

Jean-Paul Gauzès Square de Meeûs 35 B-1000 Brussels BELGIUM  By email: jean-paul.gauzes@efrag.org	7 January 2021
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Dear Mr Gauzès

**Re: CONSULTATION DOCUMENT ON THE AD PERSONAM MANDATE on potential need for changes to the governance and funding of EFRAG**

EY Europe welcomes the opportunity to offer its views on the possible changes to the governance and financing of EFRAG, in the event that EFRAG is entrusted with the development of EU non-financial reporting standards.

The Consultation Document contains questions in addition to those posed in the first public invitation to comment issued on 1 October 2020. We responded to that invitation to comment in our letter of 3 November 2020.

In this letter we set out our answers to the additional questions raised in the Consultation Document. However, we would also refer you to the points made in our letter of 3 November 2020 where we stressed the importance of multi-stakeholder involvement, the need for clear roles for bodies within the new structure including strong and separate governance/oversight, a separate non-financial reporting standard setting team and periodic reassessment of governance arrangements.

Should you wish to discuss any of the contents, please contact me or Leo van der Tas, EY's Global IFRS Leader (leo.van.der.tas@nl.ey.com) on +31 8840 75035.

Yours sincerely



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## Appendix - Response to questions

### **QUESTION 1 - DUE PROCESS**

***Do you agree that the above reflects the key due process steps for open and transparent non-financial standard setting? If not, which other steps would you advise me to consider or to remove?***

We agree that the elements set out above reflect the key due process steps necessary. However, we note that if EFRAG were to carry out all steps proposed for all projects, this would be highly resource intensive and might lead to a slow pace of standard setting. For example, EFRAG might want to distinguish between standard-setting in an entirely new field as opposed to standard-setting that builds on existing (international) standards. Therefore, we recommend that EFRAG develop a due process handbook that sets out the purpose of the due process steps, which steps are necessary in which circumstances, and the length of consultation periods. In addition, EFRAG should consider whether, akin to the IASB, it believes a Due Process Oversight Committee (DPOC) would be warranted to evaluate and guide its due process arrangements. We refer also to our comments on the topic in our letter to you dated 3 November 2020.

### **QUESTION 2 - MEMBER STATES AND NATIONAL PUBLIC AUTHORITIES**

***Considering the proposed new governance structure (see section 5 EFRAG proposed new core structure) at what level do you consider that the relevant national authorities should be involved and should they be members or observers:***

- ▶ ***EFRAG General Assembly?***
- ▶ ***The EFRAG Board responsible for the oversight of the Non-Financial Reporting Board (see diagram in the Preliminary Report)?***
- ▶ ***The Non-Financial Reporting Board?***
- ▶ ***TEG for Non-Financial Reporting?***

***Should a Consultative Forum (similar to the Consultative Forum of Standard Setters in the Financial Reporting pillar) or any other form of advisory committee; be created for the Member States and national public authorities?***

The role of Member States in EFRAG's standard-setting will depend on the legal framework around non-financial reporting. If the European Commission has delegated authority to adopt these standards, then it would stand to reason that Member States play a direct role in EFRAG's processes and the development of the standards. If not, then Member States would be able to exercise their rights in the approval process of the standards after they have been developed by EFRAG.

**QUESTION 3 - EUROPEAN INSTITUTIONS AND AGENCIES**

*Considering the proposed new governance structure (see section 5 EFRAG proposed new core structure) at which level do you consider European institutions and agencies should have representatives and should they be members or observers:*

- ▶ *The EFRAG Board responsible for the oversight of the Non-Financial Reporting Board (see diagram in the Preliminary Report)?*
- ▶ *The Non-Financial Reporting Board?*
- ▶ *TEG for Non-Financial Reporting?*
- ▶ *The Working Groups?*

*Should a Consultative Forum or any other form of advisory committee; be created for European Institutions and Agencies to provide input to the TEG for Non-Financial Reporting and the Non-Financial Reporting Board?*

European institutions and agencies can provide valuable domain expertise on non-financial reporting that should be used to the fullest extent, which could be made possible by their participation in the 'TEG for Non-Financial Reporting', working groups or consultative forum. As some of these institutions and agencies also have enforcement responsibilities, it would make sense if the European institutions and agencies took an (observer) role that is similar to the role of the European Supervisory Authorities in the current EFRAG structure for financial reporting.

**QUESTION 4 - PRIVATE SECTOR AND CIVIL SOCIETY**

*Considering the proposed governance structure (see section 5), at which level do you consider private sector and civil society ought to have representatives:*

- ▶ *The EFRAG Board responsible for the oversight of the Non-Financial Reporting Board (see diagram in the Preliminary Report)?*
- ▶ *The Non-Financial Reporting Board?*
- ▶ *TEG for Non-Financial Reporting?*
- ▶ *The Working Groups?*

Given the need for domain-specific expertise, private sector and civil society representatives would be able to provide substantial contributions to the work of the Non-Financial Reporting Board, TEG for Non-Financial Reporting and Working Groups in the technical development of the standards. As noted in our response to Question 1, the standard setting process itself should follow specific criteria to preserve quality: independence from external factors (e.g., political interference), impartiality, and due process.

We note that EFRAG's role regarding financial reporting (i.e., providing endorsement advice on international standards) is fundamentally different from its prospective role regarding non-financial reporting standards (i.e., standard setting). Also, the European Union seems to have chosen a multi-stakeholder perspective on non-financial reporting whereas the current work of EFRAG in the area of financial reporting is more geared to serve capital markets. Therefore, we do not believe that stakeholder groups that only contribute to the work of the Non-Financial Reporting Board should be given responsibilities in the new EFRAG Board for activities on financial reporting.

**QUESTION 5 - SMEs**

*Considering the proposed governance structure (see section 5 ), at which level do you consider SMEs (SMPs) should be represented:*

- ▶ *The EFRAG Board responsible for the oversight of the Non-Financial Reporting Board (see diagram in the Preliminary Report)?*
- ▶ *The Non-Financial Reporting Board?*
- ▶ *TEG for Non-Financial Reporting?*
- ▶ *A SME- focused Working Group?*

*Would it be sufficient to seek input of SMEs/SMPs in the public consultation and outreaches rather than involve them in the governance bodies?*

In our view, to the extent that Small and Medium-Sized Enterprises (SMEs) will have to apply the non-financial reporting standards, it would make sense either 1) for SMEs to be represented in the Non-Financial Reporting Board or TEG for Non-Financial Reporting or 2) to ensure that EFRAG's public consultations and outreaches specifically addressed the concerns around SMEs. An SME-focused working group would only make sense if EFRAG were developing a non-financial reporting standard that exclusively applied to SMEs, otherwise it would lead to parallel discussions on the same topic that would then need to be reconciled.

Finally, as the new EFRAG Board will also deal with the processes around financial reporting requirements that do not apply to SMEs, we do not believe it is appropriate for SMEs to participate in the new EFRAG Board activities on financial reporting.

**QUESTION 6 - COOPERATION WITH OTHER STANDARD SETTERS AND INITIATIVES**

*What do you see as main features of cooperation with the (global) reporting initiatives?  
What kind of involvement could you consider?*

Whatever solution or regime is chosen for non-financial reporting, it is important to address urgent stakeholder needs while, at the same time, building towards a globally consistent framework for corporate reporting and set of standards for NFR in the long term. This is particularly important where non-financial reporting is relevant for the proper functioning of capital markets as they are global.

We believe the work of the Non-Financial Reporting Board should, as much as possible, build on and align with international standards in the non-financial reporting domain.

Representatives of existing international standard setting bodies could be involved in technical working groups that develop the standards.

**QUESTION 7 - EFRAG BOARD**

*What in your view should be the maximum size the new EFRAG Board?  
Which stakeholders should be represented and in which proportion?  
Should there be observers? If so, who should be the observers?  
Do you foresee any obstacles that may arise were the EFRAG Board charged with oversight to include representatives of the Non-Financial Reporting Board and the Financial Reporting Board?  
Should the EFRAG Board appoint the members of both TEGs and the European Lab, or should this be done by their respective Boards (Non-Financial Reporting Board and the Financial Reporting Board)?*

In the existing EFRAG structure both the current EFRAG Board and TEG deal with aspects of the technical work. We believe that a strong and transparent governance/oversight role is crucial to ensure the credibility and acceptance of non-financial reporting standards by all stakeholders. Therefore, the governance/oversight role needs to be separate so that it can focus on the relationship with stakeholders, nomination of those in the standard setting roles, the quality of the due process, and the funding of different parts of the organisation.

If the purpose of the new EFRAG Board is to provide governance and oversight of the Non-Financial Reporting Board and Financial Reporting Board then dual membership at two levels in the structure would not be appropriate and could harm the credibility of the new EFRAG Board.

The question whether the new EFRAG Board should appoint members of both TEGs raises questions about the separation of duties between the roles of the various boards and whether it is strictly necessary to have a Non-Financial Reporting Board that is separate from the TEG for Non-Financial Reporting.

**QUESTION 8 - NON-FINANCIAL REPORTING BOARD**

*What in your view should be the maximum size of the new Non-Financial Reporting Board?  
Which stakeholders should be represented and in which proportion?  
Should there be observers? If so, who should be the observers?  
Should the Non-Financial Reporting Board members be appointed by the EFRAG General Assembly on recommendation of the EFRAG Board or directly by the EFRAG Board?  
How can the interconnectivity between the Financial Reporting Board and the Non-Financial Reporting Board be ensured?*

Please refer to our answer to Question 7 where we refer to the Non-Financial Reporting Board.

**QUESTION 9 - TEG FOR NON-FINANCIAL REPORTING**

*What in your view should be the maximum size of the new Non-Financial Reporting TEG?  
Which stakeholders should be represented and in which proportion? Should there be observers? If so, who should be the observers?  
Do you agree that EFRAG NFR TEG members are recommended by the EFRAG Non-Financial Reporting Board but appointed by the EFRAG Board rather than be appointed by the EFRAG Non-Financial Reporting Board?  
How can the interconnectivity between the Financial Reporting TEG and the Non-Financial Reporting TEG be ensured?*

The maximum size of the TEG for Non-Financial Reporting should be similar to that of the existing Financial Reporting TEG (i.e. ideally not more than 12 to 15 members) because it strikes an appropriate balance between broad representation and meeting manageability.

Interconnectivity between the Financial Reporting TEG and the Non-Financial Reporting TEG can be ensured by way of occasional joint meetings between the TEGs and close cooperation between the staff of the EFRAG secretariat that works on the various projects.

**QUESTION 10 - ACTIVITIES OF THE EUROPEAN LAB**

*Do you agree that there is a need for a European Lab activity in the revised EFRAG governance structure?*

*Do you agree that the European Lab could address both non-financial reporting and financial reporting activities?*

*Do you have other comments or suggestions regarding the activities of the European Lab?*

To date the European Lab has been focused on fact finding, rather than the development and testing of new ways of financial reporting. For the European Lab to contribute it should be clearly defined what its relationship to the Boards and the TEGs should be. In our opinion, the European Lab would be most useful if it would be able to focus on carrying out pro-active projects related to non-financial reporting.

**QUESTION 11 - FUNDING**

*Considering the proposed governance structure in this consultation document:*

*Should the majority of the funding, or even all the funding, be provided by the European Commission and the Member States?*

*Is it important that the private sector contributes to the funding and why? Should the public-private sector partnership model also be reflected in the funding?*

*Would a levy at national or European level be feasible?*

*What alternative financing mechanism would you suggest being considered?*

Other respondents are better placed than EY to answer this question.