

Assuring Integrated Reports – A Double-edged Sword?

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In Johannesburg this week, the first of a series of forums was held to discuss whether assurance of integrated reports is necessary and what are the benefits and challenges. The key issues to be addressed at this and future forums planned around the globe¹ are the nature of assurance, how different approaches build credibility and trust, and particular challenges that integrated reports will present to assurance providers (including materiality, reporting boundary and of information).

A new approach to accountability?

Integrated reporting presents both exciting opportunities and significant potential challenges. Integrated reporting is not just sticking your sustainability report and your financial report inside the one cover. It is truly attempting to connect the dots between a company's financial and ESG performance, and articulate how a company's management of those aspects adds value for the business and its investors.

Integrated reports account for value changes within a business over a set period of time, typically a financial or calendar year. At the start of the period the business ascribes value(s) to its key assets (called capitals) that it uses or influences. The business' management model is the means through which it transforms value in those capitals over time. This value transformation depends on how the business senses, understands and responds to a range of internal and external factors, which are disclosed in their integrated report.

The potential for integrated reporting to transform and even replace traditional financial reporting is significant. It responds to the one dimensional, short term, backward-looking disclosures that plague financial reports and limit informed decision-making. It also creates opportunities to transform business thinking around strategy and accountability.

Yet, by its nature, integrated reporting presents some fundamental challenges to reporters and users of the report alike. An organisation can identify and evaluate changes in the value of its assets over time, but how does it know (or demonstrate) that its own management of those assets has in fact enhanced or influenced their value? Can it truly connect the dots in readers' minds about where it adds value to its assets or has it just re-arranged the numbers used in its financial and sustainability reports? Can the business honestly claim to have successfully added significant value through careful and integrated management, or did it just get lucky and have a good year? Clearly and unambiguously accounting for such changes can challenge a company's credibility with its stakeholders.

But isn't this exactly where assurance can help? After all, assurance is primarily designed to bridge the gap between the reporter and the report user in terms of facilitating credibility for the report's content and, by extension, trust in the reporter. Yet the challenges facing reporters around integrated reports also face the assurers of those reports. They will be tasked with assuring the legitimacy of the claims made in integrated reports, particularly at a time when integrated reporting is still finding its way towards legitimacy in the broader market, and when appropriate fit-for-purpose assurance mechanisms are not yet fully in place.

¹ Other forums are being organised in Australia, Belgium, Brazil, Japan, Malaysia, Singapore and the US.

What are the biggest challenges around assuring integrated reports?

A number of these opportunities and challenges are raised in a new paper, '*Assurance on <IR>: an introduction to the discussion*'² released last month by the International Integrated Reporting Council (IIRC). It is complemented by a more detailed document, '*Assurance on <IR>: an exploration of issues*'³ recently produced by the IIRC's Assurance Technical Collaboration Group (IIRC TCG).

In reviewing these documents I believe that some statements and assumptions warrant particularly close attention and thoughtful consideration at the proposed forums, such as:

"The availability of suitably skilled and experienced practitioners."

This would rank pretty well up amongst my top concerns, as the quality of the assurance practitioner is just as important as the robustness of the methodology.

The integrated reporting framework is a principles-based approach rather than a prescriptive formula for reporting, and it needs an assurance approach that reflects this fundamental characteristic. Rather than a 'tick and flick' auditing exercise, it will need trained auditors who can apply their knowledge and experience to examine not only the fundamental assertions being made, but the assessment of value transformations between different assets (or capitals) of the organisation.

We are in a classic conundrum with this one, as how do assurance practitioners acquire and demonstrate skills and experience with something so new and so ground-breaking as integrated reporting? And please don't let anyone tell you that they can easily transfer their skills and knowledge from assuring financial and sustainability reports. We are talking "chalk and cheese" differences here as some of the principles that are fundamental to integrated reporting have never collectively been encountered or addressed before in other forms of corporate reporting; value transformations, future orientation, connectivity of information (to name a few) are still largely untrodden ground for reporters and assurers alike.

"Unwarranted inconsistency or a lack of robustness in assurance processes can have the same effect as no assurance at all."

I have to say that I disagree with this view. Weak methodology or poorly undertaken assurance is, in fact, *significantly worse* than no assurance at all. Assurance is designed and sold as a confidence-instilling tool. External users of reports, as well as the internal stakeholders of the reporting entity, make the natural assumption that the assurance has delivered the necessary confidence in the assertions and data disclosed in the report – and they are often in no position to question the quality or integrity of the assurance process or provider.

Once a report has been stamped "Assured", it creates confidence. Inconsistent or weak assurance creates for all stakeholders a false sense of security and comfort that things are 'as wrote'. This creates significant risk for all those parties as a result. Lack of assurance is different – it simply says "buyer beware" to the report user, enabling stakeholders to form their own view as to the level of comfort or scepticism they have about the claims and information in the report.

"Some have suggested that, just as IR is a new approach to reporting, a new approach to assurance is needed, involving a rethink of tenets such as independence...."

This is spot on, in my view. There have always been significant stakeholder concerns about the independence of assurers and, in my view, these have become more acute in recent years with the

² <http://www.theiirc.org/wp-content/uploads/2014/07/Assurance-on-IR-an-introduction-to-the-discussion.pdf>

³ <http://www.theiirc.org/wp-content/uploads/2014/07/Assurance-on-IR-an-exploration-of-issues.pdf>

rise of sustainability reports and their assurance. I'm still amazed these days how some assurance providers blatantly profess independence in their assurance statements whilst another arm of their business has been consulting on, or even writing, those very same parts of the report they are assuring.

Integrated reporting is so new and so challenging for businesses to come to terms with, that there is little doubt that many will be seeking significant input and support from external consultants in developing their reports. Many large audit and accounting firms are already positioning themselves in the market to ride this next wave of reporting as a revenue source in these lean economic times. Will we see more of them both consulting on integrated reporting (or on any of the process and strategies that sit behind it) and then 'independently' assuring those integrated reports? I think there is significant potential that assurer 'independence' will be more strained than ever before in this pioneering area of accountability.

Why is it so important to get assurance right?

Done transparently, consistently and competently, assurance will help integrated reporting to take root in businesses. The future success of integrated reporting goes hand-in-hand with robust, reliable, value-adding assurance. In other words, assurance has the potential to contribute much to the realisation and acceptance of integrated reporting in the wider global market.

In addition to building external trust and transparency, assurance underpins internal confidence for the reporting entity. The very nature of integrated reporting makes company directors highly nervous about what they are prepared to sign their name to, so any assurance will not just have to satisfy external stakeholders' (i.e. investors') expectations, but sufficiently and successfully bridge the gap between principles and pragmatism to satisfy internal stakeholders too. Assurance offers the very confidence-building tool that company directors need to get comfortable with integrated reporting.

Having been a member of the IIRC TCG, I found a lot of good thinking being done around assuring integrated reports. One significant concern remains however - the ability of assurance to fulfil its fundamental intent of providing confidence that public claims made around value creation are real and evidence-based.