



GUIDANCE ON THE ROLE OF THE REGISTERED AUDITOR IN RELATION TO SUSTAINABILITY INFORMATION

HOW TO PREPARE

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Non-financial or sustainability information

Capital markets play a crucial role in achieving the climate goals set out in the EU Green Deal and the Paris Agreement 2050. The success of the EU's sustainable funding programme depends on the availability of relevant, comparable and reliable data. In addition, stakeholders' demands for information, both financial and non-financial or sustainability-related, are increasing significantly. Non-financial reporting requirements are part of the broader area of corporate social responsibility.

The way in which organisations report on their role in society is changing rapidly. More and more organisations have understood this and are using their non-financial and sustainable development reports to fulfil this role. Organisations prepare these reports on the basis of regulations (e.g. the European Directive on the disclosure of non-financial information, currently being amended by the proposal for a European Directive on corporate sustainability reporting) or on a voluntary basis, using various recognised frameworks or standards for the preparation of such reports, such as those developed by the Global Reporting Initiative (GRI), the Sustainability Accounting Standards Board (SASB), the UN Global compact (Sustainable Development Goals, or 'SDGs') or the Task Force on Climate-related Financial Disclosures (TCFD).

The Environmental, Social and Governance (ESG) criteria, which generally constitute the three pillars of extra-financial analysis, are taken into

account in socially responsible management. Through ESG criteria, it is possible to assess how companies are exercising their responsibility for the environment and their stakeholders (employees, partners, subcontractors and customers).

— The environmental criterion takes into account in particular the management of waste, the reduction of greenhouse gas emissions and the prevention of environmental risks and includes in particular the Sustainable Development Goals (SDGs) 3, 6, 7, 9, 11, 12, 13, 14 and 15.



— The social criterion takes into account elements such as accident prevention, staff training, respect for employees' rights, the supply chain and social dialogue. It is related to SDGs 1, 2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12 and 16.



— The governance criterion checks the independence of the board of directors, the management structure and the presence of an audit committee as well as their expertise in ESG matters and aspects relating to ethics and anti-corruption. This criterion is related in particular to SDGs 4, 5, 8, 10, 12, 13, 16 and 17.



The proposal for a directive relating to corporate sustainability reporting: expected changes

Currently, only large public interest entities have a legal obligation to report on their non-financial information.

In Belgium, public interest entities are targeted provided they meet the following criteria:

- having an average workforce of 500 workers (annual average in full-time equivalent); and
- having a balance sheet total of more than EUR 17,000,000 or a turnover of more than EUR 34,000,000 (excluding VAT).

In Belgium, the companies which must be considered as public interest entities are:

- companies whose securities are admitted to trading on a regulated market within the European Economic Area;
- credit institutions;
- insurance and reinsurance undertakings;
- securities settlement institutions as well as organisations assimilated to settlement institutions.

Currently, there is no real obligation to audit non-financial information. The statutory auditor is only required to confirm that the entity's non-financial statement contains the required information and that it is consistent with the annual accounts for the same financial year.

It is always possible for any company which wishes to do so, to draw up such a report and to voluntarily request an audit of this non-financial information. A few companies that have understood the importance of this certification to strengthen the credibility of the information

they publish have indeed already followed this example. Nine of the BEL 20 companies have so far voluntarily requested an audit (assurance) of their non-financial information by a registered auditor on the basis of an internationally accepted standard (the ISAE 3000 standard, see below under Regulation).

With the proposal for a directive relating to corporate sustainability reporting adopted by the European Commission in April 2021, an audit of non-financial information (renamed 'sustainability information' by the proposal for a directive) will become mandatory and **the criteria for the companies concerned will be lowered to 250 employees** (as compared to 500 so far). In addition, the company will no longer have to be a public interest entity to be subject to the sustainability reporting requirement.

As regards the type of assurance, the proposal for a directive provides for **the obligation to obtain 'limited assurance' on sustainability information**. It is also foreseen that this assurance is provided by the auditor (registered auditor) or a qualified independent expert, on the basis of national or international standards relating to the assurance of sustainability information as long as such a standard has not been approved at European level. The broad outlines of the sustainability information report's content are reflected in the proposal, but the European Commission is expected to adopt standards by the end of 2022 that will make this content more explicit.

The proposed directive introduced a requirement for companies to report both on how sustainability issues affect their performance, position and development (the 'outside-in' perspective), and on their impact on people and the environment (the 'inside-out' perspective). This is often known as 'double materiality'.

It is expected that this proposal for a directive, once implemented by the Member States, will apply to large companies as from January 2023 and to all SMEs listed on the EU market as from 2026.

Are considered as large companies (and groups), companies which, on their balance sheet dates, exceed at least two of the three following criteria:

- (i) a balance sheet total of 20 million euros,
- (ii) a net turnover of 40 million euros, and
- (iii) no more than 250 employees (annual average in full-time equivalent over the financial year).

The scope would include companies not established in the EU that are listed on EU regulated markets, and the European subsidiaries of non-European companies.

The proposal for a directive does not include listed micro-undertakings which are defined as undertakings which on their balance sheet dates do not exceed the limits of at least two of the three following criteria:

- a) balance sheet total: EUR 350 000;
- b) net turnover: EUR 700 000;
- c) average number of employees during the financial year: 10¹.

Due in particular to the reduction of the minimum employee threshold by half, a significantly higher number of Belgian companies will be required to report sustainability information under the upcoming proposal for a directive.



¹ See art. 3, 1, of Directive 2013/34/EU.

Assurance obligation for sustainability information

An assurance engagement is a professional service within the framework of which an independent and competent practitioner will obtain sufficient appropriate information to express a conclusion, with a reasonable or limited level of assurance, that the certified information is free from material misstatements in relation to the criteria used in the report.

As mentioned above, the proposal for a directive will initially require 'limited assurance' of sustainability information. Such an assurance will therefore not be as extensive as an audit of the annual accounts. Indeed, the nature, timing and

extent of the procedures performed within the framework of a limited assurance engagement are less detailed than within the framework of an audit of the annual accounts, but aim to obtain an assurance level which, according to the registered auditor's professional judgement, makes sense. To make sense, the limited assurance level obtained by the practitioner must make it possible to increase the user's confidence in the subject matter's sustainability information to a level which is not insignificant. This limited assurance level is obtained through an assessment of the sustainability information according to defined criteria used in the report.



How is the limited assurance engagement on sustainability information conducted?

Having satisfied himself that he complies with the ethical and independence requirements, the registered auditor in charge of the engagement shall assign a team that has the necessary competence and capabilities to perform the engagement. Depending on the subject matter information (for example for the review of the CO₂ emissions), further sustainability experts may need to be involved in the assurance team. Generally, for this type of engagements, a multi-disciplinary team is put in place, comprising assurance personnel and subject matter experts.

In the planning phase, the registered auditor will have to carry out investigations in order to understand the sustainability information related to the engagement and determine the materiality² that will need to be considered when performing the engagement and when evaluating whether the information is free from material misstatements.

Based on this, the engagement team shall identify the areas where a material misstatement is likely to occur and design and perform procedures to address the identified areas of attention. The registered auditor will use this concept of materiality to determine the nature, timing and extent of the procedures to be performed in order to obtain 'appropriate evidence'. The type of evidence to be obtained depends on the subject matter information, but mainly consists of investigations and analytical procedures, combined, for example, with inspection, observation or recalculation procedures if deemed necessary by the registered auditor.

The registered auditor is well positioned to address this type of work in relation to sustainability information and inform stakeholders, given that he is used to understanding and reviewing processes (and internal controls) within the framework of preparing financial information and to providing assurance on financial information, by applying his professional judgement, with a guarantee of independence and quality.

² An information is material when it can reasonably be expected that its omission or inaccuracy may influence the decisions users make on the basis of the company's financial statements.

The final result according to the proposal for a directive

Within the framework of the proposal for a directive, when performing a limited assurance engagement on sustainability information, the registered auditor will provide a conclusion on (1) the compliance of the sustainability report with reporting standards (still under development), (2) the process carried out by the undertaking to identify the information that is provided in the sustainability report, (3) the preparation of the sustainability report, and (4) the key performance indicators used in the report (including with regard to the Taxonomy Regulation³).

The registered auditor's conclusion shall be formulated in such a way as to express, based upon the procedures performed and the evidence obtained, that there is no reason to believe that the subject matter's sustainability information contains one or more material misstatements. The registered auditor will formulate a conclusion on the reliability of the information. To this end, he will use negative wording ("We have not noted any facts which suggest that...").

The conclusion aims to increase the level of confidence of the intended users in the subject matter's sustainability information. The proposal for a directive can only reinforce this by creating a harmonised framework for sustainability reporting which will put undertakings on the same level and improve the comparability of sustainability information.

Calling on an independent registered auditor makes it possible to obtain an objective point of view and to give credibility and legitimacy to this information. His assurance report will help to enhance the confidence of stakeholders in the quality of the information reported to them. Internal or external stakeholders will thus be able to assess and to take informed decisions and actions.

The registered auditor has developed expertise in the use of internationally recognised methodologies (in particular in the context of his audit of financial information) to provide limited

³ Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088. This Regulation aims to establish 'the criteria for determining whether an economic activity qualifies as environmentally sustainable for the purposes of establishing the degree to which an investment is environmentally sustainable'.

assurance which enhances the quality of the information, for the benefit of an organisation or undertaking. He is also subject to strict ethical rules requiring in particular his independence and to an external control of the profession (public oversight) which ensures compliance with methodologies at national level (standards) by practitioners. This constitutes a guarantee of quality as to the work accomplished and allows users of the information to understand in a transparent way the work carried out and the assurance provided, across borders. The registered auditor's report thus contributes to improving the business value and its attractiveness. The registered auditor's knowledge of the organisation and his expert role add value to the process of reporting on financial or non-financial (or sustainability) information.

Reliability enhanced by the registered auditor's high-quality opinion on the level of assurance

The reliability or credibility of financial and non-financial information can only be enhanced if the conclusion is based on a qualitative standard and has been formulated by an independent and recognised assurance practitioner, such as a registered auditor.



How to prepare for the introduction of the legal obligation to provide limited assurance of sustainability information

Companies that have not yet started preparing a sustainability information report need to address the following elements:

- Define the ESG strategy, the reporting framework that the company wishes to use to prepare its report (for example, the one developed by the Global Reporting Initiative⁴);
- Organise a dialogue with the stakeholders in order to obtain a better idea of their expectations and the topics relevant to them, which, in conjunction with the information relevant to the company, will make it possible to define a materiality matrix from which the content of the report will be derived;
- Define the internal team which will be responsible for organising this reporting and the integration of ESG issues into the governance structure (responsibilities, monitoring, etc.);
- Define the sustainability information relevant to the company according to its environment, its activities and the sustainable development goals with regard to which it wishes to take action;
- Define the relevant key performance indicators (KPIs) to be included in the sustainability information report and set short- or medium-term goals for these KPIs;

- Organise the collection of useful information (system, tools, processes, internal control circuits) to ensure that the company is able to collect the relevant information (preferably over several years to allow comparisons) and that it is able to ensure its quality and punctuality;

- Write the report and define the distribution format;

- Start preparing now, for example, by already planning to hire a registered auditor to check the sustainability information in 2022. This will test whether the company is ready.

The time required to set up high-quality sustainability reporting should not be underestimated.

As regards the preparation for obtaining limited assurance, it will be necessary to be able to explain to the independent auditor, the registered auditor, how the information has been compiled, verified and organised through the processes put in place internally. If the information is compiled using a monitoring tool, the registered auditor will be able to analyse the reliability of this tool. It is also useful to compile the sources of the different information to facilitate the registered auditor's understanding. Finally, key people will need to make themselves available to answer to the registered auditor's questions.

⁴ The global standards for sustainability reporting, <https://www.globalreporting.org/standards/>.

Regulation in the future

In order to perform a limited assurance engagement on sustainability information, the registered auditor will measure or assess this information according to predefined criteria. The criteria are reference elements, namely a normative control framework, a law or regulation. For the moment, the only existing standards in this area for carrying out this assessment are international standards, more specifically the International Standards on Assurance Engagements, and in particular ISAE 3000 on assurance engagements other than audits or reviews of historical financial information. To date, there is no other standard, either at national or European level.

However, a standard is being developed at European level. It is therefore difficult to comment on the future requirements of this standard and on the actual content of the sustainability report. The objective here was to draw up a current state of play, taking into account the available information. This document will be updated as information becomes available and as standards and legislation evolve.

Until then, large companies are strongly advised to prepare themselves now to be ready for 2023, by already providing in 2022 for an analysis, by a registered auditor, of reported sustainability information. Remember to contact a registered auditor now to guide you through this .





Questions?

Please consult the IBR website (www.ibr-ire.be)

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