

This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of EFRAG SR Board. The paper forms part of an early stage of the development of a potential EFRAG position. Consequently, the paper does not represent the official views of EFRAG or any individual member of the EFRAG SRB or EFRAG SR TEG. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG SRB, are published as comment letters, discussion or position papers, or in any other form considered appropriate in the circumstances.

## **Cover Note on the LSME Working paper V2**

### **Objective of the session**

- 1 Discuss the version 2 of the draft LSME ESRS and address remaining questions or possibility for simplifications.

### **Background**

The SRB last discussed LSME on 8 March 2023 and received a paper that summarised the overall process followed by the EFRAG Secretariat in the preparation of V1. Please refer to the following link to that document as a background for this meeting.

03-01-SRB 230308 Cover note:

### **Papers provided**

- 2 EFRAG SRB has been provided with the package v2 LSME discussed at the public session of EFRAG SR TEG paper (13 March meeting) and with the
- 3 Input paper on figures, written feedbacks from LSME Community and EWG, answers received from financial market participants on SFDR and other EU datapoints (Agenda Paper 03-02)

### **Summary of the changes in v2 LSME**

- 4 The following changes have been integrated in v2 LSME compared to previous version 1, reflecting the last SR TEG discussion on 13 March 2023. To note that Application Requirements and Appendixes are still subject to revisions, as better specified below.

#### Section 1 “General requirements” and section 2 “General disclosures”

- Items outside the materiality assessment: (E1 Climate - section 3, corresponding ESRS E1 - and General Disclosures - section corresponding to ESRS 2): Clarification added that this is limited to the chapters in Section 2 corresponding to ESRS2. Hence the new centralised disclosures on policies, actions and targets remain under materiality assessment (it is not outside materiality only because it is sitting centrally).
- IR3, IR4, IR5: policies, actions and targets, clarification added that the location of the disclosure can either be in centralized section of the sustainability report or in the relevant topical section of the sustainability report.
- Interests and views of stakeholders. In reviewing the new AR in v2, the SR TEG recommended to adopt a different approach, i.e. ‘when the undertaking engages with stakeholders to incorporate its views and interests as part of its materiality assessment, it shall disclose a), b), c)’. No voluntary disclosure

on this point, no mandatory disclosure when there is no engagement. This approach has not been reflected to the current version of the working paper.

- Financial effects for environmental sustainability matters (pollution, water and marine resources, biodiversity and ecosystems, circular economy) have been centralised in chapter IR 1; for climate, financial effects have been left in section 3 Disclosure Requirement E1-5. Despite it being central this is still considered as pertaining to the ‘topical’ content. To avoid multiple repetition of the same content, the same DR covers more than one topic. Climate is in a separate DR due to granularity linked to EU Laws (i.e. benchmark, pillar 3)
- Regarding the human rights due diligence, the two disclosure requirements related to (i) processes for engaging with stakeholders about impacts, and (ii) processes to remediate negative impacts and channels to raise concerns have been merged and simplified for S1 to S4. In the current version, these two disclosure requirements are still in Section 4, but they will be moved to Section 2 as centralised disclosures in line with SR TEG recommendations. In this way all the content on policies, actions and targets for all the topics will be centralised.
- SR TEG recommended that “reasonable effort” is used instead of “impracticable” for i) Presenting comparative information, deleting the requirement on updated estimates (section 1, 6.1ii); and Changes in preparation, reporting errors in prior periods (section 1, 6.4, 6.5). SR TEG rejected the proposal to delete these two datapoints for simplification as they are considered essential to understand the basis for preparation of the sustainability statements. This is still not reflected in the drafting.
- SR TEG rediscussed the initial proposal (currently in V2) to amend the definition of policies admitting that for LSME the policies could be ‘not formalised’. SR TEG orientation is to confirm the same definition of policies as set 1. Application Requirements to be drafted to illustrate examples of when policies are not formalised but actions and /or targets documented.

#### Section III Environmental Disclosures

- DR E1-5, E4-1 and E4-5 have been further simplified.

#### Section IV Social Disclosures

- Changes on due diligence disclosures reported in Section 2. (see above)

#### Section V Business conduct

- No changes compared to V1 LSME.

### **Additional issues for discussion in this session**

- 5 Following the SRB meeting on 8 March and SR TEG meeting on 13 March, the following issues for discussions are addressed in this paper/session.
- 6 Approach to SFDR/Benchmark/Pillar 3 ESG risk: mandatory versus materiality assessment. A mixed approach that balances proportionality with user needs seems supported by members of SR Board, SR TEG and by feedbacks received from financial market participants (see Agenda Paper 03-02). As follows:
  - Table 1 SFDR Principal Adverse Impacts (PAI) Indicators: always to be reported mandatorily.
  - Table 2 and Table 3 SFDR Principal Adverse Impacts (PAI) Indicators + Benchmark + Pillar 3: materiality assessment, under the assumption that this

allows to preserve the datapoint along the value chain of the large undertakings (value chain cap).

- 7 Should Table 2 and 3 of SFDR PAIs be in the materiality assessment, orientation is sought on the disclosures if data omitted because not material. This point was raised by some SRB and SR TEG members. Should this be explicit: i.e. (i) not reported because not material, (ii) not reported because the value is (almost) zero?
- 8 GOV1: simplifications proposed to SR TEG (not in current v2) to reduce granularity of par.20 by deleting let. d and e. as follows, subject alignment with IFRS not impaired. This item triggers a general question on whether priority should be given to simplification or to alignment with IFRS, as these points are included in ESRS 2 due to alignment with IFRS S1 ED.
  - ~~— d) the disclosure shall include a brief description of how the administrative, management and supervisory bodies ensure the availability of the appropriate skills and expertise to oversee sustainability matters, including: the sustainability-related expertise that the bodies, as a whole, either directly possess or can leverage, for example through access to experts or training; and~~
  - e) how it relates to the undertaking's material impacts, risks and opportunities.
- 9 New definition of policies (that refers to not formalised) in current v2 not to be retained. The set1 definition of policies shall be reinstated.

#### **Other matters not yet discussed by SR TEG**

- 10 The following items have not yet been discussed by SR TEG:
  - (a) Section 2, Appendix D “Disclosure/Application Requirements in [draft] topical ESRS that are applicable jointly with [draft] ESRS 2 General Disclosures” would not be applicable due to the fact that GOV, SBM and IR have been centralised in Section 2 and deleted from topical sections (if confirmed). The proposal is to replace this Appendix with a table showing the list of DRs according to whether they are mandatory / subject to materiality / voluntary. This table could be a useful guide for undertakings in understanding the 3 categories of DRs.
  - (b) Art 29c(2) of the CSRD indicates that *Sustainability Reporting Standards for small and medium sized undertakings (...) shall also, to the extent possible, specify the structure to be used to present this information.* The authoritative status of Appendix G in section 1 (currently illustrative example of structure in ESRS1 set 1) could be changed and could be binding rather than example.

#### **Call for more implementation guidance (and consequences on resources)**

- 11 The written feedbacks received from LSME Community and EWG (written questionnaires) show the need to add illustrative examples to the LSME ESRS to facilitate preparers. In particular:
  - impact materiality
  - value chain guide
  - financial materiality
  - HR and Due Diligence.

The EFRAG Secretariat observes that the same areas are often associated with similar requests of implementation guidance for large undertakings. EFRAG gave priority in its current workplan to the completion of the first Set of standards (until November) and currently on the preparation of the second set of ESRS (sectors, LSME). In addition, EFRAG may soon start operating in the field of implementation support for Set 1. There are several competing activities and the priority of preparation

of additional guidance for LSME has to be considered broadly, including the population that would be in scope as opposed to the population of undertakings in scope of Set 1. In addition, the understandability to the market of guidance for LSME in absence of a similar guidance for the large undertakings might trigger questions in terms of its applicability to large undertakings.

In conclusion, the EFRAG Secretariat considers that the preparation of such guidance should not be included in the timetable to the completion of the LSME ED.

**Questions to EFRAG SRB members and observers**

- 12 Do EFRAG SRB members have comments on the additional simplifications and discussion points in par. 6 -11? Is there any specific point that is raising concerns and should be changed?
- 13 Do EFRAG SRB members have suggestions for additional simplifications?