

14 July 2021

Commissioner McGuinness
Directorate-General for
Financial Stability
Financial Services and
Capital Markets Union
European Commission
B-1049 Brussels

Submitted electronically via the EU Commission's website

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Re: Proposal for a Directive on Corporate Sustainability Reporting (CSRD)

Dear Commissioner McGuinness

The Institut der Wirtschaftsprüfer in Deutschland e.V. [Institute of Public Auditors in Germany, Incorporated Association] (IDW) is pleased to provide its views concerning the EU Commission's Proposal for a Directive on Corporate Sustainability Reporting (CSRD) (hereinafter referred to as "the Proposal"). The IDW has previously responded to the EU Commission's Consultation Document "Review of the Non-Financial Reporting Directive 2020" in a letter dated 8th June 2020.

The IDW represents over 11,000 Wirtschaftsprüfer [German Public Auditors], which is approximately 85 % of all Wirtschaftsprüfer in Germany. Our members are from the only profession in Germany to have been entrusted with the performance of statutory audits of the financial statements of all entities that are legally required to have their financial statements subject to audit in Germany, including the larger publicly listed companies that are presently required to publish non-financial information (NFI).

We agree with many aspects of the Proposal, and support the EU Commission's goals, but would like to comment in more detail in this letter in order to explain the points raised in our electronic submission. Our comments are intended to be constructive and supportive to ensuring the success of the CSRD once applicable in practice.

GESCHÄFTSFÜHRENDER VORSTAND:
Prof. Dr. Klaus-Peter Naumann,
WP StB, Sprecher des Vorstands;
Dr. Daniela Kelm, RA LL.M.;
Melanie Sack, WP StB

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Support for the EU Commission's initiatives

The IDW is supportive of the EU Commission having taken the lead in driving sustainability and commends the EU Commission on the recent completion of its Action Plan "Financing Sustainable Growth". We support the aims behind the Action Plan and its associated initiatives, including the revision of the extant Non-Financial Reporting Directive. We also support the proposed change in name to Corporate Sustainability Reporting Directive.

Recent developments at a global level and in certain other parts of the world are also encouraging, as is the increase in the pace of progress given the need for global action on climate change and further sustainability related matters. The EU Commission's initiatives have also encouraged others to take action in this arena.

The necessity of a globally accepted basis for sustainability reporting

We support the EU Commission's acknowledgement that global solutions are needed, notwithstanding a potential need for supplementary measures at national or regional level to accommodate respective different legal environments. Without a significant degree of global alignment there is a danger that sustainable growth may not be achieved as intended. Raising finance and conducting business in a particular regulatory environment must not become onerous in a single region to the extent that investment capital essential to the transition to a sustainable economy moves elsewhere. Corporate sustainability reporting is one of several such issues in this context.

The Proposal envisages adoption of EU sustainability reporting standards by way of delegated acts, with an appropriately restructured EFRAG tasked with the development of new standards. We note that this way of "legislating" in the EU would be new to corporate reporting. Currently the Accounting Directive applies to all limited liability companies, with the IAS Regulation applying only to the consolidated financial statements of capital market-oriented companies, whereby the international standards IFRS are subject to an EU-endorsement mechanism. This two-pronged approach is accepted and has created a "level playing field" for the majority of European companies and their competitors operating globally.

As the EU Commission is aware, recent global developments include statements issued by major ESG standard setters highlighting their joint support of the IFRS Foundation's initiative. International organisations, such as the Financial Stability Board (FSB) and the International Organization of Securities

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Commissions (IOSCO), now also see a need for global standards for sustainability reporting and therefore support their planned development by an international standard setter. There is also support from the G7 and the G20. The IFRS Foundation is expected to establish a separate international standard setting board for sustainability reporting later this year, with preliminary work underway, such that it appears unlikely that EFRAG would develop EU-only standards more quickly.

Given the incidence of global supply chains and the worldwide use of financial and non-financial resources, all stakeholders have an interest in ensuring that entities' sustainability reporting is globally comparable: a global regulatory "patchwork" would result in additional costs for stakeholders as well as being detrimental to sustainable growth by impairing market transparency.

We therefore encourage the EU Commission (via EFRAG) to examine which aspects of sustainability reporting should – at least in the long term – be better addressed at the global level i.e., where it would make sense for EFRAG to become involved in the development of global principles, which would then be supplemented at the regional or national level as appropriate.

We accept that the European approach is intended to go beyond the IFRS Foundation's initiative, which will most probably be initially limited to specific aspects (climate, and financial materiality, i.e., an investor lens). However, intensive cooperation and coordination should result in considerable synergy benefits for all concerned.

In the context of integrated reporting, "connectivity" to IFRS could be established with a solution whereby a global sustainability reporting standard would be developed for globally active companies with substantial support from the EU. Global standards on sustainability reporting could then be adopted into European law analogously to the IFRS using the well-established "endorsement" mechanism. Such a global baseline of sustainability reporting standard with a focus on market transparency would then be supplemented by EU legal requirements or standards as necessary to achieve EU-specific public policy objectives.

As the Proposal extends sustainability reporting to large privately-owned companies, numerous companies in the EU, and Germany in particular, will be obliged to report on sustainability for the first time in accordance with the Accounting Directive as transposed into national law. The "connectivity" between sustainability and financial reporting will therefore need to be addressed at the European or Member State level. We also suggest the EU Commission also consider the potential need for "scalability" as well as a staged

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approach to implementation for those (newly included) companies that neither fall within the scope of the IAS Regulation nor that will be entitled to apply the European standard for SMEs.

As far as standard setting by EFRAG is concerned, we note that work on European sustainability reporting standards is ready to begin at the request of the EU Commission, although the formal structures have not yet been established. It will be important for the EU Commission to ensure transparency in its decisions as to which relevant groups should participate in standard setting mechanisms from the outset and that the due process is followed so as to increase acceptance of the output and EFRAG as a standard setter.

Implementation deadlines will potentially pose significant challenges to all parties affected

Article 5 of the Proposal requires the European legislative procedures to be completed by June 2022 and the Member States to transpose Articles 1 to 3 of the Directive by 1 December 2022, and to ensure that its provisions apply to companies for the financial year starting on 1 January 2023 or during calendar year 2023. Article 6 sets out the date of entry into application of the amended provisions of Regulation (EU) No 537/2014 (the Audit Regulation) on 1 January 2023.

We acknowledge the EU Commission's drive to enact the necessary legislation to bring corporate sustainability reporting to the next level quickly. However, we note that the deadline proposed will pose practical challenges to the EU Commission itself as well as to Member States having to transpose specific matters into national law (e.g., in exercising Member State options). In addition, many entities within the EU, and particularly those not currently subject to the NFRD will find the proposed deadlines challenging – for Germany it is expected that the number of reporting entities falling under the CSRD and thus required to prepare sustainability reports will increase thirty-fold! Indeed, because the (first) standards will not be available until the end of October 2022, entities only have a few months before the start of the first financial year affected by the new regulations to implement the necessary systems to capture the information to be reported. They must also develop the necessary (new) technical expertise. These systems are also needed as a basis for reliable reporting and for an external assurance engagement, irrespective of whether this is a limited assurance or reasonable assurance engagement. The deadline is likely to result in problems for many of the reporting entities affected, especially as the scope of sustainability reporting is likely to be significantly expanded in comparison to

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current non-financial reporting. The audit profession is ready to play its role in actively supporting the implementation of the many necessary changes.

Furthermore, we doubt that there would be sufficient time for EU Member States to ensure adequate processes are in place to allow the accreditation of other assurance services providers that are not already members of the auditing profession – notwithstanding that they may have been active in this area. High quality assurance is in the public interest.

In addition, reporting standards are needed before the ESEF taxonomy can be extended to cover the information required by the CSRD and before reporting entities will be in a position to tag their sustainability information. The Proposals do not appear to allow sufficient time for this. In the appendix to this letter, we also point out that, in relation to financial statements, certain aspects of the ESEF Regulation proved problematical. Indeed, with the exception of four Member States, the requirements could not be implemented within the original timeframe. It would be unfortunate were this to be repeated in regard to sustainability reporting.

We therefore urge the EU Commission to reconsider the proposed deadlines in order to ensure all affected parties have sufficient time to achieve a successful implementation of these significant changes. This might involve, providing for an appropriate transition period – as a minimum – to allow those entities not covered by the NFRD currently sufficient time to establish effective sustainability reporting systems ahead of the requirement to report under the CSRD for the first time.

Scope expansion – all large and all listed entities except micros

We agree that the Proposal's expansion of the scope of sustainability reporting is appropriate. The need for transparency concerning the sustainability aspects of corporate activities ought not (in contrast to the current legal situation) to be determined solely on the way in which an entity raises capital or the sector in which an entity operates. Certainly in Germany, entities that neither use the regulated capital markets nor operate in the financial sector represent a significant part of economic activity. They commonly use bank lending, such that banks demand reliable and comparable information on sustainability-related aspects when granting loans to such entities.

The EU Commission assumes that the number of affected companies in the EU will more than quadruple. According to initial estimates, the scope of application in Germany will increase by a factor of 30. Instead of around 500 companies at

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present, from 2023 onwards around 15,000 companies will be subject to the obligation to report on sustainability as all large, limited liability companies come under the scope of the CSRD.

Above we express concerns as to the ambitious timeframe envisaged by the Proposal. In this context we suggest the EU Commission discuss whether entities due to come under the scope of the CSRD might be introduced in a phased approach. For example, initially only entities with 500 or more employees might be covered.

We agree that small and medium-sized listed companies should only be included from 2026, with specific SME standards to be submitted by the EU by October 2023 (Article 19c Draft Accounting Directive). These companies therefore have a significantly longer preparation period at their disposal.

Placement of sustainability reporting in the management report

We support the proposed removal of the current Member State option on where and when non-financial information may be reported. Limiting the increasing "fragmentation" of company-related information in terms of where and when information is published, is helpful.

Information on sustainability aspects is increasingly viewed as equally important as financial reporting, not least because sustainability aspects can influence the economic situation of entities in many ways: inclusion of sustainability reporting within the management report is appropriate, especially as it mirrors the increasing integration of financial and non-financial aspects an entity reports to investors and other stakeholders.

Embedding sustainability within reporting entities' systems of corporate governance

We support the proposed inclusion of sustainability reporting within Article 33 of the Accounting and Article 4 of the Transparency Directives, as this secures equal status to financial reporting.

We are aware that the EU Commission is intending to finalize a further Directive on sustainable corporate governance later this year, addressing the role and responsibilities of a reporting entity's Board of Directors. As we have commented above, an entity's systems for capturing the information to be reported are also needed as a basis for reliable reporting and for an external assurance engagement, irrespective of whether this is a limited assurance or

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reasonable assurance engagement. We would therefore support the EU Commission clarifying the specific duties and responsibilities of the reporting entity's management board regarding such systems and internal controls in finalizing these two Directives.

In view of this, we welcome the proposed expansion of the Audit Directive to assign a specific responsibility to the audit committee for monitoring the sustainability reporting process similar to that already in place regarding the entity's financial reporting. An explicit legal responsibility for monitoring the effectiveness of the reporting entity's internal quality control and risk management systems regarding sustainability reporting serves to ensure entities establish the necessary systems with an appropriate degree of diligence.

General comments on assurance-related aspects

In relation to assurance, we note that there are important arguments for requiring reasonable rather than limited assurance, but we recognize that for cost reasons, limited assurance may be acceptable for a transitional period. We note a number of assertions made in the Proposal regarding assurance standards and limited assurance that are not factually correct. We also note that permitting assurance practitioners other than statutory auditors to obtain assurance on CSR reporting within the management report involves difficulties for users. It is particularly serious from a quality of assurance point of view that the proposals do not adequately ensure the quality of assurance practitioners that are not statutory auditors. Although we support the digitalization through ESEF, we identify some misconceptions about the ability of ESEF to be used for the preparation of financial statements, the management report and CSR reporting. We have also identified some potential issues with assurance on CSR reporting when information in those reports include information from supply chains outside of the corporate group. The details supporting our concerns are included in the appendix to this letter.

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We would be pleased to provide you with further information if you have any additional questions about the content of this letter, or to discuss our views with you.

Yours sincerely

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Chief Executive Officer

Bernd Stibi
Technical Director Reporting

Appendix

Detailed comments on assurance-related aspects of the Proposal

1. Interconnectivity of financial reporting and sustainability reporting and the public interest need to ensure a comparable level of both quality and assurance

Taken together, corporate reporting of financial and non-financial information provides stakeholders with a far more comprehensive and holistic picture of an entity's past performance and an indication of its future potential than either could do in isolation, and it is anticipated that over time corporate reporting will be further integrated.

Users of corporate reports on sustainability related matters increasingly view this information as at least equally important to their decision-making as the "traditional" financial statements, although concerns remain as to the potential for greenwashing and there have recently been many prominent calls for sustainability related information to be more comparable as well as more reliable.

We anticipate that EFRAG's mandate in regard to standard setting for sustainability reporting will address the need for comparable information. It is no longer acceptable that non-financial information reported could be of lesser quality than financial information, nor that independent external assurance is dispensable in this context. The quality of sustainability-related information reported ultimately needs to be equivalent (so-called "investor grade" reporting) if stakeholder perceptions of a reporting entity presented in its financial statements and management report are not to be distorted by misleading, inaccurate or biased sustainability reporting. Thus, we support the EU Commission's goal for reasonable assurance in order to serve the public interest.

We note the Proposal initially requires limited assurance on sustainability reporting. The statement on page 12¹ of the Proposal is important and we support the EU Commission being required to report to the EU Parliament and Council on the implementation of assurance requirements no later than 3 years

¹ Page 12: "The proposal includes a requirement that the Commission report to the European Parliament and to the Council on the implementation of assurance requirements no later than 3 years after the entry into application of this Directive. The report will be accompanied, if appropriate, by legislative proposals for stricter assurance requirements ('reasonable assurance')."

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after the entry into application of the new CRSD, and to accompany its report, if appropriate, by legislative proposals for stricter assurance requirements (“reasonable assurance”) and urge the EU Commission to act on this in due course.

In several EU Member States assurance on NFI reports is already a feature either due to the exercise of Member State option in the current NFRD or voluntarily; and limited assurance is expected to be voluntarily replaced by reasonable assurance as use of this reporting advances.

In Member States such as Germany, an audit of financial statements already encompasses reasonable assurance on the management report with the exception of information specifically identified as not having been subject to assurance. The auditor expresses an opinion as to whether the management report as a whole provides an appropriate view of the Entity’s position. However, German law currently does not require NFI to be subject to assurance as part of this work. Having a report only partly subject to assurance already poses challenges to readers’ understanding and perceptions of the quality of information. Considering the importance attached to information reported in the management report as well as the awkward situation that having a management report with different parts subject to different levels of assurance and reported upon by different assurance services providers would cause, we suggest the EU Commission consider including a Member State option permitting reasonable assurance to accompany the application of new sustainability reporting standards.

2. Scope and underlying subject matter of an assurance engagement under the CSRD will require clarification

In the absence of sustainability reporting standards for application in the EU, the underlying matter subject for assurance and the design of assurance engagements discussed in the Proposal cannot yet be fully anticipated. Various aspects need careful consideration. Clarification will be essential so that readers of assurance reports on European corporate sustainability reporting have reasonable expectations in regard to the scope and any inherent limitations of both reporting and assurance engagements, but also to ensure that their valid needs can be adequately addressed as far as possible.

Requiring an auditor or other assurance practitioner to obtain assurance on a sustainability report as a whole involves a very different work focus to requiring that assurance be obtained in respect of one or more specific individual item(s)

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that are either within such a report or reported separately. Similarly – and from a German perspective of significant importance – requiring the statutory auditor obtain reasonable assurance on a management report as a whole, of which sustainability-related information forms a part, would also change the work focus in regard to sustainability reporting.

A number of issues need to be considered in determining precisely what assurance on sustainability reporting should and can encompass. For example,

- Recent discussions the IDW has held with certain NGOs reveal that they expect that assurance would always be obtained on certain specific matters within a report irrespective of their relevance (or materiality) in the reporting entity's unique circumstances – i.e., there appears to be no common understanding of the assurance engagement approach to the concept of risk assessment and materiality. Most generally accepted assurance standards follow a risk-based approach, which, also taking materiality considerations into account, means that the auditor's (or assurance practitioner's) procedures are not focused on each separate matter reported to the same level of scrutiny, since, often contrary to the expectations of such parties, the assurance opinion relates to the view portrayed by the report taken as a whole or in relation to certain information categories.
- With regard to assurance on individual matters within a report, we understand that some investor representatives believe that assurance specifically on one or more selected individual KPIs would be highly beneficial to their investment decisions. Essentially such users may desire an assurance opinion on more than one KPI, with each being viewed in isolation.
- It may not be possible to obtain any meaningful level of assurance on certain information on e.g., unreliable future oriented information (i.e., forecasts that are based on assumptions that are largely speculative in nature). In other cases, assurance is not obtained on the forecasts, but rather on the reasonableness of the assumptions and whether the forecast is appropriately prepared on the basis of the assumptions in accordance with the reporting framework.
- The nature of some elements of reported sustainability information may mean that there are further inherent limitations impacting reporting or the assurance engagement which may demand transparency.

Such diverging demands and limitations together with related cost: benefit considerations will need to be taken into consideration in determining the scope

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of assurance engagements to be performed under the CSRD and any limitations thereof.

Furthermore, the Proposal's reference to the assurance provider's opinion covering the process carried out by the undertaking to identify the information reported pursuant to the sustainability reporting standards is unclear. This could be interpreted as constituting a materiality judgment (i.e., is the information sufficiently material from a quantitative or qualitative perspective as to warrant disclosure in the corporate sustainability report), whereas others may interpret this as meaning the process of data collection, assimilation and report preparation (which in the context of the preparation of financial statements would equate with what is commonly referred to as "internal control over financial reporting" and for which the auditor does not explicitly provide an opinion in the EU). The latter interpretation would only make logical sense if management were required to describe this process within the sustainability report: however, the EU Commission must also bear in mind that a requirement for assurance on internal control over sustainability reporting would add significant cost to assurance engagements. We urge the EU Commission to clarify its intention when finalizing the Directive.

3. Provision of assurance services by the statutory auditor with a Member State option to allow assurance by another independent assurance services provider

Whilst the Proposal would require the statutory auditor perform assurance work on sustainability reporting, it also foresees permitting Member States to allow any independent assurance services provider accredited in accordance with Regulation (EC) No 765/2008 of the European Parliament and of the Council to provide an opinion on sustainability reporting on the basis of a limited assurance engagement.

In some jurisdictions assurance providers other than the statutory auditor currently provide assurance services in regard to NFI or further sustainability-related information reported. However, in Germany generally the statutory auditor has been engaged to perform voluntary assurance engagements in this area. A recent publication by IFAC in cooperation with the AICPA and CIMA: "The State of Play in Sustainability Assurance"² provides relevant information concerning four of the larger EU Member States, which indicates minimal

² See pages 7 and 15: [IFAC-Benchmarking-Global-Practice-Sustainability-Assurance \(1\).pdf](#)

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involvement of assurance providers other than audit firms or affiliated firms in this field. We discuss two practical issues in this respect:

3.1 Two different assurance providers: two different assurance reports

An adequate understanding of the impact sustainability-related issues can have on a business and the impact a business can have on its environment demands thorough familiarity with all aspects of that business. Given the comprehensiveness of the statutory auditor's understanding of the reporting entity's business, including its legal and economic environment, and internal systems and organisation, there are clear advantages in terms of assurance and audit quality as well as efficiency gains and improved effectiveness from the synergy involved in requiring the statutory auditor obtain assurance on corporate sustainability reporting. An independent assurance service provider will generally neither possess, nor be able to obtain, such extensive knowledge of the company, because a limited assurance engagement would focus primarily on obtaining only a general understanding of the entity's reporting process for corporate sustainability reporting.

Having different assurance providers would also have unintended consequences for the supervisory bodies of the reporting entity (e.g., audit committee), because their own monitoring of the reporting and assurance process (covering both financial and sustainability reporting) would become considerably more burdensome and complex.

Since, with a few specific exclusions, the required content of the management report in Germany is covered as part of the financial statement audit and reported upon in the auditor's report, it would be confusing for users of corporate reporting were the section of the management report relating to sustainability-related issues to be addressed by another assurance services provider using a separate assurance report. Even more confusion might be generated in future as reporting standards further integrate sustainability information with financial information. In other EU Member States where the management report is not subject to assurance the same disadvantages of splitting assurance work would apply.

In addition, if the assurance engagement on the sustainability reporting in the management report is not performed by the auditor, but by another assurance services provider, information on this part of the assurance work would be missing from the auditor's audit file, which would complicate external supervision (in Germany, the auditor oversight authority would not have the

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possibility to fully assess the quality of all work performed for a client in the course of an inspection at the auditor's premises).

3.2 Ensuring a level playing field and equivalent quality of assurance services

The Proposal also requires Member States to ensure that consistent requirements are established for all persons and firms, including statutory auditors and audit firms, who are allowed to provide an opinion on the assurance of sustainability reporting.

However, this aspect of the Proposal needs to be more robust to ensure a level playing field between those assurance providers who hold the recognized professional qualification as a prerequisite for them to serve as statutory auditors and all other assurance providers. Permitting the engagement of other assurance providers would result in considerable implementation problems in practice and lead to massive distortions of competition as well as a significant impairment in users' perceptions about the quality of assured sustainability information. This could undermine confidence in the reliability of corporate reporting as a whole.

If the Proposal's Member State option is retained, the EU Commission should address the fundamental question of how the Directive can ensure a level playing field.

The term "consistent requirements" (see amendments to Article 34 of Directive 2013/34/EU) is insufficiently clear and could be interpreted as being different from the – arguably more appropriate term – “equivalent requirements”. Indeed, whether equivalence could actually be achieved in practice is questionable, since it is not readily conceivable that, for example, an NGO intending to provide such assurance services would be subject to an oversight and disciplinary system that is even remotely comparable to the comprehensive and strict regulatory framework applicable to the auditing profession.

True equivalence would require equivalent professional codes of conduct and ethical behavior, equivalent licensing and registration requirements, equivalent standards governing education training, examinations and CPD, equivalent professional qualifications, equivalent standards of professional practice, equivalent internal quality management systems, as well as equivalent external quality assurance and disciplinary systems, and public oversight, etc.

In addition, the CSRD would need to ensure Member States using this option establish and maintain a mechanism for determining equivalence as part of their

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accreditation of independent assurance services providers, which would appear to be a challenging and costly exercise in practice. The Proposal is unclear as to which body would monitor equivalence at Member State level and who would bear the costs of this. It will be essential for Member States to establish effective mechanisms quickly, such that the quality of assurance is not compromised.

In the context of consistency, the Proposal addresses only certain requirements of the Statutory Audit Directive. Certain requirements of the EU Audit Regulation and professional standards for auditors would also need to be matched with equivalent requirements for any other external assurance services providers. In regard to ensuring independence and safeguarding assurance engagement quality, the amendments of the Proposal relating to Article 5 of the Audit Regulation (EU) No 537/2014 should equally apply to any other assurance services provider. So as not to put statutory auditors at a competitive disadvantage, the amendment to Article 14 of that Regulation – if retained (here we refer to our comment on auditor independence below) – ought also to apply to any other assurance services provider.

4. Auditor independence: Classification fees received by an auditor for assurance services relating to corporate sustainability reports

As noted above, in Germany, a statutory audit of financial statements already encompasses obtaining reasonable assurance on information reported in the management report. In the absence of convincing arguments to the contrary, further additional assurance requirements becoming applicable to sustainability reports that – under the Proposal – are to be included within the management report, would logically also form part of a statutory audit of financial statements in Germany. Those charged with governance – not management – are responsible for engaging the auditor for such statutory audits. Hence, if assurance on the sustainability report were to be a part of the statutory audit, it would be those charged with governance who would be engaging the auditor to perform the assurance engagement. Indeed, as we have discussed above, where the statutory auditor performs such assurance procedures on corporate sustainability reporting, there is a clear advantage in terms of assurance and audit quality in addition to efficiency and improved effectiveness through synergies, but no impairment of auditor independence (it merely extends the scope of work done by that auditor). Consequently, we fail to see any valid reason for fee income (from this additional assurance work) to be classified as a non-audit service subject to fee caps or to be subject to any approval by those charged with governance as a non-audit service. In our view this forms part of

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the audit fee not subject to fee cap restrictions applicable to “true” non-audit services. Indeed, there may be cases where an auditor could not accept an assurance engagement if the respective fee relationships were such that the cap precluded this, resulting in an entirely counter-intuitive situation, and certainly detrimental to the statutory auditor from a competitive standpoint.

We therefore suggest that in finalizing the Directive, the EU Commission should consider this aspect of the Proposal and refrain from amending Article 14 of Regulation (EU) No 537/2014 to require statutory auditors and audit firms to annually inform the competent authority in question of which revenues, among the revenues from non-audit services, were generated from the assurance of sustainability reporting.

5. Assurance Standards

The Proposal requires a limited assurance engagement be performed in regard to sustainability reporting and also amends the Audit Directive adding Article 26a: “Assurance standards for sustainability reporting” to prescribe that where the EU Commission adopts standards for reasonable assurance, the opinion referred to in Article 34(1), second subparagraph, point (aa) of Directive 2013/34/EU shall be based on a reasonable assurance engagement.”

As explained above, we agree that reasonable assurance must be the EU Commission’s goal, in order to serve the public interest.

The preamble to the Proposal refers to the absence of a commonly agreed standard for the assurance of sustainability reporting, suggesting that this creates the risk of different understandings and expectations of what a reasonable assurance engagement would consist of for different categories of sustainability information, especially with regard to forward looking and qualitative disclosures.

However, there is already an international, commonly agreed-upon standard currently being applied worldwide for sustainability reporting for both limited and reasonable assurance engagements – ISAE 3000 (Revised) *Assurance Engagements other than Audits or Reviews of Historical Financial Information*. The recent publication by IFAC in cooperation with the AICPA and CIMA: “The State of Play in Sustainability Assurance” mentioned above also provides an insight as to the current use of assurance standards within four of the larger EU Member States, indicating that ISAE 3000 is widely used in these four European

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Member States³. ISAE 3000 (Revised) is now supported by additional guidance recently issued by the IAASB (Extended External Reporting (EER) Assurance Non-authoritative Guidance). Since limited assurance is conceptually more challenging than reasonable assurance (which is why ISAE 3000 (Revised) provides considerably more guidance on limited rather than reasonable assurance), we do not understand how the Proposal can assert that the lack of a standard for reasonable assurance (which is not true, as noted above) means that practitioners would be able to perform a limited assurance engagement without a standard (which is also not true, as noted above). We do not believe that fragmentation in the assurance and audit market globally is helpful and therefore would not support the EU prescribing an EU-only assurance standard, as we do not envisage that this would be specifically needed to address the “mechanics” of assurance engagements on EU reporting elements that go beyond a core global sustainability reporting base. Instead, we believe the EU Commission should clarify the scope and underlying matter subject to the assurance engagement as explained in point no. 2 above.

The preamble also suggests that a progressive approach should be considered to enhance the level of the assurance required for sustainability information starting with an auditor’s opinion about the compliance of the sustainability reporting with EU requirements based on a limited assurance engagement. It goes on to say that “this opinion should cover the compliance of the sustainability reporting with Union sustainability reporting standards, the process carried out by the undertaking to identify the information reported pursuant to the sustainability reporting standards and compliance with the requirement to mark-up sustainability reporting....”.

The argument regarding the consideration of a progressive approach to assurance is unconvincing, as it lacks substance in claiming that limited assurance is possible (in practice ISAE 3000 (Revised) has become generally accepted as the assurance standard for limited assurance engagements relating to NFI) whereas reasonable assurance is not due to a supposed lack of (this same) standard. Certainly, a limited assurance engagement is likely to be of less value to users of corporate reporting for the reasons discussed above and so can only be an interim solution for a short period of time.

We also note that the progressive approach refers to limited assurance allowing “for the *progressive development* of the assurance market for sustainability information, *and of undertaking’s reporting practices*”. This suggests that reporting practices need not be as well-developed for limited assurance

³ See page 18: [IFAC-Benchmarking-Global-Practice-Sustainability-Assurance \(1\).pdf](#)

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engagements as for reasonable assurance engagements. This is a fallacy because the reporting practices need to be equally well-developed as a prerequisite for both limited and reasonable assurance engagements: if the reporting criteria are unsuitable, the underlying subject matter being assured is not appropriate, or the evidence used to prepare the CSR reports is not sufficient and appropriate (including due to less mature systems of internal control), then neither limited nor reasonable assurance is possible. The reason for this is because, regardless of the level of assurance desired, once an assurance practitioner obtains evidence that the CSR report may be materially misstated, the practitioner must, and needs to be able to, “dig deeper” to determine whether the CSR report is in fact materially misstated or not. Regardless of the level of assurance desired, assurance practitioners cannot simply choose not to “dig deeper” when necessary, as this would constitute a self-imposed scope limitation, which auditing and assurance standards (including ISAE 3000 (Revised)) worldwide do not allow. Consequently, the basis for reporting (that is, the evidence obtained by preparers to prepare the report) and hence the reporting quality must be equally adequate for both limited and reasonable assurance engagements.

We would also like to inform the EU Commission that with the German Assurance Standard: *IDW Assurance Standard 350 (Revised) “Assurance on the Management Report as part of the Financial Statement Audit”*, which complies with and goes beyond ISAE 3000 (Revised), the German profession has a standard explicitly tailored to reasonable assurance of non-financial information in the German management report. The IDW is currently considering which further material may be necessary to address changes expected from the Proposal. In our opinion, a (new) European-only assurance standard specifically for sustainability reporting is neither needed nor appropriate.

In this context, we would support the EU Commission clarifying that it would not be responsible for establishing an endorsement process for assurance standards relating to the assurance of sustainability reporting, in regard to assurance standards that have been developed by recognized national or international standard setters on the basis of a generally recognized and accepted due process, but instead restrict its own responsibility to determining the matters subject to assurance engagements on sustainability reporting in the EU, and adoption of the international standards. (IAASB’s ISAE 3000 (Revised) in conjunction with EER pronouncement mentioned above), mirroring the approach envisaged for the international standards on auditing (ISAs), i.e., by establishing an adoption process for the IAASB’s international standards.

6. ESEF requirements

The IDW supports the EU's digital agenda and hence the transfer of sustainability information into a digital reporting form. Since Germany is one of the few Member States that did not exercise the Member State option to postpone the application of the ESEF, based on our recent experiences in the application of the ESEF Regulation, we would like to point out one important matter:

Article 19d to Directive 2013/34/EU of the Proposal requires an entity's financial statements and management report (including sustainability reporting) to be *prepared* in a single electronic reporting format (ESEF). **The XHTML and iXBRL formats are not suitable for preparation of the financial statements and management report or the audit thereof, since under both the EU Accounting Directive and IFRS as adopted in the EU, the financial statements must present a true and fair view, which neither XHTML nor iXBRL can do since the former has no fixed presentation (the presentation varies depending upon the software and devices used) and the latter has no presentation at all (it is only tagging used to manipulate the numbers through automation). Furthermore, neither XHTML nor iXBRL can be used for preparation of the financial statements or their audit because neither format can be used as a basis for electronic signatures, since opening the files results in invalid signatures (which also precludes using XHTML for legally required archiving).** Consequently, when transposing Article 4 para. 7 subpara. 1 of the Transparency Directive into German law, the German legislator correctly chose to not require the financial statements and management report to be *prepared* in XHTML (and iXBRL for consolidated financial statements and group management reports). This implies that the financial statements to be adopted or approved by management and those charged with governance must continue to be prepared (and audited) in a format associated with a specified presentation (either on paper or a fixed format like pdf). Only for publication purposes must reproductions of these financial statements and the associated management reports be prepared in XHTML format and, for consolidated financial statements and group management reports, iXBRL. Auditors obtain assurance on only the appropriate reproduction of the audited financial statements and assured management report in XHTML and iXBRL.

We strongly recommend that final changes to the Directives not refer to the financial statements and sustainability or other reports of the companies concerned having to be prepared in XHTML and iXBRL format, but instead

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recognise that these must (continue to) be prepared in the traditional format (i.e., as paper or PDF-based versions), which then have to be converted to XHTML and iXBRL solely for the purpose of publication. In addition, since the ESEF Regulation, and hence German law, only require the publication of the ESEF reproductions of the audited financial statements and (in Germany, assured) management report, this means that users no longer have access to the actual audited financial statements and the approved management report. We therefore strongly recommend that the European legislator and Commission consider requiring the publication of the audited financial statements and the management report in addition to the publication of these in ESEF Format.

We would also like to point out that many parent companies that fall within the scope of Article 19d of the Draft Accounting Directive, also fall within the scope of the Transparency Directive or the ESEF Regulation. Such entities thus fall under two different sets of regulations, which is not appropriate. We therefore urge the EU Commission to remedy this by specifically excluding (domestic) issuers from the scope of Article 19d of the Accounting Directive.

We also note that a sustainability reporting taxonomy has yet to be developed in accordance with the ESEF Regulation - i.e., using iXBRL technology – as in the Proposal for a CSRD at least according to para. 1 for individual company sustainability reporting; differently in para. 2 for consolidated sustainability reporting, where a reference to the ESEF Regulation is missing.

7. Auditor reporting responsibilities

The Proposal would update the references to provisions of the Accounting Directive and Directive 2006/43/EC (the Audit Directive) as regards the requirement to audit financial statements in accordance with Article 34(1) of the Accounting Directive, and to state whether the auditor or audit firm has identified material misstatements in the management report, and as regards the requirement to disclose the audit report, including the opinion on the assurance of sustainability reporting.

There is some confusion as to this aspect, as the text underlined relates to reasonable assurance, rather than a limited assurance engagement.

8. Consideration of supply chain legislation and related reporting implications

In the absence of final sustainability reporting standards, it is difficult to anticipate and comment on potential practical and legal challenges. Should supply chain information be required as part of sustainability reporting, there are certain issues that we would like to flag in regard to assurance engagements.

Firstly, unlike the situation in which a group prepares consolidated financial statements and the group management will have full access to financial information of group entities that are controlled by the parent company (control implies access can be demanded), an entity will generally not have such control over supply chain “partners” and therefore will not be able to demand full access to information they need to comply with (future) EU sustainability reporting requirements. Thus, there may also be limited or no possibility for the reporting entity to exercise control over the quality of information forthcoming from its supply chain “partners”.

Similarly, unlike a group audit situation where the group auditor may request and use work performed by other auditors (component auditors under ISA 600 (Revised)) there may be little ability for the reporting entity’s auditor or assurance provider to be involved in assurance of sustainability related information from supply chain “partners”. Consequently, the current model of “group auditor involvement” in the work of component auditors for audits of group financial statements may not be feasible when dealing with assurance practitioners of entities in the supply chain outside of the corporate group. In addition, when the assurance on sustainability reporting in these circumstances is part of the statutory audit, this also raises issues with respect to the application of the independence considerations in EU law currently applied to component auditors to assurance providers engaged by supply chain “partners”.

To our knowledge these issues have yet to be fully addressed, so our intent was merely to flag these factors for due consideration.