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Assurance on <IR>, an exploration of issues

Thank you for the opportunity to provide comments on the paper: *Assurance on <IR>, an exploration of issues* (discussion paper) issued by the International Integrated Reporting Council (IIRC) in July 2014. This submission provides an SMP perspective of experience with middle-market growing businesses and is based on:

(i)   my previous experience as the Technical Standards Partner for a large mid-tier firm in Australia, with responsibility for Independence and Quality Control for more than a decade;

(ii) my experience as a board member of the AUASB[1] for a period of 8 years;

(iii) my previous experience as chair of a group of technical representatives from ten large national networks in Australia over a period of approximately six years;

(iv) my continuing experience acting as a consultant to firms in a large international network of firms; and

(v) my role as an independent audit committee member.

1.   General Comments

1.1   Growing businesses and <IR>
        It is important to note that entities will usually progress through a life cycle, often following a path from privately owned, to publicly owned, to being listed on a stock exchange. Regulators tend to consider corporates at a particular stage of their evolution, rather than recognising that the business environment is dynamic. It is also important to note that the capital markets include a significant proportion of relatively small listed entities, and only a minority have the sophistication of the multinational corporates that often drive external reporting requirements. Consequently, proposals for <IR> could have significant impact on growing businesses which are seeking listing, or which may already be listed on a stock exchange. However, entities in the middle market are rarely diversified, and therefore <IR> reporting would be relatively straightforward, once robust internal processes were established.

1.2   A new paradigm for assurance reporting on <IR>
        The request for feedback on questions posed in section 4 of the paper recognises that new ideas on assurance should be heard without discussion being constrained by past thinking. This is an important consideration as the current framework for assurance reporting is unlikely to be compatible with the philosophy to promote clear, concise, easily understandable information content for users.

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[1] Australian Auditing and Assurance Standards Board

2. Specific requests for feedback

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

The AUASB glossary of terms defines an assurance engagement as "an engagement in which an assurance practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria."

This definition presents the likely common understanding of user expectations of assurance to drive credibility and trust in <IR>.

In respect of <IR> the boundaries to define the subject matter are not yet clear (hence concerns regarding the completeness of an <IR> report), criteria for the evaluation of subject matter is still evolving, and measurement techniques are also in the early stages of development. Consequently, it is more important to develop a common understanding of subject matter, criteria and appropriate measurement techniques, before assurance can be considered, or provided on an entire <IR>.

However, in this period when a common understanding of 'completeness' of an <IR> needs to be established, independent assurance could play a key role in identifying management bias or a lack of objectivity in the way information is presented to users of the <IR>.

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

Assurance reports are currently written in technical language in a standard format. Long-form auditors' reports are yet to be widely experienced in the marketplace, although preliminary review indicates that they are unlikely to be concise reports that are compatible with the nature of an <IR>. There is an urgent need for ***innovation in assurance reporting*** to enable delivery of assurance reports in a clear, concise format using non-technical language, which will be consistent with the philosophy underlying the <IR>.

The qualitative characteristics of financial reports are clearly articulated in the financial reporting framework. Hence, in the context of financial reporting, the attributes of assurance are well understood. As a consequence, an assurance report to users of a financial report enables those users to take confidence in the consistent, comparable, reliable and complete presentation of information contained in that financial report.

The qualitative characteristics of <IR> are yet to be defined at an operational level and therefore the meaning attributed to assurance of <IR> needs to be debated and agreed first, before an appropriate format for assurance reports can be established.

2.3 *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?*

Although <IR> is not a new concept, formal processes to enable <IR> reporting are relatively new. The internal processes to be established by entities who adopt integrated thinking are now being developed, and the nature of internal <IR> is evolving. Management tools such as "the balanced scorecard" went some way towards promoting internal reporting processes

for non-financial information. However <IR> takes the internal reporting processes needed to a more sophisticated level.

Therefore, it is not surprising that there are relatively few experienced practitioners in Australia and in the Asia-Pacific region more broadly, as the <IR> industry is not yet mature. The skills required are not entirely new, but rather, there is a need to 'regroup' existing skills and the way in which those with differing expertise work together.

2.4 *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?*

There is a need to monitor practice and ensure frequent communication between entities, practitioners, educators and standard setters. As best practice evolves, the learning and methodologies should be shared to identify those practices that are acceptable to both the business community and its stakeholders.

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

Until a common understanding of subject matter, criteria and measurement techniques is defined by the business community, it is not feasible to expect that internal systems can be evaluated as robust or otherwise. Rather, we should expect to see incremental continuous improvement in internal systems as they are shaped to provide the information needed.

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

It is unlikely that assurance will be a cost effective mechanism to ensure credibility and trust in the short/medium term, if existing assurance reporting frameworks are followed. Refer also to the response to Q2 above.

"New thinking" and innovation for assurance reporting is needed for assurance to provide a cost-effective mechanism at any stage in the future.

An example of "new thinking"' for assurance reporting is perhaps illustrated by the "Behind the Brands Scorecard" reports, which is presented here for illustrative purposes only. This initiative, launched by the Oxfam GROW campaign, is focussed on a world where everyone has enough to eat and examines various criteria in the supply chain of large corporates. Although the key objective of the Oxfam report is not the same as <IR> there are many similarities and the scorecard report, which is supported by uniform measurement techniques, provides an easily understandable, visible report of how corporates are performing in various aspects of their business operations.

The following shaded text represents extracts copied from the website at http://www.behindthebrands.org/en-us/about

THE ISSUES
The Scorecard looks at seven themes, weighing each theme equally. The seven themes are:
1. Transparency at a corporate level
2. Women farm workers and small-scale producers in the supply chain
3. Workers on farms in the supply chain
4. Farmers (small-scale) growing the commodities

The visual scorecard is available at http://www.behindthebrands.org/en-us/scorecard

I cannot endorse the methodologies used by Oxfam, but as a user of the website, this form of visual reporting appears far more compatible with <IR> than long-form reports with extensive detail. Of course, the summary scorecard report could also be supported by narrative and other information when appropriate.

In terms of "new thinking" for assurance reporting, the objectives for various aspects of the <IR> capitals would need to be agreed and scores assigned as to how well or otherwise a corporate might be achieving, or seeking to achieve best practice.

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

New thinking and innovation for assurance is urgently needed,
Refer response to Q6 above

2.8 *Should assurance standard setters develop either or both (a) a new assurance standard; (b) guidance, to ensure consistency of approach to such issues?*

Assurance standard setters need to first identify a new paradigm for assurance reporting as it applies to <IR>. Refer responses to Q2 and Q6 above.

2.9 *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, e.g., should a standard/guidance on assuring narrative information, either in an integrated report or elsewhere, be developed?*

Refer Q8 above

2.10 *What are (a) the 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?*

Refer response to Q6 above.

There is a need to develop a scorecard or similar mechanism, as a first step in identifying boundaries for reporting in respect of each capital. This mechanism would provide visibility of those areas/capitals that are actively managed and reported by the entity, and those which are yet to be examined.

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

In developing a scorecard for reporting, assurance practitioners would need to work closely with industry experts and those with expertise in managing non-financial assets.

2.12 *What are the (a) key challenges and (b) proposed approaches that assurance standard steers should consider with respect to:*
- *Reasonable assurance?*
- *Limited assurance?*
- *Hybrid engagements?*
- *Agreed-upon procedures engagements?*
- *Other approaches?*

A new paradigm for assurance reporting is needed to enable clear concise communications to be provided to users of the <IR>. The current methodologies and reporting referred to above are unlikely to provide clear, concise, understandable assurance reports for users. The presentation and nature of current assurance reports are not compatible with the philosophy underlying <IR>.

2.13 *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?*

The assurance standard setters have a strong and well established framework which is applied to reporting on financial information. The key challenge will be to set aside the past thinking applied to financial information, to identify a new paradigm for assurance reports on non-financial information. Assurance reports on <IR> will perhaps need to focus on performance of non-financial capitals measured in relative terms, rather than absolute measures of financial capital.

Please feel free to contact me to discuss further any matters arising from this submission.

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