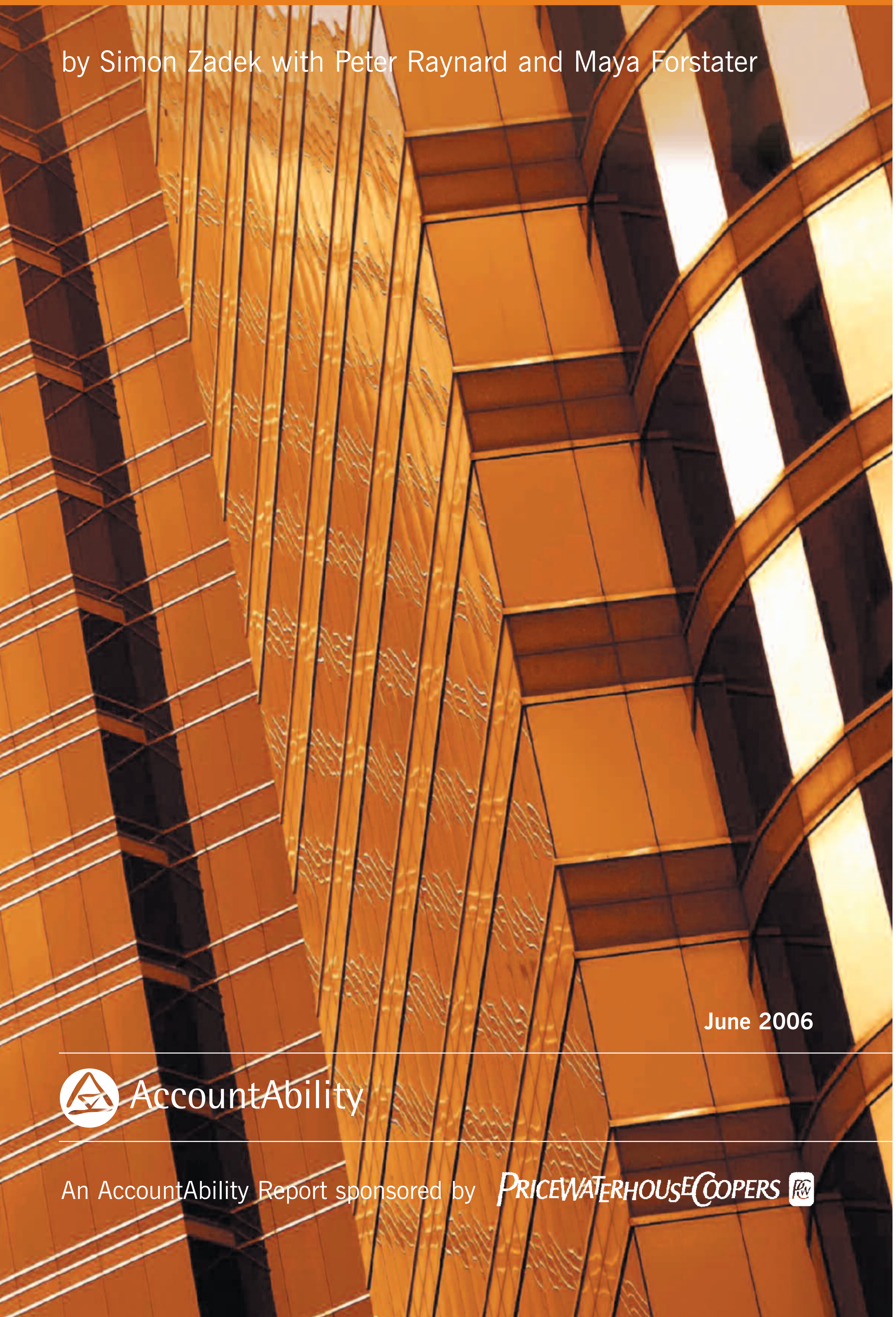
What Assures?

Listening to words of assurance



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AccountAbility

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Forewords

PricewaterhouseCoopers, as the world's largest professional services firm, with a major assurance practice, clearly has a substantial interest in exploring how organisations can get more value from those aspects of their operations where they seek formal assurance.

Whilst much of our assurance work still relates to the audit of financial statements, we also provide public assurance over data and wider information processes in a very wide range of circumstances – from sign off of information included in listing documents, to regulatory returns and environmental, social and economic information included in sustainability reports.

We recognise that the environment in which we provide assurance is consistently evolving and it is vital that we, and other assurance providers, understand the changing assurance needs of our clients.

For this reason we have asked Accountability to undertake some independent research to explore 'What Assures' as part of our long term programme of research and thinking in this area. We believe this study provides a significant contribution to the debate about the future direction of assurance – an important issue for society. We will therefore be reflecting on its findings and will continue to work with others externally to engage on this issue

David Phillips, Corporate Reporting partner, PricewaterhouseCoopers LLP

The conclusions and views expressed in this study are those of AccountAbility and are not necessarily shared by PricewaterhouseCoopers, the sponsors of the work.

Assuring stakeholders that your organisation is delivering on its commitments is ever more challenging in today's increasingly complex, interconnected and fast-moving world. All the more so for larger corporations that often have, literally, hundreds of thousands if not millions of stakeholders, clustered into groups with diverse perspectives and interests.

Our collective challenge is to understand the evolving assurance needs of organisations' stakeholders, including investors and wider communities of interest. This challenge underpinned PricewaterhouseCoopers' decision to invite AccountAbility to explore the question of 'what assures', taking as a starting point stakeholders' own experiences and needs, rather than the traditions of professional auditing.

The findings provide much food for thought, and carry lessons for professional service firms like PricewaterhouseCoopers and other groups assisting in the delivery of this assurance. Professional auditing has a critical role to play, but clearly has to be part of a wider approach. Assuring stakeholders requires a complex mix of 'hard' auditing skills and experience, wide-ranging expertise in subjects as diverse as emissions, labour standards and economic impact, and communication and engagement techniques that enable stakeholder involvement.

What assures stakeholders evolves over time, as well as varying between institutions and geographies. This piece of work is one contribution to our evolving understanding of this complex field, and we hope will serve a useful purpose.

Tom Delfgaauw, Chair of the Council, AccountAbility

1. Executive Summary

Today, a diverse set of stakeholders are demanding a higher level of assurance about the products and practices of companies. Whether as a consumer, investor, trades unionist, activist, or auditor, we are seeking assurance about the products, services, financial health, employment conditions, and overall propriety of the businesses we interact with. At the same time, these are also the concerns of those within companies, whether they are a CEO, manager, or employee.

Against a background of growing suspicion of business, historic mechanisms for providing assurance may not be adequate. There is concern amongst a number of stakeholders that traditional forms of reporting and assurance, i.e. those which focus solely on financial reporting and audit methodologies, are not adequate to provide reassurance to stakeholders over the wider challenges now facing companies, such as human rights, environmental impact and labour conditions. One response by companies to these growing concerns has been 'sustainability reporting', which is increasingly assured by a currently diverse range of independent third parties.

Sound non-financial reporting and associated assurance is now understood as an important element of good corporate governance. The reporting and assurance of social and environmental performance was initially seen by many as incidental to core business activities. This viewpoint, however, is changing and a growing number see non-financial reporting and assurance as key to understanding how businesses perform. In particular, the reporting and assurance of social and environmental information, often in the form of Corporate Responsibility or Sustainability Reports, is increasingly seen as providing a test bed for developing some of tomorrow's mainstream reporting and audit practices.

AccountAbility, sponsored by PricewaterhouseCoopers, has carried out this study, 'What Assures', to listen to the assurance concerns of those stakeholders who are interested in and affected by the social and environmental impact of companies. The report therefore concentrates on the practice of assurance in the sphere of corporate responsibility, but also considers the implications of these developments for the wider field of assurance covering both financial and non-financial aspects of corporate performance. The study examines the diversity of stakeholders seeking assurance, the type of data they are looking for, and how well they are being assured, and offers a set of predictions of what will assure stakeholders in the 21st century.

We interviewed over forty opinion leaders and practitioners from a range of organisations. These included: the newspapers Guardian and Financial Times; non-governmental bodies such as Amnesty International, Friends of the Earth, WWF, the National Consumer Council, and Association British Insurers; the trades unions the International Textile, Garment and Leather Workers Federation; the labour rights partnerships, The Ethical Trading Initiative, and Fair Labour Association; and the companies, The Gap Inc., Glaxo Smith Kline, Marks & Spencer, Novozymes, and Starbucks.

In determining 'what assures', one of the greatest challenges for businesses today is to decide which stakeholders count most, and thus need to be reassured to secure their contribution to business performance and success. In this context, effective assurance is driven by the demands of stakeholders for material and reliable information on which to make decisions. Identifying who needs assurance is therefore not straightforward or amenable to a 'checklist' approach. Stakeholder engagement and assurance need to be focused and targeted to meet the needs of dynamic stakeholder sub-groups, ranging from politicians and regulators to consumers and NGOs. Those companies interviewed, were well aware of the complexity of stakeholder relations, recognising the need to understand differences within, as well as between different stakeholder groups.

The challenge of providing assurance to stakeholders is often heavily influenced by the type of data, information and reporting proffered by companies. One of the areas where there was strong agreement across the interviewees was the need for reporting and assurance to enable forward-looking assessments to be made about a company's performance. But they also recognised the difficulty of integrating such forward-looking assessments into traditional conceptions of audit and assurance that have arisen in the context of audits of financial statements. This gave rise to discussions concerning how different stakeholders are assured on the basis of different parts of the data chain, which spans information about values and strategy through decisions and actions to end-of-pipe impacts, conformity with laws and standards, and reputation.

The Data Chain

Values/ purpose	Strategy	Behaviour/ actions	Impacts	Compliance	Reputation
'What you say'	*'What you plan'*	*'What you did'*	*'How much value you created (or destroyed)'*	*'Whether you meet standards'*	*'How others judge you'*
Statements, commitments	Plans, policies	Narrative description, system documentation	Performance indicators and analysis	Standards certification, conformity assessments	Endorsements Stakeholder perceptions of performance

Although helpful as a framework, it is also clear that describing a data chain in this way may mask the challenge faced by companies in meeting the diverse appetite of stakeholders for different data, at different times, and in different forms. But in general, what this means is that traditional reporting and audit methods that focus on accurate descriptions of historic performance, rather than predictive value, whilst still important, are not sufficient to deliver assurance to these groups.

Traditional, formal audit processes have led the way in securing a level of trust and stability to financial markets but how well stakeholders are assured depends on a mix of formal and informal sources of information. These information sources may be in the public domain or shared amongst a privileged set of networks. These sources range from public statements embodied in corporate reports and independently assured, through to direct engagement with stakeholders, both in one-off consultations or more long-term multi-stakeholder partnerships. There was a recognition by interviewees that although informal information flows were valuable, they did not necessarily undermine the need for formal assurance. Yet, there was also scepticism that formal assurance of non-financial information could not be provided solely by those traditionally engaged in financial auditing and related practices, particularly with regard to labour rights and employment conditions in developing countries. Thus, assurance providers themselves need to ensure credibility with stakeholders through both a technical competency as well as a set of values conducive to the social and environmental concerns of the stakeholders in question. In essence there is a need for them to develop a social contract with stakeholders as part of an assurance process.

The methodology employed by assurance providers is also a factor in determining how well stakeholders are assured.

- Firstly, stakeholders feel there is a need to link formal assurance more effectively with informal information flows and networks; interviewees agreed that assurance as an outcome often has as much to do with the engagement of the organisation wishing to assure as with formal assurance processes (for example, the ability and willingness of senior management to engage with investor analysts and fund managers).

- Secondly, there is a need to move beyond assuring accuracy to assuring materiality. This means it is key that the inclusion of information is both relevant as well as reliable. The present challenge is a lack of established suitable criteria by which to evaluate the relevancy and completeness of the information presented.

- Thirdly, is the need for formally recognised standards for governing sustainability assurance. Efforts here are underway, but the limited range of formally recognised assurance standards and a lack of a generally accepted process, accompanied by the diverse range of practice, leads to confusion and cynicism.

- Finally, interviewees agreed that assurance is not a panacea, and that it could be most effective when its role was clear and limited to providing confidence in information.

So what will assure stakeholders in the 21st century?

Assuring stakeholders in the 21st century will be an increasingly difficult feat. The challenges include the diverse nature and fluidity of stakeholders and their information needs, which range from job insecurity, health care costs and pension deficits through to terrorism and climate change. What is certain however, is that there is no one action or process that assures stakeholders, but rather a number of occurrences that happen along the pathway of engagement in which trust can be fostered, as well as undermined. It is this engagement pathway then that links informal with formal generally accepted processes.

Effective routes to assuring stakeholders have also to be protected from systemic factors over which the company has little or no control. For the company this may be the impact of a general sceptical view of business (fat cat pay, financial misdemeanours, poor supply chain working conditions), whereas for the assurance provider claims to independence will be challenged if a competitor's conflict of interest with a client makes the front page. Robust methodologies employed in formal assurance need to be complemented by integrity and independence, but also reflect the wide set of values held in high regard by stakeholders. As such, in the future, effective assurance is just as likely to be based on values and commitments as on the principle of independence or technical competency.

Finally, effective assurance in the future is likely to be based on a 'joined-up' approach rather than a module assembly of different elements. Today's practice involves companies engaging with stakeholders, and then auditors being brought in to check the data. Tomorrow's practice will involve assurance providers in the engagement of stakeholders in order for them to build trust and credibility by demonstrating knowledge, sensitivity and individual integrity.

2. The assurance imperative

Assurance to secure trust is the currency of the age. As Doug Miller, President of GlobeScan, underscored in launching the second global survey of trust at the Davos 2004 meeting of the World Economic Forum, *"Trust is the single largest driver of public attitude on a whole range of issues from globalization to terrorism to the role of governments. Trust also is a prime driver of corporate and country brands. As goes trust, so goes the world*"[1]. Yet trust appears to be thin on the ground – some have said it is in crisis.

Trust in information often underpins, but is not the same as *trust in an organisation* itself. The annual Edelman Trust Barometer Survey makes this distinction by asking people to rate how much they trust different types of organisation to "do what's right" and as credible sources of information. Organisations are perceived differently according to the two different types of trust. For example in the US, 48% of respondents trust businesses to 'do what's right' but only 25% trust what a CEO says as a reliable source of information about his/her own company. In both Europe and the US around 50% of people trust the media as a source of credible information about companies but only 30% have any faith in the media's own principles to 'do the right thing'.

Many of society's historic assurance mechanisms, signals and informal codes of conduct linked to membership of a family, community, class or religion, to mention but a few, are in decline. The tradition of the handshake once lay at the heart of the basis of trust for many business dealings, but has in most societies long since lost its reassuring value. Even electoral representation, the modern mechanism of securing the legitimacy and accountability of our political representatives and one of humankind's greatest single accountability innovations, is proving less than reassuring to growing numbers of disillusioned youth and minorities.

The evolution of assurance

The investment community has historically been the focus of business's assurance activities. The main mechanism by which investors are assured of the performance of a company is through the financial facts and figures proffered by businesses and audited by professional accountancy firms. This process has a long and rich history and has been the foundation to securing trust in a company's financial health - and it remains so today.

Financial auditing is now a complex business, the practice of which is enshrined in a multitude of different standards all reflecting the convoluted nature of the modern company. But business has always had to provide assurance to others as well.

Customers have been assured for example through advertising and independent product labelling schemes; governments through inspection and statutory reporting; and employees both directly through contracts and personal assurances and through agreements to recognise and consult with trades unions. And the list of stakeholders and issues which companies recognise as important to their business is growing. Companies have to consider issues from employee health and the impacts of outsourcing to climate change and international conflict.

But there is a growing concern about the way in which this expansion in assurance is going. In a study of the state of auditing in the UK, Professor Michael Power of the London School of Economics, described the UK as the 'audit society' and is sceptical about whether audits deliver what they promise in terms of greater accountability, efficiency and quality, and questions whether they in fact fuel the problems which they address by exacerbating distrust. He has gone so far as to suggest that there is a 'pathologicality of excessive checking' (Power, 1997). Similarly, the philosopher Onora O'Neill in her 2002 Reith lectures, believes that accountability mechanisms, which essentially are there to secure trust in society, have largely failed. "Auditors scrutinise accounts (but are they trustworthy?). Examiners control and mark examinees (but are they trustworthy?). The police investigate crimes (but are they trustworthy?)…. The efforts to prevent abuse of trust are gigantic, relentless and expensive; and inevitably their results are always less than perfect" (O'Neill, 2002). It is clear that, despite the development of more and more mechanisms of assurance in recent years, people have continued to become less and less trustful of organisations. The World Economic Forum's annual global survey of trust in national governments, the United Nations and global companies has reported a downward trend since tracking began in 2001. What this means is that technical solutions to assurance on their own do not build trust.

Assurance services in the context of business, aim to underpin trust in information about the profitability, legality and sustainability of a company's operations and activities. They guarantee the quality of data which allows managers, investors and regulators to make decisions. However, the spate of corporate failures and accounting scandals have somewhat undermined trust throughout the corporate reporting supply chain: from company executives and boards of directors through to independent auditors, the media and PR companies, as well as third-party analysts. Less high-profile, but ultimately more significant, has been a growing concern that traditional financial audit methodologies are not adequately capturing emerging new sources of economic value or risk. PricewaterhouseCoopers, in their work on the future of corporate reporting highlight the challenges to reporting and assurance[2]:

- **Accounting and assurance systems have struggled to keep up with the growth in magnitude, complexity, and exposure to risk of modern businesses.** The patchwork of national regulations developed over time to address specific needs has become unwieldy and not fit for purpose.

- **Information needs are changing.** Stakeholders increasingly seek assurance about how an organisation creates economic and broader societal value (positive and negative). Current modes of assurance governed by tradition, regulation and existing standards may not meet the needs of investors and other stakeholders for timely, relevant information on which to base their decisions. For example, a PricewaterhouseCoopers' survey of 43 investment professionals in the UK found overwhelming agreement that the current reporting model fails to meet investors' needs for the information necessary to assess growth prospects and risks.[3]

- **Stakeholders seek the information they need from a range of sources.** Peer-to-peer communities whether in the real world or mediated by technology are increasingly providing information and influencing opinion. *e*Bay demonstrates the power of a peer-to-peer assurance system for building trust between anonymous buyers and sellers. Non-governmental organisations, together with the communications and media industry, provide a source of unregulated, network-based, open source assurance.

In the face of these changes, auditors, the global profession most focused on the provision of assurance, have begun to adapt. They have become more sophisticated in applying increasingly complex techniques to identify, assess and report on financial and non-financial transactions, measures of value, and indicators of quality. But there is a view emerging from thinkers in business, the investment community and in particular other information users, as well as amongst audit professionals that today's systems are too steeped in outdated tradition, too patchy, complex and unresponsive to be fixed, and must be rebuilt. As PricewaterhouseCoopers's Viewpoint on the future of corporate reporting concludes: *"Corporations are providing a huge volume of information at considerable cost (including the cost of assurance), solely to meet the needs of regulators. Yet the increasingly voracious, and legitimate, information demands of today's investors and other stakeholders are not being adequately met. Much of the information they receive today strikes them as irrelevant, and much that they want and deserve has no place in the current reporting model. They go in search of the information they need from other sources. Today's questions are not satisfied by yesterday's answers."*[4]

Added to financial and other non-financial assurance (e.g. third party assurance over specified controls commissioned by outsourcing service providers on behalf of their customers), has been what has commonly become known as sustainability reporting and assurance. Companies have for a number of years been reporting on their social and environmental performance. The latest international survey of corporate responsibility reporting by KPMG shows there to be a rapid increase in such reporting over the past three years, in particular there has been a historical shift from purely environmental reporting to sustainability (social, environmental and economic) reporting (KPMG, 2005). But it was soon recognised that there was a need to provide external assurance of the data, akin to their parallel financial reporting and assurance processes. Consequently, as with sustainability reporting, year-on-year there has been a steady increase in associated sustainability assurance.

Sustainability reporting and assurance was initially seen by many as a side affair, essentially a niche market requiring specialised competencies on the part of both the reporter and assurance provider, and an unusual and somewhat unprofessional, 'engaged' approach to building credibility. This point of view is, however, changing. Sound sustainability reporting and associated assurance is now understood as an important element of good corporate governance. Indeed, measuring good corporate governance requires increasingly sophisticated non-financial metrics, including social and environmental (SustainAbility/UNEP, 2004; Global Reporting Initiative, 2002).

There is now an emerging 'standardisation' of sustainability assurance. The International Auditing and Standards Board (IAASB), of the International Federation of Accountants, which regulates the accountancy profession, has released an international standard on assurance engagements (known as ISAE3000), to guide professional accountants in, amongst other things, engagements relating to sustainability assurance (IAASB, 2003). You will now see amongst the assurance statements of major companies' sustainability reports reference to the use of ISAE3000 by the provider, as well as other standards and guidelines developed by national accountancy bodies (e.g. Standards Australia; Dutch Royal NIVRA). The other main standard used by companies but not developed by an accountancy body is AccountAbility's AA1000 Assurance Standard. Established in 2003, it 'is a generally applicable standard for assessing, attesting to, and strengthening the credibility and quality of organisations' sustainability reporting' (AccountAbility, 2003a). Sustainability and corporate responsibility reporting and assurance, as the practice matures, is seen by growing numbers as providing a test bed for developing some of tomorrow's mainstream audit practices, i.e. practices that may be applied to assurance of the whole gamut of financial and non-financial information. The test will come in meeting what has been termed the 'audit expectations gap', where there has been an overemphasis on the accuracy of data to the detriment of its completeness and materiality, which requires the involvement of a wider group of stakeholders than have been included to date (Zadek & Raynard, 2004; Adams & Evans, 2004).

What assures?

PricewaterhouseCoopers has asked AccountAbility to explore the trends and developments in the field of corporate responsibility and sustainability assurance to date and to consider how these innovative and experimental approaches can illuminate the future of assurance in relation to both emerging issues and the traditional sphere of financial assurance.

> The question "What Assures?" makes the distinction between assurance as an *outcome which stakeholders seek*, and assurance as a set of processes which *organisations and individuals carry out* in order to meet this appetite. This includes professional assurance services, but also a wider range of other approaches, which organisations use to provide confidence in their assertions.

The context for this report is a view held by both PricewaterhouseCoopers and AccountAbility that to understand the drivers of business success you ultimately need to understand the interconnectivity between non-financial and financial aspects of performance. Effective corporate governance, and elements of the emerging 'corporate responsibility' agenda are increasingly recognised as core performance drivers. Support for this view was given by several thousand investors, analysts, and business executives surveyed by PricewaterhouseCoopers who agreed that the current reporting model lacks valuable contextual and non-financial metrics. More than 75 percent of the measures that management and investors ranked as important were contextual and non-financial (Thomas, 2002). A report by Travis Engen of Alcan and Samuel DiPiazza of PricewaterhouseCoopers for the World Business Council for Sustainable Development (WBCSD), concluded: "companies that infuse accountability into their business strategy find they are better able to connect their people to value creation" (Engen & DiPiazza, 2005).

This report concentrates on the experience of assurance in the sphere of sustainability reporting as it is currently practiced, and labour standards supply chain monitoring, but also considers the implications of these developments for the wider field of assurance covering both financial and non-financial aspects of corporate performance.

Our approach builds on our previous work on sustainability assurance – notably 'The State of Sustainability Assurance' published in 2003 and 'The Future of Sustainability Assurance' published for ACCA in 2004. Both reports focused on professional non-financial assurance from an organisation-centred viewpoint. This report takes a wider and more audience-centred focus in asking stakeholders, interested in and affected by the social and environmental impact of companies, "What Assures?"

Figure 1:What Assures? The relationship between assurance as process and outcome

Assurance as an outcome *Audience centred*	***What Assures?***	**Assurance as a process** *Organisation centred*
Stakeholder confidence that the information they have is accurate and complete enough for them to make an informed decision (for example based on an organisation's values, commitments, policies, actions or performance)		**Formal assurance services** *"an evaluation method that uses a specified set of principles and standards to assess the quality of an organisation's subject matter and the underlying systems, processes and competencies* that underpin its performance" AA1000 Assurance Standard *"the provision of confidence or certainty by an independent assurance provider to a party or group of persons in relation to certain subject matters"* FEE 2003
		Other means of assurance • Gossip, word-of-mouth • Personal statements from those responsible • Demonstration, see for yourself • Guarantees • Quality marks, certification • Membership of professional bodies and multi-sector initiatives • Expert authority • Brand reputation • Legal liability • Peer review

'The Future of Sustainability Assurance' used an analytical framework based on four key dimensions of assurance: 1. Appetite (who is assurance for?), 2. Methodology (how is assurance carried out?), 3. Focus (what is covered by the assurance?) and 4. Providers (who gives the assurance?). Building on this research and discussions within our networks we have developed a set of four propositions and related questions about the current state of developments in sustainability assurance, which capture leading edge thinking and experience in the assurance debate:

Figure 2: What Assures? Propositions and Questions

	Proposition	Questions
Appetite	**Effective assurance is driven by the demands of stakeholders for reliable and trustworthy information on which to make decisions** rather than simple compliance with legal requirements.	• What value do stakeholders place on the current assurance they receive, and what actions do they take on the basis of their level of assurance?
Scope	**Assurance can add most value when it enables forward-looking assessments** by establishing what is material to whom, why and to what effect, and illuminating the ways in which the organisation has a social, economic and environmental impact.	• Why and about what do key stakeholder groups want assurance on a company's assertions about their performance? • How can formal assurance support forward-looking, rather than rear-view mirror, views of the organisation?
Methodology	**Effective assurance must be defined in terms of an outcome, not a process.** Stakeholders often seek assurance through informal, high-trust dialogue, and word-of-mouth between stakeholders, rather than through formal assurance.	• What would provide stakeholders with greater assurance, and to what effect? • How can formal assurance draw from and influence informal assurance processes and conversations?
Providers	**The credibility provided by assurance providers depends on their relationship with stakeholders** – are they able to interact with and understand stakeholder views and are their pronouncements deemed trustworthy by the particular group of stakeholders they seek to assure?	• What kinds of formal assurance are likely to deliver value in the future to the business community by being meaningful to its stakeholders? • How can assurance providers demonstrate their credibility and integrity, given the complexity and intertwined nature of network relationships with both the organisation and its stakeholders? • What forms of accountability should formal assurance providers have to non-traditional stakeholders (e.g. NGOs) who are becoming either the audience or subject of their assurance processes?

Our research approach has been, quite straightforwardly, to ask people. By taking this approach, we have not sought to secure robust sampling that would in turn provide statistically meaningful results. Rather, we have taken the view that more at this stage can be learned through an in-depth qualitative dialogue with the right people, complemented by a review of thinking, experience and opinions from the relevant literature.

Specifically, we conducted a series of interviews with some forty opinion leaders and practitioners, experts and users of assurance in the field of social and environmental performance. Those people selected and who agreed to participate come from business, the financial community, the media and civil society organisations. Although having diverse jobs in very differing institutional environments, they have in common, knowledge and in many cases visible international leadership in the management and integration of social, economic and environmental issues into business process and performance management.

The range of organisations we interviewed representatives from were: the UK newspapers Guardian and Financial Times; non-governmental bodies such as Amnesty International, Friends of the Earth, WWF, the National Consumer Council, and Association British Insurers; the trades union, the International Textile, Garment and Leather Workers Federation; the labour rights partnerships, The Ethical Trading Initiative, and Fair Labour Association; and the companies, The Gap Inc., Glaxo Smith Kline, Marks & Spencer, Novozymes, and Starbucks.

We hold in high regard the views of the individuals who agreed to participate in the interview programme. We also recognise, however, the limits to this approach given the relatively small number of interviews undertaken and sectors, and regions involved. This cautions us in the broader interpretation of our findings, at least until their relevance is more robustly tested elsewhere.

At the same time, we have drawn on a wider body of literature concerning the linked matters of assurance and trust (see bibliography). Furthermore, the extensive experience of the research team has provided a strong basis for assessing the broader relevance of our findings, across constituencies, organisations, sectors and geography.

Terminology and Definitionsv

Within this paper:

Assurance is defined broadly in terms of its outcome: "*Enabling the confidence of a party or group of people that the information they have is accurate and complete enough for them to make an informed decision about a certain subject matter".*

An assurance engagement is one method of securing this outcome: this is *"an engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence that intended users can have about the evaluation or measurement of subject matter that is the responsibility of a party, other than the intended users or the practitioner, against criteria (IAASB, 2003)*

Such assurance engagements usually result in a report or statement. In practice a diverse range of terms are used to describe: (independent) auditor's report, auditor's statement, independent assurance report, (independent) assessment statement, independent statement, third party review, external verification, verification statement, independent review. This type of assurance may also be linked to certification of compliance with voluntary standards such as the labour standard SA8000 or the environmental standard of the EU, the Eco-Management and Audit Scheme (EMAS).

The people we interviewed spoke from their own experience about assurance in relation to social and environmental performance. Where relevant, the specific subject matter of their comment is highlighted, but more often we seek to highlight the lessons which emerge from their common experience across this broad field.

3. Who Needs Assurance?

Everyone needs assuring. True, but unhelpful for businesses needing to protect and add value in the most effective way with limited resources. One of the greatest challenges for businesses today is to decide which stakeholders count most, and so need to be reassured to secure their contribution to business performance and success.

High profile corporate scandals beset companies that fail to put in place robust assurance processes to secure the quality of information that their shareholders and regulators are legally entitled to. Such scandals are rare though. In general the combination of market abuse rules, listing rules and financial auditing does protect investors from fraud. But companies can also fail to thrive if they are unable to identify, engage with and assure key stakeholder groups around a broader range of emerging and contested issues. There are a number of companies whose ability to create value has suffered because they failed to effectively understand who their stakeholders were, what they were concerned about, what kinds of assurance they were seeking and how they could impact on the organisation itself.

The organisational competency to be able to understand and predict emerging trends and engage with dynamic communities of interest is crucial to organisational success. On reflection, this should come as no surprise, since this is the same competency required to assess changing market conditions. All that differs is that it is being applied to the underlying, societal factors that impact on market conditions and business performance.

Interviewees were generally in agreement that assurance needs to be guided by the information needs of stakeholders and designed to enable decision making in order to be effective. As one reporting organisation stressed;

> *How will the general public (not just customers but investors, NGOs, trade unions etc) use [the report]? You need to clarify this before you get to a point of formalised reporting because it begs the question of who are you assuring for.*
> ***Retailer***

> *There is a growing chorus of opinion that box ticking may be diagnosing stuff but it's not fixing stuff.*
> ***Labour rights NGO***

Any effective assurance on human rights has to move beyond the very narrow, legal definitions that are in place at the moment.
Human Rights NGO

However, many, particularly from civil society organisations were concerned that this emphasis on stakeholder orientation risked neglecting the need for a basic compliance framework to ensure effective assurance by all companies, not just those that recognise its value.

There is a slightly easy rhetoric of beyond compliance that you hear from anyone who works in any form of assurance. I don't think it means anything.
Consumer NGO

You need to have compliance; there needs to be a basic framework which companies are complying to. We can't move beyond compliance until we actually have it and I don't believe we have it.
Environmental NGO

Despite these differences in emphasis on regulatory requirements versus value creation as drivers of assurance, there was **wide agreement on the need to understand the information and assurance needs of stakeholders.**

People are primary or secondary receivers of information… It is a sophisticated art, knowing what strength of message to give to whom.
Retailer

In order to answer the question about assurance of stakeholders, you need to understand a prior question - what is the information seeking behaviour of stakeholders?
Consumer NGO

What is value creation for one stakeholder will be of no value for others.
Environmental NGO

Respondents recognised the validity of considering the information needs of a wide range of stakeholders. The list of who counts has inexorably grown. Investors, customers, employees, suppliers, government and the (usually local) community are well established as primary stakeholders. Regional and international public bodies, NGOs and the media have now been added.

How and why these stakeholders add value to the business, or indeed damage or destroy it, has become far more complex and volatile. Notable has been the emergence of many stakeholder groups whose potential impact on the business is indirect, mediated through civil society organisations. Workers in global supply chains rarely have any direct power over the purchasing brand, but can have enormous influence through the 'lent power' labour and human rights organisations leveraging reputational impacts through the mass media and, increasingly, e-based networks (AccountAbility, 2005b).

The companies we interviewed were well aware of this range of stakeholders. For example, one discussion centred on the need to understand the differences within, as well as between, stakeholder groups. The New York taxi driver 'day trader' and Warren Buffet's Berkshire Hathaway are both investors. But beyond this headline, they share little in common. The day trader adopts an essentially arbitrage strategy, seeking to gain from very short-term price movements. Berkshire Hathaway, on the other hand, invests in under-managed companies, and seeks to make a long-term gain by building their investees strategies and competencies. Whilst both are investors, they have very different routes to success and so require different information and types of assurance.

Companies were also developing a nuanced understanding of the information needs of their stakeholders and the ways in which their interests and influence could strengthen or damage the company's ability to create value.

It feels that pressure groups want information, but in order to beat us over the head with it. The really noisy external drivers [for assurance] are not doing it because they want to add value to the company but for their own, localised reasons.
Pharmaceutical company

We do not wish to do business with policy holders who are not willing to deal with issues like this [climate change] and we are going to be more selective about whom we'll do business with, with that in mind.
Investment company

In practice, however, those interviewees representing assurance audiences and information users expressed dissatisfaction with the quality of information in corporate non-financial reports.

We have an interest in companies performing to higher standards with regard to the full spectrum of human rights but we are not a user of the information they provide on this.
Human Rights NGO

We are not very interested in sustainability reports because they tend to obscure the issues.
Investment Company

Relatively few organisations fully understand themselves how they think their various organisational working processes create particular kinds of value.
Think Tank

This brings up the issue of who the reports are actually for. As discussed earlier, stakeholders seek assurance from a wide range of sources, which may or may not include a company's sustainability report. The over-reliance on such a report to communicate performance and thereby assure stakeholders, may therefore be misguided.

Key messages

- **Effective assurance is driven by the demands of stakeholders for reliable and material information on which to make decisions**.
- Which stakeholders count in being able to create or destroy economic value changes over time, reflecting the complexity and dynamism of economic value creation.
- Identifying who needs assurance is therefore not straightforward or amenable to a 'checklist' approach. Stakeholder engagement and assurance must be focused and targeted to meet the needs of dynamic stakeholder sub-groups.
- The dynamic organisational competency to understand emerging trends and associated communities of interest is crucial to business success.
- Information users are not confident that current reporting and assurance mechanisms meet their needs.

4. What Data Assures Who?

Labour activists care about labour standards and their application, environmentalists about resource use and pollution, and investors about the financial bottom line and levels of risk. These factors are not always independent, in fact they are becoming less and less so. Some labour activists care about the environment, either in its own right or because the state of the environment impacts in turn on the lives of workers and their families and communities. Similarly, some investors increasingly care about labour standards and the environment. Again, at times this is 'just because they care', and in other cases because they see these factors as significant downside business risks, or their effective handling opening profitable business opportunities. For example, the world's largest life re-insurance company Swiss Re now considers climate change a quantifiable risk and one that should be considered more widely by the investment community (Murray, 2004).

But what data would satisfy a labour activist that a business is fulfilling its code-based obligations, or an environmentalist that a business was doing all it could reasonably do to reduce carbon emissions, or a financial analyst that today's information offers some indication of tomorrow's financial performance?

There was strong agreement across the sectors that reporting and assurance needs to enable forward-looking assessments by stakeholders. For most people interviewed, historic data was mainly used to gain a sense of where the company is going in the future. One NGO summed this up simply,

Some sort of rear view mirror is important to see where they have come from, as this is crucial in terms of knowing where they are going.

A financial journalist put the point more bluntly,

Corporate responsibility should be like any other business planning…if you are only looking at 'now' you are not doing your job.

In considering what kind of data could support forward-looking analysis they emphasised the need to delve into **organisational competencies, strategies and values**. As one investor pointed out,

One is not concerned with a transactional analysis of how an organisation has responded to a particular risk that arose over the past year, but in their capacity to understand, identify and manage risk.

However, not all interviewees were interested in such upstream processes; their concern was outcomes.

Many highlighted the difficulty of integrating forward-looking assessments into traditional conceptions of audit and assurance and the need to allow for different levels of confidence.

> *Yes, the future is what we are interested in, but assuring the future is not possible…all we can hope for is a credible view of what has happened in the past and then it is up to us to judge what this means for the future. The future bit should be audited to a different standard and approach to the things you have to comply with.*
> ***Retailer***

> *'We give them [analysts] earnings guidance, but I'm not sure what other forward looking information we could give them that wouldn't give spurious certainty.'*
> ***Pharmaceutical company***

> *There is a strong tradition in financial reporting to look back on the year that's gone. Therefore the forward-looking aspect of the non-financial area is quite hard to integrate*
> ***Pharmaceutical company***

Discussion amongst the different respondents focused on how different stakeholders are assured on the basis of different parts of the 'data chain' from forward looking but uncertain information to accurate but out-of-date historic data. This data chain spans information about values and strategy through decisions and actions to end-of-pipe impacts, conformity with laws and standards and reputation. The diagram below maps out this data chain.

Figure 3: The Data Chain

Values/ purpose	Strategy	Behaviour/ actions	Impacts	Compliance	Reputation
'What you say'	*'What you plan'*	*'What you did'*	*'How much value you created (or destroyed)'*	*'Whether you meet standards'*	*'How others judge you'*
Statements, commitments	Plans, policies	Narrative description, system documentation	Performance indicators and analysis	Standards certification, conformity assessments	Endorsements Stakeholder perceptions of performance

Forward looking — Backward looking

Although helpful as a framework, it is also clear that such a data chain may mask the challenge faced by companies in meeting the diverse appetite of stakeholders for different data, at different times, and in different forms. But in general, what this means is that traditional audit methods that focus on historic accuracy, rather than predictive value, whilst still important, are not sufficient to deliver assurance to these groups. This problem often does not solely lie with the provider but with the information being presented by the reporter, where there has been little discussion or agreement between the two parties as to the materiality and usefulness of the information being presented (Zadek & Raynard, 2004).

The literature, experience and interviews highlighted a number of key patterns:

Different stakeholders are assured by different types of information, even when they are concerned about the same underlying phenomenon. For example environmental organisations generally focus on the end-of-pipeline 'green' performance in terms of impacts and compliance. As one environmentalist argued,

> *"…what matters most to me is how much the corporate entity cuts their CO2 emissions, not how they go about it or how it impacts on their bottom line".*
> ***Environmental NGO***

Investors are generally more interested in environmental performance as it links to potential litigation, how it reflects on management capacity more generally, and possible implications for the future of the company's underlying business model.

Which part of the data chain diverse stakeholders are assured by is closely linked to their time horizons. Stakeholders with longer term financial interests have greater interest up-stream along the chain, whereas those with shorter term interests remain focused on downstream outcomes and impacts. Non-financial stakeholders in the main are short term in this sense, in that they are interested in the impacts of current products and processes and whether the metrics indicate that performance is heading in broadly the right direction rather than the long-term future impacts of the company.

Those with a financial focus generally have the most interest in upstream data which illuminates how future value will be created. Success in outmanoeuvring the financial markets requires investors to bet on future not past outcomes. Investors are of course also interested in performance, namely profitability. But fund managers' primary focus on share price movements make factors other than observable profitability count. Share prices are clearly impacted by longer term profitability prospects, and also merger and acquisition activity, changes in management and of course changes in market conditions, including activities of state regulators and, in some instances, 'civil regulators' in the shape of NGOs. For all but the shortest-term investors, fund managers are particularly interested in the quality of management, and its ability to understand their complex and often intensely competitive environment. They are interested in proxies that capture the quality of the underlying business model, and the ability of management to steer the business in a profitable manner. As one business manager argued,

> *"…the financial community take an interest in where we are placed in customers' perception, because that's an indication of the sustainability of the business model and its likely performance".*

Similarly, a financial journalist commented,

> *"what you are really looking for is a track record of the performance of what a company has been doing and how it has improved",*

again reflecting an interest in past outcomes as a proxy for future likely performance.

NGOS are not homogeneous in their data demands. The interviews revealed significant differences between the data interests of campaign-focused activists and those more directly engaged with change processes in the business community, for example through multi-sector partnerships. The former tended to be very outcome focused; as one NGO campaigner concluded,

> *"assurance is about outcomes to me. What goes on upstream is interesting but not essential in terms of information that I need to have".*

The latter tended more to highlight the importance of company strategy and, to a greater degree, a sense of company and individual values. One argued,

> *"what we need to understand are the motives behind why the company intends to make a difference and what social value it is intending to add…because values can tell us more about how much progress a company is likely to make than its historic compliance under pressure".*

Of course this is not an either-or, and in some ways there is a perception of companies graduating over time. As one labour union leader said, when asked what led him to trust one company over another in regards of workers' rights and employment conditions,

> *"the commitment to and practice of compliance is the entry condition. If there is not much confidence in what's been done at the factory level there's not much confidence in what has been done further down the chain either. But beyond that, trust is about relationships, my belief that they want to do it right. If that trust is there, then I am less concerned about compliance failures, since these just happen at times in complex global supply chains".*

Furthermore, environmental activists seemed more focused purely on outcomes than labour activists, perhaps because of the relative ease of end-of-pipeline performance measurement as compared to human and labour rights outcomes.

The same stakeholders can shift their data focus. During much of the last decade, labour activists demanded information on whether companies had codes of conduct and associated third party audits carried out by those they considered to be credible assurance providers. But a growing sense of a disconnect between codes, auditing and actual outcomes has shifted the interests of labour activists back to a focus on end-of-pipeline performance data. As one NGO activist explained,

> *"…increasingly what stakeholders want is not a list of inputs but a clear and honest view of what the outputs and impacts have resulted from a company's application of codes and standards".*

Stakeholders' data needs appear to change over time depending on the level of maturity of the issue. At an early stage in the evolution of an issue in the public eye, the focus of stakeholders' interests is forward looking. For example, the public debate around energy companies' impacts on climate change was initially unspecific and forward-looking. When BP and Shell acknowledged the impact of our carbon based economies on climate change, this was sufficient to offer many concerned with the issue some assurance that these companies were seeking to be part of the solution. But as the issue has matured, so have calls increased for clearer progress reports. As another NGO informant commented,

> *"once we have agreed what counts, we want it counted".*

The data issues then become more specific, such as how best to calculate carbon emissions, and for what parts of the value chain particularly companies have emissions-related responsibilities. As the issue matures further, however, stakeholders seemingly become interested once again in forward-looking evidence of a company's commitment and performance such as its public policy stances. For example, one activist said,

> *"we want to know what they are going to do about their business model in the future, or how they will engage with other companies to get movement across the sector".*

Similarly, activists and financial analysts alike are today less interested in how much cut-priced products pharmaceutical companies have made available in developing countries, than in what it means for the future of the pharmaceuticals industry and health care more generally.

Assurance in one area can bolster trust in other areas. A number of people highlighted ways in which trust and credibility linked to information about one issue, or link in the data-chain can have spill over effects, when it is seen as exposing (either in a negative or positive light) the whole set of values in the company.

> *Maybe for biotechnology companies, bribery is not seen as such a hot issue. But if NGOs concerned with genetically modified organisms see that targets are not met then they worry that targets aren't being met in their area.*
> ***Pharmaceutical company***

Key messages

- **There is a demand for assurance to enable forward-looking assessments about the way organisations generate social, economic and environmental impact.**
- Diverse stakeholders are interested in and assured on the basis of different parts of the 'data chain', which spans values, purpose and strategy, decisions and actions and, ultimately, end-of-pipeline performance. Different stakeholders are interested in and assured by information at different points along this chain.
- Traditional audit methods which focus on historic accuracy rather than predictive value are therefore necessary but not sufficient to deliver assurance to some groups.

5. How well are stakeholders assured?

Assurance to stakeholders is provided by a number of sources of information. The information the interviewees mapped out covered four zones: **public assertions**, **received wisdom**, **inside information** and **gossip**. In each case they highlighted a range of different mechanisms which provide assurance.

Figure 4: Mapping sources of information and assurance

		Formal	Informal
Open		**Public assertions**	**Received wisdom**
	Information Streams	• Corporate reports, statements & websites • Advertising • Labels and certification	• Widespread word of mouth (both real and virtual) • Media coverage (including PR driven)
	What Assures?	• Brand and personal reputation • Rigor of formal assurance • Legal control • Formal peer review (e.g. scientific journals)	• Confirmation by multiple sources • Confidence in media outlets or though leaders • Brand reputation and history
Privileged		**Inside information**	**Gossip**
	Information Streams	• Internal reports and other corporate communication	• Restricted word of mouth (both real and virtual) • Direct engagement with stakeholders
	What Assures?	• Capability and clear lines of responsibility • Strength of systems • Rigour of formal assurance	• Confidence in source • Personal reputation • Strength of relationship • 'Seeing is believing'

At different times, but more often simultaneously, these streams of information will provide companies with the necessary framework to assure stakeholders of their performance. It requires a mixture of formal, often statutory reporting with more informal direct engagement with stakeholders.

The interviews consistently confirmed the importance of informal knowledge networks, as a key basis for credible assurance of business performance. One corporate responsibility activist put this bluntly,

> *"The gossip between stakeholders – including NGOs, analysts and so on, does ultimately determine the credibility of an organisation".*

One labour activist offered a reason for this,

> *Public perception of a company is good because of the way they react rather than because of the accuracy of their internal auditing system. We discover this through engagement or by finding out from others that have engaged.*

They were comfortable in defining assurance in terms of an outcome, not a process and discussed a wide range of assurance mechanisms linked to both formal and informal flows of open or privileged information. These assurance devices included the strength of company or brand reputation, the involvement of external thought leaders, the very act of making a public statement or commitment which is subject to scrutiny and possible legal challenge, the rigour of internal sign-off or peer review processes and the ability of third party labels or certificates to back up claims.

> *The way companies communicate bad things is actually what gives people assurance in the future for anything else.*
> ***Pharmaceutical company***

> *You target thought leaders because they give speeches, are quoted, write papers etc.*
> ***Retailer***

> *Investors assume information is right because they know if it's not right it would be a stupid thing to publish.*
> ***Pharmaceutical company***

> *Mostly vulnerability creates integrity more than formal processes.*
> ***Media company***

Valuing gossip is not the preserve of those stakeholders interested in the non-financials. A recent report produced by AccountAbility and the World Economic Forum on the future of Responsible Investment highlighted the importance in the investment community of fund managers betting with or against each other as much as they invest on the basis of objective performance data about the company that can be used for predictive purposes (AccountAbility/WEF, 2005). Responses from the interviews undertaken for this research tended to confirm these views:

> *How many investors actually read the Annual Report let alone the Sustainability Report? It all goes through intermediaries. Fund managers act on the opinion of others.*
> ***Financial company***

> *…we carry out our own very informal processes of assurance by trying to triangulate with people who know particular aspects of companies, we would never rely alone on the views of professional audit providers to base an investment decision.*
> ***Financial company***

Business managers interviewed were clear about the importance of informal information flows in delivering assurance. One manager responsible for interacting with labour activists commented,

> *They need to hear this word of mouth from people they think are credible.*
> ***Retailer***

Another company manager, reflecting on their treatment in the media, commented,

> *…when something goes wrong, the journalists all phone up their mates and find out what they think about so and so.*
> ***Retailer***

By way of confirmation, one journalist remarked,

> *…a company's reputation in the area of corporate responsibility… is gained and increased through word of mouth….That [gossip] is not what we should be relying on if we are talking about formal, effective assurance, which is a different thing.*
> ***Journalist***

Of course **information flows and assurance are not bound in separate silos but can inform, corroborate or undermine each other.** For example formal performance reports can be bolstered by informal assurance:

A lot of people skimming the report looked at names, names of organisations we'd included, who was willing to be quoted, and that gave them a sense of comfort that we had been talking to the right people.
Retailer

Any report that we mention, the assurance part and the credibility part probably does come more than anything from that informal gossip network.
Retailer

While equally, **stakeholders receiving informal information may seek to confirm it through a formally assured means**.

If we were to present a piece of data from our studies, they [investors] would make a value judgement based on that information on the basis that it's true but they'd also like to see it published in a peer-reviewed scientific journal.
Pharmaceutical company

…gossip comes from a lack of knowledge. By its nature it is rarely based on fact – usually it is hearsay.
Media organisation

the quality of transparency of an organisation's formal and standard reporting processes is going to impact quite a lot on the shape of the gossip that emerges.
Think Tank

Therefore, while recognising the value of informal information flows, the information users amongst the interviewees were clear about the need for formal assurance,

…we don't maintain regular dialogue with most companies…In that context if something goes wrong…you are looking for something you fall back on that has got sufficient independence and formality to be effective.
Consumer NGO

High trust dialogue is very important but formal assurance is important too.
Environmental NGO

I think that [professionalised audits] becomes more important when…auditing is supposed to provide consistency across the board for investors of all sizes.
Retailer

Trade unions and NGOs are accountable to their own constituencies, so they can't come back with off the record information to them. They need formal assurance for their own constituents.
Labour NGO

There is, then, considerable demand for formal assurance. **Yet there was a level of scepticism amongst some of the interviewees about the ability of current formal assurance processes to offer effective assurance.** One labour leader concluded, with regards to ethical supply chain auditing,

"I have less and less confidence in what you might call professional auditors…The problem at the moment is that external auditing is expensive and is of generally very poor quality… the real problem is a lack of skills on the part of those auditing…Some of the more specialised [auditing organisations], who are concentrating on social auditing and sometimes concentrating on specific sectors…do appear to provide a better service at the moment".

This is a view shared by many in the NGO sector, particularly those campaigning for labour rights in supply chains. There have recently been a spate of reports criticising the quality of such auditing practices. For example, the Clean Clothes Campaign concluded that: "Social audits are failing to deliver as a tool for assessing code compliance, particularly in determining violations of freedom of association, excessive and forced overtime, abusive treatment and discrimination of workers." (Clean Clothes Campaign, 2005).

While others were less vehement, interviewees from both external audience and internal management viewpoints highlighted concerns.

Assurance providers need to ensure credibility with stakeholders. Many recognised that while formal assurance by accountancy and certification bodies has a strong history of professionalism and rigour, it does not have credibility amongst many of the key stakeholders that companies are seeking to assure.

They [big assurance providers] have not established credibility within the stakeholder sectors we are engaged with.
Media Organisation

Mainstream investors would be more impressed by a sustainability report that had been verified by a big firm because they know these. An environmental NGO might be impressed by, for example, a good green consultancy.
Retailer

The KPMG international survey of corporate sustainability reporting summed up this problem, when saying that, "it seems that further thought is needed to develop focused and rigorous assurance processes that are useful and meaningful for both reporters and report users" (KPMG, 2005).

Need to demonstrate firm basis of integrity. Many of the NGO interviewees traced the credibility gap to the dynamics of the relationship between assurance providers and their clients, as one activist bluntly put it,

I simply cannot trust someone who is being paid by the organisation that they are meant to audit.

A leading environmental campaigner saw the problem similarly,

The problem with environmental statements provided by 3rd party assurors is that they do have a vested interest…Where you have questions of judgement being exercised, I would be extremely cautious about taking the word of anyone who had been paid to make a judgment.
Environmental NGO

Interviewees agreed that independence in traditional terms is almost impossible, given the complexity and intertwined nature of today's network relationships. But many saw the credibility of the assurance provider resting more on the perceived integrity of the organisation, in the face of its often intimate relationship with both the organisation and its stakeholders.

Integrity is very important but integrity to one organisation or group of stakeholders may be perceived very differently by another group.
Media organisation

Need for formal accountability and recognised standards. Many did not see the problem as inherently one of assurors being paid by clients, but of a lack of clear and rigorous standards to govern this relationship and set out the duty of care to stakeholders. As one member of the investment community pointed out,

If the standards the assurance provider works to are not embodied by law…then the assurance provider is going to be reluctant to upset its client…Our view is that a duty of care to shareholders is actually a useful device. It presumes shareholders will be aware of and take a candid interest in other stakeholders because we work on the basis if the company doesn't…there is a risk of loss of value.

For others, extending this responsibility directly to other stakeholders seemed consistent with any report that claimed legitimacy by listing other stakeholders as intended audiences (i.e. having legitimate interests). One corporate governance activist concluded,

[Local communities] would say that the assurance provider works for the company, so for them to be committed to factoring in the community's interests, there needs to be some kind of formal contract between the community and the assurance provider.

One of the business managers similarly concluded that

The ideal situation would be to establish a contract between the assurance providers and our stakeholders.

However, interviewees recognised the problems as well as the potential in pursuing this route,

The idea of requiring a contract is right, but a contract generates its own compliance issues…It's difficult for me to imagine how you would create a wider range of reporting standards and benchmarks that were able to be supple enough to capture the full range of interaction and communication between a set of multiple stakeholders.
Think Tank

But none of this assumes that efforts are underway to develop a set of recognised 'sustainability' standards in guiding assurance processes. As the box below demonstrates, there are burgeoning standards in this area on offer mainly to reporters but also increasingly to assurance providers.

Sustainability 'Standards'

A wide range of standards can be used to inform sustainability assurance processes, these include:

Normative frameworks **and laws** which provide a basis of responsibilities, expectations and principles of sustainability i.e. 'subject matter' against which to assess performance. Examples of these include The Natural Step, Responsible Care, the OECD Guidelines for Multinationals and The UN Global Compact Principles.

Management standards provide more detailed and practical guidance concerning how to manage performance in relation to these issues and responsibilities. Examples include EMAS, the SIGMA guidelines, ISO14000/9000, IFOAM Organic Standards and Amnesty International's Human Rights Guidelines for Companies.

Process and reporting standards provide 'suitable criteria' for reporting and assurance. These standards do not set normative goals but a framework for reporting and assurance of substantive issues and standards. The main relevant standard for sustainability reporting is the Global Reporting Initiative Guidelines. Relevant standards and guidelines for assurance in this area include the AA1000 Assurance Standard, Standards Australia, IAASB's ISAE3000, FEE's Guidelines, as well as the Swedish institute FAR's guidelines.

There is though a need for some sort of generally accepted assurance standards for sustainability, similar to GAAPs, which govern professional audit services, but go wider to incorporate all processes that assure stakeholders (Zadek & Raynard, 2004).

Need to understand, develop and demonstrate the value added by assurance. There is no clear agreement nor understanding about the value that auditing and formal assurance adds. This perception was particularly strong amongst investors, largely in relation to traditional financial assurance:

> *Audit is seen as a non-value adding service that enables the big firms to sell their consultancy services.*
> ***Retailer***

> *How far is auditing a loss leader to consultancy services? I believe that…it is under-valued, under priced and under delivered, my guess is that audit prices must be higher if quality is really to be delivered.*
> ***Investment company***

And as Professor Porter shows, "[i]n the end auditing in general, and the auditing of performance in particular, may have dysfunctional side effects and there is a need for a greater empirical understanding of the consequences of audit. In short, auditing needs to be evaluated (Porter, 1997).

Many of the interviewees discussing newer forms of formal assurance, around environmental and labour standards and sustainability reporting were more convinced of the value of assurance in terms of adding credibility to corporate claims.

> *If you choose somebody with a reputation you are buying their reputation.*
> ***Media organisation***

> *When you say ISO certificated then people know there's a certain level of performance.*
> ***Pharmaceutical company***

However, others were less certain that assurance acts as a simple 'stamp of approval'.

> *Some overall assurance would contribute to the overall credibility of the report but would be subsidiary to…the overall credibility of the company and their responsiveness in dealing with issues.*
> ***Labour NGO***

> *Assurance brand is not the value to the business. The value of auditing is the transfer of knowledge or skills or process within the business. Readers have benefited because of the process improvement, but the stamp that's given does not convey that assurance.*
> ***Retailer***

Formal assurance needs to link in better to informal information flows and networks. Interviewees agreed that assurance as an outcome often has as much to do with the engagement of the organisation wishing to assure as with formal assurance processes. Investors framed this in terms of the ability and willingness of the senior management team to engage with analysts and fund managers. Labour and environmental activists judged companies not just on the quality of their audits but also on the company's willingness to discuss and solve problems with others.

They discussed the need to integrate formal assurance with such trust-based dialogue to provide rigour to the still informal space where gossip matters. They agreed that formal assurance has to draw from and influence this conversation to be effective and began to map out some of the elements of such an approach.

> *Those assurance approaches that try and look at what a company should be doing – how it should be going about it – by involving workers, NGOs, Trade Unions and other opinion formers in the discussion around it, are bound to be more effective.*
> ***Labour NGO***

> *It is an interesting question how to bridge the gap between companies and NGOs. The assuror is one way of bridging this gap.*
> ***Media organisation***

However, they were clear that there is not yet an effective and generally accepted set of tools and approaches in this area. As commentators from NGOs and investors pointed out:

> *[Companies and assurance providers] think that if they can get a few stake-holders into a room that's a substitute for objective methodologies.*
> ***Human Rights NGO***

> *You don't solve the problems of auditing these non-financial areas just by inviting stakeholders to comment.*
> ***Investment Company***

Most recently, AccountAbility launched the first Stakeholder Engagement standard, which aims to formalise and improve the quality of engagement by organisations with their stakeholders (AccountAbilty, 2005c).

Need to move beyond assuring accuracy to assuring materiality. Interviewees agreed that unitary approaches to determining what is material tend to exclude all but relatively short-term financial impacts. They stressed that this is not only a matter of distinguishing financial and non-financial materiality, but also of considering the way that a company's ability to address social and environmental risks and opportunities can impact on the bottom line in the longer term. A materiality approach aligned to longer-term financial and non-financial value creation will require assurance providers to establish what is material to whom, why and to what effect. As one financial journalist remarked, *"it seems obvious that assurance providers must establish what is material to whom, why and at what point it will be."*

> *Formal assurance needs to be grounded in the expectations of the wide number of stakeholders that companies have.*
> ***Labour NGO***

> *Something that everyone is struggling with is when you get to materiality – material to whom?*
> ***Retailer***

> *Assurance not only needs to test the technical competence of reports but also whether they serve the needs of the stakeholders they are intending to reach.*
> ***Investment company***

Reporting companies stressed that assessing materiality and determining the scope of reporting should be the primary responsibility of the company itself.

> *We have to make a judgment of where to balance between what we're asked to do and what's practical and sensible and delivers information not just data. It is important for the company to make their own decisions on materiality but an important role of the provider is to challenge that.*
> ***Pharmaceutical company***

> *We don't look to our providers to [define scope], that's something we own.*
> ***Retailer***

As one investor pointed out, the role of assurance in this context is one of checking and challenging the company's own assessment.

> *It is more the question about using an assurance process which is actually helping to reveal blind spots and challenge boundaries.*
> ***Investment Company***

Finally, interviewees were clear that assurance is not a panacea. They agreed that assurance could be most effective when its role was clear and limited to providing confidence in information and where it was not subject to huge expectations gaps between political questions and technical solutions (Adams & Evans, 2004).

I don't think that you can expect assurance to tell you whether a conclusion is right. I'm not sure how far it can tell you whether the quality of the process is high because it is too subjective, but you can get it to tell you whether the process was followed.
Investment Company

It's one thing to verify that the numbers are what they are. It's another thing within the social context to verify the impact and the ability for the program to move forward.
Retailer

If a company does not want to move forward then it [assurance] makes no difference.
Media Organisation

It is quite important the assurance company doesn't interpret information but ensures we give the full picture, then it is up to stakeholders to interpret it.
Pharmaceutical company

Key messages

Effective assurance requires the bridging of informal 'gossip' knowledge networking and formalised assurance, for non-financial stakeholders, but also for investors.

Key concerns about the current provision of formal assurance processes include:

- Need to ensure credibility with stakeholders.
- Need to demonstrate basis of independence and integrity.
- Need for formal accountability and recognised standards.
- Need to understand and demonstrate value added by assurance.
- Needs to link in better to informal information flows and networks
- Need to move beyond assuring accuracy to assuring materiality.

Assurance is not a panacea. It can provide confidence in information, but it cannot provide a technical solution to **questions** which are essentially political.

6. What will assure stakeholders in the 21st Century?

During the course of this research we spoke to over forty people involved in the evolving domain of assurance – either as reporters of information and commissioners of assurance or as consumers of information and an audience for assurance. We asked for their opinions in order to ‘test’ a number of propositions about the current state of assurance. Their insights and opinions, as well as the wider body of literature on assurance and trust provide a basis on which we can make a set of assertions about the future of assurance.

These are not disinterested and testable hypotheses about what will happen but highlight opportunities and risks for companies, civil society organisations and the assurance profession.

Assuring stakeholders in the 21st century is going to be an increasingly difficult feat. Key factors driving both the need and the challenge include stakeholders’ diversity and fluidity, access to information and vulnerability to influence, interconnectivity as communities of interest, and the troubling blend of fear and cynicism that pervades public and private debate. As if this was not enough, the real facts underlying stakeholders’ complex and confusing expectations and perceptions are equally daunting, from job insecurity, health care costs and pension deficits through to terrorism and environmental insecurity. From this viewpoint, it is in some ways amazing that anyone believes anything!

What is certain is that there is no one route to assuring stakeholders, and that all routes will be subject to the enormous pressure of distrust generated at a system rather than a specific level. For example, whilst one company may be doing all the right things in building the trust of their key stakeholders, its efforts might be seriously undermined by the activities of another business over which they have no control whatsoever. This linkage might be because of direct connections, related ownership or activities. But often the connection is indirect, formed in the minds of stakeholders rather than on the ground. The reputational impacts of ‘fat cat’ pay, financial misdemeanours, or asset stripping and their ‘redeployment’ are increasingly crossing companies, sectors and geographic boundaries. And of course this relative aspect of assurance can have zero-sum type effects. If politicians are discredited, the reputations of business leaders might rise. If the moral high-ground of civil society organisations comes under scrutiny, their ability to cast a shadow on the activities of politicians and business leaders alike is diminished.

Effective routes to assuring stakeholders have to be protected from systemic factors over which it has little or no control. Robust methodologies underlying professional assurance will count for little if misdemeanours by members of the profession are counted to be illustrations of the whole. For example, claims to independence will be challenged if a competitor's lack of client independence makes the front page. Similarly, an assurance provider has to be clear about what it can and cannot do. If it is not possible (technically, legally or otherwise) to comment on whether the most material information is included in a report, then it is vital that this fact be articulated by the assurance provider themselves, rather than leaving it to others to point out what might seem to some disguised inadequacies.

Effective assurance in the future is just as likely to be based on values and commitments than on the principle of independence. The reason is not of course a problem with the principle, but its application, in practice. Large assurance providers, for example, are seen by some stakeholders as not being independent because they are 'like' their clients, not because they are literally dependent on them. Stakeholders concerned with non-financial issues are more likely to trust assurance providers that share concerns and even values with them, and heavily discount technical arguments for having trust. Large assurance providers have successfully launched corporate responsibility services, however, the share of the market taken by other providers has increased slightly since 2002 (KPMG, 2005). Small assurance providers can often be cheaper and work with fewer constraints over the execution, quality and mode of work done. Despite their possible technical limitations, and despite the fact that their financial dependency on a small number of clients makes them quantitatively far more client dependent than any of the larger providers, they may be seen as more trustworthy by stakeholders. If the assurance offered by the larger providers is going to be effective and trustworthy in the eyes of a wide group of stakeholders they will need to demonstrably embed a set of values and commitments in their practice conducive to the social and environmental concerns in question.

Effective assurance in the future is likely to be based on a 'joined-up' approach rather than a module assembly of different elements. Today's practice, for example, involves companies engaging with stakeholders, and then auditors being brought in through a separate door to check the data. Tomorrow's practice will involve the assurance providers in such engagements with stakeholders, opening them to having to handle 'live data' (what people say and do), but also requiring them to build trust directly with a company's stakeholders through demonstration of knowledge, sensitivity and individual integrity.

We believe that securing effective and credible assurance for the 21st century in light of these challenges requires that formal assurance provision be overseen by a body independent of the profession; one that is governed through a multi-stakeholder structure and process, and draws on the experience of existing oversight bodies, such as the Public Company Accounting Oversight Board (PCAOB).

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Endnotes

1 Quoted in World Economic Forum Press Release, 'Public Trust is Recovering': 31 March 2004.

2 See PricewaterhouseCoopers Viewpoint 01: Corporate Reporting – time for a new system? http://www.pwcviewpoint.co.uk/CurrentEditionTime.html and DiPiazza, S.A and Eccles, RG (2002) Building Public Trust: The Future of Corporate Reporting, PricewaterhouseCoopers/ John Wiley & Sons.

3 Thomas, A (2002) *Outdated accounts,* in EBF issue 19 http://www.ebfonline.com/main_feat/trends/trends.asp?id=510

4 PricewaterhouseCoopers Viewpoint 01: Corporate Reporting – time for a new system? http://www.pwcviewpoint.co.uk/CurrentEditionTime.html

5 This is drawn from a longer discussion of the variety of terminology used in sustainability assurance, which can be found in AccountAbility (2003) The State of Sustainability Assurance. AccountAbility/ACCA, London.

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