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## **Approach to the Development of European Sustainability Reporting Standards for Listed SMEs – Issues Paper**

### **Objective**

- 1 The objective of this paper is to propose a methodology and workplan for the development of simplified ESRS for listed SMEs<sup>1</sup> (listed SMEs ESRS) and seek approval of SR TEG on the proposed way forward.

### **Background**

- 2 The CSRD<sup>2</sup> introduces Sustainability Reporting Standards for listed SMEs (see detailed provisions in Appendix 1).
- 3 The CSRD introduces the following provisions concerning listed SMEs ESRS:
  - Recital 21: establishes concepts for listed SMEs disclosure such as investor protection, enhanced access to financial capital and investment portfolios, compliance with SFDR, cap of value chain, proportionality, delayed application and phase-in.
  - Art 19a (6) specifies the content of simplified sustainability reporting for i) listed SMEs, ii) small and non-complex financial institutions and iii) captive insurance and reinsurance undertakings. It establishes that those undertakings may report according to sustainability standards for SMEs as per Art 29 c. The content defined by art 19a (6) is :
    - (a) a brief description of the undertaking's business model and strategy;
    - (b) a description of the undertaking's policies in relation to sustainability matters;
    - (c) the principal actual or potential adverse impacts of the undertaking on sustainability matters, and any actions taken to identify, monitor, prevent, mitigate or remediate such actual or potential adverse impacts;
    - (d) the principal risks to the undertaking related to sustainability matters and how the undertaking manages those risks;
    - (e) key indicators necessary for the disclosures referred to in points (a) to (d).
  - Art. 29b (4): sets the SMEs cap in the value chain: "Standards shall not specify disclosures that would require undertakings to obtain information from SMEs in their value chain that exceeds the information to be disclosed according to the sustainability standards for SMEs referred to in art. 29C".

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<sup>1</sup> SMEs whose securities are listed in regulated markets

<sup>2</sup> Adopted Text, P9\_TA(2022)0380, Corporate Sustainability Reporting Directive- European Parliament legislative resolution of 10 November 2022 on the 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)0189 – C9-0147/2021 – 2021/0104(COD))

- Article 29c on sustainability reporting standards for SMEs establishes that sustainability reporting standards shall be proportionate and relevant to the scale and complexity of the activities, and to the capacities and characteristics of small and medium-sized undertakings. In terms of content, it refers to art 19a (6) and to the criteria in Article 29b, paragraphs 2, 3,4 and 5. It requires the standards to specify, to the extent possible, the structure in which that information shall be reported. The Commission shall adopt those delegated acts at the latest by 30 June 2024
- 4 According to the CSRD definition, small and medium sized undertakings have between 10 to 250 employees (to be combined with turnover and balance sheet criteria). The number of such small and medium sized undertakings that are listed in Europe is estimated around 1.1 thousand which is a non-negligible proportion of the about 9 thousand listed companies in EU (or about 4 thousand if only domestic companies are considered).<sup>3</sup>
- 5 Besides art 29c on sustainability standard for listed SMEs that is legally binding, EFRAG has received feedback to develop guidelines for voluntary disclosures for all SMEs undertakings that are not in the scope of the CSRD. The potential users of the voluntary guidelines are therefore much broader compared to listed SMEs. The total number of SMEs in Europe is estimated to be around 1.5 million<sup>4</sup> (23 million if including micro). The former cluster 8 of EFRAG PTF has finalised a proposal on a voluntary reporting standard in July 2022. The proposal for this mandate and workstream is addressed in the separate Issues Paper on the Voluntary Sustainability Reporting Standard for non-listed SMEs.
- 6 The focus of this paper and the paragraphs below is on the EFRAG's mandate related to the listed SMEs ESRS.

### **Comparison between CSRD provisions for listed SMEs and the ones for large undertakings**

- 7 The following reflection points are based on Appendix 1 that analyses CSRD provisions for listed SMEs ESRS and compares them with the ones for large undertakings.
- ESRS for listed SMEs apply to i) listed SMEs, ii) small and non-complex financial institutions and iii) captive insurance and reinsurance undertakings [art 29c and art. 19a (6)]
  - In terms of reporting areas the secretariat has compared the provisions of art. 19a (6) for listed SMEs ESRS and the ones of art. 19a (2) for large undertaking ESRS. The comparison is summarised in the table in Annex 1 (par. 9). The table suggests that the overall reporting areas are the same, but many of the detailed reporting contents applicable to the large undertakings within those reporting areas are not explicitly required for listed SMEs. In particular, for the following detailed reporting contents that are not explicitly mentioned in the list of disclosures to be covered in listed SMEs ESRS, the technical question is to what extent they should or can still be included in the listed SMEs ESRS: i) opportunities, ii) targets and progresses, iii) financial plans and resources, iv) implementation of the strategy, v) due diligence,

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<sup>3</sup> Source : [FESE, Capital market Fact Sheet, Q1 2022](#), figures on number of listed SMEs and number of listed companies in EU and [COMMISSION STAFF WORKING DOCUMENT EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT](#) Accompanying the document 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

<sup>4</sup> Source: [Eurostat, Key figures on European business with a special feature on SMEs](#) , 2021 (p.11)

vi) value chain, vii) transition plans in line with Paris agreement, climate law and exposure to coal and mining, viii) dependencies, ix) role of administrative, management and supervisory bodies in sustainability matters and their expertise and skills; x) incentive schemes linked to sustainability matters.

- Listed SMEs ESRS shall also consider art 29b (par 2 to 5) that means:

i) it should cover the environmental, social and governance sustainability matters as in ESRS for large undertaking [art. 29b (2)],

ii) it should present forward-looking, retrospective, qualitative and quantitative information as appropriate like for ESRS large undertakings [art 29b (3)];

(iii) it should take into account the cap on the value chain provisions [art. 29b (4)]

iv) it should take into account the international initiatives and EU regulation listed in art 25b (5) like the ESRS for large undertakings. However, taking into account the principles of simplifications and proportionality, the secretariat asks SR TEG if a limited subset of EU legislations shall be considered (i.e. disclosure requirements related to Pillar 3 ESG risks or Benchmark Regulation).

8 Listed SMEs ESRS shall include the information related to SFDR PAI and art 8 Taxonomy Regulation [ Recital 17 and 21]. Hence the secretariat's proposal refers to those two legislations for a discretion criterion to define the sustainability matters topics and sub-topics in listed SMEs ESRS (tentative table in par. 9 in Appendix 1). Questions to SR TEG is if this approach could be a supported or if alternatives shall be considered.

9 Finally, an important element of the ESRS for listed SMEs is the implication it has in terms of setting the cap for the value chain for the ESRS for large undertakings. This will result in an amendment to Set 1.

### **Methodology for listed SMEs ESRS**

10 The below proposal for methodology concerns art 29c sustainability standards for listed SMEs (point 2 above). The proposal has been informed by the provisions of the CSRD for listed SMES ESRS outlined in Appendix 1 and the reflection points contained in the sections above.

11 Scope. Given the diversity of target groups within the scope of art 29c listed SMEs ESRS that includes; i) listed SMEs, ii) smaller banks and iii) captive insurers or iv) reinsurers – and to limit the complexity under time constraints - the proposed approach is:

✓ To take a sector agnostic approach for the listed SMEs ESRS in first phase and move the simplified requirements for smaller banks and captive insurance and reinsurances to the sector-specific layer of the standards.

✓ The sector specific layer of listed SMEs ESRS would take shape of an Annex. It will be drafted after EFRAG has finalised the sector-specific layer of ESRS.

SR TEG to approve or propose alternative options.

12 Reporting Principles. Considering the CSRD provisions (point 3 above and Appendix 1), it is proposed that the standard will elaborate on the following principles:

- ESRS 1 General Requirements would be applicable. This would be justified by the fact that, at least for financial materiality, the users are the same as the users of the reporting of larger undertakings in scope of the SMEs.

- Subject to satisfying the need of the users, proportionality shall be an additional principle (to the content of ESRS 1). Proportionality can be defined

as the relation between the sustainability report's scope and complexity compared to the undertaking's resources and know-how. This principle is connected to accessibility and processing of data to be reflected in the other general principles listed below. The following could be considered when reflecting the proportionality principle:

- Simplify the materiality assessment process and due diligence for SMEs.
- Simplification of disclosure requirements. (e.g. qualitative versus quantitative).
- Simplified application guidelines and digital questionnaires to facilitate implementation.
- The listed SMEs ESRS shall build as much as possible on existing international or national initiatives.

13 Characteristics of information. Reference to be made to Appendix C of ESRS 1.

14 Architecture. Considering the CSRD provisions (point 3 and 8 above and Appendix 1), listed SMEs ESRS shall be connected and mapped to the general ESRS in order to meet all legally binding requirements. The listed SMES ESRS will consist of one standard combining cross-sector and topical disclosures across four parts. The following architecture is proposed:

- I. Listed SMEs ESRS General Requirements. This section shall include SMEs specifications to ESRS 1, such as proportionality, simplified materiality assessment (including double materiality), guidance in presentation of information.
- II. Listed SMEs ESRS General Disclosure and Governance. This section shall include the description of sustainability matters in business model and strategy; governance; policies; principal actual or potential adverse impacts and actions; principal risks (art 19 5 (a) to (d),) and intangibles (art. 20c). This section would correspond to existing ESRS 2 and G 1 to be simplified and merged. DRs related to governance shall include the SFDR<sup>5</sup> Principle Adverse Impact indicators (SFDR PAI).
- III. Listed SMEs ESRS Environmental Disclosures. This section shall include reporting on topical environmental matters and impacts. This section would correspond to ESRS E 1-5 simplified and merged. It is proposed to reduce the number of DRs that shall include: i) green taxonomy alignment DRs and ii) mandatory and optional SFDR PAI <sup>7</sup> DRs (key metrics, art. 19 5 (e)). Question is raised on whether to also include under the E Disclosure the requirements deriving from EBA Pillar 3 ESG framework<sup>6</sup> and Benchmark Regulation as it is under ESRS. This may lead to additional complexity but would be in line with CSRD provision to consider in listed SMEs ESRS art 29b (5).
- IV. Listed SMEs ESRS Social Disclosures. This section shall include reporting on topical social matters and impact. This section would correspond to ESRS S1 – 4 simplified and merged. It is proposed to reduce the number of DRs that shall include the mandatory and optional SFDR PAI indicators 7.

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<sup>5</sup> SFDR : 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.

<sup>6</sup> [EBA Final draft implementing technical standards on prudential disclosures on ESG risks in accordance with Article 449a CRR](#)

V. Application Guidelines with enhanced simplification and digital questionnaire. SR TEG to address question under part III and approve or propose alternative options.

### **Involvement of stakeholders**

- 15 Given the specificities of SMEs and in particular the need to develop requirements that are proportionate to their organisation and resources, user-tests and outreaches are particularly important in the development of this proposal.
- 16 The following stakeholders' or expert groups are identified as relevant in the development of the Listed SMES ESRS to cover both the users and preparers perspectives:
  - Existing EFRAG Expert Group SMEs
  - Listed SMEs representatives
  - Large and smaller banks representatives (incl. EIB, ERBD)
  - Captive insurance and reinsurance representatives
  - Large companies' representatives as SME's customers
  - DG FISMA, DG Grow (SME's unit), DG Justice, ESMA, EBA, EP SMEs intergroup
- 17 To facilitate the reach-out and onboarding, it is proposed that EFRAG collects inputs and performs user tests on its proposals in two ways:
  - ✓ Internally: setting-up a testing/ sounding board within EFRAG members in TEG and SRB
  - ✓ Externally: enlarging the existing expert group (se point 14 above) and organizing outreaches, questionnaires, and informal exchanges outside EFRAG membership

SR TEG is requested to approve or suggest other alternative options.

### **Work program for listed SMEs ESRS**

- 18 The following tentative workplan is proposed:
  - Beginning of November 2022: SR TEG and Board decision on proposed methodology, scope, workplan and other elements addressed in this paper.
  - Mid - end November 2022: collecting stakeholders' specific input on basis of questions or one-to-one Informal meetings. Parallel drafting of SMEs ESRS
  - Mid December 2022: Draft 1 – Listed SMEs ESRS- discussion at SR TEG and SRB
  - Mid-end January 2023: Draft 2 – Listed SMEs ESRS- workshop outreach + SR TEG and SRB
  - Mid-February: Final Draft – approval of SR TEG and Board.
  - March 2023: Final Exposure drafts listed SMEs ESRS and launch of public consultation with 3 months period
  - March 2023 - June 2023: Cost-benefit analysis
  - April 2023: Basis for Conclusions

**Questions to SR TEG members and observers**

- 1 With regards to the scope of the listed SMEs ESRS: do you agree with the proposal to take a sector agnostic approach for the Listed SMEs ESRS and add the SMEs sector specific layer as annex? In particular do you agree that the simplified requirements for smaller banks and captive insurance and reinsurances foreseen in art. 29c and 19b(6) will be moved to the sector-specific layer of the listed SMES ESRS?
- 2 With regards to the methodology and reporting principles, do you agree to confirm the applicability of ESRS 1 and to add a principle on proportionality? Do you agree that this principle of proportionality should result in simplified materiality assessment, simplified DRs and guidance in presentation of information (qualitative versus quantitative) shall be key principles in SMEs ESRS? Do you have other proposals?
- 3 With regards to the architecture proposed for the listed SMEs ESRS. Do you agree on a simplified approach to general ESRS? Do you agree with the four parts as suggested at par. 14 above?
- 4 Do you agree that the topical disclosures shall be limited to the mandatory and optional SFDR PAI and taxonomy DRs? Should the EBA Pillar ESG risk requirements be also added? Or would this be in contrast with simplification and proportionality?
- 5 Do you have comments on the reporting areas identified in par. 7 above and detailed in Appendix1 ?
- 6 Do you agree that for the sustainability topics and subtopics (tentative table in par.16 of Appendix 1) to be covered in listed SMEs ESRS the discretion criterion to apply could be the prioritization of Taxonomy Regulation and SFDR PAI as indicated in Recital 21 and 17 of CSRD?
- 7 With regards of involvement of stakeholders, do you agree that given the specificities of SMEs user-test and outreach is particularly important in the development of this proposal? Do you agree with the identified stakeholders' groups at par. 15 and 16 above? Do you agree with the two processes/ sounding board? Internal and external at par. 17?
- 8 With regards to the workplan and timeline: do you agree with the proposal in par 18 above?
- 9 Do have any other comments on EFRAG approach to listed SMES ESRS?