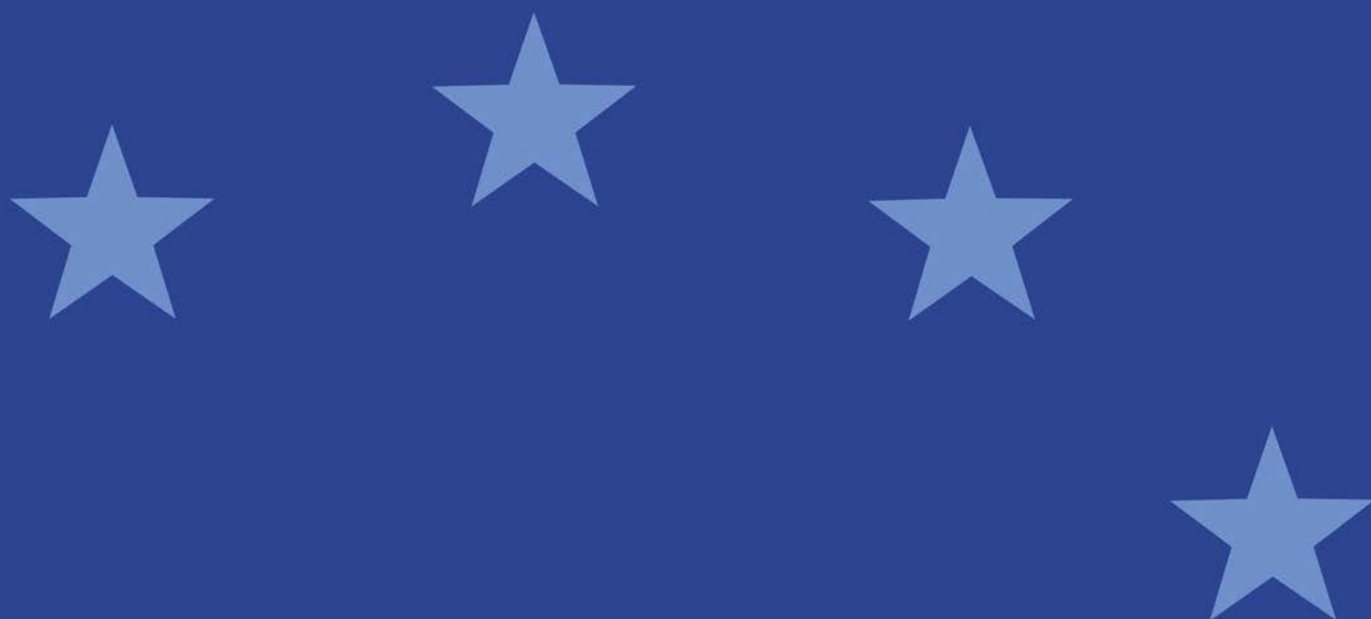


# Response to public consultation

**ESMA's response to EFRAG's consultation on the first set of draft ESRS**



## Scope of ESMA's response

This consultation response was prepared by ESMA from the viewpoint of securities regulators.

ESMA has addressed a subset of the questions in EFRAG's consultation material. This reflects the fact that ESMA has selected which remarks to raise based on the four main criteria which it will also apply when preparing its opinion on the final version of the ESRS which EFRAG will deliver to the European Commission.

The table below lists the questions ESMA has addressed in each section of EFRAG's consultation material. In light of ESMA's specific mandate on corporate governance under Art. 1(3) of the ESMA Regulation, more detailed answers were provided on the topical standards on governance-related matters (section 3D). The questions in EFRAG's consultation material to which ESMA has not responded are not included in this document.

<b><i>Section of EFRAG's consultation material</i></b>	<b><i>Questions addressed by ESMA</i></b>
1A. Overall ESRS exposure Drafts relevance - Architecture	Q1, Q3, Q4, Q5, Q9, Q11, Q12
1B. Overall ESRS Exposure Drafts relevance – Implementation of CSRD principles	Q18, Q19, Q21, Q22, Q24, Q28, Q33, Q34
1C. Overall ESRS Exposure Drafts relevance – Exposure Drafts content	Q38, Q39, Q40, Q41, Q42, Q43, Q44, Q45, Q46, Q47, Q48, Q49, Q50
2. ESRS implementation prioritisation / phasing-in	Q56
3D. Adequacy of Disclosure Requirements – Governance standards	Q117, Q118, Q119, Q120, Q121, Q122, Q123, Q124, Q125, Q126, Q127, Q128, Q129, Q130, Q131, Q132, Q133, Q134, Q135, Q136

ESMA's consultation response is delivered without prejudice to its opinion on the final version of the ESRS which EFRAG will deliver to the European Commission.

## 1A. Overall ESRS Exposure Drafts' relevance – Architecture

### *Cross-cutting and topical standards*

**Q1: in your opinion, to what extent do the structure and articulation of cross-cutting and topical standards adequately support the coverage of CSRD topics and reporting areas?**

#### *Cross-cutting and topical standards*

ESMA notes that the combination of cross-cutting and topical standards ensures the coverage of the reporting areas and topics addressed by the CSRD. However, at times the topical standards complement the cross-cutting standards with additional requirements or require that the cross-cutting standards are read in the context of the specificities of the topical standards. This may result in a situation in which finding the relevant disclosure requirements for a certain cross-cutting topic becomes challenging (e.g., requirements on the sustainable business model, on impacts, risks and opportunities or on governance) given that it is necessary to navigate through cross-cutting standards and topical standards and across both core text and application guidance. EFRAG may want to consider moving these cross-cutting requirements directly into the topical standards. This approach will help make each of the topical standards a self-contained set of requirements to the widest possible extent.

#### *'Disclosure principles' on implementation and 'disclosure requirements'*

We have doubts on the proposed cross-cutting 'disclosure principles' in ESRS 1 which are *de facto* a list of disclosure requirements complementing the cross-cutting requirements in ESRS 2 and indirectly the requirements in the topical standards. For the overall clarity and efficiency of the framework, we recommend that the content of these 'principles' be re-allocated to the relevant disclosure requirements or that they at least be renamed into disclosure requirements and that it be better clarified how they relate to ESRS 2 and topical standards.

#### *Hyperlinks and glossary*

ESMA also highlights that it would be helpful from a practical perspective to insert hyperlinks when one standard refers to another (we acknowledge this may not be possible in the delegated acts which will enact the ESRS, but it could be done if EFRAG makes a version of the standards available on its website). It would be useful to have a common glossary across the entire set of ESRS since defined terms are sometimes standard-specific and sometimes transversal.

### *Alignment and interoperability with international standards and frameworks*

**Q3: in your opinion, to what extent does the approach taken to structure the reporting areas promote interoperability between the ESRS and the IFRS Sustainability Exposure Drafts?**

#### *General comments on interoperability*

ESMA strongly encourages EFRAG to make all possible efforts to develop standards that,

while fully complying with the CSRD requirements, minimise unnecessary divergence with the upcoming IFRS Sustainability Standards and other relevant standards, like GRI. ESMA notes that the CSRD refers explicitly to the need for the ESRS to take account, to the greatest extent possible, of the work of global initiatives while remaining consistent with the EU legal framework and sustainability objectives. In ESMA's view, it is important that in finalising the ESRS, EFRAG identifies the differences with existing and developing international standards and group them into 3 categories: 1) those due to compliance with EU requirements (e.g., CSRD, SFDR, TR, BMR), including sustainability-related objectives; 2) those due to impact materiality; and 3) other differences. Differences in the third bucket should be carefully analysed to understand their rationale and the consequences of leaving them unaddressed. These differences may also constitute a basis for providing suggestions related to the development of international standards.

#### *Architecture*

One such difference that is not entirely due to specificities of EU legislation is the architecture of the ESRS vis-à-vis the architecture of the draft ISSB standards. In this regard, ESMA notes that the TCFD structure, that is used in the IFRS Sustainability Standards and that is also the starting point for the ESRS, has been re-worked by EFRAG into a more complex architecture. ESMA recommends that EFRAG seek stronger alignment with the original TCFD structure to ensure a closer consistency with this well-known and broadly endorsed architecture thus facilitating alignment with the IFRS Sustainability Standards. Such an alignment would be to the advantage of users of sustainability information under both sets of standards as they would be able to more easily compare the information. It would also be to the benefit of preparers who would be able to more easily navigate both sets of standards when compiling their reporting. Furthermore, a closer alignment would make the ESRS and ISSB standards more mutually compatible and as such easier to amend to reflect future developments in either set of standards.

Concretely, it would be important to achieve maximum consistency in the architecture of the ESRS general and climate change-related requirements and the IFRS Sustainability Standards while still catering for necessary adjustments to the TCFD architecture, e.g. to reflect the fact that in the EU context reference should be made not only to 'risk management' but also to 'impacts management' or to accept that for the structure of the governance standards, the TCFD 'governance' pillar may not be well suited.

#### *Concepts and terminology*

Similarly, when the ESRS and the IFRS Sustainability Standards intend to require the same quantitative or qualitative information, the terminology used for those common disclosure requirements should be as aligned as possible. Consistency in terminology would also be important with GRI, most notably for requirements regarding impact materiality. GRI is currently the most commonly used reporting framework under the NFRD and making the ESRS as consistent as possible with GRI will therefore be helpful for many preparers.

It would also be important to more clearly align the concept of financial materiality in the ESRS with that of enterprise value creation in the ISSB standards. This will facilitate interoperability between the two sets of standards.

ESMA also observes that the identification and description of qualitative characteristics of

sustainability information in ESRS 1 diverges from that in both IFRS Sustainability Standards and existing IFRSs (e.g., 'timeliness' is missing, the definition of prudence is not aligned to that in the IASB Conceptual Framework, in the definition of faithful representation 'free from error' is replaced by 'accurate', the definition of 'relevance' talks about 'substantive influence on the assessments and decisions of users' instead of the IFRS notion of information 'capable of making a difference in a decision').

Lastly, it would be important to seek alignment with the ISSB on the approach to sector-specific standards which would ideally be based on a converged sector classification. We note that the SASB sector classification differs from the NACE code classification typically used in Europe and, therefore, alignment should be ensured, starting with a mapping of the SASB classification to the classification that will be adopted by EFRAG. The mapping exercise may also help identify requirements that are not sufficiently relevant and could be dropped and those that better fit the sector-agnostic category to maximise comparability amongst entities, even though undertakings can still determine whether to provide the information resulting from any of the requirements based on materiality.

### ***Consideration given to EU policies and legislation***

**Q4: in your opinion, have these European legislation and initiatives been considered properly?**

#### *SFDR*

As regards the disclosure requirements applicable to financial market participants under the SFDR, ESMA has not identified any missing points or fundamental inconsistencies in the draft ESRS. It thus appears that the disclosure required under the ESRS will go far in permitting financial market participants to meet their obligation to disclose principal adverse impact (PAI) indicators.

We have the following detailed comments in relation to alignment with the PAI indicators:

- E2-4, par. AG 16(a) says '*the total amount of inorganic emissions in tons*'. We would recommend adjusting this to '*the total amount of inorganic pollution in tons*'. Making this adjustment would ensure consistency across the language within the standard and avoid creating doubt as to what the breakdown of 'inorganic emissions' is.
- In E3-4, it is not clear whether the requirement is for a composite KPI accounting for both 'emissions to water' and 'direct emissions of nitrates, phosphates and pesticides' or for two separate indicators. We observe that PAI indicator n°8 (table 1) requires one measure covering both.
- In E3-5, we suggest mentioning that the result must be expressed in 'millions' of the monetary unit in line with the SFDR PAI indicators.
- In E5, the definition of 'hazardous waste' is not fully aligned with the definition given in the SFDR Level 2 and we suggest referring to Art. 3(2) of Directive 2008/98/EC. It could furthermore be useful to add the definition of 'non-recycled waste' from the

SFDR Level 2 in Appendix A and to align the definition of 'recycling' with that in Art. 3(17) of Directive 2008/98/EC.

- In S2-2, EFRAG could consider specifying in par. AG 16 that when an undertaking does not have a supplier code of conduct, it should state that fact. This would ensure fuller alignment with PAI indicator n°4 (table 3).

In addition, we observe that the CSRD aims to ensure consistency between the ESRS and the SFDR so financial market participants have access to the information they need from their investee companies to comply with their SFDR disclosure obligations. For this reason, it would be important:

- to make all ESRS disclosure requirements which meet the needs of financial market participants under the SFDR mandatory as opposed to optional. For example, E3-5 covers the disclosure which is required under PAI indicator n°6 (table 2). However, E3-5 is optional and therefore undertakings may decide not to provide this disclosure.
- to indicate that all ESRS disclosure requirements which meet the needs of financial market participants under the SFDR are likely to be material since investor companies will be looking for this disclosure.

If these points are not clarified, financial market participants could end up not receiving the disclosure from undertakings under the CSRD / ESRS which they, in turn, need to meet their disclosure obligations under the SFDR.

We also encourage EFRAG, in its discussions with the ISSB of aligning the ESRS and the IFRS Sustainability Standards, to encourage the ISSB to consider catering, where possible, for the SFDR PAI indicators to the widest possible extent. It goes without saying that the ISSB is not obliged to onboard all EU legislation into its standards. However, financial market participants subject to the SFDR will be looking for their investee companies – whether they are EU or non-EU entities – to disclose the SFDR's PAI indicators. This may make it relevant to try to accommodate these indicators in the IFRS Sustainability Standards as far as possible.

#### *Benchmark Regulation*

ESMA observes that the ESRS contain many disclosure points which would permit benchmark administrators to disclose the ESG factors required by Commission Delegated Regulation (EU) 2020/1816. However, we note that the following disclosure point appears to be missing:

- corporate information that will enable benchmark administrators to understand the exposure of the benchmark portfolio to renewable energy as measured by capital expenditures (CapEx) in those activities (as a share of total CapEx by energy companies included in the portfolio).

We therefore encourage EFRAG to add such a disclosure point.

Furthermore, when sectoral standards are developed, we encourage EFRAG to keep in mind the requirement for benchmark administrators to disclose the percentage of underlying funds with stewardship policies in place, including measures for the planning and management of resources. This point is not covered by the first set of the ESRS, and rightly

so as it only pertains to fund managers. EFRAG could therefore consider covering this in the sectoral standard for fund managers / financial institutions.

*Taxonomy Regulation (TR)*

ESMA has not identified substantial inconsistencies between the ESRS and the TR nor between the ESRS and Commission Delegated Regulation (EU) 2021/2178.

**Q5: are there any other European policies and legislation you would suggest should be considered more fully?**

ESMA observes that ESRS 1 includes an extensive Appendix C on sustainability due diligence. ESMA recommends removing this appendix that quite clearly provides conduct requirements which go beyond the scope of the CSRD, also taking into account the ongoing development of the Corporate Sustainability Due Diligence Directive (CSDDD). In addition, it would be helpful to align the definition of 'value chain', including for what concerns the definition of 'Business relationships', with that under discussion as part of the negotiations on the CSDDD. The agreed CSRD text already provides that the due diligence process implemented by the undertaking should be in line with EU requirements on undertakings to conduct a due diligence process, i.e., those set out in the CSDDD. As a side remark, it should also be noted that the scope of application of the CSRD and CSDDD proposal are different, with the proposed CSDDD's scope being narrower, and that seems to further justify gradual phasing in of at least certain proposed ESRS on due diligence for smaller companies subject to CSRD.

Furthermore, ESMA notes that ESRS 2 helpfully refers to Art. 9(a) and (b) of the Shareholder Rights Directive II (SRD II). To complement this reference, ESMA suggests adding a reference to the forthcoming Commission Guidelines on the remuneration report, as publication of the Guidelines is foreseen for H2 2022. In addition, in order to clarify the concept of 'administrative, management and supervisory bodies', it would be helpful to use, or make reference to, the definition of 'director' in SRD II, which also includes the CEO (and deputy CEO, if existent), when these are not members of the administrative, management or supervisory bodies, and provides member states with the possibility to include other persons performing similar functions.

Finally, it should be clarified how the due diligence disclosure requirements established by ESRS 1 chapter 2.5 and ESRS 2, Disclosure Requirement 2-GOV 5 should be read together.

***Sustainability statements and the links with other parts of corporate reporting***

**Q9: would you recommend any other option(s)?**

Art. 19a(1), second subpar. and Art. 29a(1), second subpar. of the CSRD state that 'This [sustainability] information should be clearly identifiable within the management report, through a dedicated section of the management report'. Within the confines of this boundary, ESMA considers that EFRAG should allow for cross-referencing to other parts of the annual financial report, including but not limited to the management report (as covered in more detail

under question 11). ESMA thinks that such cross-references should be permitted to the extent they do not undermine the understandability of the sustainability reporting.

**Q11: in your opinion, to what extent does the incorporation of information in the Sustainability section by reference to other parts of the management report support cohesiveness throughout corporate reporting?**

*Considerations related to corporate governance*

ESRS 2 establishes disclosure requirements on the corporate governance of sustainability matters that are at the same time very wide-ranging and very detailed. These requirements correspond to the great part of the disclosures currently provided in the context of corporate governance and remuneration reports based on national law, corporate governance codes and the provisions under Art. 20 of the Accounting Directive. For the benefit of those undertakings that fall under both some / all of these provisions and the ESRS, ESMA encourages EFRAG to pursue alignment of the reporting requirements.

In this regard, the fact that incorporation by reference is limited to information in the management report may create duplication issues:

- the corporate governance report might sit outside the management report, as allowed by Art. 20 of the Accounting Directive, in which case the current draft ESRS would not permit incorporation by reference of the corporate governance report into the sustainability report.
- the remuneration report is a separate report and could therefore also not be incorporated into the sustainability report by reference.

To address this problem, incorporating information from those reports by reference should be explicitly allowed. Notably, it should be taken in consideration that information regarding administrative, management and supervisory bodies and their remuneration are at the core of the corporate governance report and remuneration report, respectively, and it would therefore be most suitable to reference the information in those reports to meet the ESRS' disclosure requirements on these topics.

*General considerations*

More generally, we believe there is a lack of clarity in the rules surrounding incorporation by reference into the sustainability report of information in other reports which already cover sustainability matters. For example, it is unclear what is meant in par. 131-132 when referring to the fact that an undertaking shall adopt presentation practices that promote cohesiveness between its sustainability report with other forms of reporting.

In particular, it would be important to allow for cross-referencing to information presented outside the management report, for example when it comes to certain regulatory information required for banks in relation to ESG risks.

In this respect, ESMA believes that the ESRS should use incorporation by reference to reduce duplications across undertakings' annual financial reports and to help build



connectivity with any other relevant information that is made available under the same terms, made subject to the same assurance regime and timing as the sustainability reporting.

More concretely, ESMA believes the ESRS should build on the experience of financial reporting whereby the relevant standards (e.g., IFRS) in selected cases allow the incorporation by reference into the financial statements of certain information that is placed elsewhere (a notable example of this are the financial risk disclosures required by IFRS 7 which would typically sit in an undertaking's management report). What is important is that the understandability of the sustainability reporting is not impaired when certain information is provided through the incorporation-by-reference mechanism.

While ESMA is strongly supportive of facilitating incorporation by reference as explained in the previous paragraphs, should cross-referencing not be possible, it should be considered whether certain requirements that duplicate information already available outside the sustainability report should be deleted from the ESRS.

Lastly, it would be important to ensure that any possibilities of cross-referencing do not impair the digital consumption of the sustainability reporting and the cross-referred information.

**Q12: in your opinion, to what extent do the requirements and provisions on how to include monetary amounts and other financial statement-related quantitative data into sustainability reporting support connectivity with the financial statements?**

Regarding cross-referencing to the financial statements, this seems to be allowed on the basis of par. 137-143 of ESRS 1, but it would be important to also amend par. 135 accordingly.

We also suggest explicitly allowing cross-referencing not only to *quantitative*, but also to *qualitative*, information in the financial statements.

In relation to the connectivity with financial statements, we recommend *requiring* (rather than merely *allowing*, as in par. 139), a reconciliation between the amounts presented in the sustainability report and those referred to in the financial statements.

Finally, ESMA also suggests including in the basis for conclusions of ESRS 1 a reference to the fact that it may be important that also the financial statements include references to information in the sustainability reporting, as appropriate and compatible with the relevant reporting standards.

We recommend performing a consistency check of how the topic of connectivity with the financial statements is addressed across the topical standards and how this relates to ESRS 1, par. 137-143. Currently, different approaches are taken at various places in the topical standards: sometimes, only the body of the standard reminds undertakings to relate / reconcile monetary amounts with the financial statement (e.g., E1-4, par. 30(b)), sometimes only the application guidance makes this point (e.g., E3-5, par. AG 33), sometimes it is mentioned in both the body of the standard and the application guidance (e.g., S1-9, par. AG 110). It would be helpful to always take the same approach, potentially referring back to par. 137-143 of ESRS 1. (In addition to this remark, in some cases we suggest specifying

that the 'most relevant line item' in the financial statements will be the revenue item in the income statement; we have inserted this point in our response to a few of the topical standards.)

## 1B. Overall ESRS Exposure Drafts relevance – Implementation of CSRD principles

### *Double materiality*

**Q18: in your opinion, to what extent does the definition of double materiality (as per ESRS 1 paragraph 46) foster the identification of sustainability information that would meet the needs of all stakeholders?**

ESMA has a number of comments about the approach to materiality in the ESRS which relate to parts of ESRS 1 that are not explicitly addressed in the consultation questions. ESMA has included these comments in the responses to Q18 and Q19, the first questions in the survey that address materiality.

In line with the CSRD, ESRS 1 complements the distinction between impact materiality and financial materiality with examples of disclosure requirements that would fulfil one or another. ESMA encourages EFRAG to clarify the interplay between those two notions and the process for identifying material impacts, e.g., by reference to the extensive guidance of GRI standard no. 3 *Material Topics*. ESMA also notes that, while it is important to have clarity on the differences between these two perspectives, it is important to emphasise the examples in which an entity's impacts may result in risks (or opportunities) for the same entity. This is an important aspect of corporate risk management systems which should consider in an integrated way sustainability-related risks and opportunities and impacts and ESMA believes it should be further emphasised in the ESRS.

ESRS 1, par. 43 refers to the 'European public good' as one of the drivers for identifying material information. This notion is unclear and open to wide interpretation, and it does not refer to any specific aspect of the CSRD. Furthermore, this notion is not conducive to consistent application and reflects a very region-specific approach to disclosures which contrasts with the fact that issuers operate beyond European boundaries and should, for example, consider their impacts on local communities irrespective of where these are located.

ESRS 1, par. 44-45 refer to a broad range of stakeholders and it is difficult to understand which stakeholders should be the reference point for the identification of material information under the two materiality lenses. As part of these stakeholders, it would also be important to consider the inclusion of governments since some of the disclosures will be important to monitor the progress of the corporate sector and of financial institutions towards public policy objectives. ESMA further notes that according to ESRS 1, the category of 'affected stakeholders' is not clear in how it differs from the other category of 'users'. We highlight that the definition of affected stakeholders is very broad since it refers to every individual who can have an interest in the undertaking. ESMA suggests considering the GRI definition of stakeholder (GRI 101) according to which stakeholders include entities or individuals whose rights under law or international conventions provide them with legitimate claims vis-à-vis the organisation.

In addition, ESMA observes that other EFRAG standards (e.g., ESRS 2 and precisely with reference to the process of identifying material topics) introduce additional specifications of

the stakeholder notion, such as 'relevant stakeholder', 'key stakeholder', 'key relevant stakeholder'. ESMA suggests retaining only one of these, for example 'relevant stakeholder'.

**Q19: to what extent do you think that the proposed implementation of double materiality (as per ESRS 2-IRO 1, paragraph 74b(iii) and AG 61) is practically feasible?**

In par. 47 of ESRS 1, it is not clear what it is meant by '*beyond considering the actual and potential financial consequences of its material impacts, the undertaking shall consider how it is affected by sustainability matters which are external to its activities*'. ESMA suggests deleting par. 47 which does not seem to add much compared to the two sets of paragraphs on impact and financial materiality, respectively.

According to ESRS 1, par. 48 the terms 'significant' and 'material' have the same meaning when referring to impacts, risks and opportunities in the ESRS. However, the term 'significance' is then used as part of the identification of material impacts in par. 51. For consistency and clarity purposes, we suggest always using the term 'material'.

We would recommend specifying that materiality is an aspect of relevance. Once linked to the notion of relevance, it may be unnecessary to retain the text in par. 43 of ESRS 1.

The topical standards sometimes oblige undertakings to provide information 'where relevant' / 'as relevant' / 'to the extent relevant'. We note that the materiality assessment applies to all parts of the ESRS, as established by ESRS 1, par. 42. We therefore question whether it is necessary to include 'where relevant' and similar wording in individual disclosure requirements as this may create confusion and undermine the general obligation to always assess materiality. We recommend EFRAG to carefully consider the use of expressions such as "Where applicable" or "Where relevant" to make sure it is clear in which cases certain requirements may not be applicable or relevant for a certain undertaking and to ensure that no confusion exist with the materiality assessment. For example, if such expressions are meant to target cases where certain disclosure requirements cannot be fulfilled due to legal restrictions at national level, this may need to be clarified in the cross-cutting requirements.

Finally, ESMA also recommends providing application guidance on the double materiality concept. We note, for example, that EFRAG's *Conceptual framework for non-financial information standard-setting* contains useful explanations in par. 47-49, including a helpful visual illustration. Additionally, the European Commission *Guidelines on reporting of climate-related information* contain a useful illustration on page 7, even if this specifically relates to climate. EFRAG could consider incorporating these explanations / illustrations in the application guidance relating to ESRS 1, for example around par. AG 60.

***Impact materiality:***

**Q21: to what extent do you think that the determination and implementation of impact materiality (as proposed by ESRS 1 paragraph 51) is practically feasible?**

To help undertakings carry out the task of assessing impact materiality, and as previously mentioned in question 18, we believe it would be important to set out a clear process for identifying material impacts and for how the identified impacts should then be captured under the lens of financial materiality. On these points, it would be important for EFRAG to work closely with GRI and the ISSB to agree on a common approach.

***Financial materiality:***

**Q22: in your opinion, to what extent is the definition of financial materiality (as per ESRS 1 paragraph 53) aligned with that of international standards?**

ESMA suggests better aligning the notion of financial materiality to that of enterprise value creation and to make all possible cooperation efforts to reach a converged position with the ISSB.

We note that it would be important to ensure that material information can include information about sustainability-related risks and opportunities with low-probability and high-impact outcomes, as well as high-probability events with low-impact outcomes, where the low level of impact results from mitigation measures put in place.

***(Materiality) Rebuttable presumption***

**Q24: to what extent do you think that the (materiality) rebuttable presumption and its proposed implementation will support relevant, accurate and efficient documentation of the results of the materiality assessment?**

ESMA does not support the proposed rebuttable presumption. ESRS 1 explains that while all mandatory disclosure requirements in the ESRS shall be presumed material, this presumption is rebuttable if undertakings have reasonable and supportable evidence. When undertakings decide to rebut this presumption and avoid providing certain disclosures, they shall produce ad hoc explanations. The basis for conclusions further explains that this approach was considered 'necessary and appropriate to manage the amount of mandatory disclosure requirements under ESRS'. There are four main issues that make this requirement problematic.

Firstly, this presumption may be conducive to a checklist approach since ESRS 1 refers to materiality *of the disclosure requirements* and not to materiality *of the information*. This focus on material disclosure requirements risks translating into an approach whereby undertakings have to look at the list of ESRS requirements and consider which of these can be avoided by producing supporting documentation necessary to justify that choice. This approach is the opposite of a proper materiality assessment, i.e., starting from the identification of relevant events/transactions and assessing the materiality of the information that would result from the reflection of these events/transactions through the application of the disclosure requirements.

Secondly, providing a structured non-disclosure route through the rebuttable presumption may incentivise undertakings to perceive the ESRS as a menu of disclosure requirements they can choose from through a type of comply or explain mechanism. This would be contrary to the spirit and letter of the CSRD. ESMA underlines that it is very important to oblige undertakings to only disclose information that is material for investors and other stakeholders. However, in financial reporting this is done via a simple requirement not to disclose immaterial information. The proposed rebuttable presumption departs from this principle and places more emphasis on the possibility for undertakings to decide not to disclose certain information.

Thirdly, the rebuttable presumption is introduced 'to manage the amount of mandatory disclosure requirements', i.e., to ensure proportionality. This risks creating confusion between the materiality assessment and cost-benefit considerations which may ultimately reduce the quality of sustainability reporting. Here as well the experience of financial reporting standards may be useful, as in this domain materiality considerations never have reduction of the reporting burden as their primary objective. Furthermore, this requirement may even be counterproductive and further complicate the disclosure overload problem as some undertakings may have an incentive to disclose immaterial information to avoid developing more burdensome supporting documentation to justify the non-disclosure of that information. Alternatively, undertakings may decide to provide the explanation for why a certain piece of information is immaterial, however, such explanations will themselves constitute immaterial information and contribute to the disclosure overload problem.

Lastly, ESRS 1 seems to make the rebuttable presumption dependent upon not only the materiality assessment but also other unspecified facts and circumstances. The standard indicates that '*all mandatory disclosure requirements established by ESRS shall be presumed to be material*' but '*to consider the undertaking's facts and circumstances and the outcome of its assessment process, such a presumption is rebuttable based on reasonable and supportable evidence*'. It thus seems the presumption can be rebutted on grounds that go beyond the materiality assessment based on factors that are not specified. For example, undertakings might try to rebut the presumption based on facts/circumstances related to costs.

ESMA notes that the basis for conclusions of ESRS 1 (par. 58) indicates that the rebuttable presumption pursues the objective of enabling comparability. ESMA does not believe that this is the case since par. 62 of ESRS 1 sets out an exemption from the rebuttable presumption which would undermine such objective.

ESMA would therefore recommend that EFRAG (a) removes the rebuttable presumption and avoids requiring explanations for why certain disclosures were deemed immaterial since such explanations would by extension constitute immaterial information which would further contribute to the disclosure overload problem, (b) emphasises the importance of the materiality assessment to ensure that only material information is reported, (c) clarifies that the materiality assessment is not intended to pursue proportionality purposes and (d) pursues proportionality via other means, such as allowing for the gradual phasing-in of certain requirements, reducing the complexity of the requirements themselves and deferring some disclosure requirements to the later development of industry-specific standards.

### **Reporting boundary and value chain**

**Q28: in your opinion, to what extent would approximation of information on the value chain that cannot (practically) be collected contribute to the reporting of understandable, relevant, verifiable, comparable, and faithfully represented sustainability information?**

ESMA notes that the definition of reporting boundary aims at capturing activities across an undertaking's entire value chain which is consistent with the CSRD. The extension of the reporting requirements to entities in the value chain that are not subject to the CSRD, including those in non-EU countries, may be problematic. At the same time, for other areas of sustainable finance (SF) legislation, such as the TR, the need to look across the value chain is a key feature to ensure that ESG impacts, risks and opportunities are properly assessed and disclosed. The CSRD envisages a 3-year period during which it is envisaged that the necessary information regarding the value chain may not all be available and foresees specific disclosures to address these situations. The ESRS should reflect this requirement in its phase-in approach. In ESMA's view, this requirement also implies that after the initial period, the value chain information is expected to be provided which the ESRS should reflect.

The CSRD also indicates that the ESRS '*shall specify disclosures on value chains that are proportionate and relevant to the scale and complexity of the activities, and the capacities and characteristics of undertakings in value chains*' especially those undertakings that are not subject to CSRD. EFRAG will need to take account in the standard-setting process of these new specifications, in particular regarding the scale and complexity of the activities and type of entities in the value chain.

The CSRD does not explicitly foresee that value chain information may be based on estimates or approximations. We note that in other SF legislation, the use of estimates and 'equivalent' information varies (e.g., SFDR reporting vs. Taxonomy-related reporting) but with a tendency to allow for a limited and careful use of estimates (e.g., in TR Art. 8). We therefore recommend extra care in foreseeing in the ESRS that gathering necessary information may be impracticable and that '*the undertakings should seek to approximate the missing information [...], by using all reasonable and supportable information, including internal and external information, such as peer groups or sector data*'. We suggest that approximations should be limited to cases explicitly mentioned in the CSRD as requiring special attention, such as SMEs, non-CSRD entities and undertakings in emerging economies/markets that may not be subject to sustainability disclosure requirements. Conditions on the quality of such estimates and approximations should also be included in terms of their relevance, reliability, comparability and timeliness.

A way to combine the need for transparency and reliable information with proportionality would be to disclose the level of quality of the information which the undertaking has used to prepare its disclosure, distinguished into homogenous groups of value chain counterparties according to their geographical location and size. The groups could be the following:

- EU counterparties required to report under the CSRD

- EU counterparties not required to report under the CSRD
- Non-EU counterparties that are SMEs and/or based in emerging economies/markets
- Other non-EU counterparties

Any 'approximation' clause should generally apply to EU counterparties that are not required to report under the CSRD and to non-EU counterparties that are SMEs and/or based in emerging economies/markets, as well as to non-EU counterparties that are subject to less stringent sustainability disclosure requirements. To ensure that only relevant estimates and approximations are used and that they reflect the topic at hand, such a clause should be tailored to the parts of the standards to which it is relevant (and complement a generic 'catch-all' clause in the cross-cutting standards). Undertakings should explain their use of approximations, not only the type as already proposed in par. 68 of ESRS 1, but also their attempts to retrieve the necessary data, the impediments encountered and a statement that their administrative board signed off on the approximations used. The application guidance should provide examples of estimation methodologies starting, e.g., from industry-level information.

The meaning and role of 'operational influence' should be clarified. It seems obvious that operational influence will have an impact on an undertaking's ability to obtain data, but the basis for conclusions of ESRS 1 (par. BC72) indicates the contrary. ESMA also recommends defining the notion of upstream entities.

Users should be able to understand how the reporting boundary for sustainability reporting compares with that for financial reporting for example to identify sustainability-related risks and opportunities that may arise from value chain activities and which may have an impact on future financial statements.

In developing the final approach to reporting boundaries in the ESRS, we encourage EFRAG to engage in discussions with the ISSB to seek a converged approach.

### ***Time horizon***

#### **Q33: if you disagree with the proposed time horizons, what other suggestion would you make? And why?**

Across the standards, the definition of short, medium and long term is not fully clear. ESRS 1, par. 83 provides a clear definition, but this is not used consistently across all other standards. Instead, other standards mention that the undertaking should itself define these terms and then disclose how it defined them (for example, ESRS E2, par. 52). We suggest looking at the approach to short, medium and long term across the entire set of standards and ensuring consistency.

In general, we would suggest taking a more principles-based approach to the definition of time horizons to account for the specificities of different sectors and product lifecycles. In this respect, it is not clear whether ESRS 1, par. 84 (which hints at some tailoring of time horizons) takes precedence or should be read in conjunction with par. 83 (which instead mandates strict time bands).



ESMA suggests that EFRAG work with the ISSB to get to a common understanding of time horizons and their possible definition. The draft IFRS S1 proposes a principles-based approach that EFRAG may want to consider. In relation to this, we do not believe that the statement in the basis for conclusions of ESRS 1 that there is consistency between the approach to time horizons of EFRAG and ISSB is accurate.

***Disclosure principles for implementation of Policies, targets, action and action plans, and resources***

**Q34: in your opinion, to what extent will DP 1-1 contribute to the reporting of understandable, relevant, verifiable, comparable and faithfully represented information on sustainability related policies?**

Please see our comments under Q1 in relation to the use of disclosure principles in general. In relation to ESRS 1-1, ESMA suggests also requiring disclosures on the extent to which available resources are sufficient to pursue the policies, objectives / targets, etc. A link with ESRS 1-3 on resources needed to fulfil the policies could be made.

We also note that par. 98 on policies adopted to manage material sustainability matters addresses the case in which entities 'cannot' disclose policies and, in this case, indicates that explanations shall be provided. If this is a general requirement, it should be reflected more clearly in the topical standards. However, we question whether such a requirement will promote good reporting practices. If information on policies in a certain sustainability area is material, this information should be disclosed. If this is not disclosed because of lack of materiality, there is no need to further explain that fact. On the contrary, if a policy is material but information about it is missing, undertakings should simply make sure they provide this information. ESMA would suggest not giving the impression that undertakings may choose whether to adopt policies with respect to sustainability matters which are considered material.

## **1C. Overall ESRS Exposure Drafts relevance – Exposure Drafts content**

### ***ESRS 1 – General Principles***

**Q38: in your opinion, to what extent can ESRS 1 – General principles foster alignment with international sustainability reporting standards (in particular IFRS Sustainability Reporting S1 Exposure draft)?**

ESMA's main observations in relation to ESRS 1 are reflected in sections 1A and 1B of the questionnaire.

### ***ESRS 2 – General, strategy, governance and materiality assessment***

**Q39: Please, rate to what extent do you think ESRS 2 – General, strategy, governance and materiality assessment:**

- A. Covers sustainability information required by articles 19a and 19b of the CSRD proposal (see Appendix II for CSRD detailed requirements)**
- B. Supports the production of relevant information about the sustainability matter covered**
- C. Fosters comparability across sectors**
- D. Covers information necessary for a faithful representation from an impact perspective**
- E. Covers information necessary for a faithful representation from a financial perspective**
- F. Prescribes information that can be verified / assured**
- G. Meets the other objectives of the CSRD in term of quality of information**
- H. Reaches a reasonable cost / benefit balance**
- I. Is sufficiently consistent with relevant EU policies and other EU legislation**
- J. Is as aligned as possible to international sustainability standards given the CSRD requirements**

ESMA's observations on the interplay between the cross-cutting standards and the topical standards are presented in section 1A of the questionnaire.

In relation to ESRS 2, we have a number of observations on terminology:

- Value creation: this concept should be defined, and it should be clarified how and to what extent it takes into account the double materiality perspective since in some disclosure requirements (in GR4) it seems to purely relate to the financial materiality perspective, whereas ESRS 2, par. AG 17 extends the notion of 'value creation' to 'non-financial benefits' for other stakeholders. We also highlight that DR2-GR4

makes reference to the 'overall performance of the value chain' which is a notion that requires explanation.

- The ESRS' concept of financial materiality should be as aligned as possible with the ISSB's concept of enterprise value creation to facilitate the task of undertakings who will prepare reporting under both frameworks. If any differences remain, they should be clearly stated to avoid confusion.
- As mentioned earlier in our response, the notion of 'key drivers' of value creation should be defined, it should be explained how it differs from 'key resources' and it should be complemented with examples.
- The standard refers to 'governance bodies' in the disclosure requirements, but Appendix A only defines a particular type of these bodies, i.e., the 'administrative, management and supervisory body'. We recommend using this notion to replace the term 'governance bodies' throughout the standards and to define 'administrative, management and supervisory body' by making reference to the wider definition of 'director' that is provided for by SRD II. Helpfully, this definition i) includes also the CEO and deputy CEO, if applicable, when these are not members of an undertaking's administrative, management or supervisory bodies and ii) provides member states with the possibility to include other persons performing similar functions.

ESMA also notes that ESRS 2 contains several disclosure requirements on governance that appear to go beyond simple transparency and veer into behavioural requirements. For example, an undertaking might not be obliged to apply a specific governance code, and the disclosure requirements should therefore focus on what undertakings are currently doing without suggesting that application of a governance code is mandatory. Another example, though this time in ESRS 1, relates to Appendix C of ESRS 1 on 'sustainability due diligence', whose nature is unclear as it seems to set out definitions and conduct requirements of a binding nature. While disclosure requirements may be a way to encourage certain behaviours and discourage others, certain requirements may create the risk of changing corporate governance legislation through the back door and, in general, it is ESMA's view that disclosure obligations should prioritise improving transparency rather than addressing conduct issues for which other more targeted measures exist.

In addition, as set out in the section concerning G1, we believe the interaction between this part of the standards and ESRS G1 could benefit from clarification. Some of the requirements overlap and the alleged distinction between sustainable corporate governance and more general corporate governance does not seem to fully justify the split into two standards. In ESMA's view, it would be more beneficial to have the two addressed together, with sustainable corporate governance being a sub-topic of general corporate governance disclosures.

## **ESRS E1 – Climate change**

**Q40: Please, rate to what extent do you think ESRS E1 – Climate change:**

- A. Covers sustainability information required by articles 19a and 19b of the CSRD proposal (see Appendix II for CSRD detailed requirements)**
- B. Supports the production of relevant information against the intended objective of the sustainability matter covered**
- C. Fosters comparability across sectors**
- D. Covers information necessary for a faithful representation from an impact perspective**
- E. Covers information necessary for a faithful representation from a financial perspective**
- F. Prescribes information that can be verified and assured**
- G. Meets the other objectives of the CSRD in term of quality of information**
- H. Reaches a reasonable cost / benefit balance**
- I. Is sufficiently consistent with relevant EU policies and other EU legislation**
- J. Is as aligned as possible to international sustainability standards given the CSRD requirements**

Par. 4 states that beyond the GHGs covered by E1, other impacts on climate change should be part of an undertaking's assessment of its material impacts. We support this approach. Par. 4 mentions land use change, we suggest inserting a reference to E4 so undertakings use the disclosure requirements established therein for this topic.

E1-3, par. 24(c) permits undertakings to disclose their GHG emissions reduction targets separately for Scope 1, 2 and 3 or combined. We believe separate disclosure of the three scopes gives a clearer impression of an undertaking's objectives which seems consistent with what is already described in par. AG 28(b).

It would be useful to add clarifications/examples on how to apply the disclosure requirements, notably for disclosures which are currently provided by few companies/in few sectors or for which there are no internationally recognised standards (e.g., Scope 3, GHG removals, carbon credits). It would also be useful to add further references to frameworks or international initiatives which undertakings may use, e.g., to demonstrate their business model's alignment with the Paris Agreement, for the definition of targets, for the calculation of their energy consumption, for scenario analysis or for calculating the financial effects of transition/physical risks.

We support the fact that undertakings may not count GHG removals, carbon credits or avoided emissions in their emission reduction targets (par. 24(c)). Requiring undertakings to disclose their 'gross' emission reduction targets gives users clear information about undertakings' ambitions for future emissions and acknowledges that removals, carbon credits and avoided emissions cannot be considered equal to actual emission reductions in an undertaking's own value chain. E1 instead foresees that removals may be used when an undertaking discloses a net zero target, that carbon credits may be used when an

undertaking discloses GHG neutrality claims and that avoided emissions may be disclosed under E1-14. ESMA supports this distinction and suggests further clarifying the difference between ‘emission reduction targets’, ‘net zero target’ and ‘GHG neutrality claims’.

We suggest clarifying the use of reporting boundaries and exclusions vis-à-vis ESRS 1, par. 63-66, notably for E1-5 and E1-7 to E1-10. E.g., E1-5, par. AG 36(a) specifies that energy consumption information should be provided with reference to energy consumed by processes owned or controlled by the undertaking but applying the same boundary as for Scope 1 and 2 emissions reporting. However, par. AG 43(b) specifies that the undertaking must consistently apply the reporting boundaries in ESRS 1, specifying and explaining any exclusions. ESRS 1, however, refers to a boundary that includes the upstream and downstream value chain. As a result, the reporting boundary of E1-5 is ultimately unclear.

We suggest adding definitions of ‘dependencies’ and ‘operating lifetime’. Additionally, in E1-7 to E1-10, if ‘operating segments’ in par. AG 53 is to be defined as the segment reporting in the financial statements according to IFRS 8, we would recommend mentioning this, as is done in par. AG 73 (alternatively, both paragraphs could require that operating segments be defined the same way as in the undertaking’s accounting framework). In E1-15, it should be clarified if ‘assets’ are limited to tangible assets.

ESMA welcomes the fact that there appears to be good alignment between the parts of E1’s objectives that relate to financial materiality and the objective of IFRS S2. Both objectives require that undertakings disclose information that gives an understanding of the climate-related risks and opportunities that could affect their enterprise value, that shows how they manage those risks/opportunities and that explains their ability to adapt to them (though E1 also focuses on contributing to limiting global warming due to its double materiality lens).

While both E1 and IFRS S2 require undertakings to report their gross GHG emissions, the standards have different approaches to GHG emissions *targets*: while E1 does not permit undertakings to count offsets in their targets, IFRS S2 does. The gross targets disclosed under E1 may appear less ambitious than the netted targets under IFRS S2 which could be confusing and give an artificially negative impression of undertakings’ targets under E1 compared to under IFRS S2. We have encouraged the ISSB to seek alignment with EFRAG in this regard.

We note that there is a difference in the terminology on offsets (EFRAG uses ‘carbon credits’ while the ISSB uses ‘carbon offsets’). We support EFRAG’s terminology and have suggested to the ISSB that they generally align their terminology with EFRAG. In the climate-related application guidance on the materiality assessment, we suggest having a reference to a 1.5°C climate scenario not only for risks and opportunities but also for impacts which could be added in par. AG 14(a) and AG 15.

## **ESRS E2 – Pollution**

**Q41: Please, rate to what extent do you think ESRS E2 – Pollution:**

**A. Covers sustainability information required by articles 19a and 19b of the CSRD proposal (see Appendix II for CSRD detailed requirements)**

**B. Supports the production of relevant information about the sustainability matter**

covered

**C. Fosters comparability across sectors**

**D. Covers information necessary for a faithful representation from an impact perspective**

**E. Covers information necessary for a faithful representation from a financial perspective**

**F. Prescribes information that can be verified and assured**

**G. Meets the other objectives of the CSRD in term of quality of information**

**H. Reaches a reasonable cost / benefit balance**

**I. Is sufficiently consistent with relevant EU policies and other EU legislation**

**J. Is as aligned as possible to international sustainability standards given the CSRD requirements**

In ESRS E2-4, par. 36(a) requires undertakings to disclose, for the pollutants to air, water or soil, the total amount of emissions 'in a defined period'. We suggest making this requirement more precise by indicating the time-period for which the information should be disclosed – from the table in the application guidance (under par. AG 22), we presume that the information should be disclosed for the reporting year.

Still in E2-4, par. AG 13 requires undertakings to refer to information that they are required to report under other legislation, if relevant. Given that the ESRS do not permit incorporation by reference of information outside the management report, the meaning of this requirement is not fully clear. We suggest aligning this with whichever approach the final ESRS take to incorporation by reference (please note that we have provided our comments on incorporation by reference under question 11.)

We have a number of comments in relation to E2-5:

- There appears to be an inconsistency in the wording between E2-5 and E2-2. E2-2, par. 26(d)(ii) and 26(e)(ii) require undertakings to report their targets for generation and use of substances of concern and most harmful substances by disclosing the amount of 'absolute turnover' and 'share of total turnover' of the undertaking realised with products and services that are or that contain substances of concern / most harmful substances. E2-5, par. 41(b) – which sets out the performance indicator corresponding to this target – requires undertakings to report their generation and use of substances of concern and most harmful substances by disclosing the amount of 'net turnover' and 'share of total net turnover' of the undertaking made with products and services that are or that contain substances of concern / most harmful substances. We believe the denominations of the indicators in par. 26 and 41 should be aligned, so the target and the performance indicator are consistent. Furthermore, the application guidance related to E2-5 (see table under par. AG 23, third column from the left) uses a third formulation - 'absolute net turnover' – instead of 'net turnover' as in par. 41(b) and this should also be aligned with the wording that is chosen for par. 26 and 41.

- Par. 41(b) and (c) of E2-5 require an undertaking to disclose the amounts of 'net turnover' and 'absolute raw material cost' regarding substances of concern and most harmful substances which are generated, used or procured and leave the undertaking's facilities. We suggest that undertakings should be required to reconcile those indicators to the most relevant amounts presented in the financial statements, similarly to the requirement in ESRS E5, par. AG 36. For 'net turnover', it could specifically be required to reconcile with the revenue item in the income statement.
- The application guidance contains a table which undertakings are obliged to use for their disclosure (table under par. AG 23). The table requires three comparative figures (two of which are called 'Reporting comparative' and one which is called 'Comparative'). It is not fully clear what each of these three comparative figures should refer to, as there are only two performance indicators in the table.

In relation to ESRS E2-6, par. 49 requires undertakings to disclose their provisions for environmental protection and remediation, if not already disclosed in the financial statements. We believe it should be clarified that entities must disclose quantitative information (as specified in par. AG 25) and also qualitative information (i.e., the nature) about the provisions for environmental protection and remediation recognised in their financial statements. Additionally, it would be useful to further clarify the difference in scope between E2-6 and E2-7, for example by adding application guidance for E2-7. Furthermore, as par. 48 requires undertakings to disclose their operational and capital expenditures regarding pollution-related incidents and deposits, we suggest clarifying that these measures should be used in a way that is consistent with their use under Commission Delegated Regulation (EU) 2021/2178, for example by inserting wording similar to that in ESRS E1, par. AG 35. Lastly, par. AG 7 states that the undertaking 'shall' describe how it has applied Commission Recommendation (EU) 2021/2279. As a drafting matter, since the Commission Recommendation is non-binding, we would suggest adjusting the wording by changing 'how' for 'if and in this case how'.

### ***ESRS E3 – Water and marine resources***

**Q42: Please, rate to what extent do you think ESRS E3 – Water and marine resources:**

- A. Covers sustainability information required by articles 19a and 19b of the CSRD proposal (see Appendix II for CSRD detailed requirements)**
- B. Supports the production of relevant information about the sustainability matter covered**
- C. Fosters comparability across sectors**
- D. Covers information necessary for a faithful representation from an impact perspective**
- E. Covers information necessary for a faithful representation from a financial perspective**
- F. Prescribes information that can be verified and assured**
- G. Meets the other objectives of the CSRD in term of quality of information**

## **H. Reaches a reasonable cost / benefit balance**

### **I. Is sufficiently consistent with relevant EU policies and other EU legislation**

### **J. Is as aligned as possible to international sustainability standards given the CSRD requirements**

The water and marine resources-related application guidance on the materiality assessment states that undertakings should provide the assumptions they have used for their assessment of their material impacts, risks and opportunities related to water and marine resources (par. AG 13(a)). We suggest adding that undertakings should disclose some information regarding what these assumptions were based on.

E3-1, par. 14(b) requires undertakings to disclose how their policies for material water and marine resources-related impacts, risks and opportunities relate to EU and international reference frameworks. It is specified that those international reference frameworks should be third party standards of conduct. While disclosure on the use of such international standards of conduct may be useful, as a securities regulator we wish to highlight that it will be difficult for national competent authorities to enforce this disclosure requirement due to such standards not sitting within the legislation in national competent authorities' remit.

We observe that E3 does not specifically require disclosure of targets or performance measures related to areas with high water stress. We recommend that EFRAG consider adding specific requirements relating to areas with high water stress in this or a next version of the standard and that such requirements be aligned with those of GRI 303.

We recommend that EFRAG consider increasing the consistency between the targets required under E3-2 and the performance measures required under E3-4. While E3-4 par. 29 requires undertakings to disclose performance measures on the water they have recycled / reused and stored, there is no corresponding target requirement in E3-2. Adding such a target would allow users to understand an undertaking's intentions for future amounts of recycled / reused / stored water and as such to put the performance measure in par. 29 into context. EFRAG could equally consider adding (optional) targets corresponding to the optional performance measures on water intensity performance in E3-5.

E3-4, par. AG 26, AG 27 and AG 28 use the term 'per segment'. We would recommend clarifying what is meant by segment, e.g., whether it corresponds to the segments that are disclosed in the operating segments note in the undertaking's financial statements.

The application guidance for E3-5 (par. AG 33) states that net turnover should be reconciled to the most relevant line item in the undertaking's financial statements. We believe the most relevant line item will be the revenue item in the income statement, and to enhance comparability across different undertakings' disclosure, we suggest specifying this in par. AG 33.

We observe that E3 has a strong focus on disclosure reflecting an impact materiality perspective whereas disclosure requirements reflecting a financial materiality perspective are scarcer. To strengthen the financial materiality perspective and as such ensure the standard provides for a faithful representation from both angles, EFRAG could consider including application guidance to further specify the disclosure required under E3-7.

Across the standard, there are references to 'material priority substances of concern' (par.



20(d), table under AG 30), 'material substances of concern' (par. 35(b)(vii)), 'priority substances of concern' (par. 28(d)), 'list of priority substances' (par. AG 18) and 'priority substances' (par. AG 24). We recommend aligning the terminology so the same wording is always used, and it would furthermore be useful to carry over the definition of substances of concern which is included in E2.

### ***ESRS E4 – Biodiversity and ecosystems***

**Q43: Please, rate to what extent do you think ESRS E4 – Biodiversity and ecosystems:**

**A. Covers sustainability information required by articles 19a and 19b of the CSRD proposal (see Appendix II for CSRD detailed requirements)**

**B. Supports the production of relevant information about the sustainability matter covered**

**C. Fosters comparability across sectors**

**D. Covers information necessary for a faithful representation from an impact perspective**

**E. Covers information necessary for a faithful representation from a financial perspective**

**F. Prescribes information that can be verified and assured**

**G. Meets the other objectives of the CSRD in term of quality of information**

**H. Reaches a reasonable cost / benefit balance**

**I. Is sufficiently consistent with relevant EU policies and other EU legislation**

**J. Is as aligned as possible to international sustainability standards given the CSRD requirements**

In the biodiversity and ecosystems-related specific application guidance on the materiality assessment, par. AG 19 requires undertakings to disclose a number of material risks, including in relation to 'contribution to systemic risk'. Under the sub-title 'contagion', par. AG 19(c)(iii) requires undertakings to disclose the risk that 'financial difficulties at one or more financial institutions linked to failure to account for exposure to biodiversity-related risks spill over to the financial system as a whole'. We understand that this disclosure relates to the risk that the undertaking fails to adequately assess and disclose its biodiversity-related risks and that, via the financial institutions that are exposed to the undertaking, this has a systemic impact on the financial system. We believe assessing this risk will be quite challenging for undertakings which may therefore lead to boiler plate disclosure. For the same reason, we consider that it will be challenging to provide assurance on this assessment and that it will be difficult for national competent authorities to enforce the disclosure. If the requirement is maintained, we observe that i) there could be systemic risk when the undertaking is independent of financial institutions which does not appear to be covered by the wording, and ii) EFRAG should consider why this disclosure requirement is particularly pertinent to the area of biodiversity and ecosystems and not to other areas where it does not appear to

be addressed in the same way.

In E4-2, par. 21(d) combined with par. 23(a) require undertakings to provide information on how their policies on biodiversity and ecosystems allow them to undertake biodiversity friendly production, consumption and sourcing of raw materials with or from third-party certification. The role of the third-party certification is not entirely clear, as the application guidance (par. AG 31 and AG 31(a)) states that undertakings 'may' refer to recognised third-party certifications. It would be helpful to elaborate on the status of these certifications by clarifying whether their use in the disclosure is mandatory or optional and by adding further explanation on what type of disclosure is expected (if such third-party certification schemes are overseen by a regulator, this may for example be relevant to disclose).

In E4-3, there are several references to 'raw material of concern' and we suggest defining when raw materials are 'of concern' to ensure consistency and as such comparability across undertakings' disclosures. Par. 33(d) again mentions third-party certification schemes, and we reiterate that it would be useful to provide further explanation on the disclosure that is required here, including whether such schemes are overseen by a regulator.

In E4-4, we would recommend defining what is meant by 'traditional knowledge and nature based-solutions'. For the latter, the glossary of IPBES' Global Assessment Report (Annex I) may provide a useful basis. For the definition of 'traditional knowledge' it may be useful to refer to the same glossary which may provide relevant examples linked to the notion of traditional knowledge (e.g., 'traditional farming'), as well as to the factsheet of the United Nations Convention on Biological Diversity and Regulation (EU) No 511/2014 for access and benefit-sharing.

In E4-9, we would recommend clarifying the wording of par. 64 and 65 of the disclosure requirement a bit further, as the meaning of 'the undertaking may disclose the actions...of biodiversity and ecosystem mitigation projects' and 'the undertaking may disclose the development of biodiversity and ecosystem mitigation projects' is not fully clear (what is meant with 'actions' and 'development'?). We also observe that par. AG 81 and AG 83 relate to behaviour (how the undertaking should go about designing its offsets) rather than disclosure. We suggest reconsidering the inclusion of these paragraphs or potentially rephrasing them to focus more on methodological / quality requirements for which types of offsets undertakings are permitted to include under this disclosure requirement.

It would be helpful to add application guidance for E4-10 to provide further clarifications, explanations and examples of what undertakings should disclose in relation to the potential financial effects of their biodiversity-related impacts, risks and opportunities (for example, that undertakings could disclose the costs of restoring their material impacts on biodiversity, a performance metric required under E4-7). This would add more disclosure from the financial materiality perspective and as such make the standard more balanced and contribute to a faithful representation from both materiality perspectives. EFRAG could also consider making the disclosure on the costs of financing biodiversity offsets in par. 66(b) mandatory rather than optional.

## ***ESRS E5 – Resource use and circular economy***

**Q44: Please, rate to what extent do you think ESRS E5 – Resource use and circular**

economy:

- A. Covers sustainability information required by articles 19a and 19b of the CSRD proposal (see Appendix II for CSRD detailed requirements)**
- B. Supports the production of relevant information about the sustainability matter covered**
- C. Fosters comparability across sectors**
- D. Covers information necessary for a faithful representation from an impact perspective**
- E. Covers information necessary for a faithful representation from a financial perspective**
- F. Prescribes information that can be verified and assured**
- G. Meets the other objectives of the CSRD in term of quality of information**
- H. Reaches a reasonable cost / benefit balance**
- I. Is sufficiently consistent with relevant EU policies and other EU legislation**
- J. Is as aligned as possible to international sustainability standards given the CSRD requirements**

We have a few observations in relation to E5-7 on resource use optimisation:

- Firstly, the current wording in par. AG 33 and AG 34 requires undertakings to explain 'the business model to strengthen value retention' and suggests that they consider various circular business models. It is not clear what undertakings should do if their business model does not strengthen value retention or align with a circular business model, and it would be useful to address that in the application guidance.
- Secondly, par. AG 33 states that undertakings shall consider the sector-specific standards and how the circular economy is addressed in those standards. Since the sector-specific standards will be issued at a later stage and may as such also become applicable only later, it would be helpful to include a clarification of how undertakings may comply with this requirement in the meantime.
- Lastly, par. AG 36 states that 'net turnover' should be reconciled to the most relevant line item in the undertaking's financial statements. We believe the most relevant line item will be the revenue item in the income statement, and to enhance comparability across different undertakings' disclosure, we suggest specifying this in par. AG 36.

As we have mentioned in relation to other of the environmental standards, it would be helpful to add application guidance for E5-9, so that undertakings' disclosure in relation to the potential financial effects from impacts, risks and opportunities related to resource use and circular economy becomes more consistent and as such comparable. Currently, the wording in par. 53-55 stands alone and the disclosure required in these paragraphs is quite general. The general nature of the requirements will furthermore be challenging for natural competent authorities to enforce as it will leave much room for interpretation on the side of undertakings.

Lastly, we have a few observations in relation to the definitions in the standard:

- The definition of ‘circular economy’ differs from that in Art. 2(9) of the TR, and we recommend aligning with that definition.
- In relation to interoperability with GRI, we note that Appendix A makes a number of references to GRI by mentioning that various terms are either ‘inspired by’ a given GRI standard or that a given GRI standard is the ‘source’ of that term. We are supportive of alignment with GRI and to facilitate the task of undertakings preparing their reporting, we think it would be useful if the final version of the standards would be accompanied by a mapping of how these terms compare to GRI.
- Across the standard, we encourage EFRAG to check that all key terms are defined or explained (for example, ‘reparability’, ‘upgradability’).

### **ESRS S1 – Own workforce**

**Q45: Please, rate to what extent do you think ESRS S1 – Own workforce:**

- A. Covers sustainability information required by articles 19a and 19b of the CSRD proposal (see Appendix II for CSRD detailed requirements)**
- B. Supports the production of relevant information about the sustainability matter covered**
- C. Fosters comparability across sectors**
- D. Covers information necessary for a faithful representation from an impact perspective**
- E. Covers information necessary for a faithful representation from a financial perspective**
- F. Prescribes information that can be verified and assured**
- G. Meets the other objectives of the CSRD in term of quality of information**
- H. Reaches a reasonable cost / benefit balance**
- I. Is sufficiently consistent with relevant EU policies and other EU legislation**
- J. Is as aligned as possible to international sustainability standards given the CSRD requirements**

On scope of application, ESMA observes that par. 6 explains what types of workers are covered by S1 and distinguishes whether the undertaking controls the work/workplace of certain workers. This distinction determines whether workers are in the scope of S1 or S2. The standard does not explain how to determine whether such control exists. We recommend adding guidance and refer in this respect to the explanations/examples in GRI 403.

Moreover, it appears that some disclosure requirements require information on all affected stakeholders and not only the undertaking’s own workers. This applies, e.g., to the requirements in par. 18(a) and (c), 87, AG 42(e), AG 49(b) and (d) and AG 50(g). ESMA recommends reconsidering the scope of these requirements.

We also recommend increasing the consistency of the terminology in S1, particularly the terms

'own workforce', 'employees' and 'non-employee workers'. Alongside these terms, which are defined in Appendix A, other terms such as 'workers' or 'own employees' are used, the exact meaning of which is not clear. Additionally, some KPIs are required for own workforce and others for employees only and it is not clear why there are such differences. In other cases, it is not specified to whom the requirements apply. In addition, numerous terms are used for remuneration: wage, salary, pay, compensation, hourly earnings. We consider that the number of used terms could be reduced or that the differences between these terms could be better explained.

ESMA notes that CSRD Art. 29b mentions the social factor 'diversity' in addition to gender equality and employment and inclusion of people of disabilities. We recommend adding explanations on the approaches taken by the undertaking to identify and manage any material actual and potential impacts on its own workforce in relation to other diversity aspects than those mentioned above (e.g., antiracism).

In S1-1, where a policy related to own workforce is publicly available, par. 17 permits undertakings to provide a link to it. We suggest adding a clarification that including the link does not imply that some disclosures required by S1-1 may be omitted. Moreover, par. AG 20 requires an undertaking to disclose the alignment of its policies with internationally recognised standards relevant to its own workers. Here, ESMA recommends referring to the UN Convention on Persons with Disabilities.

ESMA notes that it is not clear whether S1-3 covers establishment of a procedure for whistleblowers and considers it helpful to clarify this.

Information required in S1-7 appears very granular. In addition, the total number of headcount and its breakdown by significant countries is already required under ESRS 2-GR2, par. 12. ESMA also considers that very careful consideration should be given to whether specific quantitative significance thresholds should be defined for social topical standards or whether it should rather be left to undertakings' discretion to determine what is significant in relation to their activities. E.g., the reference to 50 and more employees in par. 51 could be very granular for a large multinational company but very high for a smaller undertaking. The same applies to the guidance provided for S1-20 (par. AG 153), S1-22 (par. AG 155) and S1-23 (par. AG 160). As CSRD Article 29b explicitly requires the ESRS to specify the information to be disclosed on working time and as the ESRS already envisage requirements on policies relating to working time, it would be important to ensure that adequate KPIs are also mandatorily reported. ESMA therefore suggests that EFRAG considers that S1-12 should become mandatory after an initial phase-in period during which it may need to remain optional.

The notion of fair remuneration in S1-14 appears to be relatively subjective and might in practice be based on different methodological principles. The information on fair remuneration will most likely not be easily comparable despite the guidance provided. Moreover, due to the granularity required to provide such information we consider that this disclosure should only be provided for those countries in which the undertaking has significant employment.

S1-19, par. AG 150 requires undertakings to behave in a certain way rather than to require disclosures on the employment of persons with disabilities. ESMA encourages EFRAG to reconsider this wording as it may create the risk of changing corporate governance requirements.

Finally, ESMA observes that S1 is very extensive with 26 disclosure requirements and 173 paragraphs of application guidance. This poses the risk of information overload which could impede the ultimate goal to provide greater transparency about undertakings' practices in the social area. We recommend that EFRAG, taking into account stakeholders' input, analyse which disclosures are fundamental for stakeholders and should be prioritised. Other less essential disclosure requirements could be considered for gradual introduction.

### ***ESRS S2 – Workers in the value chain***

**Q46: Please, rate to what extent do you think ESRS S2 – Workers in the value chain:**

- A. Covers sustainability information required by articles 19a and 19b of the CSRD proposal (see Appendix II for CSRD detailed requirements)**
- B. Supports the production of relevant information about the sustainability matter covered**
- C. Fosters comparability across sectors**
- D. Covers information necessary for a faithful representation from an impact perspective**
- E. Covers information necessary for a faithful representation from a financial perspective**
- F. Prescribes information that can be verified and assured**
- G. Meets the other objectives of the CSRD in term of quality of information**
- H. Reaches a reasonable cost / benefit balance**
- I. Is sufficiently consistent with relevant EU policies and other EU legislation**
- J. Is as aligned as possible to international sustainability standards given the CSRD requirements**

CSRD Art. 29b emphasises that the ESRS shall take account of the difficulties that undertakings may encounter in gathering information from actors throughout their value chain, especially from those which are not obliged to report sustainability information. ESMA assumes that this is the reason why S2 does not at this stage require disclosure of specific KPIs.

Given that S2 includes very detailed disclosure requirements that might be challenging for undertakings to comply with in the first years of implementation, ESMA suggests that EFRAG consider a progressive approach in which application of some disclosure requirements included in this standard would be phased in (e.g., explanation of targets or actions taken on material impacts).

In relation to the scope of S2 (par. 5), please refer to our comment on par. 6 of ESRS S1 under Q45.

In relation to disclosures on policies related to value chain workers (S2-1) required by par. AG 25, we draw attention to our comment on par. AG 20 of S1 under Q45.

### ***ESRS S3 – Affected communities***

**Q47: Please, rate to what extent do you think ESRS S3 – Affected communities:**

- A. Covers sustainability information required by articles 19a and 19b of the CSRD proposal (see Appendix II for CSRD detailed requirements)**
- B. Supports the production of relevant information about the sustainability matter covered**
- C. Fosters comparability across sectors**
- D. Covers information necessary for a faithful representation from an impact perspective**
- E. Covers information necessary for a faithful representation from a financial perspective**
- F. Prescribes information that can be verified and assured**
- G. Meets the other objectives of the CSRD in term of quality of information**
- H. Reaches a reasonable cost / benefit balance**
- I. Is sufficiently consistent with relevant EU policies and other EU legislation**
- J. Is as aligned as possible to international sustainability standards given the CSRD requirements**

ESMA generally supports the proposed disclosure requirements relating to communities which may be impacted by the activities of undertakings.

In order to ensure that the implementation of this standard leads to disclosure of a high quality, ESMA suggests that EFRAG consider a gradual phase-in of the requirements which are more detailed than what is currently required to be reported on the basis of the most commonly used sustainability reporting standards, most notably GRI (e.g., explanation of targets or actions taken on material impacts).

Lastly, while still reflecting the specificities of disclosures applicable to affected communities and consumers, respectively, we would recommend that EFRAG consider merging S3 and S4 given the large overlaps between these two standards.

### ***ESRS S4 – Consumers and end-users***

**Q48: Please, rate to what extent do you think ESRS S4 – Consumers and end-users:**

- A. Covers sustainability information required by articles 19a and 19b of the CSRD proposal (see Appendix II for CSRD detailed requirements)**
- B. Supports the production of relevant information about the sustainability matter covered**
- C. Fosters comparability across sectors**
- D. Covers information necessary for a faithful representation from an impact perspective**
- E. Covers information necessary for a faithful representation from a financial perspective**

**F. Prescribes information that can be verified and assured**

**G. Meets the other objectives of the CSRD in term of quality of information**

**H. Reaches a reasonable cost / benefit balance**

**I. Is sufficiently consistent with relevant EU policies and other EU legislation**

**J. Is as aligned as possible to international sustainability standards given the CSRD requirements**

ESMA generally supports the proposed disclosure requirements relating to consumers and end-users which may be impacted by the activities of undertakings.

We note that it is not entirely clear why S4 distinguishes between consumers and end-users. All requirements of the standard seem to apply equally to both groups. Furthermore, the terms 'consumers' and 'end-users' seem to overlap. EFRAG could simplify the standard by defining and using a term (e.g., customers) that covers both groups.

In order to ensure that the implementation of this standard produces disclosure of a high quality, ESMA suggests that EFRAG consider a gradual phase-in of the requirements which are more detailed than what is currently required to be reported on the basis of the most commonly used sustainability reporting standards, most notably GRI (e.g., explanation of process for setting targets or actions taken on material impacts).

Lastly, while still reflecting the specificities of disclosures applicable to affected communities and consumers, respectively, we would recommend that EFRAG consider merging S3 and S4 given the large overlaps between these two standards.

***ESRS G1 – Governance, risk management and internal control***

**Q49: Please, rate to what extent do you think ESRS G1 – Governance, risk management and internal control:**

**A. Covers sustainability information required by articles 19a and 19b of the CSRD proposal (see Appendix II for CSRD detailed requirements)**

**B. Supports the production of relevant information about the sustainability matter covered**

**C. Fosters comparability across sectors**

**D. Covers information necessary for a faithful representation from an impact perspective**

**E. Covers information necessary for a faithful representation from a financial perspective**

**F. Prescribes information that can be verified and assured**

**G. Meets the other objectives of the CSRD in term of quality of information**

**H. Reaches a reasonable cost / benefit balance**

**I. Is sufficiently consistent with relevant EU policies and other EU legislation**

**J. Is as aligned as possible to international sustainability standards given the CSRD requirements**



ESMA's appreciates G1's goal of supporting the production of relevant information about governance matters and sets out its detailed comments on the standard below.

Firstly, it should be noted that the interaction between G1 and the governance standards under ESRS 2 could benefit from clarification. Some of the requirements overlap and the alleged distinction between sustainable corporate governance and more general corporate governance does not seem to fully justify the split into two standards. Here, it would be more beneficial to have the two addressed together, with sustainable corporate governance being a sub-topic of general corporate governance disclosures.

A second comment pertains to the wide scope and detail of the disclosure requirements, which reflect the great part of the disclosures currently provided in the context of corporate governance and remuneration reports based on national law and corporate governance codes as well as the provisions under Art. 20 of the Accounting Directive. On the one side, this means that Accounting Directive requirements are indirectly extended to the larger group of undertakings that fall under the CSRD but do not fall under Art. 20 of the Accounting Directive (which is limited to undertakings admitted to trading on a regulated market). On the other side, for those undertakings that fall under both sets of provisions, alignment in reporting should be pursued and redundancies should be avoided.

We observe that in some cases, G1 appears to go beyond the requirements included in the CSRD. We suggest simplifying the standard to avoid duplication of information requirements and to focus only on the information relevant for users (e.g., we suggest that frequency and number of meetings are not indicators for an undertaking's productivity and may as such not be core pieces of disclosure).

Thirdly, it is not always clear whether information involving 'administrative, supervisory and management bodies' should be complemented with information on other functions, given the several references to other concepts such as 'senior management', 'other key personnel', 'management level', 'senior executives', 'executive and operational levels', in addition to 'governance bodies', that can be found in ESRS 2-GOV and in ESRS G1 and G2. To enhance clarity, it may be helpful to consistently use the wording 'administrative, supervisory and management bodies'.

Fourthly, as already mentioned under the relevant general questions, the envisaged interaction between these standards and other EU requirements such as the SRD II and the CSDDD proposal might be better clarified and further attention should be paid to avoid the risk that disclosure requirements end up indirectly introducing conduct duties, such as the application of a specific corporate governance code.

Lastly, we observe that our remarks in relation to incorporation by reference of governance-related information are set out under Q11.

## ***ESRS G2 – Business conduct***

**Q50: Please, rate to what extent do you think ESRS G2 – Business conduct:**

**A. Covers sustainability information required by articles 19a and 19b of the CSRD proposal (see Appendix II for CSRD detailed requirements)**

- B. Supports the production of relevant information about the sustainability matter covered**
- C. Fosters comparability across sectors**
- D. Covers information necessary for a faithful representation from an impact perspective**
- E. Covers information necessary for a faithful representation from a financial perspective**
- F. Prescribes information that can be verified and assured**
- G. Meets the other objectives of the CSRD in term of quality of information**
- H. Reaches a reasonable cost / benefit balance**
- I. Is sufficiently consistent with relevant EU policies and other EU legislation**
- J. Is as aligned as possible to international sustainability standards given the CSRD requirements**

ESMA generally appreciates the goal of G2 to support the production of relevant information about business conduct matters.

As further explained under the questions on each respective disclosure requirement in section 3D of the questionnaire, we observe that certain notions could be clarified. For example, the notion of 'relevant management' in par. AG 3(c) could specify whether it refers to persons involved in business conduct matters, those exposed to non-compliance risks or other. Moreover, there is no definition of what is considered 'unethical behaviour'. In the absence of such a definition, reporting may be subjective and will depend on the interpretation of each individual undertaking. Finally, as argued below under Q132 and Q135, concepts such as 'bribery', 'lobbying', etc. could benefit from clarification.

## 2. ESRS implementation prioritisation / phasing-in

### *ESRS implementation prioritisation / phasing-in options*

**Q56: beyond feasibility of implementation, what other criteria for implementation prioritisation / phasing-in would recommend being considered? And why?**

ESMA observes that a number of the topical standards in the ESRS establish very detailed and / or very numerous disclosure requirements. For this reason, sustainability reports prepared under the ESRS are likely to be quite long and detailed. While ESMA is very supportive of robust and precise reporting on sustainability matters, overly long or detailed reporting could impact users' ability to properly focus on material information and risk obscuring material information by an overload of disclosure points. For undertakings preparing reporting, it could furthermore be burdensome and complex to prepare the disclosure as well as difficult to establish the new systems to provide this disclosure in time for the expected application deadline for the standards. Undertakings may equally experience difficulties collecting information about value chains, especially from entities who are not themselves obliged to publish sustainability information (EU entities which are not subject to the CSRD or non-EU entities, notably those which are SMEs or based in emerging economies / markets).

ESMA therefore considers that EFRAG should assess whether each of the disclosure requirements in the 11 topical standards should be included in the first set of ESRS. Such an assessment could rely on the following principles:

- Thoroughly checking whether all the proposed requirements are relevant for virtually all or for a significant number of undertakings in scope of the CSRD or whether any requirements, due to their specificity, are relevant only to undertakings in certain sectors. For example, specific water-related disclosures may be of most relevance for sectors that heavily rely in water resources as part of their production processes. Any requirements which would only be relevant to a subset of undertakings, even if that subset is large, should be moved to the relevant sector-specific standards. In this regard, when preparing the sector-specific standards ESMA encourages EFRAG to ensure that similar topics addressed in different sector-specific standards are subject to the same disclosure treatment.
- Considering whether all the proposed requirements should be part of the earliest ESRS reporting (2025 for undertakings already reporting under the NFRD, 2026 for large undertakings newly included under the CSRD, 2027 / 2028 / 2029 for SMEs) or whether some of them should be i) changed from mandatory to optional in the first version of the standards, ii) subject to a delayed application deadline which could be specified within the standards, iii) taken out of the first set of the standards altogether and considered for a later version. When considering whether a specific disclosure requirement should be part of the earliest ESRS reporting, EFRAG could use the two following points as guidance:
  - o Whether undertakings are likely to have access to the data from other entities in their value chain which is necessary to meet each disclosure requirement. For example, when undertakings already reporting under the NFRD prepare their disclosure in 2025 and 2026, they will not have access to disclosure

provided from smaller entities in their value chain that will start reporting under the CSRD in 2026 onwards. Where necessary, it may be useful to permit these undertakings to use topic-specific approximations.

- Unrelated to the value chain, whether the data which undertakings are themselves able to compile is robust. For example, many undertakings will need to establish new systems for computing their disclosures and it will take some time before such systems can ensure fully reliable reporting. For that reason, there may be a need to permit reporting to commence in relation only to core areas of certain topics, let undertakings' systems mature and then add further requirements in a next version of the standards.
- Considering the phase-in provisions in the CSRD (for example, on value chains) and the timing of development of other closely linked areas of EU legislation, such as the CSDDD. With regards to the latter, ESMA highlights that before establishing extensive disclosure requirements on due diligence duties for all undertakings in scope of the CSRD, EFRAG should consider the scope of the due diligence obligations in the CSDDD. At the moment, the CSDDD proposal sets out scoping requirements which would currently result in establishing certain due diligence obligations only for a sub-group of the large entities and for some third-country undertakings addressed by the CSRD. If this is confirmed in the final text of the CSDDD, EFRAG should reflect this fact accordingly on the disclosures.

**Given the critical importance of implementation prioritisation / phasing-in, please justify and illustrate your response**

To illustrate, some of the disclosure requirements that could be considered for reprioritisation are:

- ESRS E2-4, emissions to air, water and soil all along the value chain as this information may be very difficult for undertakings to obtain when downstream activities are located outside the EU.
- Some of the disclosure requirements included in ESRS S2, ESRS S3 and ESRS S4 (e.g., explanation of targets or actions taken on material impacts), as undertakings may encounter difficulties in gathering information from actors throughout their value chain.

### **3D. Adequacy of Disclosure Requirements – Governance standards**

#### **DR G1-1 – Governance structure and composition**

**Q117: Please, rate to what extent do you think G1-1 – Governance structure and composition:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements**
- H. Represent information that must be prioritised in first year of implementation**
- I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

ESMA observes that it would be useful to further clarify this disclosure requirement, namely by (i) addressing the overlap with the information required by Art. 20 of the Accounting Directive, and (ii) further specifying what is meant in par. 14 on the number of significant positions and commitments held in governance bodies and the nature of commitments (specifying if this refers to the issuer or also to other companies; if the latter, we suggest the positions held in the governance bodies of other companies should be disclosed).

#### **DR G1-2 – Corporate governance code or policy**

**Q118: Please, rate to what extent do you think G1-2 – Corporate governance code or policy:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements**

## **H. Represent information that must be prioritised in first year of implementation**

### **I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

We suggest simplifying and clarifying the requirements under par. 18, which may go beyond what is envisaged by the CSRD. More specifically, it may be helpful to clarify the differences between the requirements under this disclosure requirement and those under the Accounting Directive. This, in turn, would facilitate the understanding of what should be disclosed if the undertaking is not listed and does not apply any corporate governance code.

## **DR G1-3 – Nomination process**

### **Q119: Please, rate to what extent do you think G1-3 – Nomination process:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements**
- H. Represent information that must be prioritised in first year of implementation**
- I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

ESMA observes that these disclosure requirements appear highly granular, and that it should be considered whether they can be streamlined. In addition, it would be useful to clarify if the criteria used to nominate members have to be published ex-ante or ex-post.

## **DR G1-4 – Diversity policy**

### **Q120: Please, rate to what extent do you think G1-4 – Diversity policy:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**

**F. Is sufficiently consistent with relevant EU policies and other EU legislation**

**G. Is as aligned as possible to international sustainability standards given the CSRD requirements**

**H. Represent information that must be prioritised in first year of implementation**

**I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

We suggest clarifying the differences between the requirements imposed under this disclosure requirement and those under the Accounting Directive and to ensure that undertakings make reference to the legislative provisions which they are subject to in this area.

In addition, specificities included in national legislation should be taken into account as potential limitations for the collection of data on diversity.

#### **DR G1-5 – Evaluation process**

**Q121: Please, rate to what extent do you think G1-5 – Evaluation process:**

**A. Requires relevant information about the sustainability matter covered**

**B. Requires information that is relevant for all sectors (sector-agnostic only information)**

**C. Can be verified / assured**

**D. Meets the other objectives of the CSRD in term of quality of information**

**E. Reaches a reasonable cost / benefit balance**

**F. Is sufficiently consistent with relevant EU policies and other EU legislation**

**G. Is as aligned as possible to international sustainability standards given the CSRD requirements**

**H. Represent information that must be prioritised in first year of implementation**

**I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

ESMA suggests broadening the definition of 'evaluation process', for example as follows: 'process through which the administrative, management and supervisory bodies assess their size, composition and functioning, including the involvement in the definition of the company's strategy and in the monitoring of the management of the company'.

Additionally, we recommend requiring undertakings to disclose what the conclusions of the evaluation are, so it is easier for users to understand the basis for the actions taken in response to the evaluation.

## **DR G1-6 – Remuneration policy**

**Q122: Please, rate to what extent do you think G1-6 – Remuneration policy:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements**
- H. Represent information that must be prioritised in first year of implementation**
- I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

Generally, ESMA observes that this disclosure requirement seems to go beyond the requirements included in the CSRD and does not seem fully aligned with the SRD II. In particular:

- It would be good to clarify the scope of the disclosure requirement, especially by further specifying what is meant by 'senior executives' who are referred to in the application guidance.
- As mentioned under previous questions, it would be helpful to use consistent wording across the standards (i.e., 'administrative, management and supervisory bodies') and align the scope of application with the SRD II notion of 'director', which also includes the CEO (and deputy CEO, if existent), when these are not members of the administrative, management or supervisory bodies, and provides member states with the possibility to include other persons performing similar functions.

As a side comment, it should be noted that disclosing the difference in treatment with 'other employees' may be difficult to implement in practice due to the heterogeneity of provisions among employees.

## **DR G1-7 – Risk management processes**

**Q123: Please, rate to what extent do you think G1-7 – Risk management processes:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**



**E. Reaches a reasonable cost / benefit balance**

**F. Is sufficiently consistent with relevant EU policies and other EU legislation**

**G. Is as aligned as possible to international sustainability standards given the CSRD requirements**

**H. Represent information that must be prioritised in first year of implementation**

**I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

ESMA considers that it would be useful to further clarify if this disclosure requirement relates to both ESG risks and other risks incurred.

In addition, par. AG 16(d) could be amended to request a breakdown of segments (rather than a breakdown of responsibilities by business units).

#### **DR G1-8 – Internal control processes**

**Q124: Please, rate to what extent do you think G1-8 – Internal control processes:**

**A. Requires relevant information about the sustainability matter covered**

**B. Requires information that is relevant for all sectors (sector-agnostic only information)**

**C. Can be verified / assured**

**D. Meets the other objectives of the CSRD in term of quality of information**

**E. Reaches a reasonable cost / benefit balance**

**F. Is sufficiently consistent with relevant EU policies and other EU legislation**

**G. Is as aligned as possible to international sustainability standards given the CSRD requirements**

**H. Represent information that must be prioritised in first year of implementation**

**I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

Similarly to what is mentioned under G1-7, it is suggested to change par. AG 21 to include a breakdown of segments involved, rather than business units.

#### **DR G1-9 – Composition of the administrative, management and supervisory bodies**

**Q125: Please, rate to what extent do you think G1-9 – Composition of the administrative, management and supervisory:**

**A. Requires relevant information about the sustainability matter covered**

- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements**
- H. Represent information that must be prioritised in first year of implementation**
- I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

ESMA recommends aligning the wording in par. 24 and 43 so that undertakings who have adopted policies for diversity are required to disclose the same information both under their diversity policy and in the context of their disclosures on board composition.

We also note that national legislation can hinder the collection of information on diversity, and as such it would be important to highlight that these disclosure requirements are subject to national restrictions.

Finally, it would be useful to have further clarity on the concept 'independent shareholder-elected members'.

#### **DR G1-10 – Meetings and attendance rate**

**Q126: Please, rate to what extent do you think G1-10 – Composition of the administrative, management and supervisory:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements**
- H. Represent information that must be prioritised in first year of implementation**
- I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

ESMA suggests further clarifying the disclosures required under this point, in particular in

connection to whether the attendance rate should be disclosed for each meeting (as under par. 48(b)) or per director (as under par. 46).

## **DR G2-1 – Business conduct culture**

**Q127: Please, rate to what extent do you think G2-1 – Business conduct culture:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements**
- H. Represent information that must be prioritised in first year of implementation**
- I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

Generally, we note that the information to be provided under this disclosure requirement is very granular.

Furthermore, it would be helpful to clarify the difference between points (a) and (c) of par. 17. Additionally, it is suggested to correct the reference in par. 17 (from par. 16 to 14).

Finally, expressions such as 'tone from the top' and 'tone from the middle' would benefit from clarification.

## **DR G2-2 – Policies and targets on business conduct**

**Q128: Please, rate to what extent do you think G2-2 – Policies and targets on business conduct:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD**

## requirements

### H. Represent information that must be prioritised in first year of implementation

#### I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities

ESMA encourages EFRAG to improve the wording of this disclosure requirement by further clarifying what is meant by 'unethical behaviour' and by requiring undertakings to report on how business conduct incidents are investigated, including in terms of timing and independence, rather than only requiring undertakings' commitment to that.

In addition, the training strategy described under par. 20(g) seems to overlap with the requirements covered by ESRS G2-1 and ESRS G2-5, so it may be worth considering merging these into one.

## DR G2-3 – Prevention and detection of corruption and bribery

**Q129: Please, rate to what extent do you think G2-3 – Prevention and detection of corruption and bribery:**

- A. Requires relevant information about the sustainability matter covered
- B. Requires information that is relevant for all sectors (sector-agnostic only information)
- C. Can be verified / assured
- D. Meets the other objectives of the CSRD in term of quality of information
- E. Reaches a reasonable cost / benefit balance
- F. Is sufficiently consistent with relevant EU policies and other EU legislation
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements
- H. Represent information that must be prioritised in first year of implementation
- I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities

We suggest further clarifying the concept of 'corruption', for example to ensure that undertakings can make reference to definitions included in national law. In addition, in par. 24(d), we observe that the reference to 'where relevant' may not be needed, as the materiality assessment applies across the entire set of ESRS, as established by ESRS 1, par. 42.

## DR G2-4 – Anti-competitive behaviour prevention and detection

**Q130: Please, rate to what extent do you think G2-4 – Anti-competitive behaviour prevention and detection:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements**
- H. Represent information that must be prioritised in first year of implementation**
- I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

We only have one editorial comment in relation to this disclosure requirement which is to replace the cross-reference in par. 29 with the actual requirements from G2-3, adapted so they refer to the subject matter of this disclosure requirement (i.e., allegations or incidents of anti-competitive behaviour).

#### **DR G2-5 – Anti-corruption and anti-bribery training**

**Q131: Please, rate to what extent do you think G2-5 – Anti-corruption and anti-bribery training:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements**
- H. Represent information that must be prioritised in first year of implementation**
- I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

Generally, ESMA finds that this disclosure requirement could be combined with G2-4 in order to streamline the standards.

## **DR G2-6 – Corruption or bribery events**

**Q132: Please, rate to what extent do you think G2-6 – Corruption or bribery events:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements**
- H. Represent information that must be prioritised in first year of implementation**
- I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

ESMA considers that it would be helpful to further clarify the concepts of 'bribery' and 'bribery events', in particular vis-à-vis the concept of corruption and to provide details on any links to the disclosures under IAS 37 (contingent liabilities) or similar provisions in the accounting framework which the undertaking uses to prepare its financial statements.

## **DR G2-7 – Anti-competitive behaviour events**

**Q133: Please, rate to what extent do you think G2-7 – Anti-competitive behaviour events:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements**
- H. Represent information that must be prioritised in first year of implementation**
- I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

ESMA observes that this disclosure requirement – as currently drafted – seems to extend to information on litigations that are not 'publicly announced' litigations and that as such might

be confidential.

In addition, similarly to what is argued for G2-6, further clarity could be provided on any links to relevant disclosure requirements in IFRS or whichever other accounting framework the undertaking applies.

## **DR G2-8 – Beneficial ownership**

**Q134: Please, rate to what extent do you think G2-8 – Beneficial ownership:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**
- F. Is sufficiently consistent with relevant EU policies and other EU legislation**
- G. Is as aligned as possible to international sustainability standards given the CSRD requirements**
- H. Represent information that must be prioritised in first year of implementation**
- I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

ESMA suggests that EFRAG further specify what is meant by key concepts such as 'ownership', 'beneficial ownership' and 'control'. It would be good to also clarify how these terms may interact with the definitions and transparency thresholds under the Transparency Directive as well as with relevant definitions in the relevant accounting framework.

Furthermore, as ownership information varies depending on the specific moment it is reported, it may be helpful to require clarity on the precise timing which ownership information refers to.

## **DR G2-9 – Political engagement and lobbying activities**

**Q135: Please, rate to what extent do you think G2-9 – Political engagement and lobbying activities:**

- A. Requires relevant information about the sustainability matter covered**
- B. Requires information that is relevant for all sectors (sector-agnostic only information)**
- C. Can be verified / assured**
- D. Meets the other objectives of the CSRD in term of quality of information**
- E. Reaches a reasonable cost / benefit balance**

**F. Is sufficiently consistent with relevant EU policies and other EU legislation**

**G. Is as aligned as possible to international sustainability standards given the CSRD requirements**

**H. Represent information that must be prioritised in first year of implementation**

**I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

Firstly, ESMA notes that it would also be useful if the envisaged disclosure contained information on transparency of lobbying activities, such as the registration in any transparency register.

In addition, it is suggested adding further wording to clarify the concept of 'lobbying', e.g., by referencing EU law, and its link with the concept of 'advocacy'. Further concepts such as 'comparable position', 'type of beneficiary/recipient' and 'professional or advocacy associations' could also benefit from further clarification.

Finally, it could be considered whether a time limit could apply to par. 50, after which no reporting is required.

## **DR G2-10 – Payment practices**

**Q136: Please, rate to what extent do you think G2-10 – Payment practices:**

**A. Requires relevant information about the sustainability matter covered**

**B. Requires information that is relevant for all sectors (sector-agnostic only information)**

**C. Can be verified / assured**

**D. Meets the other objectives of the CSRD in term of quality of information**

**E. Reaches a reasonable cost / benefit balance**

**F. Is sufficiently consistent with relevant EU policies and other EU legislation**

**G. Is as aligned as possible to international sustainability standards given the CSRD requirements**

**H. Represent information that must be prioritised in first year of implementation**

**I. Is well suited to be transformed in a digital reporting taxonomy that will avoid creating misunderstandings or practical complexities**

ESMA suggests that it may be worth reconsidering whether this disclosure requirement is strictly needed given, on the one hand, the limited relevance of payment practices for governance and sustainability and, on the other hand, the relatively high burden it may place on undertakings.