



The Chairman

To the kind attention of

1 February 2024

Mr. Hans Buysse
President
EFRAG
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CC:
Mr. Patrick De Cambourg
Sustainability Reporting Board
Chair
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Mrs. Chiara Del Prete
Sustainability Reporting TEG
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Comments to EFRAG's draft Implementation Guidance IG 2 on Value Chain

Dear Mr. Buysse,

Assirevi is the association of the Italian audit firms. Its members represent the vast majority of the audit firms licensed to audit companies listed on the Italian stock exchange and other public interest entities in Italy, under the supervision of CONSOB (the Italian Commission for listed companies and the stock exchange).

Assirevi promotes and carries out technical research in the field of auditing, assurance and accounting and publishes technical guidelines for the benefit of its members. Assirevi is a founding member of OIC (Organismo Italiano di Contabilità – the Italian accounting standard setter) and collaborates with CONSOB, the Italian accounting profession and other bodies in developing auditing, assurance and accounting standards.

We acknowledge that guidance issued by EFRAG is limited to providing clarifications and illustrations to the European Sustainability Reporting Standards (ESRS) and is non-authoritative in nature, as interpretations are outside of EFRAG's mandate and fall instead under the European Commission's (EC) remit. This caveat informs our comments as summarised in this document (and its attachment).

We welcome EFRAG's efforts to develop guidance on the value chain (and materiality) as interpretations of these areas will be critical in supporting consistency and comparability in sustainability reporting. We really appreciate the clarifications of some key elements of value chain-related topics, such as the different requirements to provide value chain information for impacts, risks and opportunities (IRO), policies, actions and targets (PAT), and metrics; the difference between the requirement to consider the value chain in the materiality assessment and the need to collect value chain data and the inclusion of the value chain map, which clarifies what is needed to be reported on.

However, we believe that there is room to further improve the Value Chain Implementation Guidance (VC IG) to ensure it is comprehensive and can be regarded as a useful tool in applying the ESRS, as better detailed in our comments provided in this document (and its attachment). In particular, we refer to:

- the definition of value chain boundaries;
- the practical application of the concept of "operational control";
- estimated information on the value chain (VC);
- interoperability with international standards.

Value chain boundaries

We understand from the value chain definition that it includes activities, resources and relationships of the entity, as well as of the external environment it operates in. We also appreciate EFRAG's attempt to clarify this complex matter in various paragraphs of the VC IG, including FAQ1.

However, we suggest that EFRAG provide more guidance, including the factors to consider, and examples that further clarify where the value chain starts and ends.

In addition, more guidance and examples would help ease ESRS-related burdens such as for reporting and in making judgements, estimates and assessments.

More detailed guidance would also be useful to better understand reporting requirements and expectations for investments outside the value chain.

Practical application of the concept of "operational control"

We believe that the practical application of the concept of "operational control" is one of the cornerstones for the value chain guidance.

We suggest that EFRAG consider whether it can provide more comprehensive guidance within its remit on this topic. If not, we recommend that EFRAG bring this to the attention of the European Commission as we appreciate that this may be a case where additional interpretation, or an amendment to the European Sustainability Reporting Standards (ESRS), could be warranted.

We would appreciate if the VC IG could include more examples to help illustrate how to approach the concept of operational control, which at this point in time still remains quite theoretical in our view.

We also suggest that EFRAG reconsider the approach to various accounting treatments when finalising the guidance to ensure connectivity. While we appreciate that many connectivity considerations in the ESRS refer to the IFRS, there will be entities applying the ESRS that adopt national accounting standards. Therefore, EFRAG could also consider the Accounting Directive when thinking about connectivity between the ESRS and reporting standards.

Estimated information

The guidance states that entities should aim to gather reliable data from the various players in its VC, but in many cases the use of estimates or proxies appears to be the only available option. Indeed, it is expected that the reliability of information directly obtained from the VC may improve over time, since VC players who may not yet be able to quantify their impacts could be in a position to do so in the future given the evolution of sustainability reporting. Using estimates, similar to financial reporting, is acceptable if determined under a process designed to comply with the characteristics of quality expected from sustainability information.

We call for clearer guidance on the definition of such process, particularly in terms of reliable sources, which is critical for the reliability and quality of information provided, including for assurance practitioners.

Interoperability with international standards

As we find the VC IG very useful, we urge EFRAG to continue its collaboration with the International Sustainability Standards Board (ISSB) and the Global Reporting Initiative (GRI), as it is critical to ensure that their respective guidance, including any future thinking on value chain related matters, is aligned. Alignment of guidance will ensure consistent application of the respective standards, which in turn will facilitate interoperability.

We are deeply appreciative of EFRAG's efforts in prioritising the preparation of this guidance, as we realise that application of the standards will be challenging, particularly for the early years of reporting and for those entities that have not previously reported on non-financial matters under the Non-Financial Reporting Directive (NFRD).

With specific reference to the role of auditors and assurance providers going forward, we acknowledge that the delivery of high-quality assurance services depends on the clarity of the reporting requirements and related guidance, but we are also aware that preparers will need time to collect data and build processes, systems, and internal controls that are needed to support high-quality corporate reporting. As a result, it cannot be ruled out that in this initial phase auditors and other assurance providers may have to issue qualified assurance reports in a number of cases. Clear communication to the markets on the challenges of sustainability reporting may help alleviate market concerns if qualified assurance reports are issued: given the critical role that ESMA and member state regulators will play in this area, we encourage EFRAG to remind the Commission to take appropriate steps in that direction and communicate with them in this respect on a timely basis.

As previously highlighted in our 2023 comment letter on the first set of the ESRS, time appears to be crucial to deliver such guidance as the ESRS have already become effective as of 1 January 2024 for some entities. Following the practical application of new reporting standards over the next few years, further aspects may emerge that require further investigation or requests for clarification to be included directly in the standards when they will be open for revision, or in future versions of this VC IG.

Going forward, the successful implementation and development of additional ESRS and guidance will require a robust due process to give stakeholders sufficient time to express their views. This should include ongoing dialogue with stakeholders to identify issues as well as the development of high-quality guidance by EFRAG. For a more granular analysis of the topics mentioned above, please refer to the detailed comments included in the attachment to this document.

We would welcome the opportunity to discuss these matters further with you if it would be helpful.

Yours sincerely,



Gianmario Crescentino
Chairman

(Enclosure)

COMMENTS ON EFRAG's DRAFT IMPLEMENTATION GUIDANCE

IG 2 on Value Chain

(December 2023)

Chapter 2: Navigating value chain under CSRD and ESRS

Reference	Description
Paragraph 20 (d)	The paragraph refers to Appendix C to ESRS 1 which sets forth the qualitative characteristics of reported information. Appendix C refers to a "List of phased-in Disclosure Requirements", while the correct reference to be included in this paragraph should be Appendix B to ESRS 1 "Qualitative characteristics of information".
Paragraph 36	It would be helpful in our view to provide an explanation as to why subsidiaries are excluded from financial reporting consolidation, especially as regards the considerations to be made about the inclusion or exclusion of these subsidiaries from sustainability reporting. The reference to the materiality guidance does not appear to be sufficiently comprehensive in this respect.
Paragraph 38	This paragraph states that joint ventures and associates may be actors in the value chain, for example, when they are customers or suppliers. The wording suggests that there may be cases other than those mentioned above in which joint ventures and associates could be considered as actors in the value chain. If other cases exist, practical examples would be helpful.
Paragraph 45	This paragraph states that the concept of operational control, as defined by standards ESRS E1 Climate Change, ESRS E2-4 Pollution of air, water and soil and ESRS E4 Biodiversity and ecosystems, could be applied in other circumstances. More details of these other circumstances should be provided as the example is not clear.
Paragraph 49	We suggest that the VC IG should provide practical examples of circumstances in which associates and joint arrangements do not form part of the value chain and, hence, should be treated as "investments", in order to understand how they may give rise to impacts that are connected with the undertaking and how they should be considered in the materiality assessment. While it is specified that topical standards do not have specific reporting requirements indicating how to measures these impacts, the VC IG is not conclusive in this respect and leaves room for interpretation.
Paragraph 52	The note underneath the table states <i>"Please note that this is a very simplified description of the financial reporting requirements (and may differ between IFRS and local GAAP used in European countries) and so does not capture the nuances involved in classifying investments."</i> If the guidance intends to refer to the definitions in the financial reporting framework, the reference to these definitions should be more specific in order to avoid potential different interpretations by both the undertakings and the assurance providers.

<p>Paragraphs 52 and 53</p>	<p>The VC IG does not clarify the treatment of joint operations in the context of sustainability reporting, i.e., when they should be included in the “own operations” metrics or when they form part of the value chain.</p> <p>Specifically, the table in paragraph 52 states for joint operations <i>“Same as for associates except for joint operations where the assets/liabilities belong to the reporting undertaking and so form part of own operations”</i>. Similarly, the flow chart in the next paragraph shows that the “Reporting undertaking” is defined as the <i>“Parent plus subsidiaries (including leased assets and own assets/liabilities used in Joint Operations)”</i>.</p> <p>Based on the above, it seems that data related to joint operations are part of the “Group” and, therefore, should be included in the “own operations” metrics.</p> <p>However, this seems to contradict paragraph 46 of ESRS E1, which states <i>“when disclosing the information on GHG emissions ... for contractual arrangements that are joint arrangements 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”</i>. It follows that, based on ESRS E1 DR6, if the undertaking has operational control of the joint operation, it should include the joint operation’s full GHG emissions in its “own operations” (scope 1 and 2); otherwise, it should include them in the scope 3 emissions based on the existing business relationship. Moreover, paragraph 62 of ESRS 1 states that, if an undertaking is a parent company required to prepare consolidated financial statements, the sustainability report will be for the group. Both the Accounting Directive and IFRS 10 define a “group” as a <i>“parent and its subsidiaries”</i>. Finally, paragraph 67 of ESRS 1 does not refer to joint operations although it states that the metrics for joint ventures and associates should be reported in accordance with the approach adopted for the other business relationships in the value chain.</p> <p>A solution to these inconsistencies could be to:</p> <ul style="list-style-type: none"> -eliminate the words <i>“except for joint operations where the assets/liabilities belong to the reporting undertaking and so form part of own operations”</i> in the far-right column relating to joint ventures and joint operations and just leave <i>“Same as for associates”</i>; -eliminate the words <i>“(including ... own assets/liabilities used in Joint Operations)”</i> in the first box in the flow chart. More broadly, we believe that the flow chart could even be taken out of the document, as it does not add clarity to the concepts already presented in the previous paragraphs. <p>In the end, the treatment of joint operations as actors in the value chain is consistent with the fact that, if operational control does not exist, the entities with investments in joint operations do not have the power to independently influence policies, actions and targets and, hence, the joint operations can decide what disclosure methods to adopt.</p>
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	In addition, with respect to the line "Associate" in the table, we recommend eliminating the sentence " <i>GHG emissions to the extent of operational control. (ESRS 1 par. 67)</i> " that follows the heading "Operational control" in the right-hand column "Measuring impacts by metrics in topical standards". This would ensure consistency with paragraphs 40 to 47 which clarify that this concept is applied not only to GHG emissions but also to the environmental metrics, and possibly the social standards.
Paragraphs 52 and 53	The VC IG does not include circumstances in which there could be double reporting along the value chain. We recommend that this concept be supplemented with an indication of where this situation can arise most frequently or with greater probability.
Paragraph 69	We suggest making reference not only to the document on the LSME ESRS but also to the VSME ESRS.

Chapter 3: FAQ 1

Reference	Description
Paragraphs 71-74	<p>As it is formulated, the FAQ should inform the identification of the extent of the VC. However, it is not clear from the answer how far the analysis should extend.</p> <p>In addition, paragraph 74 includes three examples of risks and opportunities arising from dependencies on natural, human and social resources which refer to tier 1 only. We recommend including examples that extend to the other tiers as well.</p> <p>Moreover, neither the Commission Delegated Regulation (EU) 2023/2772 nor the VC IG provide a definition of what a "tier" is. Therefore, given the lack of a clear definition of the extent of the value chain, the undertaking has to define this through an internal due diligence process, as well as identifying the material IRO. We believe that it is fundamental for the guidance to emphasize the importance for undertakings to have a governance and internal control systems that are able to identify where the IRO are in the value chain and the extent of the value chain (when this is relevant).</p>
Paragraph 72	With respect to " <i>the location and characteristics of suppliers included beyond the first tier of their upstream VC or supply chain</i> ", we recommend adding the words " <i>where applicable</i> " or " <i>where relevant</i> " (as it may be very complex for financial intermediaries to go beyond the first tier and, moreover, it probably would not be very relevant with respect to their supply chains).

Chapter 3: FAQ 3

Reference	Description
Paragraphs 89, 126, 131 and 151	<p>The possibility of obtaining information or making estimates when reliable data from the actors of the value chain are not available is dealt with in several paragraphs. We recommend concentrating in just one paragraph the discussion on the use of estimates to present information about the value chain.</p> <p>Paragraph 131 states that <i>“Using estimates, similar to financial reporting, is acceptable if organised under a process designed to comply with the characteristics of quality expected from sustainability information.”</i> However, the VC IG does not provide any explanation of either the process to be followed by the undertaking to guarantee the quality of the information or the minimum elements of an estimate (e.g., methods and assumptions). This issue is of great importance for the purpose of providing assurance about sustainability statements, and more guidance should therefore be provided.</p>
Paragraphs 90, 91, 92 and 93	<p>Paragraph 93 refers to the three types of involvement of an undertaking in determining impacts: <i>“cause, contribute or be directly linked to an impact in the value chain”</i>. It states that it is important to distinguish the type of involvement as it could lead to a different assessment or categorisation of negative impacts. We believe that a presentation of the three types of involvement in a graph would be helpful as this would also clarify the implications on the assessment and categorisation of negative impacts. Practical examples could also be included. This would complete paragraph 93, which is otherwise inconclusive in our view.</p>

Chapter 3: FAQ 4

Reference	Description
Paragraphs 95-113	<p>Paragraph 100 describes how the due diligence process is used to collect information about the value chain. However, there is no guidance about how to perform this process (or details about the various methods).</p> <p>Given that, as specified in paragraph 105, ESRS 2 BP-1 requires an undertaking to specify the <i>“extent of any limitations”</i> on the materiality assessment process with respect to the VC, we believe that the definition of a <i>“limitation”</i> should be included.</p> <p>One approach could be to include more specific guidance for the due diligence process or, should this not be possible, to highlight its subjective nature, with disclosure thereof in the sustainability reporting.</p>
Paragraph 109	<p>As this paragraph solely refers to ESRS 2 without providing any additional implementation guidance, we believe it should be removed.</p>

Chapter 3: FAQ 5

Reference	Description
Paragraph 114	The references to ESRS 2 paragraphs 64(b), 67(b) and 70(b) appear to be misstated and should be replaced by "ESRS 2 paragraphs 65(b), 68(b) and 79(b)".

Chapter 3: FAQ 7

Reference	Description
Paragraphs 128 and 129	<p>The VC IG in paragraph 128 refers to a case where, given the severity of the impact, the actors of the value chain could be strongly incentivised to omit sensitive information, which could compromise the reliability of the information.</p> <p>The second paragraph notes the current operating difficulties for some VC actors in providing the requested information and states that <i>"supporting such actors to set up effective systems may be important"</i>. It continues by saying <i>"It may be advisable to engage with them and where relevant, also encourage them to do the same with their value chains"</i>. We recommend integrating this paragraph to indicate the need for the undertaking to carefully evaluate the reliability of the data provided by the actors of the value chain and to implement suitable processes and controls and, if appropriate, to make estimates as per paragraph 131. This aspect could be particularly critical for the purpose of providing assurance, if the reliability of data included in the sustainability reporting is not sufficiently supported.</p>
Paragraph 133	This paragraph refers to the requirement to disclose the metrics that include VC data estimated using indirect sources, and includes considerations about their <i>"level of accuracy"</i> . We recommend that additional guidance be provided to clarify this latter concept.

Chapter 4: VC map

Reference	Description
Paragraph 155 VC coverage map of Set 1 ESRS	With respect to the disclosure requirements regarding item 4 in the table (<i>"The undertaking shall reflect whether and how policies, actions or targets (PAT) cover VC"</i>), reference is also made to the DR from S1-1 to S1-5. We believe that this reference is incorrect, as these disclosure requirements relate to own workforce (and, therefore, own operations) and should therefore be removed. The fact that the above disclosure requirements do not relate to the value chain is confirmed by the fact that they are referred to under item 6 in the same table (<i>"The disclosure only reflects own operations, as no coverage of VC is required"</i>).
Paragraph 157	This paragraph has cross references to paragraph 114 and does not add anything new. It should be eliminated in our view as it is redundant.