UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

OFFICE OF THE
COMMISSIONER

01 July 2021

IFRS Foundation
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Re: Proposed Targeted Amendments to the IFRS Foundation *Constitution* to Accommodate an International Sustainability Standards Board to Set IFRS Sustainability Standards

Dear IFRS Foundation Trustees:

Thank you for the opportunity to comment on the IFRS Foundation's proposed constitutional amendments to create a new board for promulgating sustainability standards, the International Sustainability Standards Board ("ISSB"). As a Commissioner on the United States Securities and Exchange Commission ("SEC"), I have a deep interest in how the Foundation operates given the vital role the Foundation plays in global accounting standard-setting.[1] I understand the allure of setting up a sustainability standards board under the same umbrella as an established international accounting standard-setter, the International Accounting Standards Board ("IASB"). Nevertheless, the Foundation should avoid this venture into sustainability standard-setting because doing so would (i) improperly equate sustainability standards with financial reporting standards, (ii) undermine the Foundation's current important, investor-centered work, and (iii) raise serious governance concerns.

I. Accounting Standards and Sustainability Standards Are Fundamentally Different

Accounting and sustainability standards are fundamentally different from one another. Equating the two, as the Foundation's current effort does,[2] risks misleading investors.

[1] The views I express are my own and do not necessarily reflect those of the Commission or my fellow Commissioners.
[2] *See* IFRS Foundation Exposure Draft: Proposed Targeted Amendments to the IFRS Foundation *Constitution* to Accommodate an International Sustainability Standards Board to Set IFRS Sustainability Standards (Apr. 2021), https://www.ifrs.org/content/dam/ifrs/project/sustainability-reporting/ed-2021-5-

The singular focus of financial reporting—to paint an accurate financial picture of a company for investors—lends itself to objective, auditable, quantifiable, and comparable metrics. Assets, liabilities, revenue, and expenses can be measured, reported, and audited. Preparing and auditing a company's financial statements entails judgment and there are cross-jurisdictional differences in accounting standards, but the purpose of financial reporting is not up for debate.

Financial statements, prepared according to high-quality accounting standards, enable investors to make informed economic decisions. As the Foundation's website explains, "IFRS Standards contribute to economic efficiency by helping investors to identify opportunities and risks across the world, thus improving capital allocation."[3] Although investors are not uniform, by definition, an investor is "a person or group of people that puts its money into a business or other organization in order to make a profit."[4] Financial reporting is designed to help investors understand whether they will make a profit from their investment of money in a particular issuer.

By contrast, not only is the term "sustainability" imprecise, but the objective of sustainability standard-setting and sustainability reporting is not universally agreed upon and is not consistent over time.[5] Sustainability standard-setting is an inherently more subjective, less precise, less focused, more open-ended activity than financial accounting standard-setting. Symptomatic of this ambiguity and boundlessness, the Foundation proposes "provid[ing] the ISSB with the broadest possible objective within the strategic scope set by the Trustees."[6] The consultation document defines sustainability reporting as a "catch-all phrase referring to information related to all environmental, social, and governance (ESG) matters."[7] It is not limited to information in financial reports, but

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proposed-constitution-amendments-to-accommodate-sustainability-board.pdf [hereinafter Exposure Draft], 8, para. 14 ("The proposed amendments to create and incorporate a new board under the governance structure of the Foundation deliberately reflect the structure and function of the IASB where possible.").
[3] IFRS Foundation, *Who We Are* (last visited June 30, 2021), https://www.ifrs.org/about-us/who-we-are/.
[4] Cambridge Dictionary, *Investor* (last visited June 30, 2021), https://dictionary.cambridge.org/us/dictionary/english/investor.
[5] The Foundation's explanation of the ISSB's purpose provides little clarity. *See* Exposure Draft at 9, para. 16(b) (explaining that the ISSB's standards "would help investors and other participants in the world's capital markets to understand, compare and contrast a company's sustainability performance with that of other companies, and to determine how a company's performance relates to its value creation").
[6] Exposure Draft at 8, para. 14(a).
[7] IFRS Consultation Paper on Sustainability Reporting (September 2020), https://www.ifrs.org/content/dam/ifrs/project/sustainability-reporting/consultation-paper-on-sustainability-reporting.pdf [hereinafter Consultation], 17, n.39.

encompasses information in the more capacious set of "corporate reports."[8] Before the ISSB even begins setting standards, therefore, it will have to make difficult judgments about what areas those standards should cover and whom they are intended to serve. While the ISSB's efforts would be limited at first to climate issues, which are believed to be most urgent, the intention is to expand into other ESG issues.[9] Involving the Foundation in the inherently fraught and often political exercise of choosing sustainability issues for which standards are warranted risks tainting the IASB's financial accounting standards by undermining the apolitical nature of the organization within which these standards are made.[10]

Sustainability standards are intentionally laden with judgments about where capital should flow, a concept foreign to financial reporting standards. Hence, they must not be intermingled. Former SEC Chief Accountant Wes Bricker explained the difference between general purpose financial reporting standards and special purpose standards:

> When formulating standards for general purpose financial reporting, the IASB and the FASB do not seek to influence the outcome of investor capital allocation decisions or actions taken by management; instead, the boards' design standards that provide better information to inform those decisions and actions. The alternative, whereby standards are designed to privilege specific objectives, economic activities, financial products, or market participants, could diminish confidence in the accuracy or quality of reported information, which could thereby impair capital formation, and in turn, negatively impact economic activity.[11]

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[8] Exposure Draft at 16, para. 2(b). *Cf.* Exposure Draft at 16, para. 2(a) (explaining the IASB's focus on information in financial statements and other financial reporting).

[9] *See* Exposure Draft at 4, para. 2(b) ("The new board would initially focus on climate-related reporting while also moving quickly to work towards meeting the information needs of investors on other environmental, social, and governance matters.").

[10] The Foundation acknowledges the political undertones of the issues the ISSB will undertake. *See, e.g.,* Role Specification for Chair (and Vice-Chair) of the ISSB, https://www.ifrs.org/content/dam/ifrs/news/2021/issb-chair-role-specification.pdf [hereinafter Role Specification], 5 (stating that one of the "critical competencies for success" for the positions include "Political sensitivity—understanding political implications of sustainability reporting, including sensitivity to the impact of adoption of sustainability standards globally and nationally").

[11] Wesley Bricker, Chief Accountant, SEC, Remarks to the Institute of Chartered Accountants in England and Wales: "The intersection of financial reporting and innovation" (June 6, 2018), https://www.sec.gov/news/speech/speech-bricker-060618.

These concerns appear relevant to sustainability standards, which are designed for the particular objective of influencing capital flows.

Sustainability standards are unlikely to foster the same degree of accuracy, comparability, objectivity, and reliability across the reporting of a wide range of issuers that financial reporting standards do. Although sustainability standards at times may touch on economics, they are not fundamentally about economic decision-making. Indeed, whereas the IASB is charged with developing standards for use in "economic" decision-making, "economic" is conspicuously absent from the ISSB's mandate.[12]

The ISSB's standards will speak to more than just enterprise value and economics. The Foundation acknowledges that the ISSB's focus will shift over time from investors to the larger set of stakeholders. The latest proposal initially limits the ISSB's mandate to "information that is material to the decisions of investors and other participants in the world's capital markets."[13] However, the trustees also adopt a wide-ranging view of investors' needs, which could lead to mission creep.[14] Moreover, the articulated objective of the ISSB includes the goal to "connect with multi-stakeholder sustainability reporting," which further underscores that the board intends to serve the needs of constituencies other than investors.[15]

The consultation document points to, but fails to detail, synergies between financial and sustainability standards as a reason for the IFRS Foundation assuming this role.[16]

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[12] *Compare* Exposure Draft at 16, para. 2(a)(explaining that IASB standards should require information to help investors and others "make economic decisions"), *with* Exposure Draft at 16, para. 2(b) (explaining that ISSB standards should require information to help investors and others "in their decision-making").

[13] Exposure Draft at 4, para. 2(a). The consultation paper recommended a "gradualist approach" to materiality that would initially focus the ISSB's efforts on information material to investors and other market participants but consider how to broaden its scope as it proceeds with its work. *See* Consultation at 14, paras. 50-51.

[14] *See* IFRS Foundation Trustees' Feedback Statement on the *Consultation Paper on Sustainability Reporting* (Apr. 2021), https://www.ifrs.org/content/dam/ifrs/project/sustainability-reporting/sustainability-consultation-paper-feedback-statement.pdf, 28 ("To meet investors' needs, a company would need to report its significant impacts and dependencies on society and the environment that it is reasonably possible will affect its business model over the short, medium, and long term, and, therefore, drive the determination of its enterprise value.").

[15] Exposure Draft at 16, para. 2(b).

[16] Consultation at 8-9, paras. 25 ("The proposed establishment of the SSB within the institutional and governance structure of the IFRS Foundation could achieve the objectives of developing a framework for sustainability reporting which is coherent with and connected to financial reporting.") and 27 ("The SSB would operate alongside the IASB, and the two boards would benefit from the increasing interconnectedness between financial reporting and sustainability reporting.").

Certainly, as the IASB's sister, the ISSB automatically will enjoy a patina of trustworthiness and credibility, but that sisterhood will mask the assumptions, ambiguities, and uncertainties that characterize sustainability standards in a way that distinguishes them materially from financial reporting standards. Plans to weave sustainability standards and financial reporting standards together[17] are less likely to create synergies than to make it more difficult for investors to analyze financial reports by eroding the standards that undergird—and hence the objectivity, reliability, and comparability of—those reports.

II. The New Sustainability Standards Board Threatens to Undermine the Foundation's Current Important Work

The Foundation is proposing to amend the Constitution in ways that would dilute the Foundation's focus on "develop[ing] a single set of high-quality, understandable, enforceable and globally accepted accounting standards—IFRS Standards—and [] promot[ing] and facilitat[ing] adoption of the standards."[18] Adding another board under the Foundation's umbrella will cost the Foundation time, resources, and attention. Time spent setting up and overseeing the ISSB will not be spent overseeing the IASB. Expertise in financial accounting and expertise in sustainability are two distinct skill sets, and bringing sustainability experts on as Trustees or Advisory Council members could dilute attention from accounting standards and financial reporting expertise. Although there will be no immediate change in the Foundation's Trustees or the Advisory Council, the Foundation notes that the Trustees' and Advisory Council's "membership and [] expertise can be sufficiently adjusted where necessary in the coming years" to reflect the new sustainability mandate.[19]

The Trustees will be required to consult with both the IASB and ISSB in appointing the Foundation's Executive Director,[20] which will again dilute the Foundation's and the Executive Director's attention on accounting standard-setting. Likewise, the technical staff will be accountable to the Chairs of both the IASB and the ISSB,[21] which will result in a weakening of the technical staff's single-minded focus on technical accounting

[17] *See, e.g.,* Exposure Draft at 39, para. B20 (envisioning work to "explore how, conceptually, [the ISSB's] standard-setting could be linked to the work of the IASB, and how sustainability reporting and financial reporting would be linked").
[18] IFRS Foundation, *Who We Are* (last visited June 30, 2021), https://www.ifrs.org/about-us/who-we-are/.
[19] Exposure Draft at 6-7, paras. 10(b) and 10(d).
[20] Exposure Draft at 30, para. 60.
[21] Exposure Draft at 30, para. 61.

issues. Full-throated support of the ISSB will be a requirement for all Trustees, which means that people who do not equally value sustainability reporting and financial reporting will be ineligible to serve on the Foundation,[22] thus limiting the perspective diversity the Foundation values.[23]

III. Proposed Constitutional Provisions Could Undermine the Integrity of the New Board's Standards

Protecting the independence of the ISSB through appropriate governance, structural protections, and funding is essential for its credibility. Cutting corners at the beginning of the ISSB's life for expediency may adversely affect its culture, harm the quality of its standards, and impair its integrity for many years to come. Accordingly, should the ISSB be formed, the Foundation should rethink certain proposed decisions regarding the ISSB's structure. A lot of money is on the line as any new standards likely will replace or supplement existing standards already in use and will direct substantial global capital flows. Therefore, many interested parties will seek to influence ISSB standard-setting.

Governance measures that protect the integrity of the standard-setting process are a crucial prerequisite for effective standard-setting. Several governance issues embedded in the proposed amendments to the Foundation's Constitution raise concerns. The Foundation, acknowledging that the constitutional provisions applicable to the ISSB will not be identical to those applicable to the IASB, explains that lower standards are appropriate "to allow for the new board to reach an appropriate level of maturity in its standard-setting and develop its technical expertise within the confines of the Trustees' strategic direction."[24] The proposal, for example, would permit the ISSB to have a higher number of part-time members than is currently permitted on the IASB (up to 6 of 14 compared to only 3 of 14 for the IASB),[25] which heightens conflict of interest concerns as outside employment may impair part-time members' objectivity.[26]

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[22] *See* Exposure Draft at 17, para. 6 ("All Trustees shall be required to show a firm commitment to the IFRS Foundation, the IASB and the ISSB as high-quality global standard-setters . . .").
[23] *See* Exposure Draft at 27, para. 44 ("A broad base of skills, experience, and perspectives is needed [for the ISSB]").
[24] Exposure Draft at 8, para. 14.
[25] Exposure Draft at 26, para. 43 (allowing for a "minority" of ISSB members to be part-time). By contrast, only three members of the IASB are permitted to be part-time. *See* Exposure Draft at 22, para. 24.
[26] *See* SEC Final Staff Report, Work Plan for the Consideration of Incorporating International Financial Reporting Standards into the Financial Reporting System for U.S. Issuers (July 13, 2012), https://www.sec.gov/spotlight/globalaccountingstandards/ifrs-work-plan-final-report.pdf [hereinafter SEC

Proposed procedural decisions also raise concerns. Unlike the IASB's standards which require approval by a supermajority of members,[27] the ISSB's standards would require approval by only a simple majority of members.[28] This lower approval standard implicitly recognizes the difficulty in getting consensus around sustainability standards. When combined with the rule allowing the chair to cast an additional vote in the case of a tie,[29] the simple majority rule means that only seven members of the board would have to vote in favor of a sustainability standard for it to be approved. The Foundation also has deferred establishment of due process procedures for the new board,[30] which makes it difficult to understand how the standard-setting process will work.

Also of concern from an independence perspective is a provision that requires the ISSB "to establish and maintain liaison with relevant stakeholders with an interest in sustainability reporting standard-setting."[31] This provision is much more open-ended than the equivalent paragraph for the IASB, which requires that board "to establish and maintain liaison with national standard-setters, other standard-setters, and other official bodies with an interest in accounting standard-setting."[32] The ISSB's liaisons with non-official stakeholders as opposed to official standard-setters and other official bodies affords an opening for improper influence on standard-setting. Similarly, a provision that allows the ISSB to outsource work to "national standard-setters or other organisations" raises independence concerns.[33]

Finally, as compared to that of the IASB, the geographic composition of the ISSB would give one less guaranteed member to each region (other than Africa, which only has one board seat on the IASB) in favor of more at-large members.[34] Allowing the trustees this kind of enhanced discretion over the composition of the board could erode the ISSB's independence and objectivity. A better approach would be to replicate the IASB's

Staff Report], 50 (in the context of the IASB, raising concerns about part-time members: "Although this is limited to a small minority of members and does not appear to have resulted in an actual issue in the past, the presence of such relationships does pose the possibility of including board representation of individuals who are not viewed as objective.").

[27] Exposure Draft at 24, para. 35.

[28] Exposure Draft at 28, para. 54.

[29] Exposure Draft at 28, para. 53.

[30] *See* Exposure Draft at 7, para. 10(f) ("The potential revision of procedures concerning the new board's due process will be considered separately."). *See also* Role Specification at 3 (referring to "the new ISSB's *Due Process Handbook[]* (To be developed in discussion with the Chair)").

[31] Exposure Draft at 27, para. 46.

[32] Exposure Draft at 23, para. 27.

[33] Exposure Draft at 29, para. 55(e).

[34] Exposure Draft at 27, para. 45.

geographic balance with more representation for the Americas to balance out the "specific relationship established between the EU and the Foundation"[35] and perhaps another seat for developing nations whose most pressing concern may be raising their citizens' standard of living, an objective that may not align perfectly with the developed world's sustainability measures.

The Foundation's hurried approach to starting the ISSB is another cause for concern.[36] Rushing such an important change raises the likelihood of design flaws in the board and the standards it ultimately produces. The Technical Readiness Working Group is already providing a "running start" for the ISSB by starting to formulate standards.[37] Exploratory work has begun on the establishment of a multi-stakeholder expert consultative committee.[38] The Foundation already issued a call for nominations for the ISSB Chair and Vice Chair.[39] All these steps have happened before the Foundation's definitive decision on whether to stand up the ISSB.

The questions around ISSB's funding also raise concerns. The Trustees acknowledge that additional money will be needed to finance the new board and the importance of keeping that funding separate,[40] but do not specify where the funds will come from.[41] Even the Foundation's current funding structure, which relies on voluntary contributions from public and private entities, presents independence challenges.[42] The Foundation should resolve the funding issues before forming the ISSB.

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[35] Exposure Draft at 38, para. B12.

[36] *See, e.g.,* Exposure Draft at 40, para. B26 ("the Trustees remain on track to make a final determination about a new board in advance of the United Nations Climate Change Conference (also known as COP26), scheduled to be held in November 2021").

[37] *See, e.g.,* IFRS Foundation, *Technical Readiness Working Group* (last visited June 30, 2021), https://www.ifrs.org/groups/technical-readiness-working-group/; Exposure Draft at 40, para. B25 ("the Trustees have established a technical readiness working group; that group's proposals could assist the new board in making a running start to its standard-setting").

[38] *See* Exposure Draft at 38, para. B13.

[39] *See* Role Specification.

[40] Exposure Draft at 39, para. B16.

[41] Exposure Draft at 39, para. B18 ("the Trustees are seeking funding from a diverse range of sources to secure the board's future and independence").

[42] *See* Peter Williams, *The Vulnerability of the IASB's Funding Structure*, ACCOUNTING & BUS., July 1, 2018, https://www.accaglobal.com/my/en/member/member/accounting-business/2018/07/in-focus/iasb-funding.html ("Lack of certainty over funding is a risk for the work of the IASB . . . as is having to fend off accusations that those who pay the piper have undue influence on the choice of tunes."); SEC Staff Report at 52 ("The Commission previously has noted that the IASB may be subject to a perceived, or potentially an actual, connection between the availability of funding and the outcome of the IASB's standard-setting process."), 57-58 ("[T]he continued reliance by the IFRS Foundation on funding from the largest

IV. Conclusion

I urge the Foundation to reconsider the plan that it has already set in motion to form the ISSB as a sister organization to the IASB. The motivating objective of the Foundation's effort—a set of globally accepted and consistently applied sustainability standards—is well-intentioned but unrealistic and may undermine the important concerns at the heart of this effort. We do not have perfectly converged global financial reporting standards. A single set of sustainability standards is an even more difficult task given the uncertainties around the scope of issues such standards should cover and their purpose, and the difficulty in reducing sustainability matters to objective, easily comparable, broadly applicable metrics.

Moreover, sustainability standard-setting will shift the flow of capital in ways that inadvertently may undermine sustainability goals. Advocates of the Foundation's plan embrace the power of sustainability standards to direct capital flows to meet net zero emissions goals,[43] but what if the sustainability standards turn out to be flawed? Deciding how and from where transformative technologies and socially beneficial innovations will emerge relies on the collective wisdom and on-the-ground experience of the billions of people who contribute to and draw from the global economy. By contrast, centrally determined, universally applicable, inflexible standards can impede the global economy's ability to effectively address climate change and the other critical issues on which the ISSB will likely focus.

I appreciate having the opportunity to comment on the proposed amendments and would be happy to speak with you about the issues I have raised in this letter.

Sincerely,

Hester Peirce

Hester Peirce
SEC Commissioner

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accounting firms will continue to cause concerns as to the adequacy and independence of the IASB's funding model").

[43] *See* G7 Finance Ministers & Central Bank Governors Communiqué (June 5, 2021), https://home.treasury.gov/news/press-releases/jy0215 (welcoming the IFRS Foundation's efforts as part of a mobilization of "private sector finance . . . to meet our net zero commitments").