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Cover Note – Approval of draft ESRS Set 1

Objective and content of this paper

- 1 This cover notes illustrates the status of the drafts presented for approval of the SRB on the 15 November 2022. It has to be read in conjunction with Agenda Paper 02-03 uploaded for the EFRAG SRB meeting on the 27 October¹ that illustrated the due process followed by EFRAG from the issuance of the Exposure Drafts on 29 April 2022 until the SR TEG approval of the 25 October 2022.

Consideration for re-exposure

- 2 One of the questions that have been considered by the EFRAG Secretariat and the SR TEG is whether the changes from the Exposure Drafts require a re-exposure before being include in the final drafts.
- 3 On this regard, EFRAG due process procedures address the re-exposure as follows:

5.30 Decisions to re-expose are taken by the EFRAG SRB, in consultation with the EFRAG SR TEG. In doing so, the EFRAG SRB considers whether the revised proposals include any fundamental changes on which respondents have not had the opportunity to comment because they were neither contemplated nor discussed in the basis for conclusions accompanying the exposure draft. The EFRAG SRB also considers whether it will learn anything new by re-exposing the proposals.

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5.31 If EFRAG SRB is satisfied that the revised proposals respond to the feedback received and that it is unlikely that re-exposure will reveal any new concerns, it proceeds to finalise the proposed requirements. Once discussions have been finalised, the final draft standard (or draft amendment) will be submitted for approval by the EFRAG SRB.

- 4 Considering the above, the need to re-expose would only apply if there were any fundamental change that don't address comments received in the public consultation.
- 5 The EFRAG Secretariat notes that several changes have been made (see Agenda Paper 05.02 of the SRB 26 August 2022²), in order to reflect the updated CSRD text issued in June 2022. For these changes, the question whether a re-exposure is appropriate doesn't apply, as they derive directly from level one regulation and should simply be reflected in the standards.
- 6 The changes other than those needed to align to the new CSRD have been made to address concerns received in the public consultation.
- 7 In this context, the SR TEG has considered as part of its deliberations on the drafts whether any change to the draft would result in an approach that would be significantly 'new', i.e. not subject to exposure as part of the public consultation. On this basis, it was considered not appropriate to include guidance on value chain for financial institutions before consulting on their specific content. Similarly, it was considered not appropriate to include datapoints on ethnicity without consulting specifically on them.
- 8 In conclusion, there are no elements that would lead to consider that a re-exposure is needed.

Additional items considered by the SRB that didn't result in changes to the drafts but trigger more research and consultation in the coming months

- 9 During its deliberations the SRB considered the possible inclusion of a phase-in provision that would allow financial market participants (banks, insurers, asset managers) to postpone the inclusion of downstream value chain until the effective date of the future ESRS draft sector standards, in order to avoid double counting of the impact metrics and pending the establishment of a clear methodology. Considering the complexity of the topic and the need to have a public consultation on the approach to the value chain for financial market participants, the SRB finally decided not to include this phase-in provision. The SRB consider this as an area of priorities for research and public consultation in the next months/next sets of standards.
- 10 EFRAG SR TEG recommended to the SRB to decide whether to include a datapoint on ethnicity in [draft] ESRS S1³ and its nature (voluntary/mandatory), not expressing a technical advice in the approval of ESRS S1. EFRAG SR TEG suggested as well to the EFRAG SRB to have technical discussions, involving experts of this specific matter, and to consider the necessity to have a public consultation before including it in the standards, if

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<https://www.efrag.org/Assets/Download?assetUrl=%2Fsites%2Fwebpublishing%2FMeeting%20Documents%2F2208181115277740%2F05-02%20Assesment%20of%20the%20CSRD%20changes%20-%20Analysis.pdf>

³ The undertaking may disclose the percentage of the undertaking's own employees by ethnic origin. If the undertaking cannot collect ethnicity data due to legal restrictions, the undertaking can gather the required data by means of an anonymous and voluntary survey and disclose accordingly.

feasible already in time for the adoption in June 2023. This datapoint was not included in the Exposure Draft given that the topic of Diversity has been emphasized in the last text of the CSRD released only at the end of June. In a previous preparatory SR TEG discussion, members were split, with an equal number supporting this datapoint to be optional and required. Due to limits imposed by the GDPR (data privacy regulation), EFRAG TEG members acknowledged that this datapoint could be based on voluntary surveys, where only employees that are willing to disclose this information would do so. The SRB discussed the possibility and opportunity to include this datapoint and more broadly the coverage of the topic of ethnicity in the first set of standards. It was noted that the inclusion of this datapoint in time for June 2023 is not compatible with the need to run a public consultation. The EFRAG SRB recognises the importance of non-discrimination, diversity and equality at the workplace, whereby ethnicity is an aspect of diversity and that diversity was included in the final text of the CSRD. The SRB notes that specific datapoints on ethnicity were not consulted on in the Exposure Drafts on the First Set of draft ESRS and there is a need for proper definition and need for quality data serving comparability. The SRB finally decided to cover in the [draft] ESRS to be released in November 2022, the requirement to describe policies, action plans, targets and resources in relation to ethnicity as one of the dimensions of diversity. The SRB also decided not to include quantitative disclosures on racial and ethnic origin at this stage, but to undertake more research including obtaining the input of experts, noting that the deadline of November is not compatible with the depth of analysis that the subject deserves. As such, ethnicity is a priority topic for EFRAG future research and consultation in the coming months.

- 11 The SRB discussed the challenges of disclosing quantitative data on financial effects arising from opportunities. The absence of a common practice is the main reason to justify the three-years phase-in foreseen in the environmental standards for this datapoint (one year for climate considering that the topics is more mature). The SRB considered in particular whether the provision of data on opportunities shall be limited to opportunities that are factored into the business plans or for which business decisions to pursue the opportunity do exist at the reporting date, so that the management is able to elaborate reliable forward looking-estimates. Pending a specific public consultation on a framework to disclose on quantitative data on opportunities, the SRB agreed to amend the environmental standards, in order to clarify that the disclosure of such quantitative data is required only provided that the resulting disclosure meets the qualitative characteristics of quality (ESRS 1 Appendix C, including reliability). The SRB agreed that this is an area that deserves more research and public consultation in the coming months.
- 12 The SRB decided to amend ESRS 1 to clarify the threshold for impact materiality, including a reference to the 'most significant' impacts, a threshold used in the OECD and UNGP Guidelines, as well as in GRI standards. The SRB agreed to undertake further research in the coming months on the implementation of the impact materiality, to support the correct interpretation of the threshold and to support preparers in the implementation of the impact materiality.

Progresses on the drafts since the SR TEG approval on 25 October 2022

- 13 The SRB has agreed on a number of changes to the drafts and these changes are already reflected in the drafts uploaded for approval on this meeting. Below is a description of the changes on content of the standards (other than editorial changes):

ESRS 1

- 14 Approach to materiality (illustrated in Appendix F of the [draft] ESRS 1): The SRB confirmed the overall approach as approved by the SR TEG. However, it clarified more in detail when Disclosure Requirements (DR) and/or datapoints may be omitted (no omissions for DRs related to policies, actions and targets, no omissions in ESRS E1 and ESRS 2) and it introduced a condition to omit a datapoint (the information provide shall allow to meet the objective of the DR). It also decided to modify the area of mandatory items (to be reported irrespective of materiality):
- (a) to include⁴ the Disclosure Requirements in ESRS S1 Own workforce from S1-1 to S1-8 (adding to the 3 DR already mandatory, the DRs on policies, actions and targets – the latter mandatory only for undertakings with more than 250 employees);
 - (b) to exclude E5-4/E5-5 Circular economy: qualitative info on: resources inflow/outflow;
 - (c) to exclude G2-9 Political engagement and G2-10 Payment practices;
 - (d) to move ESRS S1-14 Fair remuneration and ESRS S1-15 – Social security from mandatory items to items subject to materiality assessment but requiring a reinforced transparency (i.e. when omitted the undertaking shall report that all the employees are covered by fair wage/social security).
- 15 Criteria for impact and financial materiality. Following the decision of the ISSB to discontinue the term 'significant' as a reference to materiality of risks and opportunities and in order to enhance the alignment with impact materiality assessment in GRI, the threshold for material impacts, risks and opportunities for reporting is now linked to the concept of them having respectively material effects on people and the environment and material financial effects. In the context of impact materiality, the threshold is further linked to the 'most material' criterion used in OECD and UNGP Guidelines in the sustainability due diligence process.
- 16 The language on financial materiality has been adjusted to come closer to the IFRS S1 language.
- 17 The overall approach to value chain information is confirmed. However, the wording has been reinforced to clarify the focus on material impacts, risks and opportunities.
- 18 The reference to the Member States option in the CSRD to omit prejudicial information has been replaced by a new option to omit information on intellectual property, know-how or result of innovations. The wording of this option uses language from the Trade Secrets Directive.
- 19 The possible sources of incorporation by reference has been broadened to also include EMAS, with reinforced conditions for the incorporation (same basis for preparation of ESRS information, including scope of consolidation and treatment of value chain information).

ESRS 2

- 20 Structure and index adjusted to mirror TCFD/IFRS four pillars, targets moved at the end, together with metrics.
- 21 GOV 1: Elimination of the datapoint: number of significant positions and commitments, and the nature of the commitments of members of the administrative, management and supervisory bodies (AMSB).

⁴ The numbering of DRs in this paragraph refer to their identification number in the EDs.

- 22 GOV 2: Elimination of the datapoint: key decisions made by the AMSB to address material IROs and of the specifications of which matters triggered initiatives to adjust the undertaking's strategy and business model.
- 23 SBM 1: this is now the result of the merger of three DRs (Market position, Strategy and Business Model and Value Chains). Elimination of the datapoint: breakdown of revenues by significant country.
- 24 Rationalization and streamlining of content and language in SBM and IRO.
- 25 Reporting on opportunities: provided new guidance on what the reporting on opportunities should contain.

ESRS E1

- 26 Moved climate-related requirements on resilience, IRO identification and governance from Application Guidance/requirements to the main body
- 27 Moved SFDR energy and GHG emission intensity per revenue in Energy and GHG emissions disclosure requirements
- 28 Merged removals and carbon credits in one DR with net zero targets
- 29 Presented internal carbon pricing as a separate DR
- 30 Moved Targets requirements to Metrics and targets
- 31 Added 4 EBA datapoints namely E1-1 (if the company is in Paris aligned benchmark) and E1-9 on potential financial effects (disaggregation by chronic and acute risk, location of significant assets and breakdown of real estate assets by energy performance)
- 32 Added exposure to coal, oil and gas related-activities in terms of revenue and CapEx
- 33 Deleted phase-in provisions on potential financial effects as these are addressed in ESRS1
- 34 Clarified that current/past financial effects are a requirement under ESRS 2
- 35 Modified language on potential financial effects on opportunities
- 36 Added language on reporting boundary and refined language on disaggregation and disclosure of Scope 1 and 2 emissions by consolidated accounting group (parent and subsidiaries) and unconsolidated investees (associates, joint ventures, other joint arrangements (joint operations) and unconsolidated subsidiaries (investment entities)
- 37 Clarified in the main body that scenario analysis is included in how the resilience analysis is conducted and in its results.
- 38 Clarified that ISO requirement may be referred to when determining GHG emissions if the undertaking already uses ISO14064, provided it complies with E1 by adding any missing datapoints.
- 39 Amended the language in the Application requirements on reference values for targets to make it clear that an ongoing monitoring of the latest reference material will be necessary and pointed to the acceptable sources of guidance.

ESRS E2

- 40 "Interactions with other ESRS": clarification of boundaries across E standards;
- 41 Elimination of the paragraph on "General, Strategy, Governance and Materiality assessment"

- 42 DR E2-3 (targets): additional datapoint on whether legal requirements has taken into account in the consideration of ecological thresholds;
- 43 DR E2-4: elimination from the main body of the unit to measure the emissions;
- 44 DR E2-6 (financial effects):
 - (a) elimination of reference to “dependencies” in the DR
 - (b) additional content on “financial effects arising from opportunities” [quantification not required if it would result in disclosure that does not meet the qualitative characteristics of information]
 - (c) elimination of transition provision requirement
- 45 Appendix A: introduction of the following terms:
 - (a) “ecological threshold”
 - (b) “installation” and “site”
 - (c) “substances of concern”
- 46 AR: alignments across E standards
- 47 Deleted phase-in provisions on potential financial effects as these are addressed in ESRS1

ESRS E3

- 48 “Interactions with other ESRS”: clarification of boundaries across E standards;
- 49 Elimination of the paragraph on “*General, Strategy, Governance and Materiality assessment*”
- 50 DR E3-3 (targets):
 - (a) additional data point on targets relate to “the management of material impacts, risks and opportunities related to areas at water risk, including improvement of the water quality”;
 - (b) additional data point on whether legal requirements has taken into account in the consideration of ecological thresholds
- 51 DR E3-4 (water consumption): replaced “or” with “and” in: “total water recycled and reused in m³” to be stick to SFDR KPI
- 52 DR E3-5 (financial effects):
 - (a) elimination of reference to “dependencies” in the DR and elimination of transition provision
 - (b) additional content on “financial effects arising from opportunities” [quantification not required if it would result in disclosure that does not meet the qualitative characteristics of information]
 - (c) elimination of transition provision requirement
- 53 Appendix A: introduction of the term “ecological threshold”
- 54 Application Requirements: alignments across E standards
- 55 Deleted phase-in provisions on potential financial effects as these are addressed in ESRS 1.

ESRS E4

- 56 E4-1 Transition plan on biodiversity and ecosystems: scope was specified for sectors listed in ESRS SEC1 that were identified by TNFD as priority sectors.
- 57 E4-5 par. 40: LCA on land-use now mandatory for priority sectors material impacts on land-use change and the status of ecosystems. Datapoint on EMAS was moved into AR and fully aligned with EMAS.
- 58 E4-5: SFDR-datapoint to report the share of non-vegetated surface area compared to the total surface area was removed.
- 59 In E4-5 clarification that boundaries for par. 43 to 46 is drawn around own operations.
- 60 E4-6 on Financial effects was aligned across environmental standards.
- 61 Appendix A: Amended a number of definitions (mitigation hierarchy; planetary boundaries; No net loss or net gain), added others (physical risks; transition risks) and deleted (biodiversity offsetting as now part of mitigation hierarchy; ecosystem preservation, genetic resources; local and indigenous knowledge) some.
- 62 IRO 1 par. 23 (d) (iii) was toned down to not require reporting of exact coordinates of sites.
- 63 IRO 1 AR 4: Added freshwater-use change as sub-sub-topic, as requested by TNFD.
- 64 IRO 1 AR 9 (d): Categories of opportunities aligned with TNFD.
- 65 E4-5 AR 38: Additional AR with reference to UN SEEA EA added.
- 66 Deleted phase-in provisions on potential financial effects as these are addressed in ESRS 1.

ESRS E5

- 67 ““Interactions with other ESRS”: clarification of boundaries across E standards;
- 68 Elimination of the paragraph on “General, Strategy, Governance and Materiality assessment”
- 69 DR E5-3 (targets):
 - (a) elimination of data point related to “outflows and waste (including in production, use phase and at end of functional life)”;
 - (b) improvement of the wording on “waste treatment” [the waste management, including preparation for proper treatment];
 - (c) additional data point on whether legal requirements has taken into account in the consideration of ecological thresholds
- 70 DR E5-5 (resource outflows): additional data points on “waste streams” and “materials that are present in the waste “ (see par. 39);
- 71 DR E5-6 (financial effects):
 - (a) elimination of reference to “dependencies” in the DR
 - (b) additional content on “financial effects arising from opportunities” [quantification not required if it would result in disclosure that does not meet the qualitative characteristics of information]
 - (c) elimination of transition provision requirement
- 72 Appendix A: introduction of the following terms:

- (a) “business as usual”
 - (b) Hazardous waste [new wording];
 - (c) Waste management
- 73 Application Requirements:
- (a) alignments across E standards
 - (b) more guidance on E5-3 (AR 19 and AR 21;
- 74 Deleted phase-in provisions on potential financial effects as these are addressed in ESRS 1.

ESRS S1

- 75 Scope. Adding back privacy and housing from the April ED
- 76 Additions to the list of mandatory Disclosure Requirements: Disclosure requirements S1-1 to S1-5 and S1-9 Diversity for undertakings with 250 employees or more.
- 77 Architecture of Disclosure Requirements. Increase of the number of Disclosure Requirements by 1 as diversity and people with disabilities has been split.
- 78 S1-1 Policies. A number of new datapoints (approx. 10) for diversity policies to be mandatory . Reduction of datapoints as list of international instruments that policies were to be aligned reduced to only UNGP, UNGC and OECD.
- 79 S1-6 Characteristics of the undertaking’s employees. Reduction of datapoints/breakdowns of full time by gender and by region and part-time by gender and by region. No further option to use other methodology that differs from FTE or headcount.
- 80 S1-8 Collective Bargaining. Reduction of 2 datapoints on c) regarding operations outside EEA.
- 81 S1-9 Diversity indicators. Reduction of datapoints as ethnicity was not included in set 1 as a KPI.
- 82 S1-10 Adequate wages. Additional datapoint from the April ED on percentage of own workforce paid below the adequate wage, broken down for employees and non-employees.
- 83 S1-11 Social protection. Reduction of quantitative datapoints on lack of social protection coverage.
- 84 S1-12 Persons with disabilities. Reduction of datapoint on the breakdown by gender.

ESRS S2/ S3/ S4 (Mainly editorial changes)

- 85 Objective - Specification of the scope of the standards/IROs covered by the standards (paras 1, 4 and 5).
- 86 DR2 and DR3 - Clarification/simplification of disclosure requirements
- 87 S3 Glossary - Definitions - Inclusion of missing definition on Free, Prior and Informed Consent in relation to the rights of indigenous people
- 88 S3 Application requirements - New paras covering IROs in relation to affected communities connected to environmental IROs

ESRS G1

- 89 ESRS G1-2 Management of relationships with suppliers: added a requirement for a description of policies/practices to prevent late payments to SMEs.
- 90 Streamlined paragraph 17 under ESRS G1-3 Prevention and detection of corruption/bribery to align with wording in social standards.
- 91 Aligned requirements on training in paragraph 18 with those in GRI and deleted voluntary information around the information programme with own workforce and management.
- 92 ESRS G1-5 Political influence and lobbying activities: updated the wording to that of the new CSRD. Financial information about spending on lobbying activities now voluntary and additional granular information similarly deleted.
- 93 ESRS G1-6 Payment practices: Split of SME information deleted and while the standard payment terms requirement was simplified, this still includes the requirement to provide such information by main category of suppliers.

Next steps: editorial review of the drafts

- 94 The drafts provided for the meeting today are subject to editorial review. This includes, among other steps:
 - (a) editorial review of SRB members and EFRAG Secretariat;
 - (b) checking references to number of paragraph and name of paragraph/chapter within the same standard and in other standards;
 - (c) streamlining/understanding of the language;
 - (d) alignment of language across standards;
 - (e) formatting.