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DEAKIN-AUASB SUSTAINABILITY ASSURANCE RESEARCH WORKSHOP

Research informing the AUASB's Sustainability Assurance Agenda

December 2023

Editors of this research report

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Disclaimer

The views expressed in this research report do not represent formal views of the Board, which are established only through appropriate due process. The Board respects the independence of the researchers and has not attempted to influence the research or findings in any way.

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Foreword

The AUASB recognises the importance of relevant and reliable evidence and academic research to inform our standard-setting activities. The AUASB's Evidence Informed Standard Setting (EISS) strategy directs our activities to ensure that standard-setting deliberations and decisions are informed by relevant and reliable evidence and research. The AUASB encourages and supports research that provides evidence on the current audit and assurance environment that informs our current and future agenda.

In October 2023 we engaged with the academic community through the Deakin-AUASB Sustainability Assurance Research Workshop. As we prepare for the proposed introduction of mandatory climate reporting and assurance, this Workshop served as an important element in our collaborative efforts, fostering discussion on research that can inform our standard-setting activities.

The Workshop involved a presentation of the AUASB's agenda and priorities as they relate to sustainability assurance and the AUASB's information gathering activities, presentations from academics on existing research and its possible implications to the AUASB, and the identification of gaps that present opportunities for future research.

The AUASB extends its sincere appreciation to workshop attendees for their active participation, with special acknowledgment given to those who presented their research findings. The AUASB welcomes and values input from academics regarding potential opportunities for research in the future.

Mr Doug Niven
Chair
Auditing and Assurance Standards Board

Deakin University's Faculty of Business and Law has a proud tradition of engaging with the community, undertaking research and supporting events that are a catalyst for positive societal change. We believe that all public policy and legislative initiatives should be informed by high quality research, ensuring an evidence based approach in order to achieve optimal benefit for our nation.

With the objective of ensuring that the Australian government's Auditing and Assurance Standards Board (AUASB) is fully informed of current research findings as it pursues its agenda of developing standards in the important area of sustainability assurance, Deakin University hosted a roundtable in October 2023. At this roundtable leading researchers in auditing and assurance presented their research findings to the AUASB. Those findings can have important implications for AUASB initiatives in the area of sustainability assurance. The efforts of the Department of Accounting and the faculty research centre, the Deakin Integrated Reporting Centre, in co-ordinating and facilitating this roundtable, are a living demonstration of the vital role that universities can play in informing the development of public policy.

This roundtable was a demonstration of the benefits of collaboration across academia and government and I commend the organisers and the AUASB for this program. Deakin University's Faculty of Business and Law stands ready to support such important initiatives.

Professor Jenni Lightowlers
Executive Dean
Faculty of Business & Law
Deakin University

Preface

This Research Report provides a summary of academic presentations at the Deakin University (Deakin) – Australian Auditing and Assurance Standards Board (AUASB) Sustainability Assurance Research Workshop held on 25 October 2023, at CPA Australia.

Facilitated by the organising committee consisting of Anne Waters (AUASB), Rebecca Mattocks (AUASB) and Roger Simnett (Deakin University), the Workshop aimed to foster dialogue on research related to the recently issued Exposure Draft on the proposed International Standard on Sustainability Assurance (ISSA) 5000, *General Requirements for Sustainability Assurance Engagements*. It also aligned with the AUASB's broader Sustainability Assurance agenda including assurance on climate reporting, intending to pinpoint areas warranting future research.

The Workshop featured presentations by researchers and culminated with insights from the AUASB Chair, Doug Niven, and AUASB Staff, providing a comprehensive overview of international and domestic developments in Sustainability Assurance, along with highlighting the relevance of existing research and outstanding research opportunities that could inform the AUASB's framework for assurance.

Executive Summary

This Workshop was undertaken with the objective of informing and supporting the AUASB in developing the framework for assurance over sustainability related information. This involved gaining a deeper understanding of existing research on current sustainability assurance practices in Australia to assess the preparedness of the assurance market in transitioning from a voluntary to mandatory reporting environment.

The Workshop commenced with an introductory session outlining the objective of the Workshop and informing participants of the AUASB's agenda as it relates to sustainability assurance including climate. This was followed by four academic sessions which explored issues pertaining to current sustainability reporting and assurance practices in Australia, the use of accounting versus non accounting assurance practitioners, materiality considerations, alternative credibility enhancing mechanisms, voluntary versus mandatory assurance, greenwashing considerations and the effects of greenhouse gas multidisciplinary teams on performance.

Some of the key considerations for the AUASB were:

Considerations for the AUASB	Reference
The AUASB's Sustainability Assurance Agenda	
There is a need to consider the readiness of the Australian assurance market for the proposed sustainability and climate-related standards, including a consideration of processes, controls, disclosures required and data availability. This involves gaining a thorough understanding of the current reporting and assurance environment in Australia, including who the assurance practitioners are, what assurance is being given and over what information, and any capacity and capability concerns.	1.2, 1.3
Current Sustainability Reporting and Assurance Practices in Australia	
An increasing number of Australian listed entities are reporting climate-related information in their Annual Reports with the rate of such disclosures increasing from 36.1 % in 2021 to 42.8% in 2022. A significant jump in disclosures in the Financial Reports (and the Notes) by 75.3% in 2022 compared with 2021, and by 59.5% in disclosures in the Directors' Remuneration Report compared with 2021. The large jump in the disclosures in the Notes to the Financial Report is especially reflected in a large increase in the specific notes related to accounting policies and judgement, or basis of preparation, with an increase from 19 instances in 2021 to 64 in 2022. However, most disclosures still occur in the other information sections in the annual report, emphasising the importance of ensuring that Auditing Standard ASA 720 *The Auditor's Responsibilities Relating to Other Information* is fit for purpose and properly applied.	2.1
The number of entities mentioning the provision of external assurance of climate-related information in the Annual Reports increased from 18 in 2018 to 40 in 2022. Among them, there are 22 assurance reports attached to (included in) the Annual Reports in 2022. Limited assurance is the dominant assurance level being provided over climate related information, that is predominantly quantitative in nature. As we prepare for mandatory reporting, there will need to be a large uplift in the level of assurance provided. The Big 4 auditors are the most common assurance providers, the majority of which are also the financial statement auditor. Reasonable assurance provided on scope 1 and 2 greenhouse gas emissions are identified, resulting in hybrid (both limited and reasonable) assurance reports. There is an opportunity for	2.1, 2.2

guidance by assurance standard setters for such hybrid levels of assurance engagements and the format of the assurance report that should result.	
When looking at sustainability and climate-related information outside the annual reports for ASX 300 companies, 30% have some form of sustainability assurance in place. Of these, a substantial majority (89%) obtained assurance from accounting firms, while the remaining 11% were assured by non-accounting firms. The main assured reporting framework is GRI, and the assurance of selected information, mainly quantitative information is predominant. It is proposed that Australia will introduce mandatory assurance in line with the IAASB's proposed standard, with additional requirements for frameworks most commonly used.	2.3
Accounting versus Non-Accounting Assurance Practitioners	
Accounting practitioners are the dominant providers of assurance over non-financial information in Australia. Accounting assurance practitioners have been found to have an advantage over non-accounting assurance practitioners in detecting and preventing sustainability errors while synergistically improving financial reporting quality, and applying their skills to enhance the value relevance and quality of sustainability reporting in the capital market and fostering trust among stakeholders.	3.1, 3.2
The provision of assurance impacts financial statement users' perceptions of credibility and reliability, with differences in perceptions dependant on the level of assurance being provided. Users were found to value assurance provided by all assurance providers, including non-accounting assurance providers. If non-accounting assurance providers are being used it is important that they are required to comply with equivalent quality management and ethical standards as those in the accounting profession.	3.1
Non-accounting practitioners are not subject to the same professional requirements as professional accountants, despite being able to use the same assurance standards. Advantages were found to non-accounting assurance practitioners using ISAEs, but there continue to be a number of instances where the underlying ethics and quality management frameworks applied are not included in the assurance report.	3.2
Materiality, Other Credibility Enhancing Mechanisms and Voluntary versus Mandatory Assurance	
There is no evidence to suggest that users, preparers or assurers are different in their perceptions of materiality, or of the factors that determine materiality. It is important however, to explore and compare the information needs across different user types for misstatements in qualitative disclosures. Proposed ISSA 5000 proposes that judgments about impact materiality and double materiality matters are based on the assurer's consideration of the common information needs of intended users as a group. Given the acknowledged diversity of user types, how is this practicable?	4.1
Listed Australian companies are unique in that they have available to them multiple credibility-enhancing techniques to safeguard the integrity of unaudited information, including internal control processes and board reviews. For example, recommendation 4.3 (Rec 4.3) within the ASX Corporate Governance Principles and Recommendations 4th Edition encourages companies to disclose the processes they used to ensure the integrity of periodic corporate reports. Considering recent initiatives such as the three lines of defence and the IAASB's trust model that include both internal and external mechanisms in ensuring the credibility and trust, the AUASB may consider its mandate over this broadening view of credibility enhancing mechanisms.	4.2

With regard to Auditing Standard ASA 720, *The Auditor's Responsibilities Relating to Other Information,* a standard issued by the AUASB that mandates auditors to consider the unaudited information contained within the annual report, there is an increasing trend over time in the proportion of auditor observations that received all of the other information prior to the date of the auditor's report. This suggests that the requirement for the auditor to disclose whether they have been provided with the other information has potentially facilitated their access to such information.	4.2
There are few countries where assurance of sustainability information has been mandated. Assurance versus non-assurance over non-financial information has been found to result in higher sustainability reporting scores, greater integration of non-financial information into companies' decision-making processes, increased analyst following and reduced cost of debt. Mandatory versus voluntary assurance is significantly associated with expanded assurance scope and a shorter assurance report lag.	4.3
Perceptions of Audit Committee Chairs, Group Decision Making and Greenwashing	
Audit Committee Chairs see it as very important to have consistent worldwide sustainability reporting and assurance requirements.	5.1
While Audit Committee Chairs consider the accounting profession as having the skill set, global scale and experience needed to conduct financial statement audits, they are less confident as to whether there are currently sufficient skills in the market to carry out some aspects of sustainability assurance.	5.1
Audit Committee Chairs are confident in the management and systems providing the financial reports, but less confident in the systems and processes in house, and skills available for reporting entities in providing the content of the sustainability information provided.	5.1
Audit Committee Chairs have a strong preference for the assurance provider to come from the same firm as their financial statement auditor, due to perceived synergies.	5.1
Combining assurance experts and subject matter experts into multidisciplinary teams can bring benefits as a result of greater collaboration on diverse perspectives, which eventually enhances assurance teams' performance. However, there can also be biased evidence processing within teams, as accounting experts overweigh the evidence suggested by experts. It is therefore important for guidance to be developed on how the work of assurance experts and subject matter experts can best be integrated.	5.2
Greenwashing poses a risk of material misrepresentation on claims made in annual and sustainability reports. Stakeholders believe sustainability assurance can help reduce greenwashing, but there's a need for caution concerning greenwashing issues.	5.3

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1. The AUASB's Sustainability Assurance Agenda

1.1. Sustainability Assurance Developments

In December 2022 the Treasury issued a Consultation Paper seeking initial views on the key considerations for the design and implementation of standardised, internationally-aligned requirements for disclosure of climate-related financial risks and opportunities in Australia.

Following feedback received, a second Consultation Paper was issued in June 2023, seeking views on proposed positions for the detailed implementation and sequencing of reporting and assurance requirements. The policy parameters for climate disclosure assurance include:

- A requirement for limited assurance, moving to reasonable assurance over time.
- Reasonable assurance of Scope 3 emissions as a final step in scaling requirements.
- Assurance to be provided against the Australian equivalent standards to the ISSB standards and Corporations Act/Corporations Regulations requirements, in line with AUASB standards.
- Assurance to be carried out by a qualified and experienced independent provider (conducted or led by the financial auditor).

With the aim of fostering trust in reported sustainability information from investors, regulators and other stakeholders, the IAASB is developing a global baseline sustainability assurance standard, International Standard on Auditing (ISSA) 5000, *General Requirements for Sustainability Assurance Engagements*. The proposed standard, applicable to any sustainability topic and various frameworks, addresses both limited and reasonable assurance and is designed to be profession-agnostic, accommodating both professional accountants and non-accountant assurance practitioners.

In August 2023, the AUASB issued a Consultation Paper on the IAASB's Exposure Draft on ISSA 5000, for a 85-day comment period which closed on 10 November 2023.

Aligned with its Evidence Informed Standard Setting strategy, the AUASB has been conducting information gathering and research activities to support decision making on climate-related reporting assurance in Australia. The focus of the activities to date has been to understand:

- The ability of assurance providers to meet the demands for assurance under the Treasury proposals;
- Stakeholder feedback on Treasury's second Consultation Paper seeking views on proposed positions for reporting and assurance requirements.
- Relevant research that exists including on the current level of reporting and assurance on climate related information in Australia.
- Developments and plans in other jurisdictions in relation to climate reporting and assurance requirements and pronouncements.

External assurance has a key role in contributing to trust and confidence that decision makers have in the reliability of sustainability disclosures, as highlighted in Treasury's second Consultation Paper.

1.2. Key Assurance Considerations

A review of the submissions to Treasury's Consultation indicates that those who commented on assurance matters were broadly supportive of mandatory assurance on climate-related information. Specifically:

- Many respondents were supportive of phasing and scaling of assurance requirements to allow for skills, capacity and processes to be developed over time. However some commented that the assurance roadmap included in the Consultation Paper was too ambitious, particularly the timing of the transition from limited to reasonable assurance.
- The majority who responded supported assurance by the financial statement auditor, supported by third-party or internal subject matter experts.

The AUASB's objectives are to influence the ISSA 5000 Exposure Draft, determine the need for local standards and guidance on assurance over governance, strategy, metrics including Scope 1, 2 and 3 emissions, quantitative scenario analysis and transition plans, and to understand the appropriate transition period from limited to reasonable assurance over different information for different groups of entities. The AUASB intends to achieve these objectives by activities which include gaining an understanding of the current state of play in Australia and the status of international developments in sustainability reporting and assurance.

1.3. Research Opportunities

This Workshop brought together specialist audit and assurance academics from across Australia and other stakeholders to share and discuss research relevant to climate and broader sustainability assurance in Australia, while simultaneously highlighting areas for future research. In particular:

- Readiness of reporters
  - What is currently being reported and under what frameworks?
  - Magnitude of increased disclosures from current requirements/practice to the AASB's proposed ASRS1 and ASRS2?
  - The level of voluntary sustainability reporting?
  - Readiness for assurance i.e., processes, controls, governance, identifying disclosures required, data availability?
  - Current capacity and capability?
- Assurance providers
  - Do financial auditors provide assurance over climate disclosures (supported by experts)?
  - To what extent are non-accountants providing assurance?
  - What are the required competencies/accreditation vehicles?
  - What assurance is being given over what information?
  - What assurance, quality management and ethical standards are used?
  - Demand for voluntary assurance?
  - Current capacity and capability?
  - Issues affecting capacity and/or capability building?

2. Current Sustainability Reporting and Assurance Practices in Australia

The first academic session covered the current sustainability reporting and assurance practices in Australia. As we move towards a mandatory climate assurance setting, it is important that we have a thorough understanding of the current sustainability assurance environment, including the type of information that is currently being assured, the rate at which it is being assured, and by whom.

- What is the current capacity and capability of the assurance market?
- Do financial statement auditors currently provide assurance over climate disclosures? What is the current proportion of accounting versus non-accounting practitioners?
- What reporting frameworks are being followed?

Structure of the Session	
Professor Elizabeth Carson (RMIT University)	Session Chair
Academic Presentations:	Research Topic:
Ms Jean You (UNSW Sydney)	Assurance of Climate-Related Information in Australia
Associate Professor Mukesh Garg (Monash University)	Impact of Climate-Change Financial Disclosures on Accounting Numbers and Assurance Practices
Dr Farah Zamir (Deakin University)	Review of Sustainability Assurance Practices by ASX 300 Firms
Ms Anne Waters (AUASB)	AUASB Wrap-Up

2.1 Assurance of Climate-Related Information in Australia

Ms Jean You, UNSW Sydney

Introduction

This research aims to provide an update to the AASB-AUASB research report (You and Simnett 2022), which examines the trend of climate-related disclosures and assurance in the Annual Reports of ASX listed entities from 2018 to 2021, by extending this analysis to consider 2022 Annual Reports. With the emphasis of IFRS S2 on informing users of General Purpose Financial Reports (GPFR), this report does not explicitly cover climate-related disclosures and assurance practices outside the Annual Report, except to the extent that those disclosures are replicated or summarised in the Annual Report. As such the findings of this report have implications for considerations of climate-related disclosures under AASB standards for the AASB, and auditing (ASA) and assurance (ASAE, ASSA) standards for the AUASB.

Research method

We examined the Annual Reports of ASX listed entities excluding trusts and funds.[1] We define the Annual Report as the reporting package that entities are required to deliver under the corporate, compliance or securities laws of the country in which they operate. As such, we focus on the climate-related disclosures in the Annual Reports, which contain the audited financial reports and the associated Appendix 4G Corporate Governance Statement (CGS) as it is required under the reporting framework of the ASX Listing Rules. Our data are sourced from the Connect4 database for Annual Reports (including Corporate Governance Statements) of ASX-listed companies. We identified climate-related disclosures with a list of key terms,[2] which is extended from ASIC (2018) and consistent with You and Simnett (2022).

Results

An increasing trend of ASX listed entities disclosing climate-related information in their Annual Reports continues, with the rate of such disclosures increasing from 36.1% in 2021 to 42.8% in 2022. This increasing trend is observed in all industry groups, and on average, climate-sensitive industries continue to be more likely to disclose climate-related information with extant reporting standards and/or guidelines. In relation to ASX entity size, while there has been a plateauing in 2022 of the disclosure rates for ASX 300 entities, there has been a marked increase in other listed entities incorporating climate-related information into their Annual Report. As the largest 300 ASX entities appear to be reaching close to a saturation point in voluntarily disclosing climate-related information in the Annual Report, given proposals to mandate disclosures for all listed entities over a certain size, it may be informative to understand why the small number of the largest ASX companies that are currently not disclosing, or disclosing outside the annual report but not referencing such disclosures in the annual report, have decided to-date not to do so.

Concerning the location of climate-related information in the Annual Report, most disclosures are still in the other information section of the Annual Report (outside the Financial Report and the Directors' Remuneration Report). From an assurance perspective, these disclosures are outside the Financial Reports and thus not subject to audit. The credibility-enhancing techniques for such disclosures are currently covered by ASA 720, *The Auditor's Responsibilities Relating to Other Information*. We also observed a significant jump in 2022 in disclosures in the Financial Reports (and the Notes) by 75.3% compared with 2021, and by 59.5% in disclosures in the Directors' Remuneration Report compared with 2021. This provides support for the view that Australian entities are increasingly recognising the significance of climate-related impacts on their financial position and performance.

The increase in the disclosures in the Notes to Financial Reports for 2022 are particularly pronounced for the largest ASX 500 entities. For example, more than 50% of the largest ASX 100 entities that disclose climate-related information are now disclosing such information in these statements, compared with 36.3% of such entities in 2021. This increase is also seen to be spread across all industry groups. 85% of entities disclosing climate-related information in their notes to financial reports were audited by one of the Big 4 firms (EY, Deloitte, PWC and KPMG) in 2022, and 90% of them were audited by one of large audit firms (Big 4, BDO and Grant Thornton).

The large jump in the disclosures in the Notes to the Financial Report is especially reflected in a large increase in the specific notes related to accounting policies and judgement, or basis of preparation, with an increase from 19 instances in 2021 to 64 in 2022. Other notes in which climate-related

1 This is consistent with the emphasis on climate-related information being disclosed in general purpose financial reports from the perspective of IFRS S2 (IFRS 2023a).

2 "climate change", "global warming", "carbon emission", "greenhouse gas", "climate risk", "carbon risk", "CO2", "climate related", "climate-related", "climate strategy", "TCFD", "Climate Resilience", "climate active", "climate action" and "GRI".

disclosures were most frequently observed were the carrying value and impairment of non-financial or intangible assets (26 in 2021 to 34 in 2022), followed by risk management (17 in 2021 to 23 in 2022), property, plant and equipment (11 in 2021 to 21 in 2022) and subsequent events, including provisions and contingencies (14 in 2021 to 19 in 2022).

The largest entities are identified as those that are most likely to include climate-related content in their remuneration reports. There are significant increases for ASX 100 entities from 31.9% (29 of 91 disclosers) in 2021 to 41.8% (38 of 91 disclosers) in 2022, and for ASX 101-300 entities, increasing from 5.8% (6 of 103 disclosers) in 2021 to 16.8% (19 of 113 disclosers) in 2022. We continue to observe very limited climate-related disclosures in the remuneration reports outside ASX 300 entities in 2022.

We find a rising number of disclosers referencing the Taskforce on Climate-Related Financial Disclosures (TCFD) recommendations in the Annual Reports, which continually increases from 61 of 1,914 (3.2%) in 2018 to 181 of 1,930 (9.4%) in 2021, and further to 211 of 2,004 (10.5%) in 2022. The number of entities reporting in accordance with the explicit four pillars of the TCFD (S2) reporting structure increases from 17 of 1,914 (0.9%) in 2018 to 62 of 1,930 (3.2%) in 2021, and further to 69 of 2,004 (3.4%) in 2022. Given IFRS S2 builds on the legacy of TCFD recommendations (2023b), the AASB may consider providing guidance for ASX listed entities moving forward to IFRS S2. Among those with TCFD (S2) reporting structure in 2022, around 90% were audited by Big 4 auditors.

The number of climate-related Key Audit Matters (KAMs) continues to increase, from 9 in 2021 to 14 in 2022. Climate-related KAMs are often sticky and commonly recur in subsequent years. There is no guidance or examples in the current ASA 700 series for auditors as to how, what and why they should incorporate these types of KAMs in their auditor's report. In 2022, KAMs with climate-related information were primarily issued by Big 4 auditors, especially for entities resided in Australia.

In addition to audits, we also consider the situations where companies provide external assurance of their climate-related disclosures. Despite increasing, a limited number of entities mentioned the provision of external assurance of climate-related information in the Annual Reports, from 18 in 2018 to 40 in 2022. Among them, there are 22 assurance reports attached to the Annual Reports in 2022, increasing from 9 in 2018. Having examined these assurance reports, we find all of the assurance reports are issued by Big 4 auditors in 2022, and 76.2% of them are also the incumbent Financial Report auditors of the entity. Limited assurance is still the dominant assurance level while we identify three situations where reasonable assurance is provided specifically on scope 1 and 2 greenhouse gas emissions. The assurance providers for these three situations are EY, Deloitte and KPMG.

Implications for the AUASB

An increasing number of listed entities report climate-related information in other information sections in the Annual Reports. The final revised ASA 720 was one of the more contentious outcomes from the revision of the auditor reporting standards, with concerns about whether the level of involvement of the auditor is correctly understood. We continue to believe that this disclosure trend increases the importance of ensuring that ASA 720 is fit for purpose in the current environment. It is noted that the proposed ISSA/ASSA 5000, *General Requirements for Sustainability Assurance Engagements,* also includes other information requirements for assurance engagements of sustainability/climate-related information. It is important that the assurance requirements for other information are fit for purpose before we extend/replicate these requirements for a broader range of assurance engagements.

We also suggest that the AUASB consider application material on climate-related information in financial report audits. A continuing increase in climate-related information in the notes to several accounts can lead to direct impacts on Financial Report audits. Although this was anticipated by the

AASB-AUASB (2019), there has not been a consequential change in underlying auditing standards or application material to support audit practice in these circumstances. Application material may be especially beneficial with the proposed IASB S2 disclosures requiring assurance in the near future.

The Australian Treasury (2023) provides an assurance roadmap, with, for example in 2026, reasonable assurance for scope 1 and 2 emissions and limited assurance of scope 3 emissions, scenario analysis and transition plans. Very few entities' disclosures are currently being assured at this level. There is an opportunity for guidance by the AUASB for such hybrid levels of assurance engagements and the format of the assurance report that should result.

Summary and further research opportunities

Focusing on the Annual Reports of nearly all ASX listed entities (excluding trusts and funds), we provide the AASB and AUASB with an analysis of the Australian market for the upcoming adoption of IFRS S2. In regard to reporting, we observe there has been an increasing trend of disclosing climate-related information since 2018, which continues in 2022. While climate-sensitive industries have more disclosers than other industries, the increasing trend is observed across all industries. A majority of the largest ASX 300 entities have been disclosing climate-related information, and a growing number of smaller entities are joining the trend. Despite this increase, only around 10% of listed entities referenced TCFD recommendations in 2022.

From an assurance perspective, we observe an increasing amount of climate-related information subject to audit, with disclosures in the notes to the financial statements. However, most disclosures are still outside the financial reports, and thus not subject to audits while within auditors' responsibility to other information in the Annual Reports (ASA 720). The number of climate-related content in KAMs continues to increase. In addition to audits, only a limited number of entities disclose their provision of external assurance of climate-related information in their Annual Reports. Among those, the Big 4 are the dominant providers, and limited assurance is the most common assurance level.

We expect further research on suggestions for preparing the Australian market for the upcoming climate-related reporting and assurance standards.

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2.2 Impact of Climate-Change Financial Disclosures on Accounting Numbers and Assurance Practices

Associate Professor Mukesh Garg, Monash University

Introduction

This summary report is part of ongoing research examining the credibility and value relevance of climate-related financial disclosures authored by John Campbell (University of Georgia), Anita Foerster (Monash University), Mukesh Garg (Monash University), and Luisa Langer (University of Mannheim). Climate change refers to the long-term alteration of temperature and weather patterns on a global scale, primarily caused by human activities such as burning fossil fuels and deforestation. Studies examining the impact of climate change on financial and economic issues argue that corporations face adverse shocks in terms of productivity, profitability, financing, and valuation due to the physical, transitional, and regulatory risks associated with climate change (Chava, 2014; Bernstein et al., 2019; Huynh and Xia, 2021). Organisations should, therefore, provide accurate and reliable information regarding their efforts to address climate change. Climate change can impact an entity's business and elevate both inherent risk and audit risk. Consequently, the verifiability and assurance of climate change and sustainability disclosures are essential to ensure credibility. This is because stakeholders, including auditors, investors, customers, regulators, and the general public, rely on these disclosures to make informed decisions. To ensure high-quality audits, auditors should respond to increased climate, sustainability, and other related risks by increasing audit efforts (i.e., decreasing detection risk) and/or charging a fee premium (e.g., Niemi et al., 2018). It is important to note that investors and other stakeholders continue to raise concerns about the quality and usefulness of climate disclosures provided by Australian companies. Many companies now provide climate risk disclosures in the annual report or dedicated climate change reports, and there is ostensibly high uptake of TCFD standards. However, the majority of companies only partly implement the TCFD recommendations, and there is considerable variation in reporting.

In Australia, the Australian Accounting Standards Board (AASB) and the Auditing and Assurance Standards Board (AUASB), in December 2018, issued Practice Statement 2 (APS/PS 2) on climate change and other types of risk disclosures in the financial statements. This statement advises that reporting entities can no longer treat climate-related risks as merely a matter of corporate social responsibility and may need to consider them in the context of their financial statements (AASB and AUASB, 2018). The AASB and the AUASB expect that directors, preparers, and auditors will be considering APS/PS 2 when preparing and auditing financial statements (Li et al., 2019). In June 2023, the International Sustainability Standards Board (ISSB) issued IFRS *Sustainability Disclosure Standards,* IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information,* and IFRS S2 *Climate-related Disclosures* (IFRS, 2023). Subsequently, the Department of Treasury in Australia issued a consultation paper on climate-related financial disclosure seeking feedback and comments (Australian Treasury, 2023). In August 2023, the International Auditing and Assurance Standards Board (IAASB) issued the *Proposed International Standard on Sustainability Assurance 5000 General Requirements for Sustainability Assurance Engagements* (IAASB, 2023),

followed by the AASB Exposure Draft ED SR1 *Australian Sustainability Reporting Standards – Disclosure of Climate-related Financial Information*, which was issued on 23 October 2023. These standards and guidelines aim to enhance financial reporting quality and assurance related to the impact of climate change and sustainability. In this report, we provide a summary of our research on the impact of climate-change financial disclosures on financial reporting with implications for assurance regulators, providers and users of assurance information.

Literature review

Climate change related natural disasters may have immediate consequences, such as the destruction of corporate assets, long-term consequences such as production stalling or supply chain disruptions, and lead to a decline in financial performance (Hallegatte, 2014). Due to the relatively lower risk of litigation in Australia (Khurana and Raman 2004, Garg et al., 2017) and in the absence of a mandatory external audit of climate change and sustainability related information, management may be forthcoming with disclosing low-quality information on climate-related risks. Therefore, companies may face severe reputational risks if the public perceives them as not contributing to climate goals and a sustainable future. Li et al. (2018) demonstrate that auditors charge a higher fee when their clients face more complex applicable environmental regulations. A climate change study by Truong, Garg, and Adrian (2020) find that clients located in the U.S. states with more severe drought conditions are considered riskier and are charged higher fees. Similarly, Hartlieb and Eierle (2022) find a positive relationship between audit fees and the level of climate change-related risks.

Climate change can impact a firm's business and elevate both inherent risk and audit risk. As the global climate continues to change, organisations may face increased costs and risks associated with extreme weather events, such as hurricanes, floods, and droughts. These events can damage infrastructure, disrupt supply chains, and lead to higher insurance premiums. Additionally, businesses that rely heavily on fossil fuels may face financial challenges as governments and consumers increasingly demand cleaner energy sources. Transitioning to more sustainable practices, such as investing in renewable energy, reducing greenhouse gas emissions, and implementing climate adaptation measures, can help mitigate these risks and even create new business opportunities. Companies are, therefore, expected to make adjustments and revalue their long-term assets considering the impact of climate change and other risks on their operations and future cashflows (Scholten et al., 2019). Since climate science predicts an increase in the frequency and severity of extreme weather events as a result of climate change caused by anthropogenic greenhouse gas (GHG) emissions, the loss and damage arising from natural disasters is likely to rise in the future (e.g., IPCC, 2012; Van Aalst, 2006). These events could impact an entity's future cash flows associated with their production assets, therefore impacting their reported assets and accumulated depreciation and amortization. Simnett and Nugent (2007) suggest that the credibility of disclosure of carbon emissions (a key indicator of transition risks) would be strengthened by the implementation and enhancement of assurance standards and services. Whether and how much climate change risk disclosures in the financial statements are considered by auditors is vastly unknown.

Description of research, method, and results

In this study, we examine voluntary climate change, sustainability, and other risk related disclosures in the financial statements of Australian Securities Exchange (ASX) listed companies to understand their impact on accounting numbers and assurance practices. Our study aims to answer two research questions: (i) whether climate change, sustainability, and other risk related disclosures have an impact on accounting numbers, and (ii) whether there are audit quality implications of such disclosures. We rely on information disclosed in the annual report as well as companies' financial statements and notes and construct an index score of company-level voluntary climate change, sustainability, and other risks. We conduct machine learning-based textual analysis for the period 2018 to 2022. We start

with S&P/ASX300 companies with an initial sample of 1,287 annual reports that are readable using Python. After controlling for financial variables, the final sample comprises 796 firm-year observations for the accounting implications analysis and 663 observations for the audit fees models. Our analysis suggests that voluntary climate change, sustainability, and other risk related financial disclosures are heterogeneous, and are mostly of low quality and inadequate, with little clarity on their real impact on the disclosing companies' operations and long-term assets.

We then conduct empirical analysis using financial and disclosure scores. Our main variables of interest are *CLIMATE_CHANGE*, *SUSTAINABILITY,* and *RISK* which are proxy measures of climate change and sustainability, and other risk-related disclosures. Our approach is consistent with prior studies (see, for example, Phang et al, 2022; Hollindale et al., 2019), which also use a keyword search in the annual report to derive a firm-specific measurement of variables. For the regression models, our two dependent variables for the research questions related to accounting implications and assurance quality are *ACCU_DEP&AMOR* and *LOGAUDITFEE* respectively. First, we consider the disclosure determinants model and find that disclosures on climate change, sustainability, and other risks are mainly by larger companies. We find *CLIMATE_CHANGE* and *SUSTAINABILITY* variables are positively and significantly associated with *DEP_AMOR_ACCUM*, suggesting that companies disclosing climate change-related information make accounting and operational adjustments resulting in a higher amount of accumulated depreciation and amortization. Higher reported accumulated depreciation and amortization charges are likely due to the revision of long-term asset values considering the lowering of future cash flows. We then employ the audit fees model following Simunic (1980) to examine whether disclosing companies are charged higher audit fees by their auditors to answer the research question on the impact on assurance. We expect auditors to make more efforts to ensure their clients have adequately considered the impact of risks on the value of their long-term assets. We find that audit fees are positively associated with *CLIMATE_CHANGE*, *SUSTAINABILITY*, and *RISK*, suggesting additional audit efforts by audit firms to ensure voluntary disclosures contribute to higher-quality financial reports. We find that the disclosures on climate change, sustainability, and other risk-related disclosures have economic significance with a minimum mean increase in audit fees of approximately AUD$5,000 and an increase of over AUD$500,000 for very large listed companies.

Implications for the AUASB

Our study makes academic and practical contributions and has implications for the AUASB, Treasury, and the IAASB (i.e., ISSA 5000). Climate-related risks and other emerging risks are predominantly discussed outside the financial statements, if at all. However, as set out in the AASB/IASB Practice Statement 2 Making Materiality Judgements (APS/PS 2), qualitative external factors such as the industry in which the entity operates, and investor expectations may make such risks 'material' and warrant disclosures when preparing financial statements, regardless of their numerical impact (AASB and AUASB, 2018). Analyses of current disclosure practices suggest that specific reporting guidelines or standards could improve the quantity and quality of disclosures in the financial statements and notes. One potential financial implication arising from climate-related risks include asset impairment and changes in the assets' useful life. From a practical point of view, we provide evidence that companies making voluntary climate change, sustainability, and other risk related financial disclosures (in response to existing regulatory signals) revalue their long-term assets, considering the future cash flow implications. Auditors are expected to consider and understand the implications of climate-related risks (Li et al., 2019). This evaluation includes consideration of the qualitative aspects of an entity's accounting practices and financial disclosures. Therefore, auditors must make additional efforts to verify the value of reported long-term assets when providing financial reporting assurance. Higher fees charged by auditors from companies making climate change related disclosures signal a commitment towards thorough audit investigation and high-quality reporting. However, due to the heterogeneous nature of climate, sustainability, and risk related financial disclosures, the AASB should consider developing standards or guidelines to increase the uniformity of disclosures in the financial

statements. Such standards or guidelines would assist the AUASB in developing assurance guidelines which will benefit auditors in providing financial reporting assurance. Our study has practical and regulatory implications as it informs on the financial items that auditors must focus on in light of climate change and sustainability risks (ISSB, 2023), and contributes to the debate on whether there is a need for a mandatory audit of climate change, sustainability and other risk related disclosures.

We expect companies from certain industries such as mining, energy, and agriculture to disclose climate risk as they are likely to be exposed to climate risk (see Truong et al., 2020), but many companies from these industries still do not make any reference to climate risk in their financial statements and notes. While there is increasing demand for information on climate risk, assurance on the aspects of impact of climate risk on an entity's financial statements and asset values can be costly and requires specialist skills.[3] We recommend that audits of climate change and sustainability risks be restricted to large private and ASX-listed companies, at least initially. However, the AUASB could encourage auditors to report on concerns related to audit clients' valuation of reported long-term assets considering the impact of climate change on future cash flows as part of Key Audit Matters (KAMs). Proposed requirements from the Treasury for the phased introduction of independent assurance requirements are considered appropriate in light of the need to upskill and build capacity for an independent audit of climate disclosures. In light of the high cost of audit and shortage of appropriate skills, the findings of our study suggest that auditors may only be able to provide limited assurance considering increased qualifications if reporting entities are pushed too hard and too early. Climate-related litigation cases have more than doubled from 884 in 2017 to 2,180 in 2022 in the U.S. alone (UN Environment program, 2023). Limiting mandatory reporting and audits to very large entities that have the resources and processes in place would be a recommended approach, with gradually spreading the scope to medium-sized entities, as the process of reporting and audit builds on capabilities.

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[3] In their audit report for BHP in 2023, Ernst & Young disclosed that "We involved our valuation and climate change specialists to assist in assessing the reasonableness of commodity and carbon prices …….. and we involved our mining reserve specialists to assist in the assessment of the reserve estimation methodology…...".

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2.3 Review of Sustainability Assurance Practices by ASX 300 Firms

Dr Farah Zamir, Deakin University

Introduction

This paper provides a review of the sustainability assurance practices within the Australian context, specifically focusing on non-financial reporting among firms listed on the ASX 300. This report extends the research of Zamir et al. (2023), which examined the sustainability reporting practices of the ASX 300 companies in 2022.

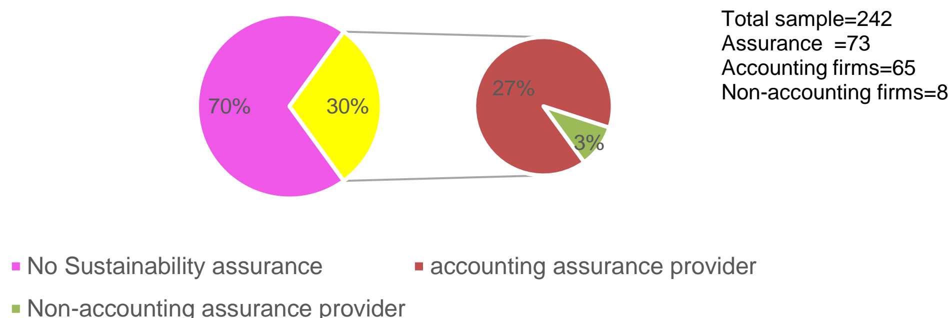
Results and Analysis

In this study, a detailed analysis of sustainability assurance practices was conducted for a subset of 242 firms[4] from the ASX 300 index.

Rate of sustainability assurance

The findings indicate that 30% of the sampled firms (73 out of 242) have some form of sustainability assurance in place. Of these, a substantial majority, 89% (65 out of 73 firms) obtained assurance from accounting firms, while the remaining 11% (8 out of 73 firms) were assured by non-accounting firms (See Figure 1). Within the accounting sector, EY is the most prevalent assurance provider, responsible for 33% of the reports. This is followed by PWC, KPMG, Deloitte, BDO, and GPP Audit Pty Ltd, assuring 22%, 19%, 12%, and 1% of the reports, respectively. In the non-accounting sector, Bureau Veritas stands out, having audited 5% (4 out of 73) of the reports.[5]

Figure 1 Sustainability Assurance



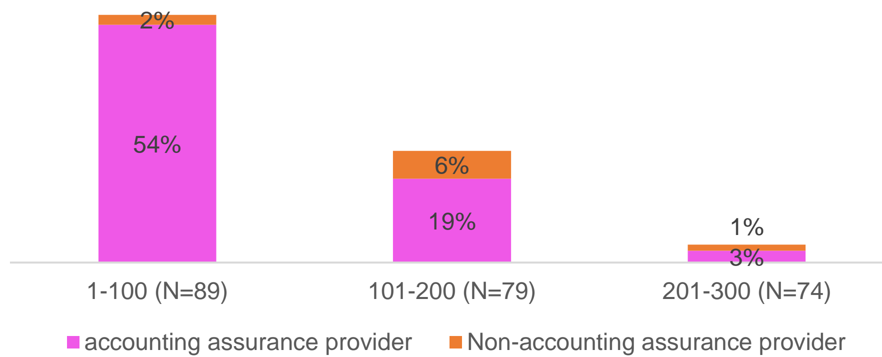
Type of Audit Firm Providing Assurance

The firms were further categorized by size for a more granular analysis of the assurance practices: 89 firms from the ASX 100, 79 from the ASX 101-200, and 74 from the ASX 201-300. This segmentation revealed that the largest firms (ASX 100) demonstrated the greatest engagement with sustainability assurance, with 56% (50 out of 89 firms) having such measures in place. In contrast, the smallest cohort (ASX 201-300) showed the lowest engagement, with only 4% (3 out of 74 firms) undertaking sustainability assurance. Accounting firms were the predominant assurance providers across all tiers, with their influence most pronounced within the ASX 100 group, where they provided assurance for 54% (48 out of 89 firms) of the firms. The least representation was in the ASX 201-300 group, where they assured just 3% (2 out of 74 firms). Interestingly, non-accounting assurance providers were more prominent within the mid-sized firms (ASX 101-200), accounting for 6% (5 out of 79 firms) of the assurance activities (See Figure 2).

4 The final sample comprised 242 firms, with the following breakdown by market capitalisation: 89 firms within the ASX100, 79 within the ASX 101-200, and 74 within the ASX 201-300. 58 firms were excluded because either they were foreign exempt or followed the AQUA rules.

5 Other Non-accounting assurance providers were Carbon Intel, Point Advisory, Social Responsibility Asia, and WSP, each auditing one report in the sample firms.

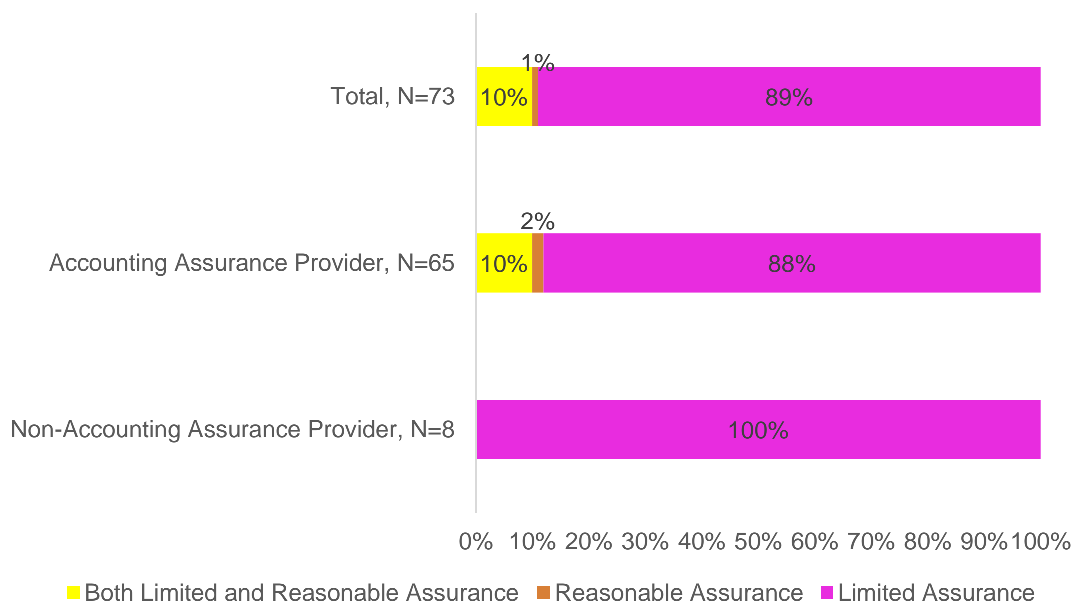
Figure 2 Sustainability assurance across sizes



Level of Assurance

Most sustainability assurances were limited in scope, with 89% (65 of 73 firms) receiving limited assurance. Specifically, accounting firms provided limited assurance for 88% (57 of 65 firms) and reasonable assurance for 2% (1 of 65 firms). Accounting firms offered both reasonable and limited assurance in 10% (7 of 65 firms) of cases, typically giving reasonable assurance for scope 1 & 2 emissions and limited for scope 3. Non-accounting firms exclusively provided limited assurance (See Figure 3).

Figure 3 Level of assurance



Nature and Proportion of Report Assured

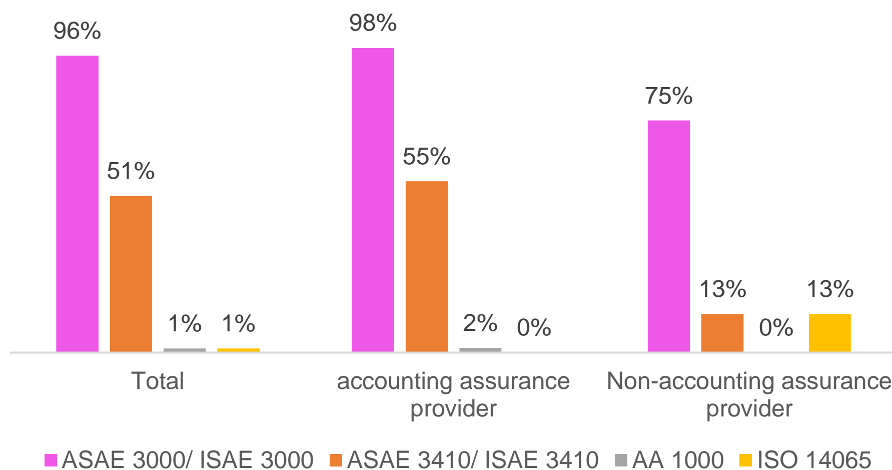
In our sample, quantitative data assurance dominates, with 85% (62 of 73 firms) providing it. Qualitative data assurance is less common at 5% (4 of 73 firms), and 10% (7 of 73 firms) assure both data types. Regarding report coverage (selected vs whole report assured), 94% (61 of 65 firms) of

accounting firms and all non-accounting firms (8 of 8 firms) assured selected report sections. Non-accounting providers did not assure any whole reports.

Assurance Standards

The IAASB's ISAE 3000, *Assurance Engagements Other than Audits or Reviews of Historical Financial Information,* and its Australian equivalent, ASAE 3000, were the primary standards for ESG assurance, applied by 96% (70 of 73 firms). ISAE 3410 and ASAE 3410 for GHG statements followed at 51% (37 of 73 firms). Both accounting and non-accounting firms utilised ASAE/ISAE 3000. Notably, one accounting firm (2%) and one non-accounting firm (13%) adopted AA1000 and ISO 14065 standards, respectively (See Figure 4).

Figure 4 Assurance standards

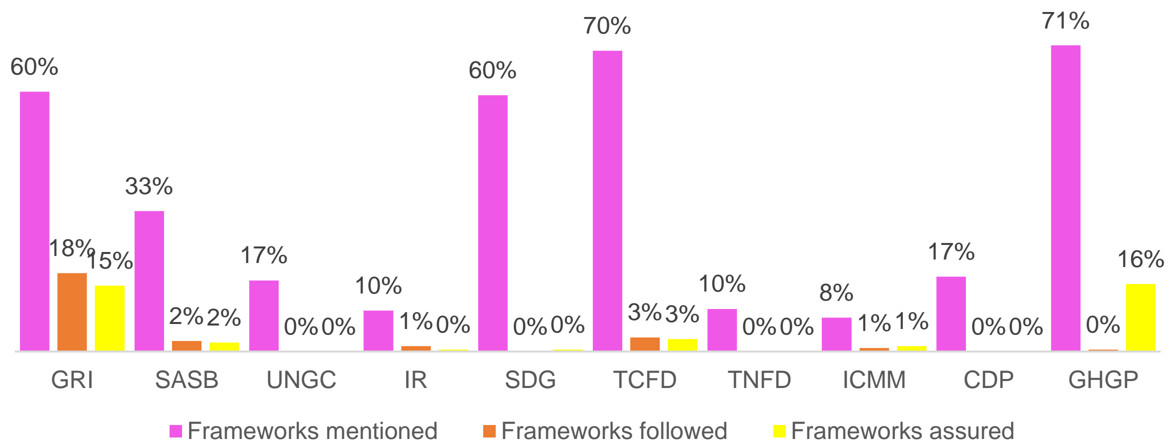


Assured Sustainability frameworks

Our complete sample analysis of 242 firms revealed significant differences in the mention, compliance, and assurance of sustainability frameworks, with figures for framework mentions and compliance sourced from Zamir et al. (2023). Many firms reference frameworks, but fewer verify compliance and even fewer secure assurance. GRI standards are assured for 15% (37 of 242 firms) against the 18% (44 of 242) that implement them. Although 70% (170 of 242 firms) mention TCFD, just 3% (7 of 242) have assured TCFD-aligned reports. Similarly, GHGP is mentioned by 71% (171 of 242 firms); however, despite none following it, 16% (38 of 242) have assured related disclosures (See Figure 5).

Further analysis indicates that assurance providers frequently cover multiple frameworks. Nearly half (47%) of firms receive assurance for a single framework, while 32% have assurances spanning multiple frameworks. Non-accounting providers predominantly (70%) assure a single framework. Where multiple frameworks are involved, a combined assurance on GRI and GHG protocols is most common.

Figure 5 Comparison of the overall sample



Compliance with the code of ethics

Within the ASX 201-300 firm bracket, 30% of non-accounting assurance providers failed to adhere to the code of ethics in their audit reports.

Conclusion and Recommendations

Based on the above findings, the following are the recommendations/implications proposed for the AUASB:

i. It is important for that the AUASB continues to understand the current state of the assurance market and enhances that understanding. The Australian assurance market is dominated by accounting firms, an extreme as compared to other countries (IFAC, 2023). However, there are still some non-accounting entities providing assurance for ASX 300. They predominantly use ASAEs but don't necessarily outline Ethics frameworks.
ii. Assurance currently focuses mainly on quantitative data. The credibility of qualitative data is expected by users, and arguably even more beneficial than the credibility of quantitative data. The current ISSA 5000 provides over 140 examples, but almost all of them (except for two) are quantitative. There's a pressing need for more examples that centre on assuring qualitative data.
iii. At present, the assurance of selected information is more common than assuring an entire report. There's a lack of clarity regarding why this is the case (one might guess it's because selected information is easier to assure or because it's quantitative). Is it possible to provide more clarity about the assurance roadmap for entities?
iv. There's a growing trend of referencing assurance within annual reports, leading to the assurance of Integrated Reports. This is as opposed to conducting separate assurance on individual engagements. While this trend is acknowledged in ISSA 5000, there's minimal guidance available currently on the assurance of integrated reports.

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3. Accounting versus Non-Accounting Assurance Practitioners

The second academic session explored differences between accounting and non-accounting assurance practitioners. There are differing views as to who should provide assurance over sustainability reporting. There may be synergies in the auditor of the financial report providing assurance over sustainability information and using experts as appropriate. Auditors are familiar with assurance levels and are subject to quality management and independence standards.

- Are financial statement users familiar with the difference between limited and reasonable assurance levels?
- Does the value of assurance on non-financial information depend on who the provides the assurance?
- What are the benefits and costs associated with the different types of assurance providers?

Structure of the Session	
Professor of Practice Michael Bray (Deakin University)	Session Chair
Academic Presentations:	Research Topic:
Professor Paul Coram (Adelaide University)	Does the Type of Assurer and Level of Assurance of CSR Reports Matter to Users' Credibility and Reliability Perceptions?
Dr Irene Ge (UNSW Sydney)	Comparing Assurance Engagements by Accounting versus Non-Accounting Assurance Practitioners
Mr Matthew Zappulla (AUASB)	AUASB Wrap-Up

3.1 Does the Type of Assurer and Level of Assurance of CSR Reports Matter to Users' Credibility and Reliability Perceptions?

Professor Paul Coram, Adelaide University

Introduction

In recent years many companies have started to disclose corporate social responsibility (CSR) information and sometimes obtained independent assurance on this information. Surveys by KPMG and the International Federation of Accountants (IFAC) indicate that disclosure and assurance of CSR information is steadily growing (KPMG, 2020, 2022; IFAC, 2023). Unlike the financial audit market monopolised by accounting firms, there is a competitive market for assurance on CSR reporting with

both accountants and non-accounting assurance providers. Those in the accounting profession have used and referred to International Standards on Assurance Engagements 3000 (ISAE 3000) (IAASB, 2013) in their work (accounting sustainability assurance providers (ASAPs)), whereas other assurance providers, such as non-accounting sustainability assurance providers (NASAPs) (sustainability experts) have historically referred to other standards or none. However, the International Auditing and Assurance Standards Board in 2013 decided to allow any assurance provider to use and refer to ISAE 3000, which will be consistent with the requirements in the proposed International Standard on Sustainability Assurance (ISSA) 5000, *General Requirements for Sustainability Assurance Engagements*. Therefore, sustainability experts can be split into two groups, NASAPs who do not follow auditing standards and those who do. Another difference is that while most financial statements receive reasonable assurance in audit reports, in the assurance of CSR reports there is more variation with both reasonable and limited assurance being provided. The purpose of this study is to assess how stakeholders who evaluate CSR reports respond to: first, the provision of assurance; second, who provides the assurance; and third, the level of assurance provided.[6]

Prior literature

Research on how users perceive CSR assurance has generally found it improves the credibility and reliability for users of this information. Pflugrath, Roebuck and Simnett (2011) reported that the credibility of CSR reports is improved through assurance, but such impact is context specific. The level of perceived credibility varies by the types of industry, types of practitioners and the jurisdiction. Hodge, Subramaniam and Stewart (2009) found that assurance improves the perceived reliability of environmental and social information and find an interaction between levels of assurance and types of assurance providers. In addition, Cheng, Green and Ko (2015) illustrated that assurance of a CSR report beneficially signals the importance of this report to investors. There have been some studies that have not been so clear on the perceived benefits of this type of assurance. Green and Li (2012) found that preparers and shareholders perceived auditors had a higher level of responsibility and perceived a lower credibility for assurance on greenhouse gas emissions than perceived by the assurers producing these reports. In a recent experiment, Hoang and Trotman (2021) found that assurance positively affects non-professional investors' assessments. However, it is not under all conditions, when investors are prompted to make an implicit assessment the effect of assurance on fundamental value is not observed.

Research on the difference between levels of assurance started when an option to produce limited assurance was first allowed. This early research found that report users could not distinguish the difference between reasonable and limited levels of assurance provided (Pany and Smith, 1982; Pillsbury, 1985). As time progressed, some research showed a better understanding of these differences by users. Schelluch and Gay (2006) highlighted that financial reports users perceive higher reliability of these reports when having an assurance statement with a positive opinion than with a negative assurance opinion. In terms of non-financial information. Hasan, Roebuck and Simnett (2003) found that report users perceive moderate assurance report of sustainability report provides a lower level of assurance than high assurance report. Further, Hasan, Maijoor, Mock, Roebuck, Simnett and Vanstraelen (2005) illustrated that users perceive a reasonable level of assurance of CSR information provides a greater level of assurance than a limited assurance opinion and the level of assurance opinion positively influences the credibility and reliability of the CSR information. Experimental research conducted by Hodge et al. (2009) demonstrated that CSR information with a reasonable level of assurance is perceived to be more credible by report users than limited assurance, however this only relates to when accountancy firms provide the assurance. However, a couple of recent experimental studies do raise some questions about how users currently perceive the

6 This presentation is based on a working paper (Niu, J., P., Coram, and A. Haji. 2023. Does the type of assurer and level of assurance of CSR reports matter to users' credibility and reliability perceptions? *The University of Adelaide Working Paper Series).*

differences between these two levels of assurance. Sheldon and Jenkins (2020) find that a broad group of stakeholders do not find a difference in perceived believability with either limited or reasonable assurance on CSR information. Hoang and Trotman (2021) in an experiment with non-professional investors find that *both* reasonable and limited assurance increased reliability assessments.

In relation to the differences between assurance providers, Hasan et al. (2003) found that report users overwhelmingly support NASAPs to assure CSR information. However, O'Dwyer and Owen (2005) document that ASAPs place greater emphasis on data verification and demonstrating rigour in how an assurance opinion has been reached. Consistent with this, some capital markets research has found that there are benefits to using accounting professionals (Simnett, Vanstraelen and Chua, 2009; Casey and Grenier, 2015). More recently, Clarkson, Richardson and Tsang (2019) found that different users perceive differences in value from the assurance reports and providers. They found Dow Jones Sustainability Index analysts are more concerned with the scope of the assurance engagement and are not concerned about who is providing the assurance, however capital market participants place more concern on whether the report was done by a Big 4 accounting firm.

Research method

This study provides some contemporary evidence on the value of assurance and perceptions related to who provides the assurance. Further, it is possible that the recent change to allow wider use of ISAE 3000 might affect users' perceptions of the assurance of CSR disclosures from different providers and that is also explored in this study. Ge, Simnett and Zhou (2023) found that the use of ISAE 3000 by NASAPs significantly increased after they were allowed to use this standard.

There are a couple of reasons why this study has importance for auditing standard setters. Over recent years CSR disclosures have become much more widespread; therefore, it is reasonable to expect that users now have much more familiarity with these disclosures and associated assurance than when earlier research was conducted. This study also specifically addresses a couple of issues considered as part of the Exposure Draft International Standard on Sustainability Assurance (ISSA) 5000, *General Requirements for Sustainability Assurance Engagements* (IAASB, 2023). First, it shows how users perceive assurance reports provided by NASAPs who refer to ISAE 3000 in their report as the new standard is proposing to provide more requirements on how the assurance standards can be used. Second, the study explores how well users understand the different between limited and reasonable assurance as the standard is exploring greater clarity on how these different levels of assurance are described.

This study reports the results of a 3 × 2 + 1 between-subjects experiment. The manipulations are three types of assurance practitioners and two levels of assurance, with a control condition where no assurance is provided on the CSR information disclosures. There were 165 participants, who had professional work experience and at least a bachelor's degree. The results of this study show that as expected, assurance does make a difference on users' perceptions of credibility and reliability, when compared to the control condition.

However, of note in this study is that when comparing the assurance reports provided by the different assurers to the control group, the only conditions that were significantly different from the control group were the two NASAP conditions and not the ASAPs. This provides some evidence that users' perceptions have changed, and they no longer necessarily assume that assurance from an ASAP automatically adds value to this information. This has implications for the accounting profession in reflecting on how they are perceived in this emerging market.

We do not find any difference between the NASAPs who use ISAE 3000 and those who use AS1000. This provides some evidence that the IAASB in allowing more widespread use of ISAE 3000 did not provide NASAPs with reputational benefits from the assurance tradition of the accounting profession. The results also indicate that users perceive higher credibility and reliability of sustainability reports with a reasonable level of assurance than a limited level of assurance. This suggests that users of sustainability reports have become more informed about the value of assurance reports on this information as it has become more widespread. In terms of the changes proposed in ISSA 5000, these findings do not suggest that limitations on the use of assurance standards is needed, or that greater explanation is needed of reasonable and limited assurance.

Implications for the AUASB and future research opportunities

This study provides some useful insights for the AUASB in their standard setting deliberations. As noted in this study, there has been research in the past that has examined the value of assurance on non-financial and CSR disclosure as well as whether users care who provides the assurance and their understanding of different levels of assurance. This study provides a contemporary update on how users perceive this type of information. We find that users do find value in NASAPs providing assurance, which would suggest that it is important for the AUASB to require compliance with the accounting professions ethics and quality control standards for any group using assurance standards issued by the AUASB. Further, we find that assurance does have value on this information and users do seem to understand the difference between different levels of assurance that are provided. This would imply that it is not important for the AUASB to provide more clarification on the difference between levels of assurance. However, given most of the assurance provided on CSR is ‘limited’ it may be an issue for standard setters to consider how higher levels of assurance could be encouraged.

Several avenues for potential future research derive from the results and limitations in this study. First, participants could be drawn from a more diverse group of stakeholders to increase the generalisability of results. Second, research could also try to understand the factors that users consider in their evaluations of CSR reports and assurance reports, given there appears to have been a change in their level of knowledge, and their perceptions on assurance providers. This type of research could be best addressed by interviews or focus groups. Finally, this study did show that accountants are not as highly regarded in CSR as they once were. Given the emergence of standards from the International Sustainability Standards Board (that is part of IFRS that is the international accounting standard setting organisation) it will be interesting for research in the future to see how this affects perceptions of accountants on CSR reporting and assurance.

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3.2 Comparing Assurance Engagements by Accounting versus Non-Accounting Assurance Practitioners

Dr Irene Ge, UNSW Sydney

Introduction

With the steadily growing demand for sustainability assurance services, the sustainability assurance market is undergoing continuous expansion (IFAC, 2023). Accounting practitioners have successfully claimed approximately 60% of the assurance market, while non-accounting assurance practitioners remain significant players in the market. Accounting practitioners dominate the markets in Australia and the European Union countries, while other assurance providers play a pivotal role in South Korea, the United States, and the United Kingdom (IFAC, 2023). While ISO 14064-3 continues to enjoy broad acceptance as the preferred choice among non-accounting practitioners, closely followed by the AA1000 assurance standards (IFAC, 2021; Ge, Simnett and Zhou 2023), the use of ISAE 3000 has managed to establish a consistent adoption rate of approximately 40% (IFAC, 2023). The disparities in regulatory frameworks and the requirements set by governing professional bodies for accounting and non-accounting assurance practitioners pose challenges for global assurance standard-setting bodies (CARE, 2023).

Prior literature

Prior research on assurance practitioners has shed light on the professional identity of both accounting and non-accounting assurance practitioners, which is manifested in their knowledge of assurance procedures, reporting on businesses and operations, and sustainability (Boiral, Heras-Saizarbitoria, and Brotherton 2020). Accounting practitioners are typically known for their in-depth knowledge of assurance procedures, their clients' industries and operations, as well as the credibility and robustness of their assurance standards. Additionally, they often provide benefits to their clients through global networks, brand recognition, reduced search costs, and increased synergies (Channuntapipat, Samsonova-Taddei and Turley 2019; Ge et al. 2023; Lu, Simnett and Zhou 2023).

On the other hand, non-accounting practitioners are recognised for their expertise in the field of assurance, particularly in sustainability and broader scope assurance engagements, and in making commentary and recommendations (Hummel, Schlick and Fifka 2019; Channuntapipat et al. 2020). With these two distinct types of practitioners have been actively shaping the sustainability assurance practice, it is imperative to understand the choices and implications associated with selecting assurance providers.

Benefits of engaging accounting practitioners as assurance providers

Value relevance

Previous research on the capital market benefits of sustainability assurance discovered no association between sustainability assurance and market value (Cho, Michelon, Patten, and Roberts, 2014). In a later sample period, Peters and Romi (2015) found a positive association. Extant research has increasingly demonstrated the value relevance of sustainability assurance, particularly in reducing information asymmetry and the cost of equity capital (Dhaliwal, Li, Tsang, and Yang, 2011; Fuhrmann, Otto, Looks, and Guenther, 2017). Building upon Dhaliwal et al.'s (2011) work, Casey and Grenier (2015) present evidence that the negative association between sustainability assurance and the cost of equity capital becomes more prominent when accounting practitioners are engaged as the assurance providers. This evidence finds additional support in Clarkson, Li, Richardson and Tsang’s (2019) paper, which find that capital market participants value a CSR report only when it is assured by an accounting practitioner.

Error restatements

Prior research suggests that sustainability assurance enhances the quality of sustainability reporting in terms of error restatement (Michelon, Patten, and Romi, 2019), with this effect (detection of inaccuracies in previous reporting and prevent future reporting inaccuracies) being more pronounced when sustainability reports are assured by accounting practitioners (Ballou, Chen, Grenier, and Heitger 2018). Bentley-Goode, Simnett, Thompson, and Trotman (2023) further confirm the evidence on the benefits of engaging accounting practitioners in improving sustainability reports. Specifically, the improvement includes improved methodology, increased scope of reporting, and updated definitions. Additionally, accounting practitioners are significantly associated with greater likelihood of restatement of prior period errors.

Financial reporting quality

Accounting practitioners apply their knowledge from financial statement audits when providing sustainability assurance. On one hand, their experience as financial statement auditors equip them with a deep understanding of their client companies' business operations, enhancing their background knowledge for providing assurance services. On the other hand, this expansion into sustainability assurance services can raise concerns about their independence. Based on an international sample, Lu et al. (2023) found that 33.9% of firms engage the same provider for both the financial statement audit and sustainability assurance. When narrowing the sample to Big 4 firms, this percentage increases to 64.5%. They present empirical evidence that companies with the same providers have lower levels of signed discretionary accruals and higher chances of receiving going concern modifications when in distress, indicating higher audit quality. This finding not only indirectly provides evidence to support the synergistic benefits of accounting practitioners but also offers insights into the upcoming implementation of IFRS S1 and S2 within the same reporting framework as financial reporting.

The role of non-accounting practitioners

While we acknowledge the benefits of accounting practitioners, it is important to recognize that non-accounting practitioners continue to play a significant role in the global sustainability assurance market. Existing research in accounting and assurance is limited in understanding the role of non-accounting practitioners in the sustainability assurance market.

Unlike financial audits, sustainability assurance encompasses a broad scope of subject matters. A diverse range of engagement types leads to a significant variance in the required subject matter expertise (Huggins, Green and Simnett 2011). Depending on the specific purpose of an assurance engagement, non-accounting practitioners can bring valuable subject matter expertise to meet the demands of various types of engagements.

Non-accounting practitioners fundamentally differ from accounting practitioners in their perception of sustainability, the terminology and methodology they adopt, as well as the ethical standards required by governing professional bodies. In contrast to accounting practitioners, non-accounting practitioners may operate under less rigorous quality controls, allowing them to offer assurance services at a more competitive cost (Huggins et al. 2011).

Non-accounting practitioners applying the ISAEs

In the pursuit of serving the public interest, international accounting and accountability standard-setting bodies are actively promoting the adoption of their standards by non-accounting practitioners. Nonetheless, it is crucial to ensure that these standards are diligently followed and that their intended purposes are effectively fulfilled. To address concerns about inconsistency in assurance quality, and to allow a full and transparent assessment of the integrity of the assurance engagement undertaken, all practitioners claiming to follow ISAE 3000 were required to disclose the ethics and quality control

frameworks that underpin their engagement. To ensure "public interest" is served, the IAASB proposed that ISAE 3000 (revised) required the following conditions of use: (1) practitioners comply with Parts A and B of the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants (IESBA), or requirements at least as demanding; (2) the engagement partner is a member of a firm applying ISQC 1, or other requirements at least as demanding as ISQC 1; and (3) compliance with these requirements is documented in the assurance report. No definition or specific requirement has been provided in revised ISAE 3000 regarding the term "at least as demanding as ", for code of ethics and quality control standards (Ge et al. 2023). This requirement introduced in the revised ISAE 3000 is further discussed in the proposed ISSA 5000, *General Requirements for Sustainability Assurance Engagements*. Specifically, the explanatory memorandum para. 25 requires "regulators and national standard setter share the responsibility for determining what may be considered "at least as demanding" in their respective jurisdictions". Recognizing the complexities involved in determining "as demanding as", national standard setters and regulators could offer additional support and guidance to standard users in their respective jurisdictions. This guidance would assist these users in assessing whether their existing practices align with the specific requirements.

In the post-revision period of ISAE 3000, as demonstrated by Ge et al. (2023), the revised standard did not deter non-accounting practitioners from adopting it. Additionally, they are more likely to adhere to the disclosure of stringent ethical and quality control standards, which are "at least as demanding" as those prescribed for professional accountants. However, there is a risk that remaining levels of non-compliance with the requirements of the revised ISAE 3000 requiring disclosure of the underpinning ethics and quality control frameworks may lead to a loss of confidence in the assurance profession.

An assessment of the consequences of adopting the revised standard revealed that switches to ISAEs by non-accounting practitioners have led to enhanced transparency in assurance procedures and independence of the assurance provider within the assurance report. There is a benefit for those non-accounting practitioners switching to the use of ISAEs in the form of an increase in their assurance market share, indicating that the market perceives that assurance quality is being enhanced. Ge et al. (2023) suggests that post-implementation reviews by standard-setting bodies are essential. It also serves as evidence supporting the promotion of assurance standards prescribed by accounting standard-setting bodies to be adopted by non-accounting practitioners.

Implications for the AUASB

- Australia is fairly unique in that we currently have one of the lowest rates in the world of non-accounting practitioners as assurance providers. This is despite the AUASB acknowledging that their remit on assurance providers extended outside the accounting profession.
- Accounting practitioners have been found to have an advantage in detecting and preventing sustainability errors while synergistically improving financial reporting quality, and transferring their skills to enhance the value relevance of sustainability reporting in the capital market, thus enhancing the quality of sustainability reporting and fostering trust among stakeholders.
- Significant challenges persist for accounting standard-setting bodies, particularly in the context of acknowledging that non-accounting practitioners are not subject to the same professional requirements as professional accountants.
- Recognising the complexity of following the international standards in jurisdictions with divergent legal system, corporate governance models and presence of non-accounting practitioners' share of their national sustainability assurance market, national regulators and standard setters should focus on delivering more detailed guidance to assist assurance practitioners in following the applicable standards.

- In the promotion of the use of assurance standards by non-accounting practitioners, a post-implementation review of assurance standards is essential.
- Enhanced transparency and independence disclosure in the assurance report by non-accounting practitioners contribute to improved consistency and comparability of assurance reports issued by different types of assurance providers. Consequently, this builds trust in stakeholders' perception of the quality of the assurance report.

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4. Materiality, Other Credibility Enhancing Mechanisms and Voluntary versus Mandatory Assurance

The third academic session covered specific assurance and other credibility enhancing mechanisms. It is important to consider, in the absence of assurance over non-financial information, how the integrity of unaudited information is maintained.

- How are listed entities complying with ASX Corporate Governance Principles recommendation 4.3?
- What credibility enhancing techniques beyond external assurance are being used?
- What do we know from other jurisdictions about the transition from voluntary to mandatory assurance over climate related information?
- Do preparers and auditors have different materiality perceptions? What are some of the challenges in identifying materiality?

Structure of the Session	
Associate Professor Noel Harding (UNSW Sydney)	Session Chair
Academic Presentations:	Research Topic:
Professor Greg Shailer (ANU)	Some Challenges in Identifying Materiality in Sustainability Reporting
Dr Dale Fu (Deakin University) Dr Pei-Jia Lum (Deakin University)	Alternative Credibility-Enhancing Approaches: ASX Corporate Governance Recommendation 4.3 and ASA 720

Dr Jenny Yang (UNSW Sydney)	Mandatory versus Voluntary Assurance on Sustainability Information
Dr Rebecca Mattocks (AUASB)	AUASB Wrap-Up

4.1 Some Challenges in Identifying Materiality in Sustainability Reporting

Professor Greg Shailer, The Australian National University

Introduction

The proposed ISSA 5000, *General Requirements for Sustainability Assurance Engagements* is intended to be a comprehensive, stand-alone standard suitable for any sustainability assurance engagements, for any sustainability topic under multiple frameworks. It is also intended to be agnostic in relation to assurance engagements performed by professional accountant and non-accountant assurance practitioners. However, the standard adopts or adapts many concepts and application principles from audit standards, some of which appear problematic in assuring sustainability disclosures. Our focus here is on some particular issues relating to how the standard seeks to apply materiality considerations.

The Exposure Draft makes numerous references to materiality and material misstatement, consistent with materiality (which entails relevance) being fundamental to the credibility of information. It is also a consequence of the requirement that the assurance practitioner determine (consider) materiality in planning and performing the assurance engagement and in evaluating whether the assured quantitative (qualitative) disclosures are free from material misstatement (para 91). For quantitative disclosures, the assurer must also determine applicable performance materiality (para 92). The requirement that assurors document factors relevant to their determination (consideration) of materiality means that concerns with identifying and assessing materiality has considerable practical importance.
The complexity of identifying materiality factors and assessing the materiality of identified misstatements across the diverse disclosure elements in, and diverse users of, sustainability reports give rise to many challenges in guiding the application of ISSA 500 requirements. This commentary addresses four selected (and partly interconnected) concerns regarding high level concepts.

Issues of materiality considered and implications for AUASB/IAASB:

1. How might any guidance obviate the risk that "*financial materiality*" will be subject to the perception / practice issues with materiality in financial statement audits?

In identifying the information needs of the **intended users,** proposed ISSA 5000 para A180 describes materiality of the: (i) impacts of sustainability matters on the entity as **financial materiality;** (ii) impacts of the entity on sustainability matters as **impact materiality**; and (iii) both impacts together as **double materiality**.

After 130-plus years, the dominant approach to assessing materiality in financial reports to shareholders is focussed on a simple "uniform" numerical benchmark measure. The proposed ISSA 5000 approach appears to be trying to avoid this for impact materiality but identifying "impact of

sustainability matters on the entity" as financial materiality raises concerns that the "accidental" heuristic approach to financial statement materiality approach will be repeated.

A field study reported in Edgeley, Jones & Atkins (2015) looked at what they describe as the interplay between old and new logics shaping materiality in 'social and environmental reporting'. They found that:

- among non-accounting assurors, a business case for materiality melds with a stakeholder logic, focussing on corporate performance.
- amongst accounting assurors, a stakeholder logic has been absorbed into a professional logic, driven by a liability constrained market logic.

Moreover, this concern may extend beyond financial materiality. This concern is enforced by evidence that synergistic interactions between accountants and non-accountants in multidisciplinary assurance teams facilitate the transfer of financial audit-styled concepts (such as materiality) to non-financial audit arenas (e.g., Canning, O'Dwyer & Georgakopoulos 2019).

The tendency to seek legally defensible materiality judgments has encouraged reliance financial statement auditors to rely on simplistic heuristics. Eilifsen and Messier (2015) report that the policy manuals of six of the eight largest audit firms "expect, suggest, or require the use of 5 percent of income before taxes" to set overall materiality (p.12). However, disclosure requirements may obviate this practice. In a study of UK firms reporting their materiality thresholds under ISA 700, Go, Lee, Li, Li & Wang (2023) identified some variation from the most common "5% of pre-tax profits" styled of criteria, as summarised below:

Materiality Base	Obs.	Mean	Std. Dev.	p5	Median	p95
Pre-Tax Income Related	1,160	0.052	0.010	0.040	0.050	0.075
Revenue	152	0.010	0.009	0.004	0.009	0.020
Assets	33	0.008	0.003	0.004	0.008	0.010
Gross Profit	26	0.017	0.018	0.002	0.020	0.030
Equity	26	0.018	0.008	0.005	0.020	0.030
EBITDA	25	0.035	0.011	0.020	0.035	0.050

Source: extracted from Table 2, Goh et al. (2023)

It is plausible that this level of variation exited prior to the implementation of ISA 700 (UK), but it may also be a consequence of the disclosure requirement. While proposed ISSA 5000 does not require assurers to disclose their materiality criteria or thresholds, the documentation requirements might encourage the development of engagement-specific materiality factors and levels. However, objective evidence is needed in this regard.

2. *Should* an assurer's conceptual view of materiality be different from or narrower than that of management of the reporting entity?

Proposed ISSA 5000 para A157 posits that assurers should have a narrower conceptualisation of materiality, compared to management. It states that "The entity's process to identify and select topics and aspects of topics to be reported may be established by management or applied pursuant to the requirements of a sustainability reporting framework. Such a process may often be referred to as the "process to identify reporting topics," "materiality assessment," or "materiality process", among other terms. However, the concept of materiality in this regard is not the same as the practitioner's materiality. For the purposes of this ISSA, materiality refers only to a threshold of significance to user decision-making considered by the practitioner in relation to potential and identified misstatements, in the circumstances of the engagement".

It is not obvious what necessitates the proposition in A157 that management and assurors will have different materiality concepts, and it is even less obvious as to how this could be true, when both management and assurors are expected to determine materiality by reference to the information needs of intended users. Throughout, proposed ISSA 5000 refers to materiality in relation to the information needs of **intended users**. In the absence of government regulatory requirements specifying intended users for particular forms of sustainability reporting, management is responsible for determining the content of the sustainability report, which is expected to be based on their assessment of their intended users' needs. This is reflected in the example in proposed ISSA 5000 at A274:

From A274: Example: The entity operates globally in various industries, including health care and consumer goods. The entity engaged an external consulting firm to gather data on stakeholders' perspectives regarding the entity's sustainability strategy. The entity took an approach to first identify the most relevant stakeholder groups, which included "customers, suppliers, non-profit organizations, corporate/private sector, academics, consultants, government, media, finance, trade associations, and think tanks." The entity then obtained direct feedback on how its sustainability strategy affected people, wider communities and the environment. After gathering this data, the entity analysed it to determine what issues were material to those surveyed and reported on those areas.

While the Australian survey reported in Xiao and Shailer (2022) suggest there may be some differences between assurers and users of sustainability reports as to their perceptions of the relative importance of materiality as a credibility factor, we do not currently have any evidence that users, preparers or assurers are different in their perceptions of materiality per se, or of factors that determine materiality.[7]

3. Proposed ISSA 5000 proposes (e.g., A271) that judgments about impact materiality and double materiality matters are based on the assuror's consideration of the **common information needs of intended users as a group**. Given the acknowledged diversity of user types, how is this practicable?

In A274, "double materiality" applies when the applicable criteria refer to both financial impacts on the entity and the entity's impacts on the environment, society, economy or culture. The "common information needs" of diverse users concerned with such potentially diverse areas of impact mean the assuror must identify the intersection of the information needs of the various users intended by management. This identifying the common information needs of different types of users might be practicable where a small number of narrowly defined intended users groups are involved, but for the more typical diverse range of an entity's stakeholder types, it is not obvious that the intersection of their different sets of information needs will produce a non-trivial information set.

Any ambiguity about the irrelevance of different types of users' needs is removed when, at A272, it is specifically stated that "unless the engagement has been designed to meet the particular information needs of specific users, the possible effect of misstatements on specific users, whose information needs may vary widely, is not ordinarily considered".

7 Subsequent to the Workshop, the IAASB issued set of Frequently Asked Questions regarding the proposed ISSA 5000, The Application of Materiality by the Entity and the Assurance Practitioner, which provides the following advice: "The entity's "materiality process" is focused identifying the sustainability matters to be disclosed. The practitioner considers or determines materiality in developing the approach for obtaining evidence and when evaluating identified misstatements of the sustainability information. As a result, qualitative factors considered by the entity and the practitioner may overlap but need not be identical. For quantitative disclosures, the practitioner and entity will not necessarily arrive at the same materiality threshold (i.e., the entity uses a threshold to determine, for example, whether certain metrics or targets should be reported and whether they are properly disclosed in accordance with the reporting framework, while the practitioner uses a threshold when obtaining evidence about the metrics and targets that are reported by the entity and evaluating identified misstatements in that information)." (p.3).

At one level, the notion that there can be a singular conceptualisation of double materiality across different user groups appears inconsistent with the philosophy underlying double materiality. For example, double materiality of environmental impacts applies where some investors' decisions and a regulator's decisions are each (differently) influenced by both the socially-relevant and financial impacts of an entity's environmental impact, such that each type of user would have different combinations of financial materiality and impact materiality of environmental impact misstatements. A literal reading of A274 means the assuror would have to determine what information needs do these two types of users have in common, as a group, and then determine a materiality threshold for misstatements. Presumably, the materiality threshold for each type of materiality will be the lowest threshold applicable across the different types of users.

On a different note, but related to the concerns with the diversity decision relevance of misstatements across different types of intended users, it proposed in A272 that it **is reasonable for an assuror to assume that intended users** "**Understand that the sustainability information is prepared and assured to appropriate levels of materiality and have an understanding of any materiality concepts included in the applicable criteria"** (ISSA 5000 A274 (b)). At a broad level, this might mean that it is reasonable merely for assurors to assume that users have read and understood ISSA 5000. At a more challenging level, it implies that it is reasonable for the assuror to assume that each type of intended user is aware of what they do and do not have in common with other types of users (in terms of information needs and their decision sensitives to misstatements), and understands the appropriateness of how the assuror has considered materiality only for the common information needs and determined the appropriate threshold. A separate discussion is needed to explore concerns attaching to the differential materiality issues, including comparing information needs and determining the sensitivity of their decisions, across user types for misstatements in qualitative disclosures.

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4.2 Alternative Credibility-Enhancing Approaches: ASX Corporate Governance Recommendation 4.3 and ASA 720

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Introduction

This summary is structured around two independent research papers to provide insights on the current practices of alternative credibility-enhancing approaches used to enhance the reliability of information other than audited information within the annual reports of Australia's largest listed companies: (a) Lum et al. (2023) examined the Recommendation 4.3 (Rec 4.3) within the ASX Corporate Governance Principles and Recommendation 4th Edition, which encourages companies to disclose the processes they used to ensure the integrity of unaudited information (referred to as "periodic corporate reports"); and (b) Fu and Simnett (2023) examined the Auditing Standard 720 (ASA 720), a standard issued by the Auditing and Assurance Standards Board that mandates auditors to consider the unaudited information contained within the annual report (referred to as "other information") without forming an audit opinion. Background information of these two practices is summarised in Table 1 below:

Table 1 Background information

Alternative credibility-enhancing approaches?	Mechanisms other than independent external assurance used to enhance the credibility of corporate reporting Examples: corporate governance practices, internal audit, internal control, board management processes, other risk identification processes, non-traditional tasks performed by external auditors.	
Information other than audited information within the financial report?	**Within the annual report** Directors' Report, Chairman's Report, CEO Review, Shareholder Information , sustainability information.	**Outside the annual report** Quarterly activity reports, quarterly cash flow reports, integrated reports, sustainability reports, or similar periodic report prepared for the benefits of investors.
Current practice of alternative credibility-enhancing approaches in Australia?	**Recommendation 4.3 in ASX Corporate Governance Principles and Recommendation 4th Edition** Companies are encouraged to **disclose the processes** they use to ensure the integrity of unaudited information ("periodic corporate reports")	
	Auditing Standards (ISA/ASA) 720 • Auditors are required to **read** and **consider** unaudited information within the annual report • Auditor **does not express an audit opinion** or any form of assurance conclusion	

The findings around these two credibility-enhancing approaches hold significant importance for the AUASB, especially in light of the recently released International Standard on Sustainability 5000, *General Requirements for Sustainability Assurance Engagements* (ISSA 5000). Where sustainability information is not externally assured, whether it is integrated within the annual report or disclosed in a standalone report, it is recommended that any processes employed to enhance the credibility of this information be disclosed in accordance with Rec 4.3. The term "processes" in this context encompasses a broad range of mechanisms, such as internal control processes and board

management practices. Additionally, it might extend to encompass external assurance if companies decide to pursue it. These disclosures not only provide insights into the management's proactive efforts in safeguarding the integrity of periodic reports, but also help distribute the risk of sustainability assurance more equitably between auditors and management.

On another hand, if sustainability information is presented within the annual report, auditors are required to follow the ASA 720 to assess whether there exists a material inconsistency between the sustainability information and the financial statement, or the auditor's knowledge obtained in the audit. ASA 720 is considered as an alternative credibility-enhancing approach because it mandates external auditors to read and consider unaudited information within the annual reports without forming an audit opinion. Considering the ASA 720 was used as the basis in drafting the requirements for ISSA 5000, auditors will likely be confronted with unaudited information within the document containing the sustainability information subject to assurance. Understanding the current practices of auditors in considering such information is vital for the AUASB to effectively standardize sustainability assurance.

Research methods and findings

ASX Corporate Governance Recommendation 4.3

Lum et al. (2023) examined the disclosure of credibility-enhancing mechanisms used by ASX300 companies in 2011 and 2022 using a "Three Lines of Defence Model" – the first line of defence represents internal control, the second line involved reviews completed by the Board of directors, and the third level is external assurance. The study revealed that the use of credibility-enhancing mechanisms is not mutually exclusive, but rather cumulative in nature. The most common mechanism implemented by ASX300 companies is the combination of internal control and board review at 48%, followed by the disclosure internal control only (25%). There are only 2% of companies that disclosed both internal control and external assurance, and 3% of companies disclosed all three mechanisms. A point to highlight is that the identification of external assurance is contained within the context of Rec 4.3 disclosures, for which 91% of disclosures were contained in corporate governance statements. Companies might disclose assurance within their sustainability reports while omitting it in corporate governance statements. This discrepancy may be due to communication gaps within the company or between parties responsible for preparing corporate reports. Another potential reason is the lack of a clear definition "periodic corporate reports" in Rec 4.3, particularly on whether it encompasses reports that have undergone voluntary external assurance.

Lum et al. (2023) delved deeper into the various types of internal control measures to gain a better understanding of the proactive steps taken by management to ensure the credibility of unaudited information. Results revealed that among the ASX300 companies, the top three most frequently employed internal control measures are reviews conducted by: direct line managers at 38%, senior executives and/or C-suite at 36%, and internal subject matter experts at 34%. The least common type identified was reviews by internal auditors at 12%. The results also showed variations in the types of internal control measures used by companies with different market capitalisations. Subject matter expert reviews are the most prevalent among ASX100 companies (47%), while ASX101-200 companies often involve direct line managers (37%), and ASX201-300 companies frequently rely on senior management or C-suite (39%). In addition, while only 22% of ASX100 companies adopted externally hired advisors or consultants to review periodic reports, this proportion is notably higher compared to smaller companies within the ASX101-200 (8%) and ASX201-300 (10%).

ASA 720 The Auditor's Responsibilities Relating to Other Information

Fu and Simnett (2023) systematically reviewed all available annual reports and auditor reports issued by Australian listed companies over the period from 2017 to 2022, for an understanding of the reporting practices under ASA 720. Specifically, they explored disclosures relating to: (1) timing of the

receipt - whether the auditor has obtained all, part, or no other information prior to the date of the auditor's report; (2) identification- what specific information is included in the other information; and (3) conclusion - whether auditor has nothing to report or there are material misstatements in other information section.

Some key descriptive findings in Fu and Simnett (2023) include: (1) 85.0% of auditor's reports indicated that they have obtained all the other information prior to the date of the auditor's report, while 14.3% indicated that they received part of the other information and the remaining 0.7% received no other information prior to the date of the auditor's report. (2) There is an increasing trend over the years (from 79.0% in 2017 to 88.4% in 2022) in the proportion of auditor observations that received all other information prior to the date of the auditor's report. This is a positive trend, indicating that the requirement of the auditor to disclose whether they had been provided with this information has potentially facilitated their access to such other information. (3) Large audit clients (i.e., those with higher market capitalization) are less likely to have provided their auditors with all of the other information that is to be disclosed in the annual report prior to the date of the auditor's report. (4) On average, 21.7% of auditors' reports disclosed the details of the specific reports which constituted other information, with auditor's reports being more likely to disclose the specific identification of other information when clients have high market capitalisation (5) The Directors' Report is the most commonly specific type of other information referenced in the auditor's report, followed by the Chairman's Report and the Corporate Governance Statement. (6) A modified audit opinion on the basis of, or related to, other information, is extremely rare (i.e., 3 of 8,940, 0.03%). (7) A small number of auditor's reports failed to follow all the requirements of ASA 720, in that they failed to issue a statement that they have nothing to report (i.e., found no misstatements).

Implications for the AUASB

The key findings in Lum et al. (2023) and Fu and Simnett (2023) collectively provide an understanding of the roles played by both management and auditors in enhancing the credibility of unaudited information.

Findings From Lum et al. (2023) highlight that Australian large listed companies are proactively adopting multiple credibility-enhancing approaches to safeguard the integrity of unaudited information. It is crucial for the AUASB to acknowledge this diversity in practices, as it emphasizes the importance of auditors understanding that specific disclosures might be highly context-specific and rely on qualitative judgements. For example, the company might describe its sustainability commitment to reduce carbon emissions and outline specific targets, but the measurement of the social and environmental impact may not be as straightforward as financial data. In such cases, internal controls and board reviews serve as credible alternatives, offering a cost-effective and affordable approach that not only provides flexibility but also aligns with the practical constraints of the assurance process.

Findings from Fu and Simnett (2023) offer several insightful recommendations: (1) AUASB should consider encouraging a positive statement as to what constitutes other information. In the illustrations to ASA 720, there is an option that the description of the other information can be made in a specific and positive form. For example, "the management report and chair's statement," may be used to identify the other information. However, many auditors chose not to disclose the details of the specific reports which constituted other information. The authors consider that there is greater clarity with the alternative positive form and note the trend to this form of identification. (2) AUASB should consider the communication effectiveness (clarity of, and how financial report users are likely to interpret and respond to the message) of the wording of the example reports contained in ASA 720 about the reliance that the user is expected to place on other information which is reported but was not available to the auditor at the time of the signing of the auditor's report. (3) AUASB should encourage further research into ASA 720, in particular whether certain information contained in the other information section should be subject to assurance, and how terms and statements currently included, such as

other information not being available to the auditor at the time of signing the auditor' report, are impacting on the report user's assessments and decision-making. (4) In the realm of sustainability assurance, it is advisable for reporting entities to provide clear disclosures regarding the definition of "other information" (i.e., information other than sustainability or climate-related information). Furthermore, reporting entities should make every effort to ensure that all other information is provided to the auditor before the date of the auditor's report. Otherwise, they are recommended to disclose what specific information not being available to the auditor at the time of signing the auditor' report. Finally, reporting entities should ensure that the credibility of other information contained in the annual report is clearly communicated to the report user.

In conclusion, this summary offers valuable insights into the dynamics of current practices concerning alternative credibility-enhancing approaches on unaudited information. Such insights are crucial for conducting a thorough cost-benefit analysis to assess the potential impact of the proposed mandate for sustainability assurance within ISSA 5000.

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4.3 Mandatory versus Voluntary Assurance on Sustainability Information

Dr Jenny Yang, UNSW Sydney

Introduction

Extended external reporting on non-financial and sustainability information, as well as the assurance of that information, has witnessed increased demand over the past two decades (KPMG, 2022). Consequently, this surge in demand has led to the development of various sustainability reporting and assurance requirements on an international scale (IAASB, 2023; IFAC, 2023; ISSB, 2023).

Importantly, assurance bestows credibility upon non-financial information, making it an essential tool for enhancing the value of reporting. As a result, there has been a growing discussion about whether assurance for sustainability information should be mandated (Hartman, 2023). While mandatory sustainability reporting and assurance have the appeal of enhancing consistency, comparability and accountability (IAASB, 2023), they also come with additional implementation costs and the risk of suppressing the signal conveyed when companies exercise their discretion in choosing whether to be assured (Lennox & Pittman, 2011; The Treasury, 2023).

This research project is set in the European Union (EU),[8] where the Non-Financial Reporting Directive (NFRD) mandated sustainability reporting for large public interest entities in 2017 under Directive 2014/95/EU. Under the NFRD, EU countries were allowed to mandate various assurance arrangements,[9] where either the sustainability information was assured (assurance), or the assurer signed off that the NFRD directive was followed (sign-off). This then provided an experimental field for studying the effects of mandatory assurance compared to voluntary assurance in jurisdictions where non-financial reporting is mandatory. This can help to disentangle whether assurance itself has economic consequences, or whether there is information in the voluntary choice of assurance (Lennox & Pittman, 2011).

Prior literature

The ability to mandate assurance is an important policy mechanism available to governments for regulating the supply of reliable information to report users in a consistent and comparable manner (Deloitte, 2022; IAASB, 2023). However, there are associated drawbacks with mandatory assurance, including increased implementation expenses and the potential to encourage a mere checklist approach to compliance (The Treasury, 2023). Prior literature has also shown that mandatory assurance may dampen the signal conveyed when companies exercise their discretion in deciding whether to undergo audits (Chow, 1982; Lennox & Pittman, 2011).

Compared to the reporting of financial information, non-financial information is more diverse, more qualitative, and can be more forward-looking in nature. Research on extended external reporting has highlighted the importance of assurance in alleviating concerns about the usefulness of sustainability reporting which are often criticised for being used as a management tool rather than a true mechanism for the discharge of accountability (Cohen & Simnett, 2015). Literature on voluntary sustainability assurance finds that non-financial assurance may increase reporting quality and enhance decision usefulness (Simnett et al., 2009; Ballou et al., 2018; Dal Maso et al., 2020), help to drive positive internal changes, such as accelerating the strategic integration of sustainability initiatives (Ballou et al., 2012), and increase the scrutiny of performance data, such as reducing CSR-related misconduct

8 The coauthors of this research are Prof. Roger Simnett from Deakin University, Dr. Ulrike Thuerheimer from University of Amsterdam, and Dr. Shan Zhou from University of Sydney.

9 The Non-Financial Reporting Directive (NFRD) is the predecessor to the European Corporate Sustainability Reporting Directive (CSRD). The CSRD mandates assurance over sustainability reporting within the EU and becomes effective for the largest companies starting in 2024.

events (Du & Wu, 2019). Nonetheless, studies examining the economic consequences of assurance on non-financial information produce mixed evidence (Casey & Grenier, 2015; Weber; 2018).

In terms of research on mandatory non-financial assurance, empirical evidence is currently limited. Using a setting where the assurance of public resource disclosures made under the JORC Code by Australian Mining Development Stage Entities are mandatory, Ferguson and Pundrich (2015) show very weak evidence of greater abnormal returns when reserve disclosures are provided by specialist mining consultants, suggesting that mandatory assurance has little impact in cases where litigation risk is low. Another study by Kuo et al. (2021), examine listed firms in the food industry in Taiwan that are subject to mandatory assurance and find a reduction in the cost of debt capital associated with such assurance. However, it is important to note that these studies are industry- and country-specific, which limits their generalizability.

More importantly, given that most assurance on sustainability information is currently voluntary, it is empirically challenging to (i) overcome the self-selection bias (ii) disentangle the signalling effect from the actual impact of assurance, and (iii) examine the potential benefits of mandatory assurance versus voluntary assurance (DeFond & Zhang, 2014).

Methodology and data

In this research, we employ a difference-in-differences design, capitalizing on the EU setting. Specifically, in 2014, the EU enacted a non-financial information directive that mandates large public interest entities to prepare annual non-financial reports, beginning from fiscal year 2017 onward. Large public interest entities are defined as those with more than 500 employees and either more than EUR 20 million in total assets or more than EUR 40 million in sales. Regarding the requirements for independent assurance, all member states have transposed the minimum requirement for the statutory auditor to check whether non-financial information has been provided. In addition to the minimum requirement, eleven countries have an additional requirement for the auditor to check the consistency of non-financial information with the financial statements. Lastly, three member states, namely, France, Italy and Spain, require mandatory independent assurance for non-financial information.

We obtained the original sample from Compustat Global. Our treatment group consists of all large listed firms in Spain and Italy, two of the countries where assurance for EER is mandatory.[10] The control group comprises listed firms in EU countries where assurance for EER is voluntary. The matching procedure is based on a propensity score matching (PSM) approach. Specifically, we apply one-to-one matching without replacement with caliper being 0.1. We match on variables including total assets, total revenue, the number of employees, return on assets, leverage, and industry sectors, for the year 2016, which is one year prior to the effective year of the EU Directive.

Next, we extracted data from Compustat Global for the years between 2014 and 2019, and manually identified as many reports as possible that were prepared by the firm using a general searching engine, where non-financial information could potentially be disclosed. We hand-collected data related to non-financial assurance, including whether or not there is an assurance report, where the assurance report is disclosed, who the assurance provider is, the level of assurance, the assurance standards applied, and other relevant details. Financial and sustainability-related data were obtained from Compustat Global and Thomson Reuters ASSET4.

10 France is excluded from our sample because France made sustainability assurance mandatory with implementation of the Grenelle II law (n° 2010-788) in 2010, which was prior to the EU Directive. Therefore, there is a potential for the impact of the EU Directive and mandatory assurance to be confounded.

Preliminary results and implications for the AUASB

We use this research setting to provide empirical evidence on the impact of mandatory sustainability assurance on sustainability reporting outcomes (e.g., standalone vs integrated sustainability reporting), sustainability assurance outcomes (e.g., assurance scope, assurance level, assurance reporting lag), sustainability practice outcomes (e.g., the incorporation of sustainability indicators in executive compensation plans) and capital market outcomes (e.g., cost of debt and capital, analyst following). We compare these outcomes for corporations subject to mandatory sustainability assurance requirements with those in other EU countries that have voluntary assurance.

Our preliminary findings show that non-financial assurance, overall, leads to higher sustainability reporting scores, greater integration of non-financial information into companies' decision-making processes, increased analyst following, and reduced cost of debt. Furthermore, mandatory assurance is significantly associated with expanded assurance scope, and a shorter assurance report lag. On the other hand, mixed results are found when examining the differences between mandatory assurance and voluntary assurance in terms of sustainability practices and capital market outcomes.

By demonstrating the impact of transitioning from voluntary to mandatory assurance on sustainability reporting quality, assurance practices, the integration of non-financial data into decision-making, and capital market outcomes, we provide timely insights for key stakeholders, including standard setters, regulators, practitioners, and academics, who are involved in the ongoing debate surrounding the implementation of assurance requirements for sustainability information. Particularly noteworthy is the relevance of our findings to the IAASB (2023), which is currently seeking feedback on their proposed ISSA 5000, *General Requirements for Sustainability Assurance Engagements,* and Treasury (2023), which is considering extent, nature and timing of sustainability report assurance in Australia. Our research underscores the importance of informed, evidence-based decision-making in shaping sustainability assurance standards.

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5. Perceptions of Audit Committee Chairs, Group Decision Making and Greenwashing

The final academic session explored matters relating to differences in perceptions of the preparedness of the assurance market to carry out financial statement audits compared to sustainability assurance, the costs and benefits of multidisciplinary teams and the susceptibility of climate-related disclosures to greenwashing. These issues are important to consider ahead of implementing a framework for assurance over climate-related information.

Structure of the Session	
Professor Roger Simnett (Deakin University)	Session Chair
Academic Presentations:	Research Topic:
Professor Ken Trotman (UNSW Sydney)	Perceptions of Audit Committee Chairs
Dr Hien Hoang (UNSW Sydney)	Multidisciplinary Assurance Teams

Ms Camille Peng (The University of Sydney)	Greenwashing and the Risk of Material Misstatement
Ms Marina Michaelides (AUASB)	AUASB Wrap-Up

5.1 Perceptions of Audit Committee Chairs

Professor Ken Trotman, UNSW Sydney

Introduction

The AUASB has adopted an evidence-based approach to audit standard setting (Garg, Peach, and Simnett 2020). The Deakin–AUASB Sustainability Assurance Academic Research Workshop is a major advance in this program. In this overview, my aim is to provide the AUASB with evidence on the views of Audit Committee Chairs (AC Chairs) of large Australian companies. These Chairs play a particularly important role both because of their interactions with both management and auditors prior to the formal audit committee meetings as well as their role in chairing the formal audit committee. As a sub-committee of the Board of Directors, they both review and approve and thus take responsibility for any information released to the public. As such they are a very important group in the reporting eco-system, but a group that the AUASB only hears from infrequently.

The views that I outline in this summary are based on research I have conducted with my colleagues using interview data from a range of current research papers including Free, Trotman and Trotman (2021), Simnett and Trotman (2022), Simnett, Trotman and Trotman (2023), Trotman, Phua, Trotman and Wright (2023). In addition, Bradbury and Simnett (2023) undertook an interview study of AC Chairs very similar to Simnett and Trotman (2022), and thus I have reviewed this study for parallels or divergences to Simnett and Trotman (2022), with respect to implications for the AUASB. Although some of these papers are still being refined, I draw on some of the key findings with the aim of providing information to the AUASB in their deliberations on the proposed new assurance standard, ISSA 5000, *General Requirements for Sustainability Assurance Standards*.

What we know about AC Chair perceptions from research

Interviews with 24 AC Chairs of large Australian listed companies in Free, Trotman and Trotman (2021) focussed on the interactions between the audit committee and the financial statement auditor. These interviews described the importance of the interactions between the auditor, management and the audit committee (consistent with IAASB 2014), the importance of the wide range of expertise on the audit committee, the importance of pre-meetings between the AC Chair and the lead audit partner, and the AC Chair involvement in the resolution of contentious issues between the auditor and management.

Recent interviews by Simnett and Trotman (2022) involved interviews in 2022 with 21 AC Chairs of ASX 300 companies focusing on what AC Chairs saw as to be good audit quality and the present audit quality in the Australian market. At the end of each of these interviews we switched focus to sustainability assurance. The sustainability assurance issues are explored in more depth in Simnett et al. (2023).

Implications for the AUASB

There were some clear differences between how the AC Chairs perceived financial statement audit and sustainability assurance which has implications for the challenges for standard setters related to sustainability assurance. While it was unanimous among the AC Chairs that there was a high level of satisfaction with the quality of financial audits in Australia, a number of the reasons given for this

conclusion are unlikely to apply to sustainability assurance. This raises issues for the AUASB to consider. First, for financial statement audits, for the issues facing the organisations of which they were the AC Chairs which were generally large organisations with global operations, the accounting profession, and in particular the Big 4, were seen as having the skill set, global scale and needed experience to deal with these issues. However, when discussing sustainability assurance, there was more variation in the responses as to whether there were sufficient skills in the market to carry out some aspects of sustainability assurance. Second, while AC Chairs had great confidence in the management and systems providing the financial reports, there was less confidence in the systems and skills providing the content of the sustainability information reported. Third, in discussing financial statement audits, AC Chairs noted that in addition to the present auditor, they were commonly using two or more other Big 4 firms to provide these other services. As a result, given that only the Big 4 firms were seen as capable of providing audit services given the organisation's size and global reach, often they only had the choice between the incumbent auditor and one other firm if they put the audit out to tender. This does mean that in addressing the question of whether the financial statement auditor is also the sustainability assurer there often will not be another alternative.

AC Chairs were found to be overwhelmingly in favour of any sustainability information being externally reported being assured. This information was seen as being demanded by stakeholders including shareholders and the accuracy of disclosures was considered to be important. Interviewees also referred to the benefits of receiving feedback on their control systems and reducing the risk of misleading long-term targets. However, there were some major qualifications to the above conclusion. There were concerns about distinguishing between what could be assured and what must be assured. Related, there was reference to the clear guidance on relevant materiality thresholds. A number proposed a gap of a couple of years, between compulsory sustainability reporting and compulsory sustainability assurance (not discounting voluntary sustainability assurance for this interim period). This was to allow the bedding down of reporting systems, although recognising that reporting needed to be down on a best effort basis for this period. Othe mechanisms other than compulsory assurance, including voluntary assurance, could be considered. Reasonable assurance was also seen is investment grade, although limited assurance on some aspects, such as scope 3, and some forward-looking statements was seen as appropriate. Cost considerations of compulsory assurance were also raised and again related to a materiality threshold. Also, questions were asked by AC Chairs about what a reasonable timetable for the introduction of compulsory assurance is. Their concern was that if compulsory assurance was required too early there will be too many qualified assurance reports given the present lack of development of the appropriate systems. The issue was also raised that early adoption of compulsory assurance may stifle innovation in reporting. That is, company sustainability disclosures are still evolving, and given the desire for relevant company specific information, such innovations should be given some time to develop.

The introduction of greater sustainability assurance was also seen as creating new challenges for governance structures in organisations, and the role of audit committees. Of particular note for the AUASB, it was found that, at least currently, not all decisions of sustainability reporting assurance are residing with the audit committee. Quite commonly it was found that any discussions on sustainability reporting and assurance are currently involving the full Board for the preliminary or current discussions. Where sub-committees are involved, a much wider group of sub-committees are potentially involved in any discussion on assurance of sustainability information. Our recent interviews suggest that these discussions may be at the audit committee, but may also be at a risk committee or sustainability committee, if such exist. Many Boards are currently considering their structure of sub-committees as a result of the significant additional attention that Boards are placing on sustainability information. This means that assurance providers will potentially be faced with various corporate governance structures. In virtually all instances where other sub-committees are involved, the AC Chair is also a member of the other sub-committees so can provide an audit committee view to these decisions. Even in the isolated instances where the AC Chair was not a member of a relevant sub-

committee the expectation is that they would attend any meeting related to reporting, assurance and assurance provider of sustainability information. It also suggests the need for new skills on the audit committee with suggestions that audit committee members are undertaking training in sustainability issues.

AC Chairs further outlined their desire to have consistent worldwide sustainability reporting and assurance requirements. They discussed the frustration for those tasked with the production of sustainability information related to the different reporting requirements within different jurisdictions. AC Chairs referred to the differences between jurisdictions (with some in particular emphasising the differences between the USA and the rest of the world) as well as the frequent changes in sustainability requirements. Concerns related particularly to the difficulties associated with having to regularly update systems to provide additional sustainability information and deciding on which measures it is necessary to report on and how to measure these items. Also, while there was support for sustainability assurance, there were concerns about the cost of assurance and the suggestions on what were the appropriate levels of materiality and whether systems were strong enough to provide the necessary data.

On the issue of who should provide sustainability assurance, there was a strong preference for the assurance provider to come from the same firm as their financial statement auditor. Reasons given included the overlap of assurance tasks between sustainability assurance and financial statement audit, with much of the same information coming from the same systems or systems overseen by the same manager. With both audit and assurance providers needing to have a good understanding of the business strategies and underlying business models and related corporate structures of the organisation, there was seen to be synergistic benefits in having the same assurance provider. Further a better knowledge of sustainability issues was seen as aiding the financial statement audit, with a much greater emphasis on how sustainability issues were impacting on financial statement considerations, such as those outlined in the publication of the AASB-AUASB (2018). Adding to this, the increasing prominence of integrated reporting concepts in reporting by major Australian organisations, and the expectation that at least some sustainability information will be reported in the general purpose financial report (irrespective of whether the sustainability information is contained in the financial statements, in which case it is covered be the financial statement audit, or in other information to the annual report, in which case it is covered by ASA 720) provides an environment where it was commonly seen as making sense that the same firm as the financial statement auditor provide sustainability assurance.

Only one AC Chair raised concerns about using the same firm as their financial statement auditor as their sustainability assurance provider, and this was because the level of non-audit services provided by the financial statement auditor had been considered high in the past. They however agreed that a better delineation between non-audit fees and assurance fees would help to address these concerns, perhaps through clearer delineation of such fees in the note on fees paid to the financial statement auditor. AC Chairs generally agreed that any independence concerns could be dealt with through various safeguards such as use of different teams for such engagements. A couple of AC Chairs emphasised the fact that in any presentations or presentations of audit/assurance partners to the audit committee, they expected to see a clear understanding by both partners of issues which were relevant to both engagements, and both partners contributing positively to any discussion.

The issue of limited choice and capability of suppliers of this assurance was raised. Our interviewees generally had a preference to stay with the Big 4, which had been seen to be ramping up their capability in the areas of sustainability assurance. However, if compulsory assurance was introduced too quickly and across may reporting organisations this was seen as stretching the current capacity of assurance providers.

In an equivalent study, Bradbury and Simnett (2023) undertook interviews of 20 AC Chairs of large New Zealand companies. Similar findings to those reported in Australia were found, although in some

cases the thinking was more progressed as far as likely assurance providers, and therefore in the main the implications for the AUASB were similar. A couple of differences were observed. While most of the AC-Chairs did have a preference for using the same firm for providing both sustainability assurance and financial statement audit, a role was commonly seen for consultants and potential sustainability assurance providers from outside the accounting profession. This appeared to be related to the good experiences associated with using these non-accounting firms in developing in-house systems and processes. In addition, a number of New Zealand AC-Chairs emphasised not only the alignment of sustainability reporting and assurance requirements with the rest of the world, but particularly highlighted the importance of alignment with Australian sustainability reporting and assurance requirements, given the current agreements between the two countries and the large number of New Zealand companies dual listed in Australia.

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5.2 Multidisciplinary Assurance Teams

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Introduction

Auditors have worked in teams to make judgments and decisions together in financial audit engagements, and prior literature has examined the effect of different team formats on the audit teams' performance. However, the differences in the sustainability assurance context, such as the diversity in education background and expertise between assurance team members, give rise to new

challenges in enhancing the performance of multidisciplinary assurance teams. This summary will cover the literature on multidisciplinary GHG assurance teams and implications for AUASB.
Studies in the fraud brainstorming literature have examined the effect of different team formats, such as nominal vs. interacting teams, face-to-face vs. electronic teams, and unguided vs. guided teams, on the team performance in fraud risk identification, hypothesis development and assessment. Altogether findings from prior brainstorming studies in financial auditing context suggest that when audit team members work together, there can be process gains (for example, cognitive stimulation and group synergy) and process losses (for example, production blocking and social loafing) affecting the teams' overall performance.

In the sustainability assurance context, the assurance of GHG or other sustainability-related subject matters requires both accounting and non-accounting knowledge, resulting in multidisciplinary assurance teams with diversity in education backgrounds and expertise (accounting vs. science/engineering). Such a significant variation in the types of expertise and knowledge between assurance team members will alter the extent and nature of process gains and losses in GHG brainstorming sessions. Due to the unique differences in the GHG assurance setting, findings in financial fraud brainstorming setting may not completely replicate. The next section will discuss studies examining the performance of multidisciplinary GHG assurance teams.

Prior literature

Guidance from the IAASB recognises the benefit for a multidisciplinary team to be involved, and the necessity to integrate the work of assurance experts (with financial audit background) and subject matter experts (with scientific background) to ensure they are working effectively as a multidisciplinary team (IAASB 2021). There is, however, limited empirical evidence on how these multidisciplinary assurance teams work and how to improve the performance of such teams.
In a simulated multidisciplinary team setting, Kim, Green, and Johnstone (2016)' experiment finds that accounting assurers inappropriately over-rely on an explanation provided by a science-expert assurer, even though this explanation is inconsistent with other audit evidence and covers an issue that does not require specialised science knowledge. This inappropriate reliance is reduced by having a reviewer with accounting expertise. This suggests there can be source credibility biases in processing evidence within the multidisciplinary assurance team.
Ekasingh, Simnett, and Green (2019) ask GHG assurers to recall their experience on one GHG assurance engagement where there is effective teamwork and one GHG assurance engagement where there is less effective teamwork. They find that teams with more educationally diverse members are more likely to perceive that they have sufficiency of elaboration (that is, the exchange, discussion, and integration of relevant information) on diverse perspectives and perceived the team members worked more effectively together. This suggests having accounting and non-accounting assurers work together in a multidisciplinary assurance team can induce elaboration of diverse ideas which eventually benefits the team performance.

Current study: Ekasingh, Hoang, and Trotman 2023

Our study examines the effect of different team formats on the performance of multidisciplinary teams in a GHG assurance task, using a controlled experiment. Three different team formats (nominal, interacting, and review teams) suggested by the previous literature to affect the performance of audit teams are compared. The process gains from cognitive stimulation in interacting GHG assurance teams may be amplified by the complexity of GHG risk identification task which requires two different types of expertise and knowledge from accounting and non-accounting assurers to be shared, exchanged and integrated. In contrast, the process losses from production blocking and social loafing in interacting groups may also alter as team members are aware of each other's important, unique

expertise but have another barrier in technical language and communication to overcome to achieve effective teamwork.

In the nominal team, an assurance expert (with financial accounting background) and a subject matter expert (with science/engineering background) work individually in identifying risk factors for a GHG assurance engagement, and their unique risks are later combined to make the team' final list. In the interacting team, an assurance expert and a subject matter expert work together to come up with the risk factors. Finally, the review team was operationalised by having an assurance expert review the work of a subject matter expert. GHG assurers from the Big Four firms in Australia participated in this study, randomly assigned to multidisciplinary GHG assurance teams comprising an assurance expert and a subject matter expert.

We have the following main findings. First, interacting teams underperform both nominal teams and review teams in quantity and quality of risks generated. This suggests that process losses outweigh process gains in interacting multidisciplinary assurance teams. While interacting teams may benefit from exchanging and integrating their diverse knowledge and perspectives, they also suffer from the lack of overlap in their frames of reference and technical language. Second, we find that assurance experts and subject matter experts focus on different types of risks, with assurance experts generating more risks associated with comparing the subject matter with suitable criteria and subject matter experts generating more risks associated with scientific measurement of the subject matter. These findings provide evidence of cognitive diversity and potential benefits from the complementary knowledge and perspectives generated by assurers with different backgrounds, and that future research should explore ways to minimise process losses in order to realise these potential benefits of multidisciplinary assurance teams.

Implications for the AUASB

Studies in this area provide supporting evidence that combining assurance experts and subject matter experts into multidisciplinary teams brings benefits. For example, Ekasingh et al. (2019) provide evidence more diverse teams are more likely to have greater elaboration on diverse perspectives, which eventually enhances assurance teams' performance. In addition, Ekasingh et al. (2023) show that assurance experts and subject matter experts focus on identifying different types of risks, which is another evidence of cognitive diversity and unique contributions from each type of expert, supporting the need for sustainability engagements to be performed by multidisciplinary teams.

In contrast, studies in this area also highlight potential pitfalls in integrating the work of assurance experts and subject matter experts. First, Kim et al. (2106) demonstrates that there can be biased evidence processing within the teams, as accounting experts overweigh the evidence suggested by science experts. As a result, a potential implication for AUASB and other standard setters is to consider providing guidance on how to overcome this source credibility heuristic, and a potential mechanism put forward by Kim et al. (2016) is having a review process conducted by an accounting expert. Second, Ekasingh et al. (2023) demonstrate that simply letting assurance experts and subject matter experts interact and integrate their ideas in an unguided brainstorming session can cause more process losses than process gains as team members lack the common frames of reference and technical language to communicate and build on each other' ideas, affecting the team performance in identifying fraud risk factors. As a result, a potential implication for the AUASB and other standard setters is to consider providing more guidance on how the work of assurance experts and subject matter experts can best be integrated. A suggestion from Ekasingh et al. (2023) is that interaction should not be the first stage of the group process and that all team members should generate ideas individually at some point in the process. Another implication is to encourage firms to conduct more cross training sessions to improve the cross understanding between assurance experts and subject matter experts, which can eventually benefit their teamwork.

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5.3 Greenwashing and the Risk of Material Misstatement

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Introduction

Greenwashing has been a long-standing criticism associated with sustainability disclosures. Recent years have witnessed clustered legal and regulatory actions worldwide addressing greenwashing. In November 2022, the International Organization of Securities Commissions (IOSCO) issued a call for actions that would curb greenwashing among asset managers and data providers in the financial sectors. In response, the Australian Securities and Investments Commission (ASIC) in Australia published an informational document (Info Sheet 271), providing strategies to prevent greenwashing claims. From 1 July 2022 to 31 March 2023, ASIC also executed 35 actions to address greenwashing issues with various organizations. Concurrently, the Australian Competition and Consumer Commission (ACCC) launched an online sweep to understand greenwashing claims on consumer products.

Moreover, on March 29, 2023, a Senate inquiry into greenwashing began, with a report expected in December 2023. This inquiry drew significant attention from the public, receiving 126 submissions from legal entities, academic institutions, NGOs, and individuals etc. Notably, 'assurance' was a prevalent topic discussed in 28 of these submissions.

Taking advantage of the recent clustered legal and regulatory actions, this project aims to provide insights into the concept of greenwashing from a regulatory perspective by (i) examining the documentary evidence of cases studies and recently released regulatory guidance on greenwashing and (ii) interviewing staff from organizations engaged in taking actions against greenwashing. In addition, this study would seek to develop a computerized tool to aid the current manual greenwashing detection process, and to explore the role of third-party sustainability assurance in reducing greenwashing claims.

Prior Research

What is greenwashing?

Prior literature generally describes greenwashing as a selective disclosure of positive environmental or social performance and/or symbolic representation without substantive actions (e.g., Lyon and Maxwell, 2011).

The definition of greenwashing from regulatory bodies however emphasizes the misleading impact on information users including investors and retail customers. For example, ACCC define greenwashing as: 'A term used to describe false or misleading environmental claims. (ACCC, 2023a)', and ASIC defines it as 'The practice of misrepresenting the extent to which a financial product or investment strategy is environmentally friendly, sustainable or ethical (ASIC, 2022).'

With the recent clustered regulatory and legal actions against greenwashing, the definition of greenwashing is being shaped by individual cases. We learn from these cases that greenwashing can be associated with a variety of subject matters ranging across metrics, claims, labels, to image. Further, the definition of greenwashing can be very industry specific. For example, most cases against greenwashing in Australia relate to the asset management and energy sectors (ASIC, 2023). In the Asset Management Industry, greenwashing is defined as: 'Overstating the adherence to ESG screening criteria, leading to discrepancies between advertised commitments and actual practices.' In the energy sector, companies often make bold climate claims without scientific evidence or groundwork (e.g., substantive modelling, investigation). Thus, the definition of greenwashing is 'Promising future climate-related achievements, such as net zero emissions, without providing a credible foundation or thorough evidence for such claims.'

How do regulators identify greenwashing?

ASIC and ACCC are two primary Australian regulators stepping up efforts against greenwashing. They adopt both proactive and reactive approaches in combating greenwashing. For ASIC, the proactive monitoring includes 1) Managed Funds: Review of 122 Product Disclosure Statements (PDSs) and in-depth analysis of the investment processes of 17 funds 2) ESG Disclosures on ASX: Supervision of ESG-related disclosures by companies targeting retail investors (ASIC, 2023). The reactive Approach includes addressing complaints related to potential greenwashing. These complaints are mainly made by Non-government organizations (NGOs).[11]

In contrast, ACCC is in the nascent stages of comprehending greenwashing and it has not taken major legal action against greenwashing. In October 2022, ACCC conducted an online sweep against greenwashing, assessing 247 businesses across various sectors (ACCC, 2023b). The results have helped ACCC to identify 1) Cosmetics and personal care 2) Textiles, garments, and footwear 3) Food and beverage products as the three key sectors with the highest greenwashing risk that requires further proactive investigation. Similar to ASIC, ACCC also addresses complaints concerning ESG issues received through its information centre.

Legal/regulatory actions on greenwashing

The regulatory actions taken on greenwashing could take a variety of forms. For example, ASIC issued 1) 23 corrective disclosures, 2) 11 infringement notices, and 3) one civil penalty proceeding between July 2022 and March 2023 (ASIC, 2023). With an additional $4.3 million funding to ASIC from the government in April 2023 to combat greenwashing (Australian Government, 2023), there is likely to be an increase in ASIC's greenwashing oversight efforts.

11 NGOs play an important role in the legal/regulatory actions against greenwashing. They scrutinize companies for greenwashing activities, undertake investigations, file complaints with ASIC and ACCC, and take companies to court over greenwashing claims. An example is the 2021 case where the Australasian Centre for Corporate Responsibility (ACCR) sued oil company Santos over its net zero emission plan, formulating the world first court case to challenge the truthfulness of a company's net zero emission plan. The case is still ongoing.

While ACCC has not yet initiated a legal action, it is equipped with a toolkit of potential enforcement actions which includes 1) administrative resolutions, 2) issue infringement notices, 3) set Section 87B public enforceable agreements, and 4) pursue legal proceedings (ACCC, 2023c). The type of actions to be pursued are mainly determined by the severity of the misleading claim, the complexity of substantiating the greenwashing case, and the size of the greenwashing entity.

Implications for the AUASB

Greenwashing, particularly those targeted/enforced by regulatory actions has relevance to the auditing & assurance profession given (i) the risks of material misstatement and (ii) stakeholders' expectations.

Greenwashing as a risk of material misstatement

Greenwashing can arise from potential material misrepresentations on claims made in annual and sustainability reports. This is particularly the case when it comes to climate-related disclosures as evidenced in recent legal and regulatory actions. For example, Santos was taken to court for its "net-zero" claim made in the Message from the Chairman and Managing Director and Chief Executive Officer Section of the company's annual reports without a well-defined plan to achieve the target (ACCR, 2021). Similarly, Tlou Energy Limited and Black Mountain Energy Limited were issued infringement notices by ASIC with a fine of AUD $53,280 and AUD $39,960 respectively for claims of "carbon neutral", "low emissions', "clean energy" and "net-zero carbon emissions" made in their operational report and investor presentation (ASIC, 2023). While operational report and investor presentation may not subject themselves to audit, "Message from the Chairman and Managing Director and Chief Executive Officer Section" of Santo's annual report falls into auditors' responsibility for "other information" under ISA/ASA 720 *The Auditor's Responsibilities Relating to Other Information*, hence giving rise to the risks of material misstatement.

Another high-profile case on misleading sustainability claim is the Vale case in the U.S., where Vale has agreed to pay $55.9 million USD in fines for its materially false and misleading statements made in its 2016 and 2017 sustainability reports regarding the audited stability structure of the Brumadinho dam (SEC, 2022). Disclosures in stand-alone sustainability reports could fall under auditors' responsibility for other information as required in ISA/ASA 720. In addition, and interestingly, both sustainability reports are assured by third parties, demonstrating the gap/limitation of sustainability assurance in preventing greenwashing claims.

As mentioned earlier, the asset management industry is one of the most targeted industries for greenwashing claims. Several investment funds were found to fail to adhere to their negative investment screening commitments which typically excludes investments in sectors with significant ESG risks, such as fossil fuels, nuclear power, alcohol, tobacco, gambling, weapons or adult entertainment. Given that the super funds are now required to disclose current holdings (Parliament of Australia, 2021), and they often disclose investment strategy e.g., positive/negative screening, net zero commitment and overview of top shareholdings in their portfolio in their annual reports, these disclosures would give rise to risks of material misstatement under ISA/ASA 720.

These cases underscore how greenwashing can be seen as non-financial fraud, which is of high relevance to auditing and assurance profession. They also highlight the importance for assurance provider to be aware of all greenwashing actions of regulators, as they may be suggestive of risk of material misstatement in company disclosures, or certain management behaviours that warrant auditor/assuror attention. Although the word of "greenwashing" is not referred to in International Standard on Sustainability (ISSA) 5000 (IAASB, 2023), the International Auditing and Assurance

Board (IAASB) is seeking public comments on if the exposure draft of ISSA 5000 appropriately addresses the topic of fraud (including "greenwashing") by focusing on the susceptibility of the sustainability information to material misstatement, whether due to fraud or error (IAASB, 2023).

On the other hand, greenwashing claims involves a wide range of subject matters disclosed in a variety of venues and some of them may not subject to any form of third-party assurance. For example, information disclosed on websites and social media. In addition, third-party assurance is typically engaged on a company level disclosure such as the sustainability report, while greenwashing claims can by commonly associated with product level disclosures such as a particular investment product and/or a consumer product.

Stakeholders' view of sustainability assurance in reducing greenwashing

Stakeholders believe sustainability assurance can help reduce greenwashing, but there's a need for caution concerning greenwashing issues. A Senate submission[12] indicated the difficulty in verifying sustainability data. The comment letter expressed concern over the ineffectiveness of existing financial audit independence arrangements. The expectation is that audits should offer credible validation for all mandatory metrics and partial validation for the rest of the details in the reports, including a thorough review of any potentially omitted information. It referenced a 2021 Carbon Tracker study which found that, of 107 companies analyzed, 80% of auditors seemingly overlooked climate risks, and 63% failed to spot inconsistencies in climate targets throughout business reports. The letter further emphasized:

> *"Audits should offer solid verification of all obligatory metrics, give limited assurance on the rest of the document, and specifically address any potential omissions in reports. Those providing assurance must adhere to stringent independence and quality control standards. The prevalent practice where a firm chooses and compensates its own auditor poses a challenge to true independence."*

Specifically, we learn from the regulatory actions that auditors/assurors should pay close attention to some high-risk sectors prone to greenwashing claims such as Asset Management and Energy sector. In Asset Management, the ESG investment screening process is often the target of greenwashing. Assurance procedures should provide verification of documentary evidence supporting the ESG screening, checking for inconsistencies between stated investment strategies and actual portfolios, and confirming robust internal controls. In the Energy sector, claims about net zero and carbon neutrality need to be validated due to their importance for maintaining a company's social license. Assurance tasks should include assessing the feasibility of climate commitments, confirming adequate documentation for funding net-zero initiatives, ensuring thorough scientific validation for projects, and consulting external experts on technical aspects like energy consumption.

Further Research Work

In the next phase, machine learning tools will be developed to assist in identifying organizations suspected of engaging in greenwashing behaviours. One example of the use of the tool is to identify inconsistencies in sustainability claims across different disclosure venues and to identify vague claims without substantiating evidence. Furthermore, the project will explore if there are gaps in current sustainability assurance and greenwashing claims by mapping the subject matters of sustainability

12 The no.94 submission by Australia Centre for Corporate Responsibility to Senate Inquiry into Greenwashing.https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Environment_and_Communications/Greenwashing/Submissions

assurance to those of greenwashing claims. The outcomes are expected to be informative to standard setters such as the AUASB in refining the assurance standard of sustainability information.

Summary

The global effort towards sustainability has led to an increased awareness and scrutiny of greenwashing. Regulatory bodies in Australia are actively stepping up their efforts to combat deceptive sustainability claims made by companies. Preliminary findings highlight the complexity in defining greenwashing, given the wide range of subject matters that greenwashing can be associated with and the variety of venues that greenwashing claims can be made. Climate-related disclosures made in companies' annual/sustainability reports are of particular relevance to AUASB for the risk of material misstatement.

The recent clustered legal and regulatory actions demonstrate greenwashing isn't just an ethical concern but also poses substantial financial, reputational, and litigation risks for companies. Assurance providers should be aware of regulatory actions on greenwashing and keep close eyes to claims prone to greenwashing, particularly in high-risk industries like asset management and energy. Current stakeholder sentiment towards sustainability assurance is a mix of expectation and caution. While assurance is seen as a way to curb greenwashing, whether sustainability assurance could or should be expected to cover the wide range of potential claims prone to greenwashing is open to debate.

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