Brussels, 13th January 2021

EACB comments to the EFRAG's *ad personam* mandate on Non-Financial Reporting Standard Setting

13th January 2021

Executive summary:

- Although the EACB supports the proposed EFRAG governance chart and new structure that envisages the two-pillar approach to deal with non-financial reporting standards alongside the current pillar dealing with financial reporting (as it was already suggested during the first consultative process), we believe it should be however necessary to better clarify the functional distinctions between the EFRAG Board in charge of Governance and the two Boards. In order to guarantee interconnectivity between the Financial Reporting Board and the Non-Financial Reporting Board we believe that a possible solution could be to appoint some members of the FR Board observers of the NFR Board and vice versa, strengthening in this way the cooperation between the two bodies.

-With regard to non-financial reporting, the EACB believes that in addition to the stakeholders currently members of EFRAG, other players are relevant and may be willing to join EFRAG and become fully involved in the standard setting preparatory process. Nevertheless, the EACB insists on the need to hugely involve banking association due to the fact that non-financial reporting could represent a challenge for banks according to the reporting requirements that are being developed under the new legislative provisions. We believe that banking associations already members of the EFRAG should be efficiently involved in each level of the governance of the new non-financial pillar (NFR Board, NFR TEG and NFR WGs). The same should occur for the relevant existing standard setter organizations.

- We support EU leadership in NF reporting standard setting as a solution is needed in the short term (according to the European sustainable finance legislative framework) although this will represent an interim answer with the aim to stimulate and accelerate the process to create a worldwide recognized NFR standard (possibly based on the European proposal). To better guarantee an alignment between the different international non-financial reporting initiatives and

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the EFRAG future activities, we believe that IASB could be appointed as observing members of the Non-Financial reporting Board of the new structure.

- We believe that if the European Commission will increase its participation in the EFRAG funding (with a view to maintain the private/public cooperation) it should be properly represented in the EFRAG Board. Other relevant entities and institutions such as the new Platform on Sustainable Finance should be regarded as members of the EFRAG Board, contributing at the same time also to providing technical advices at the level of the non-financial reporting TEG. As already highlighted in our previous answer to the first consultation on the EFRAG governance, if EFRAG were involved in the development of non-financial reporting standards in a revised NFRD, we believe it should follow the same working arrangements with the EU Commission that are in force for the financial pillar (level II type measures) providing advice to the European Commission and maintaining, at the same time, the formal power to adopt the standards in the European Commission. We acknowledge that the non-financial pillar as standard setter will be mainly funded by European public authorities. However, we recommend to guarantee a fair percentage of private funding (i.e. 30% private) to ensure a broader representativeness and independence.

QUESTIONNAIRE

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?

EACB answer: As it is stated in the consultation document, EFRAG's legitimacy is built on its transparency, governance, due process, public accountability and thought leadership. Since its establishment, EFRAG has put in place for its financial reporting activities, a transparent public due process that has developed over time. This process allows all and mainly European constituents to put forward their views for consideration by EFRAG and ensures, at the same time, that the diversity of accounting and economic environments and views in Europe were taken into account in determining EFRAG's positions. The EACB supports the establishment of the same process in the development and of the EFRAG non-financial reporting pillar.

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?

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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?

EACB answer: We believe that relevant national public authorities should be included in the governance of the non-financial reporting pillar to provide input about whether any future standards are responsive to the public interest; the participation of these institutions is probably necessary for a higher credibility. However, if national standard setters are represented, it might be appropriate to establish a consultative forum for that purpose.

Moreover, we believe that national accounting standards setter should be involved in the process of developing European non-financial reporting standards. However, we highlight that a too large number of participants can create difficulties in the decision process. For this reason, we suggest making a distinction between voting Members and technical experts, to ensure the decision-making process will be more efficient and functional without compromising representativeness.

In particular, to the extent that Member States will contribute to the financing of EFRAG, we envisage they could play an active role in the EFRAG General Assembly.

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?

EACB answer: EACB believes that it is really difficult to make a selection as the number of EU agencies working in the ESG and sustainable finance field is currently increasing (i.e. EU Sustainable Finance Platform, EEA, ESAs, ECB, JRC). To involve them in the development of future standards we suggest the launch of an official application procedure for participation, that will ensure transparency in the selection process. We believe that if the European Commission will increase its participation in the EFRAG funding (with a view to maintain the private/public cooperation) it should be properly represented in the EFRAG Board. Other relevant entities and institutions such as the new Platform on Sustainable Finance should be regarded as members of the EFRAG Board, contributing at the same time also to providing technical advices at the level of the non-financial reporting TEG. As already highlighted in our previous answer to the first consultation on the EFRAG governance, if EFRAG were involved in the development of non-financial reporting standards in a revised NFRD, we believe it should follow the same working arrangements with the EU Commission that are in force for the financial pillar (level II type

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measures) providing advice to the European Commission and maintaining, at the same time, the formal power to adopt the standards in the European Commission.

Furthermore, we believe that ESAs (ESMA and EBA in particular) should be involved in the process of developing a European non-financial reporting standard at the most with the role of observers, providing their technical knowledge and expertise without directly influencing the standard setting process.

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?

EACB answer: With regard to non-financial reporting, in addition to the stakeholders currently members of EFRAG, other players are relevant and may be willing to join EFRAG and become fully involved in the standard setting preparatory process. The EACB thinks that stakeholder groups, such as users (investors), preparers of financial reports (companies) and auditors/accountants must be involved to a reasonable extent in the process of developing a European non-financial reporting standard in order to ensure their practicability. The EACB insists on the need to involve banking associations due to the fact that non-financial reporting could represent a challenge for banks according to the reporting requirements that are being developed under the new provisions of 1) the Taxonomy Regulation, 2) the Sustainable Finance Disclosure Regulation (SFDR) and 3) the prudential requirements envisaged according to the CRR/CRD: the request for more non-financial information will be addressed particularly in the context of 4) the revision of the NFRD (Q1 2021) integrated with the indications included in the Guidelines on climate-related disclosure. In their role of intermediaries, banks will not only prepare their own non-financial accounts, but also be one of the major users of the new standards. Financial Institutions are best placed in providing the advices and expertise needed when it comes to set a non-financial reporting standard. For this reason, we believe that banking associations already members of the EFRAG should be efficiently involved in each level of the governance of the new non-financial pillar (NFR Board, NFR TEG and NFR WGs).
The same should occur for preparers and for relevant existing standard setter organizations (in particular GRI, SASB but also TCFD, IIRF, CDP and many others) to ensure that the new Standards rules are realistic and feasible. It is to note the recent statement by CDP, CDSB, GRI, IIRC and SASB who also recently declared the intent to work together towards a comprehensive corporate reporting system[1].

[1]https://29kjwb3armds2g3gi4lq2sx1-wpengine.netdna-ssl.com/wp-content/uploads/Statement-of-Intent-to-Work-Together-Towards-Comprehensive-Corporate-Reporting.pdf

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?

EACB answer: It has to be ensured that the views of SMEs will also be included with representatives in the standard setting preparation process. In this respect, we welcome the fact that in the current EFRAG's Project Task Force on the development of recommendations and preparatory work for EU non-financial reporting standards, a specific workstream for SMEs has been created. Given the importance that the involvement of SMEs could have in the creation of a simplified standard that would allow them to start addressing the reporting of non-financial information, we believe that a specific EFRAG's SME-focused TEG could represent a good solution to guarantee their involvement in the standard setting process.

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?

EACB answer: If EFRAG were entrusted with non-financial reporting, attention should be paid in not moving away from international reporting and undermining the coherence with already existing international reporting requirements. Challenges such as climate changes, human rights and social concerns affect companies globally. Ideally the ESG reporting should be developed globally and at all levels of the economy to fulfil the data gap. However, we support EU leadership in NF reporting standard setting as a solution is needed in the short term (according to the European sustainable finance legislative framework) although this will represent an interim answer with the aim to stimulate and accelerate the process to create a worldwide recognized NFR standard (possibly based on the European proposal). Nevertheless, if the EU would decide to set standards it should continue its commitment to global standards and contribute actively to a global solution. To better guarantee an alignment between the different international non-financial reporting initiatives and the EFRAG future activities, we believe that IASB could be appointed as observing members of the Non-Financial reporting Board of the new structure, while other relevant existing international standard setter organizations (see answer to question 5) should play a more active role[2].

[2] The cooperation with other standard setters and initiatives was also addressed in the *EACB comments on the IFRS Foundation consultation about Sustainabilty Reporting*, 21 December 2020.

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)?

EACB answer: We believe that a maximum number of 20 members could be enough to allow representativeness and functionality at the same time. Although we support the proposed EFRAG governance chart and new structure that envisages the two-pillar approach to deal with non-financial reporting standards alongside the current pillar dealing with financial reporting (as it was already suggested during the first consultative process), we believe it should be however necessary to better clarify the functional distinctions between the EFRAG Board in charge of Governance and the two Boards that will be in charge of the technical work that has to be elaborated by the financial and non-financial pillar, to avoid inefficiencies and complexity in the deliberative process. This two "legs" structure is very important as their role is different: on one hand the financial pillar remains as functional to advise on IFRS work, on the other hand a new role of EU standard setter would be established for the non-financial pillar.
According to the proposal, the EFRAG Board would be responsible for the EFRAG's organisation, administration, finances and oversight of all EFRAG's bodies. To underline in particular this last competence and further clarify the functioning of the new chart we suggest to call it "Supervisory Board". The Supervisory Board could represent the two different souls at the same time: current EFRAG Members (expression of the financial reporting pillar) and new members representing the non-financial pillar (as mentioned above EU Institutions, Member states and private members who will contribute financially to the new structure). To ensure independence of the decision making process, the members of the Board should be different from the ones nominated for the two technical boards. To facilitate the functioning of the board and enrich the contribution to the discussion without affecting directly the deliberation process, observers would be welcomed, especially from institutional stakeholders (see above). The EFRAG board should not take part to the nomination process of the members of the TEGs.

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?

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How can the interconnectivity between the Financial Reporting Board and the Non-Financial Reporting Board be ensured?

EACB answer: According to the progress report of the EFRAG's Project Task Force on Preparatory Work for the Elaboration of Possible EU Non-Financial Reporting Standards (published the 31 October 2020), more than 5000 KPIs or data points of a non-financial nature have been inventoried so far. This contributes to define a very complex situation that needs the involvement of many different stakeholders. The EACB believes that stakeholder groups that are contributing to the elaboration of financial reporting standards, such as investors, preparers of financial reports (companies) and auditors/accountants shall be involved to a reasonable extent in the process of developing a European non-financial reporting standard and should be included in the EFRAG's non-financial reporting Board. The EACB insisted on the need to involve banking association due to the fact that non-financial reporting could represent a challenge for banks given the reporting requirements that are being developed according to the new sustainable finance legislative proposals (see answer to question 4). We believe that banking associations already members of the EFRAG should be efficiently involved in each level of the governance of the new non-financial pillar (NFR Board, NFR TEG and NFR WGs). The same should occur for the relevant existing standard setter organizations.
In order to guarantee interconnectivity between the Financial Reporting Board and the Non-Financial Reporting Board we believe that a possible solution could be to appoint some members of the FR Board observers of the NFR Board and vice versa, strengthening in this way the cooperation between the two bodies.

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 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?

EACB answer: Private and public sectors should be represented in the same proportion within the technical expert group on non-financial reporting. Also in this case we could envisage a participation as observers of the IASB and other international initiative in the works of the TEGs. To ensure interconnectivity among the two pillars proposed we believe that a possible solution could be to appoint some members of one TEG observers of the other TEG and vice versa. We would underline, however, that members of the TEG should be selected only on the basis of their own personal competence and that they are must act fully independent of their employer.

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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?

EACB answer: We believe the role of the EFRAG LAB could be different in the future governance, more focused on research and innovation, together with the development of cross cutting issue between financial and non-financial reporting. This new holistic approach in corporate reporting would possibly increase the interconnectivity among the two pillars. Moreover, we believe that in order to better focus the efforts on the new mandate of the non-financial reporting pillar of the EFRAG, the European Lab should be activated only with regard to specific project to which specific resources could be allocated case by case without affecting directly the broader budget of the EFRAG.

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?

EACB answer: Any funding model should be fair and built on objective criteria and be a public-private partnership model. The mandate to be given to EFRAG on non-financial reporting should also call for an in-depth discussion on the necessary funding to be provided by EU authorities. The funding mechanism of the EC also needs to be changed to avoid rigidity and counterproductive incentives and reflect the envisaged broadened mandate from the Commission and ensure stability to funding rather than the current approach which amplifies volatility as it is based on % of the total contributions instead of a fixed contribution.
We acknowledge that the non-financial pillar as standard setter will be (by now) mainly funded by European public authorities. However, we recommend to guarantee a fair percentage of private funding (i.e. 30% private) to ensure a broader representativeness and independence.
Finally, we do not believe that a levy at National or European level could be feasible.

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