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Sector Classification SEC 1 - update

Cover Note

Objective

- 1 SEC 1 – the overall ESRS Sector Classification has been approved by EFRAG SR TEG with exception of the sector descriptions of the financial sector and for the treatment of bio-energy.
- 2 The objective of this session is to decide on these two aspects, so to complete the approval of SEC 1 ED.

Background

Status of the documents

- 3 The EFRAG SR TEG has approved the SEC 1 ED on 2 March 2023 with a view to consulting on it in 2023. Due to a change in priorities starting in mid-March 2023, the approval at the SRB did not take place. This gave the EFRAG Secretariat additional time to conduct outreach with EFRAG's Sector Communities in the beginning of 2024, which led to the identification of a number of changes to be made to the detailed aggregation of NACE codes into ESRS Sectors. In particular, during February 2024 the grouping approach to drafting was discussed with the different sector communities in 11 workshops. Their comments and suggestions led to a number of changes, most profoundly, to the inclusion of specialised sales activities within the respective manufacturing sectors, the use of NACE Classes more than once and – in some cases – working with NACE economic activities at a more granular level than four-digits so as to permit assigning activities within one NACE Class to different sectors. In addition, these leasing activities have been integrated within the different sectors. To enhance interoperability with other frameworks, a few sectors have been integrated into others: Tobacco, Gaming, Paper and Wood products, and Marketing. Finally, two additional sectors have been created: Bioenergy and Household goods n.e.c. (merging and extending the previous Sports and Equipment, Construction and Furnishings sectors).
- 4 Such changes have been discussed and approved by the EFRAG SR TEG with the exception of the treatment of bioenergy (for which a supplementary discussion is needed before it concludes whether a separate sector is needed – in this draft, bioenergy activities are spread across the relevant sectors) and of financial institutions (for which the EFRAG Secretariat expects to obtain advice from the three Advisory Panels in the next two months). Accordingly, the content of this document for bioenergy and financial institutions is still subject to discussion.

Content of the documents

- 5 The ESRS sector classification is intended to be enacted as an ESRS in a Delegated Act after the public consultation and subsequent changes. This ED (SEC 1) illustrates how NACE codes are aggregated to form sectors, providing in this way a central reference for all the undertakings on how to report on their sectors of activities. This will be the infrastructure for the application of Sector ESRS. At the same time, considering the phase-ins as proposed by the Delegated Act supplementing Directive 2013/34/EU with regard to sustainability reporting standards, from 2025 onwards undertakings are due to report the disclosure required by SBM 1 of ESRS², which includes also a breakdown of the revenues by ESRS sector and requires SEC 1 to be enacted in order to be effective.

Potential future revisions to SEC 1

- 6 The sector classification approach in ESRS SEC 1 ED reflects a desktop review and grouping approach supplemented by the outreach ran in February 2024. The draft has also been prepared on the basis of a reconciliation table with the SASB classification system. The reconciliation table with SASB classification has been prepared by the EFRAG Secretariat and has not been approved by the ISSB or the ISSB. The preparatory work on the first sectors shows that the activity that leads to the definition of sustainability matters and disclosure requirements applicable at the sector level can bring new evidence on the NACE aggregation of the specific sectors.
- 7 Future changes to the aggregation of sectors cannot be in principle excluded; however, they will be kept to the minimum possible level.
- 8 EFRAG is aware that a new NACE classification is applicable as of 2025; this ED (SEC 1) has been aligned with this new NACE classification 2.1.

Relationship with the EU Taxonomy for sustainability activities

- 9 The ESRS Sectors as defined in this ED and the EU Taxonomy have very different goals. The first serves to support the disclosure requirements connected to particular sectors and the undertakings active in these sectors. The latter aims to steer sustainable investment and to implement the EU Green Deal.
- 10 For the reasons explained in the Basis for Conclusions of this ED, a mapping exercise to establish the link between the scope of the ESRS Sectors and the EU Taxonomy activities would have limited benefits. Hence, this document does not provide a mapping between those two frameworks.

Changes made after SRB approval 4 June

- 11 On 8 May 2024 EFRAG SR TEG approved the SEC 1 ED (except bio-energy and financial institutions).
- 12 On 4 June 2024 SRB approved the SEC 1 ED subject to a number of comments. In order to prepare SEC 1 for publication, the inclusion of the sector definitions of the financial sector and the creation of a bio-energy sector still needs to be discussed.
- 13 The SRB requested the following updates to SEC 1:
- (a) Clarification of what is meant with “internal activities”;
 - (b) Clarification of the 10% revenue border and incorporation of a decision tree to determine when to apply one or more sector standards;

Sector Classification SEC 1 – Cover Note

- (c) Clarify that only activities of own operations are to be considered when deciding on which sectors to apply;
 - (d) Incorporation of particular “Defined Terms” from the Oil and Gas ED and Mining, Quarrying and Coal ED. These are defined terms not included in ESRS Set 1, which arise from Oil and Gas ED and Mining Quarrying Coal ED and are expected to also be applicable to other sectors, therefore they would better be placed in a cross sector delegated act (SEC 1);
 - (e) Incorporation of the sector materiality approach from the Oil and Gas ED, as this is a cross sector authoritative requirement applicable to all the sectors;
 - (f) Replacing one of the examples (credit institution taking over a chemical company) with an explanation of which sector standards to apply when an undertaking takes over its supplier (active in a different sector);
 - (g) Incorporation of the IRO 2 approach from the General Approach document;
 - (h) Various editorial comments;
 - (i) Further detailing of the mappings with SASB as the current one was found to be too high level. The EFRAG Secretariat is developing, in cooperation with the ISSB staff, a mapping at 4- digit NACE code level. The version currently available has to be validated with the ISSB staff.
 - (j) A mapping at NACE code level with GICS, SICs, ICB, GRI and with TNFD would be helpful. The EFRAG Secretariat has produced a first version of these maps and is activating the relevant contacts for the validation with the various interested organisations.
 - (k) During the EFRAG SR TEG approval session, it was recommended to update all sector descriptions, aligning them with NACE language. In this context, for the sectors that are under development and therefore an indication of subsectors for the standards has been produced for the navigation table, such indication has also been included now in SET 1.
 - (l) In addition, mappings have been moved to the Basis for Conclusions that will accompany the ED.
- 14 The financial sector descriptions were discussed with the members of the financial institutions advisory panel of respectively the Capital Markets panel, the Banking panel and the Insurance panel. They are indicated in grey background in the SEC 1 document.
- 15 The EFRAG Secretariat intends to consult in writing on the Basis for Conclusions and the questionnaire to SEC 1.

Creation of an ESRS Sector relating to bio-energy

- 16 SR TEG members discussed a previous version of the bio-energy paper on 25 April 2024 and before taking a decision requested a more detailed overview of the creation of this ESRS sector would affect interoperability with other sustainability frameworks.
- 17 The EFRAG Secretariat has thus provided more information on how bio-energy related disclosures for this new ESRS sector would relate to GRI and SASB frameworks.

Questions for EFRAG SR TEG

- 18 Does SR TEG agree with the Capital Markets sector description and subsectors?
- 19 Does SR TEG agree with the Banking sector description and subsectors?
- 20 Does SR TEG agree with the Insurance sector description and subsectors?
- 21 Does SR TEG agree to recommend these descriptions to the SRB for approval?
- 22 Does SR TEG have comments on the incorporation of the other changes to SEC 1 described in this cover note?
- 23 Does SR TEG agree with the creation of a new ESRS sector related to bio-energy and recommend it's creation to the SRB for approval?

Agenda Papers

- 24 In addition to this cover note, agenda papers for this session are:
 - (a) Agenda paper 05-02 – SEC 1 Sector classification – clean
 - (b) Agenda paper 05-03 – SEC 1 Sector classification – compared;
 - (c) Agenda paper 05-04 – SEC 1 – Basis for Conclusions; and
 - (d) Agenda paper 05-05 – Bio-energy sector – ESRS vs other frameworks.