Subject: Consultation Draft of the International <IR> Framework – Integrated Reporting

Dear Sir/Madam,

We very much welcome the opportunity to comment on the consultation draft of this initiative. These comments have been developed with input principally from the Novartis Financial Reporting and Corporate Responsibility Reporting teams.

Opening comments

We agree that organizations, especially those that have the goal of being for profit, are increasingly expected to justify their "licence to operate" to their various financial and non-financial stakeholders. This needs to address not only whether or not they provide their financial providers of capital with adequate returns but also their impact on the other providers of non-financial capital. Furthermore, there is an increasing demand, either through legal requirements or other types of external pressure for commercial organizations to provide additional non-financial data. This is leading to an explosion of data in both financial and non-financial areas.

We are of the opinion that there is a need to curb this on-going information excess in the various documents that are produced.

We believe that many organisations have an interest in adopting pragmatic and principles-based guidelines for <IR>. We consider that this interest stems from a need for an integrated reporting framework that enables an entity to show in a holistic way how its business activities and metrics present a complete and balanced picture of how its financial and non-financial relationships are interlinked.

1. Overview

For <IR> to gain momentum, we consider that it cannot be seen as purely a marketing document for the Finance team. The general public often remains very sceptical of the perceived aims of business activity which is too often seen as just focused on short-term profit maximising goals at the expense of the social and environmental impact.

We believe that the aim of <IR> should be to present a meaningful and more balanced view of business activities for all stakeholders. We therefore doubt that it is appropriate to have "providers of financial capital" as the sole principal audience, as stated in Section 1.6. The target audience should refer to any stakeholder who has a stake in the six types of capital mentioned in the consultation draft and we see that in the current draft this is absent. If the
framework does not redefine its target audience, it will not help companies demonstrate that they are operating in a responsible manner to NGOs, employees, and political parties amongst others.

We also consider that the final framework guidelines should be high-level principles. In our opinion stating that \(<\text{IR}\>\) is to be "applied continuously to all relevant reports and communications" (Section 1.18) will create repetitive narrative for organisations when presenting information to external audiences and will have substantial resource implications on reporting entities. Companies should be allowed flexibility and be entrusted to correctly judge when discussions on short, medium and long-term strategy are appropriate and relevant to the audience. An integrated reporting framework should not be prescriptive; yet, it should provide practical guidance companies can use to determine how to best disclose their value impacts. Given that for-profit organisations will be the key implementers of the framework, the IIRC should be as explicit and "business-friendly" as possible in its guidance (recommending KPIs that align with existing frameworks and sharing examples of emerging practice from organizations currently testing the approach, for instance).


Whilst we consider that IIRC’s draft guidelines present a step in the right direction for \(<\text{IR}\>\), the following concerns should be addressed as IIRC approaches its December 2013 target for an initial version of the Framework.

We believe it is important that the guidelines are changed from a discussion on financial value creation to one of impact on value of capital. In order to satisfy the requirements of the organization justifying its "licence to operate", the guidelines need to promote a balanced view for each of the six providers of capital on how organisations are impacting value. While it is inevitable that in some of the dimensions of capital, value will be destroyed (e.g. extraction of non-renewable resources), an organization needs to openly state this and then explain how it is mitigating the impact of this value destruction in this dimension of capital. \(<\text{IR}\>\) will gain credibility with the non-financial community if it down-plays the purely financial aspect by focusing on what is necessary for a company to operate as sustainably as possible.

4. Content elements / 5. Preparation and Presentation

Emphasizing the report as “stand-alone” as in Section 4.4 introduces confusion as to how \(<\text{IR}\>\) will fit with existing reporting frameworks and communication channels companies use with investors and other stakeholders. Sections 4 and 5 should state that the Integrated Report should not necessarily be a new report but a report which draws together the strands of all presented information in a meaningful, concise and balanced way. As such the \(<\text{IR}\>\) framework should give guidance on how an Integrated Report should summarize the key elements of other reporting frameworks and standards (OECD guidelines, IFRS, GRI, UN Global Compact, country by country data, etc.) and bring them together in a cohesive way that links the overall Integrated Report to the organization’s operating model, strategy and "license to operate". It should also take into account the overall changing reporting landscape, such as within the European Union where there is currently an initiative to amend its corporate reporting directive to include additional environmental, social and related disclosures.

Furthermore, the proposal for disclosing the “materiality determination process” in reports and communications may result in lengthy, fragmented reports which will hinder the message corporations aim to make. Similarly, third party assurance, should not be mandated, however if an organization voluntarily decides for some form of external certification, it should be recommended that this should focus on factual and verifiable information, as is done today with
the financial statements. We consider that it would be difficult for assurance providers to audit qualitative aspects of the report such as strategy, business model, and external environment.

Conclusion

Generally, we support IIRC’s work and commitment in bringing these guiding principles and <IR> to the forefront of the reporting community. We believe that addressing the issues mentioned in this comment letter regarding the target audience, differences between value creation and change in value of capital and <IR> framework’s relationship to existing reporting standards will go a long way toward establishing a framework which organizations can follow in the future.

Finally, at this stage of the process, more focus should be placed on the key principles. It would be helpful to decrease the length of the document and reduce some of the discussions on preparation and presentation, especially those related to materiality. Better clarity on how connectivity between the different sections of the report would be helpful as this will be the key factor in the success of Integrated Reporting (i.e. the ability for companies to demonstrate how the different factors such as strategy, financial, environmental, social, etc., link together to create a change in value of capital).

Thank you in advance for considering our points. Please do not hesitate to contact us at malcolm.cheetham@novartis.com or reto.rieder@novartis.com should you have any questions on this response.

Yours sincerely,

M.B. Cheetham
Novartis Group
Chief Accounting Officer

R. Rieder
Head of Novartis Financial & Management Reporting