





# Comments of the AFAANZ Auditing and Assurance Standards Committee on the Proposed Standard on Assurance Engagements over GHG Emissions Disclosure

David Hay<sup>1</sup>  | Noel Harding<sup>2</sup>  | Chris Gan<sup>3</sup> | Irene Ge<sup>2</sup> |  
Linh Ho<sup>3</sup>  | Dinithi Ranasinghe<sup>4</sup>  | Harj Singh<sup>5</sup> | Nigar Sultana<sup>5</sup> |  
Shan Zhou<sup>6</sup>

<sup>1</sup>University of Auckland, Auckland, New Zealand

<sup>2</sup>UNSW Sydney, Sydney, New South Wales, Australia

<sup>3</sup>Lincoln University, Christchurch, New Zealand

<sup>4</sup>University of Otago, Dunedin, Otago Region, New Zealand

<sup>5</sup>Curtin University, Perth, Western Australia, Australia

<sup>6</sup>University of Sydney, Sydney, New South Wales, Australia

## Correspondence

David Hay, University of Auckland,  
Auckland 1142, New Zealand.  
Email: [d.hay@auckland.ac.nz](mailto:d.hay@auckland.ac.nz)

## Abstract

The New Zealand External Reporting Board (XRB) issued for public comment a standard on Assurance Engagements over GHG Emissions Disclosure. The Auditing and Assurance Standards Committee of AFAANZ prepared a submission, based on the findings reported in published research, responding to a number of the questions asked by the XRB. This technical note presents the formal submission made to the XRB.

## KEYWORDS

audit, evidence informed standard setting, greenhouse gas emissions, sustainability

## JEL CLASSIFICATION

M42, M48, Q01

## 1 | INTRODUCED

This article reports the comments of the AFAANZ Auditing and Assurance Standards Committee on the New Zealand External Reporting Board's Proposed Standard on Assurance Engagements over GHG Emissions Disclosure.

We attach our submission in response to the questions in the Consultation Document. We are pleased to have the opportunity to comment on this innovative standard about such an

This is an open access article under the terms of the [Creative Commons Attribution-NonCommercial-NoDerivs](https://creativecommons.org/licenses/by-nc-nd/4.0/) License, which permits use and distribution in any medium, provided the original work is properly cited, the use is non-commercial and no modifications or adaptations are made.

© 2023 The Authors. *Accounting & Finance* published by John Wiley & Sons Australia, Ltd on behalf of Accounting and Finance Association of Australia and New Zealand.

important topical issue. We have concentrated in our submission on issues where there is published research that contributes to deciding on the appropriate requirements for this standard.

## **2 | QUESTION 1: DO YOU HAVE ANY COMMENTS ON THE DESIGN PRINCIPLES OR KEY DECISIONS?**

We have the following comments, namely that:

1. The proposals allow the use of two alternative standards and this could cause confusion among users.
2. One of the standards, ISO 14064-3 is not freely available to users.
3. We are concerned with a potential lack of consistency and harmonisation that will accompany the approval of both ISAE(NZ) 3410 and ISO 14064-3. Although assurance practices will share many similarities, they are likely to be different and this may detract from public trust and confidence in GHG. Several research studies investigating the adoption of International Standards of Auditing suggest that harmonised audit practices and uniformity in those practices enhances public confidence and trust. Krasodomska et al. (2021) and Venter and van Eck (2021) note the importance of harmonised assurance practices over Extended External Reporting in facilitating trust and confidence. Recent research by Harding et al. (2023) finds variations in perceptions of audit quality when different standards are referred to in the Auditor's Report. We are concerned that allowing two similar, but different, standards to be used will detract from consistency and comparability and undermine trust and confidence.
4. There is evidence that non-accounting assurance providers are increasingly making use of ISAE 3410 (Ge et al., 2022).

We recommend that consideration should be given to develop a single self-contained standard using the best of the two current statements. If this is not feasible, then the differences between the types of assurance providers should not be conspicuous, and the same assurance report should be used by both.

## **3 | QUESTION 2: ARE YOU AWARE OF ANY OTHER ASSURANCE STANDARDS THAT ARE CURRENTLY BEING USED IN NEW ZEALAND TO UNDERTAKE GHG EMISSIONS ASSURANCE ENGAGEMENTS?**

A recent study by Hsiao et al. (2022) shows that, out of a small number of sustainability assurance engagements in New Zealand, the assurance standards being used were either ISAE 3410 or ISO 14064-3. There is research showing that another standard (AA1000AS) has been used (Farooq & de Villiers, 2019), but that standard applies specifically to stand-alone sustainability reports and would not be appropriate for these disclosures.

We are therefore not aware of other assurance standards.

## **4 | QUESTION 3: DO YOU CONSIDER THE PROPOSED ETHICAL REQUIREMENTS ARE APPROPRIATE? IF YOU DISAGREE, PLEASE EXPLAIN WHY**

The committee members had considerable concern about the issue of ethical requirements.

1. Paragraphs 6 (b)–(d) of the proposed standard which set out that professional and ethical standards are ‘deactivated’ seem likely to raise concern among users and to reduce trust and public confidence in assurance providers.
2. There is a risk that different standards will be applied by different groups of practitioners. Assurance providers who are part of a firm that is subject to PES 1 and PES 3 for other engagements are likely to continue to comply with these standards under their firm policies for their greenhouse gas emission engagements, while other assurance providers will not. This will result in inconsistency, and reduced standards for one group.
3. Non-accounting practitioners are less well informed about independence. Research by Ge et al. (2022) showed that while 93% of accountant assurance providers acknowledged their compliance with the IESBA Code of Ethics, the non-accountant assurance providers either do not acknowledge their independence, or add a sentence describing their independence in a variety of ways that are not comparable with other reports.
4. The proposed standard requires assurance providers to ‘address familiarity threats’ without being specific. We suggest that more detail is needed so that practitioners know how to address these threats. We recommend a more detailed requirement such as: ‘address familiarity threats by providing appropriate safeguards such as rotation of the lead assurance provider after seven years’.
5. The issue of whether the greenhouse gas emissions assurance provider may also conduct the audit of the entity’s financial report is a threat to independence that should be addressed. This issue is not directly addressed in the proposed standard, and some entities could be in doubt about whether their financial report auditor may also audit greenhouse gas emission disclosures. There is research showing that companies are less likely to appoint their financial statement auditor as assurance provider for other services such as this when their market is sensitive to provision of other services (Lu et al., 2022). In addition, research shows that joint provision of audit and sustainability assurance services by the same practitioner leads to beneficial knowledge spillovers, which also enhance the quality of the sustainability assurance (Ruiz-Barbadillo & Martínez-Ferrero, 2020).

Because of issues (1), (2) and (3), we recommend that PES 1 (the Code of Ethics) should apply to greenhouse gas engagements.

We recommend that the standard should state clearly whether conducting the audit of the financial report and also providing assurance over GHG emissions is a threat to independence.

## **5 | QUESTION 4: DO YOU CONSIDER THE PROPOSED QUALITY MANAGEMENT REQUIREMENTS ARE APPROPRIATE? IF YOU DISAGREE, PLEASE EXPLAIN WHY**

The subcommittee is concerned that the proposed quality management standards will lead to inconsistency of quality management among the different types of provider. There is evidence that disclosure of quality management by practitioners from outside the accounting profession is weak, even when they are required to disclose such a framework in their assurance report when they are using ISAE 3000/3410. This potentially raises the question as to whether they do not have sufficient quality control management in place or they simply do not follow the requirement in the assurance standard (Ge et al., 2022).

Paragraphs 42–46 of the proposed standard do not provide specific guidance on the overall quality management system applied at the practitioner firm level, which is crucial for ensuring practitioners comply with relevant ethical principles.

Because of these issues, we recommend that PES 3 (the standard on quality management) should apply to greenhouse gas engagements.

## **6 | QUESTION 5: DO YOU CONSIDER THE PROPOSED REQUIREMENTS IN RELATION TO THE ASSURANCE PRACTITIONER'S REPORT ARE APPROPRIATE? IF YOU DISAGREE, PLEASE EXPLAIN WHY**

We suggest that the statement of the client's responsibilities in the assurance report should include the responsibilities of directors (or those charged with governance) and the responsibilities of management.

We recommend requiring disclosure of materiality. There is research evidence that investors find disclosure of the reliability of information useful when the auditor's materiality threshold is disclosed but not useful when it is not disclosed (Eilifsen et al., 2021).

We have also made some comments about assurance reports under questions 6 and 7.

## **7 | QUESTION 6: DO YOU HAVE ANY CONCERNS REGARDING THE DIFFERENT TERMINOLOGY THAT MAY BE USED TO EXPRESS THE ASSURANCE CONCLUSION OR OPINION? IF SO, DO YOU HAVE ANY SUGGESTIONS TO ADDRESS THESE CONCERNS?**

We have concerns regarding the different terminology that may be used to express the assurance conclusion or opinion. ISO 14064.3 reports might use terms like 'validation', 'verification', 'verified at the limited level of assurance'. These terms are not used in ISA 3410 reports. Different terminology will lead to different actions on the part of assurance practitioners and different interpretations by users. There is evidence in a different context, the choice of audit procedures, that different verbs used in auditing standards, such as assure, verify and validate make a difference to their understanding by readers (Stepankova et al., 2022). Harding et al. (2023) also find that users perceive different meanings from an auditor's report when different, but equivalent, standards are referred to in the report. Moreover, different verbs (e.g., validate, verify, assure) are associated with different levels of thinking (Stepankova et al., 2022) meaning that variation in terminology may lead to real and not just perceived differences in the level of assurance provided.

Research highlights that users do not understand different levels of assurance as it relates to audits. To the extent that the additional terms of verification (limited or reasonable assurance) and validation (limited assurance) are introduced in the GHG setting, this is likely to detract from the public interest by frustrating a consistent interpretation of assurance opinions.

We recommend that the XRB remove the possibility of variation in the terminology employed in the prescribed format of the assurer's conclusion or opinion.

## **8 | QUESTION 7: DO YOU SUPPORT THE PROPOSED INCLUSION OF KEY MATTER, EMPHASIS OF MATTER, INHERENT UNCERTAINTY AND OTHER MATTER PARAGRAPHS WHERE APPROPRIATE?**

We support including these headings in the assurance report. However, non-accountant assurance providers are likely to be unfamiliar with these terms and we suggest that more

explanatory material should be included in the standard. We agree that including Key Matters is likely to be useful, but we suggest removing the second part of section 31 that refers to enhancing the communicative value of the assurance report, because research evidence does not support that it does (see below – it has beneficial effects in other ways). We also suggest that more explanation is needed about how to identify Key Matters, and of when Emphasis of Matter, Inherent Uncertainty and Other Matter paragraphs should be used.

Research studies using large sample archival data find only limited capital market response to key audit matters (KAMs) in financial statement audit reports (Lennox et al., 2023), but research studies using experiments generally conclude that these additional paragraphs have informational value to users in the context of financial statement audit reports (Moroney et al., 2021). As GHG-related disclosure is inherently more diverse, less standardised and developed and subject to a higher level of uncertainty compared to financial information, the additional information contained by including Key Matters in the auditors' report is expected to play a more significant role in adding to the transparency of these disclosures.

Research investigating the merit of reporting KAMs generally reveals that such reporting leads to little if any improvement in user understanding of the audit function (Sirois et al., 2018), but has been shown to lead to higher perceived value in the audit for audits performed by non-big 4 auditors (Moroney et al., 2021) and is associated with improved financial reporting quality. These findings are broadly consistent with the research that has been undertaken in a New Zealand setting (Almulla & Bradbury, 2022; Li et al., 2019). Section 31 of the Exposure Draft requires that a Key Matters section shall be included in the assurance report when such reporting will improve user understanding of the assurance function. The research suggests that this requirement is unlikely to meet that objective. However, including Key Matters may be beneficial in enhancing perceived confidence in work done by assurance practitioners coming from broader backgrounds as well as encouraging better reporting. With this in mind, the XRB may wish to reconsider the requirement regarding Key Matters to remove reference to improving users' understanding and communicative value of the assurance report.

It is not clear how Key Matters will be identified by the assurance provider. In the case of KAMs in the audit of a financial report, there is a clear mechanism by which KAMs emerge, namely matters discussed with the audit committee.

We recommend that providing guidance on how to identify Key Matters will help to make them more consistent and more useful.

## **9 | QUESTION 8: ARE THERE ANY OTHER REQUIREMENTS THAT YOU CONSIDER SHOULD BE INCLUDED IN RELATION TO THE ASSURANCE PRACTITIONER'S REPORT? IF SO, PLEASE SPECIFY**

We do not have any comments regarding question 8.

## **10 | QUESTION 9: DO YOU CONSIDER THE REQUIREMENTS IN RELATION TO THE ASSURANCE PRACTITIONERS' COMPETENCE ARE APPROPRIATE? IF NOT, WHAT DO YOU CONSIDER SHOULD BE INCLUDED IN RELATION TO THIS?**

We do not have any comments regarding question 9.

## **11 | QUESTION 10: DO YOU CONSIDER THE REQUIREMENTS IN RELATION TO RELIANCE ON THE WORK OF OTHERS IS APPROPRIATE? IF NOT, WHAT DO YOU CONSIDER SHOULD BE INCLUDED IN RELATION TO THIS?**

The proposed standard could benefit from more explicit guidance on the use of experts and their independence.

Research suggests that auditors, when assessing the competence of others, are likely to anchor on their own knowledge in the area in question and inflate their perception of the expert's competence. In a GHG setting, Kim et al. (2016) report that auditors may place excessive reliance on the views/conclusions of those with GHG expertise. These findings are consistent with research showing that auditors are sensitive to source credibility (Bamber, 1983; Hirst, 1994) and a general overconfidence bias among auditors (Hardies et al., 2011; Koch & Wüstemann, 2011). We recommend cautioning assurance practitioners on the risk of over-reliance on experts' work.

There is also a risk regarding the independence of experts. To illustrate, Boritz et al. (2020) find that auditors and their experts may not have consistent views on, and levels of, objectivity and professional scepticism. Moreover, auditors were found to trust their experts and relied heavily on their firm's quality control systems to ensure the competence and independence of their specialists. Given that PES 1 and PES 3 will be 'deactivated', the identified reliance on firm quality controls will not be appropriate in the conduct of GHG assurance. The current requirements in paragraphs 20 and 21, as well as application material in paragraph A25 may not be sufficient.

We recommend that the XRB reconsider the deactivation of PES 3 (or to introduce relevant provisions of PES 3 into the proposed standard).

## **12 | QUESTION 11: DO YOU HAVE ANY OTHER COMMENTS ON THE PROPOSED STANDARD? IF SO, PLEASE SPECIFY**

We were concerned about potential contagion effects. If some low-quality assurance services follow the introduction of these proposals, then this might also damage the reputation of other assurance services including auditing.

The research that has been undertaken highlights that there are unique quality-threatening dimensions of multidisciplinary teams that we would encourage the XRB to address in the proposed standard. There is evidence that use of multidisciplinary teams of accountants and non-accountants on sustainability assurance engagements improves the quality of assurance tasks (Farooq & de Villiers, 2019). However, Ekasingh et al. (2019) note that, while multidisciplinary teams bring expertise across different disciplines, differences in mindset, different frames of reference and communication/coordination difficulties may impede the team's effectiveness. They find that effective communication on task-relevant information and perspectives (i.e., effective elaboration) is necessary to realise the benefits of the diversity in knowledge and experience. Kim et al. (2016) find that multidisciplinary GHG assurance teams may not optimally weight the views of team members with different expertise and that this bias may be exacerbated or attenuated depending on the specific expertise of the reviewer.

We recommend that auditors are cautioned that there are risks when using multidisciplinary assurance teams.

## ACKNOWLEDGEMENTS

We appreciate the support of Paul Coram. Open access publishing facilitated by The University of Auckland, as part of the Wiley - The University of Auckland agreement via the Council of Australian University Librarians.

## DATA AVAILABILITY STATEMENT

Data sharing is not applicable to this article as no new data were created or analyzed in this study.

## ORCID

David Hay  <https://orcid.org/0000-0002-6056-6394>

Noel Harding  <https://orcid.org/0000-0003-4647-4335>

Linh Ho  <https://orcid.org/0000-0003-1847-8136>

Dinithi Ranasinghe  <https://orcid.org/0000-0002-2102-9481>

## REFERENCES

- Almulla, M. & Bradbury, M.E. (2022) Auditor, client and investor consequences of the enhanced auditor's report. *International Journal of Auditing*, 26(2), 134–150.
- Bamber, E.M. (1983) Expert judgment in the audit team: a source reliability approach. *Journal of Accounting Research*, 21(2), 396–413.
- Boritz, J.E., Kochetova, N.V., Robinson, L.A. & Wong, C. (2020) Auditors' and specialists' views about the use of specialists during an audit. *Behavioral Research in Accounting*, 32(2), 15–40.
- Eilifsen, A., Hamilton, E.L. & Messier, W.F. (2021) The importance of quantifying uncertainty: examining the effects of quantitative sensitivity analysis and audit materiality disclosures on investors' judgments and decisions. *Accounting, Organizations and Society*, 90, 101169.
- Ekasingh, E., Simnett, R. & Green, W.J. (2019) The effect of diversity and the mediating role of elaboration on multidisciplinary greenhouse gas assurance team effectiveness. *Behavioral Research in Accounting*, 31(1), 81–96.
- Farooq, M.B. & de Villiers, C. (2019) The shaping of sustainability assurance through the competition between accounting and non-accounting providers. *Accounting, Auditing and Accountability Journal*, 32(1), 307–336.
- Ge, Q., Simnett, R. & Zhou, S. (2022) *Evaluating the use of International Standards for Assurance Engagements by non-accounting practitioners*. Available from: <https://doi.org/10.2139/ssrn.2837397>
- Hardies, K., Breesch, D. & Branson, J. (2011) Male and female auditors' overconfidence. *Managerial Auditing Journal*, 27(1), 105–118.
- Harding, N., Khan, J. & Stepankova, S. (2023) *Applying independence requirements for public interest entities: how should increased transparency be operationalised?* Sydney, NSW: UNSW Sydney.
- Hirst, D.E. (1994) Auditors' sensitivity to source reliability. *Journal of Accounting Research*, 32(1), 113–126.
- Hsiao, P.C.K., Scott, T. & Zang, Z. (2022) A snapshot of sustainability assurance market in New Zealand. *Pacific Accounting Review*, 34(5), 669–686.
- Kim, S., Green, W.J. & Johnstone, K.M. (2016) Biased evidence processing by multidisciplinary greenhouse gas assurance teams. *Auditing*, 35(3), 119–139.
- Koch, C. W., and J. Wüstemann. 2011. A review of bias research in auditing: opportunities for integrating experimental psychology and experimental economics. Available from: <https://doi.org/10.2139/ssrn.1032961>
- Krasodomska, J., Simnett, R. & Street, D.L. (2021) Extended external reporting assurance: current practices and challenges. *Journal of International Financial Management and Accounting*, 32(1), 104–142.
- Lennox, C.S., Schmidt, J.J. & Thompson, A.M. (2023) Why are expanded audit reports not informative to investors? Evidence from the United Kingdom. *Review of Accounting Studies*, 28(2), 497–532.
- Li, H., Hay, D. & Lau, D. (2019) Assessing the impact of the new auditor's report. *Pacific Accounting Review*, 31(1), 110–132.
- Lu, M., Simnett, R. & Zhou, S. (2022) Using the same provider for financial statement audit and assurance of extended external reports: choices and consequences. *Auditing: A Journal of Practice & Theory*, 42(1), 125–154.
- Moroney, R., Phang, S.Y. & Xiao, X. (2021) When do investors value key audit matters? *European Accounting Review*, 30(1), 63–82.
- Ruiz-Barbadillo, E. & Martínez-Ferrero, J. (2020) Empirical analysis of the effect of the joint provision of audit and sustainability assurance services on assurance quality. *Journal of Cleaner Production*, 266, 121943.
- Sirois, L.P., Bédard, J. & Bera, P. (2018) The informational value of key audit matters in the auditor's report: evidence from an eye-tracking study. *Accounting Horizons*, 32(2), 141–162.

- Stepankova, S., Harding, N., Mayorga, D.M. & Trotman, K.T. (2022) Using more effective instructional verbs to elevate auditors' professional scepticism. *International Journal of Auditing*, 26(2), 240–251.
- Venter, E.R. & van Eck, L. (2021) Research on extended external reporting assurance: trends, themes, and opportunities. *Journal of International Financial Management and Accounting*, 32(1), 63–103.

**How to cite this article:** Hay, D., Harding, N., Gan, C., Ge, I., Ho, L., Ranasinghe, D. et al. (2023) Comments of the AFAANZ Auditing and Assurance Standards Committee on the Proposed Standard on Assurance Engagements over GHG Emissions Disclosure. *Accounting & Finance*, 63, 4813–4820. Available from: <https://doi.org/10.1111/acfi.13136>