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Consultation draft of the International <IR> Framework

Key Points

- econsense **appreciates the efforts of the IIRC** to develop a framework for integrated reporting and the invitation to provide feedback on the <IR> Consultation Draft (April 2013). Through its member firms and through meetings with the IIRC (e.g. November 2012 in Berlin), econsense has been monitoring the development of the <IR> concept with great interest. Based on discussions in the econsense working group on sustainability reporting, we want to briefly comment on the <IR> Consultation Draft and mirror it with observations of integrated reporting in German business and beyond.
- Sustainability reporting has turned into a dynamic, heterogeneous field. Several voluntary initiatives (e.g. the GRI, SASB, or the German Sustainability Codex) are competing for attention of reporters and users of sustainability information. At the same time, regulators around the world are tightening their grip on reporting of non-financial information. In our view **the development of the <IR> Framework could be more closely aligned with these developments**. While recognizing the recent efforts of the IIRC (e.g. the recent MoU with GRI), it is our impression that the alignment of the actual Guidelines/Frameworks of for instance the IIRC and GRI could be strengthened further. This could include a common definition of key terms and processes as well as a common understanding of the target audience of sustainability publications or the role of financial vs. non-financial information. Moreover, it includes a convincing concept how the different approaches fit together and – if intended – complement each other.
- Besides aligning with other voluntary reporting initiatives, the IIRC should clarify the **relation of <IR> with regulation governing the statutory "management report"** ("Lagebericht"). Regulators in Germany/EU, but also in other parts of the world are in the process of defining rules for non-financial information to be integrated in the "management report" (see e.g. proposal on non-financial reporting by the EU Commission or the DRS20 in Germany). Is the <IR> Framework a blueprint for the statutory "management report" of the future? Or put the other way around: does a thoughtfully prepared "management report" (e.g. including material non-financial aspects) provide investors already with sufficient information about a company's long-term value creation potential?
- We observe a curious **divergence of the reporting practice of many pioneering integrated reporters from what is proposed in the <IR> Consultation Draft**. Many of these companies are working towards an integration of their sustainability and financial report with the aim of producing "one report" or at least a consistent "reporting approach" to all its stakeholders. The <IR> Consultation Draft, however, asks companies to create an additional document for the providers of financial capital. The proposed procedure could have adverse consequences for the efficiency/workload of reporters. Moreover, by proposing a narrow-focused additional report, the IIRC seems to give up on providing a grand design for the future of corporate reporting.

- The **narrow focus of <IR> on the providers of capital** during materially analysis is controversial. Our expectation towards the IIRC would be a more inclusive, stakeholder-oriented framework beyond the current shareholder orientation (see also Q11). Only if the mere aim of the <IR> project is to increase awareness in the capital market for the role of sustainability information for long-term value creation, the current narrow focus might be appropriate. But we do not believe that this is or should be its mere aim.
- According to the <IR> Consultation Draft, reporting companies shall include **all material risks and opportunities for their future value creation potential in a brief report**. Some have argued that such a report should not exceed 30 pages. In our view this is a very ambitious - and in many cases even highly unrealistic - goal. As a matter of fact, we have seen few – if any – successful examples for such a report as of today.
- **Forward–looking information** (in an integrated report as well as in other reporting formats) bears risks for companies related to liability, reputation, etc. The <IR> Framework should provide more guidance on this important issue.

Chapter 1: Overview

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

- econsense welcomes the principle-based approach of the <IR> Consultation Draft for the flexibility it offers to reporters. The principle-based requirements of the current draft seem to be sufficiently comprehensive and reasonable.

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

- The fact that the respective paragraphs address the issue of interaction with other reports is highly appreciated. Here the authors should offer a grand design for corporate reporting – or at least be very precise about their vision.
- However, in our view the <IR> Consultation Draft does not provide this grand design. It departs from the idea of streamlining corporate reporting by proposing an additional standalone document on top of existing (financial/sustainability) publications. This leaves the reader with the impression that the *actual* integration of corporate reporting is still an open task.
- The <IR> Consultation Draft states that duplicate content in reporting should be avoided by all means. This is, however, difficult to imagine in a scenario where a company publishes an integrated report, a financial report, a sustainability report and additional publications. In many cases, this will increase rather than decrease the workload for reporting companies.
- The reporting practice of many pioneering integrated reporters differs from the <IR> Consultation Draft in an important aspect: many companies are currently working on an integration of their sustainability and financial reports ("one report"), whereas the <IR> Consultation Draft views the integrated report as an additional standalone document. We believe that for practical purposes it can make sense as a first step to merge existing publications and enrich the

"management report" ("Lagebericht") with material nonfinancial information before (or instead?) aspiring a standalone <IR> report.

*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?*

- Greenhouse Gas Protocol (GHG Protocol)
- GRI Sector Supplements

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

Chapter 2: Fundamental concepts

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

- The concept of the six capitals is a helpful – although not entirely new – approach to corporate value creation.
- However, the concept described in the <IR> Consultation Draft might be too academic for many practitioners. More guidance for reporters and in particular practical examples would be helpful. The IIRC Background Paper on the capitals – although helpful – cannot provide this. The authors of the final version of the framework should ensure preciseness and clarify also in other parts of the framework. The current draft has some weaknesses in this regard.
- Of course there is also a limit to how much guidance is desirable. We would propose to aim at striking a balance between the currently insufficient level of practical guidance in the <IR> Consultation Draft on the one hand and the guidance-overload in some parts of the GRI G4 guidelines on the other hand.
- Maybe the greatest challenge with the capitals is their measurability and comparability due to missing metrics or functioning "market mechanisms".
- Note: The IIRC should take into account that the term "capital" will not be regarded as adequate in many contexts and by many readers – e.g. when referring to employees.

6. Please provide any other comments you have about Section 2B (the capitals)?

*7. Do you agree with the definition of **business model** in Section 2C? Why/why not?*

- More precise guidance would be required on what exactly is meant by the term "value creation". It seems to us that different actors have different concepts in mind when talking about "value creation".

*8. Do you agree with the definition of **outcomes** in Section 2C? Why/why not?*

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).

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

Chapter 3: Guiding Principles

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

- The focus of materiality analysis mainly on the providers of financial capital is controversial. The proposed approach is not sufficiently "integrated" itself. If <IR> puts the entire business environment of a company into focus, this approach should also apply for materiality.
- Our expectation towards the IIRC would be a more inclusive, stakeholder-oriented framework beyond the current shareholder orientation. Only if the mere aim of the <IR> project is to improve the awareness for sustainability information in the capital market, one might argue that the proposed narrow focus is appropriate. But we do not believe that this is or should be its mere aim.
- We believe that a reform of corporate reporting cannot succeed without taking into account the information requirements of different stakeholders and without taking the sustainability community on board. Weakening the acceptance of the <IR> Framework in most communities other than the capital market right from the start does not seem to be a promising strategy.
- The description of materiality analysis in the <IR> Consultation Draft might still be too theoretical. Practical guidance and examples are lacking. For example, what happens if no consensus can be achieved on whether a specific risk or opportunity is material for a reporting company? Given that materiality analysis is at the heart of drafting an integrated report, it deserves more attention in the <IR> Consultation Draft.
- The issue of "connectivity" of material information in the report would also require more practical guidance.
- Performing an entire materiality analysis "at least annually" might be overly resource intensive. One might also argue that it contradicts the focus on long-term value creation, since the drivers of long-term value creation are unlikely to change annually. Nevertheless companies should report on their approach to review and monitor materiality.
- And finally, the materiality process/approach of the IIRC is based on a different logic than the one of the GRI G4 Guidelines. This should be made transparent in order not to confuse reporting companies AND readers of their reports

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

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

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

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

Regarding Section 3F "Comparability":

- The content elements in Chapter 4, which are to be disclosed by all reporters, allow for some degree of comparability – at least for certain standard disclosures.
- In terms of disclosure on corporate sustainability performance, the flexibility provided by the <IR> Consultation Draft is appreciated. This is particularly true for the proposal to select "*quantitative indicators commonly used by other organizations (…) (e.g. industry bodies)*". There is already a lot of activity in the market with regards to sector-specific indicators (e.g. GRI sector supplements, SASB sector KPIs, etc.). Therefore we do not see the need for the IIRC to come up with its own set of indicators in order to ensure comparability of reports.
- Nevertheless, since a minimum level of comparability of reports in a particular industry is essential, the recommendation to reporting companies which indicators to use could be a bit more binding as currently proposed in the Consultation Draft.

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).

Chapter 5: Preparation and presentation

*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?*

- A statement signed by a senior – or even the highest – governance body of an organization will not automatically improve the quality of reporting. If sustainability has not reached the desks of the Board members until now, a signed report will not "produce new relations".
- Moreover, one may argue that a *real* integration of corporate reporting would automatically include such a statement since it is common practice in financial reporting.

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

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

- In case of an additional standalone <IR> publication as proposed by the IIRC: If a reporter decides to obtain external assurance, it should cover the whole report rather than specific aspects in order not to contradict the purpose of integration, connectivity, conciseness and consistency

- However, when it comes to the integration of existing (sustainability/financial) publications, the question of assurance is much more difficult. When parts of the previous sustainability report are integrated into an annual report, they will be part the audit statement. When additional information is provided in other formats (e.g. the internet), an external assurance is possible but not necessarily required.

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.

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 B] in your answer to question 11 above rather than here).

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?

- Please see introductory statement ("key points").

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?*

- Collection of practical examples
- Materiality analysis
- Assurance

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