

Friday, 6 November 2020

## **Preliminary Report on the mandate on potential need for changes to the governance and funding of EFRAG**

The European Commission adopted an updated Work Programme on 27 May 2020 that foresees the publication of a legislative proposal to revise the Non-Financial Reporting Directive (NFRD).

Subsequently, on 25 June, the European Commission mandated EFRAG to undertake a preparatory work for the elaboration of possible EU non-financial reporting standards. This mandate is being carried out by a multi-stakeholder European Lab Project Task Force (PTF-NFRS).

In addition, Executive Vice-President Vladis Dombrovskis invited me, on an ad-personam basis, to provide recommendations on the possible changes to the governance and financing of EFRAG, in case EFRAG were entrusted with the development of possible EU non-financial reporting standards. This invitation was accompanied by an Annex providing the context identified as relevant for considering the governance for any eventual European reporting standard system under the NFRD. Aiming to provide well informed recommendations to the European Commission, I have on several occasions, including in our meetings and events, invited all organisations with an interest in this domain to provide me with initial views on the future governance and financing structure of EFRAG.

On 1 October, I issued a public invitation to a wide range of stakeholders to contribute their views in form of a letter with a questionnaire to allow me to develop the proposals for possible changes to the governance and funding of EFRAG. I requested responses by 30 October.

I have used the input I received so far in my preliminary proposals and will consider all the input to elaborate my preliminary proposals that will be subject to further public consultation. As at the date of this preliminary report, 37 responses have been received and these have been uploaded on the EFRAG website (Annex1). Some additional responses are expected to be received in the next couple of days. I also received contributions in different forms such as through emails and online meetings with individual organisations that requested these due to the covid-19 crisis .

These contributions will allow me to elaborate on my recommendations, which deal exclusively with EFRAG's organisation, functioning and financing.

At the present stage, I have set out below some preliminary proposals on potential changes in EFRAG's organisation and funding, taking into account the new competencies which would be needed at EFRAG.

# I – EFRAG’s CURRENT ORGANISATION AND GOVERNANCE

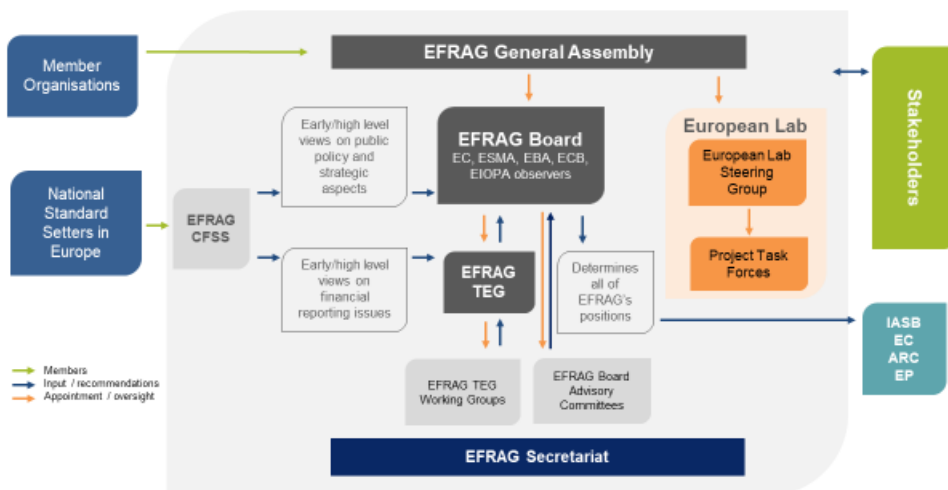
## 1.1 EFRAG’s current mission

EFRAG’s mission is to serve the European public interest by developing and promoting European views in the field of financial reporting and ensuring that these views are properly considered in the IASB standard-setting process and in related international debates. EFRAG ultimately provides advice to the European Commission on whether newly issued or revised IFRS Standards meet the criteria of the IAS Regulation for endorsement for use in the EU, including whether endorsement would be conducive to the European public good. Furthermore, EFRAG stimulates innovation in corporate reporting through the European Corporate Reporting Lab@EFRAG’s work in sharing good practices, which also complements and contributes to our work on financial reporting.

EFRAG seeks input from all stakeholders, and obtains evidence about specific European circumstances, throughout the standard-setting process and in providing our endorsement advice. Our legitimacy is built on transparency, governance, due process (which may include field tests, impact analyses and outreaches), public accountability and thought leadership. This enables EFRAG to speak convincingly, clearly and consistently, and be recognised as the European Voice in financial reporting.

## 1.2 EFRAG’s current governance

### EFRAG’S STRUCTURE



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### **1.3 EFRAG's new mission**

In case EFRAG were entrusted with the development of possible EU non-financial reporting standards, its new mission would be different from its present mission of influencing the IASB and providing endorsement advice.

As a matter of fact, standard setting is not the same activity as giving input to another standard setter such as the IASB. Standard setting is also different from giving endorsement advice. Standard setting has specific processes and activities and it is also in many respects a larger responsibility because the standard setter issues requirements that need to be complied with.

This will be true even if EFRAG would not, in practice, be given formal legal standard setting powers but would instead be the drafter of standards; while the European Commission, European Parliament and Council retain the formal power to set standards as part of law.

It is crucial for a standard setter to have a good and robust corporate governance and due process in order to get accepted by the public sector and the private stakeholders.

Therefore, at this stage, it is proposed that EFRAG has two pillars one for financial reporting activity (influencing the IASB and endorsement advice) and another for non-financial reporting standard setting (NFR). However, these two activities shall cooperate and exchange views and where possible be interconnected and draw on synergies.

As regards the financial reporting pillar, the current structure of EFRAG, which after the Maystadt reform has attained good results, could as far as possible, be preserved in its present status, in order not to compromise the quality of EFRAG's performance and the balance of views held among its stakeholders.

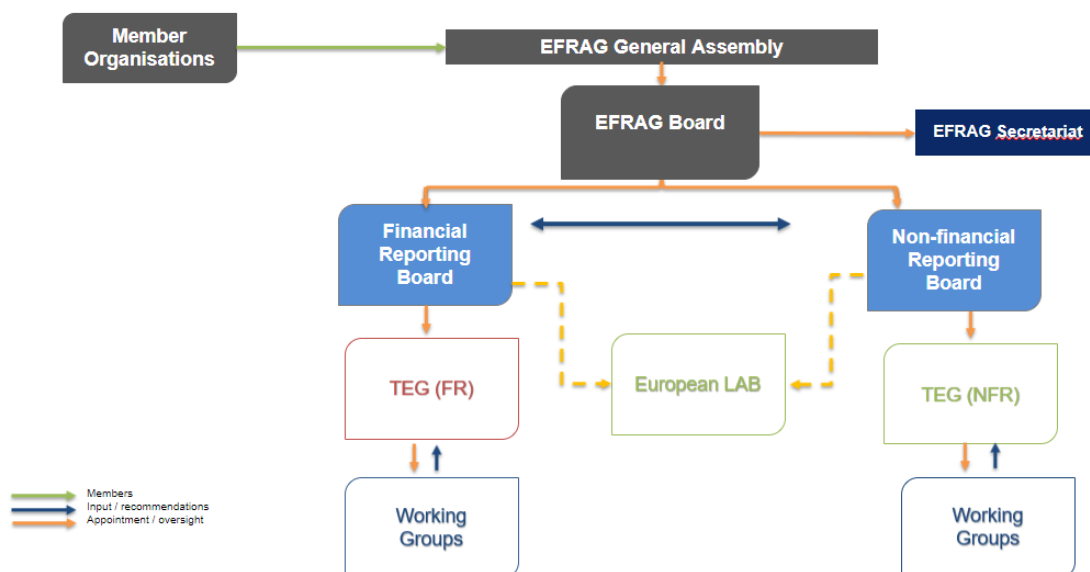
As regards the organisation of the non -financial reporting standard setting pillar, a due process similar to the one currently existing for financial reporting matters would be recommended.

The due process guidelines described in the Maystadt report currently applied to the financial reporting pillar, and designed to ensure that standards are developed in the public interest and avoiding undue influence, would also apply to the non-financial reporting pillar.

The governance principles would be as follows:

- Independent
- Open and transparent
- Due process
- Publicly accountable
- Legitimate and
- Balanced membership
- Serving the European public interest

## 1.4 EFRAG proposed new core structure



### 1.4.1 EFRAG General Assembly

The EFRAG General Assembly would continue to cover all EFRAG's activities. Its role is to take responsibility for fulfilling the legal requirements, appointing the EFRAG's President, the Board's members, and the members of both the Non-Financial Reporting and Financial Reporting Boards.

As it is currently the case, the EFRAG President responsible for the EFRAG organisation will be appointed by the General Assembly, on the proposal of the European Commission, based upon the advice of the European Parliament and the Council.

As non-financial reporting is of significant interest to a much wider range of stakeholders than financial reporting, the General Assembly could be enlarged to allow additional relevant and interested organisations, such as national competent authorities, foundations NGOs and trade unions, to participate in and contribute to EFRAG.

To become an EFRAG member organisation, a financial contribution should be made to EFRAG. Certain key non-financial reporting stakeholders might in particular be suited to become an EFRAG member organisation, but would not have the capacity to contribute financially. To be inclusive, financial contributions from these organisations should be limited.

### **1.4.2 EFRAG Board**

The EFRAG Board would be responsible for the EFRAG's organisation, administration, finances and oversight of all EFRAG's bodies. The Board may have various committees including nominating committees for appointment of the TEGs and European Lab, Audit and budget committee, Remuneration committee and Due process oversight committee.

The EFRAG Board would be responsible for selecting the CEO, who is responsible for all operational/organisation tasks for EFRAG.

The EFRAG Board would approve the due process system and evaluate the performance of the due process.

The Board's members would be appointed by the General Assembly. They should be of high calibre and ensure that EFRAG is public accountable.

The Board could be composed of the EFRAG's President, the Vice-Presidents of the two Reporting Boards (Financial and Non-Financial), representatives of European Public institutions, national standards setters, representatives of the stakeholders chosen for their competence and expertise; Board members should commit to serve in the public interest and be free from conflicts of interest.

### **1.4.3 Reporting Boards**

Taking into account the new mission given to EFRAG, the activities regarding the reporting issues would be split between two new bodies supervised by the Board, one dedicated to the Financial Reporting aspects, the other to the Non-Financial Reporting aspects: the Financial Reporting Board, and the Non-Financial Reporting Board.

The members of these two Boards would be appointed by the General Assembly, on proposal of the EFRAG Board.

Each Board would be assisted in its area of competence by a Technical Expert Group (TEG).

Each Reporting Board would be responsible for all positions regarding its area of competence, after having considered the technical advice provided by its corresponding TEG and reflecting the results of EFRAG's due process.

Each Reporting Board would have to ensure that in its area of competence, EFRAG has an open and transparent due process including a public consultation process with European constituents on draft EFRAG positions such as discussion papers, draft comments letters, draft consultation documents, draft endorsement advice, exposure drafts and other forms of draft standards.

Each Reporting Board would have to operate by consensus to the maximum extent feasible, or by a qualified majority (two-third) if there is a failure to reach consensus.

#### **1.4.3.1. The Financial Reporting Board**

The Financing Reporting Board would continue the current role of the EFRAG Board in the endorsement process and contributing to the IASB standard setting process, with the exclusion of any supervisory and oversight role.

#### **1.4.3.2. The Non-Financial Reporting Board**

The composition of the Non-Financial Reporting Board should reflect the diversity of the stakeholders. This would be specified later on.

The role of the Non-Financial Reporting Board would be focused on the review and approval of the non-financial reporting standards recommended by the Technical Expert Group for non-financial reporting (see below) and non-financial reporting research activities to support the non-financial reporting standard setting process.

The possible modalities of cooperation with the existing (global) public and or private non-financial reporting initiatives producing international standards and frameworks will be specified after the public consultation as well as the possible consideration of the SME angle.

#### **1.4.4 Technical Expert Groups (TEG)**

##### **1.4.4.1. TEG for financial reporting**

The current rules for composition and functioning would continue to be applicable.

##### **1.4.4.2 TEG for non-financial reporting**

The new Technical Expert Group for non-financial reporting will work independently from the existing TEG for financial reporting but would ensure exchanges of views are in place to support interconnectivity. Its activity will be focused on the elaboration and drafting of the non-financial standards to be recommended to the Non-financial Reporting Board.

The members of the TEG for non-financial reporting would be chosen for their experience and expertise in the drafting of standards and in the non-financial reporting domain. A geographical and professional background balance should be respected.

The role of the TEG for non-financial reporting is expected to be determined at least initially by the outcome of the revision of the 2014/95/EU Non-Financial Reporting Directive. This Group would be responsible for developing standards with help from appropriate working groups and recommending these standards for approval to the Non-Financial Reporting Board.

#### **1.4.5. Working Groups, Advisory Panels and Task Forces**

A number of new Working Groups/Task Forces/Advisory Panels would be established by each TEG. Each TEG would decide on the need for and mandate for such Working Groups.

#### **1.4.6. European Reporting Lab (European Lab)**

The European Lab would become a task force or other structure to continue the work on good practices on non-financial reporting and to stimulate innovation and debate related to non-financial reporting. The European Lab could potentially also undertake work on cross cutting issues with the financial reporting activities (or on financial reporting only). One possible example is to identify good practices in the area of digital reporting.

The Non-Financial and Financial Reporting Boards would choose the topics and select the members of the Task Force or other structure.

## **II – FUNDING**

The creation of a new pillar for non-financial information reporting will imply a need for complementary funding.

The funding could be different for each pillar.

It is envisaged that the current system would be maintained for the financial reporting pillar.

The funding for the non-financial reporting pillar should support the public- private sector partnership model of EFRAG. The public funding should play a leading part for the non-financial reporting pillar, given its standard setting function. However, it would be necessary to consider increasing funding from private entities and foundations while ensuring the absence of conflicts of interests.

These funding issues will be specified later on.

Jean-Paul Gauzès

EFRAG Board President and European Lab Steering Group Chairman.

## Annex 1 – List of Respondents to the first consultation (1 -30 October 2020)

<b>Organisations</b>	<b>Country</b>
<b>WBCSD</b>	Global
<b>Fédération Française de L'Assurance</b>	France
<b>EFFAS</b>	Europe
<b>Alfredo Romano</b>	Italy
<b>Principles for Responsible Investment</b>	Global
<b>European Accounting Association (EAA)</b>	Europe
<b>Polish Bank Association</b>	Poland
<b>WICI Europe</b>	Europe
<b>WWF</b>	Global
<b>ESBG</b>	Europe
<b>Delphine Gibassier (individual)</b>	France
<b>Christoph Toepfer (individual)</b>	Germany
<b>MAIF</b>	France
<b>Timo Punkari (individual)</b>	Finland
<b>CDSB</b>	Global
<b>ICAEW</b>	UK
<b>ACCA</b>	Global
<b>JBCE</b>	Japan
<b>Insurance Europe</b>	Europe
<b>CNC</b>	Luxembourg
<b>Danish Funding Mechanism</b>	Denmark
<b>PTF RNFRO</b>	Europe
<b>SHIFT Project</b>	France
<b>Société Générale</b>	France
<b>GRI</b>	Global
<b>Filip Gregor (individual)</b>	Czech Republic
<b>CDP Europe</b>	Europe
<b>Fondazione OIBR</b>	Italy
<b>EFAA</b>	Europe
<b>EACB</b>	Europe
<b>Yasmine Moezinia (Individual)-</b>	UK
<b>AFRAC</b>	Austria
<b>Sigurt Vitols (Individual)</b>	Latvia
<b>EY</b>	Global
<b>Organismo Italiano Contabilità (OIC)</b>	Italy
<b>IIRC</b>	Global



The following organisations provided input without submitting a formal letter:

<b>Organisations</b>	<b>Country</b>
<b>Uros Kovac</b>	Slovenia
<b>Association for Generally Accepted Principles in the Securities Market</b>	Sweden
<b>Crédit Agricole CIB</b>	France
<b>Richard Howitt</b>	UK
<b>Eumedion</b>	The Netherlands