

This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of EFRAG SR TEG. The paper forms part of an early stage of the development of a potential EFRAG position. Consequently, the paper does not represent the official views of EFRAG or any individual member of the EFRAG SRB or EFRAG SR TEG. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG SRB, are published as comment letters, discussion or position papers, or in any other form considered appropriate in the circumstances.

Input Paper basis for conclusions VSME ESRS

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Objective of the document

- 1 The purpose of this document is to provide input for the forthcoming basis for conclusions of the VSME ESRS. The document contains the main preparatory material, outcome of meetings, methodological approach of the VSME ESRS. It includes:
 - ✓ The CSRD provisions for SMEs
 - ✓ The figures from the relevant overview of studies related to the potential scope of the VSME
 - ✓ The EFRAG methodological approach of the Building Blocks, SR TEG SRB, , EWG and VSME and LSME Communities
 - ✓ Summary of the main simplifications applied for LMSE ESRS

- ✓ The comparison between proposed VSME and LSME ESRS and other existing sustainability reporting initiatives for SMEs within EU

CSRD Provisions indicative for the development of standards for non-listed SMEs (micro, small and medium companies)

- 2 The CSRD1 introduces simplified sustainability reporting standards for listed SMEs, small non-complex credit institutions and captive insurances and reinsurances (LSME ESRS) as derogation to the ESRS for large undertakings. Micro Small and medium sized companies that are not listed are not in the scope of CSRD. Micro enterprises listed are explicitly excluded from the CSRD scope.
- 3 The CSRD provides however certain indications for non-listed small and medium companies.
- 4 **Article 29c** establishes that LSME ESRS 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. This sets a principle of simplification and proportionality.
- 5 **Art 29b4** indicates that LSME ESRS will set a reference for large undertakings that are within the scope of the CSRD regarding the level of sustainability information that they could reasonably request from SME suppliers and clients in their value chains.(value chain cap)
- 6 **Recital 21** indicates that small and medium-sized undertakings that are not listed on a regulated market in the Union should also have the possibility of choosing to use such proportionate standards on a voluntary basis.
- 7 **Recital 22** says that Member States should be free to assess the impact of their national transposition measures on small and medium-sized undertakings, in order to ensure that they are not disproportionately affected, with specific attention to be given to micro-undertakings and to avoiding an unnecessary administrative burden. Member States should consider introducing measures to support small and medium-sized undertakings in applying the sustainability reporting standards.

¹ Corporate Sustainability Reporting Directive:



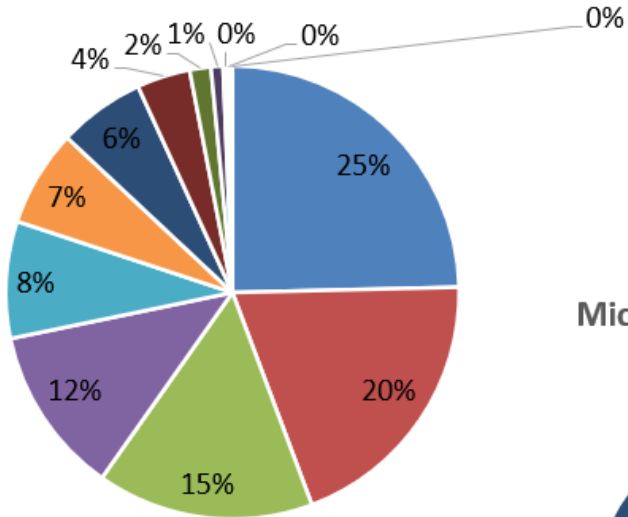
- 8 EFRAG's work on a voluntary standard for non-listed micro, small and medium companies (VSME) is outside the mandate in the CSRD and derives from the market need for a point of reference to be used by counterparties in the upstream value chain of SMEs and by lenders, when they define their data requests from non-listed SMEs and to support non-listed SME in the start of their sustainability journey.
- 9 This market need was highlighted in the EC impact assessment accompanying the CSRD proposal and confirmed by EFRAG LAB (Final Report 2021) and by former EFRAG PTF cluster in charge of SMEs that was composed by representatives of SMEs and banks. Commissioner Mc Guinness and the European Commission have recommended EFRAG to work on such a voluntary standard.
- 10 EFRAG SR TEG, SRB and VSME and LSME communities confirmed the need of a voluntary standard for micro, small and medium sized non-listed companies in Europe to enable them in facing growing stakeholders request for ESG data and to lower the entry barrier to reporting.
- 11 The values and benefits of VSME will crucially depend on the level of market acceptance and recognition that this framework will ultimately achieve as a standard for data collection requests by lenders and large companies.
- 12 VSME has no legal role in defining the value chain cap. Draft LSME ESRS is the document that defines the limit of information that large undertakings are expected to collect from their counterparties in the supply chain, in line with art 29b(4) CSRD.

Figures on the scope of VSME

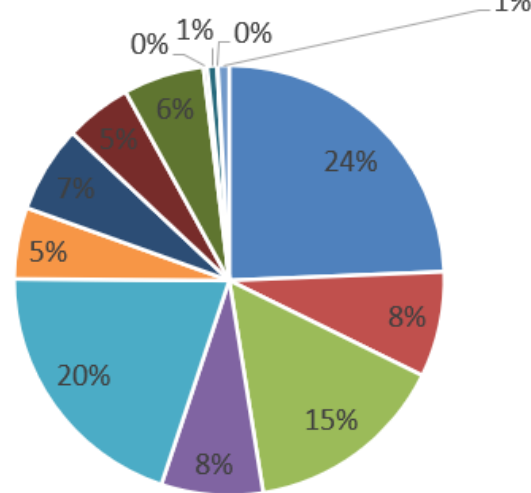
- 13 Micro, small and medium companies are the vast majority of companies in Europe. They are in total 23.2 million with the following breakdown.
 - Micro (<10 employees + balance sheet and turnover combined, accounting directive) = 21.7 million (93.3% of total EU companies)
 - Small (<50 employees + balance sheet and turnover combined, accounting directive) = 1.3 million (5.6% of total EU companies)
 - Medium (<250 employees + + balance sheet and turnover combined, accounting directive) = 202.000 (0.9% of total EU companies)



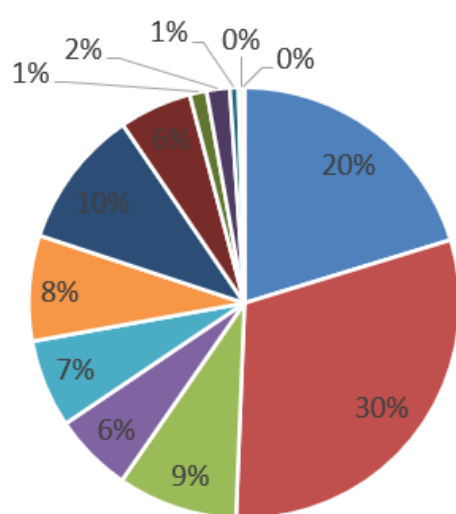
Small (10-49 persons employed)



Micro (0-9 persons employed)



Medium-sized (50-249 persons employed)



Methodological approach and Building Blocks - SR TEG, SRB, EWG and VSME and LSME Communities

- 14 The VSME proposal was discussed by SR TEG, SRB, EWG and VSME and LSME communities on the basis of the document put forward by former EFRAG PTF cluster 8 that was considered a valuable basis. The key recommendation to EFARG secretariat was to ensure consistency with the ESRS and LSME ESRS in order to achieve a fully modular, building block approach across the European system of sustainability reporting standards.
- 15 Hence, the building block approach was conceptually integrated in the design of the draft LSME ESRS and the VSME working papers as part of the methodology established in January and February 2023. At the SRB meeting on 27 January 2023, the SRB agreed to:
- i) start with LSME;
 - ii) keep LSME proportionate- but within the remit of the CSRD constraints;
 - iii) once LSME basis is stabilised, consider VSME (incl. the current draft) from a consistency and additional proportionality perspective;
 - iv) potentially consider merging LSME and VSME if appears relevant.
 - v) The overall purpose is to make available a standard for the two populations (listed and non-listed SME) in the same timeframe.
- 16 According to the decision above, and to the consideration on the role of VSME and the scope that would include also micro undertakings, the EFRAG Secretariat and SR TEG have been working on the content of a building block approach as presented at SRB meeting on 7 February. The components of this building block are described in Agenda Paper 03.03 and can be summarized as follows:
- VSME first step: Metrics data-set
 - VSME second step: Metrics data-set + narrative information on general disclosures and PTA
 - VSME third step: Metrics data-set + narrative information on general disclosures and PTA + EU datapoints module
 - LSME = VSME third step + datapoints due to value chain cap (and adjustments due to the consolidated view in VSME versus individual view in LSME)
 - ESRS Set 1 (EC DA June 2023). = top level



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Common building block (VSME) → Steps 1(metrics) + 2 (narrative)	VSME optional component (to meet the expectation of the financial market participants) Step 3	LSME additional component (CSRD)	LSME “report if you have” ³ additional component	LSME optional component	Reference to EC DA ESRS Set 1 (version June 2023)
BP 1 (simplified)		BP 1 (additional to VSME)			ESRS 1 - BP1
BP 2 (simplified)		BP 2 (additional to VSME)			ESRS 1 - BP2
GOV 1 (simplified)		GOV 1 (additional to VSME)	GOV 2 sustainability due diligence (simplified)		ESRS 2 – GOV 1
SBM 1 (simplified)	EU SF law module (SFDR table1, BR, Pillar3)	EU law module (SFDR, BR, TR, Pillar 3)	SBM 2 – Views and interests of stakeholders		ESRS 2 – SBM 1 ESRS 2 – SBM 2
Materiality matrix (list of matters identified as material)		SBM 3 (simplified)		Material opportunities Positive material impacts	ESRS 1 – Appendix B AR 16 (list of sustainability matters) ESRS 2 – SBM 3
		IR 1 and 2 centralised			ESRS 2 – IRO 1 and IRO 2
		IR 5 and 6 Process to engage and to			S1-2 and S1-3



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		remediate (centralised)			S2-2 and S2-3 S3-2 and S3-3 S4-2 and S4-3
Strategy/Targets/Progresses on material sustainability matters (Cluster 8 - inspired)	EU SF law module (SFDR Table1, BR, Pillar3)	Centralised Policies and Actions - EU law module (SFDR, BR, TR, Pillar 3)	Centralised Targets - EU law module (SFDR, BR, TR, Pillar 3)		ESRS 2 (MDR-P and MDR-A), MDR -T Policies and actions from topical standards
Metrics- Step1 Cluster 8 – inspired metrics (but using Set 1 language – no additional datapoints)	EU SF law module (SFDR Table1, BR, Pillar3)	EU law module + Value Chain Cap			Metrics from topical standards

17 In reference to the methodological approach of the “building blocks”, the responses of the majority of the EFRAG VSME Community (93 %) and LSME Community was recorded as positive and in support of the proposed VSME as the “common building block” to provide the minimum content across the ESRS. There was also general support for segmenting the users according to size: i) for micro-undertakings to use the first step of metric only (data-set) ; ii) for small undertaking to use the step1+step 2 VSME (combined or not with step3) and for iii) medium undertakings to use the more advance level of LSME ESRS or the full VSME 3 steps as preferred option.

Summary of main simplifications in VSME ESRS compared to LSME ESRS



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The table below provides an overview of the main simplifications embedded in LSME and VSME ESRS in terms of general disclosures, narrative section on governance, strategy, policies, actions and targets.

Set 1	Proposed simplifications for LSMEs ESRS Section 2 *general disclosures* (compared to set 1)	Corresponding proposed simplification for VSME (compared to LSME ESRS)
ESRS 2 General Disclosures	GOV – 1 Reduced granularity simplified (kept EU Data points), gender ratio and independent members	DR on Governance asking for (i) governance structure (highest body or individual) if applicable and (ii) related gender diversity ratio
	GOV-2 Sustainability due diligence. To disclose whether it has applied DDP or it has not (EU DP)	NA
	SBM-1 <i>Simplification instead of revenue breakdown, requirement to disclose the list of ESRS significant related sectors in which the undertaking operates and EU Data Points (revenue in certain sectors Benchmark Regulation and SFDR)</i>	The material topics and sub-topics (with brief description on how they affect people and environment) <ul style="list-style-type: none"> ➢ Effects of material topics and subtopics on cashflows, financial position ➢ How topics and sub-topics affect the strategy.
	SBM-2 On interests and views of stakeholders applies only in the case that stakeholder engagement occurs. Specific AR to support LSME	List of key stakeholders and if applicable a brief description of engagement activities
	New SBM-4 Material opportunities (as a voluntary content)	Included in VSME as additional on an optional basis
	IR1 -impact and risks centralized across E,S and G	List of material topics and sub-topics (materiality matrix)



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	IR3 and 4 – centralized policies, actions plus targets across E, S and G	A description of policies, actions and targets (simplified) to address the list of material topics and sub-topics (materiality matrix)
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- Methodological questions to be discussed by SR TEG (questions for SR TEG meeting 13 July):
- The VSME v1 includes an option for micro, small and medium sized companies in scope to report additional entity specific sustainability information. This was proposed by ex-PTF cluster 8. to maintain it. Is this supported by SR TEG?
- In line with ex-PTF cluster 8 VSME proposal, VSME v1 includes optional value chain dimension and the possibility to consolidate reporting: is this supported by SR TEG?
- In line with feedback from LSME community and other stakeholders, the VSME v1 suggests that micro-enterprises may limit its sustainability report to step1, key metric dataset. Vice-versa for medium enterprise it is suggested the use of the next level LSME ESRS. This is to ensure that the tool is modular and to proportionate with dynamic steps in the voluntary application.
- Orientation on the “additional EU-module” for VSME is sought. The module is preliminary presented to allow for timely discussion, but is still work in progress. The secretariat would like to validate the approach that only SFDR Table1 PAI, Benchmark Regulation and ESG Pillar 3 CRR datapoints are included in a simplified manner.

Comparison between draft VSME, draft LSME ESRS’ reporting areas and other voluntary sustainability reporting initiatives for SMEs

- 18 EFRAG Secretariat responding to proposals and feedback from EWG and stakeholders conducted a first comparative review of the provisions included in the draft VSME as proposed by ex-PTF Cluster 8 with the general requirements and architecture of LSME ESRS and other sustainability reporting standards directed for use by SMEs.



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- 19 The outcomes of the comparative review undertaken by EFRAG Secretariat to examine similarities and differences between the ex-PTF Cluster 8 proposal for VSME, the draft ESRS LSME and other sustainability reporting standards for SMEs voluntarily applied in EU member states in the period from November 2022 to February 2023 according to the direction of the SR TEG and the comments received from EWG members are summarized in the Table below:

GENERAL REQUIREMENTS	VSME	LSME	GERMAN SUSTAINABILITY CODE	NORDIC SUSTAINABILITY REPORTING STANDARD SMES	CDP CLIMATE DISCLOSURE SMEs	
2	DOUBLE MATERIALITY	YES	YES	Partially applicable	Partially applicable	Not applicable
3	REPORTING ON VALUE CHAIN	Optional	YES	Partially applicable	Not applicable	Not applicable
4	QUALITY OF INFORMATION	YES	YES	Not applicable	Partially applicable	YES
5	COMPARATIVE INFORMATION	YES	YES	YES	YES	YES
6	CONNECTIVITY of DRs	Optional	YES	Not applicable	Not applicable	Not applicable



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7	CONSISTENCY OF DRs	YES	YES	Not applicable	YES	YES
8	LOCATION of DRs	YES	YES	Not comparable	Not comparable	Not comparable
9	INCORPORATION by REF.	YES	YES	Not applicable	Not applicable	Not applicable
10	PROPORTIONALITY	YES	YES	Not applicable	Not applicable	Not comparable
12	REPORTING AREAS					
12.1	GOVERNANCE	YES	YES	Partially covered	Partially covered	Partially covered
12.2	STRATEGY	YES	YES	Partially covered	Partially covered	Not applicable
12.3	IMPACT MANAGEMENT (POLICIES; ACTIONS; TARGETS)	YES	YES	Partially covered	Partially covered	Partially covered
12.4	LIST OF MATERIAL SUSTAINABILITY TOPICS AND SUB-TOPICS	YES	YES	Partially covered	Partially covered	Not applicable
12.5	METRICS & TARGETS	YES	YES	Partially covered	Partially covered	Not comparable



Appendix

20 List of public meetings: TO BE UPDATED

- [EFRAG SRB meeting 14 December 2022 - EFRAG](#) on SMEs standards approach and methodology.
- [EFRAG SR TEG Meeting 17 January 2023 - EFRAG](#) on the LSME approach and decision tree.
- [EFRAG SR TEG meeting 25 January 2023 - EFRAG](#) on the LSME approach and decision tree (continuation of 17 January).
- [EFRAG SRB Meeting 07 February 2023 - EFRAG](#) on building blocks.
- [EFRAG SR TEG Meeting 19 June 2023 - EFRAG](#) on building blocks.



EFRAG SR TEG, 13 July 2023

- [EFRAG SRB Meeting 28 June 2023 - EFRAG](#) on the role of VSME, entities in scope, building blocks approach and joint consultation of LSME and VSME

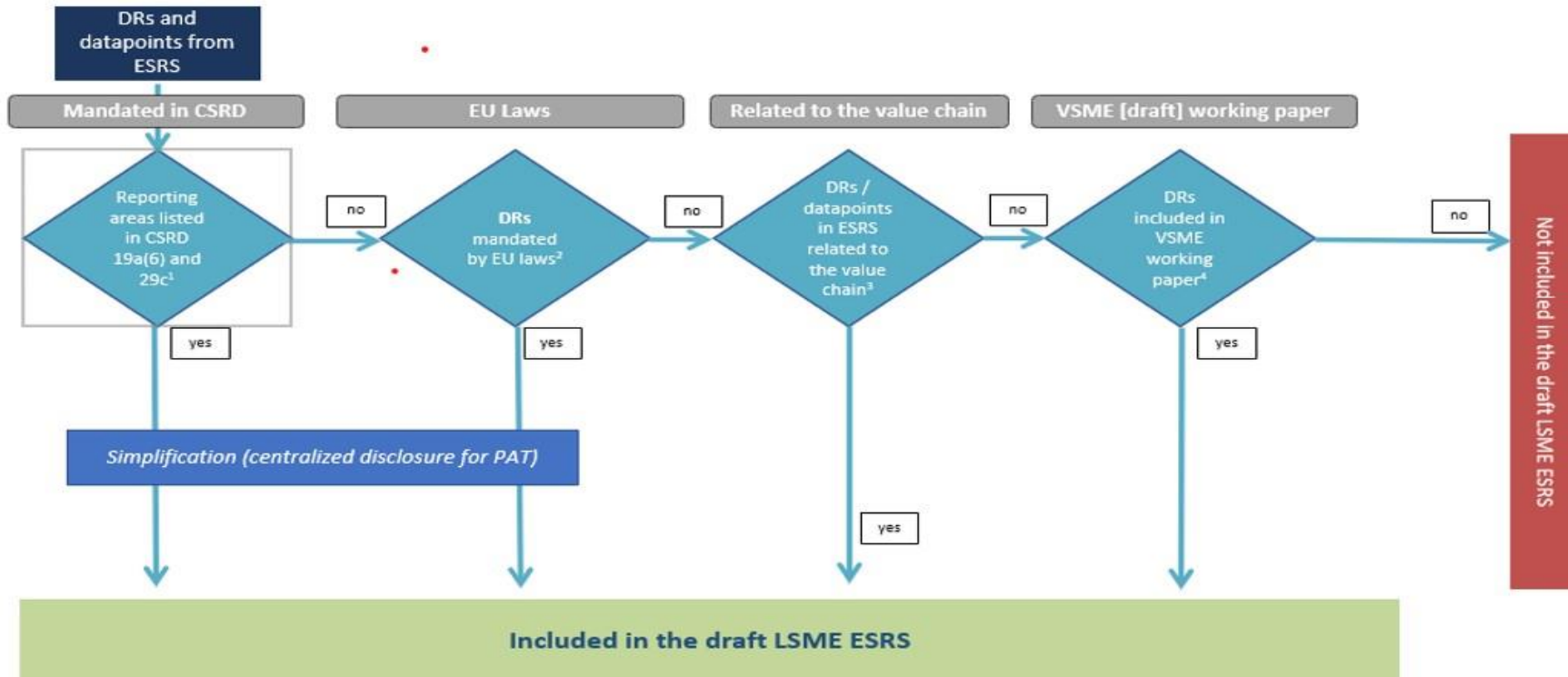
21 List of internal and closed meetings on VSME:

- 1st EWG meeting (19 December 2022): SMEs workstream and building blocks approach, LSME and VSME approach and prioritisation of work.
- SR TEG Q&A session on VSME (19 January 2023): approach taken by ex PTF Cluster 8 and the C8 proposal on voluntary standard for SMEs.
- 2nd EWG meeting (19 January 2023): LSME and VSME.
- LSME Community workshop (27 January 2023): presentation of the outcome of the questionnaire sent to the LSME community members and additional questions regarding LSME.
- SR Board meeting (27 January 2023) on approach to LSME and VSME as two separate standards.
- VSME Community workshop (31 January 2023): presentation of the outcome of the questionnaire sent to the VSME Community members and additional questions regarding VSME.
- 3rd EWG meeting (9 February 2023): discussion on LSME and VSME Communities questionnaires and LSME working papers.
- 4th EWG meeting (8 March 2023): Discussion on VSME Community feedback and LSME working papers.
- SR TEG (24 April 2023): drafting session to discuss written feedback of SR TEG on LSME.
- 5th EWG meeting (5 May 2023): debrief EWG on LSME progress.
- SR TEG (21 June 2023): building blocks continuation
- 2nd LSME Community workshop (26 June 2023): Building blocks, VSME and LSME ESRS





Decision Tree



Note 1: Art. 29c refers to the criteria set out in Art. 29b point 2 to 5

Note 2: EU laws limited to SFDR, Pillar 3, benchmark regulation, climate law and Taxonomy Regulation art. 8

Note 3: Is the DR / datapoint in ESRS essential for the depiction of the matter, or essential for the « value chain cap »?

Note 4: VSME [draft] working paper is based on EFRAG PTF cluster 8 proposal

