EFRAG: European Sustainability Reporting Standards (ESRS)

Talking points for episode 133

These talking points summarise the European Sustainability Reporting Standards (ESRS) released for comment by the European Financial Reporting Advisory Group (EFRAG).

ESRS consists of 2 **cross-cutting standards**, and 11 **topical standards.** The topical standards are split between environmental, social and governance related disclosures. These requirements will consist of a **three layer approach** to capture sector specific disclosures, non-sector specific disclosures and non-standardised reporting.

The **scope of the ESRS** expands the current scope under the non-financial directive. Examples include:

- All **large entities** and all parents of large groups, **regardless of any listing;**
- Large **(as defined by EU accounting rules)** where two of three criteria are met for two consecutive years (i.e. €20M total assets, €40M turnover more than 250 employees);
- Small medium entities, if they are listed in the EU regulated market;
- These rules apply also for subsidiaries of non-EU entities; and
- Reporting would also be required for a **non-EU company** at a global consolidated level on a later timeline if its consolidated net turnover (revenue) generated in the EU exceeds €150 million for each of the last two consecutive fiscal years and also has one of the following:
    - one or more large subsidiaries in the EU or subsidiaries listed on an EU-regulated exchange; or
    - at least one branch that generates revenue of €40 million (about $42 million as of June 30) or more in the preceding year.

The reporting structure used within the cross-cutting standards focuses on **strategy, implementation and performance** measurement. ESRS 1 provides guidance on the application of the fundamental concepts of the CSRD proposal which includes **information quality, double materiality, boundaries and value chain, time horizon and sustainability due diligence**. ESRS 2 contains 22 disclosure requirements covering and providing a common context for all topical disclosure requirements. These requirements are **not rebuttable.**

Double materiality is one of the key concepts introduced in the ESRS, which is different from materiality from a financial reporting perspective. It requires consideration of 1) how the reporting entity is **impacted by** outside factors; and 2) how the reporting entity **impacts its surroundings and its stakeholders**. The rationale is that this will result in more decision useful disclosures. However, it raises challenges for **practical implementation** as there is no defined benchmark or boundary when considering the impact of the business.

Proposed disclosure requirements in the climate exposure draft include the following:

- An analysis of the **resiliency of a company's strategy and business model** in response to climate-related risks.
- A scenario analysis to identify **physical and transition risks** over the **short, medium, and long term**.
- **Performance measures, i**ncluding scope 1, scope 2, and scope 3 greenhouse gas emissions ('GHG') emissions, and GHG emissions per dollar of net revenue (GHG intensity).

The CSRD proposes **mandatory assurance** on reported sustainability information, which will begin with limited assurance, and will expand to reasonable assurance in the future.

The deadline to respond to the comment letter is **8 August**. The draft ESRS is expected to be presented to the European Commission by Q4 of 2022. The first application is expected for FY 2024 reporting.

PwC's June EU Newsletter provides a summary of what you need to know about the EFRAG's exposure drafts.

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