

This paper provides the technical advice from EFRAG SR TEG to the EFRAG SRB, following EFRAG TEG public discussion. The paper does not represent the official views of EFRAG or any individual member of the EFRAG SRB. This paper is made available to enable the public to follow the EFRAG’s due process. Tentative decisions are reported in 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.

VCIG: update and approval

Cover note

Objective

1. The objective of this session is for the EFRAG SRB to approve the updated VCIG for publication, following recommendation and technical advice from SR TEG on 11 April 2024.

Background

2. On 20 March 2024, the SRB provided input on strategic direction following the feedback received in the consultation period.
3. On 21 March 2024, the SR TEG was informed about those strategic directions and provided input on how to implement those directions, considering the consultation feedback.

Feedback	Orientation as agreed by SRB and recommendations by the SR TEG
Linking of entity-specific disclosures with VC; whether entity-specific metrics are also required for VC disclosures;	No changes to the approach: While there may be significant judgement involved in determining the appropriate information to be provided, ESRS does not preclude the need for VC metrics as is evidenced by transitional requirements and wording in the standard.
Clarification of operational control (Chapter 2.3)	SRB agreed to ask SR TEG for its inputs. On 21 March, SR TEG agreed that: <ul style="list-style-type: none"> • the intention was to include GHG emissions from entities/sites/assets outside the consolidated group but under OC • the definition of OC is wide (similar to the GHG Protocol) and the ESRS E 1 paragraph 46 focusses on the treatment of undertakings adjacent to the consolidated group (such as associates and joint ventures) rather than limiting the application of OC to only such undertakings • OC is not relevant to any of the Social standards. • OC can only extend the perimeter of disclosure, not reduce it (i.e. assets/sites/entities in the consolidated group on which a third party exercises operational control cannot be deducted).
Harmonise approach to due diligence between CSDDD and ESRS	For CSDDD explanation have been included
More guidance for financial institutions	To be done by the sector specific standards, otherwise going beyond the scope of an IG.
Requests for more examples	Done, please see the new FAQ 5 and 6.

Feedback	Orientation as agreed by SRB and recommendations by the SR TEG
Explicit list of data sources to be included in FAQ 9	Not possible to provide complete list of possible sources as this depends on the facts and circumstances of each undertaking.
Further guidance on reasonable effort	This depends on facts and circumstances, no opportunities to extend the current guidance without going beyond the remit of an IG.
Miscellaneous smaller comments as well as drafting and editorial comments.	Updated where relevant.

4. Following the strategic direction of SRB and the inputs collected from the SR TEG, the draft VCIG proposed for approval to EFRAG SR TEG included the following changes:
- (a) The document was restructured, specifically Chapter 2.3 on reporting and disclosure boundaries to improve flow and understandability and FAQ 5 and 6 were moved to Chapter 2 as theoretical in nature.
 - (b) Two additional FAQs were added in Chapter 3:
 - (i) New FAQ 5 which updates the example in the GHG Protocol standard for changes in IFRS and to reflect the reporting under ESRS E1; and
 - (ii) New FAQ 6 which illustrates the difference in treatment of an Associate under operational control, as an actor in the value chain and as an investment only.
 - (c) Aspects related to financial reporting were moved to a separate section labelled 'The accountants' corner' to avoid the impression that these are sustainability reporting concepts.
 - (d) A caveat about CSDDD was included in a box in chapter 1.

EFRAG SR TEG approval and recommendation to the SRB

5. On 11 April, SR TEG members were asked to provide their observations on the revised IG 2 proposed for approval. The following key comments were made, and conclusions reached:

Operational control: ESRS S standards

6. The SR TEG members agreed not to mention ESRS S3 and S4, but to clarify that for ESRS S1, the notion of operational control is not applicable as the reporting is based on the definitions of employees and non-employees.

Operational control: Targets

7. The Italian liaison member raised a concern around the definition of operational control and the relevance of providing information on targets for undertakings under operational control if the reporting undertaking cannot unilaterally make investments to improve GHG emissions, e.g. an operator of a plant or an asset but is unable to reach an agreement with its partners.
8. Conclusion: Following the general approach in ESRS, the targets which the undertaking reports on is not prescribed, agreement to clarify that reporting on targets DRs may exclude items over which the undertaking does not have the power to impose investments needed to reduce GHG emissions. However, the disclosures should be clear about the scope (i.e. which entities/items are included or not) and how it relates with the total GHG emissions reported, which also includes entities under operational control.

Operational control and ESRS E1-9

9. Discussion whether for ESRS E1-9 *Anticipated financial effects from material physical and transition risks and potential climate-related opportunities*, an undertaking should consider the impact of fines over an asset where it is an operator. Such fines would impact the reporting undertaking (as operator) and the concept of operational control is not relevant. Incurred fines will be reflected in the financial statements. It could also be argued that the fines are not examples of physical or transition risks. Therefore, IG 2 should not imply that operational control is also applicable to ESRS E1-9.

Transitional provisions

10. Clarification relating to the description of the transitional provisions with respect to entity-specific disclosures and the double use of “however” in paragraph 84 and 85. It will be removed both times.

FAQ 5: Reporting perimeter for ESRS E1

11. The example FAQ 5 is fictional and follow similarities to that in the GHG Protocol of Holland Industries, but the accounting under IFRS has been updated and the types of entities expanded. This is to explain the concept of operational control according to different level of investments.

FAQ 7: How to assess and quantify the impacts of the VC resulting from business relationships

12. EFRAG Secretariat agreed to add context and separate the paragraph 137 in two to avoid any confusion or misinterpretation (and avoid an impression that a thorough VC assessment can be avoided), i.e. adding “, unless they have this data due to their sustainability and management practices with suppliers”.

Leasing: ‘The Accountant’s corner’

13. Concerns regarding the new additions on leasing which included the treatment of leases under the three approaches under the GHG Protocol. The conclusion was to delete some of these paragraphs to avoid the perception that operational control is relevant to leases in addition to the discussion in the VCIG.

Approval

14. All the SR TEG members present approved the IG 2.

- | | |
|-----------------------------|-----------------------|
| a) Chiara del Prete | i) Julian Muller |
| b) Anne Claire Ducrocq | j) Luca Bonaccorsi |
| c) Belen Varela Nieto | k) Maria Mora |
| d) Carlota de Paula Coelho | l) Philippe Diaz |
| e) Christoph Töpfer | m) PierMario Barzaghi |
| f) Signe Andreasen Lysgaard | n) Piotr Biernacki |
| g) Johan Dahl | o) Sandra Adler |
| h) July Mary | p) Thomas Schmotz |

15. Written approval prior to the meeting was provided by: Alexandra van Selm and Julia Menacher. Eric Duvaud provided in writing his intention to abstain from this approval.

After the approval by SR TEG

16. The EFRAG Secretariat notes the inclusion of the following aspects after the SR TEG approval apart from some wording changes to accommodate the ANC’s concerns where possible.

Approach under the GHG Protocol

17. Given the confusion around the approach followed by ESRS and its compatibility with the GHG Protocol, the EFRAG Secretariat has drafted a section to deal with this specifically in Chapter 2.3.
18. Given the confusion about the approach followed by ESRS under the GHG Protocol, the Secretariat has included the treatment of leases under the financial control approach in 'the Accountant's corner'.

FAQ 5: Reporting perimeter for ESRS E1

19. An additional case was added of a joint arrangement where the reporting undertaking is also the operator (number h – Oril).
20. The EFRAG Secretariat notes that the example suggests that the emissions related to the joint arrangement included in the financial statements will be reflected under ESRS E1 paragraph 50(a). The remainder will be reflected under paragraph 50(b) due to the operational control of the reporting undertaking. This is not stated anywhere in ESRS E1 but follows the financial control approach as described in the VCIG.

FAQ 6: Numerical example of GHG emissions ESRS E1 reporting

21. Where you have two sources of estimating impacts, such as GHG emission with an investee where you also have transactions with that investee, the French country liaison SRB member proposes that the VCIG should state that the higher of the impacts from the equity share or the transactions should be reflected.
22. The EFRAG Secretariat does not disagree with this proposal but as ESRS 1 paragraph 67 is not phrased in this way, we hesitate to include this notion without consultation. Therefore, the counterproposal is to do a separate IG on this topic which may be very short but allows for consultation.

Question for EFRAG SRB

23. Does the EFRAG SRB approve IG 2?

Agenda papers

24. In addition to this cover note, agenda papers for this session are:
 - (a) Agenda paper 03-02 – Updated VCIG – clean; and
 - (b) Agenda paper 03-03 – Updated VCIG – tracked changes from consulted version (but after restructuring).