POSITION STATEMENT | FEBRUARY 2024

Response to draft EFRAG Value Chain Implementation Guidance (VCIG)

Thank you for the opportunity to provide feedback on the draft Value Chain Implementation Guidelines (VCIG). We strongly support efforts to transition the EU economy to a sustainable future. Sustainability reporting is one of many tools to make this ambition a reality. Our suggestions below are intended to reinforce this objective. Our goal is to work constructively but would point out that companies will be in a much more informed position when we have had the opportunity to work through implementation over the next 12 months. It should be noted, therefore, that we may have additional comments after experience has been gained that we are not in a position to offer now. This comment applies to the Materiality Assessment Implementation Guidance also (although we have not provided any detailed comments on that document at this stage).

- We note that the implementation guidance is 'non-authoritative' and an accompaniment to the European Sustainability Reporting Standards (ESRS). We also note (paragraph 10) that the implementation support cannot develop concepts or requirements that go beyond the content of the original act and that the purpose is to illustrate how the provisions of the delegated act may be implemented, but not requirements that shall be implemented. In addition to these statements about the purpose of the guidance, we believe it would be helpful to clarify that independent auditors cannot place reliance on the guidance as part of their audit work.
- Comments on the implementation guidance also need to be seen in the context of concerns about elements of the ESRS that are unclear for report preparers, auditors, and users in their current form. For example, the continuing discussion of the concept of double materiality means that the proposed implementation guidance cannot be sufficiently practical and cannot resolve known uncertainties and challenges (such as with respect to criteria for aggregating an undertaking's impacts, risks and opportunities at a global level) in the underlying standards.
- There remains a risk, therefore, that an important objective of the ESRS – to deliver comparable information - will not be achieved, as reporters will either interpret the requirements differently or will be unable to report as envisaged. Action that simplifies, or reduces the reporting burden, or provides additional transitional provisions, would assist report preparers, and hence deliver more decision-useful information for report users.
- For example, the effort imposed with respect to the consideration of Value Chain actors must be proportionate. Undertakings do not need to collect data from all the actors in their Value Chain (paragraph 28) and could exclude those who do not provide relevant products or services. As such, more emphasis should be placed on the link with the undertaking's core activities and the relevance of the data represented, clearly excluding less relevant information. More examples in the implementation guidance could be useful, especially in distinguishing between smaller and larger companies.
- Similarly, as degrees of separation of value chain actors from the undertaking increase, clarity with regard to their identity and their specific actions and therefore impacts naturally decreases. As such, clarification could be provided to recognise that where there is less certainty and increased generic or speculative assessment of how actors execute their work, that the information is less useful to readers of the report and therefore a recognition that it becomes less relevant until such time as more robust information has been identified.

- Many medium and large undertakings will be required to report against multiple sustainability reporting standards, including ISSB. There are important differences between ESRS and ISSB requirements with respect to definitions, reporting boundaries, and content within the topical standards. We strongly encourage the continuation of efforts to converge and prevent disparities in reporting outcomes so that companies do not prepare multiple disclosures on the same or similar topics. Such an outcome would be confusing for the users of the reported information and will also have a negative impact on the competitiveness of EU companies.
- In previous engagement on the development of the ESRS reporting standards and guidance, we have commented on the need for robust due process in which there is transparency about the development process and timetable, clarity and consistency in the documentation, and sufficient time for market participants to engage meaningfully. We continue to stress that to deliver quality sustainability reporting, further time for implementation and meaningful consultation are necessary. In particular, we would highlight that, given many of our members are engaged in existing end of year reporting cycles, including the preparation of EU Taxonomy disclosures, the period over Christmas and 1Q is extremely difficult to create sufficient time to provide thorough feedback.

Joint Operations

Paragraphs 52 and 53: In our view, the guide does not clarify the treatment of Joint Operations (JO) in sustainability reporting, i.e. when JOs should be included in the 'own operations' metrics and when part of the value chain.

In particular, the table at paragraph 52 indicates for Joint Operations 'same as for associates except for joint operations where the assets/liabilities belong to the reporting undertaking and so form part of own operations.'

Similarly, the flow chart included in paragraph 53 indicates that 'Reporting undertaking' is defined as 'Parent plus subsidiaries (including leased assets and own assets/liabilities used in Joint Operations)'.

This guidance would suggest that the data referred to as joint operations are part of the 'Group' and therefore reported in the metrics related to 'own operations'.

However, this is in contrast with the ESRS E1 paragraph 46 which indicates 'when disclosing the information on GHG emissions… for contractual arrangements that are joint arrangement not structured through an entity the undertaking shall include the GHG emissions in accordance with the extent of the undertaking's operational control over them': This seems to indicate that according to the ESRS E1 DR6 if the enterprise holds operational control over the JO it must consolidate GHG emissions in the operational control boundary (100% scope 1 and scope 2), otherwise it must report them in scope 3 on the basis of the business relationships maintained.

Moreover, ESRS 1 paragraph 62 defines that if the company is a parent company required to draw up the consolidated financial statements, the sustainability statement will cover the 'Group'. The concept of the 'Group' is defined by the Accounting Directive and by IFRS 10 as 'Parent and its subsidiaries'.

Finally, ESRS 1 paragraph 67 does not mention Joint Operations, while indicating that JV and Associates may be part of the undertaking value chain and the undertaking shall include information related to those Associates or JVs in accordance with paragraph 63 if they are also part of the value chain, for example as suppliers (or in VCIG para 53 suppliers or customers).

In our view, Joint Operations should be treated as per JVs and Associates, and therefore:

- consolidated 100% if the reporting undertaking holds operational control, or
- in the absence of operational control, either: treated as value chain actors if the JO is also in the value chain, or
- not reported if neither of these are true.

This seems to be consistent with the fact that in the absence of operational control, entities holding joint operations do not have power to influence policies, actions and targets (which are defined autonomously by the JO itself or by the subject holding the operational control) and should not be held accountable for the JO performance.

Furthermore, consolidating JOs in the 'reporting entity' as 'own operations', and therefore for the interest held for the purpose of the sustainability statement cannot be applied for the following reasons:

- the majority of ESG data (i.e. such as fatalities, biodiversity and communities) are non- divisible.
- The operator of each JO, where the undertaking doesn't have operational control, can

implement their own methodology to calculate ESG data, from GHG, to Health and safety KPIs, to social matters. This makes it extremely difficult to consolidate consistent and

meaningful data if every JO has different approaches, definitions or methodologies for each key performance indicator.

In light of this, the following modifications to the current IG would be needed:

- Elimination in table at paragraph 52, *'except for joint operations where the assets/liabilities belong to the reporting undertaking and so form part of own operations.'* and retaining the text *'Same as for associates'.*
- Elimination in the first box of the flow chart (labelled 'Reporting Undertaking) at paragraph 53 the following: *'including ..... own assets/ liabilities used in Joint Operations'.*

In addition, in the mapping table referred to in paragraph 52, at the Associate tab titled 'Measuring impacts by metrics in topical standard' we believe the following wording should be eliminated:

- *'Operational control' or 'GHG emissions to the extent of operational control. (ESRS 1 par. 67)'* to make it consistent with paragraphs 40-47 where it is made clear that this concept is applied not only to GHG emissions but also to other environmental metrics, and therefore not limited to GHG emissions.

GHG Scope 3 emissions reporting for the value chain

ESRS E1 AR46(h) clarifies that an entity shall report on scope 3 GHG emissions for:

- consolidated accounting group (the parent and its subsidiaries).
- associates, joint ventures, and unconsolidated subsidiaries for which the undertaking has the ability to control the operational activities and relationship (operational control).
- associates, joint ventures, unconsolidated subsidiaries (investment entities) and joint arrangements for which the undertaking does not have operational control and when these entities are part of the undertaking's upstream and downstream value chain.

While ESRS E1 AR40 is clear that an entity is to report 100% of GHG emissions from entities under operational control (two first categories mentioned in ESRS E1AR46), we do not find similar clarity in the ESRS E1 standard or in the IGVC on how to report scope 3 GHG emissions from entities in the value chain where an entity does not have operational control (i.e. 100% or in accordance with equity share in the entity), and similar for GHG Scope 3 category 15 for investments that are not part of the value chain.

We recommend that for entities where an undertaking does not have operational control that reporting is carried out in accordance with the equity share approach – in line with established methodologies.

In the IGVC paragraph 53 illustration, where the reporting of 100% for entities subject to operational control is clarified, it would be helpful if the percentage to be reported for scope 3 GHG emissions was clarified in the two boxes related to whether an entity was an actor in the value chain or not. If not clarified here, it would be useful to do so in another part of the guidance.

Throughout the guidance, reference to a general principle of aligning with established methodologies would be helpful, rather than generation of new or potentially conflicting ESRS- specific guidance.

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