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**Ref: ESMA answer to Fitness Check of the EU framework on public reporting by companies**

Dear Mr Guersent,

On 21 March 2018, the European Commission (EC) published a Consultation Document seeking feedback to evaluate the Fitness of the European Union (EU) framework for public reporting by companies ("Fitness Check"). The European Securities and Markets Authority (ESMA) thanks you for the opportunity to contribute to this assessment. Whilst we have provided detailed input to all the questions that are relevant for the matters falling under the remit of securities regulators, we also wish to convey some overarching remarks, with the objective of ensuring that this framework continues to contribute to the orderly functioning and integrity of financial markets in the Union.

*Endorsement of IFRS:* One important question in the Fitness Check relates to whether it is still appropriate that Regulation (EC) No 1606/2002 (hereafter, the 'IAS Regulation') prevents the EC from modifying the content of IFRS as issued by the International Accounting Standards Board (IASB) (a mechanism known as 'carve-in'). We note that the EC has already sought feedback on the possibility of introducing such mechanism to the endorsement process in the context of both the 2013 Maystadt Review<sup>1</sup> and the 2015 EC's evaluation of the IAS Regulation.<sup>2</sup> In both cases, ESMA, similar to the great majority of stakeholders, has cautioned against introducing such mechanism.<sup>3</sup> ESMA understands that the recommendation made in the final report of the High-Level-Expert Group on Sustainable Finance in this regard consisted

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<sup>1</sup> Should IFRS be more European, Mission to reinforce the EU's contribution to the development of *international accounting standards*, Philippe Maystadt (October 2013)

[http://ec.europa.eu/internal\\_market/accounting/docs/governance/reform/131112\\_report\\_en.pdf](http://ec.europa.eu/internal_market/accounting/docs/governance/reform/131112_report_en.pdf)

<sup>2</sup> [Report from the Commission to the European Parliament and the Council, Evaluation of Regulation \(EC\) No 1606/2002 of 19 July 2002 on the application of International Accounting Standards, Commission Staff Working Document \(18 June 2015\)](#)

<sup>3</sup> ESMA/2013/1415, [ESMA comments on the Draft Report "Should IFRS Standards be more European"](#), 10 October 2013 and 2014/ESMA/1344/Annex 1, [ESMA response to the European Commission consultation on the IAS Regulation](#), 7 November 2014

in proposing to provide the EC with powers to modify the IFRS standards issued by the IASB in the course of the endorsement process. In line with its prior positions, ESMA strongly disagrees with this recommendation, most notably because any European-specific adjustments to IFRS would defy one of the key objectives of the IAS Regulation, namely that financial reporting standards applied by listed issuers are accepted internationally and are truly global standards. In addition, we believe that modifications to IFRS at the European level would hinder the capacity of European companies to compete for financial resources on equal terms in global capital markets. In our view, the different levels of commitment to require IFRS as issued by the IASB around the globe is not a justification for introducing carve-ins. On the contrary, Europe should show leadership in reaffirming its commitment to IFRS. This in turn would increase its ability to influence the development of IFRS, which the EU should continue to actively do as part of the IASB's due process.

*Endorsement criteria:* Another related but separate question brought up by the Fitness Check is the inclusion of considerations on sustainability as part of the endorsement criteria of IFRS. While we fully support the Commission's ambition to develop an overarching and comprehensive EU roadmap on sustainable finance, we recommend the highest caution in this matter, as we believe these considerations fall well beyond the purpose of accounting. As stated in our recent comment letter<sup>4</sup>, we believe that "the primary objective of endorsed accounting standards remains to promote transparency and better decision-making in financial markets and, therefore, they should be considered as neutral with respect to other public policy objectives. We believe that this approach is ultimately the most beneficial for the performance of capital markets, including their capacity to support long-term investments". We strongly believe that the current endorsement process already provides the necessary safeguards to the European public good, by providing the possibility for the non-endorsement of a standard, which is not conducive to European public good. Rather than introducing an additional endorsement criterion, long-term and sustainability aspects could be articulated under the concept of 'European public good'.

*Non-financial information:* ESMA strongly welcomes that an important part of the consultation is dedicated to non-financial information as this plays an increasingly important role in complementing financial information. We believe that corporate reporting will preserve its relevance for investment decision-making only if it is capable of providing an integrated overview of the relevant financial and non-financial variables that affect an issuer's economic performance and financial position and which, ultimately, determine its ability to contribute to sustainable growth of the EU economy. Whilst it is premature to assess the impact of the recent developments in the EU framework in this area, preliminary analysis indicates that probably the effectiveness of the disclosure framework would have been greater had the Non-Financial Information Directive set up or indicated a specific framework and accepted a single set of standards to report this type of information.

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<sup>4</sup> ESMA32-61-259, [ESMA response to the European Financial Reporting Advisory Group \(EFRAG\) on the Discussion Paper Equity Instruments: Impairment and Recycling](#), 23 May 2018

*Digital reporting:* ESMA believes that technology and digitalisation have the potential to catalyse the benefits of effective and transparent financial communication in the EU Single Market. The revised Transparency Directive<sup>5</sup> mandated ESMA to specify the European Single Electronic Format (ESEF) to be used by issuers for the preparation of their annual financial reports starting in 2020 to make reporting easier and facilitate accessibility, analysis and comparability of annual financial reports. ESMA's draft RTS<sup>6</sup> strikes the fairest possible balance between costs and benefits for preparers and users, and would allow the EU to catch up with other major jurisdictions in terms of digital transformation. ESMA urges the EC to swiftly endorse the draft RTS on ESEF in order to provide certainty to the relevant market stakeholders and ensure timely preparedness of both software and issuers' capabilities.

*Enforcement:* Finally, ESMA also wishes to seize this opportunity to highlight again the need for deeper harmonisation through EU-level legislative measures in the area of enforcement of financial information and the benefits on investors' confidence and development of the EU Single Market. Enforcement of financial information is currently governed by the national laws implementing the Transparency Directive that provides only a minimum harmonisation regime. Harmonisation of enforcement activities has been a pillar of ESMA's work in recent years as documented in the ESMA supervisory convergence work in this domain and the recent Peer Review on the Guidelines on Enforcement of Financial Information.<sup>7</sup> Nonetheless, the European common framework for enforcement of financial information shaped by the ESMA Guidelines, including the discussion forum of the European Enforcers Coordination Sessions (EECS) and the European Common Enforcement Priorities (ECEP), cannot fully address the differences in powers, resources and roles of accounting enforcers in the individual Member States. Without having the intention to question or express a view on the institutional set-up of enforcement of financial information of individual Member States, ESMA encourages the EC to consider ways to work towards further harmonising the supervisory regimes in order to further enhance investor protection and the smooth functioning of the Capital Markets Union. Similar considerations also apply to the supervision and enforcement of non-financial information and other parts of an issuer's financial report (i.e. the management report).

Should you wish to further discuss these or other issues relating to our response to the Fitness Check, please do not hesitate to contact me.

Yours sincerely,

A handwritten signature in blue ink, appearing to be 'S/M', is written over a light blue horizontal line.

Steven Maijor

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<sup>5</sup> Directive 2004/109/EC as revised by Directive 2013/50/EU

<sup>6</sup> ESMA 32-60-204, [Final Report on the RTS on the European Single Electronic Format](#) (18 December 2017)

<sup>7</sup> ESMA42-111-4138, Peer Review Report, [Peer Review on guidelines on enforcement of financial information](#), 18 July 2017