EFRAG Sustainability Reporting Board
35 Square de Meeüs
1000 Brussels
Belgium

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KKO/TIAG

EFRAG Consultation Survey on the Draft European Sustainability Reporting Standards (ESRS ED)

Dear Sir/Madame

First of all, the Danish National Funding Mechanism would like to congratulate EFRAG for the amount of work done in the short timespan in order to produce a set of draft reporting standards to support the CSRD. The Project Task-Force have been working under intense time pressure, leading to the unfortunate timing of the ESRS ED consultation period during vacation time in Denmark. As a result, outreach and consultation with our members have been more limited than we would have preferred.

We fully support the objective of transforming Europe into the first climate-neutral continent in the world by 2050 and we are ready to contribute. In this respect relevant and reliable sustainability information is crucial and a fundamental precondition for the success of other EU sustainability initiatives, including sustainable finance.

On this basis, we would strongly encourage EFRAG and the EU Commission to ensure that adequate resources is allocated to and sufficient time is spent by EFRAG to assess the comments received during the consultation process and make the necessary changes needed to ensure a high quality of the final standards.

The reporting standards will not only impact the 50.000+ companies directly covered by the CSRD but also the vast number of companies in the value chains. This provides a unique opportunity to support the transition of the economy but can also lead to undue administrative burdens and drive a compliance reporting regime if the reporting requirements are too excessive and requires the publication of immaterial information. We would encourage EFRAG to reduce the scope of the standards as much as possible within the already ambitious CSRD requirements and focus on the key priorities, including ensuring the consistency with the sustainable finance disclosure requirements for the financial sector in SFDR, CRR etc.

We call for a comprehensive field test of the proposed standards in due time before the implementation. It is absolutely necessary that the standards are tested to secure the quality and to identify areas which is not workable in practice.

Having read the complete set of exposure drafts our key concerns are the following:

- The **ESRSs are too granular** and will result in an unfocused reporting with an information overload in line with what was experienced in the financial reporting until efforts were made from the standard setter to focus on material issues. The level of granularity will have a negative impact on data quality and undermine the purpose of fostering the transition to a more sustainable economy.

  We suggest to limit the general disclosure requirements and make better use of sector specific reporting requirements (as a number of disclosures are not generally comparable across sectors). This would be in line with the EU taxonomy regulation focusing initially on mandatory disclosures for high-impact sectors selected for each environmental objective.

  Furthermore, the disclosure requirements should be limited to the minimum requirements according to the CSRD and Sustainable Finance requirements in SFDR, CRR etc. It is alarming that some mandatory disclosure requirements in the standards enhances the scope of the legal requirements. We're confident that many companies, as shown today, will go beyond the legal requirements establishing best practice for others to follow in due time.

  Consequently, we suggest that the description of strategy, risks, and opportunities are covered only – and fully – by ESRS 2, and without exceeding the CSRD requirements. This is particularly important for the description of opportunities, which should not exceed what the reporting entity has integrated in its strategy and business model as information beyond this is at risk of creating opportunistic expectations without proper ground. Such is better left outside the annual report in companies' dialogue with stakeholders.

- The **materiality definitions** are unclear as they are not fully aligned with neither the financial materiality approach from the financial statements section nor commonly agreed approaches to impact materiality. This combined with the rebuttable presumption foster a very granular approach to disclosure requirements, drives immaterial reporting elements, and leads to compliance reporting. With unclear definitions and the rebuttable resumption – whereby it is as complex and cumbersome to document any rebutted information as it is to disclose it – it will be safer to include the information rather than rebutting. This will not only lead to a clotted and unfocused reporting, but potentially also to a lack of management ownership and focus on key areas.

  We suggest aligning with the established and well-known international frameworks, especially ISSB (financial materiality) and GRI (impact materiality) to foster comparability across jurisdictions.

Disclosure requirements that can be directly attributed to mandatory sustainable finance requirements in SFDR, CRR etc. for the financial sector should always be disclosed independently of its materiality to the reporting entity. While for an individual company a disclosure requirement may be immaterial, added together across a portfolio of financed-/investee companies, the sum may and will in many cases be material for financial institutions.

- In general, the standards seem to have **to high a focus on year-one reporting** instead of the recurring reporting. This for instance drives extensive disclosures on policies that in most instances will remain 90-95% stable over the years.

  We suggest to focus on changes in the reporting period and leave stable descriptions on the website or at the very least in a disclosure section (notes) at the end of the sustainability report. Otherwise, material information will drown in immaterial and recurring descriptions and information.

- Overall, we support the **structure of the standards**, but the content of the standards needs to be more streamlined. From our members we have been informed that the standards are very difficult to read, even for experienced readers. Our members especially single out ESRS 1 + 2 as they overlap – and in some instances include direct duplication of language and requirements as well as indirect requirements through the use of "shall". There is for instance an almost 1 to 1 repetition of ESRS 2 DR2-GR2 to the corresponding section of ESRS 1. Further, having application guidance to ESRS 2 in the topical standards complicates the reading and understandability of the standards.

  We suggest to significantly reduce ESRS 1 to describe the principles only, avoid duplication, and to simplify the language of ESRS 2. Further, we recommend that the application guidance to ESRS 2 disclosures is only provided in ESRS 2. When additional disclosures are needed, the topical standards should include these as separate disclosure requirements and not as "masked disclosure requirement" hidden as application guidance.

  Lastly, we suggest, that some of the descriptions – especially in the application guidance – are replaced by or supported by figures, graphics, or illustrative tables.

- A number of topical standards, e.g., the ESRS on Biodiversity, covers areas where there is either a **lack of or very immature measurement principles and methods** available. The lack of knowledge of what good reporting looks like will therefore at best lead to reporting of poor quality and in worst case to unsubstantiated disclosures and erroneous investment and finance decisions.

  We suggest factoring in the maturity of the measurement and reporting areas, to move disclosure requirements to sector specific standards, and to delay the effective dates for the detailed disclosure requirements in order to ensure that an appropriate methodology is developed and that the 50.000+ undertakings covered by the standards have the resources and knowledge available to provide high quality reporting. This allows priority to be given to the most important areas and to support this by the targeted development of measurement and reporting methods. In this respect the most important disclosures are those that can be directly attributed to mandatory sustainable finance requirements in SFDR, CRR etc. for the financial sector.

Specifically, for areas that are not covered by the CSRD in articles 19a/29a we suggest that these are either removed for the first 5-8 years to allow for appropriate standards and methods to be developed, or alternative to make reporting under these standards voluntary for the said period. During these years, entities could describe their maturity in the areas and incorporate/increase the reporting as they mature.

Minimum disclosure requirements needed to be reported by entities for their cooperation with banks and insurance companies to comply with the SFDR, CRR ect. should always be followed, but the disclosures separately "marked" and only be mandatory when directly attributable to requirements in SFDR, CRR etc.

- The mandated **structure of the sustainability reporting** does not foster integration of sustainability information with financial and other information but supports a segregation of the management report. In Denmark, we have good experience with integration of the reporting and with providing required information on the entity's webpage why the required format will be a significant set-back of good reporting practices and decrease the value of the overall reporting of both the sustainability reporting and the financial reporting.

  We suggest a full flexibility in the reporting (within the possibilities of the CSRD), and that EFRAG places more emphasis on the users of the reporting instead of making this a data-provision exercise. Reporting is all about addressing the target audience and provide the relevant information in the most accessible way. It is therefore important that ESRS is not more prescriptive than the restrictions set by CSRD.

- The concept and required description of the **value chain and boundaries** thereof is a significant issue for large corporations and especially for all financial institutions. Up- and downstream value chains for these undertakings will be extensive with thousands of customers in all industries and millions of affected stakeholders. To ensure meaningful disclosures from these undertakings and avoid excessive and unproportionate burdens the value chain concept must be clarified and, above all, limited. EFRAG should take on the role of determining when information about the value chain is applicable as per the CSRD. Therefore, it should be made clear which ESRSs/disclosure requirements shall apply only for own activities, and which shall apply for activities of other undertakings in the value chain.

- **Subsidiaries – access to necessary information**. In general, we support that the reporting entities themselves decide on the level of granularity in the disclosures. However, as banks typically finance specific entities, including subsidiaries, rather than the Group, they need certain quantitative data from the financed entities to fulfil their reporting obligations, e.g. financed GHG emissions, Green Asset Ratio etc.

On this basis we encourage EFRAG to specify which limited, but essential industry defining KPIs a parent undertaking should always consider disclosing at entity level in the group reporting (unless separate reports are provided for the subsidiaries that have obtained separate funding). Without such a standardised approach, the companies will face numerous inquiries for data at entity level from the financial sector causing significant burdens for both entities and banks.

- **Time lag for the financial sector.** It is needed to introduce a time lag of at least 1 year for the ESRS disclosure requirements for the financial sector which depend on data from the non-financial entities. Without inclusion of a proper time lag the ESRS reporting from the financial sector will be based on rough approximations and consequently only have limited reliability. Furthermore, the non-financial companies will face numerous inquiries and requests for data before publication of their annual reports causing significant administrative burdens.

Flexibility of reporting
In Denmark we have over the years had a very strong focus on ensuring the readability and usability of the annual reports for the key users, many of which are stakeholders of the reporting entity. This has led to annual reports with high readability which is acknowledged by those users. One key element of this have been the ability to publish the sustainability information in a separate report on the website while still being an official part of the annual report and is filed at the same date. Often the management report includes a summary of the separate report.

With the requirement to include the entire sustainability report in the management report, a high degree of flexibility is needed to ensure that the reporting can be integrated with the other elements of the annual report. To achieve this, we would suggest that ESRS provides full flexibility to design the sustainability report as best suited to communicate with the users. For some this would include integration of certain reporting elements across all areas to avoid duplication of information. For others, separate sections by area (cross-cutting, E, S, and G) may be preferred, especially for undertakings with simpler business models.

With an integration across all areas the sustainability report could for example be structured with the following sections: a) strategy, b) value chain, c) risks and applied opportunities, d) description of developments in the year, e) tables with disclosure of all data points, including targets and a description of the related measurement and reporting policies, and f) policies and other more static information.

As a consequence, we suggest that the format currently required by ESRS 1 is deleted, or alternatively that the different formats are changed from required, alternative reporting structure to be illustrative examples. If EFRAG decides to keep the illustrative examples, we suggest adding a fourth example based on the above example. Building on the structure outlined in ESRS 1 6.2 and duplicated in ESRS DR2-GR 1 6c:

"The undertaking could for example present the sustainability report in one of the following four options, or combinations thereof*:*

...

(d) describe the different items across all areas, e.g., strategy, value chain, risks and applied opportunities, and policies, in separate sections covering all sustainability areas. Other disclosure requirements in the topical ESRS's should be structured and could be presented either by standard or groups of standards or in another logic structure that supports the understanding based of the business. Independently, information that remains almost unchanged year-on-year, e.g., polices, can be presented at the end of the report."

Rationale:

The fourth option is envisaged to support both the understandability of the annual reporting package and to foster integration and thus the connectivity between the elements of sustainability reporting and the financial reporting by allowing the undertaking to provide a more complete picture of the business model, strategy, risk descriptions, activities in the year, etc. Allowing for information in a separate disclosure section supports the readability by ensuring that the management report is not cluttered by long data appendixes. This will support the transition to a more sustainable economy by encouraging a more integrated approach. Since information is going to be digitally tagged, professional users will be able to extract the information through ESAP and reorder as they find necessary for their data analysis purposes.

Kind regards,
The Danish Funding Mechanism

Finance Denmark
Martin Thygesen

Insurance & Pension Denmark
Anne-Mette Munck

FSR – Danish Auditors
Lisbeth Frederiksen

Danish Chamber of Commerce
Filip Marott Sundram

Confederation of Danish Industry
Kristian Koktvedgaard