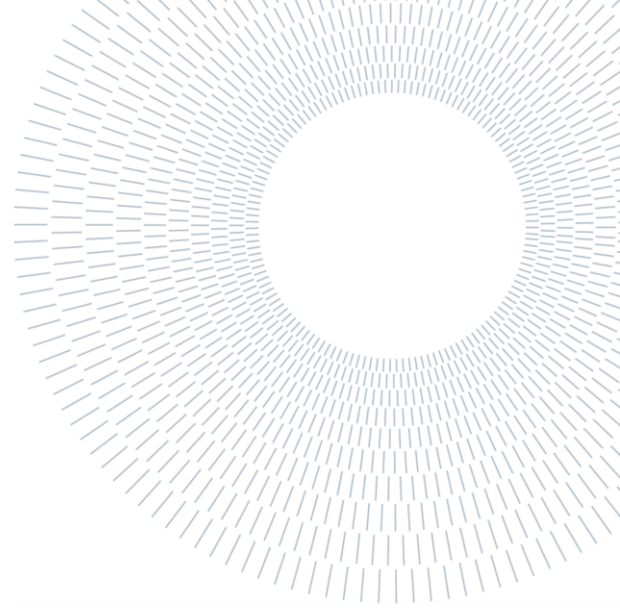




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EXECUTIVE SUMMARY OF THE THESIS

Assessing the impact of the CSRD: insights from four large Italian companies

TESI MAGISTRALE IN MANAGEMENT ENGINEERING – INGEGNERIA GESTIONALE

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1. Introduction

Following an analysis of the results achieved by the Non-Financial Reporting Directive (NFRD), which showed that non-financial information disclosed by companies was fragmented and difficult to compare, in 2021 the European Union introduced the Corporate Sustainability Reporting Directive (CSRD). The objective of the new directive is to improve the non-financial reporting process, to provide financial players with comparable and more robust sustainability reports. At the same time, the directive pushes companies to integrate deeper ESG dimensions into their strategy and organization.

In July 2023, EFRAG published the first set of European Sustainability Reporting Standards (ESRSs) relating to the CSRD. ESRSs ask companies for information on four thematic areas: “Governance”, “Strategy”, “Impact, risk, and opportunity (IRO) management” and “Metrics and targets”.

There are numerous innovative elements introduced by the CSRD:

- Double materiality on the entire value chain (referred to as “value chain mechanism”)
- Targets for ESG material topics
- Vastness of information required by ESRSs
- Link with the EU Taxonomy
- Alignment with TCFD requirements
- Reporting in the Management Report of the Annual Report
- Mandatory limited assurance

The directive, over a period of five years (2024-2028), will directly impact 4,000-5,000 companies in Italy and approximately 50,000 in the European Union. Due to the value chain mechanism, the impact will extend on 200,000 Italian companies and around 24 million worldwide. According to the CSRD, 2024 is the year in which large public interest entities and non-EU companies with transferable securities in an EU regulated market (both with more than 500 employees) must begin collecting their ESG information, consistently with ESRSs, to report it in 2025. These companies are defined as “Wave 1”.

The CSRD supports the objectives of the European Green Deal and, together with the EU Taxonomy

and the Sustainable Finance Disclosure Regulation, makes up the European Sustainable Finance.

2. Literature review

Given the maturity of the CSRD, which is a recent policy, the literature that supported an understanding of the topic was that coming from practitioners, especially consultancy firms such as Big 4 (KPMG, PwC, Deloitte, EY) and Big 3 (Bain, BCG, McKinsey).

A systematic literature review highlighted the complexity of the CSRD and the existence of five macro-families of challenges emerging from its management.

The first macro-family includes the implementation of the double materiality and the need to identify IROs along the entire value chain. For example, challenges in this area are the identification of the value chains with which a company works [1], the engagement of stakeholders on more technical aspects than the NFRD [1], and the management of financial materiality, not only on the topic of climate change, but on all ESG dimensions [2].

The second macro-family consists of the organizational impacts created by the directive, both on the structure of companies and on employees. Examples of emerging challenges in this family are the greater involvement of functions on ESG issues, especially Finance functions [3], and the consequent need for new skills and competences [4].

The third macro-family includes the necessary transparency in the disclosure phase, the risk of greenwashing in the case of imprecise disclosures, and the creation of an internal control that increases transparency and mitigates greenwashing. Examples of challenges are the definition of ESG targets [5], neither overly ambitious nor highly prudential, and the critical issues that emerge from the development of a robust control system, such as collaboration between different functions not used to working together [6].

The fourth macro-family details the management of ESG data and the mandatory limited assurance process. For instance, challenges are collecting ESG data not covered by the NFRD, increasing the quality of sustainability data to match that of financial information [7], and achieving "Audit-ready" status [8].

The fifth macro-family refers to the management of Scope 3 emissions, focusing on the use of proxy and industry average data from literature and the need to collect primary data coming from the value chain [9].

3. Methodology - Scope

To assess the overall impact of the CSRD, at the beginning of 2024 a quantitative research project was launched, to identify challenges and best practices adopted across industries, countries, and Waves. Results pursued aim to support policymakers, business players, and academics.

This dissertation represents the starting point of this project. Recognizing scarce literature on corporate reactions to CSRD challenges, on which building the research project, the thesis presents a multiple case study focused on Italian Wave 1 (IW1). The objective is obtaining a clear picture of IW1 responses to the directive.

The entire methodological process embraced is based on R. Yin's book "Case study research: design and methods" [10]. Beyond a first phase called "Scope", before conducting interviews, two steps were carried out: "Research Design" and "Case Study Protocol".

4. Methodology – Research Design

"Research Design" phase defines the study's questions, its propositions, the unit of analysis, the logic linking the data to the propositions, and the criteria for interpreting the findings.

Study's questions refer to the purpose of the case study research. As part of the thesis, two research questions were identified:

- "How are Wave 1 Italian companies reacting to the challenges of the CSRD?"
- "Is there consistency between the challenges identified in literature and those experienced by Italian companies belonging to the CSRD Wave 1?"

Furthermore, the identification of company-oriented variables able to explain an increase (or decrease) in the complexity of CSRD challenges experienced by each company was defined as a further research objective.

To answer these questions, four companies were interviewed on the five macro-families of challenges. This led to the definition of the case study propositions, which consist of a more in-depth specification of the research purpose:

- *"Which were the challenges that emerged from approaching the double materiality and working across the entire value chain? How were they addressed?"*
- *"From an organizational standpoint, how has the company changed to address the directive? For example, have there been restructuring of functions, changes in leadership or responsibilities, new roles? What have been the main challenges in this area?"*
- *"Do you think that greenwashing and transparency are topics related to the CSRD?"*
- *"What challenges have you encountered regarding data collection and management, as well as the assurance process? How have you structured yourselves to address these challenges?"*
- *"How did the company initially approach Scope 3 emissions over the years, and how have the processes changed following the CSRD?"*

The creation of the case study's propositions supported the definition of specific questions to guide interviews and to obtain timely information relating to the research objectives.

The unit of analysis of each of the four case studies is a company belonging to *IWI*. Data analysis was carried out through a cross-case synthesis process on all the cases conducted, so as to highlight similarities and differences between the four reactions implemented. Subsequently, an analytical generalization process made it possible to extend the identified trends to *IWI* and to answer the research questions.

To increase the quality of the case studies conducted, three dimensions were analyzed: "Construct validity", "External validity", and "Reliability".

- Construct validity was strengthened by integrating different sources into the case study reports, defining a clear chain of evidence, and subjecting case study reports to interviewees for review.
- External validity was improved by applying a literal replication process to the research. It consists of applying the same procedures in each case study conducted.

- Reliability was increased by defining a Case Study Protocol and a Case Study Database, containing all the material used so that it can be analyzed by third parties.

Since the definition of causal relationships was not the purpose of the research, "Internal validity" was not a dimension considered.

5. Methodology – Case Study Protocol

The Case Study Protocol is a document detailing an overview of the research project, field procedures, adopted case study's questions, and a description of the final report.

Field procedures are guidelines that explain how data collection and the subsequent creation of the case study were structured.

Once a company was identified as a target for a case study, an introductory e-mail was sent to create an initial meeting between the research team and interviewees. Following an in-depth analysis of the chosen company, one or more meetings lasting approximately one hour were held, to collect the necessary information on reactions to the challenges of the CSRD. The interviews, based on a predefined set of questions, were carried out in Italian, transcribed, transformed into case studies and, finally, translated into English. The last step of the process was the review of the final report by the interviewed company.

Case study's questions, which are a series of questions useful to the interviewer to maintain a coherent logical flow during the interview, are the same as propositions defined in "Research Design".

For each case study, the final report is a written document. It starts with an overview of the company, describing its history, its business, and its relationship with sustainability. Following a description of the people interviewed, CSRD-oriented information collected is presented in chapters. Each chapter details information related to a specific macro-family of challenges.

6. Case studies

Four different companies, all belonging to *IWI*, were interviewed. Following a pilot case study conducted on Fincantieri, the research focused on Pirelli, Eni, and Prysmian.

Apart from Fincantieri, at least two managers of the companies interviewed participated in each meeting.

7. Results – Explanatory variables

After drafting the case studies, a cross-case synthesis exercise was conducted, comparing the information collected on Pirelli, Eni, and Prysmian and, when possible, on Fincantieri. This allowed for the identification of similarities and differences between the four companies. In addition, also thanks to conversations held with the managers interviewed, it was possible to identify some variables affecting the level of complexity of each CSRD challenge.

These explanatory variables have been divided into internal and external to the company.

Internal variables:

- Corporate culture
- Corporate innovation mindset
- Proactive vs. Reactive approach towards regulatory policies
- Top and middle management engagement on the CSRD
- Maturity level on managing ESG topics
- Established presence of an Integrated Annual Report, merging financial and non-financial information
- Presence of a Consolidated Report at Group level
- Dimension of the value chain and extension of the supply chain
- Net profit over the last X years
- Alignment between ESG trends and business development

External variables:

- Stakeholders and regulatory pressure
- Number of players in the industry

8. Results – Research questions

About the first research question, for *IWI*, the double materiality presents a higher complexity than previous materiality approaches and engaging with the value chain is a strong challenge. To face it, companies are deploying digital projects to obtain ESG primary data from suppliers. The stakeholder engagement post-CSRD

is characterized by a marked reduction in the number of stakeholders involved and an increased emphasis on specialized ones. Specifically considering financial materiality, for the topic of climate change, the TCFD is adopted to evaluate financial materiality across different scenarios. For other ESG topics, the best methodology has still to be defined.

The definition of a “Dirigente Preposto” for ESG information and a stronger collaboration between Sustainability and Finance functions are common patterns across *IWI*. It’s expected that the manager responsible for financial information and the Head of Internal Control will expand their responsibilities to cover also ESG topics. The established presence of an integrated strategic plan is another common element in *IWI*. However, for many companies in this cluster, the CSRD is going to lead to managerial changes. The functions most impacted by the CSRD are Sustainability, Finance, Risk, Compliance, Internal Control, and Internal Audit. To train employees on the CSRD, companies from *IWI* are developing training material for their entire workforce and specific events for the most affected functions.

To increase transparency and to reduce the risk of greenwashing, *IWI* is currently strengthening ESG internal control systems, which are far from maturity. Cross-functional collaboration, considered fundamental to support internal control, emerges as a best practice. Even if establishing such a collaboration is characterized by tensions between the functions involved, in the short to medium term it is a value-generating approach.

The collection of information not covered by the NFRD poses additional challenges for *IWI*, including engaging business functions and establishing both controls and data governance. In *IWI*, all ESG data collection processes consist of a multi-level process, with clear control points. The strategy adopted to elevate ESG data quality is the strengthening of control processes. For non-financial reporting, each company in *IWI* has a different digital support that best fits its context. Most of them are undergoing a transition from a GRI-based model to a ERSs-based one. For *IWI*, external limited assurance on ESG data is a well-established business practice.

The CSRD does not change Scope 3 emissions management but, due to its focus on primary data, pushes *IWI* into engaging deeper with suppliers.

Regarding the second research question, apart from the assurance process (already mandatory in Italy due to the NFRD), all the challenges presented in literature have been faced by *IWI*, proving a high level of consistency between literature and practice.

All the challenges from the first macro-family have been identified as complex issues in CSRD management. Performing the double materiality, working across value chains, understanding which stakeholders to engage and how, and analyzing risks and, above all, opportunities on different scenarios have all been defined as critical problems.

About the remaining macro-families, only some challenges have been perceived as complex. The engagement of functions not used to ESG topics and financial rigor, the definition of ESG targets, the creation of robust internal controls, the implementation of new ESG data collection processes, the improvement of non-financial data quality, and the engagement of suppliers and customers on Scope 3 emissions are identified as critical issues.

Instead, even if recognized as challenges, the collaboration between Finance and Sustainability functions, the need for new skills, and the upgrading of IT system for non-financial reporting have been managed quite straightforward.

Lastly, the expansion of managerial responsibilities to cover ESG topics, the development of training material, and the improvement of transparency are challenges experienced with varying intensity by companies in *IWI*.

9. Conclusions

In terms of complexity and change, the CSRD can be compared to what SOX and IFRS frameworks represented at the beginning of the 21st century. Accordingly, CSRD management requires a massive effort and the change it leads to is radical. This creates several difficult challenges for *IWI*, except for the mandatory assurance which was already applied in Italy due to the NFRD. Each of them has manifested with different degrees of magnitude, depending on several factors, both internal and external to companies.

However, despite the various complexities, companies belonging to *IWI* appear ready to manage the directive in all its aspects.

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