

Data quality and the role of the 3rd line of defence



There is no doubt that Integrated Reporting has propelled corporate reporting into a world that expects greater transparency, and that greater transparency brings greater scrutiny and increased risk.

Under this more transparent regime, companies are required to report non-financial information alongside financial information, and boards of directors and other stakeholders expect a similar level of data quality to apply to both types of information.

The dilemma that most corporates face is that financial information has been subject to clear definition, disciplined recording, internal checks and controls and intense scrutiny for many years. Non-financial information, on the other hand, is in most cases not well defined and is not routinely subjected to objective and independent scrutiny as a matter of course. Unsurprisingly, it is for this reason, that in the first year of seeking objective and independent assurance, gross misrepresentation of key indicators, previously believed to have been accurate, is often uncovered.

It therefore is advisable for those charged with governance to consider the organisation's combined assurance model carefully to ensure that the non-financial information presented in the Integrated Report has been based on data of acceptable quality and that it has been subjected to an adequate control framework.

As a first step, organisations should identify the non-financial information presented that is used in key internal or external decision making. Each company is unique in this regard, but this may, for example, include indicators core to the nature of the business (often labour-related indicators, including BBBEE and training), those used in the

supply chain process (BBBEE and Health & Safety) and those that might impact a future tax (Carbon footprint and related CAPEX, if material to the organisation). As this type of information often has multiple owners who have been preparing information separately from the finance function and in a specific manner for many years, a rigorous and independent assessment performed by Internal Audit or an external service provider is essential to avoid embarrassment or worse.

Examples, based on practical experience, of matters to consider include:

- Inconsistent classification of Lost Time and First Aid Injuries – in some instances this is because different locations apply inconsistent principles and, in others the doctor's certificate is overruled to obtain a desired classification;
- Man hours worked is often not assurable, which can be due to the reliability of the data from the time recording systems, or an inability to accurately consolidate and aggregate data. As a consequence, total wages paid may not be correct;
- Race classification based on ID photos only, rather than on documentation or employee self-declaration and incorrect classification of foreigners leads to incorrect BBBEE statistics. This is often the case, despite external verification;
- Incorrect BBBEE classification of foreigners;
- Key training information can often not be supported and is collated in an inconsistent manner;
- Estimates are used for electricity and water consumption when meter readings are not available, but these estimates are not updated when actual meter readings become available;
- Incorrect or inconsistent application of the boundary used in assessing the carbon footprint – in particular, between owned and managed assets;
- The basis of preparation relating to non-financial information is often not clearly defined. Indicators for customer satisfaction and availability of IT systems can differ between operating units with calculation methods often not documented.

In addition to an independent assessment of key indicators, critical processes such as rigorous risk management, stakeholder engagement and materiality determination should be included on a rotational basis in the Internal Audit plan to ensure that there are sufficient controls in place to ensure reliable execution and disclosure.

One of the most common reasons for reporting inaccurate non-financial information is the application of an inconsistent “basis of reporting” for non-financial information. In accounting language, the basis of reporting should be viewed as something similar to the accounting policies in the Annual Financial Statements – a way of publically defining the rules followed when accounting for complex matters.

Many companies have turned to existing sustainability guidelines, frameworks and standards to help guide them in presenting non-financial information in a universally understood language. Most South African companies seem to use the Global Reporting Initiative (GRI) Sustainability Reporting Guidelines in the preparation of their non-financial disclosure. We can therefore conclude that GRI is the preferred “basis of reporting” in the South African context. Encapsulating principles such as materiality, stakeholder inclusiveness and reliability of data, the GRI Sustainability Reporting Guidelines provides a foundation upon which non-financial disclosure can be made.

The International Integrated Reporting Council (IIRC) acknowledges the GRI Sustainability Reporting Guidelines, third generation (G3 and G3.1), amongst other frameworks, codes, standards and initiatives, in the development of integrated reporting. The influence of GRI on integrated reporting is clear and the converse is also true. As the trends within integrated reporting, including increased governance reporting and remuneration disclosure evolve, they are also having an impact on the GRI Sustainability Reporting Guidelines. The GRI is currently in the process of developing the GRI Sustainability Reporting Guidelines, fourth generation.

The proposed focus by the GRI fourth generation includes governance, remuneration and supply chain and may be attributable to the trends associated with integrated reporting. It is interesting that G4 is proposing to strengthen the link between governance and sustainability performance. This is a fundamental component of integrated reporting and ensuring the sustainable strategic initiatives are measured and monitored at the highest level.

The King Report on Governance for South Africa (King III) specifically requires that the Board should comment on the integrity of the Integrated Report. The importance of this responsibility and the potential negative impact of approving possibly incorrect information in the Integrated Report on important operational matters, which are produced outside the realm of a well-controlled finance function, should not be underestimated.



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