EUROPEAN CENTRAL BANK

EUROSYSTEM

ECB response to the EFRAG's public consultation on the first set of draft European Sustainability Reporting Standards

July 2022

Contents

1 General remarks

The European Central Bank (ECB) strongly supports European Union (EU) efforts to improve sustainability disclosures. As explained in its Opinion[1] on the proposal for a Corporate Sustainability Reporting Directive (CSRD)[2], the ECB welcomes the directive's aim of improving the quantity, quality and reliability of sustainability disclosures in the EU. This is essential to provide investors, policymakers and all stakeholders with the key information to understand and manage the interdependencies of economic activities and the environment and society at large. The ECB welcomes the recent agreement of the co-legislators on the CSRD and urges swift transposition of the directive and timely adoption of the harmonised reporting standards: this legislation is an essential foundation for the EU sustainable finance agenda and is needed for the ECB to deliver on its commitment to include climate change considerations in its monetary policy framework[3]. It is, furthermore, key to properly understanding, measuring, and managing sustainability-related financial risks, thereby supporting the ECB's efforts to ensure the financial sector's resilience to such risks.

The ECB welcomes the progress made by the European Financial Reporting Advisory Group (EFRAG) in developing EU sustainability reporting standards (ESRS). Given the current shortcomings of corporate sustainability disclosures, the ECB supports the development and swift implementation of a common EU reporting standard. A harmonised standard of sufficient quality is key to meaningful, comparable and reliable disclosures that can be externally verified; to be fit for purpose, it should cover the needs of all stakeholders, thereby upholding the "double materiality" concept, and contribute to, and be aligned with, international sustainability reporting initiatives.

The ECB appreciates the good quality of the ESRS drafts. The ECB congratulates the EFRAG on the rapid progress and the significant work achieved within a short time frame. The draft ESRSs are a significant improvement compared with the status quo under the Non-Financial Reporting Directive (NFRD),[4] and broadly address the main information needs from the perspective of the ECB[5]. The standards are generally of good quality: they reflect an appropriate analysis of users' information needs, they provide a significant degree of comparability and verifiability,

---

1 Opinion of the European Central Bank of 7 September 2021 on a proposal for a directive amending Directive 2013/34/EU, Directive 2004/109/EC, Directive 2006/43/EC and Regulation (EU) No 537/2014, as regards corporate sustainability reporting (CON/2021/27) (OJ C 446, 3.11.2021, p. 2).

2 Proposal for a Directive of the European Parliament and of the Council amending Directive 2013/34/EU, Directive 2004/109/EC, Directive 2006/43/EC and Regulation (EU) No 537/2014, as regards corporate sustainability reporting (COM/2021/189 final).

3 See the press release ECB takes further steps to incorporate climate change into its monetary policy operations, European Central Bank, Frankfurt am Main, 4 July 2022.

4 Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups (OJ L 330, 15.11.2014, p. 1).

5 The relevance of sustainability disclosures for the objectives and tasks of the ECB and the Eurosystem is explained in detail in Section 2 of the above-mentioned ECB Opinion on the CSRD proposal.

they are broadly consistent with the data needs stemming from other EU legislation, and, in general, appear fit to deliver on the objectives specified in the CSRD.

The ECB especially welcomes the high ambition of the draft climate standard. Draft ESRS E1[6] provides a promising basis for reliable and comparable climate disclosures that meet the information needs of financial institutions, central banks and supervisory authorities. The ECB appreciates the significant ambition of the standard, which draws on reporting best practices and is consistent with the Paris Agreement goal. The ECB welcomes in particular the reliance on quantitative metrics, the requirements to disclose well-defined forward-looking targets, transition plans in line with the Paris Agreement 1.5 °C goal, Scopes 1, 2 and 3 greenhouse gas emissions (GHG), as well as quantitative estimates of exposures to physical and transition risks. The ECB considers the implementation of the climate standard to be a priority that should not be postponed.

The ECB encourages EFRAG to consider further improvements in some areas. Further efforts to simplify and streamline the architecture would be welcome to improve readability and reduce redundancies. While the ECB is generally satisfied with ESRS E1 (climate change), the disclosure requirements included in the other topical standards would benefit from further prioritisation. Better tailoring the requirements to the sectors for which they are presumed to be material would improve the focus and relevance of the disclosures, while at the same time improving the usability of the topical standards applicable to all undertakings.

The ECB considers that the materiality assessment requires some fine-tuning. The ECB is of the view that climate-related information should always be considered to be material, and the climate standard (ESRS E1) should accordingly be deemed to be material by default to all undertakings. For the other topical standards, a materiality assessment conducted at the level of individual disclosure requirements would be generally preferable to avoid the risk of falling back to the broad-brush comply or explain approach currently in place under the NFRD. However, the level of detail and granularity of the ESRS drafts could make such item-by-item materiality assessment challenging and make disclosures less focused and useful. This reinforces the argument for streamlining the requirements of the (non-climate) topical standards for all undertakings and making them more tailored to specific sectors. In general, the ECB considers that a thorough materiality assessment within a more focused ESRS would be preferable to comprehensive standards that allow too broad discretion in the determination of materiality.

The ECB encourages the development of the ESRS sectoral standards, and in particular the timely development of standards for credit institutions. Here, special attention will be needed to ensure alignment with existing prudential disclosure requirements. The ECB notes that the ESRS will coexist alongside the Pillar III disclosure requirements on environmental, social and governance (ESG) risks for banks that are already in force. To ensure consistency, the ECB strongly encourages EFRAG to closely adhere to the prudential requirements and to avoid

---

6 EFRAG (2022a), ESRS E1: Climate Change – Exposure draft, European Financial Reporting Advisory Group, Brussels, April.

divergences or duplications. Relatedly, special care is needed to ensure that the disclosure requirements for all undertakings provide banks with all the corporate-level information that they require to fulfil their own prudential disclosure requirements.

The ECB emphasises the importance of the global coherence of sustainability disclosures and urges EFRAG and the International Sustainability Standard Board (ISSB) to continue their cooperation to minimise divergences. The development of the ESRS by EFRAG is occurring at the same time as the work of the ISSB on a global baseline. In its opinion on the CSRD, the ECB stressed the importance of global coherence and called on EFRAG and the ISSB to co-construct their respective standards in order to ensure their alignment and compatibility. The ECB welcomes the past and ongoing technical cooperation between the two bodies and appreciates that – as a result of these interactions – the draft climate standards already display a good level of overlap. The ECB calls on both organisations to continue and intensify their bilateral interactions to ensure the closest possible alignment between the two standards. The cooperation between the two standard-setters should be a two-way process driven by genuine effort by both parties towards upward convergence. The ECB expresses its expectation that the final ESRS will be fully interoperable with the ISSB global baseline, avoiding any double reporting. This will be key to minimising any fragmentation of reporting requirements, reducing reporting burdens, and ensuring the availability of consistent sustainability information for all users globally.

The ECB welcomes the opportunity to provide its feedback to the public consultation on the ESRS drafts. The detailed answers to selected questions of the public consultation documents are provided in Section 2.

2 Reply to selected consultation questions

The consultation documents are available at the following link.

2.1 Survey 1A. Overall relevance of the ESRS drafts – Architecture

Cross-cutting and topical standards

2.1.1 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?

The ECB generally supports the overall architecture of the cross-cutting, topical, and sectoral standards. At the same time, it notes that the internal structure of the draft ESRS is complex and results in some redundancies. Overlaps notably exist between the cross-cutting ESRS 2 and the requirements related to “General, Strategy, Governance and Materiality assessment” and “Policies, targets, actions and action plans” within each of the topical standards. While a degree of duplication may be justified in specific cases, especially for ESRS E1 (Climate change), to ensure close alignment of the sectoral standard with international initiatives (notably with the framework set by the Task Force on Climate-related Financial Disclosures (TCFD) and the ISSB climate standard), the ECB encourages further efforts to streamline the architecture by consolidating the above-mentioned requirements in ESRS 2 whenever possible. In general, where there are overlaps, the overall usability and simplicity of the ESRS as a whole should take precedence over a scrupulous subdivision of the requirements by topic.

The ECB supports a clearer articulation between disclosure requirements and application guidance. All normative requirements, including sub-requirements, should be presented together in the main body of the ESRS. The application guidance should not generate additional requirements on top of those presented in the main text, but rather be limited to explanations, reporting recommendations, and voluntary guidance.

Greater reliance on sectoral standards would help focus and streamline the disclosure requirements and ease the process of adoption. The ECB considers that the articulation between topical and sectoral standards could be improved: in particular, several of the disclosure requirements currently included in the (non-climate) topical standards could be better tailored to the specific sectors based on the presumed materiality of the requirements across sectors. See the answer to Q6 below (Section 2.1.4).

Alignment and interoperability with international standards and frameworks

2.1.2 Q2: in your opinion, to what extent is the TCFD framework of reporting areas (governance, strategy, risk management and metrics/targets) compatible with the structure of the ESRS?

The ECB appreciates that all elements of the TCFD framework are present in the ESRS but would see merit in minimising divergences in the architecture*.* The ECB welcomes the fact that the TCFD framework is fully integrated within the ESRS but notes that the proposed architecture results in elements of the TCFD framework being spread across the various standards rather than presented in a singular location in their conventional format[7]. For example, several requirements related to governance are located in ESRS 2 (e.g. requirements GOV 1 on the roles and responsibilities of the governance bodies, or GOV 4 on climate-related remuneration), as well as in ESRS G1 (e.g. processes for identifying, assessing, and managing climate-related risks). While it is acknowledged that a trade-off exists between complete alignment with the TCFD framework and the need to avoid duplications in the ESRS structure, the ECB would see merit in avoiding substantial departures from a climate disclosures format that has become widely adopted by companies and financial institutions and has become familiar to both users and preparers. The ECB invites EFRAG to further align the ESRS architecture, and particularly ESRS E1 on climate change, with the TCFD recommendations. This would also facilitate alignment of the ESRS with the ISSB climate standard.

2.1.3 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?

The ECB welcomes the past and ongoing technical cooperation between the ISSB and EFRAG and calls on both organisations to continue and intensify their bilateral interactions to ensure the closest possible alignment between the two standards. In its legal opinion on the CSRD proposal[8], the ECB called for coordinated global efforts to converge with common global transparency and disclosure standards, in particular with the International Financial Reporting Standards (IFRS) Foundation's proposal. The ECB expresses the expectation that the cooperation between EFRAG and the ISSB should result in as close an alignment as possible between the two standards, while remaining mindful of the fact that the EFRAG standard is, by design, broader, given its double materiality

7 As summarised in EFRAG (2022b), Draft European Sustainability Reporting Standards: Appendix IV – TCFD recommendation and ESRS reconciliation table, Cover note for public consultation, European Financial Reporting Advisory Group, Brussels, April.

8 See the Opinion of the European Central Bank of 7 September 2021 on a proposal for a directive amending Directive 2013/34/EU, Directive 2004/109/EC, Directive 2006/43/EC and Regulation (EU) No 537/2014, as regards corporate sustainability reporting (CON/2021/27) (OJ C 446, 3.11.2021, p. 2).

perspective. The cooperation between the two standard-setters should be a two-way process whereby both the EFRAG and ISSB learn from each other and adjust their respective standards with the aim of achieving a mutually beneficial process of upward convergence.

The ECB appreciates the good degree of overlap already achieved between the initiatives. In particular, the ECB welcomes the fact that all the requirements in the ISSB climate standard (IFRS S2) are reflected, often with more granular guidance and detail, in the corresponding requirements in the EFRAG standard (ESRS E1). This high level of correspondence is essential to ensure that compliance with the EU standards also secures compliance with the (narrower) ISSB disclosure requirements. This high level of correspondence should be reflected at the granular level of each individual reporting requirement to entirely avoid the risk of double reporting.

The ECB is, however, concerned by certain inconsistencies between the two climate standards, most notably in relation to the definition of GHG emission reduction targets, transition plans and the use of offsets: in these instances, the EFRAG standard displays greater ambition than the ISSB standard. In line with the ECB's expectation of a mutually beneficial process of upward convergence, the ECB encourages the ISSB to benefit from the advanced requirements set out in the ESRS. On the other hand, the ECB encourages EFRAG to draw from the ISSB's (IFRS S2) example in terms of the high degree of transparency as regards how physical and transition risks are estimated.

The ECB appreciates EFRAG's efforts to demonstrate the current level of interoperability by providing a reconciliation table[9]. The ECB considers it to be of the utmost importance that – where full alignment is not possible, or desirable, between the ESRS and the ISSB and standards – a clear reconciliation table is provided to users to enable interoperability and avoid double reporting. To ensure mutual recognition of interoperability, the ECB invites EFRAG and the ISSB to cooperate in mapping the ESRS requirements against those of the ISSB draft standard. This could provide a consensual basis for mutual recognition of (parts of) the ISSB and the ESRS.

Consideration given to EU policies and legislation

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

The ECB welcomes the efforts made to ensure alignment of the ESRS with the information requirements stemming from EU legislation. The ECB strongly supports the CSRD's stated goal of ensuring the consistency of the sustainability

[9] EFRAG (2022b), Draft European Sustainability Reporting Standards: Appendix IV – TCFD recommendation and ESRS reconciliation table, Cover note for public consultation, European Financial Reporting Advisory Group, Brussels, April.

reporting standards with the requirements set by other EU legislation, and welcomes the efforts made by EFRAG to align the ESRS with – among others – the proposed Corporate Sustainability Due Diligence (CSDD) Directive,[10] Sustainable Finance Disclosure Regulation (SFDR)[11] and the EU Taxonomy.[12]

The ECB welcomes the close alignment of the ESRS with the SFDR. The first set of ESRSs that are the subject of this public consultation already incorporate the SFDR Principle Adverse Impacts (PAIs)[13] that are applicable to all undertakings. The ECB also welcomes the intention to implement the remaining PAIs, which only apply to certain sectors (e.g. the PAIs applicable solely to real-estate investments), in the forthcoming sectoral standards. Information needed by the financial market participants is generally easy to identify in the ESRS, and this will enable the financial institutions to fulfil their reporting obligations under the SFDR.

Given the reliance of Taxonomy disclosures on self-reporting, ESRS disclosures are not necessary, in principle, to meet the information needs of the EU Taxonomy. For non-financial companies, the assessment of Taxonomy alignment (including both compliance with the technical screening criteria (TSCs), as well as with the do-no-significant-harm (DNSH) criteria) is intended to be a granular activity-level exercise to be carried out by companies themselves, based on their internal information and accounting systems. This means that for corporates to be able to fulfil their disclosure obligations under the EU Taxonomy, corporate-level information from the ESRS is, generally, not necessary, although the two efforts are complementary and may support each other. Since financial institutions are dependent on the EU Taxonomy values self-reported by their investee/counterpart companies to inform their own reporting, there would seem to be no residual corporate-level information needs that should be met by the ESRS[14].

Further analysis is, however, needed to assess whether assessment of Taxonomy alignment may in some cases require additional corporate-level information. The ESRS may nonetheless be relevant for Taxonomy disclosures where the activity-level self-assessment of alignment with the TSCs or DNSH criteria relies on information obtained from the value chain or, more generally, from

---

10 Proposal for a Directive of the European Parliament and of the Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937 (COM/2022/71 final).

11 Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector (OJ L 317, 9.12.2019, p. 1).

12 See Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088 (OJ L 198, 22.6.2020, p. 13) and its delegated acts.

13 See EFRAG (2022c), Draft European Sustainability Reporting Standards: Appendix III – SFDR Principle Adverse Impacts Indicators in the ESRS, Cover note for public consultation, European Financial Reporting Advisory Group, Brussels, April.

14 The issue is more complex when financial institutions may produce Taxonomy disclosures for companies not within the scope of the Taxonomy regulation. There are three such cases: (a) the SFDR Regulatory Technical Standards, which make it possible to use 'equivalent information' for assessing the Taxonomy alignment of financial products issued by non-EU companies or by EU SMEs; (b) the Banking book Taxonomy Alignment Ratio (BTAR) in the Pillar III disclosure requirements for banks, which allows banks to use estimates for those counterparties that do not have Taxonomy disclosure obligations; and (c) voluntary disclosures, which have no restrictions on the use of estimates (that rely on publicly available corporate-level information). While these generate information needs at the corporate level that will need to be met somehow, the ESRS would not seem be the solution in these cases, since the scope of the ESRS is the same as that of the Taxonomy Regulation, and hence does not overlap with the set of non-EU companies, and out-of-scope SMEs.

companies other than the reporting entity itself. The ECB encourages EFRAG (supported by the Platform on Sustainable Finance) to conduct a careful analysis of all the sectoral TSCs and DNSH criteria to ensure that such indirect information is available to undertakings and hence that the self-assessment of Taxonomy alignment is not impaired. Additionally, some investors (e.g. those subject to the SFDR) may be interested in assessing the degree of Taxonomy alignment of securities issued by entities that are outside the scope of entity-level Taxonomy disclosures: in such cases, additional entity-level information, e.g. on DNSH and minimum social safeguards, might support this exercise. Where gaps are identified, there may be scope for the ESRS to fill the gap.

Greater alignment is required between the ESRS and the information that credit institutions need in order to be able to fulfil their prudential disclosure requirements. The ESRSs currently do not allow credit institutions to obtain all the information they need from corporates in order to fulfil their own requirements under the Pillar III disclosures of ESG risks[15]**.** Several gaps have been identified in this regard:

- The implementing technical standard (ITS) on Pillar III disclosures requires eligible institutions to report alignment metrics, defined as emission intensity per unit of production (varying depending on the sector), while the ESRS E1 currently only requires the disclosure of GHG intensity per net turnover. The ECB expects these sector-specific GHG intensity metrics to be specified in the forthcoming sectoral standards and urges EFRAG to carefully consider the Pillar III ITS in developing them.
- The ITS requires financial institutions to disclose information about the energy performance certificates and energy consumptions of the collateral they are financing. Such information is not specifically requested in the ESRS for commercial facilities. The ESRS E1 could include additional requirements for companies to disclose this information for the real-estate assets they own, or relevant subsets thereof.

Coverage of sustainability topics

2.1.5 Q6: in your opinion, to what extent does the proposed coverage of set 1 adequately address CSRD sustainability topics?

The drafts adequately cover all relevant reporting, but the non-climate topical standards would benefit from further prioritisation and more sectoral tailoring. The ECB welcomes the fact that the draft ESRSs cover all relevant sustainability topics. Given the urgency of climate change and the need to obtain reliable and climate information on climate-related impacts and risks, the ECB considers the

[15] See EBA (2022), Final draft implementing technical standards on prudential disclosures on ESG risks in accordance with Article 449a CRR (EBA/ITS/2022/01), European Banking Authority, Paris, 24 January.

ESRS E1 to be a priority and welcomes the good maturity and ambition of the climate standard. For the other topical standards, however, the ECB considers that further streamlining and prioritisation would be warranted: while climate change can be deemed material for all undertakings, and hence the related disclosure requirements are appropriately located in a topic standard applicable to all entities, the nature of the other sustainability topics would call for a more differentiated approach.

In particular, the disclosure requirements currently included in the (non-climate) topical standards could be better tailored to the specific sectors based on the presumed materiality of the requirements across sectors. This could be done either by assisting the materiality assessment for these topics by providing for each sector a list of the reputed material disclosure requirements (i.e. a sector-by-sector mapping of the presumed materiality of the various topical standards or sections), or, alternatively, by moving some of the requirements that are currently mandatory for all undertakings to the sector-specific standards, based on the materiality of the topic for each sector. Such prioritisation would significantly improve the usability of the ESRS, ease its adoption and minimise the incentive for box-ticking exercises that might dilute the usefulness and focus of sustainability disclosures.

Sustainability statements and the links with other parts of corporate reporting

2.1.6 Q8: Do you agree with the proposed three options to organise the information within the management report?

The options for how to organise information, as outlined in paragraphs 148 and 149 and the related guidance, seem to be appropriate when considering the aim of making information easily identifiable for the users of the report. With the goals of transparency and ease of use in mind, the use of location tables is welcomed for all the proposed options with a view to facilitating the identification of relevant sections of the disclosures for different stakeholders. The use of incorporation by reference with other sections of the management report (paragraphs 135 and 136) and with the financial statements (Chapter 5.2) is supported and the location tables could help with navigating the different documents. With a view to ensuring that the reporting principles of relevance and comparability are enforced, consideration should be given to how to best deal with static information (e.g. on policies and governance structures), balancing the need for it to be accessible to users and, at the same time, reducing repetitions within the sustainability reports and over time.

Digitisation of the ESRS should be considered as a matter of priority to enable rapid access and analysis, ideally already from the first year of reporting. In order to ensure understandability and comparability of sustainable information, including in relation to other parts of corporate reporting, the ECB encourages explicit reference to the application of a common machine-readable structure and format. Harmonised reporting templates would facilitate fulfilment of the various reporting obligations by undertakings and, consequently, increase the value and comparability of reported information for all users. In this regard, the ECB welcomes the preliminary attempt in the Basis for Conclusions on the ESRS E1, to provide data in a homogeneous reporting format via a digitally tagged taxonomy.

The ECB encourages EFRAG to further collaborate with the European Securities and Markets Authority in order to ensure that sustainability information reported under the ESRS will be readily available in the future European Single Access Point (ESAP). Company disclosures are expected to eventually be accessible and easily comparable through the ESAP proposed by the European Commission. For the ECB's work on sustainability issues, it is of the utmost importance to be able to access quantitative disclosures on sustainability in a user-friendly manner. Moreover, regarding disclosure by banks, the ECB is interested in participating in the collection chain, following the same rules as in place for other regulatory information. However, it is not clear whether the disclosures will be collected using the established decentralised channel for regulatory reporting, i.e. via national central banks (and/or national competent authorities) and the ECB. This is particularly relevant if the ECB to be able to access and analyse these disclosures during the phase-in period.

2.2 Survey 1B. Overall relevance of the ESRS drafts – Implementation of CSRD principles

Double materiality

2.2.1 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?

The ECB welcomes the identification of double materiality as a key principle for the identification of sustainability information for all stakeholders. In its opinion on the CSRD, the ECB stated that the EU sustainability standards should require companies to disclose not only issues that influence enterprise value, but also information on the company's broader environmental and social impact ("double materiality"). However, the ECB encourages more explicit guidance on the methodological approach to be applied in the materiality assessment exercise (e.g. in ESRS 1, paragraph 58) to allow for comparable results across organisations. This could also be complemented by guidance or reference documents, for example at sector-specific level. More clarity could be provided on the expected stakeholder engagement in the materiality assessment process. As the current phrasing under ESRS 1 seems to point to a significant degree of flexibility in the granularity of the materiality assessment, it could be made even more explicit that all topical standards ESRS are to be considered material unless the materiality exercise proves the contrary for all the disclosure requirements included therein. Nevertheless, to support a sound and thorough materiality assessment, it is proposed that further streamlining of the disclosure requirements be considered so that stakeholders could assess the sustainability performance of organisations based on relevant key indicators. Improved prioritisation in the topical standard could then be complemented, where needed, through the sectoral standards.

(Materiality) Rebuttable presumption

2.2.2 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?

The climate standards (ESRS E1) should always be deemed material. As the activity of every undertaking contributes to greenhouse gas emissions, and hence affects climate change to some degree, the ECB is of the view that – at least from an impact materiality perspective – climate-related information should always be seen as material; hence, the climate standard (ESRS E1) should be deemed material for all undertakings, by default, without the possibility of opting out, as is the case for cross-cutting standards.

The ECB supports a sound materiality assessment. As explained in the general remarks, the ECB would explicitly support a requirement for the materiality assessment to be conducted at the level of individual disclosure requirements, without the possibility of opting out of whole topical standards. Such an approach would minimise the risk of falling back to the broad-brush comply or explain approach currently in place under the NFRD, and would compel undertakings to carefully reflect on all their possible impacts and risks. It would also be more aligned to the approach used for financial reporting. However, the current level of detail and granularity of the ESRS drafts could make such an item-by-item materiality assessment challenging and make disclosures less focused and useful. This reinforces the argument presented in Q6 above (see Section 2.1.4) for the streamlining and better prioritisation of the requirements of the (non-climate) topical standards. In general, the reporting burden of entities should be addressed through an appropriate prioritisation of the relevant disclosure requirements, rather than by relaxing the terms of the materiality assessment. A thorough materiality assessment coupled with a more focused ESRS would seem preferable to comprehensive standards that allow too broad a discretion in the determination of materiality.

Time horizon

2.2.3 Q31: do you think it is relevant to define short-, medium- and long-term horizon for sustainability reporting purposes?

The ECB welcomes the clear definition of short (one year), medium (two to five years) and long (more than five years) term for sustainability reporting purposes. The ECB encourages international alignment of those definitions and calls on EFRAG to cooperate with the ISSB to also reflect these choices at the international level. It is also noted that ESRS E1 includes several references to the possibility of adopting different definitions, but this seems inconsistent with the general definition of time horizon provided in ESRS 1 (e.g. "it shall explain how it has defined short-, medium- and long-term time horizons" in ESRS E1 AG17, AG30(a), AG71(b), AG80(b)), and is not in line with a truly prescriptive approach.

2.3 Survey 1C. Overall relevance of the ESRS drafts – Content

Overall content of the draft standard on climate change (ESRS E1 – Climate change)

2.3.1 Q40: Please rate what you think of ESRS E1 – Climate change

The ECB especially welcomes the high ambition of the draft climate standard. As explained in the general remarks, the draft ESRS E1 provides a promising basis for reliable and comparable climate disclosures that meet the information needs of financial institutions, central banks and supervisory authorities. The ECB appreciates the significant ambition of the standard, which appears commensurate with the urgency and scale of the climate challenge. The level of ambition appears appropriate to contribute to climate action consistent with the Paris Agreement objective and the EU climate goals. The ECB welcomes the fact that the draft climate standard draws on reporting best practices and goes significantly beyond the requirements under the NFRD, by requiring quantitative indicators that exceed the qualitative nature of existing disclosures. The ECB also appreciates the fact that the draft standard incorporates the 2019 Guidelines on reporting climate-related information[16], and in turn incorporates the key elements of the TCFD framework. The ECB welcomes in particular the reliance on quantitative metrics, the requirements to disclose well-defined forward-looking targets (with absolute targets), transition plans in line with the Paris Agreement 1.5 °C goal, Scopes 1, 2 and 3 GHG emissions, as well as quantitative estimates of exposures to physical and transition risks. More

[16] See EC (2019), "Guidelines on reporting climate-related information", *Banking and Finance*, European Commission, Brussels, June.

detailed comments on the individual disclosure requirements of ESRS E1 are provided in Section 2.5 below. The ECB considers the implementation of the climate standard to be a priority that should not be postponed.

In view of the development of the forthcoming sectoral standards, climate disclosures for the financial sector are especially relevant and, in this regard, financed emissions should be part of the requirements. At the same time, the broad range of existing GHG emissions allocation methodologies could hinder the comparability of the figures that are disclosed by each entity. As stated in the Basis for Conclusions on ESRS E1, the Partnership for Carbon Accounting (PCAF) standard builds on the GHG Protocol rules and is already widely used in the financial industry. The ECB hence welcomes the fact that the ESRS E1 already includes a reference to PCAF in Application Guidance 48(b) in relation to the disclosure of GHG emissions: the inclusion of this guidance in the cross-sectoral standard is necessary to provide financial institutions with the necessary guidance on how to calculate their Scope 3 financed emissions. Looking ahead, the ECB supports the explicit reference to the PCAF methodology for the calculation of financed emissions in the development of the forthcoming sectoral standards for the financial sector, while being mindful that this approach stills allows for some flexibility, notably as regards Scope 3 financed emissions. It would be useful, in this regard, to complement the headline figure with a disclosure of the share of GHG financed emissions that are based on reported emissions (collected directly from the borrower or investee company) and those that are estimated, together with an indication of the methodology used for that estimation.

Overall content of the draft standards on other environmental topics

2.3.2 Please rate what you think of (ESRS E2 – Pollution; ESRS E3 – Water and marine resources; ESRS E4 – Biodiversity and ecosystems; ESRS E5 – Resource use and circular economy)

Climate change and other environmental topics such as biodiversity, pollution, water and use of resources are inextricably linked; the ECB deems it important to adopt an integrated approach to these threats. The recent work of the Central Banks and Supervisors Network for Greening the Financial System (NGFS) shows that nature-related risks, including biodiversity loss, could have significant macroeconomic implications[17]. Failure to account for, mitigate, and adapt to these implications is a source of risks relevant to financial stability. In this regard, the ECB considers the ESRS standards on environmental topics to be a significant advance. It is recalled, in this context, that in the ECB Guide on climate and environmental

[17] NGFS (2022), Statement on Nature-Related Financial Risks, Network for Greening the Financial System, Paris, 24 March.

risks[18], Expectation 13.7, already states that financial institutions are expected to comprehensively evaluate any further environmental risk-related information, such as water stress, biodiversity loss, resource scarcity and pollution, that is needed to convey their risk profiles. The ESRS will support the production of this data, which is very much welcomed, thereby enabling financial institutions to collect the relevant information required to produce the expected supervisory indicators.

Coherence and interoperability with the ongoing international initiatives is of the essence. The development of nature-related risks disclosure frameworks has gained momentum, with multiple initiatives currently working on these topics: the ISSB, the Global Reporting Initiative revision of its biodiversity indicators, the Taskforce for Nature-Related Financial Disclosures framework (TNFD), the Science Based Targets Network guidance. In the light of this, the ECB praises the collaborative efforts already made by EFRAG and the TNFD. In the medium term, the ECB expresses the expectation that consistency between the initiatives should be ensured. The ECB encourages EFRAG to make nature-based risk concepts more accessible to companies. To this end, it recommends applying the TNFD approach of adopting a set of core definitions/concepts mirroring the approach well-known for climate (e.g. Scopes 1-3, science-based targets, etc.). To ensure alignment with international initiatives, the ECB advocates an ad hoc update of ESRSs E2-5 before the scheduled three-year maintenance period in order to take into account the outcome of global initiatives, such that of the TNFD.

2.4 Survey 2. ESRS implementation prioritisation/phasing-in

ESRS implementation prioritisation/phasing-in options

2.4.1 Q57: please share any other comments you might have regarding ESRS implementation prioritisation/phasing-in

The ECB is not in favour of a gradual phase-in or tiered approach, but should a prioritisation prove necessary, the ECB considers the climate standard to be of the utmost priority. The ECB recognises that starting with the ESRS requirements may be difficult for new preparers. However, the ECB subscribes to the view expressed in the CSRD that sustainability reporting should be recognised as having the same level of importance as conventional financial reporting. Should a prioritisation ultimately prove to be necessary to ease the process of adoption, the ECB would highlight two conditions to be considered. First, given the urgency of addressing climate change, and given that climate reporting is by far the most mature topic for the global sustainability reporting initiatives, the ESRS E1 as a whole should be the absolute priority, and should not be postponed under any circumstance. Second, all disclosure requirements already linked to current EU

[18] ECB (2020a), Guide on climate-related and environmental risks: Supervisory expectations relating to risk management and disclosure, European Central Bank, Frankfurt am Main, November.

legislation (e.g. the SFDR, EU Taxonomy, the accounting directives, the Seveso directives on dangerous substance hazards) and requirements present in global initiatives (i.e. TCFD, ISSB, etc.) should be included from the first reporting exercise.

The ECB considers that the update of the standards should be carried out before the three-year timeline set in the CSRD in order to reflect the rapidly changing sustainability disclosure environment. Ad hoc updates could notably take place after finalisation of relevant EU legislation that affects, or depend on, the CSRD disclosure requirements, or to take into account the outcome of global initiative such as the Taskforce on Nature-related Disclosures (TNFD) for the ESRSs E2-5.

2.5 Survey 3B. Adequacy of Disclosure Requirements – Climate Standard

2.5.1 Transition plan for climate change mitigation (DR E1-1)

The requirement to disclose transition plans for climate change mitigation is of critical importance to ensure that corporate sustainability efforts are aligned with the goal of limiting global warming to 1.5 °C in line with the Paris Agreement. For financial institutions specifically, the requirement also provides a proper complement to the requirement under the proposed Capital Requirements Directive (CRD) VI[19] for banks to understand the risks of misalignment with respect to the EU transition pathways. For such a requirement to be effective, it is important to ensure that transition plans provide comparable information in order to ensure that stakeholders can understand the differences in the underlying plans. In this respect, the requirement to clearly disclose the alignment benchmark (e.g. the pathway) underlying the plans of the undertaking concerned is particularly welcome and would facilitate the monitoring of progress by all stakeholders. In addition, the quality of the plans is directly linked to the possibility of monitoring and measuring short, medium and long-term targets: targets and metrics are the only possible way to assess these plans when it comes to actions and strategic objectives. See next paragraph for more detailed comments on targets.

The ESRS transition plan requirement should provide a single harmonised framework that is consistent across EU legislation. The ECB supports the adoption of a common transition plan methodology in the CSRD that would provide a harmonised template for all the related requirements in the CSDD Directive and (depending on the final agreement of the co-legislators) the European Green Bond standard. The elements in the EFRAG draft standard provide a good basis for this: the ECB holds that such transition plans should make it possible to draw a clear and direct assessment and comparison of a company's GHG emission reductions and

---

19 Proposal for a Directive of the European Parliament and of the Council amending Directive 2013/36/EU as regards supervisory powers, sanctions, third-country branches, and environmental, social and governance risks, and amending Directive 2014/59/EU (COM (2021) 663 final).

their alignment with a 1.5 °C trajectory, as well as of the decarbonisation levers proposed/the key actions planned, the financial resources that support implementation of the transition plan, the non-reliance of target achievement on carbon credits, the locked-in emissions from key assets and products, and the alignment with overall business strategy.

2.5.2 Measurable targets for climate change mitigation and adaptation (DR E1-3)

The ECB welcomes the disclosure of measurable targets, which are key to ensuring the disclosure of comparable and reliable forward-looking data. The suggested disclosure standards provide sufficiently precise guidance for firms to report their forward-looking targets. At the same time, the scope of these targets, in terms of activities, geographical regions and subsidiaries covered, should be fully aligned with the disclosures on backward-looking metrics, in particular those on GHG emissions (E1-7 to 10). Similarly, the methodology of Scope 2 emission targets should be aligned with the methodology in E1-8, which requires the disclosure of location *and ma*rket-based emissions rather than either of the two.

The frequency of updating forward-looking targets needs to be further clarified and the reference period should be stable over time. The disclosure requirements in paragraph 24(d-e) specify that firms should update the base year and its targets in five-year rolling windows. However, it is not clear whether this implies that firms should update their targets every year with a new five-year forward-looking horizon and a new base year, or whether they should update their base year and targets every five years. The former would lead to a multiplicity of several vintages of previous targets, which would complicate ex post performance measurement. Furthermore, the standards allow for a degree of flexibility so that three-year averages can be used for the base year in order to limit the impact of idiosyncratic events in the base year. While this is welcome to enable meaningful comparisons across time, firms should be consistent in the computation of their base year over time to avoid arbitrary adjustments to the base-year calculation.

Progress that occurred before the entry into force of the ESRS should not be penalised. In this regard, the inclusion of reference to past progress referred to in AG29(c) is welcome and could be further strengthened, given that the disclosure requirements should carefully mitigate both the risk of penalising first movers (i.e. undertakings that have already undergone a deep decarbonisation effort) and of undertakings postponing action to follow more ambitious decarbonation pathways within the new five-year reporting time frames (e.g. by having a higher baseline year).

The disclosure of intensity-based targets should be mandatory and should be complemented with industry-specific output-based intensity metrics in the sectoral standards. The disclosure requirements in paragraph 24(b) focus on the target setting for absolute GHG emissions and only mention the disclosure of intensity values as optional (“if meaningful”). Absolute emissions, however, depend on the total production of a firm, and therefore not only reflect the carbon intensity of production but also the expected growth of the company in the target period. Requiring instead the disclosure of intensity-based metrics would make it possible to abstract from this growth component and might help with comparison of efforts to decarbonise production in the target period across undertakings with different growth trajectories. While the disclosure of turnover-based carbon intensity seems appropriate for the cross-cutting ESRS E1, the ECB considers it to be of key importance, that this horizontal metric be complemented, in the sectoral standards, by industry-specific intensity metrics based on industry-specific outputs.

2.5.3 GHG emissions (Scopes 1, 2, 3) (DR E1-7 to 9)

The ECB welcomes the inclusion of the disclosure requirements on GHG emissions (E1-7 to 9) and the reference to existing reporting standards, such as the GHG Protocol. In order to facilitate the comparability of the emissions' disclosures, information on the Scope 3 boundary could be reported in a tabular format, matching the 15 Scope 3 categories listed by the GHG Protocol Corporate Standard, as reiterated under AG 48(b). This table could also be used to incorporate information on data quality, especially for Scope 3 (e.g. the uncertainty assessment), and to add information vis-à-vis reported data and approaches for the various Scope 3 categories. Every effort should be made to avoid the disclosure requirements discouraging companies from expanding their reporting boundaries in order to report lower emissions (e.g. reporting only on the minimum boundary). It is also to be noted that certain organisations also report on factors that go beyond the greenhouse gases listed under paragraph 4 of the objective section of ESRS E1, such as the Radiative Forcing Index for air-travel-related emissions; it might therefore be helpful to require information on the methodology in order to favour the comparability of different inventories. As undertakings may be using proprietary emission factor databases or data provided by third parties for Scope 3 emissions, they may not be in a position to fully comply with AG43(d) and (e).

The ECB welcomes the reference to the use of the Partnership for Carbon Accounting (PCAF) standards for financial institutions to calculate Scope 3 emissions. Under these standards, financial institutions should report borrowers' and investees' absolute Scope 1 and Scope 2 emissions across all sectors. For reporting borrowers' and investees' Scope 3 emissions, the PCAF follows a phased-in approach, which requires Scope 3 reporting for lending to, and making investments in, companies based on the sector in which they are active (i.e. where they earn revenues). The phased-in approach applies the list of sectors established by the EU Technical Expert Group on Sustainable Finance (EU TEG)[20] ranging from 2021 to 2026. Considering the high relevance of those Scope 3 emissions within the total financed emissions, it would be beneficial, in terms of harmonisation of reporting, if the ESRS standards were to include a view on those Scope 3 financed emissions and related proposed phase-in. The PCAF standards also state that, for

[20] Included in Article 5 of the Supplementing Regulation (EU) 2016/1011 of the European Parliament and of the Council as regards minimum standards for EU Climate Transition Benchmarks and EU Paris-aligned Benchmarks.

sectors where Scope 3 emissions reporting is required, financial institutions should separately disclose these absolute Scope 3 emissions, including for the specific sectors covered. Separate reporting ensures full transparency, while acknowledging potential double-counting issues when these emissions are added to the borrowers' and investees' Scopes 1 and 2 emissions. In view of the foregoing, the inclusion in the ESRS of a specific requirement to disclose the Scope 3 financed emissions separately would make it possible to gain a better understanding of the potential methodological differences across financial institutions.

2.5.4 GHG removals in own operations and the value chain and GHG mitigation projects financed through carbon credits (DR E1- 12, 13)

The ECB appreciates EFRAG's approach on reporting carbon removals and offsets separately from disclosures on targets. The ECB agrees with the adopted view that the GHG emission reduction targets should be disclosed gross without offsetting. The ECB considers that reporting on progress against the target including carbon offsets would make the GHG emission targets less transparent, possibly misleading, and generally less credible. Offsets are widely considered as only imperfect substitutes for actual GHG emission reductions. The use of offsets should be understood as being a residual complementary measure that should not take precedence over, or distract attention and resources from, tangible efforts to reduce emissions. The proposed approach is appropriate to prioritise mitigation efforts, as well as to enhance the comparability of targets and transition plans. When disclosing separately, only certified carbon removals and offset should be accepted under these disclosure requirements to avoid double-counting and ensure additionality.

2.5.5 Potential financial effects from material physical and transition risks (DR E1-15, 16)

The ECB welcomes the requirement to disclose the potential financial effects arising from physical and material risks and the quantitative assessment of the potential effect on assets and liabilities. This requirement will help investors to gain a better understanding of the relevance of these physical and transition risks for a company. To achieve this goal, however, it is important for companies to also disclose the specific risk drivers of potential losses for each of the assets and liabilities that could be affected by transition or physical risk, as well as an estimation of the expected likelihood of losses arising from the different risk drivers and the time horizon in which these losses might be realised. For example, a company might be subject to transition risks arising from a specific regulation in its sector, as well as from a possible increase in carbon price. Where that is the case, the company should specify, for each risk driver, the potential effect on assets, liabilities and turnover, the likelihood of occurrence, and when these effects might materialise, given that all these might differ for different risk drivers.

The ECB appreciates the reference scenarios provided for the assessment of physical and transition risks, and would welcome more normative guidance on the recommended scenario and increased transparency regarding the choices made by preparers. The application guidance given in AG 17 to 19 provides useful instructions on the use of scenarios, and the ECB welcomes the concrete examples provided to inform the estimation of transition and physical risks. The ECB recommends narrowing down the list of those examples and providing more normative guidance on the application of scenarios, as well as ensuring consistency with the NGFS scenarios widely used by financial institutions and by the ECB and other central banks. In particular, the ECB considers that a high-risk scenario, such as IPCC SSP5 8.5, is the appropriate choice for physical risks and would be consistent with a precautionary principle. For transition risks, on the other hand, it would be appropriate to use a scenario consistent with the Paris Agreement, such as the International Energy Agency net zero emissions by 2050 scenario (which serves as a reference for the EBA ITS on Pillar 3 disclosures) or the IPCC SSP1 1.9. It is also of the utmost importance that corporates ensure transparency in terms of scenario selection (or lack thereof) and related sensitivities. Consequently, the ECB would recommend that mandatory narratives on the reasons for the selection of a certain scenario be added to the explanation requirement on "whether and how". The ISSB climate standard (see Paragraph 15 in ISSB S2) serves as good practice in this regard and ESRS E1 should be closely aligned to this standard.

2.5.6 Potential financial effects from climate-related opportunities (DR E1-17)

We would encourage efforts to ensure that the standards also provide an adequate level of disclosure of opportunities, making it possible to identify concrete actions and financial benefits deriving therefrom while limiting the risk of overemphasising symbolic actions. Disclosure of opportunities could provide important information on the business model and strategy of companies, as well as on their resilience to transition to a sustainable economy: if well-articulated, disclosure of opportunities should enable preparers to provide quantitative estimates of the financial benefit of early sustainability action. However, such disclosures must be well structured and properly substantiated in order to avoid this requirement being used to overemphasise symbolic action to compensate for more material downside risks. The ECB Banking Supervision, while conducting its assessment on banks' progress towards transparent disclosure of their climate-related and environmental risk profiles, has observed a tendency to extensively report on opportunities rather than on risks[21]. There has been some disconnect between banks' perception of the importance of climate-related risks as communicated to the supervisor, and what banks choose to publicly disclose. This practice of selective disclosure could mislead investors and consumers about environmental performance as a result of more

---

[21] ECB (2022b), Full disclosure: coming to grips with an inconvenient truth: Keynote speech by Frank Elderson, Member of the Executive Board of the ECB and Vice-Chair of the Supervisory Board of the ECB, 14th European Bank Institute Policy Webinar on the ECB's supervisory approach on climate-related and environmental risks, European Central Bank, Frankfurt am Main, 14 March.

thorough disclosure of very positive information and the omission of negative impacts.