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20 November 2023

## Submission on Consultation Document - Sustainability Assurance

Dear Sir / Madam

Ernst & Young New Zealand (EY) welcomes the opportunity to comment on the Consultation Document, *Sustainability Assurance*, issued by the External Reporting Board (XRB).

The views expressed in our response to this consultation are based on two underlying principles:

1. The lessons, experience and practices developed over decades of assurance over financial statements are highly relevant in considering the appropriate settings and standards to be applied to assurance over non-financial disclosures.
2. New Zealand organisations have benefited from a historical regulatory practice of adopting international standards for financial assurance with only minor modifications. Aligning has strengthened the trust that can be placed on New Zealand assured information by local and international stakeholders, and has supported confidence in New Zealand capital markets. Consequently, we consider a similar approach, of building wherever possible on international standards for sustainability information, would be advantageous for sustainability information assurance.

Our view is that non-financial disclosures, particularly significant Environment, Social and Governance (ESG) disclosures, should have the same level of integrity as financial statement disclosures. Decades of experience with independent assurance on financial statements has resulted in a high degree of public trust in them. For this reason, we believe independent assurance is a key contributor in ensuring this objective is also met in non-financial disclosures. The ultimate goal of ESG assurance standards should be to align with financial reporting assurance expectations. Over time, there should be a desire to move towards an “integrated assurance” approach, reflecting the importance of both financial and ESG information to users in assessing an entity’s overall performance and the interconnected nature of this information.

We believe that any approach which does not seek alignment and consistency with the proposed international sustainability assurance standard(s), will lead to a complex assurance landscape that users do not understand and will likely undermine the credibility of assurance over sustainability information. We are also concerned that any assurance failures over sustainability reporting as a result of having inconsistent requirements, could erode the public confidence in the audit of financial statements as they won’t understand the differing requirements and will consider “an audit to be an audit”. We are mindful that the existing Professional and Ethical Standards (PES) series and financial statement assurance standards have been developed and strengthened over time as a result of regulator and market demands and that such requirements have been considered necessary to ensure



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robust and consistent quality assurance. Given current and emerging concerns with “greenwashing” and the increased reliance on greenhouse gas (GHG) emissions and other sustainability disclosures by financial statement users, we see no reason to believe that the market and regulators will not demand equivalent rigour and standards in the assurance of GHG emissions and (in time) other sustainability information.

We welcome the opportunity to contribute to the improvement of assurance over climate-related disclosures that will continue to drive the quality, consistency, and integrity of such disclosures in New Zealand. We would be pleased to discuss our comments with members of XRB and its staff.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Simon O'Connor', written over a horizontal line.

Simon O'Connor  
Managing Partner

A handwritten signature in black ink, appearing to read 'Pip Best', written over a horizontal line.

Pip Best  
Partner  
Climate Change and Sustainability Services

**XRB Consultation – Sustainability Assurance**

*Consultation Questions Respondents are asked to consider the following specific questions and to respond to the XRB by 20 November 2023:*

**New Zealand specific considerations**

**Question 1. What sustainability assurance engagements do you currently perform?**

New Zealand sustainability-related assurance engagements	International sustainability-related assurance engagements
<p>EY New Zealand provides predominantly limited assurance and occasionally reasonable assurance over the following subject matters:</p> <ul style="list-style-type: none"> <li>▶ GHG emissions assurance (mandatory from 2025 for Climate Reporting Entities)</li> <li>▶ NZ ETS return assurance (voluntary)</li> <li>▶ New Zealand Climate Standards</li> <li>▶ Sustainability report assurance (mainly against voluntary GRI)</li> <li>▶ Sustainable finance assurance (voluntary)</li> </ul>	<p>EY internationally provides a mix of reasonable and limited assurance over the following subject matters:</p> <ul style="list-style-type: none"> <li>▶ GHG emissions assurance</li> <li>▶ ETS submissions assurance</li> <li>▶ TCFD and scenario analysis assurance</li> <li>▶ Sustainability report assurance (most current interest is around ISSB and CSRD related assurance)</li> <li>▶ Sustainable finance assurance</li> <li>▶ Sustainability targets</li> </ul>

Although the list above makes the subject matter of NZ and international assurance engagements look similar there are some key differences, we think are important to highlight:

- ▶ **Maturity of the sustainability-related assurance market:** NZ is less mature than many other comparable countries and there are fewer voluntary engagements for similar organisations<sup>1</sup>. Consequently, record keeping on sustainability-related metrics is comparatively poor in New Zealand. We would expect a Basis of Preparation to exist for companies looking to assure sustainability-related information, which is equivalent to our expectations for financial statement assurance. In New Zealand, for most first year assurance engagements (including many that have previously been subject to assurance by other assurance providers), this documentation does not normally exist.
- ▶ **Assurance over GHG reporting requirements:** Most comparable countries have had some level of mandatory assurance over their main GHG emissions reporting regimes<sup>2</sup>. New Zealand has no visible assurance programme over any GHG emissions reporting to-date (e.g. NZ ETS). Voluntary engagements over this subject matter have been limited to-date, despite the significant financial implications for some entities and Government. The NZ GHG reporting criteria is also less developed and rigorous than comparable documents (e.g. the Australian NGERs Determination) in other jurisdictions.

<sup>1</sup> For example, based on our report *New Zealand Insights: How can ESG reporting fuel positive change?* Fourth ESG reporting maturity assessment (September 2022) where we assessed the ASX200's and NZX50's sustainability reports, it was found that 19% of NZ companies sought assurance over sustainability disclosures compared to 36% of Australian companies.

<sup>2</sup> For example, Australia's Clean Energy Regulator runs a rigorous annual assurance programme over NGERs reporting and Safeguard Mechanism, Europe and UK require third-party verification over EU ETS submissions.

- ▶ Forward-looking assurance: Internationally, sustainability-related subject matter with some element of forward-looking calculation is common-place (e.g. TCFD scenario analysis assurance, GHG emissions and production forecasts and sustainability target setting)

**Question 2. What sustainability assurance engagements have you been requested to perform?**

As above.

**Question 3. What assurance standards do you currently use to perform each type of sustainability assurance engagement?**

We use the following standards for sustainability assurance engagements:

- ▶ ISAE (NZ) 3000 (Revised) Assurance Engagements Other than Audits or Reviews of Historical Financial Information (ISAE 3000); and
- ▶ For GHG assurance only - ISAE (NZ) 3410 Assurance Engagements on Greenhouse Gas Statements (ISAE 3410).

We have found that ISAE 3000 can be used broadly across all sustainability-related subject matters. The characteristics of suitable criteria is an extremely useful tool for assessing whether an assurance engagement can be conducted over bespoke criteria. This is particularly important for sustainability-related subject matters due to the concept of materiality meaning not all metrics are fit-for purpose for all users and some need tailoring.

**Question 4. What are the key challenges in assuring sustainability information in accordance with these standards?**

ISAE 3000 lacks clarity in certain areas which creates challenges when performing sustainability assurance engagements. For example, the nature, timing and extent of procedures required for limited versus reasonable assurance, is not covered in sufficient detail to create a consistent expectation of the work required. The variety of sustainability subject matters also adds inherent challenges when performing assurance against ISAE 3000. Adopting Exposure Draft: Proposed International Standard on Sustainability Assurance 5000 (“ED-5000” or “ISSA 5000”), a specific sustainability assurance standard, that can be applied across type, industry, sectors and varying sizes of entities and complexities would be useful in addressing these issues.

We believe the requirements and application material dealing with assurance engagements on GHG statements should be aligned as soon as possible with ED-5000 instead of ISAE 3410. Assurance over GHG statements should not be conducted substantially differently than assurance over other sustainability information. Once this has been aligned, we suggest all regulatory required GHG assurance engagements follow this standard for consistency across the New Zealand market, and likely alignment internationally.

Unless specific standards are used, companies use bespoke calculation methodology and emissions factors to measure or create a metric that addresses their specific areas of interest. As the methodology and criteria are bespoke, each of these (including the disclosures) are required to be assessed to determine if they are appropriate in accordance with the ISAE 3000 characteristics of suitable criteria. This also requires that bespoke calculation methodologies are made available to the intended users of the assurance reports so users do not have to make their

own interpretation and potentially misunderstand the metric. Similar to our above comment, a specific sustainability assurance standard that addresses the varied nature of sustainability related information would help address current challenges.

Although not related to an issue with ISAE 3000 or ISAE 3410, one of the key challenges faced when performing sustainability assurance is insufficient record keeping. The control environment over sustainability information varies across entities, and on the whole the record keeping for sustainability-related subject matter tends to be poor in New Zealand. The level of controls, documentation of processes and methodologies (such as a Basis of Preparation) and general document keeping often present initial challenges for the purposes of assuring the subject matter.

We encourage the XRB to adopt any amendments to ISAE 3000 which are expected to be made by IAASB to align ISAE 3000 with ED-5000. Otherwise, there is a risk that assurance over non-sustainability related information is seen to be performed using a lesser standard, and there will be confusion about why ED-5000 would have more robust requirements.

#### **Question 5. What assurance activities do you think are most suited to sustainability reporting in New Zealand and why?**

Assurance should be conducted over material topics and the key disclosures that relate to these topics, based on a double materiality assessment. As sustainability assurance is primarily voluntary within New Zealand, the reasons and rationale for obtaining assurance over a given metric varies entity by entity. The metrics selected for assurance are often inconsistent with those reported within public reports and some do not have significant connections with the strategic direction of the organisation.

We need to facilitate a shift in the New Zealand assurance market to focus on material non-financial metrics and disclosure contained within public reports, to provide confidence and reliability over this information to users.

#### **International Developments**

#### **Question 6. Do you have any comments on the IAASB's ED 5000 to inform the External Reporting Board's submission?**

As this relates to an international standard, our EY Global Assurance Standards and Global Professional Practice (EY Global) is also responding on ED-5000 directly to the IAASB. We understand that EY Global is supportive of ED-5000. To avoid duplicating EY Global comments through our EY New Zealand response, we refer the XRB to our EY Global response, which we understand will be provided after the XRB's consultation response date. We have provided a summary of our thoughts on ED-5000 and its application to the New Zealand market.

We think New Zealand has benefited from its historical approach to accounting and assurance, which is to adopt international standards and then provide only the modifications or additions that are needed to align with our national situation, in essence a "fatal flaw only" approach to modifications or additions. We are therefore in favour of standards that are able to provide international comparability, such as IAASB ED 5000. Our main comments on ED-5000 are listed below:

- ▶ We are supportive of ED-5000 as an international standard for sustainability assurance

- ▶ We support the approach taken by IAASB to develop ED-5000 based on ISAE 3000 (revised), ISAE 3410, some ISA requirements and some aspects of EER guidance
- ▶ As above, although we strongly support ED-5000 we are concerned about the consequences it brings in the form of inconsistencies with existing assurance standards. We believe the requirements and application material dealing with assurance engagements on GHG statements should align as soon as possible with ED-5000 instead of ISAE 3410 and be moved to the ISSA 5000 series. Coexistence of ISAE 3410, ISO and ISSA 5000 would create undue complexity and be difficult to understand by the users of the assurance report
- ▶ We support the XRB Board maintaining its approach to harmonising accounting and assurance standards with Australia and adopting international auditing and assurance standards, such that they are substantively identical to the international standards. One assurance standard that is applicable to all jurisdictions is efficient and improves assurance understanding, particularly for entities that operate and report in multiple jurisdictions.
- ▶ Currently ISSA 5000 does not contain anything to assist the assurance practitioner in determining whether the client’s material sustainability risks have been identified and disclosed. More should be included in the standard regarding this.

**Question 7. What standards do you apply for quality management for sustainability assurance engagements?**

We apply PES 3 for quality on sustainability assurance engagements and will also be applying NZ SAE 1 shortly.

**Question 8. What standards do you apply for Ethics and Independence when performing sustainability assurance engagements?**

We apply PES 1 and the NZICA Code of Ethics for ethics and independence on sustainability assurance engagements. We will also be applying NZ SAE 1 when conducting future assurance over GHG emission disclosures. As mentioned above, the IESBA Code of Ethics and NZ equivalents are the most appropriate standards for quality and ethics and independence.

**Question 9. What could be some key pillars for Ethical and Independence standards for sustainability assurance?**

We strongly recommend assurance practitioners ethical and independence pillars should at least be as demanding as the ethical and independence matters relating to audit (part 4A in PES1) in the IESBA code (and the New Zealand equivalents). We agree with the general approach of NZ SAE 1 to apply tighter independence requirements to sustainability assurance than would be applied by part 4B of PES 1.

As the IESBA code, or at least as demanding requirements, are expected to be adopted by those applying ED-5000, we strongly recommend XRB adopts the IESBA’s developing profession-agnostic ethics and independence standards for sustainability assurance, which is expected to be international leading practice, and issued by the end of 2024. IESBA has already determined that “...certain sustainability assurance engagements must be underpinned by the same high standards of ethical behaviour and independence that apply to audits of financial information. ...”. We understand that new professional and ethical standards issued in New Zealand to date

have been based on the IESBA code with minor New Zealand amendments and we strongly recommend this approach is maintained. This keeps New Zealand assurance quality, independence and ethics requirements in line and consistent with the global practice, ensuring that the users of assurance reports have the same trust and understanding of New Zealand assurance engagements compared to international assurance engagements.

However, we acknowledge the challenges raised by others, who are not accountants, that the IESBA code concepts are complex, detailed and may be difficult to implement. We suggest the XRB leverages the guidance set out by IAASB on what standards are at least as demanding and gives clear guidance to New Zealand users how to apply this in New Zealand. We note the XRB could address the concerns of the non accounting profession by:

1. Giving an appropriate amount of time and education for adoption to allow other providers to meet the standards of other practitioners.
2. Applying the IESBA code to at least engagements with a wide audience or range of stakeholders. This would include but not be limited to assurance reports in the public domain. In particular, this addresses the rapidly changing sustainability reporting landscape we see internationally (e.g. Europe and Australia), where integrated assurance is expected to be leading practice and the non-financial assurance subject matter expanding to and interlinking with financial information. Therefore, the pillars for these types of assurance engagements (climate / sustainability related annual disclosure reports) should follow international standards used by assurance practitioners, in particular to protect the wide audience and range of stakeholders.

If the XRB decides to use standards not developed by the IESBA, or makes amendments substantially reducing the independence and ethical requirements for any sustainability assurance engagements, we would have the following concerns:

- ▶ Variances in requirements undermines assurance credibility, increases confusion over the standards and results in a loss of stakeholder trust and confidence in the assurance practice, which is paramount to our service.
- ▶ Any New Zealand standard setting initiative which reduced independence, ethics and quality management standards for sustainability-related engagements below the requirements of the IESBA code, PES 1 and PES 3, would also likely be out of step internationally, and this may have wider implications in the assurance market. For example, New Zealand firms are not engaged internationally as they don't meet other country or organisation independence and ethical requirements for their assurance providers.
- ▶ There will be a perceived two-tiered system, as regulated practitioners (i.e. those registered with NZICA to perform financial statement audits) will still be required to apply the IESBA code and New Zealand equivalents, creating cost inequalities on one provider versus another.

**Question 10. What issues could Ethical and Independence standards for sustainability assurance address?**

Refer above.