

EFRAG SRB

ESRS 2 – analysis of comments and EFRAG
Secretariat recommendations

3 October 2022



GENERAL APPROACH

- Suggestions of wording/simplifications that do not impact substance are presented in the detailed file supporting this meeting.
- This presentation focuses only on the proposed changes of substance and on the items where the EFRAG Secretariat does not consider appropriate/necessary to take actions.
- EFRAG Secretariat proposal, subject to SR TEG recommendations and SRB decision.
- **Proposed simplifications/aggregations of DRs in Green**

Q1: DR 2-GR 1 – General characteristics of the sustainability reporting

- Architecture: align with TCFD and ISSB
- Concepts and terminology: align with ISSB
- A number of wording changes
- Align to last CSRD text
- Simplify ESRS 2 wording
- No references to future regulation and separate appendix with regulation used
- Level of granularity / excessive number of DRs
- Connectivity

Q2: DR 2-GR 2 – Sector(s) of activity

- Definition of market and customer group: **No action**
- Define internal transactions: examples to be added
- AG6 is commercially sensitive to be deleted
- AG 12 could be moved to SEC 1 (**disagree** as this part of the general description of the business model).
- Breakdown by headcount and country excessive (**disagree**, as breakdown of HC by country is necessary in order to understand impact profile incl. for social issues).
- Sector breakdown should be IFRS 8 and not NACE (**disagree** as NACE is the link to sector specific standards and IFRS 8 doesn't foster comparability and doesn't support information about impact profile as NACE does).
- ISSB alignment
- Significant country/segment: 10% ignores the impact materiality dimension. A different filter is appropriate than a financially material one. Agree / **alternative to be discussed**
- SDFR always mandatory
- AG 5 (internal transactions) to be eliminated as commercially sensitive: **disagree** as this is key to understand impacts inside-out
- Definition of FTEs (headcounts): align with that the undertaking discloses in FFSS

The details provided by country/sector/market is supported by comments from civil society as necessary to understand impact profile.

Q3: DR 2-GR 3 – Key features of the value chain

- Clarify value chain / approximation (see paper Value Chain)
- Alignment with ISSB
- New text of the CSRD for subsidiary exemption
- Confidentiality of AG 14: The main groups of business relationships together with the related underlying contractual terms (including relevant rights and obligations) shall be disclosed. **To be discussed**
- Merge GR 3, 4 and SBM 1 (only business model description, strategy will stay in SBM1)

Q4: DR 2-GR 4 – Key drivers of the value creation

- Avoid to use 'key' and use 'material in all cases' (to be consistent across standards) - disagree
- ISSB alignment (avoid reference to the capitals at this stage) – for financial mat.
- Clarify what is the disclosure objective for 'value creation', link to where the margins/revenues come from (IFRS 8) – as a starting point – but focus on value distribution/ value creation for customers and for other stakeholders (nature environment included) / but avoid the word 'sustainable products' / manufacturing and intellectual capital
- Simplification and less detail
- Merge GR 3, 4 and SBM 1
- Rebuttable presumption

Q5: DR 2-GR 5 – Using approximations on the disclosure in relation to boundary and value chain

- **Proposal for all the DR GR from 1 to 10:** eliminate from ESRS 1 the equivalent concept, incorporate in ESRS 2 corresponding DR any eventual missing elements in the concepts. This will simplify ESRS 1. Also, merge from GR 5 to GR9 in only one GR.
- Joint ventures / proportional consolidation: same accounting treatment as for financial statements (same perimeter), however included in the disclosure as value chain participants when they are in value chain.
- Auditability (no action)

Q6: DR 2-GR 6 – Disclosing on significant estimation uncertainty

- Clarify that undertakings should disclose inputs and methodology of estimation.

Q7: DR 2-GR 7 – Changes in preparation and presentation

- Merge ESRS 1 and 2: **Disagree**. Move from ESRS 1 to ESRS 2 the principles underpinning the GRs and merge GR as proposed in previous points. ESRS 1 should stay as concepts and principles need to be separate from disclosure requirements.
- Limit restatement: Proposal to require only explanations and not restatement for value chain; restatement only for financial reporting perimeter.
- 25 d: change to the wording d) to “if impracticable or too onerous” (allow to omit restatement if too onerous)

Q8: DR 2-GR 8 – Prior period errors

- Align with ISSB
- The info should be presented next to each datapoint not centrally: **Disagree**. This DR requires to present information for errors, but does not mandate the location (central rather than next to each datapoint)
- Clarification that only “material” errors should be corrected.

Q9: DR 2-GR 9 – On other sustainability reporting pronouncements

- DR should be deleted: **Disagree**. This is needed to provide linkage with IFRS reports.
- DR should be voluntary: **Disagree**. This DR is applicable only when other standards are used voluntarily on top of ESRS. It is not creating additional burden
- ‘Pronouncement’ is not defined
- Agree: when the voluntary information is presented in ESRS statements next to ESRS disclosure, companies should identify separately this information, explain whether whether they meet ESRS quality criteria and explain why the company has decided to report on them
- Is audit extended to such additional info? **Disagree**. ESRS cannot mandate audit requirements. The proposal to separately identify this additional voluntary information will help to distinguish between the two sets of info. In the BC to be explained that the inclusion of this info doesn't imply that the undertaking has assessed compliance with these other frameworks/standards. **To be discussed**

Q10: DR2-GR 10 – General statement of compliance

- Simplify / reduce granularity
 - 30(b) ii, It is difficult to understand how this differs from the materiality analysis and its disclosure
 - 30 (b)(i) excessive. The characteristics of information quality should underpin all information disclosed, so no need for this specific statement
 - AG 23 redundant with IRO
- AG22 to be moved to the main text
- Need a non-compliance statement (e.g. par. 93 ESRS 1) **Disagree.**
- This DR could be deleted: **disagree**, we need a compliance statement

S1 Q39: ESRS 2

- Consolidate in ESRS 2 elements from G1 / all G1
- Architecture and wording to be aligned with ISSB (building blocks)
- Shall in AG to be moved in main text
- Address overlaps between different DRs
- Include materiality matrix
- Limit elements that are commercially sensitive
- Avoid wording that implies management of sustainability is decoupled from general management
- Simplify / streamline

REMIND: CHANGES IN ARCHITECTURE ALREADY AGREED

- Move IRO2 and 3 to SBM – AT THE BEGINNING
- Merge IRO 2, IRO 3, SBM3 and SBM4
- Move DP1 and DP 3 from ESRS 1 next to IRO 1
- Move DP 2 from ESRS 1 to ESRS 2 (at the end)
- Align the titles (Strategy – instead of Strategy and Business Model, Governance – instead of Governance and Organization, Metrics and Targets – instead of Performance Measures)
- Start from GOVERNANCE
- Risk management to be changed into MANAGEMENT OF IMPACTS, RISKS AND OPPORTUNITIES (instead of PTAPR) – PTAPR to stay as sub-sections
- G1-7 and G1-8 (modified after CSRD) to be moved into GOV (other G1 DR to be discussed after we address G1)
- Merge GR 3, 4 and SBM 1 (see previous pages)
- Move GR 2 next to GR 3+4+SBM
- Merge SBM 3 and 4
- Merge GOV 2 and 3
- Merge G1-6 in GOV 4

Refer to the SRB discussion 5 September 2022

<https://www.efrag.org/Assets/Download?assetUrl=%2Fsites%2Fwebpublishing%2FMeeting%20Documents%2F2208191301558297%2F04-01%20Alignment%20with%20IFRS%20Sustainability%20Standards%20Architecture.pdf>

Q11: DR 2-SBM 1 – Overview of strategy and business model

- Move BM to GR3+4 here we would leave only 'strategy', i.e. forward looking summarized strategy where you want to go, e.g. transition plans sustainability dimension of it
- Value creation for all the stakeholders VS enterprise value creation
- Having sustainability plans is not mandatory, so need to redraft 'whether and how'
- Transition Plans on climate in E1, but here open to other matters (where relevant) – moved from environmental standards to sector specific standards – e.g. 'when an undertaking has transition plans for biodiversity they have to be illustrated'
- Mission, purpose, vision. value are commonly used should be defined/deleted. **Disagree.** No need to define them.
- Streamline, align with ISSB (but we need also to cover value creation for other stakeholders)

Q12: DR 2-SBM 2 – Views, interests and expectations of stakeholders

- Simplification
- Do we need this DR or shall we simply have it integrated into the different topics?
"Usefulness to AG 30 c) and 38 a), b) to be considered/ Simplification needed.
Agreed to simplify, however this DR covers stakeholder engagement and a central disclosure across all topics is necessary
- Refocus this DR on methodology and results: how **stakeholder engagement** is organized and how it is being used – based on the individual needs (and impacts) of different organizations – 38 b refer to undertakings' understanding of stakeholders' expectations
- Proposal to change the name of this DR to be 'stakeholder engagement' / no merger into other DRs

Q13: DR 2-SBM 3 – Interaction of impacts and the undertaking' strategy and business model

Q14: DR 2-SBM 4 – Interaction of risks and opportunities and the undertaking' strategy and business model

- Merge SBM 3 with SBM 4 with IRO 2 and IRO 3 + what is left of SBM 1 (Strategy)
- The comment is suggesting to refer to interactions of the STRATEGY with IROs as it is not clear how the BM interacts with IROs. Agree and propose to refer to Strategy only.
- Definition of the concept of resilience (AG32b) - alignment with IFRS to help
- Clarify better what is expected undertakings to report
- 47 (c) i and ii to be removed: **Disagree**. We need to be kept in the standard as they are core. However all the text will be reviewed for simplification.
- Refer to 'integrated thinking' to clarify that it is not the general strategy that matters here but the integration of sustainability in strategy. **Disagree**.

Q15: DR 2-GOV 1 – Roles and responsibilities of the administrative, management and supervisory bodies

- Merge GOV 1 and G1-1 and G1-9 (to be discussed when we discuss G1)
- See ESRS 1 T1 comments: refer to the European definition of ‘Directors’
- **Disagree** that this DR should be limited to the governing body. See GRI 2-13: delegation of responsibilities in management of impacts. Important to disclose also other levels involved. Add ‘and management roles’ in the title of this DR (as it is already in par. 50 of ESRS 2)
- Include also CEO and deputy CEO
- Reference to the nomination process to be discussed as part of G1 discussion
- Include in this DR information on composition of bodies as proposed in ESRS G1

Q16: Q16: Please, rate to what extent do you think DR 2- GOV 2

- Merge DR 2 – GOV 2 with DR 2 – GOV 3
- Exclude senior executives (as not required by CSRD): **Disagree** as this is a relevant information. Propose to change the title of the DR into *‘Information of administrative, management and supervisory bodies and senior executive management about sustainability matters’*
- Excessive level of detail / simplify
- Phase-in: proposal to postpone to year 2. **Disagree** as for IFRS alignment we need this point.
- Information §53 (who is in charge and organizational structure for IROs that trigger changes to business model) could be confidential – proposal to refocus following GRI 2-13 delegation of responsibilities in managing impacts
- Eliminate 56 d. **Disagree**. Process whereby the Due diligence is communicated to the management is an important step. Possible merging in 56 a.
- It should be limited to listed undertakings – **Disagree**. CSRD applies to all
- This DR should cover process of assessing/ considering/managing sustainability IROS instead of on how the governance bodies and management are merely informed – **Disagree** as this would result in additional datapoints

Q17: DR 2- GOV 3 – Sustainability matters addressed by the undertaking's administrative, management and supervisory bodies

- Merge DR 2 – GOV 2 with DR 2 – GOV 3
- As it is the DR is resulting in excessive and immaterial info. It should instead require a list of material sustainability matters addressed in the reporting period and the key decisions made regarding sustainability matters.
- Alignment with IFRS S1 par. 13
- Phase-in: proposal to postpone to year 2. **Disagree** as for IFRS alignment we need this point.
- Paragraph AG46 is not requiring to disclose the discussions and the outcome of the decisions taken when addressing sustainability-related matters by its governance bodies BUT IT SHOULD. **Disagree** to add another datapoint
- Include disclosure about the number and nature of critical concerns that have been communicated to the governance bodies during the year under review / AG 47 'as well as other issue of critical importance' risks to result in long not focused disclosure. Agree to refer to the nature of critical concerns instead of issue of 'critical importance' (no number)
- Recommend to limit it to key sustainability matters **Disagree**, Need to cover material

Q18: DR 2- GOV 4 – Integration of sustainability strategies and performance in incentive schemes

- Limit to members of the bodies, exclude senior executives and other employees – **'may'** keep optional (in particular for other employees), also for alignment with: GRI 2-19 covers also senior executives. CSRD textually limit this disclosure to members of the bodies and IFRS S1 par. 13 f. Nevertheless, we suggest to maintain the current scope as datapoint is relevant.
- Simplify
- Phase-in: proposal to postpone to year 2
- **Overlap with G1 – 6 (G1-6 to be integrated here)**
- Disclose how remuneration during the year under review has actually matched sustainability- or climate-related metrics + Add the proportion of variable compensation conditioned to sustainability KPIs in relation to the whole compensation paid or, in the absence of these variable parts, why it is not conditioned. **Move AG 52 to the main body**

Q19: DR 2 – GOV 5 – Statement of due diligence

- Burdensome / Rudimentary and vague. **Disagree**. This is useful info
- Postpone to year 2. **Disagree**
- Postpone to when CSDDD is effective. **Disagree** as OECD guidelines are embedded in CSRD.

Q20: DR 2 – IRO 1 Description of the processes to identify material sustainability impacts, risks and opportunities

- Clarifications on implementation of double materiality to be included in Set 1. More AG in future sets.
- Cost/benefit rating particularly negative: need to simplify (without compromise on content)
- Consolidate elements on the process into ESRS 1 as part of guidance on materiality assessment
- Better reference to the content of UN guiding princ., OECD guidelines and GRI universal standards

Q21: DR 2 –IRO 2 – Outcome of the undertaking’s assessment of material sustainability impacts risks and opportunities as identified by reference to and in compliance with sector-agnostic and sector-specific level ESRS

- IRO 2 and 3 to be merged and moved at the beginning of the SBM
- Comments against rebuttable presumption and related costs
- Suggestions to avoid overlaps in specific paragraphs
- Phase in not possible (IRO is fundamental info)
- Centralized info about IROs complexifies the report as many cross-references to topics are needed. List of IROs is considered part of the cross cutting disclosure so centralized presentation is preferable.

Q22: DR 2 –IRO 3 – Outcome of the undertaking's assessment of material sustainability impacts risks and opportunities that are not covered by an ESRS (entity specific)

- IRO 2 and 3 to be merged and moved at the beginning of the SBM
- Centralized info about IROs complexifies the report as many cross-references to topics are needed. List of IROs is considered part of the cross cutting disclosure so centralized presentation is preferable.
- Comments against rebuttable presumption and related costs