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).

Comments should be submitted by Monday 15th, July 2013.

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

Organization name:	BDO International Limited
Industry sector:	Financials
Geographical region:	Global

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.

12 July, 2013
Mr. Paul Druckman
Chief Executive Officer
International Integrated Reporting Council

Dear Mr. Druckman:

BDO is pleased to have the opportunity to respond to the Draft International <IR> Framework ('the Framework'). We continue to support the IIRC proposal to move to <IR>, particularly for larger, globalised businesses where such a reporting model would provide better information to users of the report.

In our view, the Framework should be focused on achieving consistency and comparability of integrated reports across boundaries and jurisdictions whilst, at the same time, 'cutting clutter'. The Framework has taken a positive step towards achieving this objective.

We strongly believe that <IR> should result in an enhancement of the communications currently produced by companies, rather than being an additional burden. This will depend upon the current reporting requirements in each jurisdiction. Some risk remains, however, that adoption will result in a combined report-- one that brings together financial, sustainability, and other reports without the linkages that would be embodied in an integrated report. We believe it is up to each organisation to best apply the principles to avoid unnecessary 'clutter' and duplication.

We see the key benefit of best practice adoption being open and transparent communication between a company and its stakeholders, and very much welcome the spirit of <IR>.

The Framework is a good base for the Pilot Programme to continue adopting and innovating report content and style. It also allows further consideration by all stakeholders and how their needs should be addressed. In that regard, we would like to see specific development in the following areas:

1) Stakeholder needs

The Framework assumes that providers of financial capital are the primary users of the report. However, large multinationals, privately-owned SMEs, not-for-profit entities, and other organisations are likely to have very different forms of capital, business models, and indeed primary users, who may not be providers of financial capital. In that regard, the Framework should eventually reflect the needs of the broad range of stakeholders in various types of organisations.

2) Competitive harm

A key ingredient of a valuable integrated report is the completeness of the information included therein. However, the Framework allows for organisations to opt out of including any narrative that may result in commercial harm. We consider this to be in conflict with the principles on which the Framework is based and are concerned that necessary disclosures will be omitted under the pretence of competitive harm. To address this we think that specific guidance should be provided on what constitutes competitive harm.

3) Creation of an assurance model that would allow users to gain the most benefit

An assurance model should add credibility and reliability to an integrated report. However, there is a need for assurance standards to be developed to deal with the requirements of <IR>. Assurance providers will also need to adapt to be able to provide an integrated assurance report and this will include improving their skills in understanding the nature of capitals and their relative importance in value creation.

We expect that many users of <IR> would welcome the Framework providing guidance on which elements of the report are conducive to targeted high level assurance reporting (e.g. KPI's) and which elements may be covered by a lower level of assurance (e.g. negative assurance). This multi-layered approach may be the most practical in the short-medium term.

4) Application of the Framework to smaller entities, in the longer term.

Whilst the concepts of reporting how an organisation creates and sustains value are appropriate to all entities, the Framework structure as it currently stands is not well suited to SMEs. Therefore, we would caution against application of the Framework by SMEs until further guidance is provided.

However, where these enterprises have stakeholders that require <IR> or if they have the ability to report under <IR>, then they should be encouraged to do so. For example, we envisage SMEs adopting <IR> where they are part of a supply chain or industry where <IR> is generally adopted by other similarly situated entities.

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.*

Paragraph 1.12 allows organisations to exclude material information on the grounds of 'competitive harm', subject to disclosure of such exclusion and the underlying reasons. This exclusion, if retained, increases the risk that organisations will misuse it in order to avoid adverse disclosure under the pretence of competitive harm. If this provision is retained, then guidance should be provided as to what would likely constitute genuine and valid competitive harm. In practice, companies should be able to provide a description of material matters at an appropriate level without compromising sensitive information in most circumstances.

Paragraph 1.12 also requires companies to provide details of steps being taken to obtain data that was unavailable and resulted in the omission of information in a material area. In such circumstances, a company should be required to explain the extent to which the absence of such information has or may impact upon the strategic management of the business. Exclusions of this nature would be likely to raise concerns for providers of financial capital; therefore, management should be required to justify why any such exclusion has not had a detrimental effect on the ability of management to make appropriately informed strategic decisions. The Framework should also provide guidance for instances where data is unobtainable and where management cannot rectify this.

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?*

Yes. The principles-driven approach allows logical incorporation of the integrated report with other reports and communications and we consider that such flexibility is required to accommodate the multiplicity of situations that can arise. Consistent application of the principles in communications throughout the year will benefit all users of the report. However, there may be some challenges for organisations to achieve consistency in communication through the style and content needed for different communication channels.

The key risk regarding the interaction with other reports is if the end result of application of the Framework is a 'combined' report-- one that brings together financial, sustainability and other reports without the linkages that would result in an 'integrated' report. We consider the reduction of duplicate content to be a critical factor in the evolution of <IR> as large companies are frequently subject to onerous and extensive reporting requirements, much of which has resulted in reporting that is overly lengthy and complex, providing little benefit to the intended users. Accordingly, we believe that Relevance should be added to the guiding principles.

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?*

Financial measures should be based upon International Financial Reporting Standards to provide consistency with the audited financial statements and information presented to the providers of financial capital. Reconciliations between any non-GAAP measures and International Financial Reporting Standards should be provided.

Non-financial measures should, depending on the area of focus, be based on the latest research and guidance from credible bodies, including the Global Reporting Initiative (GRI), United Nations Finance Initiative (UN-FI), Carbon Disclosure Project (CDP) and The Economics of Ecosystems and Biodiversity Board (TEEB).

If such a database is created it should be made clear in the Framework whether its use is mandatory or recommended.

Other

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

Paragraph 1.8 states that providers of financial capital that take a long-term view are particularly likely to benefit from <IR>. This creates the impression that short-term investors (the great majority of investors) are likely to benefit less. It also implies that long-term value creation is more important than short- or medium-term value creation and that a long-term value horizon is needed to align value creation across all capitals. This seems to be inconsistent with other assertions in the Framework, which provide that an integrated report should provide insight into the organisation's strategy, and how that relates to its ability to create value in each of the short, medium- and long-terms.

Paragraph 1.9 states that the assessment of performance or the quality of an organisation's strategy is the responsibility of the users of the information. This responsibility should also be assigned to those charged with governance, as they retain a primary responsibility to assess and report material information.

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?

Yes. We believe that the use of the standard categories will provide consistency and allow comparability for users. The use of capitals in the wider sense will focus organisations on considering the business model, risks and opportunities in a more holistic and structured manner, rather than primarily through short-term financial performance.

Our experience suggests that whilst reporting exists in areas such as sustainability and health and safety, these areas frequently receive less Board level focus and operate in silos within organisations.

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

As we have discussed above, the approach to the capitals is considered to be appropriate. However, we believe that certain of the capitals are more subjective than others (e.g. Social and Relationship capital) and some capitals cover an extremely broad spectrum (e.g. Natural capital). There is a risk that the very nature of these capitals, as well as the subjectivity inherent in them, may create excessively voluminous content rather than concise messaging, which could also result in a tendency for organisations to over-emphasise the more narrowly defined/tangible capitals.

We suggest that the following may be considered for inclusion under Social and Relationship Capital in Paragraph 2.17: (1) an entity's ethical considerations (especially around anti-corruption and bribery) and (2) reference to indigenous populations/land-owners as stakeholders.

For completeness, we suggest that the judgements applied in deciding not to report on any capital should be explained in order that the user can understand how an organisation has taken into account stakeholder needs when considering material areas of capital.

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?

Yes, in that it conforms to many established definitions. However, it appears to be static in its nature, capturing the business model at a point in time and excludes possible changes in future direction or options available. In practice, a business is a continuously evolving and flexible system of inputs, business activities etc. to deliver against a given strategy and objectives that are shaped by the environment.

Accordingly, a key aspect of an effective integrated report should involve providing information regarding the extent to which the business model evolves over time and has the flexibility to adapt to change, whether through need or choice.

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?

Yes. In particular, we agree that the positive and negative consequences should be objectively described.

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)?

Paragraph 2.28 describes the need to explain how inputs relate to capitals. Describing these relationships appears to represent a key challenge. The nature of the relationships within (rather than just between) some of the capitals is potentially complex and inter-woven, and guidance will be required to assist organisations in identifying and describing their key relationships in order to achieve conciseness and completeness in line with the guiding principles.

Paragraphs 2.32 and 2.33 are likely to be perceived as commercially sensitive, so this may be an area where certain information is withheld by organisations.

Paragraph 2.36 refers to the consideration of capitals owned more broadly than an organisation's boundaries. This is relevant to some of the capitals (e.g. carbon emissions) and for certain industries (e.g. retail, where the supply chains are an integral part of the outcomes). We would welcome further reporting relating to these areas.

Other

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

We believe that there is a lack of detailed guidance in the Framework regarding multi-segment businesses. Paragraph 4.24 provides a brief acknowledgment of the challenges posed by such businesses, but disaggregated disclosure may result in excessively lengthy reporting that loses its impact with users.

Section 4E should explicitly include details regarding material changes in the business model during the year and material anticipated changes. In contrast, the proposed disclosure focuses on the business model at a point in time.

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?

We agree that the approach to materiality should normally be from the viewpoint of providers of financial capital (which corresponds with the approach taken with respect to financial statement materiality). In that regard, we believe that this viewpoint should be evaluated by those charged with governance, based on what they assess as material from the perspective of intended users. We agree that the materiality determination process should be described (Paragraph 3.28), with particular consideration given to the stakeholder communication process and any issues that have arisen directly from it. Consideration should also be given for those organisations where providers of different forms of financial capital (e.g. investors and lenders to a company) have diverse perspectives or where conflict arises, or where the creation of value in one capital erodes value in another.

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

Restricting the integrated report to material matters is critical as it will help improve the quality of reporting and minimise the volume of irrelevant and unhelpful disclosures. This is consistent with initiatives within the financial markets, in which there is significant focus on reducing unnecessary disclosure.

Consideration should be given to how management and those charged with governance will be protected from omission of matters considered material by other users, for example through the explicit statements in the basis of preparation of the integrated report and a safe harbour provision to be provided by applicable lawmakers or regulators.

Paragraph 3.25 indicates that determining materiality involves identifying matters that 'could' have a future effect. This implies that matters should be identified and considered even if they are remote, which seems to create the potential for excessive disclosures. Also, Paragraph 3.27 states that to be most effective, there should be regular engagement with the primary intended users of the report. This may be impractical, particularly in light of liability concerns.

Finally, in section 5.11, the use of the words 'large' and 'small' does not sit well when defining materiality. These terms are vague and can lead to ambiguity around qualitative explanations.

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?

Given the subjective and qualitative nature of much of the report, providers of financial capital are likely to treat it as being reliable if it is clear that it is presenting information in a balanced manner, and the information is consistent with the communications those users receive from the company during the year.

Reliability can be demonstrated, to a certain degree, by describing the process used in developing the information, including the source of the information and the internal reviews performed in line with governance policies. In that regard, 3.32 uses the term 'ensure reliability' and we consider that this should be toned down since reliability cannot be guaranteed. In addition, reliability will be demonstrated through transparency and consistency in application involving boundaries, methodologies, calculations and judgements.

External independent assurance can also demonstrate reliability. However, because of the qualitative nature and subjectivity of much of the information presented in the reports, a high level of assurance on the entire integrated report is likely to be unachievable. In that regard, standards need to be developed for the performance of <IR> assurance engagements, which may result in different levels of assurance or some other form of association provided on different elements of the report.

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

Paragraph 3.42 states that it is not expected that an organisation will disclose information that will ‘significantly’ harm its competitive advantage. It is natural that organisations would be reluctant to harm their competitive advantage at all. For example, in our experience, UK Companies are already concerned that Mandatory Emissions Reporting will allow others to extrapolate data to identify production capacity and competitive performance and are worried about the implications this might have. <IR> may amplify that concern and any resulting lack of reporting will have an impact upon reliability.

Other

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

Paragraph 3.5 deals with care in providing future-oriented information to avoid boilerplate disclosures, e.g. those that are not tailored by participants for their own circumstances. However, there does not seem to be sufficient focus on the liability issues created by such information. In that regard, we would expect the Framework to mention the need for safe harbours to be created by the applicable lawmakers or regulators.

Paragraph 3.30 states that a reliable report is one that is ‘free from material error’. It would appear appropriate to extend the definition to ‘no material error or omission'.

Paragraph 3.33 refers to ‘no bias’. An element of bias is inevitable in any reporting and therefore this should be refined to ‘no material bias’.

Paragraph 3.37 states that completeness assessments include consideration of costs. Reporting should either be materially complete or not. The phrasing suggests that matters may be considered less material if the costs are high. Cost should not have a bearing on whether a matter is considered to be material. Rather, cost-benefit criteria should be assessed in developing the aspects of the Framework itself.

Paragraph 3.49 refers to qualitative and quantitative explanations in respect of significant changes. The guidance should indicate that the explanation needs to be provided for the historical impact of any significant changes and what impact this has on the forward looking elements of the report in comparison to the previous policy applied.

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).

Paragraph 4.7 mentions identification of the bargaining power of customers and suppliers. This is extremely sensitive information and could harm relationships. We consider that this is an example of what might well be considered valid ‘competitive harm' and suggest that it should be removed from the Framework.

Paragraph 4.9 refers to regarding the needs, interests, and expectations of the stakeholders. We consider this to be vague and would require significant interaction with the stakeholder groups, which may be highly impractical. The same paragraph also refers to companies providing details of the strengths and weaknesses of their competitors. From legal and business perspectives, this would appear to be a risky area for a company to provide commentary.

Paragraph 4.17 mentions disclosure of risks that could have extreme consequences even where the likelihood of their occurrence is quite small. This would seem to require disclosure of remote risks, which goes beyond the requirements for financial statement disclosures of uncertainties. We feel that this is highly impractical and could be misleading.

Paragraph 4.28 requires disclosure of quantitative indicators with respect to value drivers, opportunities and risks. It would seem to be impractical to develop quantitative indicators for much of this. Rather, it would seem that qualitative indicators would be more readily applicable. While Paragraph 4.32 mentions that sometimes it may not be practical to measure quantitative indicators, Paragraph 4.28 seems to create a presumption that anything short of quantitative is of lesser quality.

For Principal 4G - Future Outlook, we believe there should be a discussion of liability implications, including the need for a safe-harbour, when reporting on possible future performance.

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. Those charged with governance should make a statement of responsibility for the report, similar to statements made in respect of financial statements. This will help promote preparation of reports that are reliable and complete and subject to careful consideration by those charged with governance. In addition, it will form a necessary foundation for any assurance engagement.

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

None.

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?

Under current standards, it may only be practicable to provide a high level of assurance on certain aspects of the report, most likely the quantitative historical portions. Different levels of assurance (or some other form of association) may apply to other portions. Accordingly, new standards may be necessary to expand the circumstances where a high level of assurance can be provided. Experimentation by organisations and their assurance providers will help identify potential solutions.

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.

In our view, the Framework will make it impractical for auditors to provide the same level of assurance they provide on financial statements. It is important, therefore, for either the guidance in the paper to be tightened considerably to allow for some high level of assurance to be provided on at least some portion of the report, or for the assuror's association to be tailored to the circumstances (e.g. agreed upon procedures, negative assurance). As described in our Key Points section above, assurance teams will need to develop new skills to be able to provide any kind of assurance on the report as a whole, or certain aspects of it.

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).

Paragraph 5.28 refers to the reporting boundary, including entities over which the parent has control, joint control or significant influence. Whilst significant influence may exist, such influence would not provide the company with the ability to impose the necessary controls and reporting on these entities, unless they themselves prepare integrated reports. As such, the boundary should be limited to controlled entities and those entities over which the company has significant influence and that entity employs <IR>.

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?

Overall, we feel that the Framework is a valuable platform for continuing to pilot its use and for consideration by relevant standards setters and regulatory bodies. We recommend that the Pilot Programme continue whilst an assurance model is created. This will allow best practice reporting to be achieved and an assurance model created that is fit for purpose. Over time, it will be necessary to support the principles with guidance on preparation as well as sector- based guidance. However, until best practices are developed by industry leaders, any lack of guidance could result in boilerplate narrative.

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?

1. Materiality. The identification and reporting of material items is the fundamental basis of <IR>.

2. Capitals. Guidance relating to the relationships within and between capitals, in particular Social and Natural capitals.

3. Commercial harm. Guidance will be needed on the application of this ‘exemption’.

Other

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

Whilst the concepts of reporting on how an organisation creates and sustains value are appropriate to all entities, we would caution against its application to SMEs until further guidance is developed for these entities.

SMEs, which are often privately-owned and frequently owner-managed, represent key sources of job creation and innovation. Such enterprises are likely to be ill-equipped to implement a fundamental change in reporting without incurring significant relative costs associated with training and systems implementation. The costs, in both monetary terms and the demands on management time, risk reducing SMEs’ competitiveness.

However, in the event that SMes have external investors or lenders that require <IR>, we recommend that the needs of SMEs that elect to adopt <IR> are taken into consideration (e.g. the Framework should be scalable and specific guidance should be provided for them). Unlike existing reporting frameworks when the size of the entity often drives the complexity of reporting, the way in which <IR> is implemented is dependent on the industry and operations of the entity. This may eventually result in many smaller companies adopting an <IR> model as this will provide more meaningful information about the company and how it creates value. For example, companies operating in the brewing or clothing industries may choose to produce an integrated report due to the fact that brewing companies have very high energy and water impacts at the point of production and clothing companies tend to have complex supply chains with a high degree of commercial sensitivity.

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We appreciate the opportunity to comment on the Framework and hope that our comments and suggestions will be helpful to you as you deliberate on its evolution.

Please contact me should you wish to discuss any of these comments.

Yours sincerely,
BDO International, Limited
Wayne Kolins
Global Head of Audit & Accounting