



21 October 2022

Mr Serdar Celik
Acting Head of the Corporate Governance and Corporate Finance Division
Organisation for Economic Cooperation and Development (OECD)

Via email to: CorporateGovernance&CorporateFinance@oecd.org

Comments on proposed review of the *G20/OECD Principles of Corporate Governance*

Dear Mr Celik,

On behalf of the members of the Global Public Policy Committee (GPPC), I am pleased to submit the attached paper in response to the OECD's Public Consultation on the Review of the G20/OECD Principles of Corporate Governance (G20/OECD Principles or Principles). The GPPC comprises representatives of the six largest global audit and accounting networks¹ who meet to discuss public policy and capital markets issues of relevance to investors, our profession and the wider public interest.

The GPPC strongly believes that strong corporate governance contributes to well-functioning capital markets, robust and reliable corporate reporting, and higher quality audit and assurance. In light of rapidly changing expectations on companies from the society at large and evolving reporting requirements for corporates on sustainability and ESG-related matters, a revised and sound framework for corporate governance can help companies recognize and respond to the respective interests of shareholders and other stakeholders necessary for such companies to succeed in the long term.

We are supportive of the OECD's overall aims for this review and agree that the topics covered in it are the pertinent ones. We are glad to have the opportunity to share the GPPC's views with the OECD Corporate Governance Committee and Secretariat.

We would be happy to answer any questions you may have and to discuss our response to the consultation further. Please contact Andrew Hobbs for that purpose: Email ahobbs@uk.ey.com Tel: +44 20 7951 5485.

Yours sincerely,

Stephen Allis
Chair, GPPC
KPMG International

¹ BDO International, Deloitte, EY, Grant Thornton, KPMG International, and PwC.



Attachment:

Corporate governance in the light of sustainability and ESG: a view from the global accounting profession

Corporate governance in the light of sustainability and ESG: a view from the global audit and accounting profession

October 2022

Based on our analysis of the consultation document, we have identified 10 key themes for consideration by OECD as it finalizes its review. They are as follows:

1. Integrate sustainability in the entire document/Principles
2. Apply the stakeholder approach
3. Emphasize the importance of the role of risk management and internal control systems
4. Link remuneration and sustainability
5. Promote the alignment of ESG rating information with sustainability disclosures based on international standards
6. Clarify the role of the external auditor
7. Focus on sustainability assurance
8. Enhance guidance on the role and responsibilities of the board as it broadens with sustainability
9. Chapter VI *Sustainability and resilience* – comments on the new section
10. Definitions/language/clarity of guidance

More detailed comments have been included in an appendix to this letter. They include more detailed comments on the new chapter VI on *Sustainability and resilience* and the definitions, language and clarity of the guidance provided in the Principles.

1. Integrate sustainability in the entire document/Principles as far as possible

Although sustainability is included in the updated Principles as a separate chapter, greater steps could be taken to fully integrate the long-term value creation approach (including sustainability) into the Principles or at least to create explicit cross reference to chapter VI in the other sections. Chapters I to V remain very focused on a *shareholder-only* approach rather than a *stakeholder* approach. In many places terms like economical, wealth and financial prevail over a broader purpose and strategy that is focused on long-term value creation.

2. Apply the stakeholder approach

The draft updated Principles also tend to still focus on the *shareholder* approach (i.e., investor focused approach) instead of the *wider stakeholder* approach. A company that takes account of stakeholder interests may be better able to attract and retain a productive workforce, get support from the communities in which it operates, and win more loyal customers. We believe that long-term value is created by focusing on a broad set of stakeholders, including when defining organizational purpose, strategy and measuring and reporting value. It also involves finding out what sustainability aspects matter most to an entity's stakeholders and ensuring those are reflected when defining the above. We suggest that a company that takes account of all their stakeholder interests will be much



more likely to create long-term value for their shareholders. In other words, how could a company maximize shareholder returns/profits if they are ignoring their employees, customers, suppliers and the communities in which they live, work and operate.

Linked to this, we would have expected to see the *concept of trust* explored in the introduction to the Principles. A move away from the shareholder-only approach to a multi-stakeholder approach is driven by changing expectations of business by society. A company's licence to operate is dependent on trust and if societal expectations are not met, trust is lost. And when trust is lost, companies will struggle to be successful in the long term.

3. Emphasize the importance of the role of risk management and internal control systems

Corporate reporting no longer focuses solely on financial performance but on a broad spectrum of corporate information. As a result, the underlying system that allows the company to identify, manage and control a company's risks, and that supports the integrity of disclosed information, needs to evolve to cover this broad scope. Accordingly, the role and responsibilities of those charged with governance – management, board and audit committee (where applicable) – expand significantly. In that regard we recommend to include, as a good practice, to assess the effectiveness of the risk management and internal control systems by management and overseen by the board. Hence, risk management and internal control systems and the accountability thereover needs to evolve to support those charged with governance.

Accordingly, the Principles could place more emphasis on the role of risk management and internal control as a crucial system to support management, the board, and audit committees (where applicable) as well as its stakeholders. See for example Sections IV.A.8 and V.D.2/3:

- Section V.D.2 on Reviewing and assessing risk management policies and procedures: We recommend updating the wording to explicitly refer to internal control (i.e., risk management *and internal control* system (RMICS)). Such a concept should be consistently applied throughout the Principles.
- Section V.D.2 – In addition, we understand the desire to mention some specific risk types but recommend doing so in a separate section V.D 2a/b/c etc. We recommend first focusing on the RMICS as a whole and then addressing specific topics separately.
- Section V.E.2 relates to boards setting up specialized committees, includes internal controls. We recommend it also explicitly refers to *risk management*.
- Section VI.C. "*Boards should ensure that governance practices, strategy and risk management policies adequately consider material sustainability risks and opportunities, including climate-related physical and transition risks*": This should be integrated into the overall risk management and internal control system. In addition, this guidance should not just focus on risk management policies but on the entire risk management and internal control *system*.

4. Link remuneration and sustainability

Having the right remuneration in place supports the company, its management and board to achieve its strategic objectives. Sections IV.A.5, V.D.4 and V.D.5. focus on this topic:



- Section V.D.4 focuses on the nomination committee – This promotes a rather “reactive” role for the nomination committee i.e., initiated only when a board member or management resigns. Active management of succession planning and skills/experience needs is vital for companies in the modern world. We recommend that the Principles reflect a more proactive role, also including active talent management and assessing needs of board now, next and long term plus managing board composition accordingly.
- Section V.D.5 focuses on remuneration – We recommend that Key Performance Indicators (KPIs) should not solely be financial but tied to the long-term value of the company across different forms of capital, e.g., human capital (i.e., training provided, diversity in executive teams which helps drive performance and long-term value).



5. Promote the alignment of ESG rating information with sustainability disclosures based on international standards

ESG rating plays an important role when evaluating the sustainability, and the underlying ESG performance, of a company. The Principles refer to ESG ratings (e.g., in Section III.D.). We note that disparity exists between the different rating applied by the rating agency and how an overall governance system encourages transparency (i.e., differences between the raters). As a result, ESG ratings may be based on different information than the information required based on sustainability standards. We strongly recommend clarifying this in the Principles to address if and how ESG ratings are compliant with the taxonomies. In addition III.D seems to have the presumption that all entities providing analysis or advice relevant to the decisions by investor (e.g., proxy advisors, ESG and credit rating agencies etc.) are regulated, however we do not believe that is the case globally.

6. Clarify the role of the external auditor

We are supportive of the overall way the role of the external auditor is articulated in the Principles. We also have the following observations:

- We recommend to more explicitly and holistically including the role of the external auditor in the corporate governance framework (corporate governance triangle: stakeholder-company-external auditor). The current references to the auditor are overly output and process focused and could better explain the relevance and added value of the auditor.
- Audit results and outcomes – the output of external audit goes beyond a true and fair view of the accounts and includes:
 - Key audit matters and the role of the company and its board in relation to these matters
 - Observations and recommendations on internal control in management letters/board reports from the external auditor
 - Role of the auditor in relation to the board/directors' report (ISA 720) which is in particular relevant given the integration of sustainability in the OECD Principles
 - Section IV.D. "Shareholders and external auditors should also have the possibility to communicate directly on the findings of the annual audit.": We understand the reasoning of adding this to the guidance however in practice this may be impossible, e.g., management letter findings and recommendations are often considered confidential to the audited company

It would be helpful to refer to these elements in the Principles.

7. Focus on sustainability assurance

If the Principles are designed to be future-proof, assurance over sustainability reporting should also be included in the guidance. Mandatory assurance is on the horizon, as for example stipulated by the future EU Corporate Sustainability Reporting Directive. The Principles should explain at least that legislators are increasingly seeking to mandate assurance over other corporate reporting whether that assurance is performed by the financial statement auditor or another independent and qualified provider. In addition, we observe a increase in voluntary assurance on sustainability information across the globe. Stakeholders are increasingly expecting validated information. Good governance should recommend an evaluation of the need for assurance regardless of regulatory circumstances. We also refer to our comments on the new chapter VI. in section 9 of this letter.



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In addition, we would make the following comments:

- Section VI.A.5 - Sustainability assurance: We recommend referring to the possibility of different levels of assurance in this context. For example, starting with limited assurance over sustainability reporting and moving to reasonable assurance (higher level of assurance) at a later stage. This is the approach adopted by the European Union and the SEC. Next to regulatory requirements we believe that the expectations of stakeholders and the risk of the subject matter are important, and companies may need to accelerate the assurance over sustainability information beyond the local and international regulatory requirements. In addition, we emphasize the importance of creating a level regulatory playing field for assurance - i.e., it is important that an assurance provider have experience in measuring, analyzing, reporting or attesting and that standards of transparency, capability, and independence are met to ensure the reliability of the results.
- Section V.D.8: We recommend including how to use internal independent assurance or even external assurance to ensure the integrity of the company's accounting and reporting systems for financial and sustainability disclosure.
- Section V.D.8/9: We believe it would be useful for the Principles to recommend consideration of including personal accountability for accurate corporate reporting and the monitoring, testing and reporting on internal controls structures as can be found in markets like Japan, Italy, South Africa and the USA.

8. Enhance guidance on the role and responsibilities of the board as it broadens with sustainability

As the role and responsibilities of the board evolves and broadens, we would note the following:

- Chapter V should include provisions on accountability, enforcement and consequence management.
- We recommend including guidance on how the board can make sustainability part of the board strategy and board duties. This should include the need to review expertise, experience and mindset of the board members. We note that the provisions on succession planning and board composition could be a lot more actively written and would also benefit from guidance relating to talent management, assessing the needs of the current and future boards including board composition.
- With the focus on sustainability and the related disclosures additional responsibilities for the board and in particular the audit committee will come. We recommend providing guidance for the board and its audit committee specifically in relation to the reporting process and internal controls. This would include the following:
 - Reporting process: Audit committees should monitor the sustainability reporting process, including the digital reporting process, and the process carried out by the company to identify the information reported under the relevant sustainability reporting standards.
 - Internal controls: Audit committees should monitor the effectiveness of the company's risk management and internal control systems and, where applicable, its internal audit function with a view to enhanced reporting and external assurance requirements



9. Chapter VI *Sustainability and resilience* – comments on the new chapter

We welcome that the draft revisions and the new Chapter VI *on Sustainability and resilience* address the important topic of sustainability. We have the following observations and recommendations:

- Chapter VI *“The corporate governance framework should provide incentives for companies and their investors to make financing and investment decisions, as well as to manage their risks, in a way that contributes to the sustainability and resilience of the corporation.”*:
 - This could be read that OECD is interested in ‘outside in’ effects and not so much ‘inside out’ although this is indirectly mentioned in VI.A.1 (i.e., the corporation’s impact on environment and society) which in the longer term will also affect sustainability/resilience of the company.
 - We strongly recommend also using the term “long-term value creation” where relevant – the ‘umbrella’ term of sustainability
- Chapter VI, para. 1, sentence 1 *“Companies play a central role in our economies by creating jobs, contributing to innovation, generating wealth, and providing essential goods and services.”*: We recommend including text to note that companies have a societal impact on sustainability matters. It has become obvious that companies should not only be focusing on shareholder value but shift to a focus on stakeholder value as part of which a positive contribution to our planet and societies is key.
- Chapter VI, para. 1, sentence 4 *“A sound corporate governance framework would allow investors.”*: We recommend changing the term “investors” to “stakeholders”.
- Chapter VI, para. 2, sentence 3 *“A core feature of these disclosures is to provide investors with a better understanding of the governance and management structures and processes for managing climate risks.”*: We recommend focusing on all material sustainability risks, not just climate.
- Chapter VI, para. 2, sentence 5 *“The combination of sound governance and clear disclosures will promote fair markets and the efficient allocation of capital, while supporting companies’ long-term growth.”*: We recommend replacing the term *growth* by *value creation for all company’s stakeholders*.
- Chapter VI, para. 4, sentence 1-2 *“In jurisdictions that allow for or require the consideration of stakeholders’ interests, companies should still consider the financial interests of their shareholders. A profitable company provides jobs for its employees and creates wealth for investors, many of whom are part of the general public and have invested their retirement savings.”*: We recommend updating this to focus more on sustainability and a positive contribution to value creation for the stakeholders that in turn compliments the entity’s sustainability and opportunity for financial success (rather than safeguarding retirement plans).
- Chapter VI, para. 5 *“Corporate directors cannot be expected to be responsible for resolving major environmental and societal challenges stemming from their duties alone. On the one hand, a narrow view of directors’ fiduciary duties as a simple obligation to maximize short-term profits may have detrimental effects, for example on the corporate sector’s long-term performance. On the other hand, an opposite approach also presents risks. If directors in all companies are required to equally balance shareholders’ financial interests with the interests of all stakeholders and, in addition, to fulfil a number of specific public interest missions, the corporate sector could become less efficient in allocating resources. To guide corporate activities, policies that make companies internalise environmental and social externalities as well as set predictable boundaries within which directors have to exercise their fiduciary duties are relevant. These policies could relate to, for instance, environmental regulation, or directly investing in or incentivising research and development of technologies that may contribute to addressing major environmental*



challenges.”: This section should more properly consider the externalities but also the corporation’s impact on environment and society the costs of which are not fully borne yet by the company. We recommend reviewing this section accordingly.

- Section VI.A. *“Sustainability disclosure should be consistent, comparable and reliable, and include retrospective and forward-looking material information that a reasonable investor would consider important in making an investment or voting decision.”*

We recommend updating this principle explicitly to reflect the interests of investors and separately to the interests of other stakeholders, including employees and customers, in terms of what information may be considered material. This concept could be reflected throughout this Principle including its sub-paragraphs.

- Section VI.A.1. Materiality: We strongly believe it is necessary to refer to the option of a ‘double materiality’ concept in this context. This concept describes how corporate information can be important both for its implications about a company’s financial value, and about a company’s impact on the world at large. We strongly suggest referring to the double materiality concept here and what it means for the company and its stakeholders (we do acknowledge that this concept is not (yet) recognized by all regulators).
- Section VI.A.4. *“If a company publicly sets a sustainability-related goal or target, the disclosure framework should ensure that verifiable metrics are disclosed to allow investors to assess the credibility and progress toward meeting the announced goal or target.”*

We believe that a link to remuneration and remuneration policies should be added here. See also our comments above on section VI.A which apply equally here.

- Section VI.C.1. *“Boards should ensure that companies’ lobbying activities are coherent with their sustainability-related commitments”.*
We recommend referring to the Social and Governance of ESG here as lobbying relates to those factors. In addition, we recommend adding references to alignment with corporate values and strong ethical principles as it is unclear why this should be limited only to sustainability.
- Section VI.D. We recommend replacing *“wealth”* with *“value”*.

10. Definitions/language/clarity of guidance

We believe there are opportunities to clarify the text in places and sharpen definitions to aid user understanding. To this extent we make the following observations:

- We recommend using the term *‘sustainability’* consistently throughout the Principles. We noted different terminology at certain instances, e.g., ‘ESG’, ‘Non-financial information’ both of which risk introducing nuances into the Principles which may not be helpful to the overall objectives of the OECD. It would be helpful to clarify that the ‘sustainability’ concept goes beyond climate include pollution, biodiversity, and social and governance related topics: among other things. In addition, we recommend avoiding the term *“non-financial information”* as it may be misleading. Information that is material to assessment of company’s value creation may well become financially relevant in the future even if quantification is not included in the current reporting period.
- Wording of the Principles could be enhanced by using more direct wording and or including recommendations as good practices rather than just stating what some jurisdictions have in place.
 - Examples: II.G. *“some jurisdictions place limitations on certain structures of company groups such as cross-shareholdings”*. And also, III and III.A. *“Many jurisdictions, as a complementary governance tool, countries have begun to consider adoption of adopted codes on shareholder engagement (“stewardship codes)”*.



We do not fully understand what the added value/relevance is of including “some or many jurisdictions”. If this means that practices in some jurisdictions are considered good practice than include as much, the current wording could be enhanced to understand whether that some regions do it (and thus others not) is good corporate governance (or not). For example, the guidance on III.B is clear and direct, we recommend rewriting the other guidance in a similar manner.

- Consistency – It is important for clarity to be consistent with terms used throughout the Principles. For example, the Principles use the terms “*compensation*” and “*remuneration*” seemingly interchangeably.
- Focus on positives/opportunities - I.H. the role of regulatory frameworks to ensure effective oversight – the guidance under this Principle has a negative focus on risks. We recommend amending the wording to focus on how the Principles support companies to do the right thing and seize opportunities rather than focus solely the negatives



Appendix – Detailed comments and observations per section (where relevant)

On Integrate sustainability in the entire document/Principles (No. 1)

To illustrate our observation on integrating sustainability in the entire document/Principles, we include the following examples:

- About the Principles 3. “Achievement of broader *economic* objectives”.
We recommend also including sustainability objectives
- About the Principles 5. “...share in corporate *wealth creation*”.
We recommend referring to “*long-term value creation*” rather than corporate wealth creation. In addition, we recommend including a definition for long-term value creation, for example: “Long-term value is created by focusing on a broad set of stakeholders, with a distinct purpose in mind, to sustain a business for the long-term.”
- Section I.C. “legal domains impacting corporate governance requirements.”
The guidance under this Principle could also usefully cover topics such as, environmental law, health and safety.
- Chapter IV. Disclosure and transparency
 - “*Material information can be defined as information whose omission or misstatement can reasonably be expected to influence an investor’s assessment of a company’s value and likely future cashflows. This would typically include the company’s own assessment of the value, timing and certainty of its future cash flows.*”
We recommend better linking this section with section VI. Materiality can be about more than enterprise value in some markets and corporate reporting is broader than reporting on financial (cash flow) performance only.
 - “*While corporate disclosure should focus on what is material to investors’ investment decisions and may include an assessment of a company’s value, it may also help improve public understanding of the structure and activities of companies, corporate policies and performance with respect to environmental and social and governance matters*”.
We disagree with the guidance that disclosures should focus on what is material only to investors investment decisions”. We recommend emphasizing that the disclosures should be about corporate reporting – the full spectrum of company performance to all stakeholders that drives long-term value creation.
 - Section IV.A.2. “*Company objectives and sustainability information*” .
We recommend integrating this guidance with the financial guidance and not just refer to chapter VI as the current presentation creates an imbalance between financial and sustainability information and may encourage a separation from financial information which should be avoided given the context of long-term value creation.
 - Section IV.A.8. Foreseeable risk factors – “*Users of financial information*”
The focus of this guidance is narrow. We recommend using the term corporate information instead. Also, the risks included could be taken to include only the E of ESG (Environmental, Social and Governance). However, all material sustainability risks are relevant here and merit inclusion.
 - Section IV.B. – “*Information should be prepared and disclosed in accordance with high quality accounting and disclosure standards*” . We recommend adding the following sentence at the end: “Disclosure of sustainability information should also be understandable, enforceable and consistent and compatible with high quality and



generally accepted disclosure standards.”

We recommend the guidance to fully integrate financial and sustainability information as follows: “Corporate information should be prepared and disclosed using high quality standards including standards for financial and sustainability reporting”.

- Section V.D – “key functions the board should fulfil.”

We strongly recommend including a sustainability element for the strategy amongst these responsibilities (e.g., climate impact, social matters etc.) and also overseeing both financial and sustainability operations.

On Apply the stakeholder approach (No. 2)

To illustrate our observation on integrating sustainability in the entire document/Principles, we include the following example:

- Principle I.A. “The corporate governance framework should be developed with a view to its impact on corporate access to *finance*, overall *economic* performance...”.
This Principle and underlying explanation focus heavily on the financial, economic and efficiency aspects. It is unclear to us why there is no reference in this provision and the underlying explanation to sustainability and the interests of stakeholders beyond shareholders. We recommend including the stakeholder approach and sustainability performance more explicitly in this Principle and more broadly through the other Principles.

On Emphasize the importance of the role of risk management and internal control systems (No. 3)

Detailed comments on risk management and internal control systems

- Section V.D.2 “To support the board in its oversight of risk management, some companies have established a risk committee and/or expanded the role of the audit committee, following regulatory requirements or recommendations on risk management and the evolution of the nature of risks.”
We challenge the value of this statement in its current form – as worded it may be easily disregarded by the intended audience. We recommend rewording it to become more of a recommendation by using some parameters that justify or require risk and/or audit committees to support the board in its oversight role.
- Section V.D.3 “Monitoring the effectiveness of the company’s governance practices and making changes as needed.”
We do not understand what this means and what it intends to include or exclude. We recommend revisiting the wording. We believe that the issue of this section is the alternating between “company” and “board.” If this is getting at the board’s self-evaluation of its structure and effectiveness, then any reference to similar effectiveness or structures within the company should be included. If the intent is to oversee company structure, then omit board references. Or make them two separate objectives.

On Enhance guidance on the role and responsibilities of the board as it broadens with sustainability (No. 8)

Detailed comments on the role of the board in relation to sustainability

- Section V.A “*Board members should act on a fully informed basis, in good faith, with due diligence and care, and in the best interest of the company and the shareholders, taking into account the interests of the company’s key stakeholders.*”
We recommend including wording that essentially defines “key” by encouraging boards to focus on the interests of those of the company’s stakeholders who are directly material to the company’s strategic success.



- Section V.A. – the last part of this guidance is not clear, we suggest updating the text as follows:
“boards should consider the interests of stakeholders, notably when making business decisions in the interest of the company’s long-term success and performance. This may help companies, for example, to attract productive employees, to be supported by the communities in which they operate, and to have more loyal customers, thus creating value for their stakeholders.”



On Definitions/language/clarity of guidance (No. 10)

Detailed comment:

- Chapter IV. Disclosure and transparency – *“Disclosure requirement should not place unreasonable administrative or cost burdens on companies”*.

It would be helpful to clarify what “unreasonable” may mean. We recommend including wording around the balance between the need of the stakeholders of the company and the burden on the company. For example, not placing costs or burdens unless the benefits exceed the costs or there is otherwise a public interest in imposing them.