Douglas Hileman Consulting, LLC
13630 Crewe Street
Van Nuys, CA 91405-4235
www.douglashileman.com

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International Integrated Reporting Council
29 Lincoln's Inn Fields
London, WC2A 3EE
United Kingdom
Sent via email to: assurance@theiirc.org

SUBJECT: Assurance on Integrated Reporting; an Exploration of Issues
Comments on Exposure Draft

Dear IIRC:

This submittal provides my comments, thoughts, and suggestions on assurance with regard to integrated reporting (IR). By way of background, I have been involved in the auditing field for over 35 years. Focus areas have included environmental compliance, management systems, transactions, audits to contracts, litigation support, technical support to financial audits, internal audits, and auditing to U.S. Generally Accepted Government Auditing Standards (GAGAS or "yellow book") for the SEC's rule on conflict minerals rule pursuant to Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. I hold credentials as a Certified Risk Management Assurance professional, and a Certified Professional Environmental Auditor. I am a member of the Institute of Internal Auditors (IIA). I submitted comments on the exposure draft of the reporting framework in July 2013. Although I am a member of the IIA, hold several professional certifications, and am active in other groups, all comments and content submitted herein are strictly my own.

<u>Introduction</u>

The Integrated Reporting Framework ("IR Framework" or "Framework") describes a framework whereby organizational leadership recognizes six types of capital, and that organizations use these types of capital in varying and interconnected ways in order to "create value." The IIRC and the Framework champion external reporting ("Integrated Reporting") so that investors can make more informed decisions. I support the global trend towards transparency, better reporting, and confidence in that reporting. However, in reviewing the Framework, other publications available on the IIRC website, and other professional publications on the matter, I continue to note that one aspect of the Framework continues to be unrecognized (or at least under-emphasized). The Framework's focus is on investors of financial capital, and the reporting is almost (if not entirely) exclusively on the organization's ability and plan to continue creating [financial] capital. The Framework describes and encourages integrated thinking. It describes and encourages integrated management. The Framework encourages external reporting on integrated thinking and management. However, there are no provisions for reporting on the impact (positively or negatively) on the five non-financial capitals, except to the extent that impact on them detracts from the organization's short, medium, and long-term ability to create [financial] value.

Many stakeholders regard an organization's impact on non-financial capitals as being critical. Impact on non-financial capitals can impact the organization directly and indirectly in many ways. Potential employees may consider how the organization's integrated management affects their own human capital, or the capital of their peer group. Government entities should be interested in an organization's impact on manufactured capital in considering whether to grant permission to construct facilities or begin business in their jurisdiction; the ability to compare performance on non-financial capitals between competitive companies would be especially useful to these agencies. The Framework does, indeed, integrate many considerations for organizations – and the stories on the IIRC website include examples of organizations who believe they are better for it. However, "integration" is not complete. Other reporting and transparency initiatives will continue to be important.

The integrated thinking and integrated management concepts have much in common with other models, including some that have greater history than Integrated Reporting. These include the COSO Internal Controls and Enterprise Risk Management frameworks and ISO management systems frameworks. To the extent that the IIRC can leverage constructs, experience, credentials, and resources that are built around these frameworks, it will make for a simpler journey of experimentation, adoption, use, and improvement.

<u>The Questions Posed by IIRC</u>

Assurance on <IR>, an Introduction to the Discussion includes thirteen (13) questions where the IIRC asked for comments. Each question is listed below, with the author's comments. Some comments may apply to more than one question. Indeed, some comments may apply better to questions other than the one for which it is provided. The author encourages the IIRC and other stakeholders to read the comments, consider their intent as a whole, and use the thoughts and principles towards more effective, efficient, useful, and trustworthy assurance of integrated reporting.

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

I believe that assurance enhances the credibility and trust of anything an organization provides externally that is core to its organizational value proposition. This includes products, services, communications, and reporting. Assurance is particularly critical for matters that are more complex, more technical, and where stakeholders place a greater deal of reliance on the product, service, or communications. Assurance is also critical where stakeholders do not have access to information for themselves. Assurance is provided on a wide range of products, services, and communications and reporting. A century ago, the public was at risk due to lack of standards and assurance mechanisms for electrical appliances; creation of suitable standards and assurance mechanisms were critical to gaining trust of households buying more compliances. Investors depend upon financial reports for accurate information in making decisions on entrusting their investments. Assurance standards, organizations, and professionals developed as a result. Similarly, if Integrated Reporting is to be regarded as critical to the safety of the users, then there must be a role for assurance.

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

Integrated reporting will evolve, driven in large part by how users come to recognize, use, and provide meaningful feedback on the value of integrated reporting and their expectations. This commenter believes it will become adopted more widely and more quickly if users provide meaningful, tangible feedback directly to report issuers – such as direct investments made (or not made) solely on the basis of their integrated reports (or lack thereof).

This commenter believes that the emphasis and needs for assurance will also evolve over time. “An Exploration of Issues” highlighted challenges posed in providing assurance over different types of information, including quantified measurements, factual narrative, soft narrative, etc. (paragraph 4.30). The needs for assurance on these types of information will be different. The commonality will be the need for the user to understand what the assurance does – and didn’t do. This would include description of key elements such as the scope, limits of scope, type of assurance effort, conclusions, and notable exceptions.

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

The availability of assurance practitioners may be a problem in the short and medium term. However, integrated reporting and assurance thereof are likely to grow in parallel. There are professional associations of auditors and suitable credentials, such that if these organizations collaborate, there should not be a problem in meeting these needs over time.

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?

There are several credentials that align with the goals of Integrated Reporting and the skill sets desired for assurance providers. The credentials include education, competence, proficiency, and continuing education. The certified public accountant (CPA) credential (and similar designations worldwide) is highly regarded. The IIA maintains several such credentials. This commenter strongly urges the IIRC to avoid the temptation to become a certifying body, to issue certification standards, or to take other actions that could compromise the independence of the IIRC, the professionals involved, or the intended underlying value proposition of integrated reporting.

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

This commenter believes that there is room for improvement in the robustness of internal systems of controls and risk management, particularly as it pertains to non-financial aspects, and the connectivity of different functions or factors. In the U.S., Sarbanes-Oxley has placed considerable emphasis on robust internal systems and controls related to financial reporting. These are reviewed by independent financial auditors. Sarbanes-Oxley requires internal certifications regarding systems and controls over operations and compliance. External assurance of operations and compliance is not required.

The Institute of Internal Auditor's (IIA) position paper on the "Three Lines of Defense" (3LOD) serves as an excellent model. Various oversight groups provide a degree of comfort on operations and compliance – IT auditing, environmental auditing, security auditing, supply chain auditing, and others. Internal Audit's role can be to monitor completeness, accuracy and support for operations and compliance, and (the fourth component of Enterprise Risk Management) business strategy. Financial auditors provide external assurance, which could be thought of as a fourth line of defense on financial reporting only.

Given the degree of reliance on financial reporting, the regulatory requirements related to financial reporting, and the potential for significant enforcement, legal actions, and financial consequences of improper or inaccurate financial reporting, it is no surprise that organizations devote considerable resources to developing, maintaining, and assuring their systems and controls over financial reporting. While few organizations would posit that operations, compliance, or business strategy was less important, I believe that most would acknowledge that the systems and controls over non-financial aspects of their organization would not approach those for financial reporting. [There would be notable exceptions in heavily-regulated industries, such as pharmaceuticals.]

It is an inherent value proposition of the IIRC that financial investors should understand non-financial information, how it relates to organizational management, and the potential for affect financial reporting over time. This corresponds to the non-financial categories of Enterprise Risk Management, where there is currently no widely accepted model for external assurance.

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

This commenter notes that costs will always be a concern. For the affected entity, it will often be an objection. However, if the users are to trust and rely on the contents of an integrated report, then assurance of some type is a necessity. The "assurance footprint", as well as the methodology, contents of the assurance report will evolve as the integrated report evolves. The issuers and the assurance providers can work together towards more efficient, effective means for assurance.

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

No comment provided.

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

This commenter believes that there are standards, such as the performance standards of (U.S.) Generally Accepted Government Auditing Standards (GAGAS) that could be suitable – or nearly so. This commenter argues against developing new standards or guidance for IR. If, however, a group of leading assurance professionals with experience in all six capitals (as defined by IIRC or as reasonably appropriate via other organizations) agree that no suitable standard or combination of standards exists, and that something unique to IR is required, then such an effort should be considered. If so, this should be a process open to stakeholder engagement, involvement, and comment.

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? Should a standard/ guidance on assuring narrative information, either in an integrated report or elsewhere, be developed?

The issuer cautions against new standards/ guidance unique to integrated reporting. Unless and until the IIRC can demonstrate that assurance of an integrated report replaces assurance required for other purposes (legal or regulatory requirement, condition of involvement in industry association, etc.), and is at least as effective and reduces costs compared to the alternative, then the IIRC should avoid contributing to "audit overload" experienced by many organizations.

Q10. What are (a) key challenges and (b) proposed approaches that assurance standard setters should consider with respect to: materiality; reporting boundary; connectivity; completeness; narrative reporting and future-oriented information?

Key challenges will be to clearly define what is included, and what is not. As noted in initial comments, the IR Framework integrates many things – but it does not integrate some things where external reporting (and assurance) is expected by key stakeholders. The approaches to assurance of the contents of an integrated report should clarify intent, scope, purposes – and where the assurance is expressly not provided.

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

No comment provided.

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; agree-upon procedures engagements; other approaches?

In the U.S., Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act addresses the concern of tin, tantalum, tungsten and/or gold (3TG) illicitly sourced or transported from the Democratic Republic of Congo (DRC) may be unknowingly used by U.S. public issuers in products they manufacture or contract to manufacture. As directed by Congress, the Securities and Exchange Commission (SEC) published a rule for "Dodd Frank Conflict Minerals", which went into effect for the 2013 reporting year. The rule requires an Independent Private Sector Audit; this requirement will be triggered for most affected large companies in the 2015 reporting year. The SEC rule specifies two objectives for the IPSA. The rule allows Certified Public Accountants (CPAs) or non-CPAs to conduct the IPSA, using the appropriate standards for government audits. The few IPSA reports done to date by CPAs have resembled the short, concise statements that are submitted for financial audits. The IPSA report done by this author (one of two for 2013, and the only one by a non-CPA based in the U.S.) to performance audit standards was a bit longer, and included a general description of the audit components as outlined in the applicable standards.

The SEC's conflict minerals rule provides one example that may be useful for Integrated Reporting. The objectives are for the IPSA Auditor to develop a conclusion regarding whether "the *design* of the due diligence effort is consistent *in all material respects*……….." with an internationally-recognized framework, and whether the steps described were actually done by the issuer [emphasis added]. The two objectives both center on process: the design of the process, and the way the issuer describes how they implemented the process.

This commenter suggests that Integrated Reporting and reporting on the SEC's conflict minerals rule may share some similarities:

- There is an internationally-recognized framework. This framework may change over time.
- It is not clear yet who the users are or will be, how they will use the assurance reports, what factors will cause them to make different decisions regarding their investments, or if users who are interested primarily in non-financial issues will regard the reports (either the underlying reports or the assurance thereof) with greater credibility.

Q13. What are (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 IIA's 3LOD model provides a useful construct.

Closing

I appreciate the work the IIRC is doing to call attention to the importance of various kinds of capital, the interrelationships between capitals (and people, and our planet). I wholeheartedly support the IIRC's contention that investors should focus on these matters for the longer-term; it is for the benefit of the planet, the organization's stakeholders – and their own investments. Assurance will need to play a role.

Sincerely,

Douglas Hileman, CRMA, CPEA, P.E.
President, Douglas Hileman Consulting LLC
www.douglashileman.com
doug@douglashileman.com