

## Consultation questions

The IIRC welcomes comments on all aspects of the Draft International <IR> Framework (Draft Framework) from all stakeholders, whether to express agreement or to recommend changes.

The following questions are focused on areas where there has been significant discussion during the development process. Comments on any other aspect of the Draft Framework are also encouraged through the questions.

Please provide all comments in English.

All comments received will be considered a matter of public record and will be posted on the IIRC's website ([www.theiirc.org](http://www.theiirc.org)).

### Comments should be submitted by Monday 15<sup>th</sup>, July 2013.

Name:

Email:

Stakeholder group:

If replying on behalf of an Organization please complete the following:

Organization name:

Industry sector:

Geographical region:

### Key Points

If you wish to briefly express any key points, or to emphasize particular aspects of your submission, or add comments in the nature of a cover letter, then the following space can be used for this purpose. Please do not repeat large amounts of material appearing elsewhere in your comments.

#### Introduction

I am writing a response in an academic spirit in my capacity as an incoming DPhil student (Management Research) at the University of Oxford (due to start on October 2013). The area of environmental reporting has always been a keen interest of mine, and therefore, I cannot resist the compulsion to comment on such novel approach to integrated reporting taken by the <IR> Framework (Consultation Draft), which is published by your pioneering organisation. As I have only begun embarking the research on the topic of environmental reporting, I could only hope that you might consider my comments to be insightful from an academic point-of-view. I believe that it is in the best interest of the business society that your important project should proceed, and I hope that some of my comments might be constructive toward the continuance of the <IR> Framework project.

Sincerely,

Timotius Kasim

## Chapter 1: Overview

### ***Principles-based requirements***

To be in accordance with the Framework, an integrated report should comply with the principles-based requirements identified throughout the Framework in bold italic type (paragraphs 1.11-1.12).

1. *Should any additional principles-based requirements be added or should any be eliminated or changed? If so, please explain why.*

- Integrated thinking: It is somewhat surprising not to see the concept of integrated thinking being highlighted in bold and italic as one of the key principles of the <IR> Framework. It could be contended that the actual mechanisms that drive the results surmised in the report are incrementally more important than the report itself, and therefore, the concept of integrated thinking (that leads to integrated decision-making) should be a candidate to be considered as a key principle. From a social science point-of-view, the reporting process can be argued to be 'reactive' such that the preparation of the report induces the preparers to be proactive as to influence the result that is to be published in the report either by fiddling with the numbers or actually managing the value-drivers of the goals those are considered to be the priority. As a result, it could be argued that the successful dissemination of the novel and holistic concepts such as the multiple capital concepts depends on the application of such integrated thinking by the preparers; integrated thinking is the weakest link within the integrated reporting chain. Consequently, it is rather intriguing to notice its absence as one of the key principles.

- Narrative reporting: The <IR> Framework is advocating the use of the narrative reporting format to communicate its contents. However, in the worst-case scenario, the report might turn into a mundane, un-meaningful communiqué filled with bland words. Furthermore, it is remain to be seen whether the preparers would be willing to disclose negative performance since it could be easily framed in a positive context or even omitted altogether. On the other hand, the use of a more concrete metrics such as the Key Performance Indicators ("KPIs") may allow the preparers to report the 'dark side' of the organisations ordinarily in the format of negative numbers, which still could be considered to be acceptable as long as it does not represent extreme variances. As a result, some form of further guidance on either the appropriate wordings regarding the narrative reports or the examples of the KPIs (e.g. as in the Section 6B of Background Papers: Capitals) might increase the clarity of the integrated report.

### ***Interaction with other reports and communications***

The <IR> process is intended to be applied continuously to all relevant reports and communications, in addition to the preparation of an integrated report. The integrated report may include links to other reports and communications, e.g., financial statements and sustainability reports. The IIRC aims to complement material developed by established reporting standard setters and others, and does not intend to develop duplicate content (paragraphs 1.18-1.20).

2. *Do you agree with how paragraphs 1.18-1.20 characterize the interaction with other reports and communications?*

- Agree: Since the integrated reporting concept is build on the intersection between the financial reporting and sustainability reporting concepts, the concern regarding duplicate content is understandable. However, it is to be noted that there are several variations of financial reporting standards such as the International Financial Reporting Standards ("IFRS") or the US Generally Accepted Accounting Principles ("US GAAP") that might result in an 'apples-to-oranges' comparison. As a result, it might be a good idea to

require clear referencing and some explanations regarding the methods of measurements, which are used in regard to the financial information.

3. *If the IIRC were to create an online database of authoritative sources of indicators or measurement methods developed by established reporting standard setters and others, which references should be included?*

- Some of the relevant references might include the cross-referencing to both of the financial report and sustainability report, two of the most reports with much overlap in term of contents with the integrated report. Further, the composition of the reference might include, inter alia:

- o Compliance with the type of standards
- o The methods of measurement for the financial information
- o Direct cross-referencing with the location of the information in the related reports
- o External/ independent party assurance

#### **Other**

4. *Please provide any other comments you have about Chapter 1.*

n/a

## **Chapter 2: Fundamental concepts**

### ***The capitals (Section 2B)***

The Framework describes six categories of capital (paragraph 2.17). An organization is to use these categories as a benchmark when preparing an integrated report (paragraphs 2.19-2.21), and should disclose the reason if it considers any of the capitals as not material (paragraph 4.5).

5. *Do you agree with this approach to the capitals? Why/why not?*

- Agree: Divorcing the capital concept into six distinctive branches (financial, manufactured, intellectual, human, social/ relationship and natural capitals) affords greater visibility toward the other aspects of business instead of the mere focusing on its financial aspect. However, the split seems rather unnatural, and the conception that the capitals need not be realised in financial forms represents a distinct contradiction from the conventional economic theory. Yet, it could be contended that the other five imaginary 'capitals' concept merely revolve around and gravitate toward the primary financial capital concept. The observation is deducted from the <IR> Framework's premise that its primary objective is to report the value-creation process attributable to the financial capital providers; in other words, the other capital concept is only relevant as much as it affects the short, medium or long term values attributable to the financial capital provider, i.e. the free-cash flows, the basic form of financial capital. Yet, the gravitation toward the financial concept does not necessarily diminish the importance of the other five new capitals concept, instead it allows a wider application of the traditional Hicksian capital maintenance theory, which are also being utilised in the conventional financial reporting framework to manage other social and environmental issues those are represented in the five new concept of capitals.

- Disagree: Regardless of the merits, the branching of the capital concept into six distinct aspects leads to ambiguous boundary between the different type of capitals. Furthermore, the inclusion of shared/ free goods as a capital (e.g. infrastructure in the financial capital or air in the natural capital) might result in the difficulty in operationalising the concept since those aspects are not technically economic goods, meaning that its maintenance does not depend on a single individual/ firm. On the other hand, it might be simpler to attribute the impacts caused by the depletion of those aspects to the 'social/ relationship capital' in the form of the firm's overall reputation and its relationship with the relevant NGOs; the aspects, which have more concrete impacts on the free-cash flows of the firm.

6. Please provide any other comments you have about Section 2B?

n/a

### **Business model (Section 2C)**

A business model is defined as an organization's chosen system of inputs, business activities, outputs and outcomes that aims to create value over the short, medium and long term (paragraph 2.26).

7. Do you agree with this definition? Why/why not?

- Agree: In general, it could be contended that a business model refers to the process of transformation between the inputs toward the outputs of the firms that might have multitude of outcome both internally and externally. Furthermore, the utilisation of the business model concept allows the operationalisation of the 'multiple capitals' concept that essentially gravitates toward the interest of the financial capital providers. However, in the spirit of integration, it might be worth exploring the idea of cross-referencing the business model section of the integrated report with the business reviews presented in the 'Business Review' sections of the UK annual reports or the 'Management Discussion and Analysis' sections of the US annual reports.

Outcomes are defined as the internal and external consequences (positive and negative) for the capitals as a result of an organization's business activities and outputs (paragraphs 2.35-2.36).

8. Do you agree with this definition? Why/why not?

- Agree: Generally, most of the outcomes of the business could be attributed to its ordinary business activities. A positive outcome in regard to the financial capital is more conventionally known as 'income', which according to the Hicks' theory of income is described as the amount that the firm could spend, and expects to be as well-off as it was in the beginning of the period. Hence, considering the other 'capitals' are the derivation of the original financial capital concept, it could be assumed that the 'outcomes' are the incremental amount needed to maintain the capitals at the levels, which they were as at the beginning of the period. However, it is worth noting that the capitals concept as stated in the <IR> Framework could also be depleted as a result of an extra-ordinary business activities such as a force majeure type of incidents, which also needs to be addressed in certain circumstances.

9. Please provide any other comments you have about Section 2C or the disclosure requirements and related guidance regarding business models contained in the Content Elements Chapter of the Framework (see Section 4E)?

n/a

**Other**

10. Please provide any other comments you have about Chapter 2 that are not already addressed by your responses above.

n/a

### Chapter 3: Guiding Principles

#### **Materiality and conciseness (Section 3D)**

Materiality is determined by reference to assessments made by the primary intended report users (paragraphs 3.23-3.24). The primary intended report users are providers of financial capital (paragraphs 1.6-1.8).

11. Do you agree with this approach to materiality? If not, how would you change it?

- Agree: The approach to materiality is consistent with the primary objective of integrated reporting that is to provide information regarding the value-creation process of the firm toward the financial capital providers. The explanation in the <IR> Framework also identifies the commonly used approach in determining materiality through the assessment of the impacts/ likelihood matrix, which would allow the firm to focus only several issues with high importance.

12. Please provide any other comments you have about Section 3D or the Materiality determination process (Section 5B).

Comments on the Choice of the Intended Users

- The <IR> Framework designation of the financial capital providers as the intended users of the integrated report could be contended to make the report exclusive to the other stakeholders. In comparison with the sustainability report, which normally addresses the wider stakeholders, the <IR> Framework adopts the expedient approach, which assumes that the value of the financial capital providers and the other stakeholders will merge in the long run. However, such assumption is highly sensitive to the capability of the firm to incorporate the interest of the other stakeholders that, in turn, is dependent on the awareness of the firm regarding the value-erosion that might result by taking an exclusive stance. In other words, the assumption depends on the ability of the firm to implement 'integrated thinking' in its decision-making process. As a result, it is vital for the <IR> Framework to consider the alignment of the preparers' behaviour to the spirit of the <IR> Framework.

### **Reliability and completeness (Section 3E)**

Reliability is enhanced by mechanisms such as robust internal reporting systems, appropriate stakeholder engagement, and independent, external assurance (paragraph 3.31).

13. *How should the reliability of an integrated report be demonstrated?*

Reliability could be demonstrated by obtaining (among others):

- External assurance/ independent opinion: an independent third party opinion would ensure that report is objective, and not one-sided.
- Assessment of internal control: reliability could be demonstrated if the preparers have a solid process that governs the preparation of the integrated report.
- Compliance with the guiding principles: the demonstration of the adherence toward the guiding principles presented alongside some concrete examples would enhance the credibility of the report.

14. *Please provide any other comments you have about Section 3E.*

n/a

### **Other**

15. *Please provide any other comments you have about Chapter 3 that are not already addressed by your responses above.*

n/a

## **Chapter 4: Content Elements**

16. *Please provide any comments you have about Chapter 4 that are not already addressed by your responses above (please include comments on the Content Element Business Model [Section 4E] in your answer to questions 7-9 above rather than here).*

n/a

## **Chapter 5: Preparation and presentation**

### **Involvement of those charged with governance (Section 5D)**

Section 5D discusses the involvement of those charged with governance, and paragraph 4.5 requires organizations to disclose the governance body with oversight responsibility for <IR>.

17. *Should there be a requirement for those charged with governance to include a statement acknowledging their responsibility for the integrated report? Why/why not?*

- Yes: The acknowledgement of the responsibility by those charged with governance would ideally allocate the ultimate oversight responsibility of the preparation of the integrated report toward the executives, who are actually in charge of the report.

Rather than focusing on the symbolic nature of the statement of acknowledgement, the focus should be on ensuring that there is a governance mechanism, which is in place to ensure that the preparation of the integrated report would be effective. As a result, it might be worth exploring the idea of requiring the elaboration about the preparation mechanism in addition to the statement of acknowledgement of the responsibility by those, who are charged with governance.

18. Please provide any other comments you have about Involvement of those charged with governance (Section 5D).

n/a

### **Credibility (Section 5E)**

The Framework provides reporting criteria against which organizations and assurance providers assess a report's adherence (paragraph 5.21).

19. If assurance is to be obtained, should it cover the integrated report as a whole, or specific aspects of the report? Why?

- Specific aspects of the report: In order to increase the credibility of the report, ideally the external assurance opinion needs to address the integrated report as a whole. However, due to the nature of the report, which may contain subjective opinions and future outlooks that might not so practically be verified, it would be more pragmatic, and indeed increase the credibility of both the report and the assurance providers by limiting the scope of the assurance engagements to some aspects, which could be verified. Some objective aspects including non-financial information such as the Key Performance Indicators could be audited to confirm its credibility.

20. Please provide any other comments you have about Credibility (Section 5E). Assurance providers are particularly asked to comment on whether they consider the Framework provides suitable criteria for an assurance engagement.

n/a

### **Other**

21. Please provide any other comments you have about Chapter 5 that are not already addressed by your responses above (please include comments on the materiality determination process [Section 5B] in your answer to question 11 above rather than here).

n/a

## Overall view

22. *Recognizing that <IR> will evolve over time, please explain the extent to which you believe the content of the Framework overall is appropriate for use by organizations in preparing an integrated report and for providing report users with information about an organization's ability to create value in the short, medium and long term?*

- Most of the contents proposed in the <IR> Framework conveniently overlaps with the other reports, and affords a foundation for the preparers to build the integrated report. The contents on the 'Organizational views and External Environment', 'Governance' and 'Opportunities and Risk' contain some elements, which have been discussed in the financial report of an organisation. Furthermore, the contents of the 'Performance' and 'Future Outlook' sections might also have been partially discussed in the Sustainability Report of the firm.
- However, other contents including the 'Strategy and Resource Allocation' and the 'Business Models' sections are quite contemporary, and indeed are the core elements of the integrated report, which are purported to demonstrate the value-creation process, which have not been discussed elsewhere in other companies communiqué. Regardless, some critics that might be attributed toward the current formats, especially in regard to the 'Business Model' sections include the complexity of operationalising and reliably measuring the maintenance of the 'multiple capitals' concept and tracking its flow through the business model of the company that might result in the contradicting of the objective of the integrated report of being concise. Furthermore, it is remain to be proven whether the narrative formats would be adequate to illustrate the presentation of the multiple capitals maintenance process. As a result, in the future development of the <IR> Framework, the committee might need to consider a simpler approach that focuses more on the actual application of the 'integrated thinking' process in addition to the reports' ability to comprehensively deliver information to its intended users.

## Development of <IR>

23. *If the IIRC were to develop explanatory material on <IR> in addition to the Framework, which three topics would you recommend be given priority? Why?*

- Multiple capitals/ Business models concepts: the contemporary concept represents the core content of the integrated report that might truly be an innovation if the ideas could be diffused effectively to the business community.
- Narrative formats: the explanatory materials on the choice of wordings and other narrative formats might be essential in ensuring that the bulk content of the integrated report are not merely bland content.
- Reporting boundary: some clarifications might also be necessary in regard to the scope of the report, and the reasoning beyond the belief that the value of the financial capitals providers would align with the other stakeholders in the long run.

## Other

24. *Please provide any other comments not already addressed by your responses to Questions 1-23.*

n/a