit analysis (compares the project's costs to its economic benefits), return on investment (calculates the financial return on the project's investments), economic viability (assesses the project's long-term economic sustainability), market viability (evaluates the demand for the project's deliverables), life cycle costing (accounts for all costs over the project's lifecycle), financial performance (tracks profitability, liquidity, and solvency metrics), value created (measures the economic value added by the project), transparency (the degree to which the project activities are open to scrutiny), accountability (how well the project holds individuals responsible for their actions), ethical standards: the project's adherence to ethical business practices, technological innovation (the extent to which the project uses or develops new technologies) and resilience to risks (the project's ability to handle risks and unforeseen events).

It's essential to use a balanced set of indicators that cover all three dimensions of sustainability to get an accurate assessment. The selection and prioritization of indicators depend on the project's scope, the industry, and the sustainability goals set by the organization e.g. client's environmental set of KPIs or required by relevant standards and regulations e.g. environmental aspects as defined by a business policy that endorses ISO14001 as standard for managing environmental issues.

A. *The project sustainability assessment tool*

The efficiency and effectiveness of our work and supporting business systems is continuously being improved following the requirements of international standards ISO 9001, ISO 14001, ISO 45001, ISO 27001 and ISO 20000-1, the Croatian Quality Mark of the Croatian Chamber of Economy, the UN Sustainable Development Programme for 2030 with 17 Sustainable Development Goals, established international standards for responsible business conduct, such as the United Nations Guiding Principles on Business and Human Rights and the

OECD Guidelines for Responsible Business Conduct (Due Diligence) and the European Green Deal framework.

The commitment to continuously work on the creation of new knowledge and its application to achieve quality and functional solutions for our customers, led to the development of a project sustainability assessment tool/questionnaire aiming at ensuring that our corporate quality and sustainability policies are adhered to. The tool was developed based on a checklist for integrating sustainability in projects and project management [4]. The questionnaire comprised 33 questions grouped by triple bottom line [5] assessment grouping (economic, environmental, and social) and 10 areas related to the UN Sustainable Development Goals (SDGs) that are relevant for monitoring on the project level:

- Economic: 2 (Return on investment, Business agility)
- Environmental: 4 (Transport, Energy, Waste, Materials and resources) and
- Social: 4 (Labor practices and decent work, Human rights, Society and customers, Ethical behavior).

The assessment tool is being used on Oikon's EU-funded projects with high transportation influence (fieldwork) and a wide stakeholder base (financiers, regulators, developers, beneficiaries/ users, public).

B. *The implications of ESRs implementation on the project level*

After the publishing of the European Sustainability Reporting Standards (ESRSs) at the end of July 2023, we analyzed data points required by the standards and the indicators used for assessing project sustainability in assessment tool that were based on UN sustainable development goals (UN SDGs) were correlated to provide a blueprint for change of assessment tool.

The correlation results of key indicators are grouped and outlined as follows:

Environmental indicators

- Carbon Footprint - ESRs include specific requirements for reporting greenhouse gas emissions (Scopes 1, 2, and 3), which directly relate to a project's carbon footprint.
- Energy Efficiency - Under ESRs, organizations would report on energy consumption within the organization, which covers energy efficiency metrics.
- Water Usage - The ESRs would have data points related to water withdrawal, consumption, and recycling, aligning with water usage indicators in project sustainability.
- Waste Management - Waste generated and management strategies, including recycling and disposal methods, are part of the ESRs, corresponding to waste management indicators.

Social indicators

- Job Creation - ESRs cover employment data points such as the number and type of jobs created, which

reflects the job creation indicator of project sustainability.

- Community Engagement - This may align with ESRS data points on the impact of the organization on communities, including engagement activities, investments, and development programs.
- Equity and Inclusion - ESRSs will likely include aspects of diversity and equal opportunity, which can be correlated with equity and inclusion indicators at the project level.

Economic indicators

- Economic Viability - Financial performance and market presence are part of the ESRSs, which would correlate with a project's economic viability indicator.
- Return on Investment - This could be related to the broader financial data points in the ESRSs that look at the economic performance of an organization.
- Transparency and Accountability - The ESRSs emphasize governance aspects, such as the organization's governance structures, practices, and sustainability risk management, which would relate to transparency and accountability indicators.
- Technological Innovation - While the ESRSs may not directly address technological innovation, they could cover aspects of research and development that can be linked to this indicator.
- Resilience to Risks - The ESRSs require organizations to report on their risk assessment and management processes related to sustainability, which would include resilience to risks.

While the assessment tool can be used in the future to quickly assess the alignment of our projects with the set corporate policy based on quality standards and sustainability principles, the inclusion of ESRSs data points requires additional work that would be best planned, budgeted, and executed through one of scientific EU funded initiatives we plan to apply for.

IV. CONCLUSION

The European Union is adopting a new set of regulations, gradually coming into force, to shift capital flows into sustainable economic activities and achieve climate neutrality by 2050 in line with the European Green Deal. It is undeniable that one of the biggest reforms of the financial sector related to improving the quality of information in terms of comparability and intelligibility of adverse effects of business on sustainability issues is underway.

The European Union's legal sustainability framework encompasses a broad array of policies, directives, and regulations aimed at fostering sustainable development across member states. This framework addresses environmental protection, social equity, and economic development, aligning with the broader objectives of the EU's sustainability and climate agendas. The EU Taxonomy Regulation provides a classification system,

establishing a list of environmentally sustainable economic activities to clarify which can be considered environmentally sustainable. Meanwhile, the Sustainable Finance Disclosure Regulation (SFDR) requires financial market participants to disclose how they integrate Environmental, Social, and Governance (ESG) risks in their investment decisions, as well as the adverse impacts of their investments on sustainability factors. Furthermore, the Corporate Sustainability Reporting Directive (CSRD), along with a corresponding set of sustainability standards (ESRSs), expands the existing non-financial reporting directive. This requires large and listed companies to report on their impact on people and the planet. This framework is continuously evolving, with new policies and regulations being introduced to tackle emerging sustainability challenges. The EU's strategy is comprehensive, aiming to embed sustainability in all facets of policy and economic activities.

While the CSRD and ESRSs mandate obligatory adherence to sustainability reporting at the corporate level, the integration of corporate sustainability policies into project guidelines, standards, and practices has been gradual. This slow integration primarily stems from the need for a paradigm shift in project management, moving from focusing solely on the bottom line (profit) to managing the triple bottom line (economic – including cost, resource management, profit; social – people; and environmental – planet).

Global project management standards and guidelines, based on best practices across industries and utilizing widely used methodologies, still lack comprehensive guidelines for incorporating sustainability dimensions at the project level, including their planning, implementation, monitoring, and control. Nonetheless, sustainability policies and strategies at the company level are beginning to influence project-level management. Sustainability consultancies are ideally positioned to develop rapid assessment and/or monitoring tools that can assist practitioners in more effectively managing the sustainability aspects of their projects as part of their routine project management practices."

REFERENCES

- [1] R. Carson, *Silent Spring*, Boston: Houghton Mifflin, 1962.
- [2] W. C. o. E. a. Development, »Our Common Future,« Oxford University Press, Oxford, 1987.
- [3] P. M. I. PMI, *A Guide to the Project Management Body of Knowledge (PMBOK® Guide)*, Sixth ed., Maryland: Project Management Institute Inc., 2017.
- [4] A. a. S. R. Silvius, »A maturity model for integrating sustainability in projects and project management,« u *24th International Project management Association (IPMA) world congress*, Istanbul, 2010.
- [5] J. Eklington, *Cannibals with forks: The tripple bottom line of 21st century business*, Oxford, UK: Capstone Publishing Ltd., 1997.