EFRAG ESRS Q&A Platform

COMPILATION OF EXPLANATIONS

DECEMBER 2024

EFRAG
sustainability reporting

Disclaimer

This Compilation of Explanations by EFRAG provides non-authoritative guidance and accompanies the European Sustainability Reporting Standards (ESRS), as stipulated in Article 19a and 29a of Directive 2013/34/EU (the Accounting Directive). This means that if anything in this document appears to contradict any requirement or explanation in ESRS, ESRS take precedence. This Compilation of Explanations is issued following EFRAG's due process for such non-authoritative documents and under the sole responsibility of EFRAG.

EFRAG assumes no responsibility or liability whatsoever for the content or any consequences or damages directly, indirectly or incidentally arising from following the advice or guidance contained in this document. Users of this document are advised to exercise their own judgment in applying ESRS. Information contained in this document should not be substituted for the services of an appropriately qualified professional.

This Compilation of Explanations has been developed for use by large listed and unlisted companies that are subject to ESRS. It is therefore not intended for use by non-listed small- and medium-sized enterprises (SMEs), which may use the upcoming voluntary standard for SMEs.

This Compilation of Explanations relates to the sector-agnostic ESRS as adopted by the European Commission on 31 July 2023. Sector-specific standards may add sector specifications.

The content of each Explanation has been drafted to provide an answer to a specific technical question and cannot be directly extended by analogy to a different fact pattern.

About EFRAG

EFRAG's mission is to serve the European public interest in both financial and sustainability reporting by developing and promoting European views in the field of corporate reporting. EFRAG builds on and contributes to progress in corporate reporting. In its sustainability reporting activities, EFRAG provides technical advice to the European Commission in the form of draft European Sustainability Reporting Standards (ESRS) elaborated under a robust due process and supports the effective implementation of ESRS. EFRAG seeks input from all stakeholders and obtains evidence about specific European circumstances throughout the standard-setting process. Its legitimacy is built on excellence, transparency, governance, due process, public accountability and thought leadership. This enables EFRAG to speak convincingly, clearly, and consistently and be recognised as the European voice in corporate reporting and a contributor to global progress in corporate reporting.

EFRAG is funded by the European Union through the Single Market Programme in which the EEA-EFTA countries (Norway, Iceland and Liechtenstein) as well as Kosovo participate. Any views and opinions expressed are, however, those of the author(s) only and do not necessarily reflect those of the European Union, the European Commission or of countries that participate in the Single Market Programme. Neither the European Union, the European Commission nor countries participating in the Single market Programme can be held responsible for them.

Table of Contents

Introduction ***4***

Environment ***5***

ESRS E1 *Climate change* **5**

ESRS E1-4 Targets related to climate change mitigation and adaptation **5**

ESRS E4 *Biodiversity and ecosystems* **7**

ESRS E4 Disclosure Requirement related to ESRS 2 SBM-3 – Material impacts, risks and opportunities and their interaction with strategy and business model **7**

ESRS E4-5 – Impact metrics related to biodiversity and ecosystems change **8**

The Questions in this document are identified by the progressive number (ID) that they receive at the beginning of the submission to the Q&A Platform. The system attributes identification numbers also to partial submissions. For this reason, the ID number is not indicative of how many questions EFRAG has finally received.

Introduction

EFRAG has started the collection of questions related to ESRS through the EFRAG ESRS Q&A Platform on 24 October 2023. EFRAG releases explanations following due process on a regular basis. Explanations are non-authoritative in nature and answer technical questions on ESRS by showing where in the standards the content is provided and how to navigate it accordingly.

Since October 2023, EFRAG has released the following batches of explanations (number of explanations):

February 2024	12
March 2024	12
May 2024	44
July 2024	25
November 2024	64
December 2024	5
Total	162

Explanations released from February to November have been combined and been published in the Compilation of Explanations – January–November 2024. The December 2024 batch contains explanations for five additional questions, some of which are expected to be particularly relevant to certain sectors. They will later be added to the next major update to the Compilation of Explanations expected to be released in Spring 2025. The questions are identified by a progressive identification number (ID), which they received when submitted to the Q&A Platform.

Environment

ESRS E1 *Climate change*

ESRS E1-4 *Targets related to climate change mitigation and adaptation*

Questions ID 1033, 1076 and 1122 – Value chain phase-in for climate-related targets and credit institutions

Release date

December 2024

Questions asked

ID 1033: In the context of ESRS E1 paragraph 34 (a) and in a situation where a credit institution has set GHG emissions intensity targets, are credit institutions expected to provide associated absolute values in relation to their emissions intensity targets even if such metric is not used to steer the portfolio and due to the fact that it can be neither predictive or of confirmatory value due to the business model of the credit institutions?

ID 1076: Would it be possible for a financial institution to disclose GHG emissions targets set on Scope 3 category 15 (i.e. 'financed emissions') without reporting the corresponding targets in absolute emissions?'

ID 1122: Regarding absolute values for financial institutions – why not show exposure and exposure percentages instead of GHG emissions?'

Key Terms

GHG removal; GHG emission reduction; value chain phase-in; credit institutions

ESRS reference

ESRS E1 paragraphs 34 and AR 23; ESRS 1 paragraphs 132 and 133

Background

Questions ID 1033, 1076 and 1112 as listed above were merged and answered simultaneously in this Explanation.

ESRS E1 paragraph 34 (a) states: 'If the undertaking has set GHG emission reduction targets, ESRS 2 MDR-T and the following requirements shall apply:

(a) GHG emission reduction targets shall be disclosed in absolute value (either in tonnes of CO2eq or as a percentage of the emissions of a base year) and, where relevant, in intensity value …'.

ESRS E1 paragraph AR 23 states: 'Under paragraph 34 (a), the undertaking may disclose GHG emission reduction targets in intensity value. Intensity targets are formulated as ratios of GHG emissions relative to a unit of physical activity or economic output. Relevant units of activity or output are referred to in ESRS sector-specific standards. In cases where the undertaking has only set a GHG intensity reduction target, **it shall nevertheless disclose the associated absolute values for the target year and interim target year(s).** This may result in a situation where an undertaking is required to disclose an increase of absolute GHG emissions for the target year and interim target year(s), for example because it anticipates organic growth of its business.'

ESRS 1 paragraph 132 states: 'For the first 3 years of the undertaking's sustainability reporting under the ESRS, in the event that not all the necessary information regarding its upstream and downstream value chain is available, the undertaking shall explain the efforts made to obtain the necessary information about its upstream and downstream value chain, the reasons why not all of the necessary information could be obtained, and its plans to obtain the necessary information in the future.'

ESRS 1 paragraph 133 of Chapter 10.2 *Transitional provision related to Chapter 5 Value chain* states: 'For the first 3 years of its sustainability reporting under the ESRS, in order to take account of the difficulties that undertakings may encounter in gathering information from actors throughout their value chain and in order to limit the burden for SMEs in the value chain:

(a) when disclosing information on policies, actions and targets in accordance with ESRS 2 and other ESRS, the undertaking may limit upstream and downstream value chain information to information available in-house, such as data already available to the undertaking and publicly available information; and

(b) when disclosing metrics the undertaking is not required to include upstream and downstream value chain information except for datapoints derived from other EU legislation as listed in ESRS 2 Appendix B.'

Answer

Scope 3, category 15 (Investments) targets for the lending portfolio are considered value chain information (see also IG 2 *Value Chain*, FAQ 2).

When reporting on GHG emission reduction targets, an undertaking may refer to ESRS 1 paragraph 133 (a) of Chapter 10.2 *Transitional provision related to Chapter 5 Value chain*, which allows an undertaking to adopt transitional measures for value chain information in the first three annual sustainability statements.

This provision is applicable when the undertaking has adopted intensity targets for its Scope 3, category 15 (Investments) emissions, but the corresponding associated absolute values for the target year and interim target years (ESRS E1-1 paragraph AR 23) are not available (see ESRS 1 paragraph 132).

When only targets in intensity value are available, in the first three years of reporting, a financial institution may limit the information on value chain targets to the information available in-house, which might include data already collected for Pillar 3 reporting.

EFRAG may work on specific sector provisions in the future to cover this issue.

ESRS E4 *Biodiversity and ecosystems*

ESRS E4 *Disclosure Requirement related to ESRS 2 SBM-3 – Material impacts, risks and opportunities and their interaction with strategy and business model*

Question ID 1116 – Disclosure requirements related to ESRS E4 Disclosure Requirement SBM-3 if biodiversity is material for the upstream value chain only

Release date

December 2024

Question asked

Is the ESRS 1 Disclosure Requirement SBM-3 metric to be reported for ESRS E4 if biodiversity was assessed as not material for the company's own operations but material only for the upstream value chain? The SBM-3 metric specifically refers to the company's own sites, i.e. own operations. Additionally, no sites were found located in or near biodiversity-sensitive areas that have negative impacts on these areas.

ESRS Reference

ESRS E4 paragraph 16 (Disclosure Requirement SBM-3 *Material impacts, risks and opportunities and their interaction with strategy and business model*)

Key terms

Value Chain

Background

ESRS E4 paragraph 16: states: 'The undertaking shall disclose:

(a) a list of material sites in its own operations, including sites under its operational control, based on the results of paragraph 17 (a). The undertaking shall disclose these locations by:

  i. specifying the activities negatively affecting biodiversity-sensitive areas;

  ii. providing a breakdown of sites according to the impacts and dependencies identified, and to the ecological status of the areas (with reference to the specific ecosystem baseline level) where they are located; and

  iii. specifying the biodiversity-sensitive areas impacted, for users to be able to determine the location and the responsible competent authority with regard to the activities specified in paragraph 16 (a) (i);

(b) whether it has identified material negative impacts with regard to land degradation, desertification or soil sealing; and

(c) whether it has operations that affect threatened species.'

Answer

If the topic 'biodiversity and ecosystems' has been identified as material for the undertaking's upstream (or downstream) value chain only, the undertaking:

(a) would not disclose the information required by ESRS E4 paragraph 16 (a), which refers to own operations only;

(b) would be required to disclose information required by ESRS E4 paragraph 16 (b) in connection with its upstream (or downstream) value chain, as ESRS E4 paragraph 16 (b) applies not only to impacts connected to the undertaking's sites in its own operations; and

(c) In relation to ESRS E4 paragraph 16 (c), the undertaking would be required to disclose whether it has operations that affect threatened species (this refers to own operations and not to operations in the upstream or downstream value chain). If ESRS E4 is material and does not have own operations that affect threatened species, it shall state so.

Finally, where appropriate, following ESRS 1 paragraph 11 the undertaking shall include information, including metrics (see IG 2 *Value chain* paragraph 79) related to its upstream and downstream value chain, on an entity-specific basis.

ESRS E4-5 – *Impact metrics related to biodiversity and ecosystems change*

Question ID 1058 – ESRS E4 metrics covering own operations or upstream/downstream value chain

Release date

December 2024

Question asked

ESRS E4-5 paragraph 37 mentions that 'For datapoints specified in paragraphs 38 to 41, the undertaking shall consider its own operations'. Does that mean that ESRS E4 paragraph 33 where it says 'The undertaking shall report metrics related to its material impacts on biodiversity and ecosystems' also refers to the undertaking's own operations only?

ESRS Reference

ESRS E4 paragraphs 33–41 (ESRS E4 Disclosure Requirement E4-5 – *Impact metrics related to biodiversity and ecosystem change*); ESRS 1 paragraphs 11, 30 and AR 3

Key terms

Metrics, own operations, materiality

Background

ESRS E4 paragraph 33 states: 'The undertaking shall report metrics related to its material impacts on biodiversity and ecosystems.'

ESRS E4 paragraph 35 states: 'If the undertaking identified sites located in or near biodiversity-sensitive areas that it is negatively affecting (see paragraph 19(a)), the undertaking shall disclose the number and area (in hectares) of sites owned, leased or managed in or near these protected areas or key biodiversity areas.'

ESRS E4 paragraph 36 states: 'If the undertaking has identified material impacts with regards to land-use change, or impacts on the extent and condition of ecosystems , it may also disclose their land-use based on a Life Cycle Assessment.'

ESRS E4 paragraph 37 states: 'For datapoints specified in paragraphs 38 to 41, the undertaking shall consider its own operations.'

ESRS 1 paragraph 11 states: 'In addition to the disclosure requirements laid down in the three categories of ESRS, when an undertaking concludes that an impact, risk or opportunity is not covered or not covered with sufficient granularity by an ESRS but is material due to its specific facts and circumstances, it shall provide additional entity-specific disclosures to enable users to understand the undertaking's sustainability-related impacts, risks or opportunities. Application requirements AR 1 to AR 5 provide further guidance regarding entity-specific disclosures.'

ESRS 1 paragraph 133 states: 'For the first 3 years of its sustainability reporting under the ESRS, in order to take account of the difficulties that undertakings may encounter in gathering information from actors throughout their value chain and in order to limit the burden for SMEs in the value chain ...

(b) when disclosing metrics, the undertaking is not required to include upstream and downstream value chain information, except for datapoints derived from other EU legislation, as listed in ESRS 2 Appendix B.'

ESRS 1 paragraph AR 3 states: 'When determining the usefulness of metrics for inclusion in its entity-specific disclosures, the undertaking shall consider whether:

(a) its chosen performance metrics provide insight into:

   i. how effective its practices are in reducing negative outcomes and/or increasing positive outcomes for people and the environment (for impacts); and/or

   ii. the likelihood that its practices result in financial effects on the undertaking (for risks and opportunities);

(b) the measured outcomes are sufficiently reliable, meaning that they do not involve an excessive number of assumptions and unknowns that would render the metrics too arbitrary to provide a faithful representation; and

(c) it has provided sufficient contextual information to interpret performance metrics appropriately, and whether variations in such contextual information may impact the comparability of the metrics over time.'

Answer

IG 2 *Value chain* specifies in its 'VC coverage map of ESRS Set 1' on page 44 that E4-5 'only reflects own operations, as no coverage of the value chain is required.' For clarity, it is to be noted that:

(a) ESRS E4 paragraph 37 specifies, in relation to the Disclosure Requirements in paragraphs 38 to 41, that undertakings are to consider only own operations;

(b) ESRS E4 paragraph 35 specifies metrics focusing on sites owned, leased or managed by the undertaking; and

(c) ESRS E4 paragraph 36 is a voluntary disclosure on land use based on a life cycle assessment, which inherently considers the undertaking's value chain, as it involves assessing the impact of products or services on land use across all stages, from raw material sourcing to production and disposal.

In addition, if the undertaking identified material impacts, risks or opportunities in the value chain, it shall determine whether and what additional entity-specific disclosures it needs to disclose in line with ESRS 1 paragraphs 11 and 30 (b). See in particular ESRS 1 paragraph AR 3 on how to determine the usefulness of metrics for inclusion in entity-specific disclosures. It is to be noted that transitional provisions apply to the disclosure of value chain information (see ESRS 1 paragraph 133 (b)).