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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**

On behalf of the Accounting Standards Committee of Germany (ASCG), we are writing to comment on the Consultation Paper on your *ad personam* mandate on the potential need for changes to the governance and funding of EFRAG. We welcome the opportunity to comment on the proposals.

Whilst we agree with the proposal to establish a second pillar, we have reservations as to establishing two Reporting Boards underneath the EFRAG Board. We understand that the two pillars are envisaged to have separate funding and, potentially, different members; they certainly do have different mandates, with the financial pillar continuing the work EFRAG is currently pursuing and the non-financial pillar becoming involved in, or mandated with, standard-setting. However, we believe that it would be essential to build an organisational link between the two pillars to truly enable connectivity. If both Boards and TEGs just pursue their own tasks, we see the risk of two reporting streams developing rather independently from each other. We would therefore favour the continuation of a one-tier Board that takes the ultimate responsibility but is fed through two Technical Experts Groups.

In any case, we also believe that the purpose of the EFRAG Board under the new structure requires clarification, as to whether it should continue to function as the ultimate decision-maker (which would be our preference) or become a Supervisory Board that oversees the governance of the two reporting pillars. If the latter was the case, then this would probably also have consequences for the rights EFRAG members organisations have in the General Assembly.

Lastly, we would like to stress the importance that any work of a newly created non-financial reporting pillar should be as closely aligned to and draw on global developments in order not

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to create a completely detached alternative framework that merely increases cost for everyone. In that regard, we draw your attention specifically to the latest developments happening at the IFRS Foundation.

Our responses to the questions of the consultation paper are laid out in the Appendix to this letter. If you would like to discuss our comments further, please do not hesitate to contact Andreas Barckow ([barckow@drsc.de](mailto:barckow@drsc.de)) or Sven Morich ([morich@drsc.de](mailto:morich@drsc.de)) on our behalf.

Yours sincerely,

*Dr Nicolas Peter*

Chair

*Prof Dr Dieter Truxius*

Vice Chair

## Appendix – Answers to the questions in the Consultation Paper

### 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?

The points listed in Chapter 3 of the Consultation Paper constitute those that we would regard necessary for open and transparent standard-setting – regardless of whether standard-setting was financial or non-financial.

Whether *all* of these points are finally needed depends to a large degree on the specifics of EFRAG's mandate, were it to become a standard-setter. For instance, the execution of agenda consultations would be necessary and appropriate only insofar as a standard-setter has autonomy over its work programme. If, conversely, the tasks EFRAG would be mandated for were fully or largely determined by the European institutions, an agenda consultation would be permissible.

### 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 Consultation Paper seems to assume that every Member State does indeed have a national public authority that it wishes to become part of EFRAG and its different bodies. We do not think that this is necessarily the case (and would be surprised if it was in Germany).

If we contrast the proposals with the existing layout for financial reporting, input from Member States themselves is organised through the Accounting Regulatory Committee at the European Commission. We therefore believe that it would be appropriate for the European Commission (rather than EFRAG) to reflect on how to best organise the input from Member States in a consistent manner. In turn, it should be left to Member States to organise their national set-up and, if not yet in existence, to build up relevant expertise to provide meaningful input into the European process. This does not necessarily translate into the involvement of national public authorities, which may not have the competent expertise.

We therefore do not think that the relevant national public authorities should be involved in the structure – unless they are, in essence, the relevant national standard-setting bodies with a link to their respective governments. This seems to have been the model in the financial reporting chapter of EFRAG, and we see no convincing reason to go down a different route for non-financial reporting. Hence, the emphasis should less be on the legal setup (i.e., whether



the standard-setters are national public authorities or not) and more on the appropriate level of ensuring high-quality and meaningful national input.

### 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?

We believe that clarification is needed as to the purpose of the two-tier Board structure. The question seems to assume that the current EFRAG Board would be converted into an oversight body; however, we do not think that this is overly clear. We also question whether this would necessarily be the most appropriate setup. In this regard, we refer to our answers to questions 7 and 8.

Notwithstanding those remarks, we generally think that European institutions and agencies should become involved – at which level and to what degree depends on a number of factors, amongst which the size of the bodies to be created and the number of institutions and agencies to be admitted as well as the tasks required of them require consideration. For instance, as regards technical input, membership in a working group may be appropriate; in other areas where overall consistency of policies at European level is concerned, e.g., on sustainable finance, an observer role on TEG and/or the Board may be considered.

In any case, the inclusiveness of each and every player must not lead to the non-financial pillar becoming inoperable. If we consider the current size of the EFRAG Board, its 17 members and five observers are already a sizeable number that no other organisation charged with standard-setting we know would generally foresee for its decision-making body. We therefore suggest carefully considering the balance of being inclusive and at the same remaining functional. A Consultative Forum could always be an alternative, yet EFRAG needs to remain cognisant as to how many consultative and advisory bodies it could handle with its existing resources and what the mandate of such bodies should be.

### 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?



We believe that for reasons of general acceptance and usability, a broader inclusion of stakeholder groups compared to financial reporting is required. As already said in our answer to the previous question, we believe that a critical point remains the workability of the standard-setting process, as effective and efficient collaboration may be hindered if the group became too large. Standard-setting expertise and the knowledge about the processes for collecting, preparing and scrutinising non-financial information, but also about how this information can be used by market participants seems particularly relevant and should find proper emphasis in the composition of the EFRAG groups.

On the point of representation, we are of the opinion that this is inextricably linked to the funding of the organisation. Those that pay into the organisation should be equipped with membership rights and have access to its decision-making processes. We acknowledge that this may be easier for private sector organisations than for civil society, which, given its importance in the matter, requires due consideration. Relevant stakeholder groups should always be given the opportunity to provide input to the debate. However, this may be equally be achieved through an observer status with speaking rights, perhaps on a rotation or topical basis. The right to vote and make decisions should be limited to those stakeholder representatives whose organisations also contribute financially to EFRAG's work.

#### 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?

We believe that SMEs/SMPs should generally be catered for through consultation and outreaches. If they were to become part of EFRAG's structure, we would think that the vast majority of them fails to be able to provide the necessary travel and time commitment, as they are too small. So, there is a likelihood that these entities will be represented through industry organisations only. We therefore believe it might also be feasible to bring SMEs/SMPs in on a topic-by-topic basis, so probably in an SME/SMP-focused working group when direct input of SMEs is considered necessary.

In any case, an SME/SMP-focussed working group only seems necessary and justified if a revised NFRD actually results in non-financial reporting requirements for SMEs.

#### 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?



This question is hard to answer as the mandate of EFRAG is not yet known. Informal exchanges are always possible, but to our knowledge, there is no official advisory group that meets under the auspices of an umbrella non-financial reporting organisation (such as the Advisory Council or the ASAF for the IASB). In this regard, the current developments around the IFRS Foundation Trustees' consultation as well as any potential changes to the IFRSF Constitution should be monitored and considered.

In addition, cooperation/relations with other standard-setters should be considered with a more dynamic view. As a matter of fact, in recent years there has been a clear trend for consolidation of major initiatives, most recently the merger of SASB and IIRC to become the Value Reporting Foundation. Also, international standard-setters traditionally more active in the field of financial reporting are part of this consolidation effort. Therefore, any future EFRAG structure should pay tribute to such developments in its work and should not shy away from making explicit use of future consolidated international standards in this field for its own purposes. It should also not be forgotten that the European Council requested internationally consistent standards in its decision at the end of 2019 and that, currently, international cooperation in the area on sustainable finance is on the rise.

#### 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)?

Before answering the questions raised, we wish to provide some overarching comments as to the envisaged structure. Whilst we agree with the proposal to establish a second (non-financial reporting) pillar, we have reservations as to establishing two Reporting Boards underneath the EFRAG Board. We understand that the two pillars are envisaged to have separate funding and, potentially, different members; they certainly do have different mandates, with the financial pillar continuing the work EFRAG is currently pursuing and the non-financial pillar becoming involved in, or mandated with, standard-setting. However, we believe that it would be essential to build an organisational link between the two pillars to truly enable connectivity. If both Boards (and the TEGs likewise) just pursue their own tasks, we see the risk of two reporting streams developing rather independently from each other. We would therefore favour the continuation of a one-tier Board that takes the ultimate responsibility, but it be fed through two Technical Experts Groups.

In any case, we believe that the purpose of the EFRAG Board under the new structure requires clarification, as to whether it should continue to function as the ultimate decision-maker (which would be our preference) or become a Supervisory Board that oversees the governance of the two reporting pillars (which seems to be the assumption underlying many of the questions in the Consultation Paper). If the latter was the case, then this would probably also have consequences for the rights EFRAG members organisations have in the General Assembly.



Regarding the question about size, we do not think that there is any naturally given best number. The current IASB represents “the world” and has a maximum of 14 members; EFRAG's current decision-making Board representing Europe has 17 members and five observers with speaking rights, which already constitutes quite a large group that seems sometimes hard to handle in an efficient way. To us, it is key that a Board of whatever size remains functional and manageable.

The Board, whether constituted as a decision-making or oversight body, should consist of stakeholders that have demonstrated both an interest and expertise in corporate reporting. The proportion of the different stakeholder groups should be tied to their contributions to the funding of EFRAG, even though a certain misalignment may be tolerable (as is the case currently). However, membership without payment would constitute a red line for us: Inclusiveness cannot be an overarching justification vis-à-vis rights and obligations that come with membership. If inclusiveness is being viewed as important, it should be ensured through advisory and consultative structures but not through granting membership rights, esp. voting and decision-making powers. In that regard, we recommend clarifying the selection criteria and process for the members of the EFRAG Board.

If the EFRAG Board was constituted as a body overseeing the governance of the organisation, we would clearly be in favour of not having *the same individuals* on it that already serve as members on the respective Reporting Boards; we would perceive this as constituting bad governance, as the line separating decision-making from supervision over such decision-making would become blurred. We believe that a *stakeholder group* may be represented at both, the top Board, and the Reporting Boards, but should not be represented in those Boards through the same *individual*. We would therefore disagree with the EFRAG Board including representatives of the Non-Financial Reporting Board and the Financial Reporting Board on the EFRAG Board were it to be charged with oversight.

As to the question whether the EFRAG Board or the respective Reporting Boards should appoint the members of both TEGs and the European Lab, we would tie our answer to the purpose of the EFRAG Board: If it continued to be a decision-making body, we would favour it being equipped with the right to select both the members of the TEGs as well as the European Lab; conversely, if the EFRAG Board was envisaged to be turned into an oversight body, then the appointment right(s) should be left with the Reporting Boards.

Lastly, we would like to stress the importance that any work of a newly created non-financial reporting pillar should be as closely aligned to and draw on global developments in order not to create a completely detached alternative framework that merely increases cost for everyone. In that regard, we draw your attention specifically to the latest developments happening at the IFRS Foundation.

#### 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?

Building from our answer to the previous question, we do not think that having three Boards is necessarily the most appropriate solution. Our preference would be not to change the mandate of the EFRAG Board as it currently exists and leave the oversight function to the General Assembly (or a dedicated committee of the General Assembly). The new non-financial reporting pillar should be constituted downstream from a newly created non-financial reporting TEG that would exist next to the current financial reporting TEG and possibly with its own working groups and advisory/consultative bodies. We believe that such a structure better enables the connectivity between the two pillars, as connectivity issues will most likely arise at the technical and not the political level and should therefore be foreseen where the issues are considered in detail.

If our preference was not taken up and a separate Non-Financial Reporting Board was created, then many of the points made in our responses to previous questions equally apply here (such as the maximum size, the questions about the membership structure and about having observers). The question as to who should appoint the members of the new Reporting Board depends on whether the governance and supervision would be carried out by a top Board or the General Assembly. If an EFRAG (Supervisory) Board was established, then it should be this body that appoints the members of the Reporting Boards. In any case, we recommend considering cross-membership for at least the Chair (and possibly the Vice Chair) of the Boards in the respective other Reporting Board to ensure connectivity on this level, too.

### 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?

We believe that the TEG for non-financial reporting should generally be structured in a similar way as its financial counterpart, esp. as regards its size. With regard to representation, we believe that the broader focus of non-financial reporting may require looking beyond preparers, auditors, users, and academics to also consider experts in the area of sustainability reporting. However, we believe it is of utmost importance to have the majority of seats reserved for people that have a profound understanding of the reporting processes that exist in companies: If standards in the non-financial reporting area are to be developed, it is crucial that they stand the test of being capable of being applied in practice. To take civil society considerations into account, it may be appropriate to consider providing observer seats to those representatives.

As regards the appointment of TEG members, we believe that it should be within the mandate of the ultimate decision-maker: If there were to be a Non-Financial Reporting Board, then this Board appears to be the right body; conversely, if the current EFRAG Board was retained as the ultimate decision-making body, then this body would be the appropriate body in the organisation.





Lastly, as to how connectivity could be ensured, we believe that there is no single best answer to this question but an array of possible considerations, such as (but not limited to) the following:

- Cross-membership for the Chair and Vice-Chair of each TEG, who would become ex officio members of the respective other body;
- Joint meetings at least twice a year to inform the entirety of TEG members;
- Joint working groups in areas that are of mutual interest;

#### 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?

As to the first question, we do not believe that there is necessarily a *need* for having a European Lab activity. It may be *advisable* to continue operating a Lab as it is already up and running, but the Lab is not a condition for EFRAG to engage in the tasks as envisaged.

Where we do agree is that the exclusive focus on non-financial aspects is too narrow for the Lab. Its focus should be broadened to have it address both financial and non-financial reporting topics as this would inform the TEGs and the Board(s) as to how connectivity works in practice. When looking to the blueprint of the UK FRC's Reporting Lab, there may be more and even broader issues to be addressed by Lab in the future, e.g., the link of corporate reporting to capital maintenance.

Lastly, we strongly advise that the Lab become part of EFRAG's general governance structure and not remain a free-standing organism next to it. In that regard, we continue to believe that the Steering Group should be disbanded, the Lab's members be appointed by the Board(s), and its funding and work programme being overseen by the Board as is already the case for all other oversight matters.

#### 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?

Whilst public (co-)funding could underpin the public interest mission of EFRAG, we are sceptical about having the funding come mostly/entirely from the public sector. In our view, this would be at odds with having an independent standard-setting organisation. We therefore believe that private standard-setting should generally be provided through private sector funding.



Any financial support from Member States would need to be organised at local level and should be left to them as to how this is accomplished. National standard-setters could help by facilitating collection mechanisms, which may also be warranted, since national standard-setters are often the institution where national views on standard-setting issues are developed.

A levy may be difficult to justify (who should/should not be required to pay, thus leading to a potential free-rider problem). We also wonder whether introducing a levy on a European level would be in line with the European Treaties that do not foresee a right for the European institutions to charge levies or impose taxes.