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Driving Sustainable Practices in Modern Business

As environmental, social, and governance (ESG) concerns continue to shape the global business landscape, regulatory bodies have implemented increasingly stringent measures to ensure corporate accountability and transparency. Often challenging to translate into meaningful actions, there is a concerted effort on a global scale to improve the consistency of such measures to encourage organisations to adopt more sustainable and ethical practices.

Fundamentals of ESG

ESG regulations require businesses to disclose their performance against specific ESG standards publicly and represent a comprehensive framework for evaluating how an organisation is managing risks and opportunities related to three critical criteria:

- Environmental: evaluating how businesses impact nature, focusing on areas such as carbon emissions, energy efficiency, waste management, and resource usage.
- Social: examining a company's relationships with its employees, customers, and communities. Among the aspects included are labour practices, diversity, health and safety, and consumer protection.
- Governance: explores the leadership and internal structure of a company. Essential factors include board composition, executive pay, audits, internal controls, and shareholder rights.

Key regulations in 2024

Organisations should consider several key ESG regulations in 2024, many subject to ongoing updates to reflect evolving standards and expectations in sustainability practices.

Sustainability Disclosure Requirements (SDR)

The UK's Financial Conduct Authority (FCA) has introduced the Sustainability Disclosure Requirements, which came into effect in 2023 and continue to be phased in through 2024. These requirements mandate that certain UK-based companies and asset managers disclose their sustainability risks, opportunities, and impacts.

SDR applies to listed companies, asset managers, and regulated asset owners and requires disclosure of climate-related financial information aligned with the Task Force on Climate-related Financial Disclosures (TCFD) recommendations. A key characteristic is the introduction of product labels to help consumers understand the sustainability characteristics of investment products.

Streamlined Energy and Carbon Reporting (SECR)

The SECR framework, which has been in place since 2019, continues to evolve, and businesses should be prepared for potential updates and stricter enforcement in 2024. The SECR builds on The Companies (Directors’ Report) and Limited Liability Partnerships (Energy and Carbon Report) Regulations 2018, with UK companies that are quoted, large unquoted, or large Limited Liability Partnerships (LLPs) in scope. They are required to report on energy use, carbon emissions, and energy efficiency measures; disclosure is mandatory in company annual reports.

Modern Slavery Act 2015

While not new, the Modern Slavery Act continues to be a crucial piece of ESG legislation, requiring businesses to submit an annual statement outlining steps taken to ensure slavery and human trafficking are not occurring in the business or supply chains. The Act impacts organisations with a yearly turnover of £36 million or more and is expected to see increased scrutiny on the depth and quality of disclosures in 2024.

Corporate Sustainability Reporting Directive (CSRD)

The CSRD, which replaces the Non-Financial Reporting Directive (NFRD), is being phased in from 2024 to 2028 and significantly expands the scope of companies required to report on sustainability matters.

The directive applies to all large EU companies and listed SMEs (with some exceptions for micro-enterprises), requires detailed reporting on environmental, social, and governance factors, and introduces mandatory assurance of sustainability information.

EU Taxonomy Regulation

The EU Taxonomy, a classification system for sustainable economic activities, continues to evolve in 2024 with the addition of new environmental objectives. All financial market participants offering financial products in the EU and companies required to publish non-financial statements are within the scope of the regulation.

Its purpose is to address greenwashing and support investors in identifying environmentally conscious investments, with organisations having to disclose how and to what extent activities align with the EU Taxonomy using defined criteria. In 2024, the focus extends beyond climate change mitigation and adaptation to include other environmental objectives.

Sustainable Finance Disclosure Regulation (SFDR)

The SFDR became mandatory in 2023 and continues to be a critical regulation for financial market participants in 2024. SFDR seeks to improve financial sector transparency and direct capital flow to sustainable finance by applying to all EU financial market participants and financial advisers.

Organisations must disclose sustainability risks and adverse impacts at both entity and product levels to improve the clarity and comparability of sustainability disclosures and help investors make more informed investment decisions.

Corporate Sustainability Due Diligence Directive (CSDDD)

Agreed upon by EU institutions in December 2023, the CSDDD represents a significant development in corporate accountability for 2024 and beyond. The directive aims to foster sustainable and responsible corporate behaviour throughout global value chains and introduces mandatory due diligence obligations, including the need to adopt a climate transition plan.

The CSDDD captures large EU companies and non-EU companies with significant interests in the region, and as implementation begins in 2024, companies within scope must start preparations to integrate these due diligence processes into their corporate governance structures.

Future trends

As ESG regulations evolve and expand, businesses must stay informed and proactive in their compliance efforts. The trend towards greater transparency and accountability in ESG matters is clear, and companies that embrace these changes are likely to find themselves better positioned for long-term success.

Governments will likely introduce stricter laws requiring companies to disclose more detailed information about their ESG practices. Countries such as the US and members of the EU are already tightening their regulations, expecting greater transparency and accountability from corporations.

Technology is poised to play a critical role in the future of ESG. Advanced data analytics and artificial intelligence (AI) are becoming indispensable tools for monitoring and reporting ESG metrics. Blockchain technology is also emerging as a key player in ESG, providing a transparent and immutable record of sustainability efforts.

These technologies can help verify supply chain integrity to ensure materials sourced are environmentally friendly and ethically produced. Adopting them not only streamlines compliance but also enhances the credibility of ESG claims, making it easier for investors and regulators to trust the data.

Businesses must regularly review their ESG strategies, engage with stakeholders, and seek expert advice to ensure they meet all regulatory requirements while capitalising on the opportunities presented by sustainable business practices.