RAAD VOOR DE JAARVERSLAGGEVING
Dutch Accounting Standards Board

DASB secretariat:
Mercuriusplein 3, 2132 HA Hoofddorp
Postbus 242, 2130 AE Hoofddorp

Tel: +31 (0)88 4960 391
secretariaat@rjnet.nl
www.rjnet.nl

**European Commission**
Attn: Commissioner McGuiness
Rue de la Loi 200
1049 Brussels

| | |
|---|---|
| **Our ref:** | RJ-CSR 11 B |
| **Direct dial:** | +31(0)88 4960 391 |
| **Date:** | Hoofddorp, July 7, 2023 |
| **Re:** | EC consultation Delegated Act - Draft ESRS |

Dear Commissioner McGuiness,

The Raad voor de Jaarverslaggeving (Dutch Accounting Standards Board (DASB)) welcomes the opportunity to respond to the draft Delegated Act regarding the European Sustainability Reporting Standards (ESRS) - Set 1, published for public consultation on June 9, 2023. The DASB believes mandatory sustainability reporting can contribute to accelerating the transition to a sustainable economy. The DASB understands the urgency of this matter, and supports the development of mandatory sustainability reporting standards that are implementable in practice and that ensure high quality, consistent and comparable reporting.

We appreciate the enormous amount of work done by EFRAG and value the subsequent modifications of the Commission. The Commission has clearly responded to concerns raised by multiple stakeholder groups. For instance, the changes made with respect to the identification of material impacts, reducing the number of Disclosure Requirements and the phasing-in of certain requirements are, in our view, improvements to the ESRS.

The draft ESRS are substantive, ambitious and cover a wide range of Environmental, Social, and Governance (ESG) topics. Given the magnitude of the Standards and the very short consultation period of four weeks, the DASB requested its Working Group Sustainability Reporting (hereafter WG) to take notice of all standards and prepare detailed comments on the standards with a primary focus on addressing fatal flaws and inconsistencies. The WG consists of sustainability experts and is diverse in composition representing reporting entities, auditors, investors, and a wide range of users and stakeholders of corporate reporting (e.g., academics, trade unions and NGOs).

**Purpose of this letter: suggestions for implementation guidance, including practical examples**

In an earlier stage of the process of development of the ESRS, we sent a letter to EFRAG to communicate several fundamental concerns on the architecture and design of the draft ESRS, including a lack of international alignment. These concerns addressed the essence of sustainability reporting. We provided suggestions for improvement, of which several have been included in EFRAG's technical advice and others have been part of the subsequent adjustments made by the Commission.

The DASB has refrained from suggestions to substantially alter the ESRS. This is in recognition of the efforts made by the Commission to ensure proportionality and to facilitate the correct application of the standards through, for example, reducing the number of Disclosure Requirements, adding a phasing-in approach for certain requirements, and adding flexibility in certain disclosures.

However, the DASB remains of the opinion that the standards are extensive, especially for “first-time reporters” and in certain aspects give room for multiple interpretations. Therefore, this comment letter contains suggestions for implementation guidance which could be provided by EFRAG. The DASB underlines the necessity of timely and clear guidance, as well as practical examples based on current reporting practices by companies in different sectors, to support preparers as well as auditors and independent assurance providers in the successful implementation of the ESRS and high-quality sustainability reporting. Hence, we ask you to request EFRAG to provide this clear implementation guidance to assist (first-time) reporters on the following five essential topics: 1) materiality principles, 2) alignment with European and international standards, 3) consolidated sustainability reporting, 4) sensitive information, and 5) the risk of undue administrative burden due to the trickle-down effect.

The appendix to this letter contains detailed comments on the Standards as these concern fatal flaws such as inconsistencies within the set of Standards or with other European legislation. These detailed comments have been included in the feedback template.

We hope our views and feedback will help you strengthen the draft ESRS to a coherent set that will standardize sustainability reporting, and thereby contribute to an accelerated transition to a sustainable economy, foster accountability, and help redirect financial market funds to sustainable investments.

Our concerns and suggestions for improvement include:

### 1. *Materiality principles*

In the current draft ESRS, the materiality principles have been broadened. This means that all topical Standards, Disclosure Requirements and data points therein are subject to the materiality assessment, in an effort to significantly reduce the administrative burden of applying ESRS. We continue to support the application of Double Materiality in the ESRS and are satisfied with the fact that materiality will more clearly drive the required disclosures.

The significance of the materiality assessment means that companies should be well supported by strong guidance on how to perform the materiality assessment. The increased focus on materiality should not lead to cherry picking of material information due to the omission of severe impacts as a result of the (perceived) freedom for reporting companies to influence the materiality process to their liking.

<u>*Suggestion for improvement:*</u>
Clear implementation guidance will help companies strengthen their materiality assessment and with that, avoid cherry picking. We are aware and very supportive of the fact that EFRAG is currently drafting such guidance. However, the changes to the draft ESRS made by the

European Commission call for additional implementation guidance on the materiality assessment.

We suggest that the Commission asks EFRAG to address the following matters:

- The possibility that the current draft ESRS provides to decide on the materiality of information on a topical level as well as on a Disclosure Requirement level (and even data point level) raises questions on how to perform the materiality assessment on a Disclosure Requirement level or data point level. The criteria to be used for assessing Impact materiality and Financial materiality under paragraphs 3.4 and 3.5 respectively are mainly applicable for a sustainability matter as a whole, not on specific Disclosure Requirements within a sustainability matter. Clear implementation guidance on the application of materiality on a Disclosure Requirement level is crucial and will help avoid the criticism that the ESRS leaves the door open to less ambitious sustainability reporting where companies only choose a very limited set of material impacts to report on.
- The DASB values the change to the technical advice of EFRAG to apply the materiality principle in a consistent manner without exceptions, even when the previously designated exceptions (E1 and S1) might be very rarely not material to a reporting entity in practice. The DASB would welcome additional implementation guidance on the considerations under which E1 and/or S1 could be considered not material to an undertaking.
- Additional implementation guidance could include guidance on the development of applicable materiality thresholds, the way to include affected stakeholders in the materiality assessment and the use of comparative figures when a datapoint or disclosure requirements becomes material for the first time.
- We understand that S1 has been changed to mainly focus on employees first with Disclosure Requirements on non-employees voluntary. This supports the first-time application of the ESRS. However, at the same time we believe that non-employees are an equally important component of a reporting company's own workforce and should be addressed appropriately and with equal prominence going forward. Therefore, we suggest to take steps toward giving them equal prominence in the ESRS in the future.

### 2. *Limited alignment with European legislation and international standards on sustainability reporting*

As European (reporting) legislation is subject to amendments over time there is a risk that alignment between European legislation and other international standards diminishes over time. This alignment should be reviewed on a regular basis to ensure consistency and interoperability. In addition, we would like to highlight that the ESRS might not align with other international frameworks such as the IFRS Sustainability Standards and OECD Guidelines (for instance for the distinction between employees and non-employee workers as addressed under paragraph 1). We will highlight two examples to illustrate our concern in this letter and have added other examples to the detailed comments.

#### *2.1 European: Example SFDR alignment*

Entities in scope of the SFDR are obliged to report on Principal Adverse Impacts (PAI). However, under the European Commission's proposal, some of the related SFDR-disclosures have become voluntary under ESRS-reporting and some are not even included as possible disclosure requirements under ESRS-reporting. This means that data needed for entities to report under their obligations of SFDR may not have been provided by ESRS-reporters if it is not material for them to do so. However, although the information might not be relevant for the entity reporting under ESRS it could be obligatory information for the SFDR reporter. This discrepancy between ESRS and SFDR can therefore be problematic for SFDR reporters.

_Suggestion for improvement:_
The Commission expressed the specific aim, in making their modifications, of ensuring proportionality and facilitating the correct application of the ESRS by undertakings. Therefore, we suggest the Commission to explicitly allow SFDR reporters (in (guidance to) the SFDR) in need of undisclosed ESRS information – at minimum, for information related to the SFDR PAI indicators – to state that this information is not available (and/or not material). In this way, the Commission can prevent additional reporting burden on SFDR reporters and information requests from SFDR reporters that would jeopardize the aim of the Commission with respect to the ESRS reporters.

### *2.2 International: Example IFRS-S alignment*

The DASB welcomes that the Commission and EFRAG have continued to engage closely with the International Sustainability Standards Board to ensure a high degree of interoperability. We believe interoperability with global standard-setting initiatives is crucial to enhance the level playing field for multinational companies and to stimulate standardized information for investors. Unfortunately, interoperability with international standard setting is not yet sufficiently visible in the draft ESRS.

_Suggestion for improvement:_
We suggest that either the Commission or EFRAG (upon request of the Commission) publish a comparison between ESRS and IFRS sustainability disclosure standards to visualize the similarities and differences between both. It would be beneficial if this comparison is provided both on a higher level, as well as on a more detailed or individual disclosure level. This comparison will require maintenance, and will need to be broadened over time to reflect IFRS (and EU) developments. Furthermore, we urge the Commission to continue their engagement and alignment with the ISSB.

## *3. Consolidated Sustainability reporting within larger (non-EU) groups and the subsidiary exemption*

Many large EU undertakings are part of a European or an international group which prepares consolidated reporting. This results in an obligation for, and widespread use of, consolidated sustainability reporting. While the concept of consolidation is easy, in practice this leads to a significant number of practical complexities that ask for additional guidance, and the current ESRS general requirements dealing with consolidation (ESRS 1 par. 62 and par. 101 – 103) leave room for questions and interpretations.

The main questions that are currently arising in practice include the following:

- Differences between the consolidation scope for financial reporting and the consolidation scope for sustainability reporting: this can lead to a misalignment between the sustainability information and financial information which worsens the connectivity between these types of information and is therefore undesirable.
- How to perform a consolidation at EU level when the holding company is located outside of the EU and all EU companies report separately to the mother company abroad? The transitional provisions in the CSRD (new art. 48i from the CSRD) leave room for questions especially due to the date given. Guidance on the choices made is

strongly appreciated as it is expected to be extremely challenging in practice to prepare consolidated sustainability statements in this situation and consolidated financial information will not be available.

- How to report on financial metrics such as revenue under ESRS sustainability reporting when the sustainability consolidation is performed at a European level, but based on the consolidation exemption for intermediate holding companies of IFRS 10 or article 23 Directive 2013/34/EU for the financial statements, consolidation is performed at a level outside of the European level? This usually means that no financial figures at a European level are available.
- How does a company prepare consolidated sustainability reporting when only non-consolidated financial statements need to be prepared?
- When a company has to report on group level on metrics derived from a different sustainability reporting framework than ESRS, it is helpful if those metrics can be included in the ESRS reporting (with sufficient explanation on the methodology used) to avoid having to prepare several sets of sustainability reports for each standard set that the company reports on. The alignment meant in paragraph 2 will be very helpful in this regard.

*Suggestion for improvement:*
We would suggest to add to ESRS 1 more guidance on specific consolidation-related technicalities in line with consolidation standards for financial reporting such as IFRS 10 Consolidated Financial Statements or more detailed implementation guidance from EFRAG.

### 4. Sensitive information

Forward-looking information is an essential part of the management report and also required in the sustainability report (art. 19a sub 2 a(iii) CSRD). We generally support disclosure of forward-looking information. However, specific elements of forward-looking information might be of a sensitive nature and could result in risks to a company from a commercial or legal perspective.

ESRS 1 paragraph 104 contains an exemption for classified and sensitive information. However, the definitions for classified and sensitive information refer to EU legislation that indicates that this information is considered to be classified or sensitive where it could cause varying degrees of prejudice to the interests of the European Union or Member States. This means that an exemption for classified or sensitive information does not seem to be available for companies in cases where this may be a risk from a commercial (or legal) perspective.

ESRS 1 paragraph 105 contains an exemption for commercially sensitive information, however this exemption is limited to intellectual property, know-how or the results of innovation and does not apply in all situations. There is other commercially sensitive information which companies would not want to disclose in detail nor to inform their competitors, as this may significantly harm such companies (as well as their sustainability strategy).

*Suggestion for improvement:*
Therefore, we suggest to include exemptions for specific circumstances or a comparable exemption as included in art. 2:391 sub 2 of the Dutch Civil Code: *The management board report shall make mention of the course of events to be expected; in doing this, attention shall be paid especially, insofar as important interests do not oppose to this, to investment,*

*financing and staffing and to circumstances of which the development of turnover and profitability depends.*

Art. 29a of the CSRD Compromise text already contains such an exemption for trade secrets as defined in the Trade Secrets Directive. This exemption in the CSRD should also be mentioned in the ESRS itself and we suggest including a more general exemption in ESRS with specific guidance on whenever the use of this exemption is acceptable or not in a robust manner. This guidance is important to prevent abuse of this exemption by preparers not wanting to report negative impacts,

5. ***Risk of undue administrative burden as result of trickle-down effect***

The current draft ESRS requests significant information on the impacts in the value chain. We are still concerned that reporting companies may choose to send out elaborate information requests to SME suppliers which are not yet equipped to report extensively on their sustainability performance. SMEs may face a significant risk of undue administrative burden as result of the trickle-down effect, despite the European Commission's intention that non-listed SMEs will not be required to report, and listed SMEs should report in a proportionate manner, relevant to the scale and complexity of their activities, and to the capacities and characteristics of the SMEs (art. 1 (7b) of the CSRD amending article 29C of Directive 2013/34/EU).

As the standard for SMEs has not yet been published. this might lead – and in practice already does lead - to situations in which SMEs are asked to provide information on topics that might not be included in the SME standard and might also not be material information for the SME in question.

*Suggestion for improvement:*
We suggest asking EFRAG to include implementation guidance on value chain reporting and on which information can be requested from SMEs taking proportionality into account.

This should include at least the following guidance for:

- CSRD-reporting undertakings on how to use proxy data and estimates in order to avoid placing a disproportionate reporting burden on SME companies while simultaneously safeguarding the quality of the data
- CSRD-reporting undertakings on how to report on information that cannot be obtained at reasonable cost within the value chain
- SME companies on the information that may be requested of them by partners in the value chain, and support, in the form of templates and tools such as reporting platforms, that will help SME companies deliver requested information at the lowest cost and administrative burden to the company.

Our feedback is meant to help build the ESRS in such a way that the sustainability information in annual reports will be relevant, comparable and reliable for all stakeholders as of the implementation date of CSRD and onwards. We hope that our concerns will be considered in the final formulation of the ESRS and the EFRAG guidance currently under development. We believe that the provision of timely and clear implementation guidance is essential for the success of sustainability reporting. Incorporating the experiences of the first group of sustainability reporters in the implementation guidance as soon as possible will be extremely helpful for the second and latter groups of sustainability reporters and their auditors.

Given the challenging implementation timeline defined by CSRD, we hope that the final version of standards will be published within a reasonably short time frame followed shortly by clear implementation guidance to allow the first adopters to prepare themselves to report as of the financial year 2024. In addition, we encourage the Commission to identify the lessons learned from the 2024 application of ESRS swiftly so that first time CSRD reporters over the financial year 2025 can benefit from and leverage the lessons learned by the first group of CSRD-reporters.

Please feel free to contact us if you wish to discuss the contents of this letter.

On behalf of the DASB and Olga Smirnova and Simon Braaksma as co-chairs of the DASB WG Sustainability Reporting.

Yours sincerely,

G.M. van Santen
Chairman of the Dutch Accounting Standards Board

-