

SME INFO HU

ESG REPORTING AND SUSTAINABILITY REPORT UNDER ACT ON ACCOUNTING



In the European Union, more and more harmonised reporting obligations are being introduced at Member State level, such as the country-by-country report (so-called CbC report) or the report on corporate income tax information to be published together with the financial statement (so-called „public“ CbC report), which we presented in our latest newsletter.

In this publication, two new standardized reporting obligations based on EU-adopted directives and standards, effective in Hungary from 1 January 2024 are reviewed: the ESG reporting and the sustainability report under the Act on Accounting.

az SME Team

The purpose of SME INFO is to provide general information and to draw the attention to the current changes in law which we believe to be important for the business operation of our clients. It is not a replacement for careful review of the acts and rules, and the consultation with your tax advisor.

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1 INTRODUCTION

In recent years, sustainability issues have gained more and more emphasis in the European Union, as a result of which, directives and standards have been adopted (CSRD⁽¹⁾, ESRS⁽²⁾, CSDDD⁽³⁾), thus obliging Member States to transpose sustainability-related reporting obligations into their own legal systems.

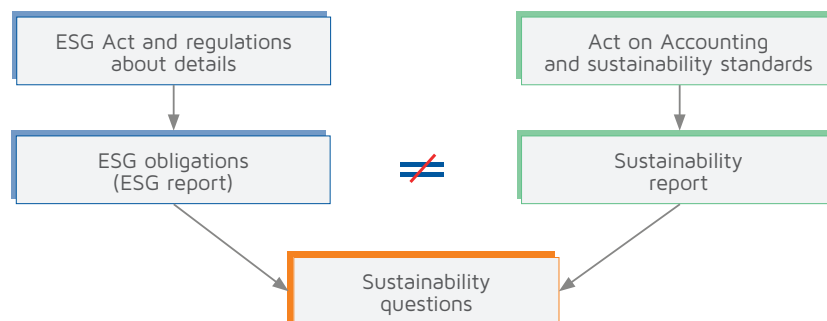
As of 1 January 2024, two important sustainability-related legislative changes have entered into force in Hungary:

- pursuant to Act CVIII of 2023 (hereinafter referred to as the ESG Act), those subject to this act must carry out sustainability due diligence, including ESG reporting, and
- the Act C of 2000 (hereinafter referred to Act on Accounting) was supplemented with requirements for sustainability reporting.

In this publication, for the sake of completeness of this topic, we provide an overview of the obligation under the ESG Act, but as a provider of accounting services, the main objective is to present the obligation to prepare a sustainability report as required by the Act on Accounting.

The issue of sustainability and the related obligations for businesses have opened up a new professional field with specific training needs, which has triggered the creation of a new pool of professionals (e.g. consultants, ESG certification bodies, auditors with sustainability rating). Consequently, we would like to draw attention to the fact, that fulfilling sustainability-related obligations is beyond the competence of an accountant, so we definitely recommend for the obliged companies to contact a consultant.

The chart below shows the „relationship“ between ESG report and sustainability report:



As can be seen in the chart, although both reports under the relevant legislation address sustainability issues and therefore there is more overlap between the two, which may justify the development of a common data collection process, however, the underlying requirements determining the specific content and structure of the reports are different, so it is not possible to generate one report simply by „extracting“ the other.

2 ESG ACT

On 12 December 2023, the law that lays the foundations for domestic sustainability reporting and supply chain due diligence obligations, ensuring compliance with the sustainability guidelines of the European Union was adopted.

The aim of the law is to ensure that companies identify and manage the sustainability risks they face, and thus help their partners who interact with them by providing transparency. The law requires companies to carry out due diligence for sustainability purposes, including the preparation of ESG report.



The legislation proposal, submitted on 19 November 2024, contains several amendments to the ESG Act, but these typically concern details that are not the subject of this publication.



2.1 Scope of the Act

The table below summarises how the scope of the ESG Act will change and expand starting **from 2024**, depending on the size of the company and whether it is considered to be of public interest.

First time application		
For financial year 2024	For financial year 2025	For financial year 2026
Obligated parties		
Large enterprises** qualifying as public-interest enterprises*	Large enterprises**	Small and medium-sized enterprises*** qualifying as public-interest enterprises*
Limits		
On the balance sheet date in the previous financial year***, either two of the following three indicators exceed the limit indicated below: <ul style="list-style-type: none">balance sheet total: HUF 10 billion,annual net turnover: HUF 20 billion,average number of employees: 500 persons.	On the balance sheet date in the previous financial year, either two of the following three indicators exceed the limit indicated below: <ul style="list-style-type: none">balance sheet total: HUF 10 billion,annual net turnover: HUF 20 billion,average number of employees: 250 persons.	No limits

- * Public-interest entities means ⁽⁴⁾:
- those entities, whose transferable securities are admitted to trading on a regulated market of any Member State of the European Economic Area;
 - any other entities other than those referred to in the previous point designated as public-interest entities by law.

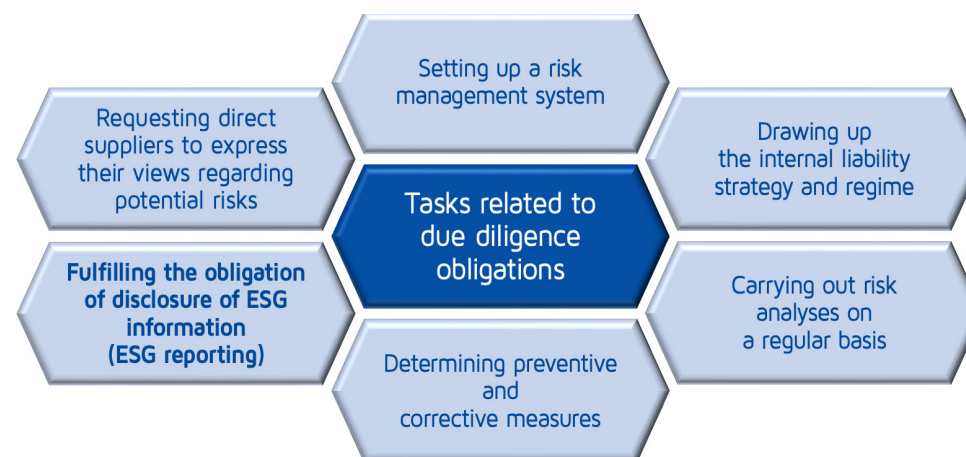
** The ESG Act has its own set of definitions for the classification of companies by size.

*** According to the legislation proposal submitted on 19 November 2024, this condition will be amended in this category for the **two financial years** preceding the current year. The relevant legislation proposal had not been adopted by the time of publication.

The law does not apply to regulated financial service providers, such as banks, insurance companies and investment service providers.

2.2 Due diligence obligations for sustainability purposes

The next chart shows the tasks that sustainability due diligence obligations mean for businesses.



Due diligence obligations for sustainability purposes must be fulfilled by the company in accordance with the detailed rules set out in the decree of the *Supervisory Authority of Controlled Activities*.

The fulfilment of obligations must be documented in the manner and with regularity specified in the minister's decree, and documentation must be kept for seven years from the date of its creation.

In the summer of 2024, the detailed regulations were published, which can be divided into two groups:

- regulations on the accreditation of ESG consultants,
- regulations on ESG reporting requirements.

This publication is **not intended** to present these detailed regulations.

3 ESG REPORTING

The company subject to the law fulfils its ESG reporting obligation by preparing an annual ESG report on the fulfilment of its due diligence obligations for sustainability purposes in the previous financial year.

The primary purpose of ESG reporting is to provide information on due diligence processes, compliance and effectiveness of social responsibility, environmental and human rights obligations related to sustainability issues.

3.1 Content of ESG report

The ESG report shall include, inter alia, the following information:

- description of the sustainability due diligence process carried out with regard to sustainability matters,
- social responsibility and environmental risks, or identification of any breach of obligations related to human rights or the environment,
- presentation of actions taken to prevent, mitigate, remediate or bring an end to adverse sustainability impacts, and the result of such actions.

The detailed content requirements of the ESG report must be established by decree by the Supervisory Authority of Controlled Activities after seeking the opinion of the National ESG Council.

The report may omit current information which is reasonably prejudicial to the interests of the company, and which does not affect the understanding of the development, performance and position of the company.

3.2 Exemption from ESG reporting obligation

A subsidiary and its subsidiaries (if any) are exempt from ESG reporting if they are included in the ESG report prepared by the parent company.

The exempted company must report:

- the information that the company is exempted from the obligations to the Supervisory Authority of Controlled Activities, and
- the name and address of the parent company in whose consolidated ESG report the subsidiary is included.

3.3 The audit and publication of the ESG report

The companies concerned should prepare an ESG report annually and have it audited by an ESG certifier and send it to the Supervisory Authority of Controlled Activities within 6 months following the end of the financial year and make it publicly available on their website free of charge.

4 SUSTAINABILITY REPORT IN ACCORDANCE WITH THE ACT ON ACCOUNTING

In a sustainability report, a company describes its goals and opportunities in relation to sustainability issues and how these affect the performance and development of the business.



The sustainability report must be clearly identifiable by the company in a separate section of the business report and the report must be prepared in an electronic reporting format (ESEF).⁽⁵⁾ ESEF is an EU-regulated uniform format in force since 1 January 2020, according to which reports, specified by law, must be published in XHTML format in a machine-readable manner.

4.1 Scope of the reporting obligation

The table below summarises how the scope of reporting obligation will change and expand starting from 2024, depending on the size of the company and whether it is considered to be of public interest:

First time application		
For the financial year starting in 2024	For the financial year starting in 2025	For the financial year starting in 2026
Obligated parties		
Public-interest enterprises	Enterprises	Entrepreneur listed on a stock exchange in an EEA country, not classified as a micro-enterprise
Limits		
On the balance sheet date in the previous financial year, either two of the following three indicators exceed the limit indicated below: <ul style="list-style-type: none">• balance sheet total: HUF 10 billion,• annual net turnover: HUF 20 billion,• average number of employees: 500 persons AND average number of employees in the actual financial year: 500 persons.	On the balance sheet date in the previous financial year, either two of the following three indicators exceed the limit indicated below: <ul style="list-style-type: none">• balance sheet total: HUF 10 billion,• annual net turnover: HUF 20 billion,• average number of employees: 250 persons.	No limits

According to the definition of the Act, other economic entities that are not entrepreneurs (e.g. other organizations, the MNB, etc.) **are not subject to the obligation to prepare sustainability report.**

4.2 Sustainability report of parent companies or undertakings not based in the EU

In the case of a company not governed by the law of an EU Member State, the EU subsidiary or branch may be required to publish a report **at the group level of the ultimate parent company for the first time for the year starting in 2028**, if the conditions set out in the table below are met:

Subsidiary	Branch
First time application	
For the financial year starting in 2028	
Obligated parties	
A domestically based subsidiary of a parent company not governed by the law of an EU Member State and obliged to publish a sustainability report.	A branch of an undertaking not governed by the law of an EU Member State which does not have a subsidiary, that publishes a report.
Limits	
The net turnover of the parent company exceeded EUR 150 million in each of the last two consecutive financial years in the territory of the European Union at group level.	The net turnover of the head quarter exceeded EUR 150 million in each of the last two consecutive financial years in the territory of the European Union at group level or, if not applicable, at individual level AND the annual net turnover of the branch in the most recent financial year exceeded EUR 40 million.

In the above cases, the report should in principle be prepared in accordance with the standards applicable to third country entities, but may be prepared differently in accordance with the provisions of the ESRS or as specified in accordance with the implementing act on the equivalence of these standards. ⁽⁶⁾

If the data required for reporting under the above third country standards are not available, the subsidiary or branch should request the parent company or head office not governed by the law of a Union Member State to provide the necessary information.

If the information requested is not provided, the report should be prepared on the basis of the information available and published together with a statement, that the information requested has not been provided to the company preparing the report.

4.3 Exemption from sustainability reporting

The **Hungarian subsidiary** is exempt from preparing and publishing the report if it is included:

- in the consolidated sustainability report of a parent company drawn up in accordance with Chapter VI/C,
- in the consolidated sustainability report drawn up in accordance with sustainability reporting standards (ESRS) of a parent company governed by the law of a Union Member State,
- in the consolidated sustainability report of a parent company not governed by the law of a Union Member State drawn up in accordance with sustainability reporting standards (ESRS) or in accordance with an implementing act on the equivalence of sustainability reporting standards.

The **exemption shall apply** if the **business report** of subsidiary contains the following:

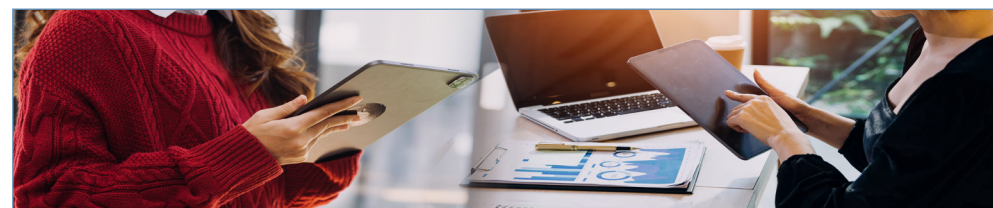
- the fact of exemption,
- the name and registered office of the parent company that draws up a sustainability report at group level in accordance with sustainability reporting standards,
- the weblinks to the consolidated business report of the parent company or, where applicable, to the consolidated sustainability report of the parent company, and to the assurance opinion.

If the parent company is not governed by the law of a Union Member State, there are additional conditions for the exemption for the publication of the assurance opinion and for the presentation of the activities of the exempted subsidiaries.



Companies listed on stock exchanges in a Member State of the EEA are not eligible for the exemption!

The consolidated business report or consolidated sustainability report of the parent company of the exempted subsidiary shall be published in at least one official language of the Union.



4.4 Content of the report

The sustainability report shall contain the following:

- a brief description of the company's business model and strategy,
- a description of the time-bound targets related to sustainability matters set by the company,
- a description of the role of the administrative, management and supervisory bodies with regards to sustainability matter,
- a description of the company's policies in relation to sustainability matters,
- information about the existence of incentive schemes linked to sustainability matters which are offered to members of the administrative, management and supervisory bodies,
- the due diligence process implemented by the company with regards to sustainability matters in line with Union requirements,
- the principal actual or potential adverse impacts connected with the company's own operations and the actions taken to identify and monitor those impacts,
- any actions taken by the company to prevent, mitigate, remediate or bring an end to actual or potential adverse impacts, and the result of such actions,
- a description of the principal risks to the company related to sustainability matters,
- indicators relevant to the previous points.

In addition to defining the content, the law requires the report to be prepared in accordance with Sustainability Reporting Standards (ESRS).



As a result of the requirement to ensure compliance with ESRS, a report ensuring full compliance cannot yet be produced solely in the knowledge of the requirements of the Act on Accounting, the intervention of a professional who also has sufficient knowledge of the relevant reporting standards is required.

4.5 Auditing and publication

The compliance of the sustainability report with sustainability reporting standards (ESRS) can be assessed by a statutory auditor with sustainability rating, taking into account the following:

- the statutory auditor or other than the statutory audit may appointed,
- the auditor examining the sustainability report should not be an advisor on the sustainability report.

The company must publish the sustainability report together with the auditor's assurance opinion (assurance report) at the same time as the annual financial statement, and the company must also publish its business report containing the sustainability report on its website.



The Act on Accounting requires business report, but it does not have to be published together with the financial statements. The question arises whether - if the disclosure of the sustainability report is mandatory and it is part of the business report - the business report will have to be disclosed from now on.

5 COMPARISON OF THE MAIN CHARACTERISTICS OF ESG REPORT AND SUSTAINABILITY REPORT

In the table below, the main parameters of ESG and sustainability report are compared in summary form for easier transparency.

	ESG report	Sustainability report
Relevant domestic legislation	ESG act, related decrees	Act on Accounting
Entry into force	To be applied for the first time for the financial year starting in 2024, with progressively extending effect.	
Obligated parties	There is a high degree of overlap in terms of obligated companies, but not complete matching.	
Publication	To be sent to the authority via the ESG management platform and made publicly available on the website within six months after the end of the financial year.	It must be published at the same time as the annual account as part of the business report and made available on the website.
Person/body certifying the report	Accredited ESG certifiers	Registered statutory auditor (audit firm) with sustainability rating
Document certifying a report	ESG certificate	Assurance opinion based on limited assurance
Publication of certification document	The ESG certificate must be published on the management platform.	The assurance opinion must be published together with the annual report.

References:

- 1 *Corporate Sustainability Reporting Directive*
- 2 *European Sustainability Reporting Standards*
- 3 *Corporate Sustainability Due Diligence Directive*
- 4 *Act LXXV of 2007 on the Chamber of Hungarian Auditors, the Activities of Auditors, and on the Public Oversight of Auditors*
- 5 *Article 3 of Commission Delegated Regulation (EU) 2019/815*
- 6 *Third subparagraph of Article 23(4) of Directive 2004/109/EC*

