

Mr. Jean-Paul Gauzès
President
EFRAG
Square de Meeûs 35
1000 BRUXELLES

By mail:
To : Nominations@efrag.org
Cc : jean-paul.gauzes@efrag.org

Brussels, 6 November 2020

Subject: Response to Ad personam mandate on Non-Financial Reporting Standard Setting

Dear Mr Gauzès,

On behalf of the Deloitte¹ firms in the European Union (EU), we are pleased to respond to your request to share views on the future governance and framework of EFRAG in the context of possible changes to non-financial reporting by companies.

As general background, we welcome the European Commission's review of the non-financial reporting directive (NFRD) and support companies disclosing high-quality, transparent, relevant and comparable non-financial information (NFI) that is connected to financial information within mainstream corporate reporting. Non-financial standards are needed to achieve this. We support global standards because issues such as climate change are global, and the UN Sustainable Development Goals are of course global. However, we recommend a 'building block approach' where core global standards can be supplemented by local requirements.

We recognise the urgency of developing harmonised standards for non-financial reporting (NFR), and the particular needs of the EU, given that the EU has adopted reporting requirements that will apply in the relatively near term, particularly for financial sector companies. We are encouraged by recent international developments, including the statement of intent of five leading sustainability and integrated reporting organisations to work together in this area and by the IFRS Foundation's consultation paper on sustainability reporting.

We agree that EFRAG has an essential role to play with respect to NFR requirements in the EU. What that role would be will depend on the overall approach agreed by the EU Institutions

¹ For more information, see [Deloitte](https://www.deloitte.com).

as well as the outcome of current developments in NFI standard-setting at the global level. We can see at least two possible roles and approaches for EFRAG.

One role could be that of an influencer and endorsement adviser with respect to global sustainability standards (for example, if a global sustainability standards board under the governance and oversight of the IFRS Foundation and Monitoring Board were to be established). For instance, it could provide views and actively influence the development of global standards and advise on EU endorsement of these standards. This would be a similar mandate for EFRAG with respect to NFR as it has for financial reporting, and relatively cost-effective.

Alternatively, if the EU Institutions choose, another role could be to embark on standard-setting activities for the EU for NFR standards. We acknowledge that various technical, practical and political factors will be considered by the European institutions and stakeholders before concluding on the role that should be entrusted to EFRAG. This could include the speed at which global and EU standard-setting developments could take place and whether the subject matters to be developed as a matter of priority would coincide.

We consider that both approaches would require substantial new resources for EFRAG in terms of expertise in these complex areas, requiring additional funding, including contributions in kind. The governance considerations are also crucial, but in our view differ depending on the approach chosen, with the latter approach possibly requiring the establishment of an independent standard-setting-board/committee. Due to the short time available to provide input on your questionnaire, we have limited ourselves to setting out some thoughts regarding these two different approaches for your consideration, rather than responding to each of your questions. Please note that these thoughts may further develop as we have the opportunity to exchange and debate with others.

We would be happy to explain our analyses and thought process should this be of interest. If you have any questions or you would like to discuss these matters, please contact Laurence Rivat on +33 1 55 61 67 60 or David Barnes on +44 (0)20 7303 2888.

Yours sincerely,



David Barnes

Global Risk, Regulatory & Public Policy Leader



Laurence Rivat

EU Corporate Reporting Policy
Leader

Context for non-financial reporting

1. We believe non-financial reporting (NFR) standards are needed to assist companies in providing transparent, relevant, comparable and reliable non-financial information (NFI).
2. There has been a groundswell of calls from capital market participants, regulators and other stakeholders in support of transparent measurement and disclosure of information about sustainability performance. Investors and other stakeholders want to understand how the risks and opportunities faced by business translate into long-term value creation and profitability and how, in turn, this relates to shorter-term financial performance. This information should be connected to financial information and be prepared with the same level of quality and rigour.
3. We support global standard-setting because global issues need global solutions. Businesses have global supply and value chains, face global risks and have global investors. Most importantly, issues such as climate change and achieving the UN Sustainable Development Goals require international solutions.
4. We welcome the European Commission's starting point that *"any future possible EU NFR standards must be built on existing reporting standards and frameworks to the greatest extent possible"*. We therefore support close involvement and/or cooperation between EFRAG and the identified key international NFR standard-setting organisations. There are currently several international developments. No doubt Europe/EFRAG will monitor these and participate actively in international debates. In that respect, please note that we have welcomed the role of the IFRS Foundation in the sustainability standard-setting debate².
5. We acknowledge that the European Union has urgent NFR standard-setting needs, particularly as a result of the upcoming implementation in 2021/2022 of the *EU Sustainable Finance Taxonomy Regulation* and the *Sustainability Related Disclosures for the Financial Services Sector Regulation*. Understanding those needs and how to address them should be carefully assessed. In that respect, we are hoping that the work of the EFRAG Lab PTF will be enlightening.

Different models for a future EFRAG role imply different structures and governance

6. The expected role of EFRAG in NFR standard-setting will depend on a proper understanding of what needs to be developed at a European level versus what could be leveraged from global existing and future developments, and related timing. This would have significant implications on the possible changes to EFRAG's governance and resourcing.

² See Deloitte [statement](#).

7. In the models we have contemplated, we came to the initial view that the more that could be leveraged from international developments, the more the future EFRAG structure could resemble the current EFRAG model for financial reporting (FR), whose primary role is that of an endorsement advisor to the EC and an influencer. However, if it is assessed that the timing and/or the subject matters of the international developments do not meet the needs of the EU, then a different model for the EFRAG structure needs to be thought through, as it will be expected to fulfil a different role, i.e. that of a developer of high quality NFR standards through a strong governance, robust due processes and adequate resourcing. The extent to which EFRAG could be solicited to develop standards, i.e. extensively or with a more focused approach (e.g. as part of a building block approach to develop supplemental standards relevant to EU needs that are not covered by global standards), would influence in our view the governance structure to be implemented, as well as the financing required.

General considerations if EFRAG were to become a NFR standard-setter

8. If EFRAG were to be entrusted with NFR standard-setting, we consider it important to address the following criteria, as set out in *Accountancy Europe's 2017 Cogito Paper on Standard-setting in the 21st Century* : Legitimacy, Independence, Transparency, Public Accountability, Due Process, Balance (multi-stakeholder) membership. We also consider that the key factors of success for NFR standard-setting as identified in paragraph 31 of the *IFRS Foundation consultation Sustainability Reporting*, adapted to the EU/EFRAG environment (see additions in square brackets below), are also relevant:
 - a. achieving a sufficient level of global [EU] support from public authorities, global [EU] regulators and market stakeholders, including investors and preparers, in key markets;
 - b. working with regional [local] initiatives to achieve global [regional] consistency and reduce complexity in sustainability reporting;
 - c. ensuring the adequacy of the governance structure;
 - d. achieving appropriate technical expertise for the Trustees, SSB members and staff [EFRAG governance structure];
 - e. achieving the level of separate funding required and the capacity to obtain financial support;
 - f. developing a structure and culture that seeks to build effective synergies with financial reporting; and
 - g. ensuring the current mission and resources of the IFRS Foundation [EFRAG] are not compromised.
9. For standard-setting, we strongly believe in the importance of public-private partnership initiatives. We believe that this provides for better buy-in and quality of the outcomes.

10. Knowledge and competencies in the field of NFR are still developing and resources are scarce. Any standard-setting structure will need to have access to a much larger number of competent resources (and so, to funding in cash or in kind).
11. As indicated above, we believe in inclusiveness for standard-setting. Many stakeholders will be interested in the developments. Not all will have the same interest for each of the topics that may be tackled and/or the capacity (time, expertise, finance...) to contribute. Some initial ideas for possible models could be as follows:
 - a. An enlarged General Assembly, where EFRAG members would continue to have the same responsibilities as today in terms of appointment of the decision-makers (board), providing financing and fulfilling the legal requirements of the organisation. The financing may be proportionate to the member organisations' financial capacity. Provision of financing in kind (i.e. resources to the organisation) rather than in cash may also be contemplated.
 - b. One or two Boards – see further thoughts below on the merits of each approach. This/these Boards would have the ultimate decision-making powers, ensure a representation of key stakeholders, and be of a reasonable size (maximum 15 to 20 people).
 - c. One or two Technical Experts Groups (TEG) – see further thoughts below. The number of TEGs would depend on the role and approach retained for the board(s). The role of a TEG is to provide independent technical expertise to the board(s).
 - d. Technical and competent supporting staff to develop proposals for standards is critical. Depending on the priorities decided, and the extent of EU developments required, NFR standard-setting will likely require more staffing than EFRAG currently has for FR.
 - e. Since many stakeholders are likely to be interested in the NFR standard-setting activities and since not all of them would/could be represented on either the Board, TEG or Advisory Groups, it could be appropriate to set up an Advisory Council that would act as a sounding board, enable outreach and be “ambassadors” of the organisation.
 - f. Consideration would need to be given as to how the EFRAG Reporting Lab would fit within the proposed structure.
 - g. As of today, we are not aware of national public authorities in the EU in charge of NFR standard-setting other than governmental departments, but this might change in the future. If so, such authorities could either participate in the Advisory Council as suggested above, or in an equivalent body to the Consultative Forum of Standard-setters (CFSS) to be created.
 - h. With respect to the relevant European institutions and agencies, it is important that they participate at each level of the organisation, with the ability to provide direct input and views. However, we generally consider it appropriate to separate the powers of

legislation and enforcement. Accordingly, we would not recommend that they are part of the ultimate decision-making processes.

Different approaches for the board(s) / TEG(s)

12. With respect to the “board(s)” – i.e. the ultimate operating decision-maker – and “TEG(s)” – a source of thorough technical expertise, we see relative merits in different approaches. In evaluating these approaches, the criteria we reference in paragraph 8 above are relevant, including considerations of accountability, connectivity and resource effectiveness.

- a. A single board looking after both FR and NFR activities. This model would ensure appropriate connectivity between FR and NFR. It is also likely to require a “lighter” structure than the alternatives laid out below. Since the board would likely include members that are not necessarily competent in both FR and NFR, the technical work would need to be supported by two TEGs (one TEG for FR (like today) and one TEG for NFR standards, where members would be chosen for their technical expertise and be independent), as well as by the EFRAG staff. This board would also be in charge of the governance of the organization. A liaison committee could be established between the two TEGs to ensure the adequate consideration of the connectivity between FR and NFR. The NFR TEG could create ad hoc Advisory Groups to inform its members as needed on certain topics (e.g. climate, social matters, etc...).
- b. Two separate boards, each in charge of the FR and NFR activities separately, with a liaison committee between the two boards to ensure that the connectivity between FR and NFR is addressed. Having two boards may reflect the fact that EFRAG would have different roles for FR or NFR respectively (influencer/endorser for FR and standard-setter for NFR). Since the roles would be different, what is required from the boards may also be different. Also, as indicated above, depending on the timetable and project plan for having NFR standards in the EU, there may be a need for an accelerated project to establish those. If so, it might be helpful to have a board dedicated to NFR standard-setting composed of members with a robust technical background, bringing various perspectives and experience, and who could spend significant time on standard-setting activities.

If there are two boards, the current TEG for IFRS would continue and an assessment would have to be made whether the creation of a NFR TEG is needed. If the NFR board is chosen with responsibilities for NFR somewhat similar to the current EFRAG Board, then a NFR TEG would be needed. If it is considered that the NFR Board should be composed of more dedicated and technical members, a NFR TEG may not be needed. In such a case, it would be appropriate that the governance of the organisation for NFR (nominations, oversight of the due processes followed and the relationships with stakeholders, budgets...) is looked after at the general assembly level.

- c. Two separate boards as in b. above during a transitory phase before moving ultimately to a single board structure as in a. above.

This model would fulfil any immediate needs for NFR standard-setting at the EU level, leave the IFRS pillar of the organisation to continue accomplishing its current mission and enable EFRAG to monitor, participate, and influence, the global developments for the enhanced interaction between FR and NFR.

Resource considerations and commitments are crucial

13. Moving to standard-setting activities for NFR will require considerable resources, including appropriate expertise in ESG/sustainability reporting and standard-setting. It is of the utmost importance to understand the willingness of parties to contribute to the sustainable financing of such activities and to understand at which levels stakeholders are willing to contribute (international and/or European). In our view, contributions could be in cash or kind. As indicated above, competent resources for NFR standard-setting will likely be scarce, particularly at the beginning. Therefore, contributions in kind should be properly taken into account in appreciating the contributions being made. The extent of stakeholders' willingness to fund EU NFR standard-setting activities in a sustainable manner will be a critical factor in determining EFRAG's future structure and governance.