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EU OMNIBUS REGULATION: SIMPLIFICATION AT THE COST OF QUALITY?

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KEY POINTS:

- A key question raised by the proposed Omnibus legislation is whether it will undermine the progress made in sustainability reporting
- There is growing concern that the Omnibus legislation will be regressive
- This regulatory instability encourages companies to view CSDR and associated frameworks as mere compliance obligations rather than opportunities for strategic transformation
- Companies may start to see sustainability reporting as a compliance obligation rather than a strategic priority

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To enhance companies' ESG (Environmental, Social, and Governance) practices and improve the reliability and comparability of ESG criteria, the European Union (EU) has implemented numerous regulations. While these measures aim to strengthen sustainability reporting, they have also significantly expanded the reporting requirements, making the process more complex.

To tackle this challenge and consequently reduce the bureaucratic complexity placed on businesses, European Commission President Ursula von der Leyen proposed an Omnibus Regulation in November 2024. The proposal seeks to consolidate and simplify the Corporate Sustainability Reporting Directive (CSRD, 2022, which strengthens non-financial reporting obligations for companies), the EU Taxonomy Regulation (2020, which classifies sustainable economic activities) and the Corporate Sustainability Due Diligence Directive (CS3D, 2024, which mandates due diligence to identify and address negative impacts across value chains). While efforts to simplify regulatory requirements are welcome, the proposed omnibus regulation raises a crucial question: will it risk undermining the progress made in sustainability reporting? Moreover, given the complexity of these three regulations (CSRD, CS3D, EU Taxonomy) and the broader political context within the EU, can an omnibus regulation realistically achieve its intended objectives?

Challenges facing implementation of omnibus package

While well-intentioned, the consolidation of these three frameworks to achieve consensus seems highly challenging given the conflicting approaches and priorities of EU member states. For instance, the CSRD has already faced significant challenges during its development and implementation. As of late 2024, hence just months before the publication of the first CSRD-compliant reports, some European regulators continue to push for a softening of the CSRD framework. Ursula von der Leyen has highlighted the challenges of overregulation for SMEs (Small and Medium Enterprises), while other leaders, such as former French Prime Minister Michel Barnier, suggested a "moratorium" to delay implementing the CSRD in France. Similarly, former German Federal Minister of Justice, Marco Buschmann has called for a revision of the CSRD text. Consensus on the CSRD has yet to be achieved, making it unlikely that an Omnibus package covering these three regulations will be finalized in the short term. According to Forbes, the EU Commission is expected to discuss this matter in February 2025.

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While the Omnibus regulation seeks to reduce the burden and cost of sustainability reporting for businesses, the CS3D goes beyond mere reporting and disclosures. The CS3D also requires companies to establish robust processes to identify and address human rights and environmental issues. Therefore, the scope of the Omnibus regulation must be clearly defined and there are basically two alternatives. As an overarching regulation, the scope of the Omnibus package could encompass those of all three regulations (CSRD, EU Taxonomy and CSRD), which in no manner would reduce the reporting burden on companies. Alternatively, it could simply reflect sustainability reporting and disclosure requirements, common to all three regulations, which would imply excessive simplification at the cost of more quality ESG practices and reporting standards. Furthermore, these regulations remain subject to potential amendments based on stakeholder feedback. Therefore, consolidating them under a single framework is a considerable challenge.

Simplification or Deregulation of Sustainability Reporting?

Amid negative sentiment, fuelled by sustainability regulations which are stunting European competitiveness and sovereignty, there is growing concern that the Omnibus package could be regressive. The CSRD, EU Taxonomy Regulation, and CS3D – each designed to complete the sustainability framework with distinct ambitions and scopes –could be reduced to just "another" set of regulations. This shift could be counterproductive, lifting the burden on companies at the expense of sustainability goals. For example, the final version of the first set of European Sustainability Reporting Standards (ESRS, standards of CSRD) has already been watered down, i.e., fewer data points and a narrower focus on materiality compared to its earlier drafts. Further simplifications, particularly concerning core CSRD concepts would potentially be counterproductive and undermine efforts to establish robust sustainability reporting practices.

Regulatory changes could penalize early adopters

The proposed Omnibus regulation has created significant uncertainty for businesses, sending troubling signals. Major changes to CSRD requirements risk penalizing early adopters who have invested substantial resources in adjusting their strategies. As shifting regulations can undermine proactive efforts, companies that have been delaying compliance may face fewer disruptions. For years, businesses were encouraged to adopt sustainability measures early on, but due to ongoing revisions, this advice now appears almost ironic. This dynamic echoes to recent cases, as seen with the EU's deforestation regulation, where early adopters were disadvantaged.

The CSRD implementation timeline varies by company size and begins with large firms. This phased approach creates a learning curve, allowing smaller companies to learn from the experiences of larger firms and potentially to reduce costs. Furthermore, large companies can support their suppliers during the transition and drive improvements in ESG performance, since the CSRD requires supply-chain information, if relevant. However, uncertainties surrounding sustainability regulations have disrupted this chain of events, reducing the ability of early adopters to influence others. This regulatory instability encourages businesses to perceive the CSRD and related frameworks as mere compliance obligations rather than opportunities for strategic transformation. As a result, many companies may postpone their sustainability reporting preparations until the last possible moment.

Bad Timing for an Omnibus Proposal

The Omnibus proposal exacerbates existing challenges. As of September 2024, 17 member states have yet to transpose the CSRD into national law. Further delays are likely until the Omnibus process is finalized.

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Meanwhile, the adoption of International Sustainability Standards Board (ISSB) standards is advancing rapidly, with 40% of the global market capitalization and 50% of European trade already aligned with ISSB standards, outpacing the slower implementation of the CSRD. This presents a significant risk. If ISSB adoption continues to spread across Europe faster than the CSRD, it could undermine the additional value provided by the CSRD, such as double materiality. Additionally, the widespread adoption of the CSRD could prove more challenging, especially as ISSB standards increasingly become the global baseline for value chain transparency and investor-focused reporting. The chair of the ISSB, Emmanuel Faber, emphasized that ISSB standards provide the type of information investors require more effectively than the CSRD. Additionally, the sector-specific ESRS, projected for adoption in 2026 and intended to provide more relevant information, could face further delays or compromises due to the Belgian Presidency's emphasis on enhancing European competitiveness and the broader adoption of ISSB standards, both globally and within Europe.

Conclusion

European regulators claim that their goal is to ease the reporting burden on companies—a positive and necessary objective—while still supporting sustainability initiatives. However, there remains concern that efforts to simplify regulations could diminish their effectiveness, by stripping them of substance and effectively representing a step backwards in sustainability regulatory standards.

The stability of sustainability regulations is crucial for businesses to plan and adjust their operations effectively. However, the uncertainties created by the Omnibus proposal, coupled with the current European political landscape, send negative signals to companies. This situation penalizes early adopters, potentially discouraging proactive efforts to comply with future ESG regulations. As a result, businesses may begin to view sustainability reporting as merely a compliance obligation rather than a strategic priority.

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