

The Office of the German Sustainability Code, German Council for Sustainable Development (RNE)

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## **Comment Letter on the Draft European Sustainability Reporting Standards by the Office of the German Sustainability Code**

Dear Mr Buysse, dear Members of the EFRAG Sustainability Reporting Board,

on 29 April 2022, you have released the first set of the Draft European Sustainability Reporting Standards (ESRS) for public consultation, which will be closed on 8 August 2022. We understand that having considered the stakeholder contributions from the consultation, EFRAG will provide its technical advice on the ESRS to the European Commission, which will adopt the standards as Delegated Acts by June 2023. The aim of the proposed ESRS is to provide a standardised reporting framework for companies, in line with the Corporate Sustainability Reporting Directive (CSRD).

We —the Office of the German Sustainability Code (The Code Office)— welcome the proposed ESRS in general. However, there are several aspects that we consider critical for a successful implementation, based on our experience in the field of sustainability reporting. The Sustainability Code was adopted by the German Council for Sustainable Development (RNE) in 2011 based on a comprehensive stakeholder review process and is an internationally applicable standard for sustainability reporting. The Code has already provided more than 850 companies of all sizes and legal forms with a condensed and user-friendly platform for sustainability reporting. Moreover, the Sustainability Code helps companies to comply with their reporting obligations, e.g. the national implementation act of the Non-Financial Reporting Directive (Directive 2014/95/EU) and reporting requirements in accordance with the EU Taxonomy for Sustainable Activities. From our perspective, the following aspects are crucial for a successful implementation and a general acceptance of the ESRS by enterprises from across Europe.

### **Compatibility with Other Sustainability Standards**

The Code Office commends that the ESRS seek to take account of existing legislation, initiatives and standards, which is a pivotal step towards streamlining sustainability reporting and increasing comparability. In particular, it is important to maximize compatibility with the standards (global baseline) that are being developed by the International Sustainability Standards Board (ISSB). To avoid fragmentation and operational burdens for companies, it is critical to align the standards – on a fundamental level – to the greatest extent possible. However, the Code Office recognises the differences between the ISSB standards and the EU’s ambitions. We acknowledge that the more extensive disclosure requirements in the context of the ESRS can increase the EU’s steering capacity and support a redirection of capital flows towards sustainable investments, thus contributing to the UN Sustainable Development Goals and the implementation of the EU Green Deal.

### **Process Orientation**

From our perspective, it is evident that the number and detail of reporting requirements is disproportionate to current organizational capacities and sustainability due diligence processes. It will take time and considerable resources to establish the necessary organizational structures and processes for full compliance with the ESRS. Thus, it is crucial that the ESRS are set up as process-oriented standards, meaning that undertakings can report in line with their current status quo. Every undertaking should be able (and required) to publish a full report - from those who have just begun the process of implementing sustainability due diligence to those who have integrated sustainability matters fully into their operations, value chain and business model. To accomplish this, the Code Office considers it critical that the “comply or explain” approach is embedded in the ESRS in a very clear and simple manner. Undertakings need to have a reliable and easily understandable option to explain why they cannot report in compliance with a disclosure requirement at a given moment. In our view, it is feasible to maintain a similar number of disclosure requirements and level of detail in reporting as proposed in the consultation drafts, if undertakings have the option to justify the omission of information in legitimate cases. Given the ambitious timeline of the EU, legitimate cases should include a lack of data collection mechanisms. In line with the aforementioned process

orientation, undertakings that omit information due to a lack of data collection mechanisms should be required to disclose planned actions and targets for setting up the mechanisms and reporting in compliance with the ESRS. Disclosure Principle 1-2 on targets, progress and tracking effectiveness should be applied to these targets.

### **Double Materiality**

The Code Office welcomes the precise definition of materiality included in the ESRS. It has been our experience that unclear and sometimes conflicting definitions of materiality in EU and national legislation have caused considerable confusion and discussion. In particular, we appreciate the inclusion of positive impacts and opportunities. This finally creates an appropriate stage for sustainability pioneers to report on their positive outcomes. We sincerely hope that this will stimulate sustainability innovation.

### **Ease of Use**

In our experience, companies need a concise and easily comprehensible reporting structure. From our perspective, more work needs to be done to reduce duplications across topical standards and with cross-cutting standards (e.g. aspects concerning governance in ESRS G1 and ESRS 2-GOV 1). Additionally, we recommend improving the ease of use of the ESRS, for instance by ensuring that no additional reporting requirements are introduced in the application guidance. The application guidance should only include examples and recommendations. Specifications regarding the type and scope of the required information need to be included in the disclosure requirements themselves.

### **SME Application**

The Code Office strives to enable SMEs to report on sustainability and is therefore particularly interested in the ESRS application in small and medium sized companies. From our perspective, more emphasis should be placed on the planned SME-specific ESRS. In Germany, there are only very few listed SMEs that will be legally obliged to report in line with the SME-specific ESRS. However, many non-listed SMEs are embedded in value chains as suppliers, contractors or service

providers, and therefore will be required by their clients to provide sustainability information (trickle-down effect). At the moment, very few SMEs are able to provide information in the required quality. We acknowledge the necessity for undertakings with a reporting obligation to acquire relevant information from SMEs in their value chain. However, this must not result in placing undue burdens on those SMEs. It is therefore critical that EFRAG increases planning security by indicating a future framework for SMEs as soon as possible, so that SMEs can set up appropriate data collection mechanisms. This would support undertakings with a reporting obligation by increasing reliability in their information collection process. We conclude that the data provision and future ESRS application by SMEs should be key considerations in the current discussion of the ESRS exposure drafts.

The Sustainability Code, which has already been used by SMEs and even microenterprises like craftsmen as an accessible reporting standard for over a decade, can serve as a benchmark at this point. We consider the following aspects to be crucial in the development of SME-specific ESRS:

- Based on our experience, we recommend that the SME-specific ESRS should have a concise structure with a manageable number of disclosure requirements. To maximize operability, the respective requirements should be phrased as precisely as possible. This ensures that the standards remain accessible to all companies and are implemented consistently.
- In addition, the limited resources of SMEs should be considered. For instance, it is evident that the ESRS requirements for the materiality assessment, especially as related to risk assessments, generally exceed SME's capacities. Therefore, the requirements regarding the materiality assessment should be significantly simplified for SMEs. We support the concept of the rebuttable presumption. However, the requirements for the rebuttal have to be proportionate to the size of the undertaking.
- Several aspects of the proposed ESRS, particularly the disclosure requirements on governance, are built on the assumption of a fairly large, hierarchical organization with several levels in the chain of command and in governance structures, as required for corporations. This assumption is also evident in the notion that undertakings have

Page 5 of 5

individual policies, targets and action plans for each topic, in addition to overarching strategies. In our experience, SMEs do not have this degree of formalized governance and layered strategic planning. The SME-specific ESRS should reflect this and offer more condensed reporting options on governance and strategic planning.

We support the ambition to create a reporting standard that compels undertakings to disclose relevant and comparable sustainability information, which can be used by stakeholders in their decision-making. Particularly financial market participants, regulators and the general public need to be enabled to appraise undertakings according to their sustainability performance. Nonetheless, we believe that complying with the ESRS will be challenging, even for undertakings with extensive reporting experience. It will therefore be of the utmost importance to provide undertakings with assistance and guidance beyond the standards themselves. Strengthening existing national support services can bolster acceptance and improve feasibility for implementing the CSRD and ESRS.

We hope that our input proves useful to you and we are looking forward to your adaptations of the draft ESRS and your future standard-setting work. Please do not hesitate to contact us, if we can be of any assistance.

With kind regards,



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Stephanie Kopp