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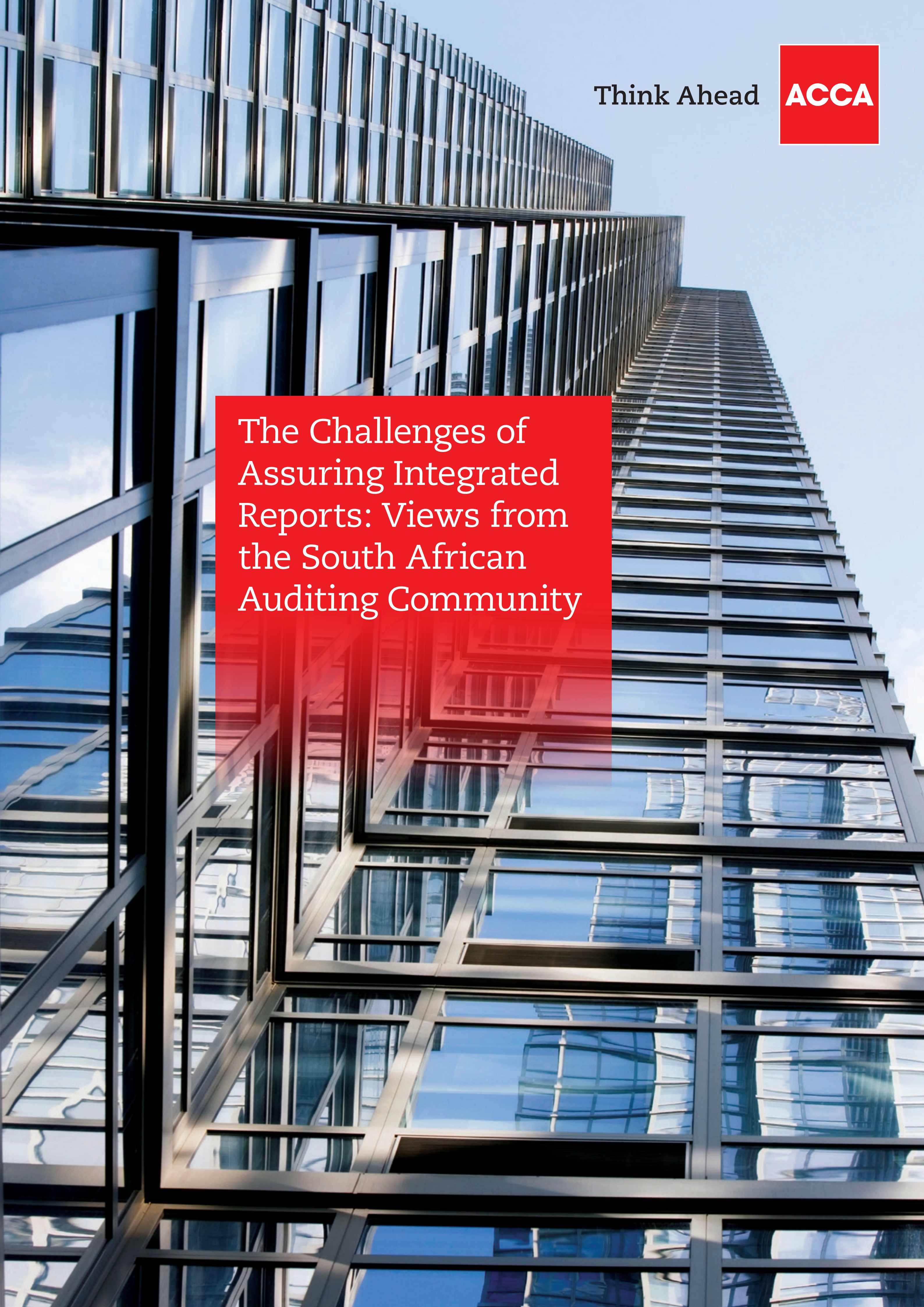

The Challenges of Assuring Integrated Reports: Views from the South African Auditing Community

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In 2010, South Africa became the first country in the world to mandate Integrated Reports <IR> for all listed companies. This report focuses on the issue of independent assurance: can and should independent assurance be delivered on <IR> in the same way as it is on conventional annual reports and financial statements? The views of a number of senior assurance practitioners from the South African auditing profession show that although most respondents support the concept of independent assurance of <IR>, they also foresee a number of technical and legal liability issues which may affect the pace of <IR> assurance development.

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ACKNOWLEDGEMENTS

We are immensely grateful to ACCA for funding this research. Our thanks also goes to the interviewees, without whose support this research would have been impossible.

The Challenges of Assuring Integrated Reports: Views from the South African Auditing Community

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Foreword

Independent assurance of corporate reports is an important means of achieving three different objectives:

- satisfying stakeholders' demands for managerial accountability
- enabling or underpinning financial market stability, and
- assisting the reporting entity to improve its operational performance.

Independent assurance of financial statements in its current form has been with us for more than a century and has consistently evolved with changes in society and business practices and it allows these statements by multinational organisations to be held up for scrutiny.

Independent assurance of non-financial reports has proved to be challenging. Unlike financial reports, sustainability reports are rarely (if ever) mandated by listing authorities and the raw materials that underpin the reports are often less quantifiable and more qualitative in nature. So, even those organisations that do issue sustainability reports do not always (or have not always been able to) commission independent assurance services that engender the same level of credibility and trust as do auditors' reports on the financial statements.

The same has held true for the new generation of Integrated Reports (IR) which are nowadays increasingly common – especially in the listed company sector – and in some areas are a listing requirement on an 'if not, why not' basis, for instance in South Africa. The increased attention to, and the potential wider adoption of, IR makes it important that a generally acceptable form of independent assurance is developed.

I am delighted therefore to welcome this new report by ACCA, the third in a series of reports using South Africa as the lens through which to observe the implications and impacts of various aspects of integrated reporting.

ACCA's report concludes that there is a strong case for making the integrated report the subject matter of an assurance engagement but that there are a number of technical challenges that currently make it difficult to assure the entire integrated report. These challenges include the difficulty of developing suitable criteria for assuring the integrated report, the limited range of skills of a traditional audit team and the adequacy of clients' records, systems and controls. As the authors also point out, the high cost of providing even limited assurance and the risk of additional auditor liability also need to be taken into account.

The interviews recorded here with senior members of the assurance-providing profession, and the conclusions drawn, strongly support the IIRC's own conclusions and lend weight to IIRC's own 'call for action' (IIRC 2015) on <IR> assurance issues. Our recent consultations have led us to conclude that:

- organisations use a range of mechanisms to enhance credibility and trust, of which assurance is only one
- the internal systems needed for <IR> are far less mature than systems for 'financial' information
- the concept of integrated reporting is relatively new and is still evolving; likewise the assurance of an integrated report is evolving
- innovation and experimentation are necessary, although existing assurance principles and methodologies should not be prematurely rejected
- the total costs and benefits of assurance are difficult to assess, but it is likely that assurance will become more cost effective as time goes by, and
- assurance practitioners will need to develop a comprehensive understanding of how value is created (for the organisation and for others) across the full range of the resources employed by the entity and its relations with its stakeholders.

Mervyn King
Chairman, IIRC

Executive summary

Initial research carried out by ACCA has shown that the introduction of integrated reporting in South Africa has been welcomed by the investor community.

Initial research carried out by ACCA has shown that the introduction of integrated reporting in South Africa has been welcomed by the investor community. As argued by the International Integrated Reporting Council (IIRC), integrated reports are becoming an important source of information for stakeholders interested in companies' financial and non-financial performance and their ability to generate sustainable returns.

As the perceived value of integrated reports continues to grow, it is perhaps unsurprising that standard-setters, preparers and users have started to explore the possibility of having these reports subjected to some type of formal assurance. In this context, this report provides an initial view of the possibilities for the assurance of the integrated report. Following 18 in-depth interviews with senior South African auditors and assurance experts, this report examines the challenges to assuring the reports and offers initial ideas of how assurance models may develop to accommodate integrated reporting. The main findings are summarised below.

CONCERNS

- Assurance of the integrated report has the potential to add value by improving the report's credibility and assisting boards of directors in fulfilling their monitoring and review functions.
- As a result, there is a case for making the integrated report the subject matter of an assurance engagement but there are a number of technical challenges which make it impossible to assure the entire integrated report. These include the difficulty of developing suitable criteria for assuring the integrated report, the limited range of skills of a traditional audit team and the adequacy of clients' records, systems and controls. The prohibitively high cost of providing even limited assurance and the risk of additional auditor liability also need to be taken into account.
- Therefore, only certain parts of the integrated reports can, currently, be the subject of an assurance engagement. These are typically those parts of the reports that include only factual disclosures with little or no evaluation by management (or forward-looking information). Information that is abstract, interpretative, predictive or qualitative is too subjective to be the subject of a limited or reasonable assurance engagement. This finding may disappoint the 60% of IIRC consultees who thought that assurance should cover the whole report.
- A key concern with existing assurance practice is that it is resulting in different types of professional opinion being given on different 'elements' of the integrated reports. This is likely to add to the 'audit expectation gap' and it poses a risk that users will place undue reliance on engagement reports found or referred to in the integrated report.
- A process-based audit was suggested as a possible way forward but this was ultimately dismissed on the grounds that systems and controls at many clients are not sufficient or adequately documented. There were also concerns that suitable criteria for describing and evaluating the control environment are not available.
- The absence of suitable criteria appears to be the most significant obstacle to assurance of the integrated report, more so than the risk of auditor liability. Even if suitable criteria can, however, be developed this could have the unintended consequence of limiting the relevance of information included in integrated reports as companies limit disclosures to only those which can be objectively verified.

RECOMMENDATIONS

- A short-term solution is to develop a set of guidelines which recommend those parts of the integrated report that should be the subject of an assurance engagement and offer a basis for describing how assurance is provided over the material components of the integrated report. This may be done by the auditor and/or those charged with governance.
- In the long-run, it may be possible to define an alternative assurance model which does not express an opinion on the extent to which the integrated report complies with the IIRC framework but instead provides something similar to a panel review by suitably qualified experts.
- There is, however, a risk that this new form of assurance will fail to command the same respect as the audit of financial statements and will simply expand or perpetuate the audit expectation gap. Equally relevant is the possibility that this new type of assurance report will be substituted for stakeholder engagement and activism. As a result, before proceeding with radical changes to existing assurance models, companies should be given the time to refine their integrated reports and engage with stakeholders to determine the extent to which external assurance is actually required.

1. Introduction

South African listed companies have been producing integrated reports for five years.

South African listed companies have been producing integrated reports for five years. Given the speed at which integrated reporting has been introduced and developed, little research, either practitioner or academic, has addressed a number of important issues. What do users want? What do the companies think about integrated reporting? Is it adding value? What form should it take? How should it be assured? This research focuses on the last of these questions, addressing the challenges faced by the South African audit community in their attempts to provide assurance over integrated reports.

Two previous ACCA reports explored the development of integrated reporting in South Africa and focused on the ways in which integrated reporting has altered the content of corporate annual reports, as well as the reactions of the South African institutional investment community to integrated reporting (see Solomon and Maroun 2012; Atkins and Maroun 2014). The first report found that the introduction of integrated reporting for South African listed companies resulted in a significant increase in the quality and quantity of social, ethical and environmental information included in companies' annual integrated reports. The research also used a simple technique to measure and assess the level of integration within these documents over a three-year period and showed that there was a significant increase in the integration of social and environmental information in the integrated reports prepared by some of South Africa's largest listed companies. There were, however, some negative findings. In particular, the integrated reports were repetitive and contained substantial elements of stakeholder-directed rhetoric that may not necessarily have been based on genuine change in corporate behaviour and attitude. The second report reiterated these concerns but provided strong evidence that the South African institutional investor community welcomed the introduction of integrated reporting.

Given the generally positive findings on integrated reporting from these two previous ACCA reports, it is necessary to complete the circle by turning our attention to the audit community in South Africa. One of the outstanding issues for the integrated reporting agenda, not just in South Africa but also globally, is the potential for these new reporting forms to be assured.

The International Integrated Reporting Committee (IIRC) has developed an integrated reporting framework which describes the primary objective of an integrated report as explaining 'to providers of financial capital how an organisation creates value over time'. An integrated report is intended to be a concise means of communicating the interconnection between business strategy, governance, performance and the organisation's external environment. The IIRC framework does not explicitly require formal 'assurance' of the integrated report, simply stating that reliability of the information found in an integrated report is 'enhanced by mechanisms such as robust internal control and reporting systems, stakeholder engagement, internal audit or similar functions, and independent, external assurance'.

Similarly, the IIRC's consultation draft does not specifically call for independent external assurance but aims to acknowledge its potential role as part of a range of methods for ensuring the reliability of the information included in integrated reports. The IIRC has stated that its framework provides reporting criteria against which organisations and assurance providers can assess an integrated report. The IIRC's questions for consultation include: (1) whether or not assurance should cover the whole integrated report or just specific aspects; (2) what respondents believed about credibility; and (3) whether or not the framework provided suitable criteria for an assurance engagement.

Respondents reaffirmed the responsibility of those charged with governance to establish an effective system of internal control and stakeholder engagement to ensure the reliability of information found in the integrated reports. Nevertheless, the majority agreed that some form of independent assurance was required. Almost 60% agreed (or agreed with minor qualification) that if assurance were to be obtained, it should cover the entire report. Twenty-one per cent believed that specific aspects of the report should be assured and only 6% disagreed with obtaining assurance on the basis that it is unnecessary, burdensome or cost-ineffective.

Several responses highlighted a number of important challenges. For example, many auditors argued that the IIRC framework might be too vague or conceptual for providing assurance on the extent to which integrated reports comply with its recommendations. Related to this are the difficulties of expressing an opinion on forward-looking information, the sufficiency of the connections described between the

The IIRC concluded that the matter of assurance is beyond the scope of a framework set up for report preparation and that it is not within the remit of the IIRC to develop assurance standards or methodologies.

different capitals in the integrated reporting framework and the completeness of information included in the integrated reports. In particular, existing assurance standards, most notably ISAE 3000, require suitable criteria for evaluating the subject matter of an assurance engagement. For a practitioner to provide either reasonable or limited assurance on the extent to which subject matter complies with a given basis, there must be an appropriate benchmark which can be consistently applied and interpreted objectively, albeit that a degree of professional judgement may be required (IFAC 2013).

The IIRC concluded that the matter of assurance is beyond the scope of a framework set up for report preparation and that it is not within the remit of the IIRC to develop assurance standards or methodologies. Nonetheless, the IIRC stated that, as part of its future work plan, it would consider developing a paper summarising the issues and concerns expressed by respondents. Such a paper would be made available to those directly involved with assurance standards-setting.

1.1 THE CURRENT RESEARCH PROJECT

Research has been published examining the extent to which companies are providing external assurance on 'elements' of their sustainability reports, such as CO2 emissions or employment statistics (for details see Ball et al. 2000; Edgley et al. 2010; KPMG 2013; Edgley et al. 2015). Other than the consultation process carried out by the IIRC, the assurance of the integrated report has not been dealt with and, in particular, there has been no effort to engage external auditors on their views about assuring integrated reports. Therefore, for this report, a number of South African auditors were interviewed and asked a range of questions about the possibilities for assuring an integrated report.

Method

This report provides findings from 18 in-depth, semi-structured interviews with senior members of the South African auditing community. All the interviews were carried out between May and December 2014 and each one lasted between one and two hours.

The interviewees were asked general questions about whether or not the entire integrated report could be the subject of an assurance engagement or, if not, which parts of the report could be assured. The interviewees were encouraged to talk broadly about their views on integrated reporting and the need to have these reports assured. All interviews were recorded and transcribed, providing a substantial amount of data. The interpretative analysis of the interviews led to the identification of a series of themes relating to the assurors' views of integrated report assurance.

1.2 THE FINDINGS

One interviewee, a Big Four audit partner specialising in sustainability, explained integrated reporting as part of a simple philosophy: 'the development of a strategy for an organisation relative to its material issues and stakeholder issues and concerns, and the execution of that strategy in terms of proper performance measurement, proper performance management, proper target setting and proper governance and accountability'.

He argued that integrated reporting is primarily about 'development and execution' and that the debate on the assurance of integrated reporting needs to take several issues into account. His views, as well as those of the other interviewees, address a number of questions.

- What is the value of assurance?
- Should the whole integrated report be assured?
- What parts of integrated reports are or are not being assured?
- Will users be confused by different types of assurance?
- Should auditors be concentrating in the integrated reporting process?
- Should auditors' liability be reconsidered?
- If integrated reports were to be assured, would this reduce their content?

2. Auditors' views on the assurance of integrated reports

Earlier research on the assurance of sustainability reports found that assurance adds credibility to the reporting process.

2.1 WHAT IS THE VALUE OF ASSURANCE?

Earlier research on the assurance of sustainability reports found that assurance adds credibility to the reporting process (Maltby 1995; Owen et al. 2000; Jones and Solomon 2010; IIRC 2015). Although assurance may be only one means of enhancing confidence in the reporting process (IIRC 2015), the auditors interviewed believed that the assurance process definitely adds credibility, with one commenting that: 'an integrated report will only be valuable to the various stakeholders if there is a sense and the feeling that the information being reported is credible and reliable'.

This is possibly the case with the audit of financial statements: 'the market would want some sort of 'stamp of approval' over the whole integrated report otherwise it is never going to play the function that it is intended to play'.

Related to this is the potential for external assurance to mitigate the risk of impression management, which several interviewees raised as a concern with some of the current integrated reporting practices. The risks posed by impression management were also highlighted by South African institutional investors (see also Atkins and Maroun 2014). A Big Four audit partner commented: 'You can very much create a perception or image of an organisation with what you say in the integrated reports…I am not suggesting that people blatantly lie in their reports [but] I think that playing with words becomes an issue and there might be a bit of carte blanche with freedom of speech'.

An audit committee member was more emphatic that assurance was necessary to limit impression management in integrated reports as: 'you can't trust corporates to actually tell the truth because they will colour things in whichever way suits them particularly'.

From a different perspective, the external assurance process can also be relevant for those charged with an organisation's governance. Respondents explained that both the IIRC's framework and South African company law vest responsibility for the reliability of information included in the report with the boards of directors. As a result, external assurance was described as having the potential to provide them with 'added comfort' over the information being communicated to stakeholders and to assist boards with managing their own professional and legal liability risks.

2.2 SHOULD THE WHOLE INTEGRATED REPORT BE ASSURED?

Given the benefits that the assurance process is claimed to offer for financial and sustainability reports, interviewee auditors were asked whether or not the entire integrated report should be assured.

Despite the value that assurance of the integrated report can add, an audit partner from one of the Big Four summarised the view of the majority of interviewees: 'Will we ever get to the point where we will be able to issue an opinion on the whole integrated report? I doubt it – not in our lifetime!' A range of reasons were provided in support of this view.

- **The range of skills of a traditional audit team** was raised by several auditors as a limitation which would frustrate efforts to assure an entire integrated report. As highlighted by the IIRC (2015), assurance in the context of the integrated report requires multiple competencies including a comprehensive understanding of how the transformation of different types of capital creates value. In this context, one audit manager explained how the focus of his training (at both university and his audit firm) was on the technical provisions of International Financial Reporting Standards (IFRS), related finance issues and the requirements of International Standards on Auditing (ISA). This auditor was of the opinion that he was unqualified to examine and report on each of the different types of capital described in the IIRC's framework, a concern raised by almost all respondents.

- **Fear of potential issues relating to auditors' liability** was also given as a reason why auditors might be unable, or unwilling, to provide assurance on the whole integrated report. As an associate director in sustainability auditing explained, auditing firms are conservative by nature and are 'not going to put their names to something without ensuring they have covered everything and made sure…that there's nothing that can come back and bite you'. This expert went on to explain that the nature of most of the information found in the integrated report, particularly qualitative disclosures and forward-looking assessments, are too subjective to express an opinion on without exposing the firm to an unacceptably high risk of litigation.

The general consensus, however, is that – in terms of existing assurance standards – assuring more than a limited number of sections of an integrated report is unlikely to add sufficient value to justify the cost of the engagement.

- **Cost was also seen as a major impediment** to making the entire integrated report the subject of an assurance engagement (see also IIRC 2015). An audit partner from one of the Big Four argued that the complexity of an engagement to cover the full integrated report, including the need to involve different experts (see the first point, above, on specialised skills), would make the engagement prohibitively expensive. In the long-run, uncertainty about the scope and purpose of assurance engagements is likely to be resolved and engagement teams will be able to develop necessary skills leading to cost savings (see also IIRC 2015). The general consensus, however, is that – in terms of existing assurance standards – assuring more than a limited number of sections of an integrated report is unlikely to add sufficient value to justify the cost of the engagement.

- All the auditors participating in the study reiterated the point raised during the IIRC's consultation process, that **suitable criteria** for expressing an opinion on the integrated report have not been developed. The auditors were unanimous in their view that the principles in the framework were too generic to be applied consistently by different audit teams and that the degree of judgement required by management when deciding what information to report makes it impossible to express an opinion on the completeness or appropriateness of the information found in the integrated reports.

- Another reason given by a Big Four associate director for not providing assurance across the whole report was that some of the **clients' record keeping was inadequate**. Linked to this weakness, **the quality of the clients' controls and the control environment** were raised as a further impediment to assuring each part of the integrated report. Interconnected with this were the **capacity and skills of a client's staff** and the **availability of resources** to ensure that the controls covered all the relevant operations and the process necessary to provide audit evidence in support of the disclosures made in the integrated reports.[1]

Given that it appears impossible to assure the whole integrated report, the parts that could be assured were discussed.

2.3 WHICH PARTS OF INTEGRATED REPORTS ARE OR ARE NOT BEING ASSURED?

The interviewees discussed in detail which 'elements' or 'parts' of integrated reports might or might not be suitable for formal assurance. Table 2.1 provides a summary of the types of information that they argued could be the subject of assurance, and which information currently being included in integrated reports would be difficult to assure.

Auditors confirmed that their consideration of the integrated report is currently limited to reading the document to ensure that it does not contain information that contradicts or is

Table 2.1: Elements of integrated reports that can and cannot be assured

What can be assured?		
Financial statements	Quantitative corporate governance information	Reconciliation of the opening and closing number of employees at a company.
Client's order books	Fatalities	Water usage
Safety statistics	Carbon emissions	Water resources
What cannot be assured?		
Integrated thinking underlying the reports	Qualitative corporate governance information	The adequacy of triple bottom line reporting
Strategy section, including key performance indicators	Management views on risk	Sustainability and corporate social responsibility narrative
Forward-looking information	Management views on direction of the company or any management interpretation	Company's corporate mission

1 Many of these concerns were also raised by respondents to the IIRC's consultation process (see IIRC 2015).

> 'The auditor can only assure what has been done. If he does anything more than that [he] is giving an interpretation or projection and that ceases to be assurance…'

inconsistent with the financial statements. This reflects existing auditing standards and forms a normal part of the audit of a client's financial statements.[2] In addition, several auditors explained that their firms regularly provided assurance on, for example, order books, safety statistics and carbon emissions, using mainly IASE 3000 and ISAE 3410.[3] These engagements were carried out independently of the audit of the financial statements and by different engagement teams. The result of these various assurance engagements is that different categories of information (which are often part of the non-financial capitals referred to in the IIRC's framework) are subject to at least some form of independent testing.

In general, however, auditors argued that in, addition to the financial statements, the only specific parts of an integrated report that could be assured were those that were objective, required little application of management's judgement and which did not include material forward-looking information. The result, as discussed in section 2.2, is that most of the disclosures included in an integrated report cannot be the subject of an assurance engagement in terms of existing standards issued by the International Auditing and Assurance Standards Board (IAASB).[4] One interviewee explained the challenge of assuring certain information: 'The auditor can only assure what has been done. If he does anything more than that [he] is giving an interpretation or projection and that ceases to be assurance…It is impossible to give assurance on the 'thinking process' which is going on behind the scenes…or to give assurance on whether or not there is integrated thinking…or if the company's strategy is right and the risks are complete… There is no objective way to gauge that and what you are asking for is the personal view of the auditor, not for independent, objective assurance'.

Interviewees were asked which types of information they believed could not be the subject of an assurance engagement in terms of existing assurance standards. One auditor gave an organisation's strategy statements as an example. The interviewee explained that the strategy section of an integrated report tends to provide management's view on risk and the direction of the company and that there is no benchmark that can be used objectively to evaluate the commentary. An audit partner from one of the Big Four supported this view, explaining that strategy was a 'nebulous area' as it was 'difficult to comment on whether a strategy is good or not'.

Similarly, interviewees were unanimous that it was not possible to provide assurance on the company's business plan, the appropriateness of the company's identified risks, the adequacy of their corporate social responsibility programmes or its corporate mission. As explained by one audit manager: 'Other than looking at the document which records…their corporate mission, you don't really know that that is their mission and you never will!'

The inclusion of forward-looking information is one of the reasons investors welcome integrated reports (Atkins and Maroun 2014) but these disclosures are, essentially, impossible to assure. As an audit partner from one of the Big Four commented: 'We are never going to look into the future. I can't see us giving assurance over future events and future management plans. The closest you will get to that is the going concern assumption where you consider management plans for the next 12 months'.

Ironically, when it comes to one of the key aspects of integrated reporting auditors argued that, at best, all they could do was perform test procedures over the inputs used in the relevant model. This engagement would adhere to ISAE3400[5] and, while this is relevant for prospective financial information, many auditors argued that this type of engagement will offer no value to users looking for assurance on management's evaluation of the prospects of the organisation or the suitability of its business model for generating long-term sustainable returns.

The same concerns were raised about assurance over anything more than objective corporate governance reporting, such as the number of board meetings or the qualifications of board members. As soon as the information is interpreted by management, interviewees were unanimous that assurance could not be provided. One

2 For details see ISA 720: The Auditor's Responsibility Relating to Other Information in Documents Containing Audited Financial Statements

3 ISAE 3410: Assurance Engagements on Greenhouse Gas Statements provides guidance on reporting on client's statements on greenhouse gasses and is often used in conjunction with ISAE3000.

4 It is possible that other useful guidelines relating to non-financial assurance could be used such as those developed by the GRI and AccountAbility. This is, however, beyond the scope of this report.

5 For details, see ISAE3400: The Examination of Prospective Financial Information

> 'the end result is that you have different types of assurance engagements covering different parts of the integrated reports. That's all well and good but don't you think that people will be confused by all of this?'

audit manager, for instance, explained that it would be impossible to conclude definitively whether the company's governance structures were suitable for promoting integrated thinking and ensuring effective management of the different capitals described by the IIRC's framework.

The process involved in deciding what should and should not be assured by the external audit function also seemed complex. An associate director from one of the Big Four said that he was aware of extensive discussions taking place at clients' boards of directors on the sections of the reports that should be assured. These discussions often focused on the elements of the integrated report that companies believe stakeholders would expect to benefit from independent assurance. Safety statistics in mining operations were provided as an example. What many auditors stressed, however, was that there were no regulatory requirements which describe exactly which aspects of an integrated report should be assured and that, consequently, the final decision is usually affected by a cost versus benefit analysis. As one audit partner explained: 'the end result is that you have different types of assurance engagements covering different parts of the integrated reports. That's all well and good but don't you think that people will be confused by all of this?'

From an auditor's perspective, it is important to ensure that the user of the assurance report does not misinterpret the nature and scope of the assurance provided on the subject matter. This was the focus of the next line of enquiry.

2.4 WILL USERS BE CONFUSED BY DIFFERENT TYPES OF ASSURANCE?

The audit expectation gap has been well documented and many auditors argued that the emerging trend of having parts of the integrated report assured will add to the problem. As an associate director from one of the Big Four explained, it is likely that the 'average user' will 'struggle to understand the scope of the assurance opinion as they will have to ascertain exactly what the assurance has been given on'. He went on to explain that, often, there are two or three different assurance reports included, or at least referred to, in a client's integrated report. For example, the integrated report will include the audit report on the financial statements, another assuring elements of the sustainability report and a third providing assurance on selected parts of the integrated report. Even for users with a reasonable understanding of accounting and auditing practices, interviewees were concerned that different reports offering different levels of assurance and subject to different restrictions would be difficult to understand.

This view is reasonable when considering that auditors highlighted at least three professional standards being used to meet their clients' assurance requirements. ISA's are applicable for audits of financial statements and provide a high (but not absolute) level of assurance. ISAE 3000 was described as a 'general purpose' standard, used to guide engagements dealing with any suitable subject matter other than historical financial information.

ISAE 3410 is used for engagements dealing with greenhouse gas statements in conjunction with ISAE 3000. These standards result in either limited or reasonable levels of assurance and the opinions provided are neither structured nor worded in exactly the same way as the audit opinion on the financial statements.

Consequently, an independent audit technical consultant argued that, even if the assurance provider is clear about the type of assurance being offered, the reader is unlikely to understand precisely the nature and extent of the assurance provided. In turn, this leads to the risk that stakeholders will misinterpret the different assurance reports as constituting the expression of an opinion on adequacy of the integrated report and, possibly, the viability of the business. In this regard, should auditors dispense with assuring the different disclosures included in an integrated report and concentrate instead on testing the systems used to prepare the integrated reports and associated controls?

2.5 SHOULD AUDITORS BE CONCENTRATING ON THE INTEGRATED REPORTING PROCESS?

In cases where the organisation already has a sophisticated control environment, one associate director argued that assuring the systems and processes being used to prepare the integrated report was one approach for 'giving comfort over the credibility of the information found in the integrated reports'. This could be especially true where the company in question is subject to the US Sarbanes–Oxley Act and has in place a formal control system that is clearly documented and can be tested.

Currently, however, there are no formal control frameworks for integrated reporting. As with the direct assurance of the information found in integrated reports, auditors expressed doubt that there would be suitable criteria for gauging the adequacy of a client's systems, processes and controls for preparing an integrated report. In particular, one interviewee explained that the most relevant controls would be those over the determination of materiality, the adequacy of stakeholder engagement and the strategy development process. These are, however, the same areas where auditors argued that there was little or no professional guidance on the types of controls which should be in place.

This concern begs the question: are auditors' concerns about additional liability contributing to the criticism of different assurance options currently available?

Even if this were not an obstacle, several interviewees pointed out that not all companies have effective internal controls, a point also raised by the IIRC (2015). Several auditors confirmed that on many engagements they were unable to place meaningful reliance on internal financial controls and depended instead on substantive tests of detail to address audit risks. In these instances, the auditors argued that it was very unlikely that clients would be able to manage effectively the very sophisticated control systems that would be needed to give assurance on the integrated reporting process. In other cases, the auditors confirmed that internal controls, which may be relevant for the integrated report, were in place but impossible to test. For example: 'What do you do in a situation where the [person who prepares the integrated report] has had several meetings with different divisional heads to ensure that he has taken all of the relevant information into account. You have spoken to these people and they have confirmed that they had really detailed discussions but they have not documented any of it. All you have is the final report. You can't test the control because you don't have any objective evidence of the control process. All you have is the output'.

Other auditors were opposed to a systems-based audit for a different reason. In their view, the assurance of internal controls and systems would simply compound the problem of producing too many different types of assurance report. As discussed earlier (see section 2.4), these auditors were concerned that reports offering different levels of assurance on different subject matters would mislead users; result in their placing undue reliance on information found in the integrated reports; and lead to increased litigation risk. This concern begs the question: are auditors' concerns about additional liability contributing to the criticism of different assurance options currently available?

2.6 SHOULD AUDITORS' LIABILITY BE RECONSIDERED?

Currently, auditors are not assuring the entire integrated report. Where an assurance engagement other than an audit of financial statements is being provided, interviewees pointed out that the terms of these engagements limit liability. Furthermore, the South African audit market is not as litigious as the US's, with the result that there are few legal cases against auditors and public indemnity insurance is available at reasonable rates. As a result, some of the interviewees did not regard auditor liability as a material consideration in the context of the services that they are currently rendering to their clients. If, however, a requirement to assure the entire integrated report is introduced, some auditors argued that it may be necessary to reassess the need to offer protection from claims by clients and third parties in order to 'be fair to the auditor, who now has to stick his neck out even more to express an opinion on a client's integrated report'.

Others took a different view. They argued that the issue of auditor liability was purely academic. In their opinion, there is no requirement to assure the integrated report and the likelihood of this materialising in the short-term is negligible. They reiterated earlier concerns (see section 1 and section 2.2) that the absence of a suitable assurance framework, a clearly defined set of criteria and a standardised subject matter are the impediments to the assurance of an integrated report, not auditors' litigation risk.

This argument suggests that the integrated report could be the subject of an assurance engagement if suitable criteria were developed, and that auditor liability is only a secondary consideration.[6] It should, however, be kept in mind that subjecting the integrated report to external assurance could have unintended consequences, one of which is the limitation of the type of information found in these documents.

6 This view may, however, be as a result of the difficulties likely to be encountered by third parties attempting to hold the auditor liable for expressing an opinion on all or part of the integrated report.

> 'Instead of a forward-looking approach where management provide detailed analysis and their own projections, companies would have to focus on reporting factual information and historic information…'

2.7 IF INTEGRATED REPORTS HAD TO BE ASSURED, COULD THIS REDUCE THEIR CONTENT?

A number of auditors raised concerns about the impact of assurance on the scope of the integrated report. One interviewee explained that, if auditors were forced to develop a framework for providing a high level of assurance over the integrated report, this could lead to the exclusion of information that users may find useful but that could not be assured. One Big Four audit partner elaborated: 'Instead of a forward-looking approach where management provide detailed analysis and their own projections, companies would have to focus on reporting factual information and historic information… This would result in stripping out half or even two-thirds of what is currently being reported…Maybe you've not achieved the desired [goal of having] some kind of assurance over the information included in the integrated report because all you have done is carve out that information'.

Most interviewees concurred that any criteria developed for integrated reports would have properties similar to those discussed by the existing assurance framework. Consequently, they reiterated the view that subjective analysis being provided by management in an integrated report could not be objectively evaluated against a given set of criteria. One audit manager used the GRI guidelines to illustrate the point: 'The GRI provides preparers with a number of excellent recommended disclosures. But if you look at the assurance reports being provided on GRI compliance, what the reports are telling you is just that the disclosure is included. The reports most certainly do not analyse the disclosures and tell you that they reflect faithfully exactly how management has used the GRI guidelines to run their business. Basically the assurance is given on a disclosure checklist – nothing more'.

In this context, an associate director of sustainability auditing pointed out that a client would react to external assurance requirements by limiting the information included in the report. The emphasis would not be on providing information that explains how the organisation is creating and sustaining value and its key financial and non-financial risks but on whether or not the disclosure can be tested or measured against prescribed criteria. The integrated reports would, in the view of several auditors, become more factual and reliable but it was questionable that they would include relevant, forward-looking information as envisaged by the IIRC.

3. Recommendations and predictions for integrated report assurance

In addition to raising concerns about expressing an opinion on integrated reports using the existing assurance frameworks, interviewees provided a number of recommendations and gave their views on how assurance requirements may evolve to accommodate an integrated approach to corporate reporting.

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3.1 NEW FORMS OF ASSURANCE

Interviewees discussed a number of possibilities for the assurance of integrated reports. In the first instance, a Big Four audit partner argued that existing standards, such as ISAE 3000 (IFAC 2013), had not been written with integrated reporting in mind but that they could be applied by analogy to the audit of different 'parts' of the integrated report. This would be similar to the current situation and would be complemented by an assurance framework, which should be issued by the IIRC in consultation with the IAASB.

According to these interviewees, the framework should not attempt to explain how an auditor would assure an entire integrated report. Instead, it should provide recommendations to preparers and their auditors to reduce the subjectivity involved when deciding which parts of an integrated report should be assured. This would form a part of the existing principles-based approach to preparing an integrated report and could be complemented by reporting guidelines on how the auditor can explain which sections of the report have been subject to test procedures, the extent of the work done and the nature of assurance provided (see also IIRC 2015).

One auditor described this as a 'jigsaw assurance model' which relies mainly on existing assurance practice. The approach was supported by those practitioners who believed that, in the near future, it would be impossible for the IAASB or IIRC to develop a generally accepted approach for auditing the full integrated report and expressing a professional opinion on the extent to which it complies with an integrated reporting framework. In this way, the 'jigsaw assurance model' would allow auditors to address the calls for at least some assurance over the integrated report while giving standard-setters the time to review the implementation of integrated reporting and devise a long-term solution to the need for assurance. This ensures that there is sufficient research and stakeholder engagement to develop existing assurance practice and avoid allowing the assurance process to become a compliance exercise which, ultimately, lacks relevance (see also IIRC 2015).

Other interviewees shared this view but argued that reporting on the extent to which information in the integrated report is assured should vest with those charged with governance. According to these auditors, practitioners provide multiple types of assurance over different parts of the report and the auditor provides the client with only the professional opinions as prescribed by ISAs or ISAEs. Management should be responsible for communicating how it has relied on a mix of services from external auditors, internal auditors, and its own experts or consultants to ensure that the information provided to users is of a high quality. This approach was summarised by one audit partner: 'There will be all the different pieces that have been assured [by the external auditor] and then there are the leftover pieces and that is where the board needs to make up its mind and decide what to cover. This approach would involve combining external efforts to assure the integrated reports on a piecemeal basis with internal assurance processes'.

Auditors supporting this approach to integrated reporting assurance highlighted two key advantages. Firstly, there is no need for the auditor to issue an additional report to summarise the professional opinions provided to a client, avoiding the possibility of further confusing the stakeholders. Secondly, the approach limits the risk that management might shift responsibility for the relevance and reliability of the information included in the integrated report to the auditor.

Some interviewees suggested, however, that the whole approach to assurance should change as the existing assurance model was no longer 'fit for purpose'. A senior manager (audit technical) suggested that a radical reconceptualisation of assurance was needed which is not constrained by the need to quantify materiality and define a rigid set of criteria. Unlike the traditionally conservative

> 'There needs to be one place for a reader to look…There cannot be more than one report from the auditor. It is not sensible to have a separate statement for the financial audit and a separate statement for the integrated report…'

approach followed by auditors, this new type of assurance was described as more subjective, dependent on professional judgement and principle-based. It would rely on the expertise of accountants and auditors (as with the audit of financial statements) and would take into consideration some of the guidance provided by existing auditing standards.[7] To this end, the principles in ISA 570 – dealing with the auditor's responsibilities to consider a client's ability to continue as a going concern – and the related provisions of ISA 700 were referred to by respondents.[8] At the same time, however, this new type of assurance engagement would depend on the skills of, for example, those responsible for internal audit, corporate governance, sustainability and finance as well as the relevant industry specialists. The intention is not to express an opinion on the extent to which the integrated report complies with a given framework. 'Assurance' no longer takes the form of one-dimensional opinion (in the positive or negative form envisaged by ISAR 3000) but offers a type of independent panel review of the integrated report. This would draw on an integrated skill set and access to information and systems that underlie, but that are not necessarily described in detail within, the integrated report.

One audit partner described this as an 'integrated assurance model' capable of offering a 'new way of expressing an opinion on a new way of corporate reporting'. In particular, the proposed approach provides a single opinion on the integrated report, avoiding the complexity of having to communicate the interconnection between different types of assurance currently being provided by external auditors.

Several interviewees were, however, sceptical. Some agreed that their firms had the necessary expertise but that it would take time to 'build the capacity to roll this out on a large scale'. Others indicated that the 'integrated assurance approach' was reasonable, especially as external auditors are already accustomed to including non-accounting experts on their financial statement audit engagements. For these auditors, the primary concern was whether or not clients would be willing to bear the significant increase in fees that would be necessary to support a rigorous technical analysis of an integrated report. The most pertinent criticism of the 'integrated assurance model' was that it requires a change in stakeholders' understanding of 'assurance'.

Many interviewees concurred that it would be very difficult to explain how the 'assurance' provided by a panel review of the integrated report differs from the traditional assurance provided by an audit opinion on financial statements. In their view, the introduction of a new type of assurance would add significantly to already existing misconceptions about the function of the external audit and lead to undue reliance on the opinion of the integrated report. For this reason, there were a number of auditors who argued that 'assurance' should be limited to the auditor expressing an opinion on the financial statements and reading the information found in the integrated reports for information that contradicts or is inconsistent with the financial statements. As explained by an independent audit technical consultant: 'There needs to be one place for a reader to look…There cannot be more than one report from the auditor. It is not sensible to have a separate statement for the financial audit and a separate statement for the integrated report…If you have multiple types of assurance over different sections of the integrated report or an audit of the financial statements which gives one type of assurance and then another report which is not 'assurance' as we understand it but some type of technical assessment/viewpoint, nobody other than the handful of people who come up with the new standard is going to be able to understand it'.

In light of this criticism, interviewees were asked if a possible solution was to leave the audit of financial statements unaltered but rely on a different service provider to express an opinion on the integrated report.

3.2 COULD A DIFFERENT PARTY PROVIDE ASSURANCE?

Interviewees concurred that the emergence of an alternative service provider to give assurance on the integrated report would render the development and professionalisation of auditing irrelevant. An independent audit technical consultant argued that: 'Audit reporting has developed over more than 100 years. Why would you

7 In this sense, the model proposed by some respondents takes into account the fact that it is possible to obtain 'assurance' other than from the traditional test procedures performed by an independent external auditor (for additional information, see IIRC, 2015).

8 A technical review of these suggestions is beyond the scope of this report. For additional reading, refer to ISA570: Going Concern, ISA 700: Forming an Opinion and Reporting on Financial Statements (Revised) and ISA 701: Communicating Key Audit Matters in the Independent Auditor's Report.

> 'There are some investors who think they can just sit back and collect dividends and take short-term profits without ever applying their minds to the integrated report. Ironically these are the same people who are demanding the assurance of the reports'.

want to abandon that and start some other model?…This has been going on for 100 years and has gone through thousands of [legal] cases in order to develop where the lines are drawn and what it means and the respective responsibilities. Why throw away all that learning?'

In addition, several respondents argued that reassuring stakeholders of the integrity of the integrated reporting process was the main reason for calling for the assurance of an integrated report. In their view, it was questionable whether a newly created group of technical experts would command the same confidence as the audit profession.[9] As part of this discussion, interviewees quickly dismissed the use of any type of peer review in conjunction with external audit as a source of assurance. A lack of independence would mean that, at best, this would merely be part of the 'jigsaw assurance model' discussed in section 3.1.

3.3 A NEED TO INCREASE DIALOGUE AND STAKEHOLDER ENGAGEMENT

Finally, the researchers asked whether or not stakeholder engagement had a role to play in an integrated approach to assurance. Some of the auditors opined that institutional shareholders in South Africa were not taking their governance responsibilities seriously enough and that, if shareholders were more active, there might be no need for the assurance of the entire integrated report. In fact, one Big Four audit partner expressed a level of anger and irritation about the passivity of the shareholder community: 'If you're in a situation where you can't even trust the statements being made by the board of directors about your integrated reports and you have to have external audit that means that the shareholders haven't done their job properly. They need to get off their arses and fire the directors! There's nothing wrong with the integrated report and there is nothing that assurance is going to fix. The problem is apathy. There are some investors who think they can just sit back and collect dividends and take short-term profits without ever applying their minds to the integrated report. Ironically these are the same people who are demanding the assurance of the reports'.

This sentiment was shared by several auditors. In their view, the audit of financial statements provides a basis for assessing the financial viability of an organisation. It is the responsibility of the key stakeholders to engage with management during the AGM in order to assess how the company is managing each of the different types of capital outlined by the IIRC. Calls for the assurance of the integrated report were, therefore, seen as an effort to 'outsource' to the external auditor the necessary rigorous analysis of the integrated report by the investor or NGO.

Other interviewees were less critical. They disagreed with the assurance of the integrated report, not on the grounds that it can promote investor apathy, but because of a lack of information. According to these respondents, many companies were still developing their integrated reports and struggling to engage with stakeholders to determine precisely what information to include in their reports. Until this process was complete, the integrated report was described by some auditors as 'a work in progress', with the result that the debate on the assurance of the integrated report was premature. As explained by one audit partner: 'There is no point in auditors working out how to assure integrated reports' because 'companies have not figured out what they are going to include in them, how they are going to the collect the relevant information and what their stakeholders actually want'.

9 Some interviewees also discussed how inconsistencies between the audit opinion on the financial statements and the views expressed in this additional report could pose significant risks to the perceived independence and integrity of the external audit function and detract from the credibility of the audited financial statements.

4. Concluding discussion

The value of integrated reporting means that there is a case for making these reports the subject of an assurance engagement, but a number of technical challenges mean that this is currently impossible.

The value of integrated reporting means that there is a case for making these reports the subject of an assurance engagement, but a number of technical challenges mean that this is currently impossible. As a result, current practice is to express an opinion on the financial statements and to complement this with limited or reasonable assurance engagements on other 'elements' of the integrated report. Unfortunately, these engagements are limited to factual subject matter and exclude the forward-looking information and subjective management assessments that institutional investors are finding useful. The different opinions being included or referred to in the integrated report also give rise to the risk that users will misinterpret the nature and extent of the work done by the external auditor and conclude that the practitioner is attesting to the respective organisation's business model.

A possible way forward is to concentrate on the assurance of the systems, processes and controls used to produce the information included in the integrated report. Unfortunately, not all organisations have a sufficiently rigorous and well-documented control environment to allow for formal testing by the external auditor. In addition, there is no suitable framework, similar to COSO, that could be used to define the dimensions of the control environment necessary for effective integrated reporting.

As a result, several interviewees concluded that the profession should expand on existing practice. In the short-term, rather than attempting to develop new types of assurance, guidelines can be provided to clarify which parts of the integrated report should be assured (if possible) and the nature of the assurance given. In turn, this can be communicated in the integrated report to clarify the nature and extent of the work done by the external auditor and those parts of the document that remain untested. Concurrently, those charged with governance should consider how they are using a mix of internal controls, monitoring and different types of existing assurance (including external and internal audit) to ensure that the information being included in their integrated reports is of a high quality. Instead of developing a sophisticated assurance model for integrated reporting, it may be easier and more effective to describe this 'assurance matrix' to the reader of the integrated report.

In the long-term, some interviewees suggested that an 'integrated assurance model' can be developed. This will redefine assurance such that the objective is not to express an opinion on the extent to which the integrated report complies with the IIRC's framework. Instead, the intention is to offer a type of review,[10] similar to the outcome of a panel discussion, which gives reader the 'assurance' that, at a minimum, a diverse group of experts have considered the content of an organisation's integrated report.

This recommendation is, however, subject to important qualifications. Firstly, care must be taken that the development of a new assurance model does not add to the audit expectation gap. There is a possibility that, rather than providing meaningful assurance, this new assurance model could confuse stakeholders by creating a new form of professional opinion which they cannot distinguish from that given in the audit report on financial statements. Secondly, it is important that any new type of assurance complements the responsibilities of those charged with governance and the role of institutional investors, rather than serving as a substitute for these essential elements of the corporate governance system. Ultimately, before any radical change to existing assurance frameworks is considered, it is necessary to give companies the time to refine their reports, identify the information needs of their stakeholders and, most importantly, discern the extent to which those stakeholders require some form of external 'assurance'.

10 A 'review' here is *not* being used in the sense defined by International Standards on Review Engagements.

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