Climate Disclosure Standards Board's (CDSB) response to contribute to the ad personam mandate of EFRAG Board President Jean Paul Gauzès on non-financial reporting standard setting

The Climate Disclosure Standards Board (CDSB) would like to thank EFRAG for the opportunity to provide comments on the ad personam mandate of EFRAG Board President Jean Paul Gauzès on non-financial reporting standard setting.

The Climate Disclosure Standards Board (CDSB) works to provide decision-useful environmental information to markets via mainstream corporate reports. Our mission is to create the enabling conditions for material climate change and natural capital information to be integrated into mainstream reporting.

CDSB is an international consortium of business and environmental NGOs. We are committed to advancing and aligning the global mainstream corporate reporting model to equate natural capital with financial capital. We do this by offering companies a framework for reporting environmental information with the same rigour as financial information. In turn this helps them to provide investors with decision-useful environmental information via the mainstream corporate report, enhancing the efficient allocation of capital. Regulators also benefit from compliance-ready materials.

Recognising that information about natural capital and financial capital is equally essential for an understanding of corporate performance, our work builds the trust and transparency needed to foster resilient capital markets. Collectively, we aim to contribute to more sustainable economic, social and environmental systems.

The CDSB Framework is used by large listed companies globally and is referenced in government guidance to reporting regulation in the Commission Guidelines on Non-Financial Reporting, the UK Companies Act 2006, and stock exchange guidance in London, Australia, Singapore, Egypt, Santiago de Chile and elsewhere. CDSB has also contributed to the work of the UN Sustainable Stock Exchanges Initiative through its working groups on disclosure, green finance and financial regulators. CDSB also hosts the TCFD Knowledge Hub on behalf of the Task Force on Climate-related Financial Disclosures (TCFD), which helps report preparers to find the resources they need to understand and implement the TCFD recommendations.

Our comments in full are provided below. Please do not hesitate to contact me directly (mardi@cdsb.net) or CDSB's EU Policy Manager Axelle Blanchard (axelle.blanchard@cdsb.net) for further information.

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Appendix: Responses to consultation questions

1. Governance – Structure and due process

1.1 Standards need to be developed in the public interest and no individual category of stakeholder may exercise undue influence: How can it be best ensured that standards are developed based on an inclusive and transparent due process? What should be the characteristics of such a due process?

Standards should be subject to well-defined development and approval procedures, which reflect and support their authority. This should be grounded in an inclusive and transparent development process, with rigorous market consultation and oversight.

The principles of standard-setting to be considered in this process are:

- Globally applicable standards, based on global participation
- High-quality independent due process
- Legitimacy from public oversight
- Appropriate stakeholder representation to ensure that standards are fit-for-purpose.

These principles should serve as a minimum set of reporting elements that are globally aligned, without precluding the European Union to innovate and produce further reporting elements.

Regarding transparency and inclusiveness, a series of best practices can be established, such as those already set up by financial and non-financial standard-setters, including public board meetings, transparency of the status of projects, the ability for stakeholders to submit comments at any time, a standing group of committed stakeholders to provide in-depth feedback, additional public consultation for broad feedback, and publication of a summary of significant issues and the comments received when a decision is made to show what shaped the decision-making process.

Full transparency, including a public schedule of activities, periodic updates on progress, published agenda papers, recordings or written summaries of meetings, and the treatment of consultation responses as public documents, is essential to build trust and develop high-quality standards.

In order to ensure that standards are considering all stakeholders' needs, the organisation in charge of the standards should have enough internal capacity, (i.e. human and financial resources) as well as relevant competences and expertise at all decision-making and operational levels, including at the top, to ensure that standards are evidence-based and are aligned with market best practices and European policy priorities. These considerations would support a successful implementation of other major European policies, such as the Capital Markets Union as well as the improvement of the state of corporate reporting in the European Union and contribute to achieve the aims of the upcoming review of the Non-Financial Reporting Directive (NFRD).

1.2 Relevant European institutions and agencies shall be invited to be fully involved in the development of future standards, including the European Securities and Markets Authority (ESMA): How can these European Institutions and agencies be involved in the development of future standards and in the standard setter? Should there a particular role for ESMA?

We support the involvement of ESMA in the upcoming discussions on European non-financial reporting standards (although it is not a standard setter) based on its role around the oversight of corporate financial and non-financial reporting. As a supervisor, ESMA plays a critical role to foster supervisory convergence and therefore harmonise the implementation of related requirements and standards across EU Member States. This is why ESMA is already contributing to the work of the EFRAG Board and Technical Expert Group in an observer capacity.

Based on the work ESMA has already done on sustainable finance and corporate reporting, it should contribute to ensure that the European non-financial reporting standards are suitable for supervision. It could also provide valuable expertise on specific topics, e.g. the digitalisation of information based on its work on the European Single Electronic Format (ESEF). ESMA could also ensure policy coherence between the different legislative requirements arising from the Taxonomy or the Sustainable Finance Disclosure Regulation (SFDR) under which the European Supervisory Authorities have suggested a set of 32 indicators to assess principal adverse impacts to sustainability factors which would need to be aligned with the upcoming requirements in the NFRD and incorporated into the non-financial reporting standards.

Such involvement will require additional resources within ESMA. To reach that objective, it is necessary to provide ESMA with the relevant mandate and funding to support compliance through proactive supervision of non-financial information. Such supervisory powers should be included in all of ESMA's core activities beyond the recent amendments made to its founding Regulation as part of the "ESA review."

Based on the importance of ESMA's role in the standard setting process outlined above, we suggest that EFRAG considers how ESMA can be firmly embedded into the non-financial standard-setting process.

1.3 To permit relevant national public authorities to provide input about whether any future standards are responsive to the public interest, how can these authorities be included in the governance of the non-financial reporting pillar? Which authorities would be the most relevant and how should they be involved?

Involving additional national public authorities should be considered, because:

- They can provide additional relevant expertise to cover non-financial reporting while ensuring the necessary connectivity between financial and non-financial reporting; and
- They are to be involved in the national implementation of the requirements coming from the standards;

National public authorities should also be targeted for ensuring consultation is done effectively within markets across Europe, by engaging them to run market outreach and roundtables to reflect fully the views from national jurisdictions in the process.

1.4 Should private sector and civil society representatives be involved in the standard setting work? If so, what would be suitable options for doing so in a balanced way? Which stakeholders should be involved? Should the standard setting pillar be a public-private partnership like in the financial reporting pillar?

We believe that proper standard setting should involve a proportionate and balanced representation from the private sector, including investors and industry representatives, as well as civil society representatives. While much attention should be given to ensure overall rigour, legitimacy and transparency, standards should also be able to reflect best market practices through the involvement of preparers and primary users of the information to ensure the feasibility of the requirements. Key stakeholder constituents from across the private sector and civil society should be identified based on a cross section then included in the development of the standard.

Such an approach of blending public and private interests is widely adopted because it leads to standards that have both legitimacy and are fit for purpose. Financial accounting standards use a public-private model, i.e. public oversight of private standard setting with an independent consultative due process. Modelling global sustainability standard setting after this structure would seem sensible.

1.5 If there were to be SME standards derived from the future EU non-financial reporting standards, how should the SME angle be addressed in the governance and in the standard setting process?

CDSB does not have views on this matter.

1.6 Which governance structure would you foresee for the EFRAG EU non-financial reporting standard setting pillar? How would this fit in the overall EFRAG governance structure? What relation would there be with the financial reporting pillar, if any?

We have highlighted in question 1.1 that standards setting should follow a set of principles, including legitimacy from public oversight and appropriate stakeholder representation to ensure that standards are fit for purpose.

A governance structure and process can be designed to acquire a level of EU ownership and reconcile international standards with European requirements and policy priorities. EFRAG can play a leading role in the development of such as system, bringing together the key parties necessary from across the globe to ensure its success and legitimacy. We recognize the importance of jurisdiction-level regulatory overlays, which can ensure that global standards are complemented by additional disclosure requirements needed for achievement of local policy objectives (specific disclosures required for the EU taxonomy is a good example of this).

On public oversight, the due process of standard setting could be overseen by a European standards oversight board which would be empowered to adopt or decline global standards.

Last but not least, it is important that the governance structure of the EU non-financial reporting standard reflects the fact that financial and so-called non-financial information is intrinsically interlinked. As such, it is crucial to ensure a link between financial and non-financial reporting standards-setting and their governance.

2. Governance – Cooperation with standard setters and other initiatives

2.1 Any future possible EU non-financial reporting standards must be built on existing reporting standards and frameworks to the greatest possible extent:

- **How can the relevant existing standard-setting organisations be closely associated in future standardisation work? How would you see cooperation and involvement?**
- **More broadly, how should cooperation with existing public and/or private initiatives producing international standards and framework be established, to ensure that any future non-financial reporting standards applying in the EU build to the greatest extent possible on existing standards and frameworks?**
- **How can the EU non-financial reporting standard setting have a global impact?**

In the Joint Statement of Intent of the global standards setters (CDP, CDSB, GRI, IIRC and SASB) to work together towards comprehensive corporate reporting[1], we have put forward a building block approach that recognises the importance of structural connectivity between reporting to providers of capital making economic

[1] CDP, CDSB, GRI, IIRC and SASB (2020) Statement of Intent to Work Together Towards Comprehensive Corprate Reporting. [PDF]. Available from: https://29kjwb3armds2g3gi4lq2sx1-wpengine.netdna-ssl.com/wp-content/uploads/Statement-of-Intent-to-Work-Together-Towards-Comprehensive-Corporate-Reporting.pdf

decisions, reporting to meet the needs of a broad range of users, and reporting to meet the needs of specific jurisdictional requirements.

- The first block of sustainability disclosures addresses significant sustainability impacts that affect company performance and risk profile, and therefore enterprise value creation over the short-, medium- and long-term. These disclosures are relevant for economic decision-making.
- The second block of sustainability disclosures address all significant sustainability impacts, in the context of their contribution to sustainable development, thereby providing a comprehensive picture of a company's positive and negative contribution to sustainable development and value creation.
- The third building block addresses specific jurisdictional requirements to support local public accountability, insofar as they are not addressed via the first and second building blocks.

Within these building blocks, the CDSB Framework's value is to provide practical guidance to support the integration of non-financial (primarily environmental) information into corporate management reports.

We believe that this approach can meet the need for globally consistent disclosures for capital markets and other stakeholders, while allowing sufficient flexibility for local policy priorities. Such an approach would foster collaboration, acceptability and adoption across a broad range of jurisdictions. Consistency between financial reporting and non-financial reporting will also be vital to advance effective sustainable development and complete the ecosystem.

For the first two building blocks noted above, our focus is on the features of standard-setting that specific institutional arrangements would need to achieve. For the third building block, we integrate jurisdiction-level regulatory overlays, which can ensure that global standards are complemented by any additional disclosure requirements needed for achievement of local policy objectives (specific disclosures required for the EU taxonomy is a good example of this). Such regional innovations may also be suitable for global implementation through integration into international standards.

We are collaborating with all parties to achieve a globally legitimate comprehensive corporate reporting system that can deliver on these building blocks. As part of this, we would welcome close collaboration with the European Non-Financial standard setting process and believe that this would be mutually beneficial.

The European Commission has been both leader and powerful catalyst for all three of these building blocks. Through its Green Deal, together with the European Parliament, it set high ambitions and strong views regarding the creation of a sustainable, equitable and just society. Both will want to see these ambitions embedded in the disclosure standards and the standard setting process aligned with the NFRD.

However, it is important to strike the right balance between the EU's global ambitions and applicability. A successful solution needs to cater to the expectations of stakeholders globally as well as to the needs of globally operating companies. That is why we wish to work with the European Commission and EFRAG to determine the most efficient and effective path forward to achieve standard setting that delivers the above features for the first and second building blocks.

2.2 How to establish an appropriate coordination between the financial and nonfinancial reporting so as to ensure that financial and non-financial reporting provide an integrated view of the performance, position, development and impacts of reporting companies?

The integration of financial and non-financial reporting would also ensure that sustainability is becoming business as usual and taken into considerations in all business and financial decisions.

We believe the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD) provide a good basis to integrate financial and non-financial thinking by including non-financial information within the mainstream report, putting in place and disclosing the governance the company has in place to address these issues from the Board to executive committees and management practices and performing scenario analysis over the short, medium and long term to explore alternatives that may significantly alter the basis for "business-as-usual" assumptions and then be able to develop the relevant critical thinking within the company to adjust its strategy and governance to address the estimated impacts.

To ensure that connectivity between financial and non-financial reporting exists, it would be necessary to have an overarching board responsible for such connected reporting and the reporting system as a whole.

Furthermore, the system needs to be able to cater for the changing business and external environment. The frameworks and standards will need to be subject to continuous review and regular updates. Identifying these evolving trends would be the responsibility of the overarching board. It will focus on what standards are required to fully reflect a businesses' value creation, and how evolving global trends (such as climate change, inequality, the SDGs) need to be reflected in reporting, as well as identifying future issues. In this process, conciseness of the information is a key principle, meaning that further details would be found within the financial or non-financial disclosure.

Another key area of work to make financial and non-financial information more interconnected lies in accounting standards. CDSB is currently working on advancing integration of climate-related matters within the financial statements, to bridge the gap between the narrative reporting and the financial statements based on the recent IASB paper on IFRS standards and climate-related disclosures.

3. Possible changes to finance of EFRAG

3.1 What ideas do you have for financing of the non-financial reporting pillar? Should the financing reflect the public-private partnership?

We do not believe the funding structure of the non-financial reporting pillar should be any different from the current funding.

Financing should reflect the public-private partnership. Stakeholders should contribute, but it must be ensured that private funding does not lead to undue influence