

Obligation to file consolidated sustainability statement versus exemption from preparation of consolidated financial statements

FEDIL – The Voice of Luxembourg's Industry

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Luxembourg, January 2024

## **FEDIL Position Paper**

### **Transposition of the Corporate Sustainability Reporting Directive into Luxembourg Law**

#### **Obligation to file consolidated sustainability statement versus exemption from preparation of consolidated financial statements**

#### **Introduction**

The Corporate Sustainability Reporting Directive (hereunder the “CSRD”), published in the Official Journal of the European Union on 16 December 2022,<sup>1</sup> amends several existing directives and regulations, including the Accounting Directive, Transparency Directive, Audit Directive, and Audit Regulation.

The CSRD came into effect on 5 January 2023. FEDIL closely monitors its implementation and transposition into Luxembourg law on behalf of its members. In this context, some members have raised concerns about specific aspects of implementation that need to be addressed so that companies can prepare in a timely manner. This paper outlines the uncertainties regarding certain reporting arrangements that certain companies may encounter when (i) they are required to prepare consolidated sustainability statements, as mandated by the CSRD, and at that time (ii) apply for an exemption from preparing consolidated financial statements, as allowed by existing Luxembourg laws and regulations (referred to here as 'the matter').

The aim of this paper is to seek clarity from the Luxembourg legislator in the context of the CSRD transposition (transposition deadline 6 July 2024).

## **I The regulatory landscape**

Luxembourg accounting law, in line with the EU Accounting Directive, requires Luxembourg-based parent companies of large groups to prepare consolidated financial statements. It also provides for an exemption (frequently referred to as the “subsidiary exemption”) from preparing consolidated financial statements if the Luxembourg parent company, together with all its subsidiaries, is included in the consolidated financial statements of its parent or ultimate parent company (including those established in a third country; “non-EU parent”). The consolidated financial statements of the non-EU parent need to be prepared under accounting regime that is deemed as equivalent to LUX GAAP to qualify for exemption.

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<sup>1</sup> Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022 amending Regulation (EU) No 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting. OJ L 322, 16.12.2022, p. 15–80. <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32022L2464>

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Comparably to the provisions on financial statements, Article 29a (1) of the Accounting Directive, as recently amended by the CSRD, requires EU parent companies of large groups to include in their consolidated management report information necessary to understand the group's impacts on sustainability matters, and information necessary to understand how sustainability matters affect the group's development, performance and position (hereafter "consolidated sustainability statement"), while Article 29 (8) of the Accounting Directive, as recently amended by the CSRD, provides for derogation from including the consolidated sustainability statement in the consolidated management report if the EU parent company, together with all its subsidiaries, is included in the consolidated sustainability reporting of another parent undertaking (including "non-EU parent"), i.e., substantially under the same rules as the subsidiary exemption for consolidated financial statement.

However, companies may only make use of this exemption if the consolidated management report or the consolidated sustainability report is drawn up in line with the European Sustainability Reporting Standards (ESRS). Vice versa this means that if a non-EU parent does not intend to prepare such consolidated sustainability statement in accordance with ESRS or equivalent, the EU parent will not be able to use the subsidiary exemption and will have to prepare consolidated sustainability reporting as required by Article 29a(1) of the Accounting Directive, as recently amended by the CSRD, while utilizing the exemption from preparation of consolidated financial statements available in Luxembourg, and in alignment with other provisions of the Accounting Directive.

As a result, an entity may be required to provide a consolidated sustainability statement, including metrics reliant on financial information, even though it does not prepare consolidated financial statements at this level.

This situation, i.e., the requirement to prepare consolidated sustainability statement and the exemption from preparing consolidated financial statements is recognized in Recital 26 of the CSRD: "*the exemption regime for consolidated financial statements and consolidated management reports operates independently from the exemption regime for consolidated sustainability reporting*". Beside Recital 26, no further provisions are provided by the CSRD in this regard. Nor is there any guidance by EFRAG or the European Commission how to close this "gap".

Furthermore, in relation to the matter, this paper also underscores the following considerations.

## II Considerations on Luxembourg transposition

### a. Location of the consolidated sustainability statement

Firstly, regarding the requirement for third-country entities to publish a sustainability report in accordance with Article 40a of the Accounting Directive, as amended by the CSRD, the directive states that an EU subsidiary or branch must make the report "accessible". However, there may be ambiguity regarding how this should be achieved. FEDIL suggests that the transposition clarify this detail. FEDIL supports the idea that the report should be filed with the Luxembourg Registre de Commerce et des Sociétés (RCS), which will then make the report "accessible" on its website (likely [www.lbr.lu](http://www.lbr.lu), as is currently the case for financial statements).

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Secondly, in regard to the preparation of consolidated management reports, as per the Article 29a (1) of the Accounting Directive, as recently amended by the CSRD, parent undertakings of a large group should include their consolidated sustainability statement in their consolidated management report. Those companies that are exempted from preparing consolidated financial statements but obliged to prepare consolidated sustainability statements, do not prepare consolidated management reports.

It is unclear whether the consolidated sustainability statement should be included in the parent undertaking of a large group statutory management report, or the reporting entity can choose to publish this elsewhere and put the related information on where the consolidated sustainability statement can be consulted in the statutory management reports of all the consolidating entities.

By being able to publish the consolidated sustainability statement outside of the statutory management report of EU parent, it could make it transparently accessible in cases where there is no financial statement published and would avoid confusion when the consolidated sustainability statement is accompanied by other information prepared on the stand-alone basis by EU parent.

### b. Availability of EU subgroup financial information

Certain metrics to be disclosed in the consolidated sustainability statement prepared are reliant on financial information (e.g., ESRS-E1: greenhouse gas intensity metrics, EU taxonomy reporting). Those companies that are exempted from preparing consolidated financial statements but obliged to prepare consolidated sustainability statements, may encounter practical challenges to obtaining the required financial information to report under the CSRD at an EU subgroup level as this information is not currently reported.

In certain circumstances, the possibility to prepare the consolidated financial information using foreign GAAP aligned with GAAP utilized by non-EU parent would significantly reduce the costs of compliance and simplify challenges to obtain the required financial information, while providing financial data on equivalent basis to IFRS-EU for disclosure in consolidated sustainability reporting and in line with Article 29b (2) of the CSRD: *“The sustainability reporting standards shall ensure the quality of reported information, by requiring that it is understandable, relevant, verifiable, comparable and represented in a faithful manner. The sustainability reporting standards shall avoid imposing a disproportionate administrative burden on undertakings, including by taking account, to the greatest extent possible, of the work of global standard-setting initiatives for sustainability reporting as required by point (a) of paragraph 5”*.

In accordance with Article 27 of Luxembourg Accounting Law, other foreign GAAPs may be accepted on a case-by-case basis by the Luxembourg Ministry of Justice. Any Luxembourg undertaking scoped in by the Law and willing to use another foreign GAAP may apply for an individual exemption with the Luxembourg Ministry of Justice. The updated changes to the Luxembourg accounting law (Projet de loi 8286)<sup>2</sup> retain the same procedures for derogation provided it is limited to the consolidated financial statements and relates to the accounting frameworks approved in the EU. However, there is no guidance if this law could be applicable in the case of preparation of consolidation financial information for the purpose of consolidated sustainability statement.

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<sup>2</sup> Projet de loi n. 8286 concernant la comptabilité, les états financiers annuels et les états financiers consolidés des entreprises ainsi que les rapports y afférents et portant abrogation de la fonction de commissaire en droit des sociétés. <https://www.chd.lu/en/dossier/8286>

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### c. Connectivity with the financial statements

ESRS and EU Taxonomy require to relate the monetary amounts and other information that are directly or indirectly related to information presented in financial statements to be reconciled and explained. For example, ESRS 2 par.125-127: *“the undertaking shall explain the consistency of monetary amounts or other quantitative datapoints, assumptions, and qualitative information included in its sustainability statement with the corresponding information included in the financial statements”*.

It is unclear whether those companies that are exempted from preparing consolidated financial statements but obliged to prepare consolidated sustainability statements, can be exempted to make these references and reconciliation due to the fact that no consolidated financial statements are prepared and therefore there is no link that needs to be made.

### d. Matters for consideration in clarifying the situation

As Recital 26 of the CSRD acknowledges the situation in which companies may be exempted to prepare consolidated financial statements but obliged to prepare consolidated sustainability statements, we urge the Government to address this matter during the CSRD transposition work.

Lack of clarity of which reporting arrangements will be required and/or could be accepted and viable for companies applying the consolidated financial statements exemption, may lead to 1) risk of non-compliance if a viable solution is undertaken by the company and then not accepted by competent authority; 2) unnecessary reporting burden penalizing those companies; 3) lack of common practice as companies need to perform interpretation individually; 4) delay in companies' timeline for implementation of new reporting processes, tools and policies, putting at risk the first reporting preparation.

Luxembourg is country of establishment for many companies which are part of non-EU headquartered groups, hence many companies in Luxembourg may be impacted with the matter presented in this paper.

Those companies that fall under the scenario explained in this paper will be subject to the CSRD and EU Taxonomy reporting as from financial year 2025. Given the significance and complexity of the expected reporting requirements, these companies are already working on preparations for the first reporting year.

### e. Other cross-industry matters for consideration

- **Entities' legal forms:** the transposition should clearly state all Luxembourgish companies' and banks' legal forms if they are in or out of scope (Société Coopérative, Société Européenne, SAS, Sarl-S, SCA etc.).

Drafting example: *“La société européenne (SE) ayant établi son siège statutaire au Grand-Duché de Luxembourg est soumise aux règles applicables aux sociétés anonymes. »*. This type of company should be specified in the transposition.

- **Limited Assurance:** Limited Assurance is crucial for implementing new corporate sustainability rules. Luxembourg should encourage the development of best practices and competition among service providers. Instead of reserving the assurance to independent auditors, Luxembourg should not overlook the opportunity to include Independent Assurance Services Providers (IASPs), meeting

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CSRD's independence and qualification requirements. With the expanding scope of CSRD to smaller undertakings, promoting competition can reduce costs in corporate sustainability services, enhancing the overall competitiveness of Luxembourg in the global services marketplace.

- **Adapted net turnover:** throughout each dedicated law, clarifications for each type of entities and terminology should be used consistently: banks, commercial companies; Insurance “prime brute”, management companies, securitization vehicles.
- **Transposition regarding other investment category:** the transposition should clearly state that investment vehicles such as UCITS, AIFs are out of scope as clearly stated in the CSRD directive.
- **Consistency between Draft law 8286 and CSRD:** the transposition should ensure consistency between draft law 8286 regarding commercial companies and CSRD to be exhaustive and clear about companies’ designation and size (larges undertakings, SMEs, microenterprises, PIEs) as well timing of application.
- **Third country exemption and local report preparation:** in case of exemption due to the fact that the parent bank produces a consolidated management report, and such report is not available at the moment of signature of annual accounts in Luxembourg, the transposition should clarify the actions to be taken by the auditors at Luxembourg level (at least for first time application).

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## About FEDIL

Founded in 1918, FEDIL – The Voice of Luxembourg’s Industry (hereinafter “FEDIL”) is a multi-sector business federation that gives a voice to nearly 700 industrial members, service providers, and construction companies, fostering economic activity in Luxembourg. Today, FEDIL represents 95% of Luxembourg’s industrial production, 75% of Luxembourg’s private research activity, 25% of national employment, and 35% of national GDP. To perform its duties, FEDIL is registered in the Chamber of Deputies’ transparency register.

FEDIL is a founding member of the European employers' association BusinessEurope and has a representative office in Brussels to ensure that its member companies' voices are heard in European policymaking. To this end, FEDIL is registered in the EU Transparency Register (number 286194516022-33).

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