New Assurance Issues
ASSURANCE FOR SUSTAINABILITY

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SUSTAINABILITY

- The Earth is a holistic and subtle bio-system where land, water and air interact and blend to generate and support all life
- corporate sustainability reporting and assurance tend to be responsive or reactionary to the impact of industrialisation on 'life'
- mostly voluntary at this time
- Legislation and a regulation disparate regarding disclosures and associated assurance
- the current accounting conceptual framework defines assets and liabilities in terms of 'economic' future benefits or losses.
- this economic focus tends not to value vital life elements such as air, water and land since neo-classical economic theory views these resources as infinite.
- Unless for economic production eg mining, agri-business

HOT TOPIC: climate change and associated risks

- climate change and associated business risks

"everything old is new again" Bob Fosse ' All that jazz'

- Global warming alarm – 1970's but regulators reluctant to act
- Increasing extreme weather events hurt business
  - Floods, droughts, rising sea levels – Science - CSIRO and IPCC – Stern Review (2006), Garnaut (2008, 2011).
- For example, 60+% of Qld's open cut coal mines flooded for several months – closed for business
- BHP reported 30% loss of revenue from their flooded Qld mines so far – direct financial impact


NORTH POLE
MELTING.
SLEIGH BELLS
ALL FINISHED.
DEAR SANTA
DEAR SANTA...
Leunig

Some factors driving interest in GHG reporting and assurance re climate change risks

- Widespread community concern about human induced global warming and associated climate change
- Supported by science

International – Kyoto Protocol

- UN Global Reporting Initiative (GRI now version 3)
- Investors - Carbon Disclosure Project and associated Climate Disclosure Standards Board
- Climate Change Reporting Framework (CCRF)

Australia – Carbon price and future ETS

International Kyoto - GHG reporting & assurance

- Kyoto Protocol (1997) - UN international treaty – an agreement to reduce GHGs re global warming and associated harmful climate change
- Kyoto strategy – to establish an international network of emissions trading schemes – carbon (GHG) price
- Six gases identified by the Kyoto Protocol: *carbon dioxide*, methane, nitrous oxide, hydrofluorocarbons, perfluorocarbons, and sulfur hexafluoride.
- Influence national policy and corporate response

World Bank's Carbon Market 2011 Report

- After five consecutive years of robust growth, the total value of the global carbon market stalled at $142 billion
- International regulatory environment remains uncertain,
- national and local initiatives may offer the potential to collectively overcome the international regulatory gap.
- During 2010, the Australian government announced plans for a carbon price mechanism with a three-to-five-year annually increasing fixed-price period that will transition into an emissions trading scheme.
- The government aims to price carbon by July, 2012, subject to negotiating an agreement and passing legislation in July 2011.

Kyoto to National Policy to Corporate Response

- Australia - Carbon price – hot political debate- misnamed a carbon tax - forerunner of a emissions trading scheme
- First measure and report Greenhouse Gases
- *National Greenhouse Gas Reporting Acts (2007-9)*
- The NGER System establishes a national framework for greenhouse and energy corporate reporting by industry to meet the current and prospective reporting needs of government, business and the public.
- 2009-2010, 700 companies registered, about 300 reported
- NGER Act establishes auditing or assurance of corporate greenhouse and energy reports as a key measure for monitoring corporations' compliance with the Act.
- Reports to the Greenhouse and Energy Data Officer (GEDO) or regulator
- EG BHP Billiton - Energy Efficiency Opportunities public report

Proposed Australian ETS

Cap and Trade Scheme – Cap is under political discussion

- Primary markets trading emissions' permits
  - allocated free by Government to trade affected industries
  - or purchased by companies via auction but possibly undervalued depending on GHG cap – political decision
- secondary markets
  - derivatives , hedging for corporate GHG/carbon risk
- Can accounting standards be used for these transactions and therefore reported in the GPFR and assured?
  - Fair value – permits as in the withdrawn 'IFRIC 3'
  - Financial instruments

Accounting for emissions' permits

- Deloitte partners Rohrig and Davis (2009, p. 4) point out:
- "The initial recording of emission allowances is also widely debated, in part due to the common practice of regulatory agencies freely allocating (or allocating at a below-market cost) many allowances to regulated entities. The two possible accounting value models for initial recognition are 'cost' and 'fair value'.

- Despite general guidelines that purchased intangibles or inventory be measured at cost, there is debate over whether allocated allowances are 'purchased,' and there are not many other analogous instances where an asset with a verifiable value is received for free. Furthermore, IFRIC 3 (prior to withdrawal) supported a fair value approach (albeit with concomitant recognition of an offsetting governmental grant)."

International NGOs promulgate standards for reporting and assurance for

- example reporting standard UN's Global Reporting Index (GRI)
  - corporate strategy and vision,
  - water,
  - biodiversity,
  - atmosphere eg ghgs
  - waste reduction
  - Energy
  - Employee relations, work practices
  - Human rights
- Carbon reporting and assurance ISO 14064-3
- Environmental Management Systems ISO 14001-1 – includes internal audit mechanism
- Energy Management Systems ISO 15000 (recent)
- Climate Disclosure Standards Board (CDP)

Climate Change Reporting Framework – World Business Summit on Climate Change – Edition 1 Sept 2010

- The CCRF is a voluntary framework to be used for the disclosure of climate change-related information in, or linked to mainstream financial reports.
- It is aligned to relevant principles and objectives of financial reporting specified in materials published by the International Accounting Standards Board (IASB), but neither the IASB nor its member bodies have been consulted on the positions taken in the CCRF.

CCRF assurance

- Under International Standards on Auditing (ISA 720) the financial statements auditor is required to read the information accompanying audited financial statements to identify any material inconsistencies between it and the audited financial statements and to consider any observed material misstatements of fact in those disclosures.
- This minimum level of auditor involvement ordinarily results automatically from including climate change-related disclosure in mainstream financial reports.
- For assurance beyond minimal level of assurance the professional advisor is encouraged to use existing assurance standards: ISAE 3000, ISO 14064-3 (2006), AA 1000


ACCORDING TO OUR BEST CALCULATIONS WE WILL MAKE A MINT OUT OF CARBON TRADING BUT ALMOST ZERO IMPACT ON GLOBAL WARMING
SOUNDS LIKE A WIN-WIN SITUATION TO ME.
SPOONER

RESEARCH: Some companies are reporting and assuring sustainability now – Why?

- "Sustainability embracers seize the advantage" - competitive edge, early adopters
- sweet spot in the adoption curve - MIT Sloan Management Review in collaboration with The Boston Consulting Group
- Tracking down the 'sustainability embracers'
- KPMG and the Group of 100 (G100) publish, *Managing Financial Impacts and Reporting of Carbon Emissions: A guide for CFOs.*
  - Carbon emissions data may be reported in many forms such as NGER/CPRS reports, financial statements and sustainability reports. As a result, the linkages between emissions-related reporting, both in terms of consistency of data and assurance coverage, needs to be considered by CFOs.

The reporting and assurance conundrum

- Disparate reporting and dimensions disclosed in various channels eg annual reports, stand-alone-sustainability reports, corporate websites
  - Economic performance in the financial reports – mandatory assurance and highly regulated
  - Current conceptual accounting and auditing frameworks focus on economic aspects of corporate value-adding - wealth = profit?
  - 'Life' is atomised for reporting economic & production purposes
  - Land and water reported and assured if monetised eg rehabilitation of land or sea bed post extraction in some accounting standards
  - Social and community eg employee information, human rights mainly voluntary exceptions eg employee benefits in accounting standard

The Way Forward -The push for Integrated Reporting

- Corporate economic performance reported in highly regulated (GPFR) financial statements for shareholders as per Corporations law 2001
- Supported by codified accounting and auditing standards
- Assurance performed by well-trained 'accountant' auditors

The Way Forward - The push for Integrated Reporting

- Corporate sustainability performance includes social and environmental issues are mainly voluntary
- A minority of listed companies report and fewer assure these reports
- Assurance performed by ‘accountant’ auditors and consultants
- training in the acceptable reporting standards and associated assurance for sustainability or GHG emissions
- Assurance tends to be ‘limited’

Example: BHP Billiton 2010 sustainability framework assurance

- GRI application assured by consultant ‘net balance’ (Australian) received A+
- sustainability elements assured by KPMG – limited review ISAE 3000
- Health and safety assurance PWC – limited review
- Consistency, credibility guidance through regulation of sustainability reporting as for financial statements.

Student learning

- student awareness of business risks associated with climate change
- An important audit skill is the auditor's ability to recognise risk factors and then link risk factors to specific assertions made by management that might be misstated in the financial reports
- Integrate into course through sensitising students to the sustainability issues and GHGs – media, case studies
- Assignment/ project -

ASSESS CARBON-RELATED RISKS AND OPPORTUNITIES (Lash & Wellington, 2007)

Consider how the following risks could hurt— or present opportunities to help business re corporate client:

- Regulatory—mandatory emissions reduction legislation
- Supply chain—suppliers' passing their higher carbon-related costs to you
- Product and technology—rivals' developing climate-friendly offerings before you do
- Litigation—lawsuits charging you with negligence
- Reputation—destructive consumer or shareholder backlash
- Physical—damage to your assets through drought, floods, and storms

Thankyou
Questions?