PROPOSED AMENDMENTS TO ASIC ACT – WHOLE-OF-SYSTEM CONTEXT

The proposed changes to the ASIC Act are an important step in the evolution of the Australian corporate reporting system and of corporate reporting in Australia.

However, it is critically important that the changes are set in a broader context. That context is of the global corporate reporting system and Australia's position within it, both now and in the future, and recognising the fundamentally important role of integrated reporting and integrated reporting assurance.

That importance has been elevated now that the IFRS Foundation has taken ownership of the Integrated Reporting Framework and Integrated Thinking Principles and the IAASB has embarked on a project to develop an overarching sustainability assurance standard which embraces integrated reporting assurance.

This is a journey that many Australian companies are already on, because voluntarily, they see the benefit of an integrated report. For example, there is already expanded disclosure on climate matters in annual reports. A number of audit committee chairs have recently attested to integrated reporting being an appropriate part of their journeys, without legislation – because it is the right thing to do.

This paper makes five recommendations to Treasury on how it can properly position its proposed legislative changes in the broader context. The following table links the covering e-mail to the analysis behind these five recommendations:

Reco	Issue Being Addressed	Solution Being Proposed	Pages
1	OFR / RG 247 is not a reporting framework, and reporting against them would not achieve all of the aims of Treasury - is not /does not: • required by legislation • based on a conceptual framework • comprehensive - its most important exclusion is *governance* – a core component of value creation and the board's governance responsibility • produce internationally consistent and comparable reports • require an insightful Basis of Preparation and Presentation • based on enhancing and revealing thinking underlying the report (integrated thinking)	Integrated Reporting Framework is an appropriate reporting framework to achieve aims of Treasury - is/ has: • an embedded conceptual framework - integrated thinking foundation and three fundamental concepts • results in an identifiable and designated, connected, concise yet insightful and comprehensive, **integrated report** • emphasises governance as a fundamental component of value creation and the board's governance responsibility for the integrity of the integrated report • is an internationally accepted framework, enhancing consistency and comparability • requires an insightful Basis of Preparation and Presentation • reveals thinking underlying reporting (integrated thinking)	1-8
2	OFR is not part of a holistic corporate reporting system – FRC and ASIC not formally linked with the ASX Corporate Governance Council	Enables a 'whole-of-system' approach - FRC and ASX corporate Governance Council working more collaboratively	8
3	Related assurance approaches: a) RG 247 / OFR not suitable criteria for assurance b) ASX CG Reco 4.3 notes Integrated Reporting Framework can be used in preparing OFRs	Related assurance approaches: a) Integrated report under Integrated Reporting Framework provides suitable criteria for assurance b) Can replace OFRs with integrated reports or use Integrated Reporting Framework to prepare OFR which would provide suitable criteria for assurance	 8-9 9-10
4	Strained financial reporting and auditing system capacity	Further benefits of recommended approach - Integrated reporting and integrated reporting assurance capacity requirement can largely be provided by existing financial report preparers / auditors and sustainability SMEs, added benefit of helping assess 'brain drain' from FS audit	10-11
5	Additional actions to facilitate effective implementation: Little integrated reporting expertise in FRC	 Consider appointing Michael Bray to FRC	11-13
No change required to legislation or new government institutions – only using IRF anchor point under 225, making appointments, getting FRC and ASX CGC closer and making public communications of context for proposed amendments to ASIC Act			

The IFRS Foundation is the world's peak corporate reporting body. Accordingly, it is natural to begin a discussion of the global corporate reporting system to provide the international context for a discussion of the Australian corporate reporting system.

Having discussed the global corporate reporting system and the role of the IFRS Foundation within it, the implications of that global system for the Australian corporate reporting system given Australia's natural desire to be globally aligned are discussed.

I start by answering the question, 'what should be the flagship corporate report for investors?'. I then move onto Australian equivalents to ISSB standards; the momentum towards integrated reporting assurance; and the system capacity / educational implications of the unprecedented changes which have taken place within the corporate reporting system within the last two years.

Finally, my recommendations require **no legislative change or new government institutions**.

<u>The International Context - Global Corporate Reporting System</u>

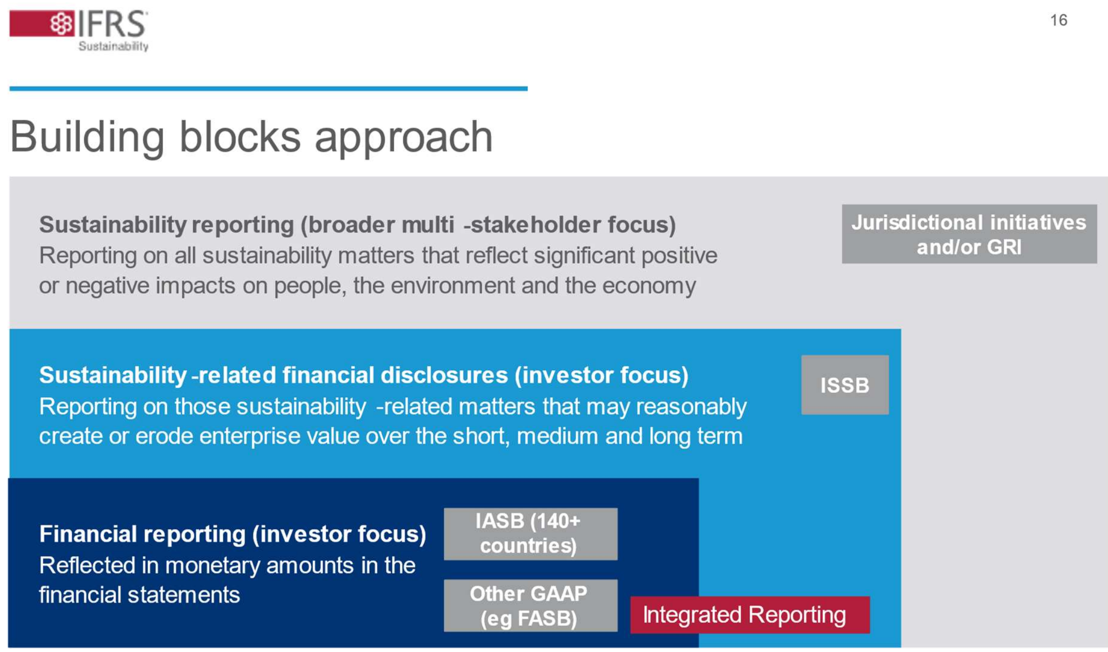
Set out below is a diagrammatic representation – the Dynamic Materiality Diagram - of the boundaries of corporate reporting for the IFRS Foundation.

The boundaries of corporate reporting for the IFRS Foundation

While the boundaries of corporate reporting under the IFRS Foundation were traditionally focussed on financial reporting, the situation is changing rapidly with the boundaries expanding to include sustainability reporting under the ISSB standards. The boundaries of corporate reporting for the IFRS Foundation are now defined by its focus on 'enterprise value'; in other words for corporate reports, the estimated discounted value of an organisation's future cash flows. Financial reporting under IASB / AASB standards reports on some but not all or of an organisation's enterprise value. This is an important first step to more informative reporting on enterprise value. Sustainability reporting under the ISSB standards / Australian equivalents to them will report on some but not all of an organisation's enterprise value, and together with IASB / ISSB reporting will not account for all of an enterprise value.

Entities may *choose* to make sustainability disclosures which go beyond enterprise value to matters which are relevant to an organisation's broader societal value and stakeholders beyond investors, matters that are not currently material to enterprise value. Accordingly, sustainability disclosures can be divided into sustainability-related financial disclosures and sustainability-related disclosures which are not currently material to enterprise value. Integrated reports are the 'connector', the glue which connects the description of an organisation's business to the metrics and other disclosures chosen to measure its prospects and future creation of enterprise value.

This relationship is well illustrated by the IFRS Foundation's 'dynamic materiality diagram' (refer below), with sustainability-related financial disclosures being in the middle box and other non-financially material sustainability disclosures being in the outer box. Sustainability matters may cross the boundary between the middle and outer boxes (either way) as circumstances change. For instance, pandemics would likely have been in the outer box, moving inside the middle box almost instantaneously when the covid crisis occurred:



The diagram shows that IFRS accounting standards and other 'GAAPs' are in the inner box (investor focus); ISSB-disclosures are in the middle box (also investor focus); and GRI disclosures are in the outer box. Importantly, **integrated reporting** is shown to bridge the inner and middle boxes.

The **Integrated Reporting Framework** defines, sets standards for and guides integrated reporting, a process a founded on integrated thinking (***better business practice***) that results in a periodic **integrated report**, a designated and identifiable, concise and comprehensive, communication about how an organisation's strategy, governance, performance and prospects, in the context of its external environment, lead to the creation, preservation or erosion of value, including enterprise value in the short, medium and long term (***better business reporting***).

We believe that the material outcomes of applying GRI standards fit as naturally in an integrated report in accordance with the Integrated Reporting Framework as do the outcomes from applying both IFRS accounting and sustainability disclosure standards, and as do self-determined metrics for matters not currently required by IFRS accounting and sustainability, and GRI, standards.

Integrated Reporting and Integrated Thinking in the IFRS Foundation – the world's peak body for corporate reporting

International consistency in descriptions of businesses in integrated reports is expected to be enhanced in 2023 and beyond with the IFRS Foundation acquiring the Integrated Reporting Framework through the consolidation of the Value Reporting Foundation into the IFRS Foundation on 1 August 2022; and also by more and more entities applying the IFRS Foundation's Integrated Thinking Principles, also acquired in the Value Reporting Foundation consolidation.

On 25 May 2022 the announcement by IASB and ISSB Chairs made integrated reporting central to the future of corporate reporting:

> *"We are convinced that the Integrated Reporting Framework drives high-quality corporate reporting and connectivity between financial statements and sustainability-related financial disclosures which improves the quality of information provided to investors. Therefore,* ***we strongly encourage continued use of the Integrated Reporting Framework and the Integrated Thinking Principles underpinning it****".* [My emphasis]

With that anchor point, I explain what is possible now for companies on a voluntary basis, starting with the foundational description of *The Business* which is required by the Integrated Reporting Framework to claim that an integrated report is in accordance with the Integrated Reporting Framework.

As to the description of *The Business* in an integrated report, the Integrated Reporting Framework's three fundamental concepts (Value Creation, The Capitals and the Value Creation Process) enable an organisation to describe its business – that is, its purpose, strategy, resources and relationships, governance, business model and risk management, and in that context select and disclose the metrics appropriate to communicating the organisation's strategy, governance, performance and prospects to investors and other stakeholders in a concise, comprehensive and compelling way.

Integrated reports in accordance with the Integrated Reporting Framework are also required to have an insightful Basis of Presentation and Presentation describing the frameworks (including the Integrated Reporting Framework) and standards used (including the ISSB, and if appropriate GRI, standards).

Accordingly, an integrated report tells the story of the organisation's use of its resources and relationships (*its with*) in its boardroom and business model (its *how*) to implement its strategy and realise its purpose (its *what*). It provides a window into the quality of the organisation's integrated thinking – in other words, its investment proposition for investors and other stakeholders –its *why*.

Successful implementation of the IFRS Foundation's Integrated Thinking Principles drives better business practice. This has been evidenced in practice by attestations from the many organisations who have had successful implementation experiences; and through a body of empirical academic research[1], which has found that integrated reporting quality is positively associated with both firm value and stock liquidity, and that the association is most likely to attributable to the integrated thinking effect of integrated reporting (a real effect) than the integrated report alone (a capital markets effect).

That is, the integrated thinking journey drives better business practice, which is communicated to investors in the integrated report, as well as the report driving better investor understanding of The Business as it is. Integrated thinking practice is supported by the IFRS Foundation's integrated thinking resources - at Integrated thinking | Integrated Reporting: Transition to Integrated Thinking A Guide to Getting Started; Integrated Thinking Case Studies; and a report by the IFRS Foundation's Integrated Thinking and Strategy Group, 'Integrated Thinking: A Virtuous Loop'. In addition, automation to support implementation of the principles, including reporting to the board of directors and investors, is under consideration.

International integrated reporting adoption has grown significantly in the last five years and is expected to grow with even more momentum under the IFRS Foundation's stewardship. Most businesses are expanding the scope of their reporting about their strategy and drivers of prosperity (refer KPMG report, 'Corporate Reporting Trends 2022 – Integration of ESG, critical to enterprise value reporting – A review of ASX 200 corporate reporting trends in the year to 30 June 2022') and an increasing number are adopting the IR framework to help structure their reporting. Through integrated reporting, investors worldwide know far more about the businesses in which they invest than ever before.

I can think of no better foundation for Australian corporate reporting in 2023 and beyond than the Integrated Reporting Framework, and no better communication vehicle on value and value creation than an integrated report in accordance with the Integrated Reporting Framework.

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1 For example, Barth, M. E., Cahan, S. F., Chen, L., & Venter, E. R. (2017). The economic consequences associated with integrated report quality: Early evidence from a mandatory setting. Accounting, Organisations And Society, 62:43-64; Zhou, S., Simnett, R., & Green, W. (2017). Does Integrated Reporting Matter to the Capital Market? Abacus, 53(1), 94-132.

The above analysis provides for the basis of our comments and recommendations for The Treasury to consider for 2023 in conjunction with the proposed amendments to the ASIC Act going through the Parliamentary process.

<u>The Australian Corporate Reporting System</u>

I now turn to five key issues for Australia:

- which report should be the flagship corporate report for investors?
- Australian equivalents to ISSB Standards
- Moving towards Integrated Reporting Assurance
- Implications for integrated reporting education to create capacity
- Government institutions in the Australian Corporate Reporting System

1. Reporting Framework to Best Achieve Treasury Aims

Producing Australian equivalents to ISSB standards will define certain sustainability-related financial disclosures but will not resolve the question of which report(s) the outcomes from applying the standards should be reported in.

I believe that there is a natural answer to this question which is providing a flagship corporate report for investors which is more concise, coherent, comprehensive and otherwise responsive to investor needs, and internationally consistent, than OFRs under ASIC's RG 247 – the natural answer is in integrated reports prepared in accordance with the Integrated Reporting Framework[2] because:

- ***'One stop shop' – the integrated report*** is a 'one stop shop', where investors can get a concise and comprehensive picture of an entity's business, performance and prospects, a report which achieves compliance with all frameworks and standards adopted (including the standards which produce <u>material</u> IASB, ISSB and GRI metrics and associated disclosures, and material licence to operate-based information in reports required by industry regulators such as the Australian Energy Regulator), and a statement of the board's accountability in this one report.

  Investors do not need to go to other statutory or voluntary corporate reports for various pieces of information and need to piece them together in a coherent way – for example, corporate governance statements, ASX Corporate Governance Principles and Recommendations disclosures, sustainability reports containing ISSB and GRI metrics including on climate matters, remuneration reports and voluminous information in reports required by industry regulators, *as well as* OFRs. They get all material information on these matters in one report.

  OFRs under RG 247 are not comprehensive nor necessarily concise, coherent or consistent, and are not connected with other separate reports that have material information for investors which would be better provided in one corporate report.

  The 'one stop shop' of integrated reports should assist in enhancing investor confidence in Australian capital markets.

- '***One stop shop' – the Integrated Reporting Framework*** has an embedded conceptual framework comprised of:

[2] Alternatively, the name 'OFR' could be retained but the Integrated Reporting Framework could be the main framework used in its compilation, with this set out in the Basis of Preparation in accordance with paragraph 4.41 of the Integrated Reporting Framework.

- an integrated thinking foundation and three fundamental concepts (summarised above in relation to the description of The Business);
- bold black letter paragraphs stating requirements in relation to describing The Business and connecting it to disclosures in relation to metrics from applying standards selected to measure the performance and prospects of The Business;
- guidance to support the bold letter requirements; and
- other bold letter requirements including that the integrated report be designated and identifiable and concise, contain an insightful Basis of Preparation and Presentation, and a statement of belief and accountability by the board of directors as the responsible body for the governance of The Business.

The frameworks and standards used must be disclosed under the bolded paragraph 4.41, "An integrated report should answer the question: How does the organisation determine what matters to include in the integrated report and how are such matters quantified or evaluated?" The bold letter paragraphs are in substance standards which must be adhered to in order to support a claim that the integrated report is in accordance with the Integrated Reporting Framework.

The Framework is backed by 'detailed how to' guidance in the non-bolded paragraphs of the Framework and in IFRS Foundation integrated reporting resources supporting integrated reporting implementation – for example, the IFRS Foundation's:

- Transition to integrated reporting: A guide to getting started | Integrated Reporting, Integrated Reporting Examples Database | Integrated Reporting;
- the various regional integrated reporting communities around the world (for instance, the Integrated Reporting Committee of South Africa Integrated Reporting SA | The Home of Integrated Reporting and the Australian Business Reporting Leaders Forum BRLF – Business Reporting Leaders Forum;
- the publications issued by these bodies; and
- the reports published by integrated reporters around the world.

RG 247 is Australian specific and does not have the depth of support resources that the Integrated Reporting Framework does. In addition, Australian reporters under it have no basis to use international comparators to support their OFRs.

The 'one stop shop' of the Integrated Reporting Framework should enhance investor confidence in Australian business and assist Australian companies to compete more effectively overseas.

- ***Governance – governance through the Board of Directors is a critical component of the whole business***, its value creation and resilience. Reporting on governance as a component of the value creation process, not an 'add on'. Reporting on governance in a connected way (how the board as a board adds value to the contribution of management and the rest of the organisation) is critical information for investors. The board must declare its responsibility for the integrated report as a bold letter requirement of the Framework.

  Governance is handled in separate reports urger than in OFRs. Governance is mentioned peripherally in RG 247.OFRs are not as comprehensive as integrated reports, and do not have their integration and connectivity. OFRs do not require a statement of accountability from the Board of Directors. Investors are lacking critical information as to the organisation's value creation and investment proposition.

  On the other hand, the integrated and connected treatment of governance in an integrated report should be of assistance to investors having confidence in the companies in which they invest, and so the collective confidence of the Australian capital market.

- ***Integrated reports*** in accordance with the Integrated Reporting Framework have proven on many occasions to be ***suitable criteria for assurance*** under International Statement of Assurance Standard ISAE 3000, 'Assurance Engagements Other Than Audits or Reviews of Historical Financial Information'.

  I am aware of no instances of OFRs being independently assured under ISAE 3000, and doubt that OFRs under the existing RG 247 could be suitable criteria for assurance under ISAE 3000 and so enhance investor confidence in the integrity of OFRs.

  On the other hand, assurance of integrated reports is of importance to investor confidence in Australian capital markets and international competitiveness, and the 'right sizing' of the cost of capital[3].

- ***Integrated Thinking (better business practice) foundation of integrated reporting***. Successful integrated reporting adopters have almost invariably said that the integrated reporting journey has allowed them to improve their businesses and report that improved business and performance to investors in the integrated reports. This is the 'Barth Effect' explained above.

  OFRs under RG 247 have no features to drive business improvement.

  Conversely, integrated reporting with its integrated thinking foundation can be a driver of improved productivity within Australian business and the Australian economy. It can enhance Australia's capital markets, international competitiveness and cost of capital[4].

There is no legal impediment to listed entities either replacing their OFRs with integrated reports in accordance with the Integrated Reporting Framework as described above, or re-badging their OFRs being based on the Integrated Reporting Framework, in both cases supplemented as need be by concise additional disclosures from applying ASIC's guidance in RG 247 – so obtaining the benefits of integrated reporting and integrated thinking described above.

Either approach will not add any additional reports or reporting and will offer opportunities to reduce the number of reports and volume of reporting if approached strategically.

An integrated report provides the business context for all disclosures, including on climate risks and opportunities, and connectivity to metrics and other disclosures, including on climate matters. Accordingly, adopting an *integrated reporting-based reporting strategy* will offer organisations the opportunity to report in one place all aspects of their business and its performance and prospects, including on governance and remuneration matters, improving clarity and ease of access to the information that investors and other stakeholders need to have confidence in the businesses in which they invest.

Powers of The Treasury and FRC under section 225 of the ASIC Act

Section 225 of the ASIC Act was referred to above, Section 225(1) of the ASIC Act states:

> "The FRC functions are: … (g) to promote and advance the main objects of this Part; and (h) any other functions that the Minister may confer on the FRC by written notice to the FRC Chair."

Included in the main objects of Part 12 of Division 1 (the financial reporting system) of the ASIC Act under section 224 are:

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[3] Section 225 of the ASIC Act refers to 'reducing the cost of capital' – refer below. It cannot be promised that integrated reports alone will <u>reduce</u> the cost of capital, but they will assist in 'right sizing' the cost of capital. Capital can be priced at the <u>right</u> level for The Business as it is, and its performance and prospects. The proposition that integrated reporting will <u>reduce</u> the cost of capital comes through application of the Integrated Thinking Principles when effectively communicated in an integrated report with independent assurance (refer below). This is the 'Barth Effect' explained above.

[4] For your information, I am aware of two PhDs being completed on integrated thinking by people associated with Deakin University. Refer also to the 'Barth Effect' discussed below.

"The main objects of this Part are:(b) to facilitate the Australian economy by:

(i) reducing the cost of capital; and

(ii) enabling Australian companies to compete effectively oversees; … and

(c) to maintain investor confidence in the Australian economy (including its capital markets)."

Integrated reporting with its integrated thinking foundation can be a driver of improved productivity within Australian business and the Australian economy. It can enhance confidence in Australia's capital markets, its international competitiveness, and its cost of capital. It can be mapped to the various elements of section 225 as follows:

Section 225 Element	**Component of Integrated Reporting**
Improved productivity	Integrated Thinking
Confidence in capital markets	Integrated Reporting Framework and Integrated Reports
Cost of capital	Integrated Reporting and Integrated Reports

Recommendation

Given the above benefits to Australian businesses and the Australian economy under section 225 of the ASIC Act, Treasury should have the Minister refer the matter of integrated reporting to the FRC for urgent action on the following matters.

2. Whole-of-System Approach / Australian Equivalents to ISSB Standards

The introduction of Australian equivalents to ISSB standards will be an opportunity for the Government through Treasury to address the concerns of Australian directors that the introduction of such standards will require additional reporting to their existing GRI reporting – they want 'one standard' against which they must report.

Treasury probably through the FRC should make clear to investors, directors, and other stakeholders that they can streamline their corporate reports through integrated reports as their flagship corporate report. Many outputs from applying the ISSB or GRI standards will be the same or similar. Such disclosures which are material can be included in integrated reports as discussed above, the focus of which is communicating matters which are material to investors / enterprise value. Stakeholders wanting extra sustainability disclosures that are not currently sustainability-related financial disclosures can be referred to, for example, online data repositories.

Clear government-led communications will be required demonstrating that investors can find all of their information requirements in integrated reports which will include sustainability-related financial disclosures under both ISSB and GRI standards; and that other stakeholders should be able to work with organisations to obtain special purpose sustainability information which is not currently relevant to enterprise value in on-line ESG data repositories. Again, it seems to me that communications around the currently proposed amendments to the ASIC Act will be an ideal opportunity to get this message across to investors and directors.

Recommendation to Treasury

I recommend that the above 'whole-of-system' approach be explained in public communications in relation to the proposed amendments to the ASIC Act, emphasising that further legislative change in addition to the currently proposed amendments is not necessary for integrated reporting to be the foundation of the Australian corporate reporting system, and for integrated reports to be the flagship corporate report in the reports portfolios of Australian organisations. Treasury should also recommend to the ASX Corporate Governance Council that Recommendation 4.3 be strengthened in an update.

3. Related Assurance Approaches - Moving Towards Integrated Reporting Assurance

Integrated Reporting Assurance – that is, assurance expressed in terms of whether an integrated report is in accordance with the Integrated Reporting Framework – is gathering pace around the world, as are regulatory and other drivers for a more integrated approach to assurance with an end game of integrated reporting assurance.

There is a rapidly growing number of integrated report assurance reports (limited assurance) around the world today from a 'standing start' of zero in only 2019, with most of these being in Brazil. ABN Amro, the large listed Dutch bank, was the pioneer or 'headline act' for voluntarily obtaining integrated reporting assurance. It continues to innovate, in 2021 becoming the first organisation in the world to obtain reasonable assurance for components of its integrated report. Rabobank, another large Dutch bank, has emulated ABN AMRO by obtaining integrated reporting assurance on a voluntary basis.

Integrated reporting assurance (and integrated reporting) was mandated by the Brazilian securities regulator in 2021 on an 'opt in' basis, strong initial delivery of integrated reporting assurance to date in 2022 under ISAE 3000. Itau Unibanco, a large Brazilian bank, provides a good example of integrated reporting assurance under the Brazilian mandate.

In Australia, Dexus became the first organisation to obtain integrated reporting assurance, joining the unlisted Cbus and CPA Australia in obtaining integrated reporting assurance.

Building blocks towards integrated reporting assurance – mandates and standards

Spain and France require assurance on partial descriptions of *The Business* on reporting required by EU NFRD / CSRD non-financial reporting requirements, under their interpretations of the assurance requirements under the NFRD / CSRD.

ISSB Standards ISSB S1 and S2 also require partial descriptions of The Business in relation to the matters they cover (eg climate matters in the case of S1). When the AUASB comes to address the potential introduction of the IAASB's overarching sustainability assurance standard, ISSA 5000, it will need to consider support to practitioners in assuring the reporting required by these standards.

Statement of Auditing Standards ISA 720, 'The Auditor's Responsibilities Relating to Other Information', already requires financial statements to read and consider, but not assure, the other information in annual reports containing audited financial statements. It will be a natural step for companies to step this up to obtaining integrated reporting assurance if they believe that their investors would value this. Conversely, financial statement auditors were reminded by the decision in the 2019 Autonomy case[5] which saw severe penalties imposed on financial statement auditors including for breaching ISA 720.

Building blocks towards integrated reporting assurance – internal control assurance

System and organisation control ('SOC') examinations are not formally required, but they are increasingly requested by businesses. The purpose of a SOC engagement is to report on the effectiveness of an organization's internal controls and safeguards in place while providing independent and actionable feedback. Financial statement auditors use them to reduce audit procedures, and sophisticated users of service organisations push for them as confirmation that systems are secure and data is protected.

[5] The facts of the Autonomy case of occurred just before 2010, before strategic reports were introduced in the UK. So this was a time when reporting on The Business was much less structured than it is today in reports such as strategic reports, OFRs and integrated reports. The financial statement auditors were aware of materially misstatements claims about The Business of Autonomy in the first half of the annual report containing audited financial statements, and did not act on that knowledge.

There are potentially three million SOC reports around the world. Given that integrated reports prepared in accordance with the Integrated Reporting Framework have embedded internal control assurance (by way of disclosures about the reporting process as a component of the business model), SOC assurance is a building block towards integrated reporting assurance.

Building blocks towards integrated reporting assurance – industry regulator reporting requirements

Industry regulators around the world require assurance on regulatory reports, including on the extensive Bases of Preparation and Presentation required in those reports. We have assurance on prudential requirements for financial institutions.

In my experience, the Australian Energy Regulator requires assurance from financial statement auditors on mandated reporting in relation to the pricing of energy services (the licence to operate). This reporting and assurance is disconnected and not part of concise, comprehensive and integrated disclosures which investors need to know in relation to licences to operate. The integrated report must include material elements of industry regulatory reports[6].

Implications for ASX Corporate Governance Council, ASX CG Recommendation 4.3 and ASX

Recommendation 4.3 of the ASX Corporate Governance Principles and Recommendations (4th Edition) states: "A listed entity should disclose its processes to verify the integrity of any periodic corporate report it releases to the market that is not audited or reviewed by an external auditor."

Essentially, Recommendation 4.3 is an assurance-based recommendation which goes to the heart of investor confidence in the credibility of unaudited periodic corporate reports.

'Periodic corporate report' is defined in the Glossary to the 4th as: "an entity's annual directors' report, … integrated report, sustainability report or similar periodic report prepared for the benefit of investors."

The Commentary to Recommendation 4.3 includes the following: "Where a corporate report of this type is not subject to audit or review by an external auditor, it is important that investors understand the process by which the entity has satisfied itself that the report is materially accurate, balanced and provides investors with appropriate information to make informed investment decisions."

Footnote 49 to Recommendation 4.3 states, "**'Integrated report' has the meaning given in the International <IR> Framework. … The principles of integrated reporting can be used in preparing existing reports, for example, the directors' report or the operating and financial review**."

Overall, Recommendation 4.3 implicitly recognises integrated reports in accordance with the Integrated Reporting Framework as good corporate governance practice; and supports a case that such reports should be subject to independent assurance given their significance to investors.

A Deakin University white paper, Review of ASX 300 Corporate Governance Recommendation 4.3 Disclosures: Effectiveness of communications and efficacy of integrity enhancement processes' states: "Our analysis reveals that the majority of ASX 300 entities have made efforts to disclose the processes and mechanisms they use to enhance the integrity of their unaudited periodic reports. However, the results reveal significant disparities between entities in the level and quality of their responses to Recommendation 4.3."
(https://www.deakin.edu.au/__data/assets/pdf_file/0006/2488542/8-August-2022-IRC-White-Paper_v6.pdf)

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[6] There is a strong case to argue that a whole-of-government review of corporate reporting is required, so that the volume, complexity and duplication in reporting requirements across all levels of government (all federal ministries, state and local governments) can be addressed and clarity and integration improved for the benefit of Australian businesses and capital markets and Australia's international competitiveness, but that probably goes beyond section 225 of the ASIC Act.

The report went on, “Overall, these results suggest considerable room for improvement in the communication of integrity enhancement processes and mechanisms.”

And, “While the primary focus of Recommendation 4.3 is on the effective communication of the integrity enhancing mechanisms or processes, the ASX has also made clear its interest in ensuring investors and other users have confidence in the credibility of all periodic corporate reports.” And “Boards of directors are ultimately responsible for the integrity of unaudited periodic corporate reports. Yet we found that just 122 out of 240 entities (51%) confirmed board involvement in their processes for ensuring the integrity of unaudited periodic corporate reports. And of these only 33%’ disclosed that the board reviews and takes responsibility for ensuring the integrity of these reports.”

The white paper noted several instances of best practice and noted that “8% of entities reviewed scored the maximum six points … for their actions in relation to Recommendation 4.3.” This was balanced against, “At the other end of the scale, a total of 20 entities (12% of the sample) scored zero across both categories.”

The white paper went on to make recommendations to each of preparers of company reports, the ASX Corporate Governance Council, the ASX and accounting bodies. The recommendation to the ASX Corporate Governance Council listed seven specific items that should be encouraged in future disclosures under Recommendation 4.3, recommending that “The Council should review the wording of Recommendation 4.3 and its associated commentary.”

The white paper made the following recommendation to the ASX: “The ASX should initiate an ongoing process to monitor the quality of Recommendation 4.3 disclosures.” In fact, the ASX has a responsibility to do this under section 792 of the Corporations Act, and to refer serious breaches to ASIC for enforcement action when the ASX does not have sufficient powers under its Listing Rules.

The FRC needs to work more closely with the ASX Corporate Governance Council given its stake in the quality of Australian corporate reporting, including assurance, particularly in light of the findings and recommendations in the Deakin white paper. This would be a significant movement towards a whole-of-system approach to Australian corporate reporting. Attached to this report is a draft briefing paper for the use of the Chair of the ASX Corporate Governance Council with Council members on what is possible regarding integrated reporting. It covers similar ground covered.

Recommendation to Treasury

A joint communication on integrated reporting and integrated reporting assurance from Treasury and the ASX Corporate Governance Council would appear to be appropriate in the light of the significant momentum globally towards a more integrated approach to assurance.

4. Further benefits - implications for integrated reporting education to create capacity

Much has been written about skills gaps in the current Australian corporate reporting system’s traditional almost exclusive coverage of financial reporting and financial statement auditing. That discussion is increasingly being complemented about skill requirements in relation to ISSB and GRI-based sustainability reporting including on climate matters.

The topic is equally relevant to integrated reporting and integrated reporting assurance, with a significant nuance. Education on integrated reporting and integrated reporting assurance will be required. However, unlike ISSB / GRI-based sustainability reporting, the gap is not in the number of qualified people. The right people are already largely in place.

The right people for integrated reporting and integrated reporting assurance is already in place. The key people are in fact the professionals who prepare and audit financial reports. The gap is in their integrated reporting and assurance knowledge, skills and experience.

The required knowledge can be built through the integrated reporting courses available at places such as Deakin University - in courses at under- and post-graduate levels, and through executive education for the accounting, director and investment professions. Accreditation on integrated reporting and integrated reporting assurance can be built into, for example, the entry and continuing professional development requirements of CAANZ and CPA Australia; in the requirements to be a Registered Company Auditor; and in the education curricula of accounting firms.

Integrated reporting skills and experience can be built up on the job and in continuing education as further momentum for integrated reporting develops around the world. The ability of Australians who have integrated reporting expertise should be more internationally transferable given the international coverage of integrated reporting.

As Chancellor of Deakin University, I am confident that those having integrated reporting proficiency will be more inclined to stay in the accounting profession as they will simply have more interesting careers, which will address the current 'brain drain' being experienced in financial statement auditing firms.

Recommendation to Treasury

Addressing the areas set out above is a matter for government policy on education. Again, appropriate communications accompanying the introduction of the amendments to the ASIC Act would highlight these matters.

5. Additional Actions to Facilitate Effective Implementation

There appears to be an experience gap within the collective current memberships of the FRC, AASB and AUASB in relation to the middle box of the Dynamic Materiality Diagram (refer page 3). The gap relates to the fundamentally important place of integrated reporting and integrated reporting experience, and direct industry-based sustainability-related financial (SASB) disclosure experience, within the middle box which provides the outer boundary of reporting on enterprise value for investors.

Reporting to investors in 'middle box reporting' (integrated reporting and sustainability-related financial disclosures) is complementing 'inner box [financial] reporting' and auditing which will be at the heart of the global and Australian corporate reporting systems in the short, medium and long term, driven by the IFRS Foundation, IAASB and overseen by supervisory authorities such as IOSCO, the Monitoring Board, the Public Interest Oversight Board and the International Forum of Independent Audit Regulators.

The recent BRLF report to the FRC included the following recommendations:

- ***Integrated Reporting*** - increased prominence under IFRS Foundation ownership – important for FRC to be directly connected as IR development work and outreach is occurring one step removed from IASB and ISSB standard-setting processes
- ***Integrated Reporting Assurance*** – importance of IAASB and ISSB having a full awareness of rapidly emerging practice around the world towards a more integrated approach to assurance in advance of ISSA 5000.
- **Deakin Integrated Reporting Centre** - direct connections to integrated reporting workstreams in IFRS Foundation & IAASB

I encourage you to think about appointing Michael Bray to the FRC as soon as possible. He is uniquely qualified, possibly in the world, on integrated reporting, integrated reporting assurance, the integration of integrated reporting and integrated reporting assurance.

Michael is presently:

- on secondment from KPMG International as the Special Adviser to the Team Leader of the IFRS Foundation's Connectivity and Integrated Reporting Team;
- Professor of Practice (Integrated Reporting) at Deakin University; and

- a member of the Expert Reference Group for the IAASB's Sustainability Reporting Assurance project.

He regularly interactions with the Global Accounting Alliance, the IFAC-hosted Forum of Firms and the Global Public Policy Committee on integrated reporting assurance matters; and has provided the subject matter expertise for the first two Instalments in IFAC's integrated reporting assurance series[7].

Previously, Michael was:

- a partner of KPMG Australia for 27 years and a Registered Company Auditor;
- a member of the Board of Directors of the International Integrated Reporting Council;
- led KPMG Australia's Better Business Reporting Group, which focuses on integrated reporting and its assurance, and was a member of the equivalent global KPMG network; and
- was the accredited subject matter expert for the first two instances of integrated reporting assurance in Australia.

I believe that Michael would be well supported at the most senior levels of the IFRS Foundation, IFAC, the AUASB, the Australian professional accounting bodies and the American Institute of Certified Practicing Accountants, and at least KPMG among the large global accounting networks.

He would also be an ideal candidate for the Australian government to put forward for appointment as an IFRS Foundation Trustee indue course. Apart from Richard Sexton, former Chair of the Board of Directors of the Value Reporting Foundation, and Barry Melancon, former Chair of the Board of Directors of the International Integrated Reporting Council and CEO of the AICPA, the Trustees are also short on integrated reporting experience.

Recommendations

I recommend that Treasury consider appointing Michael Bray be to the FRC as a matter of urgency.

I also encourage the FRC to elevate the appointment of the Deakin University Integrated Reporting Centre, which provides the Secretariat for the BRLFG, currently a reporting stakeholder to the FRC, to being a formal advisory body to the FRC, replicating the status of the International Integrated Reporting Council, of which I am a member, as an advisory body to the IFRS Foundation Trustees, IASB and ISSB.

<u>No legislative change or new government institutions</u>

None of the above recommendations requires legislative change or the creation of new government institutions.

The FRC can be asked to lead the way on these recommendations under section 225 of the ASIC Act, as their implementation will facilitate the Australian economy by enabling Australian companies to compete effectively oversees; maintaining investor confidence in the Australian capital markets, and right sizing' and reducing the cost of capital. It is within the powers of ASIC to withdraw or change RG 247.

The government and Treasury will be able to inform the public of the recommendations set out above in and around announcements of the changes to the ASIC Act.

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[7] The Global Accounting Alliance is an alliance of the largest chartered / certified public accounting bodies in the world; the IFAC-hosted Forum of Firms is a forum got the world's largest 22 accounting networks; and the Global Public Policy Committee is a committee of the largest six global accounting networks. Both IFAC reports, the first on the nature and value proposition of integrated reporting assurance and the second on the board's governance responsibility for the integrity of integrated reports, can be found at [Executing the Board's Governance Responsibility for Integrated Reporting | IFAC]().