WORLD FEDERATION OF EXCHANGES

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# Response: European Financial Reporting Advisory Group's (EFRAG) public consultation on the first set of draft European Sustainability Reporting Standards (ESRS)

3 August 2022

## Background

The World Federation of Exchanges (WFE) is the global trade association for regulated exchanges and clearing houses. We represent the operators of over 250 market infrastructures, spread across the Asia-Pacific region (37%), EMEA (43%) and the Americas (20%), with everything from local entities in emerging markets to international groups based in major financial centres. In total, member exchanges trade around $100 trillion a year and are home to some 60,000 companies, with an aggregate market capitalisation of around $120 trillion. The 50 distinct central counterparty (CCP) clearing services (both vertically integrated and stand-alone) collectively ensure that traders put up $1 trillion of resources to back their risk positions.

With extensive experience of developing and enforcing high standards of conduct, WFE members support an orderly, secure, fair and transparent environment for all sorts of investors and companies wishing to invest, raise capital and manage financial risk.

Founded in 1961, the WFE seeks outcomes that maximise financial stability, consumer confidence and economic growth. We also engage with policy makers and regulators in an open, collaborative way, reflecting the central, public role that exchanges and CCPs play an internationally integrated financial system.

If you have any further questions, or wish to follow-up on our contribution, the WFE remains at your disposal. Please contact:

Christine Brentani, Senior Manager and Sustainability Lead, Regulatory Affairs: cbrentani@world-exchanges.org

Richard Metcalfe, Head of Regulatory Affairs: rmetcalfe@world-exchanges.org

Nandini Sukumar, Chief Executive Officer: nsukumar@world-exchanges.org

# Financial Reporting Advisory Group's (EFRAG) public consultation on the on the first set of draft European Sustainability Reporting Standards (ESRS)

## General Comments

Investors, issuers and other stakeholders continue to demand high-quality sustainability-related information about their investments. Investors use sustainability data to evaluate the environmental, social and governance (ESG)-related context of their investments. Focus from investors on impact[1] and sustainable investing has grown considerably, with ESG assets expected to hit $53 trillion by 2025 - representing a third of global assets under management.[2]

Exchanges sit at the interchange between issuers and investors and are crucial players for the operation of standards in a 'live' and constantly evolving environment. The WFE has been a long-standing advocate for harmonization of sustainability-related reporting requirements as a means of encouraging consistent and comparable disclosures amongst listed issuers which will benefit investors and other stakeholders.

For several years, the WFE's own Annual Sustainability Survey has highlighted the lack of consistency in disclosure frameworks as a risk to investors.

To this end, the WFE welcomes the aim of the European Financial Reporting Advisory Group's (EFRAG) draft European sustainability reporting standards' (ESRS) to create more standardized reporting in the EU. We also note, and support, that the ESRS incorporate the Task Force on Climate-related Disclosures (TCFD) recommendations. As the TCFD reporting recommendations have been in place since 2017, they form a good basis for the development of standardised sustainability reporting. We note that other sustainability reporting standards being developed around the globe (such as the International Sustainability Standards Board (ISSB) general sustainability-related disclosures and climate-related disclosures exposure drafts and the US Securities and Exchange Commission (SEC) proposals for climate-related disclosures) also utilise the TCFD requirements as their foundations.

However, one of our main concerns relates to the burden that the requirements might pose on certain issuers. Smaller and medium-sized listed issuers may struggle to provide the volume of information required. The risk also exists that if companies find it too onerous to provide the required information, they may opt to remain in or move to the private markets, which will result in less transparency for the general public.

Interoperability between the ESRS and other jurisdictional or global standards is key. Given that the requirements are geared towards a more mature listed issuer environment, those listed issuers in less developed or less mature markets who voluntarily want to comply with the requirements might find it too onerous. A potential consequence is that the universe of investments in certain cases might become limited to those listed issuers that report exclusively under the ESRS, thus preventing diversification opportunities that might otherwise be available for end investors in the EU.

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[1] Investments made with the intention to generate positive, measurable social, environmental impact alongside financial return.
[2] Bloomberg blog, ESG assets may hit 53 trillion by 2025.

Given the complexity involved in meeting some of these requirements, we believe that a phased in approach for implementation would help the provision of valuable and relevant information to investors in a timely manner. Reporting against the standards will be an iterative and evolutionary process and in order to promote consistency globally, the WFE has also asked the ISSB and the SEC to consider a similar approach for their climate-related disclosure framework.

We focus our observations on the following areas:

- Interoperability
- Proportionality
- Provision of material information
- Interconnectedness of the EU's sustainability-related regulatory developments.

## Specific Comments

**Interoperability**
As currently drafted, the ESRS are amongst the most prescriptive sustainability reporting requirements under development globally. Many jurisdictions are likely to promote the ISSB sustainability standards which contain different parameters in a number of areas, such as the area of materiality. The ISSB requirements focus on single/financial materiality[3] whereby the ESRS demand double materiality[4] considerations. The SEC sustainability disclosure requirements also diverge in some areas. We urge EFRAG to continue its discussions with the ISSB and the SEC to ensure that there is recognition of equivalence amongst the different global regulatory and normative reporting standards.

We believe a negative outcome would ensue for EU-based end clients if European investors avoided making investments in listed issuers in jurisdictions that did not meet the EFRAG standards, but that met global sustainability reporting standards such as the ISSB standards, for instance. To avoid penalising end investors, it is essential that the ESRS are interoperable with other recognised global and jurisdictional standards.

**Proportionality**
A risk exists that companies may seek to avoid coming under the scope of the requirements. In particular, this risk applies to small and medium-sized enterprises (SMEs). Companies that avoid listing may not, as a result, be providing investors and potential investors with valuable sustainability-related information they require. Another risk is that existing listed issuers may decide to de-list if the reporting requirements become too onerous. This too will reduce transparency of information to the market. In order to enhance transparency of information to the general public and end investors, the requirements should aim to strike the right balance between quantity and quality of information that is material and important for end investors. A proportional approach is essential.

**Provision of material information**
The ESRS covers a broad array of climate, social and governance metrics and information. Whilst this is laudable, we recommend that EFRAG focus on the key, material elements so that the reporting is more manageable for all types of listed issuers who fall under the scope of the requirements or who might want to voluntarily provide the disclosures. We also recommend that EFRAG consider adopting a phased-in approach for implementation as this might make the implementation more manageable and will allow users of the information, including end investors, time to become accustomed to the new level of information that will become available.

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[3] Consideration of sustainability risks to the company.

[4] Consideration of sustainability risks to the company plus consideration of the impacts of companies on society and the environment.

**Interconnectedness of the EU's sustainability-related regulatory developments**

We recommend that EFRAG works closely with other areas concerning sustainable finance regulation in and among the groups associated with the European Commission, to align corporate with investor reporting requirements (through the EU Taxonomy and EU Sustainable Finance Disclosures Regulation (SFDR)) and with the developments of the European Single Access Point (ESAP).