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Re: EFRAG Consultation on Exposure Drafts of the European Sustainability Reporting Standards (ESRSs)

Dear Madams,

OIC is pleased to have the opportunity to provide its comments, through the online survey, on the exposure drafts of the European Sustainability Reporting Standards (ESRSs).

We appreciate the work undertaken by EFRAG and its PTF-ESRS to develop the draft of ESRSs, considering the several standards to be prepared, covering all the ESG factors, and the short timeframe to do so. However, we note that the number of EDs in consultation and the timing very tight to provide inputs for all of them have made challenging to ensure a right level of depth and this could impact their quality.

In addition to the filling in the survey, we would like to highlighted the following key points:

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- **Interoperability between the ESRS and the IFRS Sustainability EDs** (survey 1-Q3)
  A precise comparison on the two sets of standards is currently not possible given the state of play of the two initiatives. In fact, only when a comparable regulatory framework will be available in its entirety (where the IFRS Foundation will have published the other topical standards and EFRAG developed the sectoral standards) it will be possible to provide you with an effective and concrete judgment on the coordination and complementarity between the two sets of standards.
  Currently, the comparison is only possible with reference to the general principles and the climate standard, albeit to a limited extent as only the ISSB has already issued sectoral disclosures. The analysis revealed, in addition to the issue of double materiality which however characterizes the European approach, a misalignment regarding other critical profiles such as, for example, rebuttable presumption, cross-references, definition of financial materiality, definition of time horizons, presentation of predefined intermediate targets, the information along the value chain for which the IFRS allows the entity, with regard to scope 3, to omit it in the absence of faithful measure while EFRAG in those circumstances requires anyway for an approximation.
  Differences in the setting, definitions and content between the two sets of standards will imply, at least from large companies, that entities will incur in significant administrative costs.
  The CSRD states in recital 37 that "*To avoid unnecessary regulatory fragmentation that may have negative consequences for undertakings operating globally, European standards should contribute to the process of convergence of sustainability reporting standards at global level, by supporting the work of the International Sustainability Standards Board (ISSB). European standards should reduce the risk of inconsistent reporting requirements on undertakings that operate globally by integrating the content of global baseline standards to be developed by the ISSB, to the extent that the content of the ISSB baseline standards is consistent with the EU's legal framework and the objectives of the European Green Deal*".
  In order to make effective the provision of the recital, a revision of the sector-agnostic standards is necessary to delete those disclosure not expressly required for by specific European regulations.
  We strongly recommend EFRAG and IFRS to closely work together forthwith to ensure the coordination and integration between these standard-setting initiatives must be absolutely pursued. It would not be good for the integration of the markets itself if there were differences such as to make the comparability of information by users complex or even to favor regulatory arbitrage.

- **Granularity of information** (survey 1-Q6 and Q54)
  All the CSRD sustainability topics are covered in the proposed draft standard.
  The information required in the ESRS standards appears very granular and complex. It is also noted that many of the information currently required as optional, for example by the GRI, are proposed as mandatory by the EFRAG standards.
  The granularity and complexity are even more critical due to the lack of sectoral standards whose development would have made it possible to adequately assess

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whether some of the information proposed currently at the sector-agnostic level is instead more relevant for specific sectors.
Therefore, we recommend in this first phase, to limit the mandatory disclosure only to the key information and make the others optional or to provide an adequate phase-in such as to allow the standard setter to consider those requirements in conjunction with the development of the industry standards and the companies to have the time to implement them. Moreover, it will ensure an adequate level of comparability between entities on the key information.
The disclosure requirements that will result more challenging to implement are the ones which exceed the current reporting obligations and for which there is not, at the moment, a shared methodology for the reporting. This is true especially for those DRs which involve a financial estimation for impacts, risks and opportunities related to specific sustainability topics. We would suggest to plan a staggered implementation process, prioritizing those core KPIs, expressly referred to by the law, for which a specific methodology is available (also in order to foster comparability) and postponing those KPIs which are not yet mature for companies to disclose on.

- **Impact Materiality** (survey 1-Q21)
  The impact materiality, which in the EFRAG perspective can also disregard the related financial effects, should be regulated more clearly in the ESRSs.
  In fact, it is necessary to establish whether the driver to assess the materiality of an impact is the relevance for the stakeholder or the relevance for the company. If the intention was to give ample emphasis to the reference that the CSRD makes to public good, and which is taken up in the definition of materiality by EFRAG, the first hypothesis would prevail: ie the relevance for the stakeholder applies.
  Therefore, in this case, a phenomenon that pervasively impacts on a small stakeholder would also be reported, without, in any way, taking into account the size of the entity.
  We observe that this approach, on the one hand, will require an improvement in the conduction of the stakeholder engagement activity and, on the other hand, will inevitably increase the volume of information.
  On the contrary, if the intention was to measure the materiality of an impact on the external environment by relating the event with the size of the company, it is clear that it will be problematic to determine which indicators need to be disclosed and which not.
  In the cross-cutting standard it needs to clarify which of the above-mentioned approaches is to be considered and the criteria to applying them.

- **Financial Materiality** (survey 1-Q22)
  Financial materiality, whether it refers to phenomena captured in the financial statements or to longer-term phenomena that do not meet the criteria to be recognized in the financial statements at the reporting date, should be assessed according to the investor's perspective as defined by the international accounting standards and by the Accounting Directive.
  In fact, the financial materiality in the sustainability report, regardless of whether it derives from a risk (e.g. physical risk) / opportunity or whether it is a consequence of an

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impact that the company generates on the external environment, it is not clear why it should be measured with different criteria than the financial materiality in the financial statements.
An investor can be misled by both omitted or incorrect financial information in the financial statements and omitted or incorrect financial information to be included only in the sustainability report, such as, for example, financial forward-looking information.

- **Rebuttable presumption** (survey 1-Q24)
  We disagree with this approach because it obliges the company to explain, based on reasonable and supportable evidence, because (i) all of the mandatory disclosures of an entire ESRS, or (ii) a group of disclosure requirements related to a specific aspect covered by an ESRS are not material for the undertaking's facts and circumstance.
  In fact, according to the point of view of the preparers, it would be preferable to let the companies defining, according to their own materiality analysis, the information to report rather than having to justify why a matter addressed in the standards is not material. Also considering the burden of applying the rebuttable presumption, companies could choose to provide all the information required by the standards, even if not material, with the risk of obscuring significant aspects.
  More guidance is needed on the application of the "rebuttable presumption" to facilitate entities in the process of considering a non-material topic (see sections on Materiality).
  To make it effective and to leave the "rebuttable presumption" as a residual principle, it would be necessary to limit the number of agnostic KPIs, as already said about the granularity of information, and move most of the KPIs to the sector-specific standards. Indeed, it is more reasonable to require a company to justify why certain aspects considered material for its sector are not significant for the company itself.
  The rebuttable presumption, as proposed in the standards, allows the company not to provide information only in the hypothesis of its non-materiality. However, it is noted that there may be other reasons that justify the entity not providing a particular disclosure.
  In fact, EFRAG itself already allows, with regard to specific aspects (e.g. policy, target, action plan), not to provide disclosure if the entity does not have these elements.
  In this regard, we recommend EFRAG not to limit this faculty to specific cases but to set it as general principle for all disclosures as well as to extend the hypotheses of omission to the further cases currently envisaged by GRI 1.

- **Potential Financial Effects** (survey 1-Q23)
  The financial materiality perspective requires companies to determine the potential financial effects on the position and performance of the company in the short, medium and long term. However, unlike the climate standard, which indicates the specific indicators to be disclosed, in the other environmental standards (pollution, water and marine resources, biodiversity and ecosystems and circular economy) the financial indicators are not defined and any application guidance is provided.
  It should also be noted that the potential information as required by the ESRS refers to timelines that may not always coincide with the time frames of the financial planning of companies.

Since this is a forecast information, and then delicate by definition, it was represented by our stakeholders that the lack of link with the financial planning, which follows a preparatory and approval process by the company, could jeopardize the quality of financial information provided over different time horizons.
For both the observations, given that today, at least from the feedbacks gained from our stakeholders, the companies do not provide such information, we suggest to introduce a phase-in solution and, in any case, to provide that the undertaking discloses qualitative information if providing quantitative information is impracticable to do as already required only for the climate standard.

- **Value chain** (survey 1-Q28)
  The CSRD states that where applicable, the sustainability information shall contain information about the group's own operations, and about its value chain, including products and services, its business relationships and its supply chain.
  Consequently, the ESRS 1 provides that the undertaking's reporting boundary for its sustainability reporting is the one retained for its financial statements expanded to its upstream and downstream value chain. The undertaking's reporting boundary is expanded when the integration of information on impacts, risks and opportunities on matters connected to the undertaking by its direct and indirect business relationships in the upstream and/or downstream value chain is necessary to:
  (a) allow users of sustainability reporting to understand the undertaking's material impacts and how material sustainability-related risks and opportunities affect the undertaking's development, performance and position; and
  (b) produce a set of complete information.
  The draft EFRAG topical standards are built on the relative presumption that the value chain is important for the company in light of the provisions of ESRS 1 and therefore require companies to provide information on impacts, risks and opportunities with reference to both their operations as well as those of their value chain, upstream and downstream.
  Therefore, in this case, at least the following three issues arise:
  1. definition of the subjects to be considered in the value chain;
  2. definition of the information to be acquired from these subjects;
  3. availability and verifiability of the value chain information.

  In the interest of comparability and verifiability of information, it would be desirable that the ESRS defined the criteria to determine the perimeter of the value chain by providing a rationale for it. For example, by delimiting the value chain to significant and stable relationships over time, as proposed in the draft on Corporate Sustainability Due Diligence.
  It should be noted that in the context of the climate, the boundary (in terms of transactions to be considered) of the value chain (scope 3) is already defined by other international initiatives taken as a reference by companies (GHG Protocol), and there are also conversion tables that allow companies to autonomously estimate the scope 3 GHG emissions without the need to obtain such data from counterparties (e.g. customers, suppliers, etc.).

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On the contrary, with regard to the other topical standards (e.g. water, pollution), it is necessary to define more precisely the boundary (which transactions) to be taken as a reference both upstream and downstream. For example, if even in terms of water consumption, in line with scope 3, reference must be made to the relationships of the value chain with the company. It is then necessary to assess whether the company is able to calculate this information independently or needs to request the cooperation of the counterparty. EFRAG standards also stipulate that information relating to the value chain should be approximated if not available. The final text of the CSRD allows, for the first three years from the application of the Directive, not to provide such information if not available. Therefore, the standards should incorporate this transitional provision in line with the final Directive.

EFRAG should consider in the review of the standard if the application of value chain concept would lead to excessive burden. To this regard, EFRAG has to take into consideration the proportional approach adopted by the CSRD final version, in particular when it states that "*standards shall also take into account of the difficulties that undertaking may encounter in gathering information from actors throughout their value chain, especially from those that*" are not subject to the CSRD (art. 29b, par. 2b CSRD).

In general, with reference to the approximation of information in the value chain we believe that it does not reflect the principles of "faithful representation", "comparability" and "verifiability" because it would reflect information not representative for the entity itself. In perspective a flexible approach (e.g. "comply or explain"; omissions set out by GRI) could be considered.

- **Cross-references** (survey 1-Q11)
  We observe that the ESRS 1 para 135 states that elements of information mandated by a disclosure requirement of an ESRS may be incorporated by reference in the sustainability statements to another section of the management report and that incorporation by reference is not allowed from reports other than the management report.
  We understood that the EFRAG approach is providing only cross references within the same document (management report) and we are aware that this can better meet the general principles of completeness and verifiability. However, in order to avoid a duplication of information and too voluminous reports, we strongly recommend to introduce in ESRS 1 the possibility of incorporating information required by ESRSs by reference to the financial statements and other external documents (e.g. pillar 3 ITS disclosures, corporate governance statements) as long as they are made available on the same terms (e.g. digitalisation) and at the same time of the sustainability statement.

- **Social standards – S3 Affected communities** (survey 1-Q47)
  Social standards focus on human rights aspects.
  We note that it is not enough clear in which cases the impact on local communities falls under the environmental standards and when it is in the scope of this standard.
  In this regard, it is noted that in some environmental standards, such as that on pollution and climate change, for the consequences on human rights, reference is made to social

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standards. In others, however, such as that on biodiversity and ecosystems, no reference is made to social standards for these aspects.
Therefore, we suggest that for the same stakeholder the environmental impact is governed by environmental standards and that on human rights is always governed by social standards.

- **Governance standards** (survey 1-Q49 and Q50)
  The final text of the CSRD has limited the governance factors with regard sustainability matters. Therefore, it is appropriate to align the standards on governance ESRS G1 and G2 to the final text of the Directive by deleting disclosure requirements concerning, for example, governance in general.

Should you need any further information, please do not hesitate to contact us.

Yours sincerely,

Angelo Casò
(OIC Executive Board President)

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