Mr Paul Druckman
Chief Executive Officer
The International Integrated Reporting Council
via email: assurance@theiirc.org

1 December 2014

Dear Paul

We are pleased to provide feedback on the paper *Assurance for <IR>* from an investor perspective.

About Regnan

Regnan – Governance Engagement & Research was established to investigate and address environmental, social, and corporate governance (ESG) related sources of risk and value for long-term shareholders in Australian companies.

Regnan's research is used in decisions made by institutional investors, and in directing the engagement and advocacy Regnan undertakes on behalf of 13 institutional investors with over $61bn invested in the S&P/ASX200 (representing more than 4% of index weight): Advance Asset Management; ACT Treasury; BT Investment Management; Catholic Super; Commonwealth Superannuation Corporation; Hermes; HESTA Super Fund; Local Government Super; NT Government and Public Authorities Superannuation Scheme; Vanguard (Australia); VicSuper; and the Victorian Funds Management Corporation.

Regnan participated in the Integrated Reporting <IR> investor network.

Introduction and Key Points

Assurance and assurance providers are not immune from the crisis of trust that has emerged from the global financial crisis. The *Assurance on <IR>* paper notes the potential for mechanisms other than external assurance to build credibility, such as sound leadership, robust internal systems, and the involvement of internal audit and stakeholders. We agree that there is a need for all of these mechanisms to be utilised to build credibility and trust in integrated reports. There should not be a sole or excessive reliance on external assurance, regardless of its scope or form.

Transparency about the application of these credibility mechanisms is also central to their effectiveness.

Regnan Governance Research
& Engagement Pty Ltd
ABN 93 125 320 041
AFSL 316351

Level 9, 387 George Street
Sydney NSW 2000
Australia

Phone +61 2 9299 6999
Fax +61 2 9299 6799
www.regnan.com

Integrated reporting practice is still in its infancy and, in our view, further innovation and evolution is needed to achieve <IR>'s aims. Seeking to detail assurance requirements at this stage may constrain innovation in both reporting and assurance and, thus, hamper the achievement of <IR>'s aims.

In our view, the focus in the near term should be on:

- **Leadership, in particular the role of those charged with governance** – both the board and audit committee. In particular, we consider that as part of the responsibility statement (s1.20 of the <IR> framework) those charged with governance should describe ***how*** they achieved comfort on the report's integrity. Such a statement would enhance credibility while continuing to provide sufficient flexibility on approach and would enable a conversation between the company and its investors and other stakeholders about the extent to which the approach meets user needs.
- **Supporting the development and entrenchment of quality** – standard setters through providing guidance (for example, developing minimum procedures in particular areas, such as completeness and materiality); academic institutions providing training; and firms dedicating senior time to audit judgements and communication of findings.

Integrated assurance presents a serious risk of widening the expectation gap - the difference between what the public and financial statement users believe auditors are responsible for and what auditors themselves believe their responsibilities are - given the scope of subject matter and the types of assertions involved. External assurance should not overreach its capability, nor should it oversell what has been done.

We note that this has often occurred in sustainability report assurance, with the result that the assurance is treated with scepticism by stakeholders. In our view, this has led to a vicious circle of stakeholders questioning the value of assurance, leading the reporting entity to question whether the cost is warranted and place downward pressure of fees and scope, leading to further narrowing of the assurance and further discounting by stakeholders - a race to the bottom to secure an assurance statement (any assurance statement) for the least possible cost. Shifting the focus of assurance from stakeholders at large to those charged with governance can put a stop to this cycle and help ensure assurance is meaningful and adds value for the business and for stakeholders.

In Regnan's experience there is little engagement by financial market participants in the detail of financial assurance. There is some understanding of its limits and a tendency to discount the value that it adds. This discounting tendency is compounded by the fact that financial assurance focusses on a report that contains little new information (lagging release of financial results) and, thus, small market sensitivity.[1]

[1] Studies which have addressed the market sensitivity of audited accounts are summarised in Ball, Ray, 'Accounting Informs Investors and Earnings Management is Rife: Two Questionable Beliefs' (May 15, 2013). *Accounting Horizons*. Available at SSRN: http://ssrn.com/abstract=2211288 or http://dx.doi.org/10.2139/ssrn.2211288

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In our view, this discounting is unjustified. Assurance of the key periodic report plays a critical role in 'confirming, and hence disciplining'[2] other disclosures to the market. The accuracy of preceding unaudited disclosures is tested and proved by their consistency with subsequent audited accounts. Further, assurance adds considerable value by testing the underlying systems and processes that produce both the audited statutory report and other financial disclosures.

We consider it unlikely that financial market participants will develop strong views on the details of assurance in isolation from examples in practice. Placing an emphasis on the role of the audit committee and board (those charged with governance), along with transparency in the responsibility statement (s1.20 of the <IR> framework) about the credibility mechanisms applied enables a conversation between investors and the board that will inform practice and result in superior approaches being rewarded. It is through such conversations that the expectation gap could be closed and greater understanding be built among investors of the value that external assurance adds.

Our response to each of the specific feedback questions is attached.

We thank you for the opportunity to provide our perspectives. Queries in relation to this matter can be addressed, in the first instance to, Alison George, ESG Engagement Manager alison.george@regnan.com.

Yours sincerely,

Amanda Wilson
Managing Director
Regnan - Governance Research and Engagement
www.regnan.com
+612 9299 6999

[2] Ibid, p4.

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Attachment 1: Response to Feedback Questions

Q1. What priority should be placed on assurance in the context of driving credibility and trust in <IR>?

Assurance and assurance providers are not immune from the crisis of trust that has emerged from the global financial crisis.

The *Assurance on <IR>* paper notes the potential for mechanisms other than external assurance to build credibility, such as sound leadership, robust internal systems, the involvement of internal audit and stakeholders. We agree that there is a need for all of these mechanisms to be utilised to build credibility. There should not be a sole or excessive reliance on external assurance, regardless of its scope or form.

Transparency about the application of these credibility mechanisms is also central to their effectiveness.

The final <IR> framework includes a requirement for a responsibility statement by those charged with governance (section 1.20). We consider that as part of the responsibility statement those charged with governance should describe ***how*** they achieved comfort on the report's integrity. The statement should be specific as to the mechanisms used, which may include external audit.

An example of such a statement is contained in Gold Fields South Africa's Integrated Annual Review 2012. Key aspects of Gold Field's 'credibility story':

- Board statement on the report (see p63) including that 'the Board approves the content of the Integrated Annual Review 2012, including the annual financial statements.'
- A specific audit committee responsibility for the integrity of the integrated annual review;
- An audit committee statement included in the integrated annual review recommending that the board adopt the report ***and going to the key processes they used to get comfort*** (see page 67);
- Three separate assurance statements, from the head of internal audit, from their AA1000 provider, and from the external (financial) auditor.[3]

Q2. What are the key features of assurance that will best suit the needs of users of integrated reports in years to come?

As noted above, we prefer the focus to be the role of those charged with governance and how they obtain comfort on the report's integrity, rather than on specific mechanisms for this. In our view, decisions on assurance (whether, what, who, to what extent) should rest with those charged with governance. This enables report users to reward those with superior assurance approaches,

[3] Available at https://www.goldfields.co.za/reports/annual_report_2012/pdf/integrated.pdf. We note Gold Fields' approach was revised in the 2013 IAR, although a statement of acknowledging board responsibility for the report was retained, at p61.

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whatever form these may take, and to apply pressure for improvement where practices do not meet user needs.

Integrated reporting practice is still in its infancy and, in our view, further innovation and evolution is needed to achieve <IR>'s aims. Seeking to detail assurance requirements at this stage may constrain innovation in both reporting and assurance and, thus, hamper the achievement of <IR>'s aims.

We consider reporting entities should not be unduly constrained in their choice of assurance provider, for example, to only utilising registered company auditors. We consider different auditors have different relative strengths and may assist reporters to improve different aspects of their reporting practice.

Where external assurance has been sought on the integrated report, we consider it appropriate that this be disclosed in the integrated report. As assurance practice with respect to 'extra-financial' disclosures varies a great deal, we consider minimum details should be provided about the assurance, including the qualifications of the auditor, scope, procedures and conclusions. This enables stakeholder scrutiny and feedback on assurance adequacy.

Q3. Is the availability of suitably skilled and experienced assurance practitioners a problem in your jurisdiction, and if so, what needs to be done, and by whom to remedy the situation?

We do not consider this to be a key problem. Most firms have developed multi-disciplinary teams for extra-financial assurance in response to client needs. We consider further evolution will occur as needed, for example, as greater connectivity between information sets evolves.

We acknowledge that integrated assurance, including communicating findings to internal and external audiences, will require a high level of professional judgement that implies greater application of senior time than other assurance engagements. This should be recognised by the firms and in any guidance provided on integrated assurance.

Q4. What needs to be done, and by whom, to ensure the quality of assurance on <IR> is maintained at a high level, including practitioners' adherence to suitable educational, ethical (including independence), quality control and performance standards?

We view supporting the development and entrenchment of quality in integrated assurance practice as critical. We see roles for a number of participants, in addition to the role of those charged with governance (the board and audit committee).

- Standard setters - through providing guidance (for example, developing minimum procedures in particular areas, such as completeness and connectivity),
- Academic institutions - in providing training, and
- Firms – in dedicating senior time to the development of practice and ensuring quality.

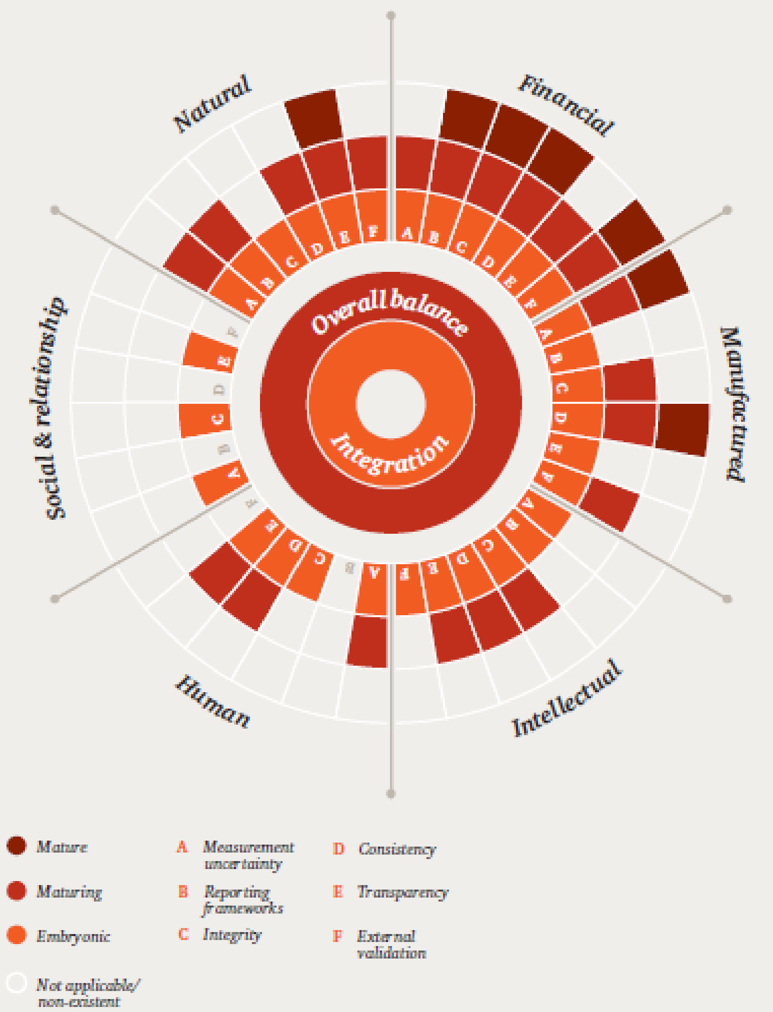
There is value in recognised and established financial assurance standard setters playing a leading role in relation to integrated assurance, to maintain consistency of language and approach and to benefit from the extensive experience of these bodies in developing guidance. Nonetheless, as noted above, we consider reporting entities should not be unduly constrained in their choice of assurance provider, for example, to only utilising registered company auditors. We consider different auditors have different relative strengths and may assist reporters to improve different aspects of their reporting practice.

Transparency on assurance and other credibility mechanisms employed by the reporting entity enables investors and other stakeholder to also play their part with respect to quality - rewarding those with superior assurance approaches, whatever form these may take, and applying pressure for improvement where practices do not meet user needs.

New approaches to transparency may be required. In this context we note with approval the maturity model proposed in PWC's paper *Inspiring Trust Through Insight*[4] (see figure right).

While this model is posed for communicating assurance ***findings***, we consider it adaptable to communicating assurance ***levels***.

Figure 4:
Insight into the maturity of an organisation's integrated reporting



[4] PriceWaterhouseCoopers (2014) available at http://www.pwc.com/gx/en/audit-services/publications/assets/trust-through-insight.pdf

Q5. Is the robustness of internal systems a problem, and if so what needs to be done, and by whom, to remedy the situation?

Experience with sustainability reporting would suggest that internal control over extra-financial information can be a concern. However, it is worth reflecting that, in the <IR> context, the information to be reported and assured is material to financial value. The information available to the business about these matters and the robustness of the systems and processes that create this information is central (or should be) to the operation of the business. Accordingly, if internal systems are not currently robust, the entity can be expected to benefit from improvements even more so than external report users.

Management, internal audit and the audit committee all have critical roles in developing robust systems for all key information. External assurance could provide a useful adjunct. We again note the value of novel approaches to communicating robustness of internal systems in different areas such as the PWC maturity model mentioned above. Such information could be used to inform conversations between investors and those charged with governance on expectations and practice.

Q6. Is assurance likely to be a cost effective mechanism to ensure credibility and trust over (a) the short/medium term; (b) the long term?

As noted above, we consider a range of mechanisms should be utilised to promote credibility and trust both over the short/medium and long terms. There should not be a sole or excessive reliance on external assurance, regardless of its scope or form.

Transparency about the application of external assurance and other credibility mechanisms is also central. Integrated assurance presents a serious risk of widening the expectation gap - the difference between what the public and financial statement users believe auditors are responsible for and what auditors themselves believe their responsibilities are - given the scope of subject matter and the types of assertions involved. External assurance should not overreach its capability, nor should it oversell what has been done.

We note that this has often occurred in the extra financial assurance space to now, with the result that the assurance is treated with scepticism by stakeholders. In our view, this has led to a vicious circle of stakeholders questioning the value of reporting, leading the reporting entity to question whether the cost is warranted and place downward pressure of fees and scope, leading to further narrowing of the assurance and further discounting by stakeholders - a race to the bottom to secure an assurance statement (any assurance statement) for the least possible cost. Shifting the focus of assurance from stakeholders at large to those charged with governance can put a stop to this cycle and help ensure assurance is meaningful and supports credibility and trust.

It is worth reflecting that in the <IR> context, the information to be reported and assured is material to financial value. Accordingly, the cost of ensuring a reasonable degree of accuracy in this information would appear justified by the benefits both to the business and its investors and other stakeholders.

Q7. If so, what needs to be done, and by whom, to maximise the net benefits of assurance?

As noted above, we consider the focus of credibility should be on the role of those charged with governance and how they obtain comfort on the report's integrity. In our view, decisions on assurance (whether, what, who, to what extent) should rest with those charged with governance. This enables report users to reward those with superior assurance approaches, and to apply pressure for improvement where practices do not meet user needs.

We consider this process will maximise the net benefits of assurance.

Q8. Should assurance standard setters develop either (a) a new assurance standard or (b) guidance, to ensure consistency of approach to such issues?

As noted above, we consider there is a role for guidance, but that it is too soon to develop a new assurance standard for integrated reporting. Integrated reporting practice is still in its infancy. Accordingly, it is too soon to detail assurance requirements which may restrict exploration and innovation in both reporting and assurance practice. Such exploration is necessary for <IR> to achieve its potential.

We consider more work needs to be done to evolve a 'best practice' framework for assurance of extra-financial material, drawing on both financial and sustainability assurance practice.
We note ongoing divergence between assurance practitioners from different 'schools' (financial and stakeholder/sustainability) in regard to:

- The relative importance of data quality versus process / principles and how much assurance effort should be spent on each; and
- What constitutes adequate procedures, both with respect to report content and process / principles.

Both of these matters should be explored and addressed in guidance.

Q9. Should any such standard / guidance be specific to <IR>, or should it cover topics that are also relevant to other forms of reporting and assurance, eg, should a standard / guidance on assuring narrative information, either in an integrated report or elsewhere, be developed?

We do not have a strong view on this matter. If guidance were specifically developed for integrated assurance, it would no doubt draw on guidance for other similar disclosures (eg, strategic reports) so the outcome would be similar to more generalised guidance.

Q10. What are the (a) key challenges and (b) proposed approaches that assurance standard setters should consider with respect to:

- **Materiality?**
- **The reporting boundary?**
- **Connectivity?**
- **Completeness?**

- **Narrative reporting and future oriented information?**

We acknowledge that all of these areas pose challenges that should occupy the minds of practitioners and standard setters.

We limit our comments to an observation from current extra-financial assurance practice that assurance procedures appear largely introspective, focussing on conversations with management and observations of stakeholder engagement conducted for the report (rather than in the ordinary course of business). There appears to be too little effort to secure independent external views, which is surprising given the increasing availability of specialist ESG research houses and coverage of ESG by brokers and other financial market participants. Such material would seem to be even more pertinent to integrated reports (especially to materiality, future orientation, and completeness).

Q11. What other technical issues, if any, specific to <IR> should be addressed by assurance standard setters?

No further issues.

Q12. What are the (a) key challenges and (b) proposed approaches that assurance standard setters should consider with respect to:

- **Reasonable assurance?**
- **Limited assurance?**
- **Hybrid engagements?**
- **Agreed-upon procedures engagements?**
- **Other approaches?**

As noted throughout our submission, we consider that of the credibility mechanisms available, the greatest reliance should be placed on leadership – especially the board and audit committee (those charged with governance). In our view, the type of assurance should be a key question for those charged with governance.

We acknowledge that once outside the relative clarity of reasonable assurance, practice varies greatly and communication to external stakeholders becomes challenging. We consider there is a role for standard setters to narrow this range of practice somewhat, eg, by providing guidance on minimum procedures to assure different aspects and reporting principles.

Communication about the type of assurance is the also key. As noted above, the maturity model presented PWC's paper *Inspiring Trust Through Insight* could be adapted to communicating the scope and level of the assurance (as well as the findings).

We have strong concerns about the use of a ratings system on report quality, consistent with those presented in the paper *Assurance on <IR>: An Exploration of Issues*.

Q13. What are the (a) key challenges and (b) proposed approaches that should be considered, and by whom, to ensure assurance on <IR> pays due regard to other assurance processes?

As noted throughout our submission, we consider that of the credibility mechanisms available, the greatest reliance should be placed on leadership – especially on the role of the board and audit committee (those charged with governance).

Coordinating credibility efforts through the board and audit committee enables appropriate co-ordination and due regard to be paid to other assurance processes. Focusing efforts on the statement by those charged with governance about how this group obtained comfort (away from a statement/s from external assurance provider/s) can alleviate risks of duplication of effort and challenges in relying on the work of other assurance practitioners. We consider those charged with governance to be uniquely well placed to integrate the multiple credibility mechanisms employed, including multiple assurances.

We note that the exposure draft of ISA720 proposed expanding the scope and responsibilities of auditors regarding other information contained in or accompanying an audited financial report. This was described as a two-way process, wherein the auditor's responsibilities included not only reading the other information for consistency with the audited financial statements but also ***reading and considering the other information for consistency with the auditor's understanding of the entity and the environment acquired during the course of the audit***. Guidance on how these responsibilities apply in an integrated reporting context will be a priority to resolve as part of, or immediately upon, finalisation of the revisions to ISA720.