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Mr. Matthew Waldron   3 February 2017
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Discussion Paper, *Supporting Credibility and Trust in Emerging Forms of
External Reporting: Ten Key Challenges for Assurance Engagements*

Dear Mr. Waldron

Ernst & Young Global Limited, the central coordinating entity of the Ernst & Young organization,
welcomes the opportunity to offer its views on the Discussion Paper, *Supporting Credibility and Trust in
Emerging Forms of External Reporting: Ten Key Challenges for Assurance Engagements*, issued by the
International Auditing and Assurance Standards Board (IAASB).

We are pleased that the IAASB has established the Integrated Reporting Working Group (IRWG) to
provide thought leadership in the important area of emerging forms of external reporting (EER), and
we commend the IRWG on its outreach to date and its analysis of the challenges that practitioners –
and preparers of information – are facing. As the discussion paper points out, this is an evolving area,
and there are many issues and challenges to overcome in the coming years. In this regard, the
discussion paper provides helpful background to EER and the issues related to providing assurance
over EER, and is a useful educational resource.

In considering the questions the IAASB poses, we have a number of overall observations, which are set
out below, in *1. Overall considerations*. The responses to the specific questions are set out in *2.
Responses to specific matters on which the IAASB is seeking comments*.

1. Overall considerations

A. Continuing outreach activities

As noted above, we commend the IAASB on the outreach activities the IRWG has undertaken to date.
We believe these activities are very valuable, and we encourage the IAASB to continue with these
activities.

In addition, we would urge the IAASB to work with those bodies developing EER frameworks that have
momentum to become generally accepted. As an evolving area, with a patchwork of competing
emerging EER frameworks, the IAASB can add considerable value by encouraging refinement and
acceptance of appropriate frameworks and underlying standards.

By having a voice in the development process, the IAASB can also help to encourage alignment and/or
consolidation of competing frameworks, which will lead to more robust standards that can be endorsed
as generally accepted. For example, we recognize the value of the International Integrated Reporting
Framework which was issued in December 2013, but we also believe that the lack of consistent
standards underpinning that framework does not enable the preparation of consistent, comparable
integrated reports. In addition, looking at integrated reports that have been prepared by companies, it

is clear that there is not a common understanding among report preparers of what is expected of an integrated report.

Managing the expectations gap

Given the expectations of the broad group of stakeholders interested in EER, as well as the IRWG's finding that many stakeholders want some form of "assurance" over the EER without necessarily appreciating the IAASB's and practitioners' use of this term, we believe there is a very real danger of an expectations gap developing.

The IAASB is well placed to dispel misconceptions, educate stakeholders, and explain the meaning of assurance. This is not a one-off exercise – to protect the integrity of the IAASB's standards, and particularly that of ISAE 3000 (Revised) and ISA 720 (Revised), outreach activities need to be ongoing, because as EER evolves, new stakeholders in an entity's reporting activities are likely to emerge.

One important concept, which we believe is not well understood by non-practitioners is that: "If the underlying subject matter is not appropriate for a reasonable assurance engagement, it is also not appropriate for a limited assurance engagement" (Page 27, paragraph 77). We welcome the IAASB's highlighting this, and note the importance of continuing to make sure the concepts of "reasonable" and "limited" assurance are well understood. In this regard, non-authoritative implementation guidance that supports the efforts of national standard setters would be helpful.

The IAASB also has a role to help practitioners:

► Explain assurance in the context of EER and when it might be an appropriate service, thereby protecting the integrity of the assurance services provided to the market.

► Better explain to management and those charged with governance when an alternative service may be better at enhancing credibility and trust in EER. While not offering limited or reasonable assurance, services such as agreed-upon procedures or "gap analyses" may provide what management needs in the circumstances.

Although it is true, as IAASB suggests, that (Page 23, paragraph 59) "The most common of these [engagements] currently performed in relation to EER reports are assurance engagements", we believe that the volume of such engagements is currently low. While this is the case, the IAASB has a window of opportunity to encourage robust application of ISAE 3000 (Revised), and to clearly articulate the benefits of other types of professional services that might be more appropriate in the circumstances of the entity.

Adding value

We believe that the IAASB can add value to the EER evolution by working with other relevant bodies. One initiative that may be worth further consideration is The Corporate Reporting Dialogue (the Dialogue). The Dialogue comprises a number of well-established and widely accepted standard setters in their respective areas. This initiative – designed to "respond to market calls for greater coherence, consistency and comparability between corporate reporting frameworks, standards and related requirements" - includes key financial reporting standard setters (the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB)), sustainability standard setters (including the Global Reporting Initiative and Sustainability Accounting Standards Board), the

International Organization for Standardization (ISO) and the International Integrated Reporting Council (IIRC).

Engagement by the IAASB with these standard setters will help to support credibility and trust through effective governance and control – however, responsibility for credible EER reports does not lie primarily with assurance practitioners but with management and those charged with governance, i.e., the report preparers. It may also help the IAASB anticipate new professional services that may be needed in the future, as EER frameworks and standards mature.

In addition, the Dialogue has recently issued a paper on common principles of materiality between the member bodies' frameworks and standards, which is a topic of paramount importance to assurance practitioners.

B. Exploring the subject matter

The Discussion Paper uses a very broad definition of EER comprising several types of information. Because the definition of EER is currently so broad, we believe it is difficult to develop generic guidance to suit all types of EER.

In addition, we have long been concerned about the issues around providing assurance on integrated reports, as we believe that clarity is needed on how assurance can be given on a report containing a mixture of EER without users taking unwarranted reliance from the practitioner's report.

Although we are aware that the interaction between traditional financial reporting and EER is receiving the attention of preparers, regulators and users, our concern relates to ensuring a clear distinction between audited information, reviewed information and information not subject to the assurance process. It is important to consider how to communicate the practitioner's opinions on these three "sets" of information when that information is embedded in a single report so as to avoid confusion or unwarranted reliance.

We believe that there is considerable merit in sub-dividing the definition to identify a number of specific types of information, and narrowing the focus to develop appropriate and relevant guidance related to each of those information types.

One approach might be to adopt the key principles of existing frameworks that are more widely accepted against which to "test" standards and guidance. Another, though similar, approach, might be to set two "extremes" on the spectrum of EER: one being a report on a single element (and the guidance for practitioners may perhaps be readily adapted from ISAE 3410) and the other being an integrated report, and develop guidance for practitioners for each of these two scenarios. By doing so, the practitioner would have guidance explaining the issues, risks and procedures to consider when reporting on a narrow set of parameters (i.e., one element measured using a publicly available set of KPIs) and those to consider when reporting on a very broad information set (i.e., one that encompasses multiple elements, estimates, narrative information, different units of measurement, information not capable of assurance, etc.).

Both approaches involve defining EER more precisely than is currently done in the Discussion Paper, which we note argues against endorsing specific EER frameworks in favor of framework neutrality. However, with respect to EER, we believe this argument is premature.

The International Standards on Auditing (ISAs) are "framework neutral", but, in reality, they have been developed against a "generic" financial reporting framework (i.e., the principles and objectives of financial reporting frameworks are well understood even if specific requirements differ) and a common measurement unit (i.e., currency). This general understanding provides a fundamental underlying foundation on which auditing standards can be developed. Although note disclosures are often qualitative in nature, the financial reporting frameworks set clear objectives or specific requirements for those disclosures.

However, no single, widely accepted definition of EER information exists, nor does a generally accepted "EER Framework". So, in reality, "framework neutrality" in an EER context results in an absence of agreed fundamental underlying principles. By selecting a representative EER framework or information set, principles and guidance developed by the IAASB can be tested against those underlying principles, and then extended, if necessary, to encompass other frameworks or information sets.

C. Materiality

We believe that the IAASB should prioritize the topic of materiality and develop implementation guidance, because this is vital to the ability of the preparer to produce an appropriate report, as well as to the practitioner in providing assurance.

First, there is an absence of common units of measurement, especially as some EER frameworks require consideration of "connectivity" and "capitals other than financial capital". Absence of common units of measurement implies that there could be multiple levels of materiality. "Connectivity" and "capitals other than financial capital" imply that trade-offs exist between capitals. These could be difficult to evaluate if different levels of materiality in different units of measurement are used to gather and report the relevant information.

Second, the discussion paper introduces the concept of the "entity's materiality process". When an auditor considers materiality in an audit, it is from a user's perspective, and the auditor uses materiality to evaluate whether the financial statements are materially misstated. The auditor does not explicitly evaluate or report how the entity determines what it considers to be material.

For EER, as the information may not previously have been gathered and/or not subject to a standardized set of principles/standards, users may wish to know that the "correct" data is being gathered. The discussion paper suggests that practitioners may be called upon to evaluate the entity's "materiality process", either as a part of determining whether suitable criteria exist or as a separate engagement.

Finally, we believe that the IAASB should define the concept of a "material misstatement" (both as to the meaning of "material" and "misstatement") in EER reporting. The discussion paper uses terminology, such as "material misstatements", that has its roots in financial reporting and auditing. The requirement that "The practitioner is required to obtain sufficient appropriate audit evidence about whether the subject matter is free from material misstatement ..." is more difficult to achieve in an EER assurance engagement than in a financial statement audit. For example:

► How does a practitioner define what is material in an immature EER framework, especially as different frameworks have different definitions of materiality? Further, how does a practitioner define and evaluate a misstatement, especially in a subjective area such as reporting on governance or human capital?

► Once information has been defined as "material", can some information be "most material" (a commonly used phrase by EER report preparers seeking to prioritize the contents of the EER report)? We have concerns about the use of the term "most material", since the omission of any material information could render the report misleading.

We are, however, pleased that the discussion paper reminds readers that "professional judgments about materiality are not affected by the level of assurance; materiality reflects the user perspective, therefore what is material is the same in both limited and reasonable assurance engagements".

D. Internal control

We are not convinced by the discussion paper's assertion that (Page 20, para 50) "Management, and in some jurisdictions, TCWG are responsible for establishing internal control as necessary to ensure that the information in the EER report is reliable and available on a timely basis". We consider that, at present, local laws and standards currently require management and those charged with governance to have internal control sufficient to prepare financial statements – not necessarily an EER report. As a result, as IAASB acknowledges, internal control in the area of EER is often informal, and entities use workarounds to obtain and process the EER information.

In addition, the boundaries to an EER report, especially when EER relates to disclosure of information and outcomes beyond the physical boundaries of the entity or group (e.g., supply chain, suppliers' workforce human rights), might affect the internal control over the EER information.

We therefore suggest that a priority for EER standard setters would be to establish robust principles and guidance for entities to refer to as they implement systems to capture and process EER – the COSO Framework may be a valuable resource in the development of guidance in this area. The IAASB might, in this case, have a role in encouraging cooperation and coordination between standard setters.

The Supplementary Paper envisages that it might be feasible for a practitioner to report on "design, operation and effectiveness" of an EER reporting system, and whether it is operating "effectively for a period". However, as the IAASB does not yet have a standard on reporting on internal control over financial reporting, there are currently no principles to draw on in developing guidance for the less formal EER systems. We therefore submit that developing such an assurance service would be a lower priority for the IAASB at this time.

E. Reporting matters

The supplementary paper discusses reports and suggests example wording. We believe that considering reporting issues and developing example assurance reports is premature until the other issues outlined above have been addressed.

We also note that paragraph 99 suggests that communicating "key assurance matters" in assurance reports may become relevant in the future. Although it is possible that this concept may become important in the future, we would caution against the introduction of such further disclosures before the foundational EER report has been agreed. In addition, the use of the concept of key assurance matters should be considered for assurance engagements holistically, not just for those related to EER information.

2. Responses to specific matters on which the IAASB is seeking comments

Q1. Section III describes factors that enhance the credibility of EER reports and engender user trust.

 a. Are there any other factors that need to be considered by the IAASB?

 b. If so, what are they?

We believe that the following additional topics are worthy of further consideration by the IAASB, since these topics, though the responsibility of management and those charged with governance, have an impact on the credibility of EER reports:

- ▶ Measurement of the EER, and the development of appropriate KPIs
- ▶ Development of robust assumptions for forward looking information
- ▶ Data collection of relevant information and KPIs
- ▶ Development of EER frameworks that are generally accepted

Q2. Sections II and IV describe different types of professional services that are either currently performed or could be useful in enhancing credibility and trust.

 a. Are there other types of professional services the IAASB needs to consider, that are, or may in future be, relevant in enhancing credibility and trust?

 b. If so, what are they?

The Discussion Paper sets out various different types of EER, and notes that EER may have the characteristics of estimates, forward-looking information or narrative information. In addition, although it may be quantitative, it may be expressed in units of measurement other than currency. Certain EER, such as greenhouse gas emissions reporting, may be confined to one type of EER. However, other EER may be in the form of, for example, an integrated report, which contains information with all the above characteristics in one report.

Therefore, although ISAE 3000 (Revised) provides standards that may be applied for all types of assurance engagements, it seems likely that specific standards that address the above different types of EER will be required – this may require standards that address reasonable/limited assurance on specific subject matters as well as standards that address different types of service, such as agreed upon procedures. Guidance that extends existing International Standards to address all the above types of information would be helpful – for example, extending the principles set out in ISA 540 (Estimates) or in ISAE 3400 (Prospective information) to EER with those characteristics. In addition, addressing the provision of agreed upon procedures to EER, or at least to non-financial information, would also be helpful – in this regard, the IAASB's public consultation on AUP is very timely.

Q3. *Paragraphs 23–26 of Section II describe the responsibilities of the auditor of the financial statements under ISA 720 (Revised) with respect to the other information included in the annual report.*

    a. *Is this sufficient when EER information is included in the annual report; or*

    b. *Is there a need for assurance or other professional services, or for further enhancement of the responsibilities of the financial statement auditor, to enhance credibility and trust when EER information is in the annual report?*

Given how broad the definition of EER is, we have concerns about applying ISA 720 (Revised) as a general rule to enhance credibility and trust in EER information in an annual report, and particularly with respect to non-financial EER. The IAASB has been very careful and thorough in defining the scope and use of its standards, which have been developed with rigorous due process. As such, we would caution against extending the use of the IAASB's standards without applying the same level of rigor to determining whether the extension is appropriate – the safeguarding of the ISA "brand" and the underlying quality of the IAASB's standards is important.

ISA 720 (Revised) clearly states that the auditor's responsibilities do not constitute an assurance engagement on other information, nor impose an obligation on the auditor to obtain assurance about the other information. Rather, the stated objectives of ISA 720 (Revised) are to consider whether there is a material inconsistency between the other information and both the financial statements and the auditor's knowledge obtained in the audit, and to respond appropriately when the auditor identifies such material inconsistencies or becomes aware that the other information appears to be materially misstated. Although the auditor may take appropriate action that results in the other information being amended or the material inconsistency or misstatement being brought to the attention of the user of the financial statements, this does not amount to an opinion on the other information, even if it is of a financial nature, and the auditor's opinion should not be extended to include "implied" assurance.

As the objectives are stated in terms of an audit of the financial statements, the auditor is likely to be able to consider only the other information that has a financial aspect to it – even with knowledge of the business the auditor may have obtained in the audit, other information about, for example, greenhouse gas emissions or human resource matters would appear to be beyond the intended scope of ISA 720 (Revised).

Although we acknowledge that some EER relates to financial information that may be reported within the financial statements – and this would clearly fall within the auditor's responsibilities for the financial statement audit – much EER is derived from non-financial systems that would be beyond the scope of the auditor's work on the financial statements. We therefore believe that further enhancement of responsibilities of the financial statement auditor to encompass EER would be inappropriate, given the diverse range of EER, the many competing EER reporting frameworks, and the current lack of maturity in both the frameworks and entities' systems for identifying, measuring and gathering the information.

Q4. *Section IV describes the different types of engagements covered by the IAASB's International Standards and Section V suggests that the most effective way to begin to address these challenges would be to explore guidance to support practitioners in applying the existing International Standards for EER assurance engagements.*

 a. *Do you agree?*

 b. *If so, should the IAASB also explore whether such guidance should be extended to assist practitioners in applying the requirements of any other International Standards (agreed-upon procedures or compilation engagements) and, if so, in what areas? (For assurance engagements, see Q6-7)*

 c. *If you disagree, please provide the reasons why and describe what other action(s) you believe the IAASB should take.*

We agree that IAASB should explore guidance to support practitioners in applying existing International Standards, extended to cover the standards relating to agreed-upon procedures, forward looking information, and applying the ISA 805 or ISA 810 standards to other financial information that is derived from or summarizes the financial information presented in the financial statements.

In particular, non-authoritative implementation guidance, focused on clarifying ISAE 3000 (Revised), to support practitioners and national standard setters would be helpful.

Q5. *The IAASB would like to understand the usefulness of subject-matter specific assurance standards. ISAE 3410, a subject matter specific standard for assurance engagements relating to Greenhouse Gas Statements, was issued in 2013.*

 a. *Please indicate the extent to which assurance reports under ISAE 3410 engagements are being obtained, issued or used in practice by your organization.*

 b. *If not to any great extent, why not and what other form of pronouncement from the IAASB might be useful?*

We note that assurance reports under ISAE 3410 are sought on a voluntary basis by entities from a variety of industry sectors. However, the incidence of use of ISAE 3410 varies by jurisdiction, and depends on local requirements and industry practice within those jurisdictions.

In jurisdictions where there is a government or regulatory focus on recognition and reporting of greenhouse gases, ISAE 3410 has been found to be very useful. Consequently, where there is a need to respond to a regulatory requirement, subject-matter specific assurance standards are particularly helpful.

Q6. *Section V suggests it may be too early to develop a subject-matter specific assurance engagement standard on EER or particular EER frameworks due to the current stage of development of EER frameworks and related standards. Do you agree or disagree and why?*

Please refer to *1. Overall considerations, B. Exploring the subject matter* above.

We agree that it is too early to develop standards on EER, but we believe that, as a starting point, guidance on how to apply existing standards to specific types of EER would be helpful. However, in providing such guidance, we suggest that the characteristics of different types of EER be articulated, and the guidance be addressed explicitly to those characteristics.

Q7. Section V describes assurance engagements and the Ten Key Challenges we have identified in addressing EER in such engagements (see box below) and suggests that the most effective way to begin to address these challenges would be to explore guidance to support practitioners in applying the IAASB's existing International Standards to EER assurance engagements.

a. Do you agree with our analysis of the key challenges?

b. For each key challenge in Section V, do you agree that guidance may be helpful in addressing the challenge?

c. If so, what priority should the IAASB give to addressing each key challenge and why?

d. If not, why and describe any other actions that you believe the IAASB should take.

e. Are there any other key challenges that need to be addressed by the IAASB's International Standards or new guidance and, if so, what are they, and why?

We agree with the IAASB's analysis of the key challenges, including that several of the challenges require further conceptual analysis and research. As we have noted above, we believe that the focus of the IAASB should be to work with other bodies to undertake further research to define EER more precisely, to develop and refine robust EER frameworks, and to address materiality.

We do, however, recognize that additional guidance would be helpful for practitioners asked to perform an assurance engagement, and recommend providing guidance about the risks the practitioner should consider before performing an assurance engagement, as well as whether another form of service would be appropriate in the circumstances.

We would also add two further challenges:

► It is important that management and those charged with governance have the necessary skill and competence to identify relevant information, to develop systems to gather that information, and to establish robust internal control over those systems. Although the competence of the practitioner is highlighted as a challenge, we believe that the competence of management and those charged with governance is of equal importance.

► In the absence of the formal systems to identify, gather and control the information needed for EER, obtaining relevant and reliable information is a key challenge. Although this underpins several of the Ten Challenges the IAASB has identified, we believe that obtaining relevant and reliable information is of sufficient importance to warrant being identified separately from the other challenges.

We appreciate that these two additional challenges relate to the preparation of the report by the entity, rather than relating to the practitioner's assurance engagement. However, we believe that these challenges are of significant importance because these are necessary "pre-conditions" for an assurance engagement, and, as described above, that the IAASB has an outreach role to help address these.

Q8. The IAASB wishes to understand the impact on potential demand for assurance engagements, if the Ten Key Challenges we have identified can be addressed appropriately, and in particular whether:

  Ø *Doing so would enhance the usefulness of EER assurance engagements for users*

  Ø *Such demand would come from internal or external users or both*

  Ø *There are barriers to such demand and alternative approaches should be considered*

  a. *Do you believe that there is likely to be substantial user demand for EER assurance engagements if the key challenges can be appropriately addressed?*

  b. *If so, do you believe such demand:*

   i. *Will come from internal or external users or both?*

   ii. *Will lead to more EER assurance engagements being obtained voluntarily or that this outcome would require legal or regulatory requirements?*

  c. *If not, is your reasoning that:*

   i. *EER frameworks and governance will first need to mature further?*

   ii. *Users would prefer other type(s) of professional services or external inputs (if so, what type(s) – examples of possible types include further responsibilities for financial statement auditors under ISA 720; agreed-upon procedures reports; compilation reports; other types of professional services or other external inputs)?*

   iii. *There are cost-benefit or other reasons (please explain)?*

If the key challenges can be appropriately addressed, then it is likely that there will be additional user demand for EER assurance engagements, as well as other types of professional services, including the use of agreed-upon procedures and, possibly, ISA 805 to report on the financial aspects of an integrated report. However, as discussed above, we believe that overcoming the challenges is the work of several years, and the nature of EER is such that the current piecemeal approach is likely to persist for some time.

We expect that such demand would come from both internal and external users, and that the "early adopters" will seek to obtain EER assurance engagements voluntarily. However, preparing the information and seeking assurance on the resulting report does incur costs, and we therefore consider that those seeking assurance voluntarily will remain a minority of organizations. If assurance is considered necessary for all entities, regulatory involvement will be necessary.

Q9. The IAASB would like to understand stakeholder views on areas where the IAASB should be collaborating with other organizations in relation to EER reporting. For which actions would collaboration with, or actions by, other organizations also be needed?

As noted above, we believe that it is important for the IAASB to collaborate with other organizations in relation to EER reporting. Although the Corporate Reporting Dialogue is relatively new, it includes a number of recognized financial reporting and non-financial reporting standard setters, and therefore provides a forum that can drive change. We recommend that IAASB consider working with this group.

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We would be pleased to discuss our comments with members of the IAASB or its staff. If you wish to do so, please contact Bob Landwehr, Global Deputy Vice Chair, Global Professional Practice (bob.landwehr @uk.ey.com).

Yours sincerely

Ernst + Young Global Limited