

Reporting ready: preparing for assurance of climate-related disclosures

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Australian companies are approaching the era of mandatory reporting and assurance over climate-related financial information. Achieving limited and/or reasonable assurance will require additional effort. Readiness is crucial.

The introduction of a mandatory climate-related financial disclosure regime in Australia (for financial years starting on or after 1 January 2025) requires companies to have their climate-related information assured, perhaps for the first time.

This paper explores:

- ▶ How companies can prepare for assurance
- ▶ The expectations for limited and reasonable assurance
- ▶ The role of the chief financial officer (CFO) and the board in preparing for assurance

For many organisations, the transition represents a significant uplift in the amount of time and effort it will take to prepare systems, processes and disclosures for regulatory assurance. Preparing early for assurance is important given the climate disclosures to be reported will:

- ▶ Form part of the annual report with a strong connection to audited financial statements.
- ▶ Be the first time for most companies that auditors will opine on the disclosures outlining the processes, systems, governance and risk management frameworks put in place to respond to material climate risks and opportunities.
- ▶ Be publicly available and receive significant scrutiny from a range of stakeholders.
- ▶ Will form a significant data point of consistent information between competitors in the market.
- ▶ Be certified by directors and form part of the annual general meetings (AGM) agenda for public companies.

The assurance journey is depicted below.

Journey towards reasonable assurance



New systems and processes will need to be established and fine-tuned now so companies are 'assurance ready'.

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Preparing for assurance requirements

What do we know about the assurance requirements?

The amendments to the *Corporations Act 2001* require entities to obtain independent assurance of their climate-related financial disclosures from the firm that is their financial statement auditor. Sustainability reports will be subject to audit (i.e., reasonable assurance) for financial years commencing on or after 1 July 2030. Until that time, the extent to which a sustainability report is subject to audit or review (i.e., limited assurance) will be determined by the AUASB, which has proposed an 'assurance pathway' in Exposure Draft 02/24 *Proposed Australian Standard on Sustainability Assurance ASSA 5010 Timeline for Audits and Reviews of Information in Sustainability Reports under the Corporations Act 2001*. The Exposure Draft is open for public comments until 16 November 2024. The final Standard is planned to be approved in December 2024.

The AUASB is proposing that assurance will be required from the first year in which an entity is required to prepare a sustainability report and will begin with limited assurance of Governance, Strategy – Risk and Opportunities, and Scope 1 and Scope 2 greenhouse gas emissions. The proposed assurance phasing is as follows:

	Year 1	Year 2	Year 3	Year 4
Scope 1 & 2	Limited	Reasonable	Reasonable	Reasonable
Governance		Limited	Limited	
Strategy – risks and opportunities**				
Climate resilience assessments/scenario analysis				
Transition plans				
Risk management				
Climate-related metrics and targets				
Scope 3 emissions	N/A			

*The same assurance pathway applies to Groups 1, 2 and 3. Year 1 for a Group 1 entity refers to financial years commencing on or after 1 January 2025. Year 1 for a Group 2 entity refers to financial years commencing on or after 1 July 2026. Year 1 for a Group 3 entity refers to financial years commencing on or after 1 July 2027.

**The phasing for assurance on Statements where there are no material climate-related financial risks and opportunities is the same as for 'Strategy – Risks and Opportunities'.

While the phasing model is proposed by the AUASB, we anticipate many entities will obtain assurance beyond what is currently proposed in the legislation to:

- ▶ Safeguard the integrity of published information
- ▶ Meet expectations of capital providers



Preparing for assurance requirements (continued)

Companies that already undertake some form of sustainability reporting and may also be subject to some form of assurance for select metrics and criteria in the report have a strong starting point. However, the new requirements are very likely to increase the compliance and governance responsibilities for teams responsible for reporting, including management and the board. This relates to the nature and form of sustainability information reported, which will have less optionality.

Each company's climate-related financial disclosures will no doubt receive an increased level of scrutiny from stakeholders, in particular investors. That scrutiny will include a focus on some of the more complex reporting requirements such as the consistency of scenarios, resilience assessment, and key judgements and assumptions made. This scrutiny also highlights the importance of connectivity and consistency between climate and financial reporting, sustainability reporting and public statements in the market.

Accordingly, the shift to mandatory climate-related financial disclosures and assurance necessitates the need for the creation or refinement of systems, processes and internal controls to manage disclosure risk and drive connectivity with financial reporting.

This step change in sustainability disclosure-related processes and systems will need to be commenced immediately with the anticipated level of effort to be higher in the establishment phase. Once set up, these systems and processes can then be improved over time to meet increasing assurance requirements and internal governance expectations.

We observe that many organisations still rely heavily on manual processes to support existing climate reporting, with limited consideration of robust governance and controls over that reporting. While there may be organisational maturity in some areas, the depth and breadth of disclosure requirements under the Australian Sustainability Reporting Standards (ASRS) and an assurance mandate will necessitate a fundamental step change going forward to how a company approaches internal controls associated with climate reporting.

Accordingly, there are a range of actions that organisations should undertake in the short-term establishment phase before preparing for the journey towards reasonable assurance. These will:

- a. Ensure appropriate procedures are in place to determine the accuracy of the climate-related disclosures.
- b. Reduce the compliance cost as they move to reasonable assurance.
- c. Help address the disclosure requirements of the standard, i.e., governance over climate-related risks and opportunities (CRROs).

Detailed on the following pages are some of the common areas that companies should consider as part of their preparation activities.



In a way not previously obligated on auditors, the scrutiny and consistency of information disclosed between the financial and sustainability reports will be paramount. This will require integration of assurance activities across these reports.

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Preparing for assurance requirements (continued)

Shift to controls audit approach

- ▶ Historically, assurance engagements on climate and sustainability reporting have involved substantive audit procedures. Whilst these are typically more time consuming and undertaken subsequent to year end, they don't seek to rely on the internal controls of an organisation.
- ▶ As audit requirements shift from limited to reasonable assurance, a controls approach will typically be the most efficient and cost effective audit,
- ▶ This approach is also critical to reducing the extent of testing that is occurring at year end, given financial reporting is also occurring in parallel.
- ▶ A controls approach is built on the foundation of an effective control environment. Whilst many organisations are of the view that their control environment is effective, experience tells us that there are controls, and then there are '*auditable controls*'. That is, controls supported by appropriate evidence in relation to design and operation.
- ▶ Accordingly, companies should consider:
 - ▶ The extent to which controls have been captured in existing risk management processes
 - ▶ Whether these controls have been subject to an appropriate form of assessment
 - ▶ What gaps exist in the control environment, and the remediation plans

Process documentation

- ▶ A significant component of the disclosure requirements within the ASRS involve process based subjective matter, i.e., identification of CRROs, materiality considerations and scenario analysis.
- ▶ The ability for these processes to be subject to an assurance process will be a factor of:
 - ▶ Adequacy of documentation maintained by the company relating to this subjective matter
 - ▶ Extent of governance processes, i.e., oversight and challenge, that support the subjective matter
- ▶ Accordingly, it is important that management maintain appropriate documentation of these activities.

Estimates

- ▶ The audit of estimates as part of a reasonable assurance engagement typically goes down one of two paths, either:
 - ▶ The auditor develops their own point estimate; or
 - ▶ The auditor tests the model, methodology and assumptions used by the company to determine their estimate
- ▶ With climate-related estimates being highly subjective, i.e., Scope 3 and financed emissions, anticipated CRRO finance impacts, it is unlikely that the auditor will be able to develop their own point estimate across all key estimates.
- ▶ Accordingly, companies will need to evaluate whether they have sufficient process and documentation associated with their estimation processes.
- ▶ Such processes can include:
 - ▶ Whether documentation is maintained that supports the methodology and assumptions used in the estimate
 - ▶ Whether the estimate/model has undergone any external or internal validation
 - ▶ Whether the company is utilising third party models/software, that restricts the ability for the auditor to evaluate the preparation of the model.

Entity level controls

These set the tone, establish the culture, and provide a foundation for an effective internal control environment.

- ▶ Entity level controls include:
 - ▶ Policy framework
 - ▶ Oversight processes
 - ▶ Education and training
 - ▶ Internal audit function and scope
- ▶ Organisation should consider whether processes relating to climate reporting are appropriately captured in entity level controls.



Preparing for assurance requirements (continued)

The role of third parties

- ▶ Often third parties play critical roles in financial and sustainability reporting activities. This can be in relation to the systems and tools utilised, the provision of data (such as the greenhouse gas inventory) and broader outsourced arrangements.
- ▶ Under a reasonable assurance engagement there are a range of considerations that are necessary to be applied when dealing with third parties, corresponding to the role they play in the reporting process. Such considerations include:
 - ▶ The extent to which the organisation and their auditor satisfy themselves around the effectiveness of controls at the third party, i.e., is there any reporting in relation to the adequacy of the third party's control environment (e.g. ASAE 3402 / GS007).
 - ▶ Accuracy of data - is the information subject to assurance by the third party's auditor, and if so, how does the company's auditor meet its responsibilities to ensure they are comfortable with the third party's audit processes, given the intended use of the data.

IT systems

- ▶ Generally, a limited assurance engagement would not seek to test application and IT general controls supporting reporting processes.
- ▶ However, under a reasonable assurance engagement, reliance on such systems would be important.
- ▶ Accordingly, companies should consider the extent to which:
 - ▶ All critical IT systems have been identified.
 - ▶ The extent to which general controls, such as user access and change management, are aligned with broader organisation control requirements, and whether these have been tested.
 - ▶ The extent to which controls supporting data linkage, i.e., input, processing, storage, transformation and reporting, have been identified and form part of any pre-assessment activities prior to a reasonable assurance engagement.

Assurance over uncertain, forward-looking, long-term disclosures

Many of the climate-related financial disclosures required by ASRS will include information that is subjective, estimates and assumptions that are uncertain (and may remain uncertain into the long-term future) and disclosures that are forward-looking. Although companies may be reluctant to disclose information with these attributes, they are required disclosures. To assist readers to understand this information, ASRS requires companies to disclose the judgements made that significantly affect the information reported and to identify those amounts that are subject to high levels of measurement uncertainty and to disclose the assumptions, approximations and judgements made in those measurements. Given the nature of this type of information, companies will also need to have processes to address changes in estimates and to identify and disclose the corrections of any errors.

Companies need to determine how to most appropriately disclose forward-looking information by getting the balance right in disclosing key assumptions and acknowledging the uncertainties. Disclosures need to be directly linked to CRROs and not just a full forecast for the business.

Disclosures need to be directly linked to CRROs and not just a full forecast for the business. Assurance providers will need to have a better understanding of the business as a whole and its material risks and opportunities than ever before.



What are the expectations of limited and reasonable assurance?

In preparing for assurance requirements, companies should understand the distinction between limited and reasonable assurance.

What is the difference between limited and reasonable assurance?

In a reasonable assurance engagement, auditors provide an opinion on whether the subject matter is free from material misstatements. This type of engagement signifies a higher level of confidence. Reasonable assurance includes extensive testing of controls, data verification, and evaluation of underlying assumptions and methods, and site visits to test data management processes.

In contrast, limited assurance is not as comprehensive and involves auditors performing fewer procedures e.g., fewer testing of controls and testing procedures more limited in scope (e.g., focussed on analytics).

As this will be the first time that assurance is provided over some types of information, it can be expected that assurance providers will have findings that result in a qualified conclusion or modified opinion, particularly given that information is being audited for the first time.

This will be the case when key data is missing (perhaps because the company does not yet have the systems or information flow to report it) or when it has not been possible to test it (perhaps because it is not of sufficient quality or granularity).

Companies should plan for baseline assurance (prior to limited assurance) to resolve any findings and recommendations that an assurance engagement might otherwise identify, which could result in either:

- ▶ A qualified / modified opinion; or
- ▶ Delays to the audit of the climate report, and consequently, impact the release of the financial statements.

Often referred to as “assurance readiness”, the procedures reflect a dry run for assurance and a ‘baseline’ for future reporting under an assurance environment. Procedures include a detailed review of data collation and reporting with findings and recommendations summarised in a report with no requirement for public release (no assurance statement issued to the public).

Limited assurance	Reasonable assurance
<ul style="list-style-type: none">▶ Limited review.▶ Focus is on inquiries and analytical procedures.▶ Understanding of the processes and systems that support the disclosures is required, unlikely to be tested▶ "Negative" form of assurance, where nothing significant has come to the auditor's attention indicating misstatements.▶ Less detailed, smaller scope and generally quicker.	<ul style="list-style-type: none">▶ Deeper examination for users requiring high confidence in the accuracy of information.▶ Detailed documentation of processes and systems and testing of controls, full validation processes and tests of details.▶ "Positive" form of assurance, suggesting that the information is free of material misstatement.▶ More detailed, broader in scope and requiring more time.
<ul style="list-style-type: none">▶ Management has the opportunity to correct errors throughout the reporting process.▶ If material errors are not corrected, a qualified assurance statement is provided.	

The impact of ISSA 5000 on assurance

The International Auditing and Assurance Standards Board has now approved an enhanced assurance standard for sustainability assurance engagements: *International Standard on Sustainability Assurance (ISSA) 5000 General Requirements for Sustainability Assurance Engagements*. ISSA 5000 provides a comprehensive, stand-alone standard suitable for limited and reasonable sustainability assurance engagements. The AUASB will consider the suitability of ISSA 5000 for adoption of an Australian equivalent at a future meeting.



The increasing role of the CFO and the board

Reporting in accordance with ASRS requires connectivity between non-financial and financial disclosures and consequently the associated reporting and assurance processes must be closely linked. The CFO and board have an increasingly critical role to play to facilitate this connectivity and to leverage the depth of understanding in maturity reporting and assurance processes within an organisation. Considerations include:

Structure and responsibilities

Companies will need to decide who will ultimately sign-off on disclosures and manage the assurance, particularly given sustainability and audit and risk committees may have different executives who are accountable for board reporting.

Audit planning

CFOs and boards need to be planning for what this means for their companies existing audit program now, including:

- ▶ Updating audit plans to include an assurance journey as outlined on page 1, including the consideration of baseline assurance.
- ▶ Creating or refining systems processes and internal controls to manage disclosure risk and drive connectivity with financial reporting.

Skills and competencies

[*'The two sides of governance in climate-related reporting'*](#), explains how board members need to have sufficient knowledge to ask the right questions of management (including the CFO) to support reporting and assurance quality, even if they are not subject matter experts themselves.

Key takeaways

The introduction of mandatory assurance necessitates significantly stronger systems, processes and internal controls, improved connectivity with financial reporting and the streamlining of a company's data collection systems and processes.

Assurance requires a step change in effort, particularly in the readiness phase.

It is therefore crucial that:

- ▶ If companies have not already, they take the opportunity to work through their gap assessments and test their systems and processes.
- ▶ Companies undertake baseline assurance to save time and effort later.
- ▶ Sustainability and finance teams will need to work together to develop and integrate their reporting systems, processes and timelines with the support and leadership of the CFO and board.

Sustainability Disclosure Hub



The EY Sustainability Disclosure Hub offers practical guidance to assist companies across the region prepare for mandatory reporting of climate and sustainability-related reporting.

Headed by Oceania market-leading financial and non-financial reporting professionals, the Sustainability Disclosure Hub brings together EY capability locally and across the globe – coupling financial and non-financial reporting strategy, readiness and assurance capabilities that have an intimate knowledge of the work of the [International Sustainability Standards Board](#) (ISSB) and local market insights, including the development of the climate-related disclosure requirements by the [Australian Accounting Standards Board](#) (AASB) and New Zealand's [External Reporting Board](#) (XRB).

The Sustainability Disclosure Hub collaborates closely with the EY Net Zero Centre, which helps EY clients to make the right decisions at the right times and set themselves on a pathway for success in a net zero economy.

Please reach out to the EY Sustainability Disclosure Hub team to discuss what the requirements mean to you.

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