


**International Federation of Accountants**

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# Item 7

**Committee:** IAASB

**Meeting Location:** Lima

**Meeting Date:** March 7-11, 2005

## Sustainability – Feedback to Royal NIVRA EDs

### Objectives

1. To familiarize the IAASB with the Royal NIVRA exposure drafts regarding sustainability assurance and the use of experts in non-financial assurance engagements.
2. To identify major issues to be included in the IAASB's feedback to Royal NIVRA and the form of this feedback.

### Background

3. In April 2004, following publication of the International Framework for Assurance Engagements and ISAE 3000 "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information," the IAASB Steering Committee decided to set up a Sustainability Experts Advisory Panel (SEAP)<sup>1</sup>. Significant factors that led to that decision included:
  - Accounting firms provide approximately 50% of publicly available sustainability assurance reports globally.
  - 50% of reports issued by accounting firms cite no reporting criteria whatsoever.<sup>2</sup>
  - 55% of assurance reports issued by accounting firms do not mention any standards in accordance with which the engagement has been performed<sup>2</sup>.
  - Despite doubts about the objectivity of some of the data, available reports and surveys show that: sustainability reporting is becoming more mainstream to investment decisions, demand for assurance has increased, and these trends will continue.
  - A major issue is the lack of reporting criteria that are generally accepted by the accounting community as "suitable criteria" in terms of the International Assurance Framework and ISAE 3000.
4. The Global Reporting Initiative (GRI) Guidelines are the most commonly adopted reporting criteria for sustainability reports. A revised version of the GRI Guidelines (known as "G3") is due to be released in 2006. The primary charge of the SEAP to date

<sup>1</sup> In July 2004 the IFAC Board decided that the SEAP should also have the role of advising the Professional Accountants in Business (PAIB) Committee. Members of SEAP are noted in Appendix 1.

<sup>2</sup> The data upon which these findings are based is pre-ISAE 3000. The introduction of ISAE 3000 is expected to increase the proportion of reports issued by accounting firms that cite reporting criteria and engagement standards (ISAE 3000 itself).

has been to liaise with the GRI in an effort have G3 generally accepted by the accounting community as suitable criteria. To this end, the SEAP has:

- (a) Engaged directly with the Chair of the GRI Board<sup>3</sup> and the Chair of the GRI Stakeholder Council, and GRI staff;
  - (b) Nominated members for the GRI Technical Advisory Committee (TAC), which provides the GRI Board with high-level technical guidance on the Guidelines revision process, and working groups dealing with specific issues for the revision;
  - (c) Provided technical background material for the TAC about what is meant by “suitable criteria,” and how the accounting framework could relate to sustainability reporting; and
  - (d) Responded to a GRI exposure draft about determining a reporting organization's sustainability reporting boundaries.
5. The secondary charge of the SEAP is to advise on the development of guidance for assurance on sustainability reports. A working group of the Assurance Standards Board of Royal NIVRA has prepared two Exposure Drafts (EDs) that were published in late January 2005: ED 3410 “Assurance Engagements Relating To Sustainability Reports”, and ED 3010 “Practitioners Working With Subject Matter Experts From Other Disciplines On Non-Financial Assurance Engagements”. The intent of the IAASB with respect to these EDs is explained in the following paragraph, which Royal NIVRA were authorized to include in the Explanatory Memorandums accompanying the EDs:
- The International Auditing and Assurance Standards Board has expressed an interest in guidance for assurance on sustainability reports, and has established an external panel to advise it on possible next steps. This is an area where IAASB may wish to build on the efforts of other standard-setters. The IAASB has not reviewed this exposure draft and therefore is not in a position to endorse it in any way. However, IAASB staff has indicated that if this exposure draft is well received and results in comments from a wide range of respondents, the resulting standard may be one upon which IAASB would be able to build for wider international use. National auditing and assurance standard-setters and other interested parties from countries beyond The Netherlands are therefore encouraged to respond to Royal NIVRA on this exposure draft.
6. The IAASB Steering Committee agreed to set up a Task Force to analyze the Dutch EDs and develop a response to Royal NIVRA. Members of the Task Force are:
- Roger Simnett, chair
  - Denise Esdon
  - Rogério Gollo
  - Cedric Gelard
7. Amongst other things, the analysis will look closely at any proposals in the Royal NIVRA EDs that are not consistent with the Assurance Framework and ISAE 3000, in accordance with the statement made by the IAASB when those documents were approved in December 2004: “*As the provision of broader assurance services is an evolving field, the IAASB intends to keep the practical implementation of the Framework and ISAE 3000 under review.*” This analysis is a part of that review and is expected to prove beneficial not only in terms of developing a response to Royal NIVRA, but also in informing the IAASB of implementation issues with the Framework and ISAE 3000.

<sup>3</sup> Two of the members of the GRI Board are also members of the SEAP: Roger Adams and Peter Wong.

**Process for Generating IAASB Feedback**

8. English versions of the Royal NIVRA EDs were distributed to the SEAP and the Task Force when they became available on 25 January 2005, allowing only a short time for a review and the preparation of agenda papers. SEAP was asked to provide initial comments by 31 January (less than 1 week), which were collated and discussed at a Task Force conference call on 1 February.
9. The response date for the Royal NIVRA EDs is 31 July. The intention of the agenda item at this meeting is for the IAASB to become familiar with the EDs and to identify, and provide guidance to the Task Force on major technical issues and the form of feedback to Royal NIVRA. A fuller analysis and draft response will be prepared by the Task Force based on the input of the IAASB, and with advice from the SEAP, for discussion at the June IAASB meeting.

**Major Issues Identified by the Task Force and SEAP**

10. The following issues have been identified by the Task Force, with advice from the SEAP, for consideration by the IAASB.

**A. SCOPE OF GUIDANCE**

- ED 3410.07 defines a sustainability report as: “a report in which a reporting organization provides information to relevant targeted groups of stakeholders and accounts for the economic, environmental and social aspects of the organization and the effects of its business activities on society. The sustainability report consequently offers a platform for dialogue between the organization and its stakeholders”.
- Should the guidance also apply to reports that only cover one or 2 components of sustainability, e.g., occupational health and safety or environmental performance?
- Need the sustainability report be “stand alone”, or can it be, e.g., part of an entity's annual report?
- The EDs are premised on an “assertion-based” approach – should direct reporting engagements also be contemplated?

**B. SUITABILITY OF CRITERIA**

- ED 3410.46-50 offer guidance about the suitability of criteria in the context of a sustainability engagement. Is that guidance consistent with the generic guidance in the Assurance Framework and ISAE 3000, and is it specific enough to result in consistent decisions by practitioners?
- ED 3410.09 states that “The primary responsibility of the management and the availability of reporting criteria do not detract from the fact that the practitioner (the team) should independently – where necessary supplementary to the reporting criteria applied – set certain minimum requirements for the content of the sustainability report”. It then sets minimum criteria. Is this approach consistent with the IAASB's view of the role of assurance standards and assurance practitioners?
- Should the guidance be linked to a particular set of reporting criteria, e.g. the GRI Guidelines?

**C. SCOPE OF ENGAGEMENT**

- Determining the reporting entity: ED 3410 does not appear to envisage the possibility that sustainability reporting boundaries may extend beyond the normal scope of consolidation (ED 3410.42) to include, for example, business partners and entities in the supply chain. The GRI's (draft) “Boundary Protocol” addresses such issues.

- Limitations: ED 3410.17-20 discuss situations in which an engagement is limited in scope to certain elements of the sustainability report. Is the guidance on this issue adequate in terms of engagement acceptance, and reporting. There will likely be an expectation that the practitioner is in some way satisfied with “other information” if it is intermingled with the assured information – is the practitioner’s responsibility in these situations greater than with respect to other information in documents containing audited financial statements (ISA 720)?

#### D. STAKEHOLDER ENGAGEMENT

- The definition of a sustainability report (above) includes reference to “relevant target groups of stakeholders”. “Target groups of stakeholders” is itself defined in ED 3410.07. There is a raft of issues related to stakeholder identification and stakeholder engagement. For example:
  - Is the presumption in ED 3410 that stakeholders are synonymous with the intended users of the report justified when in practice they are not always the same?
  - Is it appropriate to use the notion of "average representatives" of each target stakeholder group to determine what information requirements are justified. Is an average representative one who holds a middle ground view on an issue, or one who holds a scientifically established view, or one who is in the majority? What about those marginalized stakeholders whose voices are rarely heard on an issue, even if valid?
  - To what extent does the practitioner need to be directly involved in stakeholder engagement to meet requirements such as ED 3410.78 “The practitioner (the team) should ascertain whether the most relevant stakeholders are actually classified as the target group (of the report) by the reporting organization. He/she should then form an opinion on the question of whether the justified information requirements of the average representatives of each targeted group of stakeholders have been met, in conjunction with the materiality of the various subject matters and the risks of errors or omissions in the sustainability report”.

#### E. MATERIALITY AND COMPLETENESS

- Related to the preceding point regarding stakeholders, are materiality and completeness. Identifying stakeholders and their needs is central to decisions about materiality and completeness – is there sufficient guidance for practitioners to make consistent decisions on these important issues, e.g.:
  - Does the guidance on materiality in ED 3410.25-36 adequately address the fact that much of the information in a sustainability report will be qualitative rather than quantitative; is qualitative information always auditable; and how does “materiality” relate to the concepts of “significance” (e.g., ED 3410.117 uses the term “material significance”) and “relevance” (e.g., as used in ED 3410.10)?
  - ED 3410.17 requires a judgement in some circumstances about whether there is “complete information ... included in the report on all the subjects considered essential for the targeted groups of stakeholders”, and ED 3410.20 states in blackletters that “The engagement should always focus partly on the completeness aspects. This includes the completeness of the targeted groups of stakeholders, the report content relevant to these groups and the performance indicators and disclosures provided”?

## F. JOINT RESPONSIBILITY

- Much of ED 3010 is concerned with explaining 3 models for determining responsibilities and allocating work between the practitioner and a subject matter expert from another discipline, including “multidisciplinary cooperation under joint responsibility” (Model 2 see ED 3010.23-30). ED 3410 also offers considerable guidance on this matter (e.g. ED 3410 Appendix 2). Should joint responsibility be allowed? If so, is the guidance associated with each model appropriate?
- The EDs do not address in detail issues that would arise if the practitioner performing the sustainability assurance engagement is: (a) not the entity's financial statement auditor (e.g., reliance on work performed by the auditor with respect to the control environment), or (b) from a quite separate engagement team within the auditor's firm (e.g., what expectation should there be that the sustainability engagement team will have access to information obtained by the audit team?).

## G. REASONABLE ASSURANCE V. LIMITED ASSURANCE – WORK EFFORT

- ED 3410.07 contains a definition of a “review” and distinguishes it from an “audit”. ED 3410.105-108 elaborate further. Is the distinction drawn in the ED consistent with the difference between “reasonable assurance” and “limited assurance” engagements in the Assurance Framework?
- Are the sections of ISA 3410 that deal with evidence gathering procedures adequate to ensure consistency among practitioners when faced with similar circumstances?
- The Assurance Framework contemplates the possibility of an ISAE identifying particular procedures that, to an extent, “fix” the nature, timing and extent of work for an engagement, in the same way ISRE 2400, “Engagements to Review Financial Statements” establishes that sufficient appropriate evidence for reviews of financial statements is obtained primarily through analytical procedures and inquiries. Are sustainability reports sufficiently homogeneous that such an approach should be attempted for reasonable assurance and/or, in particular, limited assurance.

## H. REPORTING

- Key reporting issues (see ED 3410.120-141) include:
  - The appropriateness of short-form versus long-form reports.
  - The appropriateness of “stakeholders” as the addressee of the report, as recommended in ED 3410.124?
  - The appropriate expression of the conclusion (or multiple conclusions), including distinguishing between “reasonable assurance” and “limited assurance”, the wording of qualified conclusions and emphases of matter, and the use of “true and fair” and “present fairly”.
  - ED 3410 allows for an assurance report in which the practitioner has obtained reasonable assurance on some elements of the sustainability report, and limited assurance on others. Is this acceptable?
  - ED 3410.135 (see also footnote 5 on page 6) leaves open the possibility of a negative form of expression for an audit engagement. Is this acceptable?
  - Describing the scope of the engagement, including any limitations, and identifying the information that has been examined, including any limitations.
  - Describing the nature, timing and extent of procedures undertaken, including where appropriate reference to experts on the assurance team, and the practitioner's involvement with stakeholder engagement.

- Ensuring the presentation of the report effectively separates any recommendations from the conclusion (also, perhaps, the independence implications of making public recommendations).

#### **I. OTHER MATTERS**

- Other matters include:
  - Whether the level of detail in the EDs is consistent with ISAE drafting style?
  - Whether matters such as fraud should be addressed (see ED 3410.45)?
  - Whether there is sufficient guidance regarding topics such as documentation, quality control, subsequent events and communication with those charged with governance, and/or on the application of relevant ISAs to sustainability engagements?
  - Whether terminology use is consistent with the Assurance Framework (e.g. subject matter versus subject matter information) and ISAs (e.g. ED 3410.07 “irreplaceable internal controls”)?

#### **Material Presented**

- ED 3010 “Practitioners Working With Subject Matter Experts From Other Disciplines On Non-Financial Assurance Engagements” (Electronic file name: Agenda Item 7.1 – Dutch ED Standard 3010)
- ED 3410 “Assurance Engagements Relating To Sustainability Reports” (Electronic file name: Agenda Item 7.2 – Dutch ED Standard 3410))
- Explanatory Memorandum for ED 3010 (Electronic file name: Agenda Item 7.3 – Expl Memorandum to 3010))
- Explanatory Memorandum for ED 3040 (Electronic file name: Agenda Item 7.4 – Expl Memorandum to 3410))

#### **Action Requested**

The IAASB is requested to review the EDs to identify major issues likely to be of concern, and provide the Task Force with guidance about the categories of comments or specific comments, and the form of feedback to NIVRA.

**Appendix 1**

**Sustainability Experts Advisory Panel**  
**Membership matrix (January 2005)**

		<b>Firm or other</b>	<b>Active in member body</b>	<b>Other relevant affiliations</b>	<b>Region</b>
<b>1</b>	<b>Roger Simmett (Chair)</b>	Academia	CPA Australia	IAASB independent member	Oceania
<b>2</b>	<b>Peter Wong</b>	Ex Deloitte	Hong Kong ICPA	<ul style="list-style-type: none"> <li>GRI Board</li> <li>Ex IFAC Board</li> </ul>	Asia
<b>3</b>	<b>Roger Adams</b>	ACCA	ACCA	<ul style="list-style-type: none"> <li>GRI Board</li> <li>AccountAbility Council</li> </ul>	UK
<b>4</b>	<b>Alun Bowen</b>	KPMG		AccountAbility Technical Committee	UK
<b>5</b>	<b>Nancy Kamp-Roelands</b>	EY	Royal NIVRA	<ul style="list-style-type: none"> <li>FEE Sus. Assurance Group</li> <li>NIVRA Standard Setting Group on Sus. Assurance</li> </ul>	Europe
<b>6</b>	<b>Alan Willis</b>	CICA	Canadian ICA	Chair, former GRI Verification WG	Canada
<b>7</b>	<b>Lars-Olle Larsson</b>	KPMG	FAR (Sweden)	Chair, FEE Sustainability Assurance Group	Scandinavia
<b>8</b>	<b>Susan Todd</b>	Solstice Sustainability Works Inc		<ul style="list-style-type: none"> <li>AccountAbility practitioner</li> <li>GRI Social Indicators Advisory Group</li> </ul>	Canada
<b>9</b>	<b>Robert Langford</b>	ICAEW	ICA England & Wales	<ul style="list-style-type: none"> <li>FEE Sus. Assurance Group</li> <li>GRI Boundaries Working Group</li> </ul>	UK
<b>10</b>	<b>Beth Schneider</b>	Deloitte	American ICPA	Chair, former AICPA/CICA Task Force Sustainability	US
<b>11</b>	<b>Takeshi Mizuguchi</b>	Academia	Japanese ICPA	Advisory Committee of GRI Forum Japan	Asia
<b>12</b>	<b>Fatima Reyes</b>	Consultant	Philippines ICPA	UN Division for Sustainable Development's Experts Working Group on EMA	Asia
<b>13</b>	<b>Johan Piet</b>	Consultant	Netherlands	<ul style="list-style-type: none"> <li>Chair, FEE Sustainability Group</li> <li>AccountAbility Technical Committee</li> </ul>	Europe
<b>14</b>	<b>Preben Soerensen</b>	Deloitte	Denmark	AccountAbility Technical Committee	Scandinavia
<i>IFAC Staff</i>					
	<b>Michael Nugent</b>	IAASB	ICA and CPA Australia	<ul style="list-style-type: none"> <li>GRI Tech Advisory Committee</li> <li><a href="http://www.accountability.org.au">www.accountability.org.au</a></li> </ul>	Oceania
	<b>Paul Thompson</b>	PAIB	ICA England & Wales	Centre for Social and Environmental Accounting Research (CSEAR)	US/UK

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