ESG reporting from business perspective

Lucie Boková

Agenda

ESG Reporting – a challenge for companies

ESG Reporting – regulatory requirements

ESG Assurance

ESG Reporting - a challenge for companies

ESG Pillars

Attracting clients

Transparency

Talent attraction, employee productivity

Cost reductions

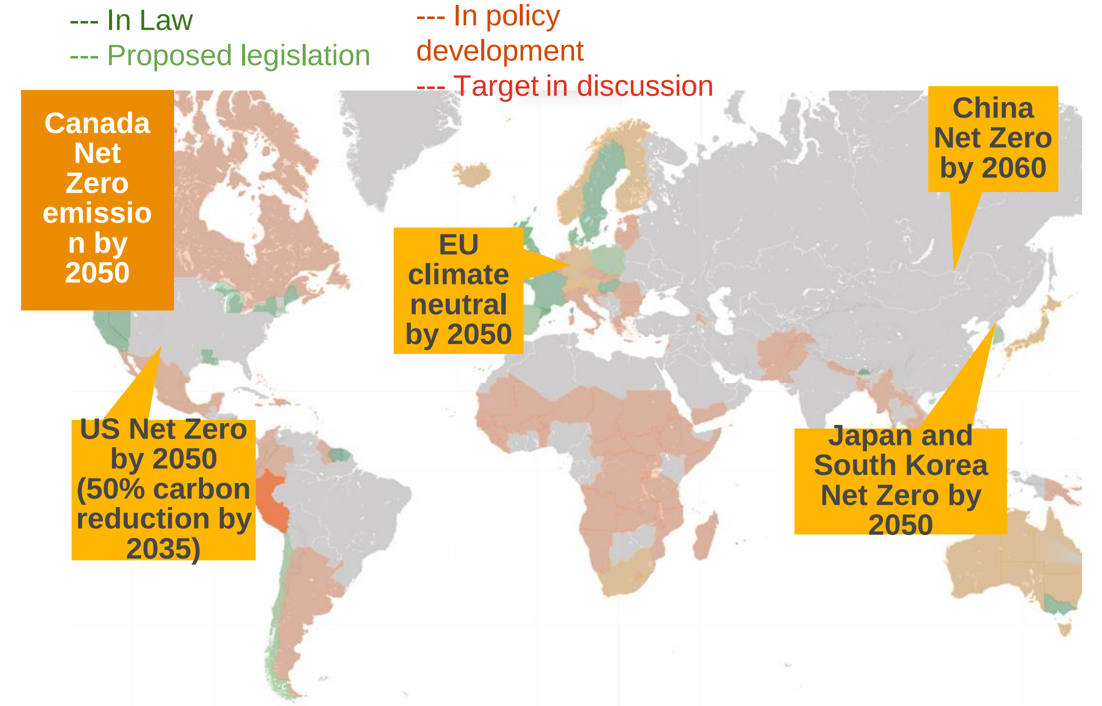
Stakeholder pressure

Risks to business caused by climate change

Regulatory requirements

The world is responding

Governments are aggressively targeting Net Zero



452 cities with Net Zero targets

LPs, banks, PortCo customers and employees are demanding action

30+ institutional investors are committed to net zero portfolios by 2050

300+ companies worldwide have set net zero targets

75% of the workforce will be Millennials and Gen Zers by 2025

We asked nearly 300 businesses in 13 European countries how they were preparing for the Green Deal given how it is likely to impact businesses' investments, strategies and reporting.

60%

The majority of companies are unfamiliar with the EU Green Deal

49%

Fewer than half of organisations are prepared for the EU Green Deal

66%

Have already earmarked capital to invest in becoming more sustainable over the next few years

51%

Of respondents intend to shift key locations in their supply chain

https://www.pwc.com/gx/en/services/tax/publications/are-europes-businesses-ready-for-the-eu-green-deal

Sustainability strategy and non-financial reporting setting

1 — Set sustainability strategy relevant for your industry

To ensure sound strategy setting we will work with:

- Industry relevant benchmark
- Stakeholder feedback (if available)
- Top-management sustainability ambition
- International sustainability framework SDGs

2 — Identify sustainability indicators to measure & disclose

Choose relevant set of sustainability indicators to:

- Score well in investors evaluation schemes
- Prepare for disclosure of Principal Adverse Impact indicators (under SFDR)
- Set strong base for KPIs and sustainability programs

3 — Set sustainability goals and action plan

KPIs should be set in a way to:

- Cover sustainability strategy scope
- Resonate with climate law targets
- Be realistic given the company maturity and set timeline

4 — Set governance structure and reporting processes

Ensure that:

- Governance structure is set
- Responsibilities are assigned
- Data monitoring and collection is ensured
- KPIs tracking and evaluation is performed

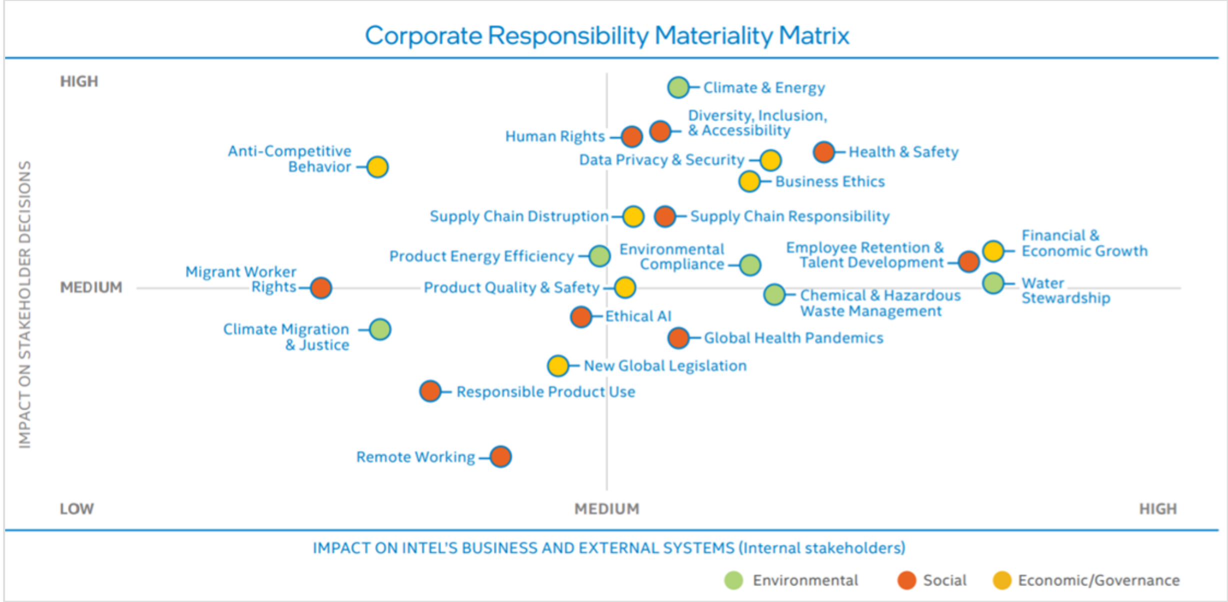
5 — Non-financial report preparation

Inform about:

- Goals
- Performance
- Progress
- Ambitions
- Projects
- Policies

Materiality Assessment

Materiality matrix creation

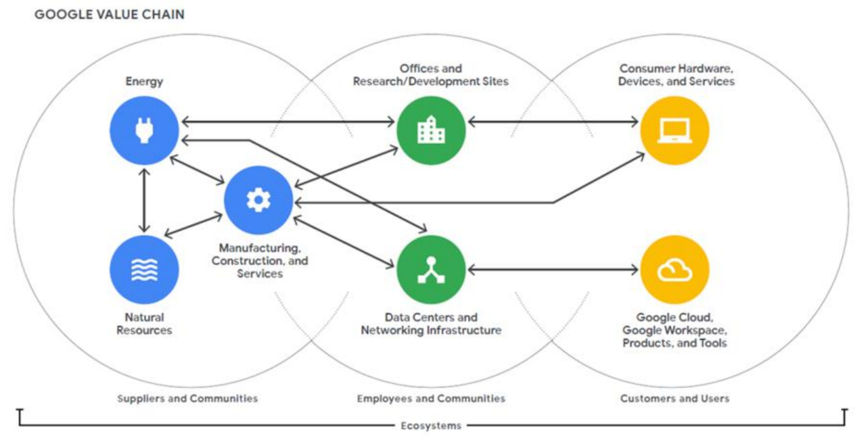


Source: Intel Materiality Matrix (http://csrreportbuilder.intel.com/pdfbuilder/pdfs/CSR-2020-21-Full-Report.pdf)

Mapping SDGs & SDG Targets

Sdg	Goal	Sdg	Target	Material Topics
	Goal 12 – Ensure sustainable consumption and production patterns	12.5	By 2030, substantially reduce waste generation through prevention, reduction, recycling and reuse	Production waste management and recycling
		12.4	By 2020, achieve the environmentally sound management of chemicals and all wastes throughout their life cycle, in accordance with agreed international frameworks, and significantly reduce their release to air, water and soil in order to minimize their adverse impacts on human health and the environment	Production waste management and recycling
	Goal 13 – Take urgent action to combat climate change and its impacts	13.2	Integrate climate change measures into policies, strategies and planning	Environmental pillar strategy covering energy, water, waste, natural resources

Identify value chain



Source: google value chain https://www.gstatic.com/gumdrop/sustainability/google-2020-environmental-report.pdf

Climate related frameworks/standards - SBTi

What is the Science Based Targets initiative?

- Initiative by CDP, WWF, UN Global Compact and World Resources Institute
- An official validation of science-based targets by the SBTi gives climate targets more credibility towards stakeholders
- Offers **methods and tools** for corporate “science-based” target setting
- Provides **mechanism for official validation** of targets against a set of criteria
- Builds a platform **for credible communication** around science-based target-setting

SCIENCE BASED TARGETS
DRIVING AMBITIOUS CORPORATE CLIMATE ACTION

Targets are considered **‘science-based’** if they are **in line with** what the **latest climate science** deems necessary to meet the goals of the Paris Agreement **– limiting global warming to well-below 2°C** above pre- industrial levels and **pursuing efforts to limit warming to 1.5°C**.

SBTi has established the accepted standard on SBTs, setting out 24 criteria for SBTs and a process for entities to develop and validate their targets.

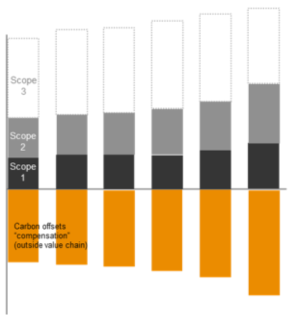
It plays an important role in independently assessing and approving SBTs so that they're credible in the market. SBTi also defines and promotes best practice and offers useful tools and guidance.

The SBTi will release **new criteria** at the end of 2021 which will come into force from **15 July 2022**

- **Increase in minimum ambition level** for scopes 1,2 & 3
- Indication of **reduction of applicable target options for scope 3**
- Companies setting targets before July 2022 according to current criteria will have to **adapt to the new strategy within five years**

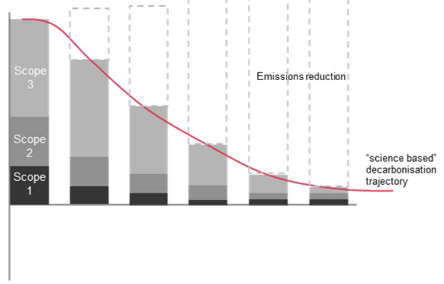
Selection of the suitable Carbon Targets

Carbon neutral (Scope 1,2)



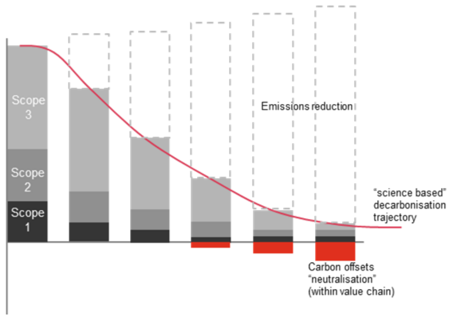
Company commits to purchasing **sufficient carbon offsets** to compensate for all emissions

Science Based Target (SBT)



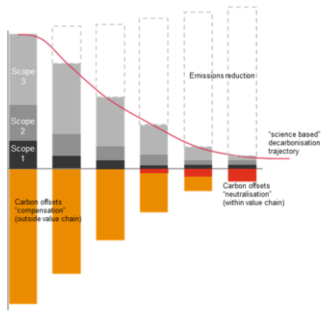
Company commits to **reducing emissions** in line with a recommended 'science-based' trajectory by a target date. **No offsets** are used for this reduction.

SBT + Net Zero* by a target date



Company commits to **reducing emissions** in line with a recommended 'science-based' trajectory by a target date. **Offsets are used** for remaining emissions.

Carbon neutral now and + SBT + Net Zero* by a target date



Company **purchases offsets** for all emissions now; and commits to **reducing emissions** in line with a recommended 'science-based' trajectory by a target date.

- Need-to-know: Risk of being accused of greenwashing without carbon reduction.
- In practice: Some companies commit to scopes 1 and 2 only, some to all scopes.

- Need-to-know: With SBTi, Scope 3 is within the coverage if over 40% of emissions. Net zero and carbon neutrality are often used interchangeably, however net zero has a stronger connotation in terms of commitment.
- In practice: Some companies commit to intensity targets, rather than absolute emissions to factor in business growth.

How finance professionals are helping to advance ESG reporting

EY ESG data and controls survey findings, May 2022

This report and the findings are based on a survey distributed to finance professionals from US-headquartered, publicly traded companies. In total, 72 chief accounting officers and controllers from some of the largest US companies responded to the survey. The findings were supplemented by interviews conducted with members of eight public companies, representing the surveyed population.

Where is your ESG information currently residing? (select all that apply)

Variety of software applications addressing individual or several ESG topics	60%
Excel	55%
ESG-specific software solution	10%
Software solution currently used for financial reporting (e.g., ERP)	15%
Other	10%

https://assets.ey.com/content/dam/ey-sites/ey-com/en_us/news/2022/ey-esg-report-may-2022.pdf

ESG Management Solution

Our solution helps you to collect ESG data, calculate indicators, set and track ESG KPIs, export or preview data in interactive dashboards from across all your entities. It will also facilitate the reporting process, ensure consistent calculations while keeping your ESG data safe and accessible from a single spot. This will help you to be compliant with ESG regulations, share ESG data with stakeholders and strategically manage ESG performance.

1 Support for your strategy

Integrated dashboards provide your management with a required level of transparency, enabling and improving strategic management of sustainability by both C and B level management.

2 Easy data mining

The ESG Management Solution provides means to streamline and automate the input of sustainability data based on NFRD and CSRD regulations, saving your time and money.

3 Access to global know-how

PwC sustainability teams have been implementing ESG solutions and tools across the globe. We are ready to support your compliance and provide you
with combined professional experience of our staff.

pwc ESG Management Solution
A PwC Product

Key features

- Integrated solution for the management, processing, storage, visualisation and reporting of non-financial data based on the most common ESG reporting methodologies
- Own KPIs, selection of indicators to report, method of calculation and whether the indicators should be calculated using own variables (e.g. emission factors) or data from internationally recognised databases
- Possibility to connect tool to existing data or reporting systems (through APIs or cloud data integration tools) or use technology for text recognition (OCR) to automatise the data input
- A data can be generated at the level of individual entities or as a group consolidated report
- Document library for all relevant documents and all ESG data at one spot
- Collaboration across different entities and cooperation of several people

Pavel Štefek
ESG Partner
pavel.stefek@pwc.co
m
+420 731 635 0810

Ondřej Rybka
Assurance Services
ondrej.rybka@pwc.co
m
+420 731 588 122

Vladimír Jaroš
Director, Digital Enablement
vladimir.jaros@pwc.co
m
+420 734 527 144

Zuzana Vaněčková
ESG Services
zuzana.x.vaneckova@pwc.co
m
+420 604 581 717

Typical ESG metrics

Environmental

- **GHG emissions**
  - Scope 1, 2 and 3 greenhouse gas (GHG) emissions
- **Energy management**
  - Total energy consumed
  - Percentage grid electricity
- **Water management**
- **Total water withdrawn/consumed**
- **Waste management**
  - Amount of waste generated
  - Amount of hazardous waste generated
- **Environmental violations**

Social

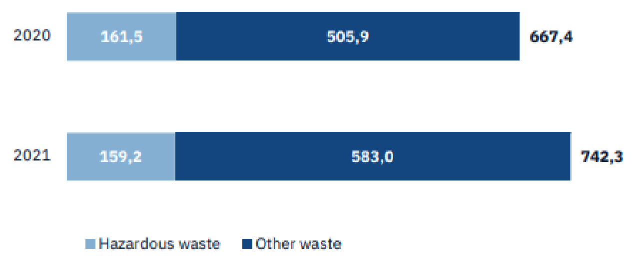
- **Diversity & inclusion**
  - Workforce / Management/ Board representation by gender/ ethnicity
- **Health & safety**
  - Lost-time injury and illness rate
  - Safety incidents
- **Community involvement**
  - Employee volunteer hours
  - Money donated
  - Jobs created
- **Product quality & safety**
  - Number of recalls issued
  - Social responsibility audits of direct suppliers

Governance

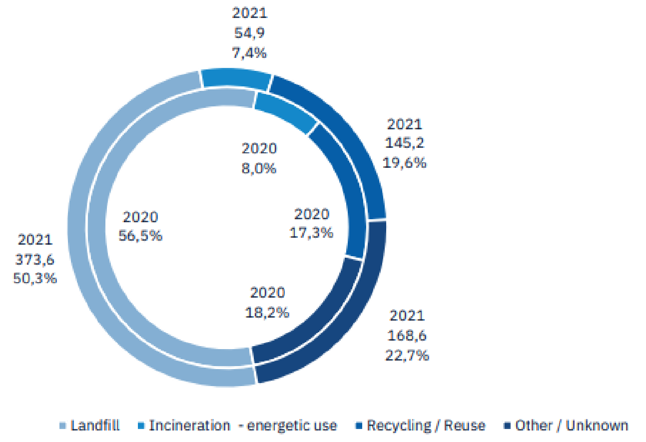
- **Total monetary loss as a result of legal proceedings associated with corruption or bribery**
- **Existence of whistleblower policy**
- **Employees trained in the code of conduct**
- **Number of misconduct cases**

Example of ESG Report content

Waste generated by category - Group (t)



Waste by disposal method - total (t, %)

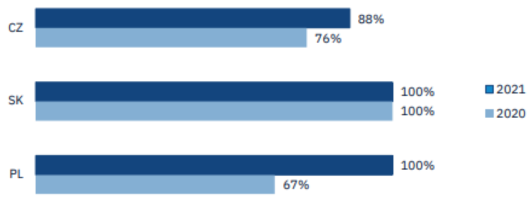


Training and development

Developing our employees is one of the pivot areas we build our sustainability strategy on. Our talent management programme is designed to reach employees at all levels and is an important way we maximize engagement and retention.

Hiring, selecting and developing future leaders, as well as evaluating employees in alignment with our values, is standard across the enterprise. Our ambition is to recruit 80% of our top and middle managers from within. In 2021, we successfully increased the share of evaluated employees in the Czech Republic and Poland.

% of employees with performance evaluation



https://img.auresholdings.eu/attachment/4191.pdf

COMPLIANCE MANUAL

The Compliance manual is a set of basic rules that ensure compliance across the Group's areas of activity. The Compliance manual also outlines the role of the Compliance Officer and describes the procedure for dealing with incidents and breaches of legal and internal regulations. Each employee must report any breach or suspected breach to his or her supervisor; for more serious incidents and compliance breaches, the Compliance Officer must also be informed. The content of the compliance manual is summarized in the brochure "Compliance Code", which is a practical and digestible guide for employees.

We have been working on increasing employee awareness of the Company's policies in the compliance area via internal communication and the Company's intranet. We aim to take this several steps further in 2022, preparing dedicated e-learning trainings and courses.

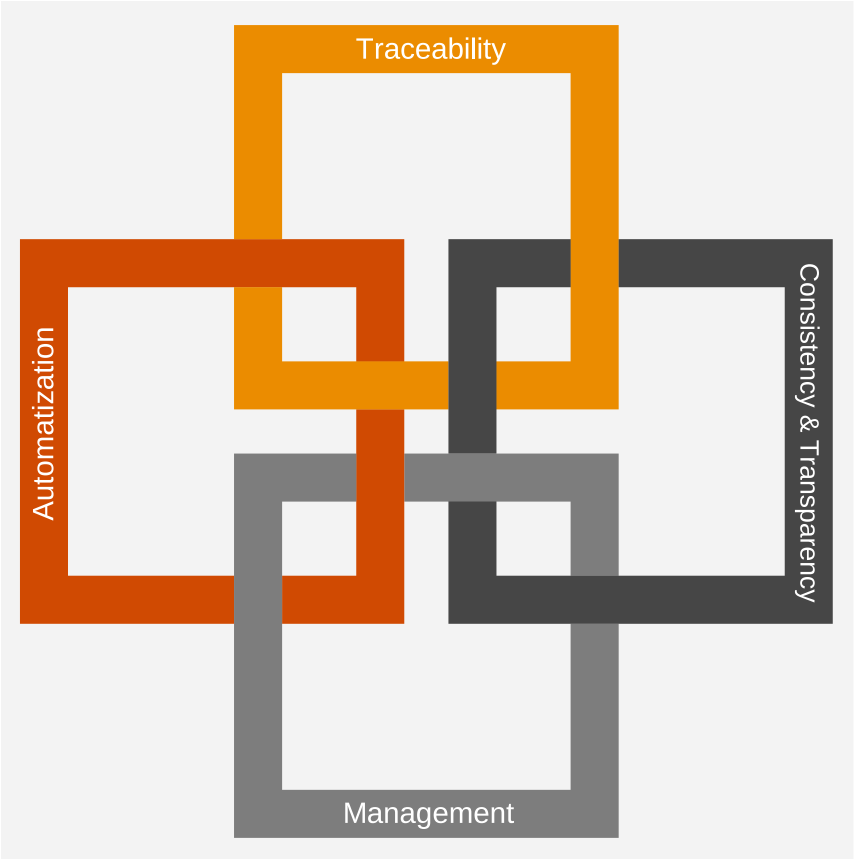
PRINCIPLES OF PROTECTION AGAINST FRAUDULENT OR CORRUPT BEHAVIOUR

The Group's internal policy stipulates a strict repudiation of corruption and the zero tolerance of it by the AURES Holdings Group. Furthermore, the Group requires all its suppliers, business partners and associates to comply with the ethical standards set out in this directive.

GIFTS AND HOSPITALITY

Rules on accepting and providing gifts and entertainment are clearly established as well as the preventive measures aimed at mitigating the risk of bribery. We also reiterate our zero-tolerance approach to corruptive behaviour. Employees, associates, officers and others acting for and on behalf of the Company may only accept small, customary gifts made for promotional purposes, e.g., diaries, pens, paper notebooks, flowers, chocolates, etc. Other customary gifts with a unit value not exceeding EUR 100 are also permitted. If our employees receive a gift, treat or entertainment worth more than EUR 50, they are obliged to inform the Compliance Officer or enter the information directly into the benefits register. It is forbidden to accept financial or non-financial benefits to which no entitlement exists in the normal course of business, and all employees and associates must expressly refuse to accept such benefits.

Challenges of ESG Reporting



Consistency & Transparency

- Data from various internal systems that do not align with each other
- Various granularity
- Inconsistency across various locations
- Tendency to disclose only positive trends

Traceability

- Zero or limited traceability of data updates
- Limited access to historical data
- Potential gaps for data assurance

Automatization

- High portion of time-intense manual calculations with room for error
- Databases of emission factors are not automated – time and quality constraints
- Difficult to track progress over KPIs in real time

Management of the reporting process

- Unclear responsibilities
- Inconsistent frequency of data collection
- Challenging data verification

1

ESG Reporting – regulatory requirements

Current developments regarding standard setting, regulation and reporting

Numerous new regulatory activities with high complexity and multi-layered effects in a short period of time

Global

Goal: globally applicable standards for sustainability reporting

- IFRS Foundation: **International Sustainability Standards Board (ISSB)**
   „global baseline“
- **TCFD** Climate reporting
- **SEC Climate Disclosure Rules**

EU

Goal: Steering effect and reporting

- Review of NFRD (**CSRD**) and development of EU Sustainability Reporting Standards by **EFRAG**
- Reporting obligations from Art. 8 **Taxonomy Regulation**
- **Sustainable Finance Disclosure Regulation**
- **Corporate Sustainability Due Diligence Directive** (proposal)

EU Member States

Transposition into national law and national emphasis

Corporate sustainability reporting is becoming an integral part of the European finance reporting system

EU Green finance reporting framework

Corporate sustainability reporting is becoming similarly important to financial reporting

	Company	Bank				European union	
Targeted at whom?	Company	Bank				European union	
What is new?	Non-financial report	ESG disclosures	ESG risk model	ESG due diligence	Sustainable products	ESG common database	Control & testing
New EU legislation	CSRD	SFDR, Benchmarking regulation, ECB guidelines / EU Taxonomy					
Activities to be performed	Collect and measure ESG data Govern the goals	Collect ESG data from companies	Perform ESG scoring based on ESG risk modeling	Assign companies to sustainable products	Report regularly towards EU	Evaluates ESG data	Performs controls

The reporting landscape today is an 'alphabet soup' of choice and it is evolving fast – there are significant moves towards a common set of standards

Umbrella reporting standards/frameworks
Covering a breadth of ESG topics

GRI · SASB · IR

Single issue standards/ frameworks/ measurement protocols

CDP · TCFD · CDSB Climate Disclosure Standards Board · TNFD · Greenhouse Gas Protocol · Science Based Targets

Other enabling initiatives

International Sustainability Standards Board

IFRS · CDSB · The Value Reporting Foundation

+ others

World Economic Forum · IBC International Business Council

Impact Management Project

20

European Commission

EU Sustainable Finance Disclosure Regulation

+ many more...

ESG Principles & Guidelines

Sustainable Development Goals · wbcsd · value balancing alliance · UN Guiding Principles Reporting Framework · PRI · OECD Responsible Business Conduct – OECD Guidelines for Multinational Enterprises · IFC International Finance Corporation · Equator Principles · Sustainable Development Goals Knowledge Platform · United Nations Global Compact · UNEP Finance Initiative

Sustainability Ratings & Rankings

World Benchmarking Alliance · Calvert · Refinitiv · RepRisk · S&P Dow Jones Indices · Alliance for Corporate Transparency · Sustainalytics · GGEI · FTSE Russell · Morningstar · MSCI · CSRHub · GRESB · Environmental Performance Index · Social Value International · ISS · Bloomberg · Global 100

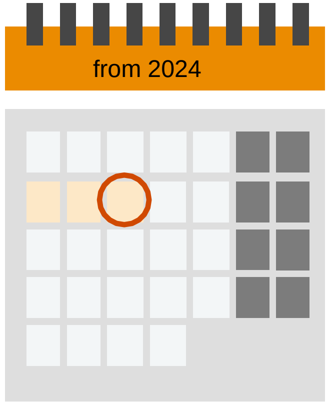
Most commonly used reporting frameworks

Framework	Focus	Target audience	Materiality Definition
SASB	ESG – Impacts to company value	Investors	Intended for use in mainstream financial reports
GRI	Sustainability – Impacts of company on environment, social and economic factors	Stakeholders beyond investors such as customers, suppliers, employees, communities & NGOs	Broad definition focused on impact and stakeholder interest – intended for use in sustainability reports
TCFD	Climate Change – Impacts to company value	Investors, lenders, insurers and other capital market participants (e.g. credit rating agencies, financial regulators, central banks)	Intended for use in mainstream financial reports
CDP	Climate Change – Impacts of company on environment	All stakeholders including investors, customers, businesses & regulators	No materiality definition applied

Corporate Sustainability Reporting Directive (CSRD)

Main changes

Who?	Significant **extension of the scope** of sustainability reporting – **Large companies** and companies that have **publicly-listed securities**
What?	• **Expanding the content** of sustainability reports • EU will create own reporting **standards (technical advice by EFRAG)** • **Double materiality** clearly defined
Where?	Sustainability report mandatory component of the (consolidated) **management report (in a dedicated section)**
How?	**Electronic format** and **tagging** of sustainability reports mandatory
Responsibility?	Responsibility of management and governance and **new role of the audit committee**
Enforcement?	Clear responsibilities for **preparation, oversight and enforcement**
Assurance?	**Assurance obligation for** sustainability reports with **limited assurance;** later transition to **reasonable assurance**



Warning!
The application of the reporting requirements is staggered depending on the respective scope of application.

Large companies are defined as companies that meet **at least two** of the following three size criteria at the balance sheet date:

- Total assets: at least EUR 20 000 000
- Turnover: at least EUR 40 000 000
- Average number of employees in the accounting year: at least 250.

Political agreement in trilogue process on the CSRD

Reporting obligations to start with financial year 2024

2021		2022		2023		2024		2025		2026	
H1	H2	H1	H2	H1	H2	H1	H2	H1	H2	H1	H2

CSRD

Q2 2021 – mid-2022: negotiations on CSRD proposal (Trilogue)

Estimated Q4 2022 Approval of final CSRD, followed by transposition into national law.

Application of CSRD for FY 2024 (first reporting in 2025) for NFRD-companies/groups**

Application of CSRD for FY 2025 for large companies/groups not already subject to NFRD (first reporting in 2026).

Application of CSRD for FY 2026 for listed SMEs*, certain small and non-complex institutions and captive insurance undertakings (first reporting in 2027).

EFRAG (European Sustainability Reporting Standards, ESRS)

29.4.2022-8.8.2022
Consultation of the ESRS Exposure Drafts

First Set of reporting standards to be submitted to the EU Commission

Nov 2022
Handover to EU Commission,
subsequent adoption of delegated acts (expected: June 2023)

Second Set of reporting standards to be submitted to the EU Commission

Nov 2023
Handover of second set of reporting standards to EU Commission, followed by adoption of delegated acts

Negotiation/Finalization

Publication/Adoption

Application

CSRD: First-time application at a glance

preliminary assessment

FY 2024 (reporting in 2025)	Undertakings already subject to the non-financial reporting directive*
FY 2025 (reporting in 2026)	Large undertakings/large groups that are not presently subject to the non-financial reporting directive*
FY 2026 (reporting in 2027)	Listed SMEs*, small and non-complex credit institutions and captive insurance undertakings Listed SMEs: possibility to opt-out for two years
FY 2028 (reporting in 2029)	Non-EU company reporting (Art. 40a-d EU Accounting Directive)

**discussion ongoing reg. first-time application for non-EU issuers*

EFRAG - Exposure Drafts

SECTOR-AGNOSTIC STANDARDS

Cross cutting standards

- **ESRS 1** General principles
- **ESRS 2** General, strategy, governance and materiality assessment disclosure requirements

Topical standards

Environment	Social	Governance
ESRS E1 Climate change	**ESRS S1** Own workforce	**ESRS G1** Governance, risk management and internal control
ESRS E2 Pollution	**ESRS S2** Workers in the value chain	**ESRS G2** Business conduct
ESRS E3 Water & marine resources	**ESRS S3** Affected communities	
ESRS E4 Biodiversity & ecosystems	**ESRS S4** Consumers and end-users	
ESRS E5 Resource use and circular economy		

COMING LATER

- **SECTOR-SPECIFIC STANDARDS**
- **SME-PROPORTIONATE STANDARDS**
- **STANDARDS FOR NON-EU REPORTING**

Financial risks associated with new regulation

Compliance with the regulation is not only important to avoid financial repercussions but also presents a growth opportunity. Not complying can cause administrative penalties and exclusion from investments portfolios.

1. First, a public statement about the breach.
2. Second, an order on the name of the entity requiring to change the conduct.
3. Third, financial sanctions.

The nature of the sanctions and the fines' amount will depend on the different Member States. For example,
if German businesses don't report compliance to the German version of the Non-Financial Reporting Directive (the Directive being amended with the CSRD) they face fines up to the amount which is the highest of the following: €10 million or 5 % of the total annual turnover of the company or twice the amount of the profits gained or losses avoided because of the breach.

On the other hand, French businesses face no fines
if they don't report according to the NFRD unless an interested party asks for the disclosure of the non-financial information.
If it is not available, subsequently, financial penalties can be imposed by a judge.

ESG Assurance

Building trust in ESG reporting through assurance

Why assurance over ESG reporting matters for your business

Build trust and demonstrate your ESG accountability

Improve internal processes and controls

Create business opportunities built on ESG principles

Mitigate risk of fraud and greenwashing

Act upon or future-proof related compliance risk

Our ESG assurance approach

- Planning and scoping
- Detailed testing using a tech-enabled approach
- Assessing ESG reporting processes a controls
- Reporting and deliverables

Level of assurance

- Internal assurance
- Limited external assurance – since 2027
- Reasonable assurance – no later than 1 October 2028

Example: negative conclusion

"Based on the procedures performed and the evidence obtained, nothing has come to our attention that causes us to believe that the disclosures in the Company's report for the period from 1 January 20XX to 31 December 20XX have not been prepared, in all material respects, in accordance with the applicable reporting framework."

Example: positive opinion

"In our opinion, the disclosures in the Company's report for the period from 1 January 20XX to 31 December 20XX is presented in accordance with the applicable reporting standard and is, in all material respects, fairly stated"

Timeline

Why assurance over ESG reporting matters for your business

Methodology

- ISAE 3000 (Revised) Assurance Engagements Other Than Audits or Reviews of Historical Financial Information; and
- ISAE 3410 Assurance Engagements on Greenhouse Gas Statements (US AT-C section 205 Assertion-Based Examination Engagements and AT-C section 210 Review Engagements).

Appropriate subject matter

whole ESG report x selected indicators x carbon footprint

Suitability and availability of criteria

- Recognised framework x Entity-developed criteria
- Available for intended users

Assessment of internal control framework

Identifying areas of risks

Inherent, control, detection, assurance

Materiality thresholds

overall materiality, performance materiality, De minimis SUM posting

Testing

test of controls, substantive or review analytical procedures, test of details (targeted testing, non-stat. Sampling, Accept-reject testing

Evaluating the results, Written representation, Documentation, Conclusion forming

ESG Assurance Criteria

Subject matter	Recognised framework	Reporting criteria
Waste generated	According to GRI standards 306, the reporting organisation shall report total weight of waste generated in metric tons, and a breakdown of this total by composition of the waste. The reporting organisation shall exclude effluent, unless required by national legislation to be reported under total waste and use 1000 kilograms as the measure for a metric ton.	The reporting organisation could further refine its reporting criteria, for example: General waste sent to landfill (tonnes) is material that has been finally disposed of to landfill or incineration. Materials diverted for recycling (tonnes) are cardboard, polythene and polystyrene from secondary product packaging and transit packaging, and carrier bags collected in store at the till point. The waste data we report relates to all domestic stores where our third-party waste provider arranges the waste collections. Waste data is not available from the two international stores. Where live data is not available, the waste contractor provides estimated data which is reviewed by us to ensure it is appropriate.

Subject matter	Reporting criteria
Water extracted in m^3	Each factory records water extracted for use in manufacturing from various sources. These sources are classified as; municipal/piped sources, groundwater (direct extraction by site), surface water (direct extraction from river or lake), brackish/saline sources (direct extraction from estuary or sea), water delivered to site by tanker, noncontact cooling water (any source). Total water extracted is the sum of these sources, measured in cubic metres.

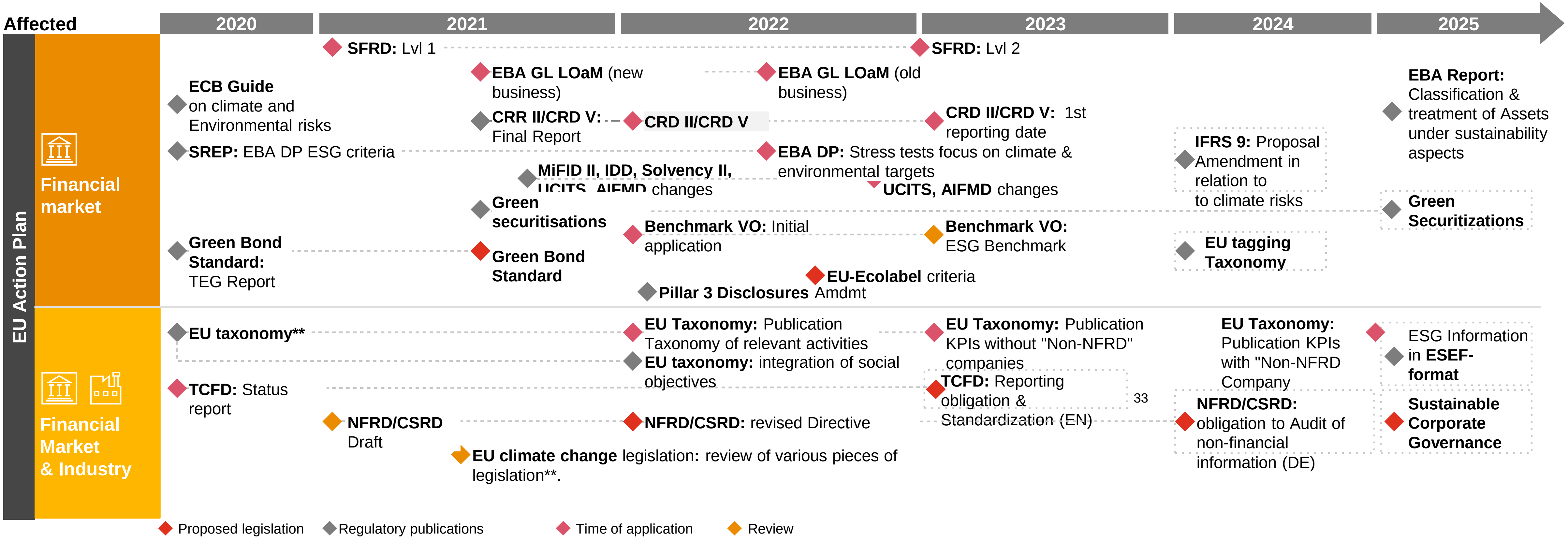
Implementace ESG do procesu banky včetně taxonomie reportingu

Zdeňka Jirasová
Matej Marsala

Implementace ESG

Regulators are creating new requirements for banks to consider environmental, social and governance (ESG) factors

A large number of regulatory initiatives are in the pipeline until 2025



33

* The EU Action Plan 2 has not yet been finalised. The publication of the final contents of the EU Action Plan 2 is expected for July 2021.
** Review of EU ETS, Burden Sharing Regulation, LULUCF, Energy Efficiency Directive, Renewable Energies Act, CO_2 emission standards for passenger cars (Art. 2 para. 4 and Recital 17, EU Climate Change Act)

ESG effects bank from various angels

Every business unit will be affected

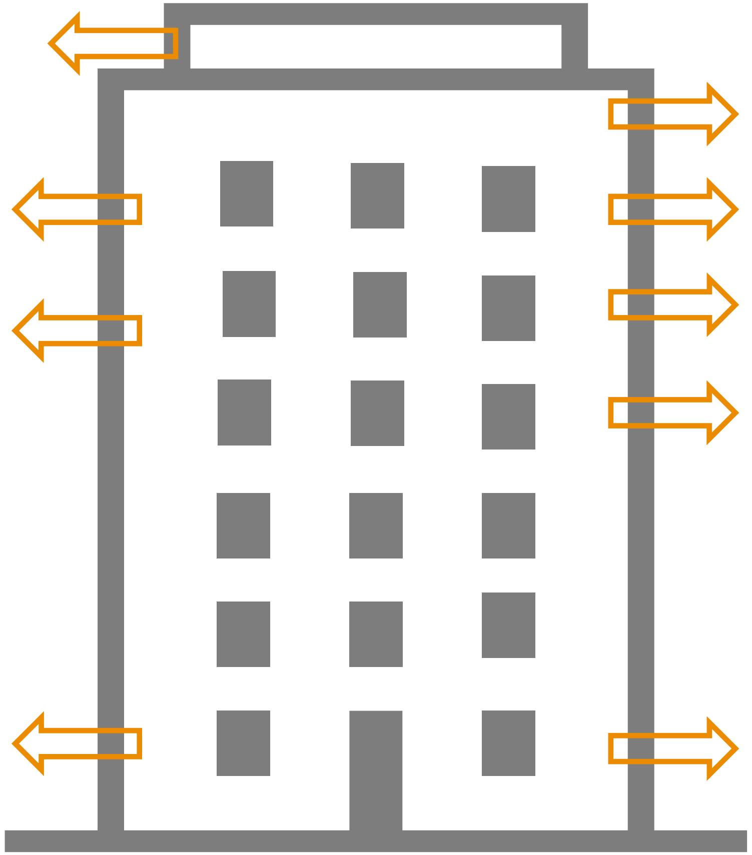
Adjustment of product and client portfolio | **Sustainability in governance and business strategy**

Identification / Classification of sustainable assets (taxonomy)

Understanding customers' ESG preferences, and incorporating into these into the sale of products

Consideration of ESG associated risks in pricing and risk management. It is important to identifying client, counterparty and transactional ESG risks, and integrating these into investment, underwriting, and lending decision making. Enhancing existing risk modelling and stress testing capabilities, for climate risk.

Integration of ESG based KPIs in sales processes



Maintaining currency with the rapidly evolving, and complex regulatory climate risk and sustainable finance landscape

Refinancing based on sustainable instruments

Managing supply chain ESG risks, and ensuring firms do business with suppliers with consistent values and standards

Consideration of ESG risks in capital management

Reporting of ESG risks and impact to authorities and stakeholders. Communicating credibly and effectively to the market the sustainability of firms' operations and financing, it's ESG impacts, and the resilience of its strategy to climate change. Providing transparency over firms' product offering to avoid risks from green and impact washing.

Bank business unit

- **Risk**
- **Finance**
- **Legal**
- **Front office**
- **Procurement & HR**
- **Communication**
- **Strategy**
- **Sustainability**
- **Internal Audit**

ESG implementation vs. audit activity

What have to be considered while performing audit assistance

1. **Analysis of current situation** (ESG strategy, organization structure with set responsible person / committees etc. for ESG agenda, proper reflection of all applicable regulations to the methodology, current data availability across the financial institution, collection / validation / monitoring and internal / external reporting process, risk appetite, concrete steps toward meeting E, S, G criteria etc.)

2. **Materiality risk assessment** (identification of materiality matrix in order to set material and non-material risks - credit, operational, market and liquidity, setting up monitoring system in order to monitor changes over time)

3. **Data** (retail / corporate / immovable assets - collection from clients / publicly available sources, verification and up-to date maintenance, responsibility)

4. **Setting Risk Appetite Statements limits** of the bank, or in line with external benchmarks (e.g., a climate science-based emission path that follows the Paris Agreement) in order to manage the banks exposure.

5. **Setting KPIs** that would be trackable in order to help understand the environmental, social and governance impact of their operations.
Green products and sustainable banking (green loans, green advisory etc.)

6. **Reporting** (internal / external monitoring process design, systems adjustments etc.)

Taxonomie

The taxonomy regulation

Taxonomy

The Taxonomy Regulation is the EU Commission's principal mechanism to address "greenwashing" as it sets out criteria for determining if an activity is environmentally sustainable, including whether the activity contributes to, or does not significantly harm, one or more specified environmental objectives. The Taxonomy Regulation requires further disclosures which need to be made in addition to those set out in the SFDR. The taxonomy regulation is effective from 01 January 2022.

There are three main groups EU taxonomy rules apply to: Financial market participants, including occupational pension providers, offering financial products in the EU; Large companies which are required to report under the Non-Financial Reporting Directive (NFRD), which is set to be revised by the CSRD; and the EU and its member states.

The European taxonomy regulation plans to extend the non-financial mandatory reporting for financial and non-financial organizations.

Regulation no. 2020/852 (Article 8)

- reporting with compliance of Article 3 and 9 – climate change mitigation and climate change adaptation
- delegated act – from 1 January until 31 December 2022 financial undertakings are required to report the following information:
  - proportion of total assets of exposure to Taxonomy non-eligible and Taxonomy eligible economic activities
  - excluded – exposure to central governments, central banks and supranational issuers (numerator and denominator)
  - excluded – derivatives (numerator)
  - excluded – exposure to companies that are not obliged to publish non-financial information pursuant to Article 19a or 29a of Directive 2013/34/EU (numerator)
  - the qualitative information – Annex XI
- KPIs – annexes III, V, VII, and XI shall be disclosed from 1 January 2023
  - annex III – KPIs of asset managers
  - annex V – KPIs for credit institutions
  - annex VII – KPIs of investment firms
  - annex XI – qualitative disclosures
- sections 1.2.3. - KPIs on services other than lending – Fees and Commissions (F&C KPI) and 1.2.4.- Other disclosures in the GAR: GAR for the trading portfolio of Annex V shall apply from 1 January 2026

The Taxonomy Regulation is one of the cornerstones of the EU Action Plan on Sustainable Finance

Key Purposes

1 Provide economic actors with a **single common list of economic activities** that are considered as environmentally sustainable and of any conditions to be met.

2 **Steer investment** towards the economic activities that will help attain the EU environmental objectives and the goals of the Paris Agreement.

3 Act as the **single yardstick** to measure the sustainability of a company's economic activities or a financial institution's loan portfolio or investment portfolio. Increase **transparency, consistency and comparability** between financial institutions.

Key Characteristics

1 The Taxonomy **does not make investment in the list of sustainable activities mandatory.** It is up to every company to decide.

2 Investment in companies of the brown economy can qualify as Taxonomy-aligned if the **purpose of the investment meets the conditions of the Taxonomy.**

3 **Financial incentives** are planned in the form of a rebate on capital requirements on Taxonomy-aligned loans.

4 The Taxonomy creates **new disclosure requirements** for all large companies (not only financial institutions)

The Taxonomy identifies the critical sectors and activities which need to decarbonise to achieve the EU's climate goals.

The Taxonomy Regulation focuses on six environmental objectives:

1. Climate change mitigation
2. Climate change adaptation
3. Sustainable use and protection of water and marine resources
4. Circular economy
5. Pollution prevention and control
6. Protection of biodiversity and ecosystems

	Mitigation	Adaptation
Agriculture and forestry	8	8
Manufacturing	9	9
Electricity, gas, steam, and air conditioning supply	25	25
Water, sewerage, waste and remediation	12	12
Transport	10	10
Information and Communication Technologies (ITC)	2	–
Buildings	4	2
Insurance services	–	1
Engineering services	–	1

To be considered aligned with the Taxonomy, an economic activity has to comply with four conditions

1 **Identification of eligible activities**

List defined in delegated acts
mainly according to European NACE nomenclature

2 **Substantial contribution**

Criteria for achieving at least one of the environmental objectives

3 **DNSH**

Do not cause significant harm to any of the other 5 objectives

4 **Compliance with minimum safeguards**

Human Rights & principles and fundamental rights at work

5 **KPIs**

Eligibility

Compliance with technical criteria

Alignment with the Taxonomy

=

Sustainable activities

Free online tool for the classification of counterparties and projects: **Taxonomy Compass**
https://ec.europa.eu/sustainable-finance-taxonomy/tool/index_en.htm

Timetable for financial undertakings

Eligibility Reporting

January 2022

Reference period: 2021

Comparative Information ✖

Eligibility Reporting

January 2023

Reference period: 2022

Comparative Information ✖

Alignment Reporting
(except trading book and fees & comm. KPIs)

January 2024

Reference period : 2023

Comparative Information ✔

Possible extension to non-NFRD entities(1)

January 2025

Reference period : 2024

Comparative Information ✔

Trading book and Fees & Comm. KPIs

January 2026

Reference period: 2025

Comparative Information ✔

(1) The exposures to non-NFRD undertakings that publish voluntarily taxonomy reporting disclosures is subject to the EC review of Taxonomy Regulation expected by 30 June 2024.

Disclosure rules common to all financial undertakings

Calculation rules

Assets excluded from the KPIs		
Asset categories	**Numer.**	**Denom.**
Exposures to central governments, central banks and supranational issuers	x	x
Derivatives	x	
Exposures to non-NFRD undertakings	x	

Review of the treatment of sovereigns and non-NFRD undertakings expected by 30 June 2024.

Possible integration of non-NFRD undertakings that would voluntarily disclose taxonomy KPIs from 1 January 2025, subject to positive conclusions of the EC review.

Quantitative disclosures

Granular quantitative data to present in **templates** that are **specific to each type of financial undertaking**.

Includes information on **environmental objectives**, the **enabling or transitional nature** of financed activities or the **type of counterparty**.

- **Optional use for eligibility reporting in 2022 and 2023**
- **Mandatory use from 2024 for alignment reporting over 2023**

Qualitative disclosures

1. **Contextual information** in support of the quantitative indicators (scope of assets, data sources and limitation…)
2. **Explanations of the nature of Taxonomy-aligned economic activities** and their evolution over time, starting from the second year of implementation
3. Description of the compliance with Taxonomy Regulation in the **business strategy**, **product design processes and engagement with clients**
4. For credit institutions not required to disclose quantitative information for trading exposures, **qualitative information on the alignment of trading portfolios**
5. **Additional or complementary information** in support of strategies and the weight of the financing of Taxonomy-aligned economic activities in their overall activity

Reporting

Overview of ESG Disclosures – Pillar 3

Pillar 3 disclosure on ESG risk

Article 449a of the CRR – from 28 June 2022, the Reporting Requirements will apply to “large institutions which have issued securities that are admitted to trading on a regulated market of any Member State“. An institution is deemed as “large”
if it meets any of the conditions in Article 4(146) of the CRR, namely if:

- **It is a “Globally Systemically Important Institution“, as defined in Article 131 of the Capital Requirements Directive (the “CRD“);**
- **It is an “Other Systemically Important Institution“, as defined in Article 131 of the CRD;**
- **It is one of the three largest institutions in terms of total value of assets in the Member State in which it is established; and / or**
- **The total value of its assets on an individual basis, or, where applicable, on the basis of its consolidated situation in accordance with the CRR and the CRD, is equal to or greater than €30 billion.**

Overview of ESG Disclosures – Pillar 3

Following **Article 449a of** Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR), large institutions which have issued securities that are admitted to trading on a regulated market of any Member State must from 28 **June 2022** disclose prudential information on ESG risks, including transition and physical risk, as defined in the report referred to in Article 98(8) CRD.

	What to disclose?	Examples of Disclosures
RISK DISCLOSURES	CLIMATE CHANGE TRANSITION RISK Information **on exposures** to sectors or assets that may highly contribute to climate change	▸ Exposures to fossil fuel companies excluded from sustainable climate benchmarks, and to other carbon-related sectors ▸ For real estate exposures, distribution of the exposures by energy performance of the collateral
	CLIMATE CHANGE PHYSICAL RISK Risk exposures subject to extreme weather events (sector/geography)	▸ Assets subject to impact from chronic climate change events by sector and geography ▸ Assets subject to impact from acute climate change events by sector and geography
MITIGATING ACTIONS	Actions that support counterparties in the **transition** to a carbon neutral economy but that do not meet taxonomy criteria	▸ Building renovation loans that improve the energy efficiency of the building but do not meet the taxonomy screening criteria
	Actions that support counterparties in the **adaptation** to climate change but that do not meet taxonomy criteria	▸ Loans to build barriers against flooding, or water management mechanisms against draughts but to not meet the taxonomy screening criteria

	What to disclose?	Examples of Disclosures
GREEN ASSET RATIO	Information **on exposures towards NFRD Corporates and Retail financing** taxonomy-aligned activities consistent with Paris Agreement goals that contribute substantially to climate change mitigation (CCM) and adaptation (CCA), including information on transitional and enabling activities.	▸ **Contributing to CCM:** Generation of renewable energy ▸ **Enabling CCM:** Manufacture of renewable energy technologies ▸ **Contributing to CCA:** Afforestation ▸ **Enabling CCA:** Engineering activities for adaptatio to climate change
BANKING BOOK TAXONOMY ALIGNMENT RATIO	Information **on exposures towards non-NFRD corporates not assessed in the GAR** financing taxonomy-aligned activities consistent with Paris Agreement goals, contributing substantially to CCM and CCA. **Simplified assessment,** based on bilateral information and estimates.	
QUALITATIVE DISCLOSURES	Qualitative information on environmental, social and governance risks	▸ Governance arrangements ▸ Business model and strategy ▸ Risk management

Timeline – Pillar 3

1. Information on ESG risks must be collected from **28 June 2022** – annual basis for the first year and semi-annually thereinafter.

2. The first disclosure reference date will be **31 December 2022** (or relevant end-of-year disclosure for financial years not ending in December) and information will be made publicly available by institutions during the first months of 2023, on the same date as the date on which institutions publish their financial statements for 2022 or as soon as possible thereafter.

3. A **phase-in period until June 2024** (end of June 2024 first disclosure reference date) is proposed for disclosures on institutions' **scope 3 emissions** and alignment metrics. However, during the transitional period, institutions must explain the methodologies they are developing to measure and estimate their scope 3 emissions and the sources of data that they plan to use. Those institutions that are already estimating this information should start disclosing it, using estimates and ranges when relevant.

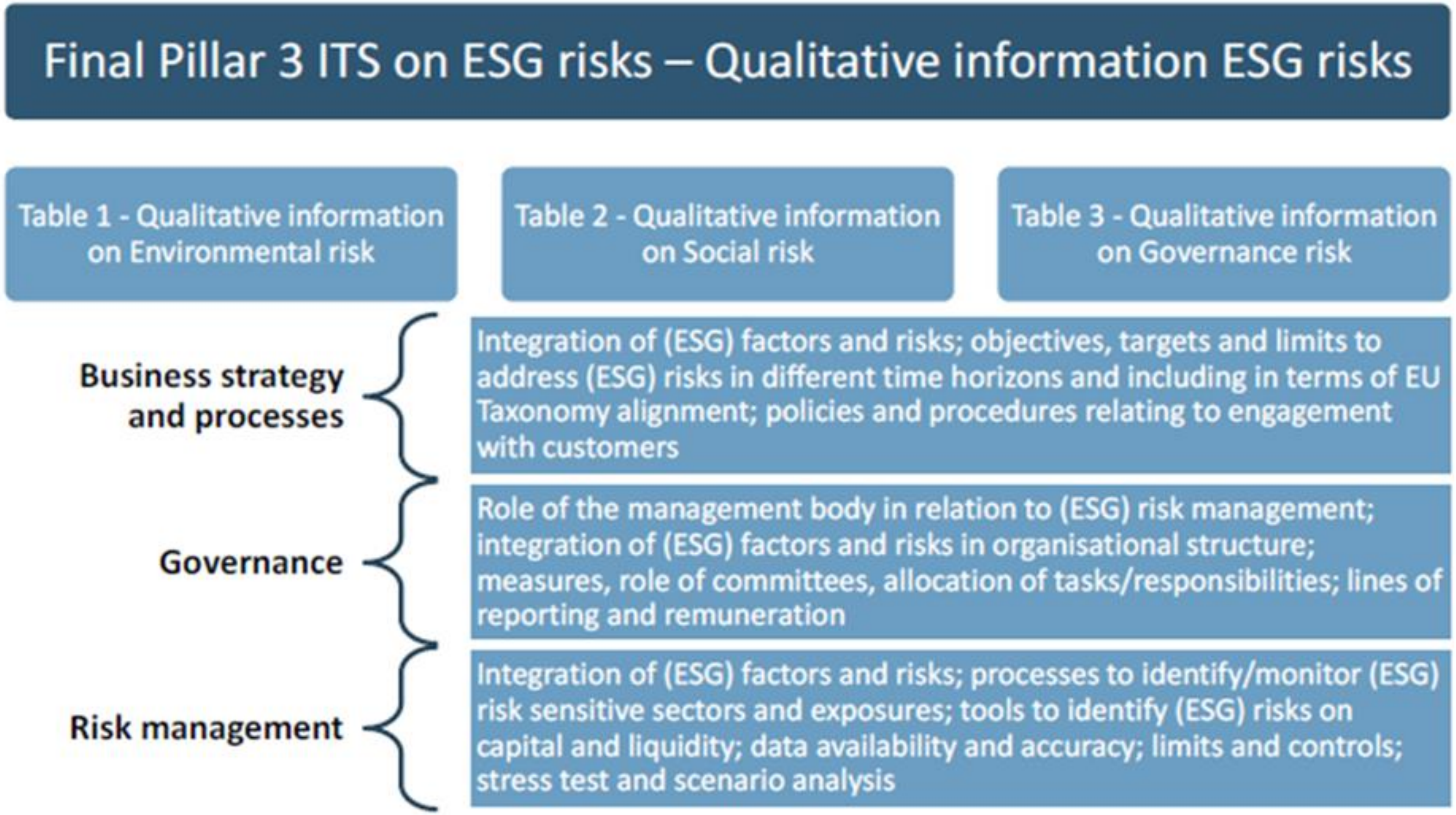
4. The disclosure of information on the **GAR will start to apply in 2024 for data as of end-2023.**

5. The additional and separate information on the **BTAR will apply from June 2024,** which means that institutions will include this additional and separate KPI in their end of June 2024 disclosure reference date Pillar 3 reports for the first time.

6. **Information on environmentally sustainable exposures (CCM) in Template 1 will be disclosed by institutions starting from end of December 2023** (for exposures included in the numerator of the GAR) and **end of June 2024** (for exposures included in the numerator of the BTAR only) as the first disclosure reference date.

Qualitative disclosures on ESG risks – Pillar 3

Overview



These disclosures are designed in line with the EBA's '[Report on management and supervision of ESG risks for credit institutions and investment firms](). The tables and instructions rely on the definitions, terminology and structure presented in that report.

Detailed instructions for filling out the tables can be found in [Annex II - EBA draft ITS on Pillar 3 disclosures on ESG risks (instructions)]()

CSDR & NFRD

Corporate Sustainability Reporting Directive („CSRD“)

The CSRD is a new EU legislation **extending the existing scope and reporting requirements for what concerns the environmental and social impact activities of large companies**. The application of CSRD will start on 1 January 2025, for the 2024 financial year.

It also applies to companies headquartered outside of the EU but with a significant presence in it should still pay attention to the CSRD.
More specifically, **CSRD will apply to non-EU companies with annual revenues of over €150 million generated inside the EU that have a significant EU branch**.

The application of the regulation will take place in three stages:

- **1 January 2024 for companies already subject to the non-financial reporting directive**
- **1 January 2025 for large companies that are not presently subject to the non-financial reporting directive**
- **1 January 2026 for listed SMEs, small and non-complex credit institutions and captive insurance undertakings**

Non-Financial Reporting Directive („NFRD”)

Directive 2014/95/EU amending Directive 2013/34/EU article 19a and 29a

The NFRD started in 2018, it is represented in the Treaty on the Functioning of the EU, and permits all EU member states to set environmental goals that exceed the ones required of them by the NFRD.

The main goal of the NFRD is to allow potential investors, consumers, and various stakeholders to have all the information necessary to decide if it is a business their values align with for participation in the project or service. Non-Financial Disclosures, like the NFRD, allow third parties to influence large companies to take a more sustainable and socially responsible business approach. In general, those who are required to comply with the NFRD should report environmental impacts, how employees are treated and various social outcomes, how they plan to respect human rights, how they prevent anti-corruption or bribery, and how they promote diversity.

Scope of application of the NFRD & CSRD

NFRD

Jan 2022 | Jan 2023

- PIE > 500 employees
- and
  - 20M€ balance sheet
  - or > 40 M€ of turnover

= NFRD scope before or after transposition?

NFRD scope (EU EIP definition) ✔

Scope after local transposition/extension ✘ country-specific

CSRD

Jan 2025 | **Sustainable report with data for 2024**

scope extension

All "**large companies**" * :
→ 2 of the 3 criteria:
- 20M€ balance sheet
- > 40 M€ of turnover
- > 250 employees

→ including European subsidiaries/subgroups of non-EU groups **

All **listed companies** ***
on European regulated markets
→ including listed SMEs
→ including non-EU issuers

*as defined by the European Directive 2013/34/EU and including credit institutions and insurance companies
**exemption for subsidiaries if the information already in the parent company's sustainability reporting and complies with EU standards (or equivalent)
*** except microenterprises, i.e. 2 of the 3 criteria: <350k€ balance sheet, <700k€ turnover, <10 employees

SFDR & MiFID

Sustainable finance disclosure regulation („SFDR“)

It is a set of EU rules introduced to improve transparency in the market for sustainable investment products, to prevent greenwashing and to increase transparency around sustainability claims made by financial market participants.

Regulation EU 2019/2088 on sustainability-related disclosures in the financial services sector

- article 4 – transparency of adverse sustainability impacts at entity level – March 2021
- article 7 - transparency of adverse sustainability impacts at financial product level – by 30 December 2022
- information should be publish on website
- delegated act - regulation 2022/1288 supplementing Regulation EU 2019/2088 from April 2022
- **PAI** – principal adverse impacts – 64 PAI – **18 mandatory** (table 1 of the regulation EU 2022/1288), 46 voluntary – regulation shall apply from January 2023 – by 30 June each year – „Statement on principal adverse impacts of investment decisions on sustainability factors“ – **first disclosure 30 June 2023** (data for 31 December 2022)

Market in Financial Instruments Directive („MiFID”)

The Markets in Financial Instruments Directive (MiFID) is a European regulation that increases the transparency across the European Union's financial markets and standardizes the regulatory disclosures required for firms operating in the European Union

Directive 2014/65/EU

- delegated directive – EU 2017/593
- delegated regulation – EU 2017/565
- delegated directive – EU 2021/1269 amending delegated directiveEU 2017/593 – apply from 22 November 2022
- delegated regulation – EU 2021/1253 amending delegated regulation EU 2017/565 – apply from 2 August 2022