

Standard Life Investments

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Dear Mr Nugent

TOWARDS INTEGRATED REPORTING: COMMUNICATING VALUE IN THE 21st CENTURY

Standard Life Investments Limited, which is a subsidiary of Standard Life plc, is a major global investor, based in Edinburgh, with assets under management of £150 billion as at 30 September 2011. For Standard Life Investments, governance, stewardship and sustainability are integral to our investment process. Indeed, a cornerstone of our 'Focus on Change' philosophy and investment process is our belief that corporate stewardship, and the ways in which companies manage social and environmental issues, have a fundamental impact on the achievement of long-term investment returns. As a global investor and shareholder, Standard Life Investments actively encourages best-practice standards in companies' management of environmental, social and governance issues.

We invest around the world in the securities of a wide range of public and private companies and, in so doing, we place reliance on the audited financial statements and annual reports prepared by these companies. Hence, we welcome the opportunity to comment on the International Integrated Reporting Committee's Discussion Paper 'Towards Integrated Reporting: Communicating Value in the 21st Century'.

We have been concerned for some time that corporate reporting is increasingly no longer 'fit for purpose' and hence we welcome the Integrated Reporting initiative as a credible and coherent means of addressing these concerns. We hope that this initiative will ultimately lead to improved communication between companies and their stakeholders, and hence achieve effective accountability and sound stewardship.

The following provides our brief comments on the specific questions in the discussion paper.

The World has Changed – Reporting Must Too

Q1. (a) Do you believe that action is needed to help improve how organisations represent their value-creation process? (b) Do you agree that this action should be international in scope?

Current corporate reporting is predominantly focused on economic decision-making and short term value drivers but does not recognise the increasing importance of stewardship and sustainability. To be more useful, corporate reports should balance the information needed for economic decision making and stewardship. Companies too will find it useful to

be able to demonstrate more clearly their stewardship and the creation of social, as well economic, value.

In order to report in this way, an Integrated Report is required which communicates key financial and non-financial information in a single document and clearly outlines the relationship between the two.

The initiative also aims to accommodate complexity. It may be preferable to focus more on achieving clarity. Accounting standards is one area where this would be relevant: although there have been great strides made in creating more international uniformity in accounting standards, the complexity arising from these standards is an increasing concern for us and others. Within the context of a coherent overall report, improving communication should be a priority.

With regard to scope, we would agree that this action should be international. One crucial aim for the project should be reduce international differences in reporting and thus ensure that reports are more easily comparable. However, there has to be recognition that the resources and skills necessary to undertake such reporting may be more of a challenge in emerging economies. This suggests a different timescale may be required here.

Towards Integrated Reporting

Q2. Do you agree with the definition of Integrated Reporting?

We would generally agree with the definition outlined. We note the reference to Integrated Reporting providing 'a clear and concise representation of how an organisation demonstrates stewardship'. We believe that the concept of stewardship should be at the heart of the corporate reporting system. In an organisational context, stewardship refers to management's responsibility properly to utilise and develop the resources of a company in a way that generates long term value on a sustainable basis. The essential stewardship factors include corporate culture and purpose, long term business sustainability, risk appetite and the allocation of resources, environmental management and relationships with society. Consideration of these factors should have greater prominence within the Reporting Framework.

Although the Integrated Report will be valuable to a variety of stakeholders, it should be noted that shareholders are in a different position to other stakeholders. Shareholders are generally there for the long term and concerned that the value of their investment will steadily increase over time. Shareholders provide the risk capital on which the company is built. They are the owners of the business and have the ability to directly influence its development via the exercise of their shareholder rights at general meetings. A company can carry on, perhaps for a long period of time, with a poor reputation or inefficient use of resources, but if shareholder value is neglected, ultimately the company will not survive. The primacy of shareholders needs to be recognised in the reporting framework that companies employ to account for their stewardship activities.

International Integrated Reporting Framework

- Q3. Do you support the development of an International Integrated Reporting Framework?**
Q4. (a) Do you agree that the initial focus of Integrated Reporting should be in reporting by larger companies and the needs of their investors? (b) Do you agree that the concepts underlying Integrated Reporting will be equally applicable to small and medium enterprises, the public sector and not for profit organisations?

In order to allow the orderly development of Integrated Reporting, a Framework is a necessary component of the proposals and hence we would support this.

More specifically, in terms of the key differences identified between traditional reporting and Integrated Reporting, we strongly support the concept that reports should be more concise

and would refer you to The Institute of Chartered Accountants of Scotland report 'Making corporate reports readable – time to cut to the chase', a valuable and practical contribution to this debate.

We would also support the concept that reporting should be 'technology enabled' so as to allow access to further detail online when appropriate. However, there is a risk that this may not, of itself, improve clarity and may simply turn information into separate items of data which do not add anything to the bigger picture. Getting the right balance between information and communication will be crucial.

Ultimately, the concepts underlying Integrated Reporting should be equally applicable to listed and unlisted companies, irrespective of size. However, it is appropriate that the initial focus be on larger companies. Smaller organisations do not have the same expertise and resource as larger ones so we should allow time for this new form of reporting to bed down before smaller organisations are required to report in this manner.

Business Model & Value Creation

- Q5. Are: (a) the organisation's business model; and (b) its ability to create and sustain value in the short, medium and long term, appropriate as central themes for the future direction of reporting?**
- Q6. Do you find the concept of multiple capitals helpful in explaining how an organisation creates and sustains value?**

It is appropriate that the organisation's business model and drivers of sustainable value creation are identified as key central themes to the Integrated Reporting model and this focus should help improve the relevance and clarity of corporate reports. However, the definition of the various 'capitals' that organisations use and depend on is somewhat artificial. It may be useful, when thinking about these 'capitals', to make a distinction between those that can more easily be ascribed a value e.g. can be bought or sold, as opposed to more intangible capital such as reputation or employee skills and experience.

Guiding Principles

- Q7. Do the Guiding Principles identified in the Discussion Paper provide a sound foundation for preparing an Integrated Report – and are the collectively appropriate; is each individually appropriate; and are there other Guiding Principles that should be added?**
- Q8. Do the Content Elements identified in the Discussion Paper provide a sound foundation for preparing Integrated Reports – are they collectively appropriate; is each individually appropriate; and are there other Content Elements that should be added?**

The Guiding Principles and Content Elements seem largely appropriate with two exceptions.

With regard to 'Conciseness, reliability and materiality', we note that senior management and those charged with governance will be responsible for deciding on materiality. Their views on materiality may differ from those of shareholders and other stakeholders so it may be appropriate to set some minimum standards in this regard.

The Principles of 'Strategic focus' and 'Future orientation' would seem to be addressing the same issue and hence there is scope to combine these two Principles into one. This would then flow through into the Content Elements i.e. 'Strategic objectives and strategies' and 'Future outlook' would be combined.

As a more general point, in order to make reports more useful, there is a need to move away from boilerplate disclosure, particularly in the areas of risk and audit reporting. The challenge, in moving towards this more open style of disclosure, is to reduce the risk of litigation, something that is a key concern in a number of jurisdictions. If this cannot be overcome, a more open style of disclosure will be difficult to achieve.

What will Integrated Reporting mean for me?

Q9. From your perspective: (a) Do you agree with the main benefits and challenges are presented in the Discussion Paper? (b) Do you agree that Integrated Reporting will drive the disclosure of information that is useful for integrated analysis?

We would agree that there will be benefits to investors. The provision of 'connected information' and improved comparability are particular positives from our point of view. With regard to the benefit of 'improved analysis' by both sell-side and buy-side analysts, we would like to make a distinction between the position of shareholders or investors and that of buy-side analysts. As stated previously, shareholders are generally there for the long term and concerned that the value of their investment will steadily increase over time. Therefore, they want to assess stewardship and use the information to hold the board to account. Sell-side analysts are primarily interested in information that can help them in short term economic decision making and analysis and are less concerned about stewardship. Useful corporate reports should balance information for economic decision making and stewardship.

We would also like to highlight a further challenge presented by Integrated Reporting. Auditors play a crucial role in providing assurance to shareholders as regards financial reporting but, to date, they do not generally provide such verification and assurance in relation to management commentary even though, in their audit work, they could be aware of matters that may contradict the information given in this commentary. Consideration needs to be given as to how they could provide an appropriate form of assurance for narrative reporting within the Integrated Reporting Framework. In addition, the role of Audit Committees as a provider of independent oversight and assurance needs to be emphasised in the Integrated Reporting process. It would seem advisable to establish an early dialogue with Audit Committees to discuss this.

We trust our comments will assist the IIRC in taking forward this important project.

Yours sincerely



Alison Kennedy
Governance & Stewardship Director
Standard Life Investments