

Key points

MerchantCantos thinks that the Integrated Reporting draft is a great step on the way in terms of helping companies on their journey towards a more holistic and inclusive description of their business, which connects financial as well as non-financial information. We are very pleased to offer our feedback to this draft.

Our business helps companies develop reports and communication strategies to reach their stakeholders in the most efficient ways. We have submitted our response based on our experience of corporate reporting and our dialogues with companies and the investment community..

Below is a summary of the key points:

- Integrated thinking is not happening in many businesses. Companies that have not developed this mind-set will find the draft difficult to implement.
- It needs to be made clear where this integrated report content goes: ie. in the Annual Report and Accounts (ARA) replacing the narrative, rather than a new report or a Standalone Sustainability Report (SSR).
- Legal and accountability issues need to be solved. ARA's are regulated documents, SSR's are not. ARAs are highly regulated but there tends only to be voluntary guidelines to follow for SSRs. There should be greater definition.
- Alignment of language is crucial. If the financial community is to buy into the concepts, careful consideration should be given to the use of specific terms and how they relate to existing usage.
- Many of the draft requirements have much in common with existing legislation that applies to ARAs in the UK so compliance for UK businesses may not be too great a burden. Businesses not accustomed to compliance with such standards will find the draft more difficult to apply.
- Calling the whole proposal 'IR' is also rather confusing and companies will understand this as 'Investor Relations', rather than integrated reporting. As the audience is precisely the financial community, we think this is very problematic.

Chapter 1: Overview

1. Principles-based requirements

Yes.

4.4. Principle 4.4 should explicitly clarify that an integrated report replaces the narrative of an annual report, and that <IR> is not a supplement or an alternative version of the company's story.

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4.5. Part of Principle 4.5 demands that companies should disclose “the nature and magnitude of the material trade-offs that influence value creation over time”. We believe this is less material than other factors and could add clutter to the report.

4C and 4G. There appears to be considerable overlap between content elements 4C (opportunities and risks) and 4G (challenges and uncertainties). A clearer distinction between the two content areas would be helpful.

2. Interaction with other reports and communications

No

The draft should explicitly clarify that an integrated report replaces the narrative of an annual report, and that <IR> is not a supplement or an alternative version of the company’s story.

3. Online database: which references to include?

No comment.

4. Other

The legislative implication of what this means for national legislation for annual reporting needs to be clarified as well, otherwise there is a risk that only countries where this is already partially included will be implementing integrated reporting going forward.

The most important thing here is to define which standards, indicators and measurements are recommended. Companies will be confused if they are asked to choose amongst a series of providers, benchmarks and standards. Also, it will be crucial that the suggested organisations clearly state whether they are assurance providers, consultants or standard-setters.

Chapter 2: Fundamental concepts

Capitals

5. Definition of capitals

The phrases used in the draft will be very important in ensuring reporting teams and investors engage with the information. Financial, manufactured, intellectual, human, social relation and natural capitals will not be familiar terms for the financial community. With legislation stipulating, at

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least in the UK, that companies need to disclose information on 'resources and relationships' there is a need to align terms and expressions to make certain that people understand which information the report is referring to.

6. Any other comments?

No comments.

7. Definition of business model

No.

The new Strategic Report Regulations, under which the current Business Review will be replaced by a Strategic Report, require UK listed companies to include a Business Model in their ARAs but do not define what this means in detail. The Financial Reporting Council defines a business model as an 'explanation of the basis on which the company generates or preserves value over the longer term'.

In our view, where the integrated reporting draft uses terms that already have a meaning in a reporting context, it is important that they are aligned as much as possible. Any differences will only lead to confusion and make comparison between companies difficult.

8. Definition of outcomes

Good and understandable definition of outcomes, but see 10 for further comments to the section.

9. Other comments about 2C

See below

10. Other about chapter 2

No comment.

Chapter 3: Guiding principles

Materiality and conciseness

11. Approach to materiality

Yes

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The description of materiality is both useful and relevant. By placing the responsibility for the determination of materiality firmly with senior management, the integrated report demonstrates a high level of accountability to the readers of the report.

12. Comments on section and on the materiality process

Many companies, especially SMEs, have not yet carried out a solid materiality analysis of their business. It's important to be aware of this fact.

Reliability and completeness

13. Reliability of an integrated report

The reliability of an integrated report is demonstrated by the commitment shown by the directors to present a balanced and complete story of their company's plans and progress in creating value.

14. Other comments on reliability and completeness

No comment.

15. Other comments to chapter 3

3.17: It is unclear whether there is an expectation to include the process description as to how stakeholders have been defined and how the engagement processes are happening, or whether companies should just include particular topics that are of concern to key stakeholders. If the former is the case, then standards and/or further guidelines would be helpful.

3.19: Stakeholder responsiveness. It is a good and clear paragraph with some concrete examples of where communication with several stakeholders could and should take place. We suggest a similar approach is taken when defining where the integrated reporting should go in the first place (Overview, question 2).

Chapter 4: content elements

16. Comments to chapter 4

4A: External environments. As mentioned in question 5, many businesses have not been used to describing trends and factors which have a potential to influence their business but, which are outside of their control. (An exception is UK quoted companies which are required to do so by the Companies Act.) Finding out which information to include and where to include it will be a challenge for many.

Chapter 5: preparation and presentation

Governance

17. Include statement of responsibility

Yes, to show the directors' commitment to <IR>.

As discussed above, the information should be available within the ARA to ensure investors and others from the financial community will find the information. If the information is woven throughout the report, one would expect all information within the report to be under the ultimate responsibility of directors and the CEO.

If a separate statement is included for sustainability/integrated reporting information, it will paint a picture of a business where integrated thinking is not taking place.

18. Other comments

None

Credibility

19. If assurance is done, to cover all – or only parts of the report?

This will depend on where content is included. If it is included in the ARA, it will only be appropriate to assure numerical information.

20. Other comments on 5E

See above.

Other

21. Other comments about chapter 5

Overall, the chapter helps to explain the concepts in plain English and gives concrete advice as to how companies should prepare the reports. It is also good that there are further explanations on defining materiality and giving information of a future nature, taking into account limitations given by legislation.

There are, however, various levels of detail given here on how to include information and where. Whilst there is a high level of detail regarding the channels of communication, which can be used (see below), there is a lack of definition of where information should be included.

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51: This section goes into a great detail around which methods can be used for reporting and how to ensure connectivity of information, for instance by using web-based media and XBRL. Compared to the rest of the draft, there is an unnecessary level of detail given here, as the platform for communicating the integrated reporting information is still unclear. A suggestion is to take out this level of detail here, or include a similar level of detail throughout section 5.

Overall view?

22. Is the framework appropriate for companies to use in explaining value creation on short, medium and long-term?

We think the draft is a great starting point, but we do recommend addressing the 6 key issues identified at the beginning of this submission.

Development of IR

23. Any other explanatory material needed? If yes, what?

- No comments.

Other

24. Any other comments not addressed by 1-23?

See 'Key points' at the beginning of this submission.