



Capitals Coalition
Mark Gough, CEO

Social Value International
Ben Carpenter, CEO

European Financial Reporting Advisory Group (EFRAG)
Patrick de Cambourg, EFRAG Chair

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Dear Patrick de Cambourg,

The Capitals Coalition and Social Value International welcome the invitation to comment on the first set of Draft European Sustainability Reporting Standards. The Capitals Coalition and Social Value International are global collaborations working on advancing the way the world understands and accounts for value provided by natural, social, human, and produced capitals. We want to ensure that value is included in decision-making. We work with other organizations and networks, such as the Impact Management Platform, to ensure that information on value is measured and managed to create a positive impact for all.

The organizations in our networks are interested and are supportive of current and future regulations of sustainability reporting standards. We welcome the opportunity of providing feedback on the Sustainability Reporting Standards. Based on our experience, we would like to share our thoughts on of Draft European Sustainability Reporting Standards.

Overall, we felt the standards were useful and thorough, but we have some concerns about their usefulness for decision making processes for businesses and feel there are missed opportunities to ensure that those who apply them can maximise the value for both the business and society.

1. There are lots of duplications and cross referencing of disclosures due to the architecture of the standard

There are lots of duplication of disclosures and cross referencing of disclosures across documents. For example, water pollution is covered from different angles in E2 and E3 respectively. This demonstrates that there is a need to be much more integrated in how these impacts are seen across an integrated view and should avoid siloes.

We encourage: Adopting a new architecture of the standard structured around impact pathways, considering the entry point of impact drivers (i.e., water pollution) or pressures, instead of the current one that mixes asset categories (i.e., water) and impact drivers (i.e., pollution). Following from our previous point, by following the same architecture as the one of Transparent draft Methodology, duplications can be avoided.

2. The standard is not clearly using the concept of business dependencies

The standard focusses on the impacts of an organizations activities but does not clearly recognise that businesses receive benefits from natural, social and human capital that do not go into financial statements (i.e., pollination services).

Reporting for sustainability is linked to the boundary of financial statements. But organizations receive benefits and so depends on natural, human and social assets someone else owns (i.e., atmosphere, sea, climate).

By omitting information on the 'dependencies' of organizations on natural, human, and social capital stocks that go beyond the boundary of financial statements, and by omitting a clear valuation process, the ESRS risks making sustainability reporting burdensome and reduces understanding impacts to a compliance exercise that organizations are forced to complete rather than an assessment that highlights positive and useful information.

Besides, other global standard setters and organizations, such as ISSB and TNFD, have adopted and included the dependencies in their frameworks and standards.

We encourage: To expand the scope of the standard (ESRS 1, section 1.1., para. 3) to explicitly include dependencies on natural, human, and social capital.

3. There are inconsistencies between different documents, especially on the type of information requested to companies (impact driver vs change in state or outcome)

The current standards are requesting two different types of information and not doing this in a consistent way across different disclosure categories. These two types of information are:

- **Impact drivers** (also called 'Outputs' or 'Pressures'): An impact driver is a measurable quantity used as an input to production or a measurable non-product output of business activity. An example is particulate matter emissions.
- **Changes in the state of nature, people, or society** (also called 'outcomes'). The change in state or condition of the capital due to business activities or external factors. Continuing with the previous example, this will be an increase in concentration of Particulate matter in the atmosphere

There is no consistency on the type of information requested on different disclosures. Most of the disclosures are focused on information about impact drivers. Some of the guidance document, such as ESRS E2: Pollution and ESRS E3: Water and marine resources, are asking information on outcomes but not going further to directly request measurable information on them

Other disclosures have very little detail when requesting information on outcomes, like in ESRS E1: Biodiversity disclosures.

We encourage: To be consistent by requesting the same type of information (ideally, outcomes) across disclosures.

4. Information on impacts (understood as consequences on the wellbeing of people) is not requested

The standards are not requesting information on impacts. By this, we mean information on how the changes in state of natural, human, and social capital affect different stakeholders. Information about impacts provide an understanding of the value or relative importance, worth or usefulness to businesses and/or to society of the changes triggered by business activities. This is the information that is relevant and useful for decision makers, from business, finance, and governments. Following from the example provided before where the impact driver were the particulate matter emissions that resulted in changes in air quality, the impact would be changes in health of people (i.e., respiratory diseases).

These impacts can be expressed in qualitative, quantitative, or monetary terms. Following up from the previous example of particulate matter emissions, the value of the impact could be expressed in quantitative terms (i.e., number of respiratory disease affections) or even in monetary terms (i.e., health treatment cost).

Missing this key dimension of impact means information regarding business risks is missed (reputational damage, exposure to future litigation or regulatory changes, losing license to operate, limitations to access to financial resources). All of which may create larger costs in the long run. At no point in this document has wellbeing been addressed which is a key component of value and understanding the impact of sustainability on people's lives.

Impact within ESRS isn't clearly defined, although ESRS2 does define 'double materiality' and 'impact materiality'. Our point being that a definition of impact should include reference to wellbeing as the result. This also highlights that wellbeing isn't considered within ESRS1 or 2 which is a key component of value and a key priority for decision makers when trying to integrate human, social and natural capital implications of business activities. This is essential for a more holistic understanding of value.

We encourage: To include a definition of impact that encompasses the consequences on wellbeing of people. This should refer to the value created or eroded by businesses. Capitals Coalition use the following definition of impact "*Impacts are positive or negative contributions to one or more dimensions of well-being*", which is aligned with the [Impact Management Platform](#) definition, adopted by the [G7 Impact Taskforce](#).

We also encourage to request business report information on impacts. This should be done in a consistent way across all the disclosures. So, following from our previous point (No. 3), companies should be reporting on impacts, rather than impact drivers or changes on state of nature, people and society.

5. We encourage to consider the outputs of EU Life funded Transparent project for companies to progress on the valuation of impacts in monetary terms

As mentioned before, impacts can be valued in qualitative, quantitative, or monetary terms. The Natural Capital Protocol and the Social and Human Capital Protocol could be referenced

to provide guidance on how to measure and value different impacts and dependencies on natural, human, and social capital.

More specifically, we encourage to consider and incorporate in the standards, the progress achieved by EU Life funded Transparent project (see Draft Methodology [here](#)), that provides indications to measure and value natural capital impacts in monetary terms.

The contribution of the preparatory project Transparent is described in the Recital 38 of the CSRD proposal: “In its communication on the European Green Deal, the European Commission committed to support businesses and other stakeholders in developing standardised natural capital accounting practices within the European Union and internationally, with the aim of ensuring appropriate management of environmental risks and mitigation opportunities and reduce related transaction costs. The Transparent Project sponsored under the LIFE programme is developing the first natural capital accounting methodology, which will make existing methods easier to compare and more transparent while lowering the threshold for companies to adopt and use the systems in support of future-proofing their business.”

The monetary valuation of impacts will help to achieve a sustainable transformation of how we do business, as it acknowledges the interconnectedness of business activity and apply a more holistic and scientific approach, avoiding subjectivity and ambiguity.

Finding a common language is difficult in the sustainability dialogue, so more and more initiatives are moving to use monetary terms. This creates one universal language understood by all stakeholders and creates an objective and comparable base for discussion.

Monetary valuation transforms traditionally non-financial impacts on the environment or society (harmful or good) into monetary values.

The first step to do this is to identify relevant activities and measure them to quantify impacts in physical terms. Then select a method to value impacts in monetary terms.

Monetary valuation also brings challenges that manifest in uncertainties around data use and calculations, the selection and use of an interest rate to discount values, and uncertainties about the potential future value of natural capital that yet cannot be estimated.

However, regardless of the critical dimensions, monetary valuation uncovers risks in supply chains and provides a common language for the sustainability dialogue. It operationalizes efforts that can ultimately result in a more sustainable future. It provides an actionable proxy and empowers actors in our economy to speed up their walk towards de-risking operations and a responsible business mainstream.

ESRS1 lacks an ability to properly value the sustainability impacts on value. Monetary valuation is mentioned in passing in the biodiversity offsets section of ESRS E2, E3, and E4 but only in relation to existing market values which doesn't begin to cover the monetary value impact required for comparability in decision-making processes and curtails the usefulness of the sustainability information collected. By using monetary valuation of impacts there will be a common unit of measurement that is useful across the sustainability realms for integrated and holistic decision-making processes.

We encourage to consider the outputs of EU Life funded Transparent project for companies to progress on the valuation of impacts in monetary terms

6. The length of the standard is too long and complicated and may be difficult to apply by many businesses

There are issues with the size of the documentation needed to assess sustainability impacts. It is a large undertaking to read, understand and then apply the guidance even at a broad level. To be able to undertake detailed assessments will require further resources. There are implications that this will deter any company, but especially small and medium enterprises from having the resources to be able to carry out these assessments themselves.

We encourage: To streamline and simplify the standard considerably with emphasis on usability and simplicity where possible.

7. There is a risk that applying this document becomes a tick-box exercise and misses a key opportunity to understand where businesses can add value to their enterprises

Sustainability reporting should be seen as part of a holistic management reporting exercise. Care should be taken that it is not siloed and is instead integrated into decision making processes. Otherwise, it is seen as a 'box ticking exercise' as something that needs to be completed and that doesn't add real value to business, nor to society.

We encourage an approach similar to that of the IFRS sustainability disclosure standard where opportunities are assessed at the same time as risks and demonstrates that investment in key sustainability areas such as the workforce, communities and the environment can create positive outcomes for businesses and is not something that should be merely observed or managed.

8. Further work is needed to ensure that assurance of financial materiality is compatible with double materiality approach

Double materiality is a principle that is central to the CSRD proposal and is represented accordingly in the ESRS materiality assessment approach that sustains the definition of mandatory requirements by the cross-cutting and topical standards. This is also true of the materiality assessment any undertaking is expected to perform, per ESRS 2 – General, strategy, governance, and materiality assessment, to identify its principal sustainability risks, impacts, and opportunities. This in turn, defines what sustainability information must be reported by the undertaking.

- **Double materiality assessment** supports the determination of whether information on a sustainability matter must be included in the undertaking's sustainability report. ESRS 1 paragraph 46 states that "a sustainability matter meets the criteria of double materiality if it is material from an impact perspective or from a financial perspective or from both." Further

indications as to how to implement double materiality is given by ESRS 2 Disclosure Requirement 2-IRO 1, paragraph 74b(iii) and AG 68.

While recognizing that both perspectives are intertwined the Exposure Drafts contain provisions about how to implement the two perspectives in their own rights.

Additionally, in relation to useful information, the definition of stakeholders in para 43 recognizes but does not specify the interests with implications for double materiality. The related issue is that some stakeholders are not in a position to take decisions, and this makes information material without it being useful in the sense used in financial statements. This difference could be explained in the section on connectivity with statements. This issue was explored by IAASB in their guidance on EER providing with a solution by proposing that one of the decision-making users would also act in their interests.

We encourage: EFRAG to work with IAASB to ensure that assurance of financial materiality recognises the need for the assurance provider to have sight of those issues identified for double materiality and the process by which these are filtered. In addition, we would then suggest that, given this information would be necessary to determine financial materiality, it should also be disclosed which would then align with ESRS.

9. Timeframes represented in the document are too short term to fully appreciate the benefits from investing in human, social and natural capital.

Many of the impacts on natural capital will take place over much longer time frames than normal accounting work on. For investments in natural capital and to see the benefits five years is still very short term and longer time frames may be required over decades or even centuries. The time frames set out in the standards are too short to see robust trends that are outside of standard variations between years that may be caused by other factors

We encourage: Guidance is updated to reflect impacts and dependencies, particularly on the environment (natural capital), may be longer than standard financial disclosure timeframes. Impacts may be subject to longer timeframes as well as tipping points. Recovery from these impacts may also be over longer timeframes of decades or even centuries and guidance should reflect this.

10. There is a need for better alignment with international reporting standards

The links between EFRAG and the ISSB should be stronger and more closely considered. For example, the ISSB is now aligned with the Taskforce for Climate-Related Financial Disclosures (TCFD) in adopting a four-part structure whereas the EFRAG standards are based on a three-part strategy. This separation in terms makes it harder for businesses to have a single clear approach to navigating these separate requirements.

We are encouraging that ISSB should follow the structure of IASB if it is to produce useful information that is consistent for the same primary user as for IASB. We would, therefore,

suggest alignment with the structure of IASB but with the motivation of investors changed to recognize that investors are interested in their financial returns and in the impacts for other stakeholders.

We encourage: Closer alignment with international standards, mainly with IFRS standards, in terms of structure as well as content as noted elsewhere in this letter. Alignment will help companies and create better outcomes in the long term both for themselves and the wider public.

11. The document needs to address stakeholder assessment better

Sustainable outcomes are only sustainably if they are operational across all three environmental, economic, and social sustainability realms and the interlinkages between these. The current EFRAG standards fails to address the social realm properly by not giving clear or effective guidance on how a business should engage with stakeholders. Not only will better stakeholder engagement increase human and social capital outcomes it will help to understand how best investment in natural capital can be used to address societal issues through nature-based solutions.

Stakeholder engagement is currently focussed on contractual groups only, i.e., those who are employed at some point in the value chain through formal contracts. This links with our earlier point about EFRAG missing wider public value from its assessment.

We encourage: A wider set of stakeholders are identified by businesses when conducting sustainability assessments beyond contractual groups. These should include, but are not limited to, local and affected communities, workers in the value chain and citizens.

12. The division of social standards into stakeholder group is welcomed

The structure recognizes that social issues are fundamentally about people, as individuals or as groups. Companies can then consider and anticipate the distinct types of impact that each stakeholder group is more likely to encounter in relation to that company's operations and value chain.

We welcome the structure of social standards to support companies identify impacts to different stakeholder groups.



We would be willing to discuss these thoughts further if we can be of any further assistance then please us know.

Kind regards,

Mark Gough, CEO Capitals Coalition

Ben Carpenter, CEO Social Value International

This letter and response have been a collaborative effort led by Marta Santamaría Belda, in collaboration with Tom McKenna (Capitals Coalition), Jeremy Nicholls (Capitals Coalition), and Ben Carpenter (Social Value International), with inputs from Ece Ozdemiroglu (Eftec).