

Feedback to the International Integrated Reporting Council (IIRC) on the Integrated Reporting Prototype Framework Working Document

Name: David Korten

Email: dkorten@bainbridge.net

Stakeholder Group: Nonprofit organization

Organization name: Living Economies Forum

Industry Sector: Public Interest

Geographical Region: North America

I submit these comments at the suggestion and request of Bob Massie. These are relevant credentials:

Dr. David Korten earned MBA and PhD degrees from the Stanford University Graduate School of Business and is a former Harvard Business School professor. He is the author of the international best seller *When Corporations Rule the World*, *Agenda for a New Economy: From Phantom Wealth to Real Wealth*, *The Great Turning: From Empire to Earth Community*, and *The Post-Corporate World: Life after Capitalism*. He is co-founder and board chair of YES! Magazine, co-chair of the New Economy Working Group, president of the Living Economies Forum, an associate fellow of the Institute for Policy Studies, a member of the Club of Rome, and a founding board member emeritus of the Business Alliance for Local Living Economies.

I strongly support efforts to assess and report corporate impact on the non-financial capitals that define the true wealth of society. Yours is a bold effort. It is, however, highly corporate centric and unfortunately falls far short of the need. I offer these observations for your consideration:

1. The report speaks only of the corporation's contribution to creating value. There is no recognition of the possibility that from a societal perspective a corporation may be a net destroyer or expropriator of value. There is need to make a clear distinction between creating value for the corporation and its shareholders and the generative creation of value for the society.

In an ideal world, creating value for the corporation and creating value for the society would be interconnected and complementary. This interconnection and complementarity is characteristic of healthy, self-organizing, self-balancing ecosystems that self-organize in ways that balance individual and community interests. Unfortunately, economic structures that hold corporations primarily answerable to financial markets that value only short-term financial return virtually preclude such self-balancing.

2. The diagrams in the report attempt to address the corporation's impact on capitals external to the corporation. The examples provided in the report to illustrate this impact, however, focus on capitals internal to and controlled by the corporation for the benefit of its owners. Perhaps the report includes examples focused on the corporation's relationship to and impact on the total capital stocks of the society on which the well-being of all depends. If so, I missed them. The societal stocks are the critical capital stocks from a societal perspective and the corporation's overall contribution to or burden on the society depends on its net contribution—positive or negative—to them.

The thrust of the reporting initiative implies that its concern is with value creation for the society. If I correctly followed the implementation, however, the business model presented equates the corporation's success in expropriating the capitals of the society into its internal capitals as contributions to societal value creation. This is a serious misrepresentation that if not corrected could result in a major setback for efforts to address the dysfunctions of the existing economic system. It is essential to be clear, "Value creation for whom?"

3. If the intention is for corporations to report their contribution to the human-systems/natural-systems ecosystem in which they operate, their results must be reported within an interactive territorial or place based community ecosystem model. Generative flows in healthy living systems are predominantly closed loop. The diagrams of the "organization's value creation process" presented in your report, however, are linear.

I suspect it may be a basic rule that it is not possible to assess the corporation's net contribution or cost to an ecosystem with a linear model focused on the interaction among capitals internal to the corporation, a point I elaborate below under the discussion below of "The Corporation and the Community."

Of course if the intention of the report, however, is only a more comprehensive accounting of value creation for the benefit of shareholders, then this should be made explicit to avoid confusion and misrepresentation.

4. Paragraph 2.23 on Ownership of Capitals touches on the question of ownership. The observation that "Not all capitals that an organization uses or affects are owned by the organization" may be one of the great understatements of all time. Paragraph 3.21 picks up on this, suggesting that a corporation may voluntarily accept stewardship responsibility for its impact on the community." This assumes that a corporation can choose to be a responsible citizen. It skirts the question of whether a publically traded corporation subject to the relentless demand from financial markets to maximize short-term share price has the option to be a responsible citizen if that comes at a potential financial cost to shareholders.
5. The reporting framework seems to be a kind of self-scoring system. This is rather like asking a company rate its own bonds—or hire an accounting firm to certify a

rating of the hiring company's choice.

6. It is not evident that there has been any operational test or implementation of the proposed framework in any individual corporation to test its workability and validity. The caveats in paragraphs 2.23, 2.24, and 2.25 of the integrated reporting draft acknowledge the difficulty for the individual corporation, but dodge the bullet by leaving it to those preparing the report to sort it out. This suggests that corporate officers who say, "Just give us the rules" have a point. Those presenting the principles have not demonstrated that it is possible for the individual corporation to implement them. I'm curious whether the committee can point to any example of a corporate report that fulfills the principles spelled out in the draft report.

The Corporation and the Community

There is a critical distinction between the interests of the corporation and the interests of the community [defined as function vs. territory by Jane Jacobs]. Place-based communities are territorial and include all capital stocks within their territorial boundaries. The corporation is functional and is only one of many players that have an impact on the generative processes of the human-natural systems of the territory in which it operates. Separating out the impact of an individual corporation on variables it may influence, but does not control, becomes extremely difficult. It is likely impossible in the absence of an accurate and comprehensive model of the generative flows and stocks of capital of the entire external territorial system in question.

The challenge this poses for assessing the impact of an individual corporation brings to mind the Carl Sagan quote that "To bake an apple pie from scratch, you must first create a universe."

To produce an integrated corporate capitals report that deals with corporate impact on the capitals of the society, you must first create an integrated community capitals report for the territory in which the corporation operates. Real capital accounting from a societal perspective is possible only on a territorial or place-based community perspective.

I'm suggesting here that quite apart from political considerations, *it may be technically possible for an individual corporation to fulfill the intent of the Integrated Reporting initiative only within the context of a true global reporting initiative providing an overall assessment of the generative stocks and flows of Earth's biosphere.* In the absence of such a global report, any corporation that truly seeks to provide an honest and accurate assessment of its impact on the real capital stocks of the society would need to first create the global report—which is not credible, realistic, or efficient.

My point here is to suggest that the task you are undertaking is far larger and more complex than what the draft report suggests.

Perhaps one benefit of the integrated reporting proposal is that as corporations attempt to comply, the need will become evident for a comprehensive community-based societal capitals accounting system for the global territorial system in which they operation. Best, however that this be recognized and addressed up front,