EXTENDED OF THE AUDIT: AUDIT OF SUSTAINABILITY REPORTS

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ABSTRACT

A concomitant of the corporate integration of sustainable development is that companies even make public reports about their relevant activity via communication channels, as they expect to see some short or long-term competitive advantages. This thesis focuses on the content and the audit of sustainability reports. Assessing the information content of these reports and trying to figure out if the producers of these reports can actually be considered socially responsible. The thesis gets a nearer view of the quality of the audit, based on the stakeholders' preferences. The basis of the dissertation was the sustainability and corporate governance reports of the companies listed on the Budapest Stock Exchange. The research has led to prove that the audit of sustainability reports has an increasing relevance among the stakeholders, even though its audit cannot lead to reasonable certainty on the account of the complexity of the used data and the subjectivity of the opinions. Having analysed the sustainability reports published in Hungary, as a conclusion the audit of sustainability reports creates value. It creates value since reliable and authentic data are more likely to be integrated in corporate decisions. No sustainability results can be achieved without a reliable reporting system, which also has a multiplier effect. The external stakeholders, including primarily investors and analysis experts, can rise to a higher level of trust and make better decisions in line with the company, in so far as they can have access to an audited sustainability report, along with the audited financial statement.

Keywords: *Corporate Social Responsibility (CSR), Accounting, Auditing, GRI, Sustainability Reports*

INTRODUCTION

The objective of the concept of sustainable development is socio-economic development that meets the needs of the present without compromising the ability of future generations to meet their own needs [1].

The implementation of the concept of sustainable development is supported by effective incentives at the global (UN), regional (EU) and national levels. Moreover, special emphasis has recently been lain on the level of microeconomic stakeholders, including especially business organizations, as the fact that the activity of the companies fundamentally influences the implementation of the concept has met with consensus. [2], [3]

Owing to legal, ethical, social and strategic pressure on business organizations, several companies have recognized that they must not disregard the issue of sustainable development, consequently, the number of companies attempting to integrate the principles of sustainability in their strategy and activity is gradually increasing. [4]

A concomitant of the corporate integration of sustainable development is that companies even make public reports about their relevant activity via communication channels, as they expect to see some consequents short or long-term competitive advantages.

Corporate communication appears already in the initial phases of integration considerably reveals the extent of the business association integrated the principles of sustainability too, because

- communication and its content denote value orientation. If a company communicates about a specific topic, it has to care for it, because the specific topic is embraced in the value system of the company at some level.

- communication is targeted at evidencing the fulfilment of various stakeholder groups' expectations. Some of the stakeholders' declared objective is to control corporate social responsibility (non-profit organizations, associations, media). [5]

- the reality content of communication can be checked. Some communication materials (e.g. sustainability reports) can be audited by external experts, and the audit covers the reality content of the communication in a number of cases. The presence or lack and result of external audit tangibly indicates corporate compliance. [5]

Here in this thesis I focus on the content and the audit of sustainability reports. I assess the information content of these reports and try to figure out if the producers of these reports can actually be considered socially responsible. I also look into the quality of the audit, based on the stakeholders' preferences.

I made some hypotheses in my research work and confirmed them with the sustainability reports published in Hungary and supported with an audit.

My hypotheses:

1. The audit of sustainability reports has an increasing relevance among the stakeholders.

2. The audit of sustainability reports cannot lead to reasonable certainty on account of the complexity of the data used and the subjectivity of the opinions.
3. The audit of sustainability reports creates value.

THEORY

Sustainable Society

Corporate Social Responsibility (CSR) means the corporate facilitation of sustainable development. CSR incorporates the social commitment, social attitude and social behavioural pattern of entities. CSR evidences that business life tends to recognize to a greater and greater extent that economy is not a stand-alone dimension in our world, but it is connected to and has an impact on both society and environment. These needs a wholly new approach in business since it should focus not only on capital return and revenues but must also take social and environmental interests into account.

Corporate social responsibility also has its critics, according to whom this approach simplifies several complex ideas and fails to recognize that there is a need for compromise among financial and ethical results. They consider responsible conduct a mere PR method which gives a false sense of security, given that in fact there is a gap among the objectives of companies and society [6]. However, everyone admits that it has a major role in the current vigorous competition. The type of the sustainability strategy taken up by certain entities, i.e. their engagement in the social and environmental sphere has become important; so, having a CSR approach in the focus of the company proves to be a good business solution, since it facilitates access to a wider layer of investors [7].

Sustainability Reports

Sustainability reports are a self-declaration made by the company as a supplement to financial statements, outlining the economic, environmental and social performance of the company in the light of the triple bottom line requirements of sustainability. Sustainability reports represent a form of communication with the stakeholders [8].

Companies intend to incite a certain reaction by way of publishing their sustainability reports. This desired reaction can be as follows:

1. Attracting financial investors and stabilizing the share price. An open and transparent sustainability report helps make a better assessment of the risks of investment in the specific company and reduces the uncertainty factor. Moreover, making a sustainability report also means, to a certain extent, that the company accepts and tries to meet the sustainability requirements, given that there is no company opting for

voluntary reporting if it were not certain that the report could contribute to a fairly positive image of itself. Consequently, companies making a sustainability report do not only mitigate the actual risk but also the sense of risk, meaning that they convey more confidence [9].

2. Access to loans under preferential conditions. Banks take more transparent risks when they give loans to companies making sustainability reports and they have bigger confidence in such companies.
3. Building trust/image in consumers/ordinary men. The stakeholders can have some insight into the internal processes of the company, so the company creates an image of reliability, consequently:
    - the market position of its products can strengthen;
    - it can conquer new markets;
    - it will be easier for it to find the proper workforce.

Making a sustainability report can have additional benefits for the internal operation of the company:

1. It can highlight processes and issues that would not have been recognized without this report;
2. It helps connect the separate functions of the company (e.g. finances, marketing or R&D) with a strategic approach;
3. It improves the capacity of the management to assess the sustainability performance of the company, and as such, it plays a central role in maintaining and strengthening legitimacy. [5].

Several researches note that the above expected reactions (mainly the benefits related to external stakeholders) to making sustainability reports represent a perceptional issue, so the average viewer can even be mistaken in placing much confidence in a company. A company will not be sustainable only on account of making a sustainability report, still, it incites this image in the stakeholder group not sufficiently sensitive to details. So, the problem here lies in conflict between self-declaration and corporate interests [4].

Consequently, sustainability reports still attract a lot of criticism [5]:

1. They are believed to be complicated, because in number of cases they report on activity indices that are incomprehensible for the readers with average knowledge and no expertise in the specific industry.
2. The question of 'compared to what' frequently arises. Is the index presented by the given company high or low? Could it be done better?
3. Due to the pagination of reports, it is quite cumbersome to interpret the content, and materiality can be lost.
4. Their exact target group is not defined. Who are sustainability reports actually addressed to, what information should they provide?

5. Critics believe that reliability/credibility is a question in sustainability reports, given that it is a self-declaration not always under control and even if so, report producers are subject to mistrust.
6. Companies can after all report on whatever they want to, they can filter the publicly accessible information to their liking.

The relevance of the last two criticisms is gradually decreasing because the GRI standard defines both auditing and the content of reports. There is an ever-increasing number of companies applying this uniform reporting framework, which thus guarantees the comparability and reliability of their reports and that they can cover each essential topic in presenting the activities of the company to those interested [10].

The external certification procedures accompanying the standard ensure the standardization of the application, and content is in some cases even compared with actual performance.

European Union Regulations

EU regulations on environment protection rank among the strictest in the world. Environmental policy implicates the protection of the state of the environment and the environment-friendly operation of the EU's economy, contributing to the EU inhabitants' improved health condition and quality of life.

In the view of achieving the above, safeguarding the quality of drinking and bathwater, improving the quality of air, mitigating noise pollution, and decreasing the toxic effects of chemicals are all listed among the objectives.

The directives of the European Union are compulsory for its member states, regarding objectives. Directive 2013/34/EU covers the environment in the range of non-financial statements. It stipulates that obligations pertaining to environmental protection also have to be indicated in non-financial statements. The business reports of companies with over 500 employees must provide information about environmental, social and employee matters, in addition to the effects of fight against bribery and corruption. This directive was modified by Directive 2014/95/EU which obliged companies with over 500 employees and of public interest to report on non-financial data in their annual financial statements.

Requirements of Sustainability Reports

There is information asymmetry between company leaders and stakeholders. This existing asymmetry needs to be diminished to have an adequate level of information available to both parties. Sustainability and environmental accounting systems are responsible for having access to adequate quality and quantity of data, leading to the production of structured and comparable information. The use of expert analyses and various rankings can also alleviate the asymmetry. Sustainability reports are expected to systematize the above-listed factors and meet the stakeholders' information needs [4].

The sustainability report provides a framework for treble optimization, the triple bottom line, comprising the economic, social and environmental effects of companies (GRI, 2000-2011). Broad-minded companies have recognized that responsible social behaviour and stakeholder relations have an impact on how the economic performance of the organization is judged. The external materialization of sustainability is the sustainability report. However, companies must have a clear understanding of the topics that stakeholders find interesting, meaning that they have to meet external expectations [11].

Sustainability reports made in accordance with the Global Reporting Initiative (GRI) must be adapted to traditional accounting, and have the qualitative characteristics required by the system itself. First, they must be transparent and controllable. In terms of transparency, all the processes, procedures and assumptions affecting reporting need to be disclosed. For the sake of controllability, the data in the report have to be recorded, analyzed and published in a way that the auditors could certify their reliability. Additionally, the published information must meet the requirement of being interpretable in the context of integrity, neutrality, authenticity, materiality, timeliness, clarity, comparability and sustainability [12].

Reporting Principles

The three key elements of the reporting process are: reporting principles; control of principles; other principles and their control. The principles are related to the content and quality of the report. The use of principles is intended to support the transparency of the report. Transparency is the basis of reporting and is conditional on presenting the reporting process, procedures, and estimations in the report. Transparency comprises the use of adequate indicators and the full publication of information concerning sustainability. Principles can be grouped in two. The first group incorporates the principles that help define the topics and indicators of the report. The second group includes the principles that assure the quality of the information in the report and its due presentation. The Guide also helps in controlling the principles, so the reporting organization can make a more efficient self-assessment (GRI, 2000-2011).

Reporting principles: materiality, stakeholder involvement, sustainability correlations and integrity.

In the sense of materiality, the reported information has to form part of topics and indicators that influence the stakeholders' decisions or can properly reflect the economic, environmental and social impacts of the company. Every economic, environmental and social impact that crosses the threshold has to be given an account. Both external and internal factors have to be considered to decide about the material information. With regard to external influence, we need to comply with international standards, treaties and meet social needs. In terms of internal factors, we have to consider the mission and strategy of the company. The principle of materiality is also checked (Table 1) according to these criteria (GRI, 2000-2011).

Control of materiality	
External factors	Internal factors
Sustainability issues	Organizational values, strategies, objectives
Sectoral issues	Stakeholders' interests, expectations
Acts, legal regulations, voluntary commitments, international treaties	Organizational risks, critical success factors
Research-based sustainability impacts, risks, possibilities	Basic competences and their relation with sustainability

Table 1. Check the principle of materiality.

According to the principle of stakeholder involvement: the person making the report has to take the stakeholders' expectations and interests into consideration and give a detailed account of how this is manifested in the report. There can be several ways to get and stay in contact with the stakeholders: they can be accessed via the media, or some activity jointly performed with the stakeholders can also be organized.

Each essential moment of involvement needs to be documented, as this is the only way to certify the above principle. The stakeholders' involvement elevates the usefulness and accountability of the report, which improves trust between the organization and them. In the course of the audit, the organization needs to be checked if it has a clear understanding of its stakeholders. An analysis has to be made to see if the information concerning stakeholder involvement is included in the report. Last, the boundaries of the report have to be inspected if they are in accord with the involvement process (GRI, 2000-2011).

According to the principle of sustainability correlations, the broader correlations of sustainability also need to be considered to present the activities of the company. The aim of this principle is that companies disclose both their positive and negative results and effects. If the reporting entities do not integrate this principle in the report, the basic objective of the report will not be fulfiled. If the performance of the organization is not assessed on the basis of sustainability, the economic, environmental and social impact of the company will not be revealed.

For the sake of integrity, the topics, indicators and frameworks of the report need to be specified so as to include the material information that can indicate the triple bottom performance of the company to the stakeholders. This principle also applies to the pagination, content, time frame and quality of the report, linked to the qualitative principles of accuracy and balanced evenness. On making the report, the companies need to care for relying on the results of stakeholder involvement and consider social expectations.

Each impact, if essential for the company and the stakeholders, must be stated in the report. The organizations and units functioning under the control and influence of the specific entity need to be identified in order to assess the framework. Additionally, those participating in production processes should also be verified in connection with corporate impacts. When reporting entities give an overview of their sustainability performance, they should be heedful to publishing the probability, type and expansion of future effects. The fulfilment of the above criterion must be analyzed upon checking the realization of the principle.

Alongside the above principles, those concerning qualities are also essential. These principles facilitate the transparency of reported information; and besides quality, they also provide a guidance regarding data formatting.

Balance, comparability, accuracy, timeliness, clarity and reliability are all integrated in the group 'Reporting principles, to define the quality of the report'.

Revised GRI Index

The objective of the updated Reporting Framework (G4) published in May 2013 was for the report to focus on materiality, thereby to become user-friendly, increase relevance and authenticity, so that the market, the stakeholders, and society could get higher quality information [13].

G4 recognizes that the world has been changed and companies need to face new challenges, which all have an impact on their reports. With the updated G4 version, GRI intended to provide a much more useful framework for reporting entities. The new guidelines have been finalized in a series of international consultations. Experts, task forces and various stakeholders made recommendations for the development of the framework, and the production phase included a public consultation period when everyone could share their expectations and thoughts.

The New Trend – Revised Standard System

GRI relied on the G4 Guidelines when it developed the new global standard which entered into force on the 1st of July, 2018. The independent standardization body Global Sustainability Standards Board (GSSB) was responsible for developing the standard. The members of the Board included experts in business, governmental affairs, HR, investment and sustainability, just as university and civil society experts [13].

The new standard has been designed to render assistance in ascertaining the material sustainability effects during reporting. Due to their simplicity, the new guidelines are expected to facilitate the production of non-financial reports [14].

Reporting entities have to report in accordance with three standards (GRI 101, GRI 1012 and GRI 103). GRI 101 defines the fundamental framework of triple bottom line reports. GRI 102 applies to general disclosure; it sets requirements with regard to the organization and the practice of sustainability reporting. The last part details the management approach [15].

The topics have been reviewed in connection with the G4 version: some topics underwent several changes, certain items were slightly clarified or revised, and some were deleted (GRI, 2017). The prescriptive nature of company introduction was mitigated and efforts were made to adapt it to the new standard. Nevertheless, new requirements were also set in connection with the reporting indicators in a number of cases (products, services, employees).

RESULTS

Audit of Sustainability Reports

The Hungarian Accounting Act obliges public-interest entities to add sustainability data to their report; and auditors are expected to check their supply.

The ISAE3000 and AA1000AS standards have to be used for the audit of sustainability reports. The ISAE 3000 standard developed by IAASB details the rules of “Assurance Engagements Other than Audits or Reviews of Historical Financial Information”.

Only statutory auditors are entitled to issue a certificate compliant with ISAE 3000. Reasonable or limited certainty needs to be gained about the audited data in the course of the audit under the standard.

Reasonable certainty means that the report does not include any essential misstatements. Reasonable certainty represents high-level certainty which can be reached after reducing the audit risk to an acceptably low level. Additionally, adequate and sufficient evidence needs to be collected to mitigate the risk.

The standard gives preference to data accuracy over transparency and integrity.

In the set of information provided in the sustainability reports I have analyzed, reasonable certainty can apply to the data relevant to carbon-dioxide emission under ETS and the number of lost time injuries occurring in a workplace per 1 million hours worked (LTIF –Lost Time Injury Frequency).

Limited certainty represents a level with less certainty. Here, the risk level of an essential misstatement in the report is still acceptable but higher than in reasonable certainty.

Auditors can only gain limited certainty about the substance of the indices and data in the report, with the exception of the above data. In connection with limited certainty, the auditor needs to assess the level of risk acceptable for the company and the owners.

The AA1000AS standard was developed by the Institute of Social and Ethical AccountAbility (ISEA), with the aim of connecting sustainability and accountability. The standard is an integral part of AA1000APS which is an international framework specialized in social responsibility and ethical accountability. The AA standard puts the stakeholders in the centre; the most emphatic part of the regulation is relation with the stakeholders from their search through their involvement to relationship creation and maintenance. It analyses materiality from the stakeholders' perspective and keeps sensitivity and inclusivity in view, in connection with the report.

Stakeholder involvement is also essential because their feedbacks help the group identify the deficient areas requiring development.

The standard assesses the company's management of sustainability issues, performance and the report based on the quality and accuracy of the information published.

Services providing certainty can be assorted into types 1 and 2. In the case of certainty type 1, only the realization of the principles of materiality, sensitivity and inclusivity is checked in connection with the sustainability report. In type 2, the reliability of the reported information is also under scrutiny, in addition to the above, and conclusions are drawn. The reports I have analyzed typically belong to services providing type 1 certainty, so only materiality, sensitivity (social susceptibility) and inclusivity (stakeholder involvement) were monitored.

In auditing sustainability reports, auditors tend to mix the requirements of the two standards. In accordance with the AA standard, auditors only gain type 1 certainty of the reported data. Under ISAE 3000, limited certainty is also permissible with the exception of carbon-dioxide emission and LTIF. Due to the joint use of the two standards, the auditors try to generate a higher value by also checking the reliability of the reported information, however, integrity is still not ensured – though it could not even be.

Audit Method; Forming an Opinion on the Sustainability Report

First, the scopes of responsibility are settled, emphasizing that the management of the given company is responsible for the collection and adequate