



DRSC • Joachimsthaler Str. 34 • 10719 Berlin

EFRAG
Mr Patrick de Cambourg (SRB Chair)
35 Square de Meeûs
B-1000 Brussels

**Sustainability Reporting Technical
Committee**

Phone: +49 (0)30 206412-12

E-Mail: info@drsc.de

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ED ESRS LSME and ED ESRS VSME

Dear Patrick,

on behalf of the Sustainability Reporting Technical Committee of the Deutsches Rechnungslegungs Standards Committee (DRSC) I would like to thank you for the opportunity to comment on the Exposure Drafts for the *ESRS for Listed Small- and Medium-sized Enterprises* (ED ESRS LSME) and the *Voluntary ESRS for Non-listed Small and Medium-sized Enterprises* (ED VSME ESRS).

We would like to provide our general feedback to these Exposure Drafts in this cover note. Further, more detailed, feedback is included in the answers to EFRAG's questionnaires.

The DRSC believes the ED ESRS LSME and the ED VSME ESRS to be very important documents of the ESRS literature. While the scope of the ED ESRS LSME might be limited, it is intended to work as the value chain cap and will, therefore, have a significant effect on the sustainability reporting of all companies (large enterprises as well as non-listed SMEs). In addition, potentially thousands of non-listed SMEs are looking for harmonised sustainability reporting standards in order address their stakeholders' numerous and still quite diverse sustainability information needs while keeping their own reporting burden within manageable limits.

Since their publication in January 2024 the DRSC has conducted a wide range of activities to explore the merits, possible issues, and the potential for improvements of both EDs. To this end the DRSC participated in and/or supported field tests for the ED ESRS LSME and the ED VSME ESRS (a total of about 30 enterprises, some of which are also participating in EFRAG's field testing) and conducted interviews with stakeholders, such as banks, large corporations, rating agencies, and data providers. As a result, we came to conclude that a comprehensive revision of the standards is advisable. In our view this revision must consider the following findings:

Contact:

Joachimsthaler Str. 34
D-10719 Berlin
Phone: +49 (0)30 206412-0
Fax: +49 (0)30 206412-15
E-Mail: info@drsc.de

Bank Details:

Deutsche Bank Berlin
IBAN-Nr.
DE26 1007 0000 0070 0781 00
BIC (Swift-Code)
DEUTDE33XXX

Register of Associations:

District Court Berlin-Charlottenburg, VR 18526 Nz
President:
Georg Lanfermann
Vice President:
Prof Dr Sven Morich

For the ED ESRS LSME:

- In Germany, approximately 40-50 listed SMEs (listed on the regulated market, not including other segments, such as the open market) and around 1.000 SNCIs will be in the scope of the ESRS LSME. This standard does not yet sufficiently address the specific characteristics and sustainability reporting needs of these undertakings.
- For example, in line with the CSRD the LSME's scope is limited to the preparation and presentation of an individual sustainability statement only. Listed SMEs are usually structured as groups and will therefore need to prepare a sustainability statement from their group's perspective in order to address the needs of users of their sustainability information. However, a consolidated sustainability statement must follow ESRS Set 1 which contradicts the EU-Legislators' objective to reduce the burden of these SMEs and to address their specific circumstances (e.g. less capacity, less complex structures etc.). During our outreach activities mentioned above preparers indicated that this would discourage SMEs from participating in the capital markets rather than increase the potential for SMEs to move towards capital market participation.
- On the other hand, the ED LSME ESRS does not address the specifics of the business model of financial institutions, such as SNCIs which are the vast majority of undertakings in the scope of the LSME ESRS.
- Furthermore, due to the complexity of the standard and the scope of the comprehensive disclosure requirements we believe the ED ESRS LSME to not effectively limit the requirements for large companies to obtain sustainability information on the value chain (so called value-chain-cap-function).

For the ED VSME ESRS:

- This ED represents a valuable and very good starting point for the further discussion of VSME ESRS and to develop a widely accepted standard for harmonised sustainability information of SME. We support the purpose of the ED to, inter alia, provide sustainability information according to the requests from lenders or suppliers. Especially the basic module with its focus on twelve sustainability reporting areas and the "if applicable"-approach (rather than the "if material"-approach) allows undertakings to effectively deal with and address the sustainability information needs expressed by their stakeholders.
- However, while EFRAG expects the VSME ESRS to have an "in fact" value-chain-cap-function once the standard is widely accepted in the market, preparers expect the comprehensive legal reporting requirements for their stakeholders to trickle down to non-listed SMEs nevertheless. This would result in enhanced sustainability information requests addressed to SMEs, contrary to the intention of the legislators.



- Some of the sustainability information requirements laid out in the PAT- and BP-module as well as the materiality assessment required for those modules, however, pose too great a challenge for the SME preparers.
- One of the challenges for EFRAG in reviewing the ED after this consultation will be to consider the differing sustainability information needs. While the ED, with the basic module and some additional data points, overall addresses credit lenders' information needs for financing purposes, in our understanding the information needs of customers that are large undertakings differ. The latter seek information on risks along the value chain, information on the management of those risks as well as sustainability information on the products they purchase from the SME.

In conclusion, the DRSC's Sustainability Reporting Technical Committee believes that a significantly less complex but effective value-chain-cap will help to address these findings. Therefore, we strongly believe that the ED ESRS LSME should be re-designed to correspond to the current ED VSME ESRS. In addition to the sustainability information stemming from the three modules of the VSME ESRS the specific needs of the capital market participants would have to be addressed by including the "EU-datapoints" (such as information on principal adverse impact indicators, PAIs, as laid out in the SFDR). In our view this streamlined ESRS LSME will better reflect the objectives for the sustainability reporting of SMEs. Regarding the ED VSME ESRS we propose reviewing the specific user needs, and to re-design the standard to clearly target the differing sustainability information needs.

If you would like to further discuss our views, please do not hesitate to contact Kati Beiersdorf (beiersdorf@drsc.de) or me.

Yours sincerely,

Georg Lanfermann

President