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15 July 2013

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Dear Mr Druckman

Consultation Draft of the International <IR> Framework

Ernst & Young Global Limited, the central coordinating entity of the Ernst & Young organization, welcomes the opportunity to offer its views on the Consultation Draft of the International <IR> Framework (the Framework) issued by the International Integrated Reporting Council (IIRC).

We support the goal of the IIRC to create a globally accepted Framework to help with the development of more comprehensive and comprehensible information about organizations in support of a sustainable global economy. We acknowledge the innovative work and efforts of the IIRC over the past two years to develop the Framework as a first step in that regard.

Our overarching comments are discussed below. Our responses to the questions posed in the Consultation Draft are set out in the Appendix to this letter.

Direction of Integrated Reporting

We believe that the Framework is an important first step in furthering the debate around the future of corporate reporting and acting as a catalyst to simplify and harmonize current reporting regimes. However, the Framework needs to articulate a clear vision of the nature of integrated reporting, and, in particular, state its ultimate aim; otherwise, it is hard to envision how an integrated report would be truly different or significantly improved from existing corporate reporting in its broader context (i.e., financial reporting, including the annual report and other communications with stakeholders).

In our view, the integrated report could take one of two forms – and the Framework is unclear as to which form it envisages:

- The integrated report could provide a "map" to assist users in accessing the other reports prepared by the organization to communicate with its stakeholders – a brief strategic summary and signposting to the organization's financial and non-financial performance, primarily its financial statements and its sustainability report. In this guise, we suggest that the integrated report will add an additional layer to corporate reporting and, therefore, add to the overall reporting required from an organization.

- The integrated report could eventually replace existing corporate reports, and become the primary mechanism for reporting to stakeholders. We believe that this should be the ultimate aim of integrated reporting – to simplify the existing reporting requirements and reduce the overall reporting burden on organizations – and that the Framework should be transparent in this being its ultimate goal. However, we recognize that this will take some time, as it requires true innovation: "revolution not evolution". This goal would mean that existing and established international standard setters and regulators, as well as users of the report, need to be actively engaged in the debate, as changes would be required to both current reporting and regulatory regimes.

Many organizations already claim to prepare integrated reports. However, in the absence of definitive guidance from regulators, practice is varied. When integrated reports are produced within an existing regulatory environment (for example, by listed companies in South Africa which are required to do so by the Johannesburg Stock Exchange), they are often either additional to required communications or a combination of required communications so that the reporting organization can continue to comply with existing reporting requirements. The Framework should help to provide some structure for an integrated report, as well as consistency, comparability and connectivity of information. However, the lack of specificity in the Framework does lead us to question whether consistency, comparability and ultimately relevance can be achieved.

The Framework (in particular paragraphs 1.5 and 1.6) articulates the objectives of integrated reporting and who its primary intended users are. These appear to be similar to the equivalent concepts in International Financial Reporting Standards (IFRS), especially as they relate to the primary intended users and some of the qualitative characteristics of information such as reliability, materiality and comparability. To avoid confusion, we believe that it is important that the boundaries of integrated reporting be clearly identified and that the relationship with financial reporting and sustainability reporting be clarified.

Focus on providers of financial capital

The Framework states that its primary audience is "providers of financial capital". Although we question whether this focus may be too narrow, and whether an integrated report should ultimately be aimed at a broader range of stakeholders (insofar as they are relevant from a value creation perspective), we acknowledge that the providers of financial capital provide an appropriate starting point in the short term. We suggest that further research would be appropriate to determine whether the information needs of providers of financial capital are aligned with those of other stakeholders.

Despite the momentum gained by IIRC over the past two years, we are uncertain whether all providers of financial capital are completely convinced by the business case for integrated reporting. For that reason, we believe that the IIRC should continue to articulate the benefits of integrated reporting and gather empirical evidence which demonstrates that integrated reporting is what providers of financial capital want or need.

We also believe that the IIRC has an ongoing role to explain the value and benefits of integrated reporting to other stakeholders, such as investors, preparers, regulators, policy-makers and standard setters. As you will see from our response to Question 23, we suggest that one of the IIRC's most important tasks is to continue to make the business case for integrated reporting.

Implementing the Framework

The Framework, by its nature as a conceptual framework, is high-level and aspirational. It provides Guiding Principles and Content Elements for the integrated report. However, it does not provide any application guidance – the detailed standards which underpin the Framework – to describe how to measure and recognize content elements or how to report on comparative information. For example, do the forward-looking disclosures in Year 1 need explicit restatement or explanations in respect of actual outcomes in year 2? To use a financial reporting parallel, the Framework could be likened to the IASB's Conceptual Framework – but that Conceptual Framework is underpinned by the whole body of International Financial Reporting Standards to support its application.

In order to develop the underpinning standards for integrated reporting, we believe that it is important for the IIRC to work closely with established standard setters, and in particular, those that are internationally recognized and accepted. For example, to support the twin "pillars" or themes that co-exist within an integrated report, the IIRC should consider working closely with the International Accounting Standards Board (IASB) and the Global Reporting Initiative (GRI), to develop standards that support the implementation of integrated reporting.

In addition, although the measurement bases for financial reporting are well established, the measurement of environmental, social and governance factors is not as well developed. We therefore suggest that the IIRC should, as its next steps, encourage collaboration among existing standard setters and possibly regulators to develop appropriate measures for the components of an integrated report, and consider endorsing those that have been developed with appropriate due process and rigour. We recognize that the development of such measures is a significant undertaking, and therefore stress the value of using the experience gained by those organizations already exploring integrated reporting.

Assurance

The provision of assurance on integrated reports is a matter of considerable concern. Current practice is such that reasonable assurance is provided on financial information in annual reports, and that limited assurance is provided on aspects of organizations' sustainability reports. This "piecemeal" approach to providing assurance is understandable in an emerging area, such as sustainability reporting. However, it could result in the situation where assurance (of different levels) could be provided on parts of an integrated report, but with no assurance provided on the integrated report as a whole. This, in turn, could lead to users of the integrated report deriving unwarranted reliance on the assurance provider's report – who may infer that because parts of the report have been assured, the rest of the report is equally credible.

If integrated reporting becomes established, we expect that users would demand assurance on the integrated report and that they would expect an assurance report that promotes credibility of the integrated report in the global marketplace. However, as the Framework currently exists, the underlying concepts are too broad and vague and therefore not sufficiently robust to constitute suitable criteria against which to provide assurance, either on aspects or on the integrated report as a whole. We suggest that the IIRC should work with the International Auditing and Assurance Standards Board and the Professional Member Bodies of the accounting profession to address the question of assurance, including the development of appropriate assurance standards and suitable training for assurance providers. The background paper currently under development for the IIRC should provide a starting point for this ongoing discussion.

Future of the IIRC

The first version of the Framework is, as noted above, a starting point, not an end in itself. We hope that our letter has provided some contribution to the shaping of the IIRC's next steps, and that the IIRC will seek to collaborate with, and bring together, stakeholders in integrated reporting to develop a clearer vision of a future form of corporate reporting.

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Should you have any questions, please contact Karen M. Golz, Global Vice Chair, Professional Practice at 44 (0) 20 7980 0004 or via email at karen.golz@ eyg.ey.com or Juan Costa Climent, Global Leader, Climate Change and Sustainability Services at 44 (0) 20 7980 0268 or via email at juan.costacliment@uk.ey.com.

Yours sincerely

Ernst + Young Global Limited

Appendix – Responses to the consultation questions on the Framework

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.*

The principles-based requirements set out in the Framework appear to be appropriate, and we welcome the focus on applying judgment. However, the principles are conceptual and theoretical, and additional guidance and/or examples would assist organizations in applying them. We also have some specific comments on materiality (see our response to Question 11).

The Framework permits “competitive harm” (paragraph 1.11) as a valid reason for not applying all the principles-based requirements identified in bold italic type. Given that this is not considered a valid basis for not providing information under IFRS, we question whether “competitive harm” should be considered an appropriate reason for not complying with some aspect of the Framework.

The concept of value creation is sufficiently important to integrated reporting that we suggest it be defined at this point in the Framework.

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 (paragraph 1.18-1.20).

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

We agree that Integrated Reporting is a continuous process, and that its principles should be applied to all of the organization’s relevant reports and communications, including its internal management reporting and reporting to those charged with governance. A periodic integrated report is also appropriate, although we are concerned that this report will be seen by preparers as an additional reporting burden requiring additional effort and resources.

As discussed earlier in our letter, we believe that it is important that the IIRC complements material developed by established standard setters and others. It would therefore be helpful for the Framework to explain how existing standards – including financial reporting, corporate governance and sustainability reporting standards – align with the principles for preparing an integrated report. We also believe that it is important for the Framework to set out the IIRC’s longer-term vision for integrated reporting.

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 reporting, corporate governance reporting and sustainability reporting standard setters that are internationally recognized should be included. In particular, these should include the International Accounting Standards Board (IASB), the Global Reporting Initiative (GRI) and the International Valuation Standards Council (IVSC). The IIRC should emphasize the need for organizations to apply judgment in the selection of indicators or measurement methods from these authoritative sources so that they are relevant to the organization's particular circumstances.

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

   a) Section 1.3 indicates that an integrated report should be prepared in accordance with the Framework. As the Framework is not yet the only authoritative source over integrated reporting, it perhaps would be more accurate to say that in order for an organization to claim compliance with the Framework, an organization should apply all of the elements of the Framework. However, as it might be difficult for an organization to claim full compliance with all aspects of the Framework in the early periods of implementation, it may be appropriate to suggest transitional provisions.

   b) Section 1.6 indicates that an integrated report should be prepared primarily for providers of financial capital in order to support their financial capital allocations. As the Framework was developed with providers of financial capital as its intended users, and this would have driven the proposed content of an integrated report, we are unclear of the purpose of section 1.6 – is it to specify that the Framework may not meet the needs of other stakeholders?

   c) As a point of detail, it would be helpful to include a summary page containing all the requirements and content elements in the <IR> Framework, to help identify the requirements. For example, within the body text, some statements that are not written in bold italics also use "should", which for those familiar with other standard setters' requirements, might be construed as requirements of the Framework, and therefore a summary of the "true" requirements (i.e., those in bold italics) would be useful to preparers.

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?*

We agree with the approach taken in the Framework in identifying six categories of capitals.

It is possible that not all organizations will classify capitals in the same way. Therefore, we suggest that organizations should explain the composition of the various capitals they choose to disclose and that they "map" these back to the six capitals.

There appears to be some confusion in the Framework between the concept of capital and that of an intangible asset /resource. We suggest that the IIRC clarifies the difference between the concepts, in order to avoid unintentional “double counting” of capitals.

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

There were a number of points in Chapter 2B that we found to be helpful guidance for users of the Framework, namely:

- It is helpful that both value-erosion and value-creation are mentioned, to counter-balance a perspective that an Integrated Report should only tell a “good news” story.
- The diagram on page 13 is helpful in contextualizing the other capitals within natural capital. We suggest that the accompanying text should also be in the main body of the Framework, as it makes an important point about how natural capital under-pins all the other capitals and also how the interaction of all the capitals collectively support the endeavours of an organization through its business model.
- It is helpful to point out that not all capitals are equal and that some may not even be relevant to an organization.
- It is wise to observe that not all capitals can be quantified or monetized and that narrative qualitative explanations may sometimes be the only option to describe an organization’s interaction with such capitals.

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?*

We agree with the definition. In addition, it would be helpful to provide a practical example of a business model, perhaps including a graphical representation, to support this section. This would help to provide a practical grounding for the concepts in this section of the Framework.

Similarly, it might be helpful to set out the process for developing an integrated report in more detail, as an example to show how the guiding principles and content elements might be applied.

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?

We agree with this definition, although we do find it unclear from whose perspective value creation / destruction (i.e., the outcomes) should be reported. It is possible to describe outcomes from the perspective of the organization, the providers of financial capital and/or other stakeholders. Given the connectivity between the capitals, and although it is possible that net value creation / destruction could be described, it is more likely to involve trade-offs between the capitals and the outcomes for different stakeholders. The boundary of the integrated report is therefore of great importance.

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 (Section 4E).*

No further comments.

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

We note that chapter 2 *Fundamental Concepts*, which we believe to be the most important part of the Framework, does not contain any words in bold italic type, which raises a question as to whether it might be perceived to be subsidiary to the wording in bold italic type. We suggest that the relationship between section 2 and the bold italic type be clarified.

We also note the following:

a) The Framework states "*An organization can create and maximise value by serving the interests of, and working with, all its key stakeholders, such as employees, customers, suppliers, business partners, local communities, legislators, regulators and policy makers.*" As discussed in our answer to Question 8 above, this statement may not always be true - trying to serve the interests of all stakeholders simultaneously is unlikely to happen in practice.

b) The Framework describes value drivers (paragraph 2.45), but it is not clear how this concept relates to the business model, capitals and value creation that has been discussed within the remainder of Chapter 2. It seems disconnected from the remainder of the chapter, and we suggest that it be challenged, and possibly deleted.

c) The Framework states that "*By communicating information that assists providers of financial capital to assess an organization's ability to create value over time, <IR> can support their decision-making, engagement and voting practices. It also supports broader societal interests by encouraging the allocation of financial capital to reward and support long term, value creation within planetary limits and societal expectations".* This paragraph could be expanded to explain how Integrated Reporting also enhances better decision-making within an organization. The allocation of financial capital by providers is only part of the story - they are also responding to how well an organization allocates its own capitals through its capital investment.

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 generally agree with the principles and leaving the final decision to be determined by senior management. However, more application guidance is required on the determination of materiality and the related disclosures in the integrated report.

Materiality is a topic that is of particular interest to institutions, regulators and standard setters, and consequently, considerable research and other work has been undertaken in this area. Rather than developing another definition of materiality, we believe that the IIRC should consider aligning, as much as possible, the definition of materiality in the Framework with the recommendations resulting from this body of work.

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

    a) There is a continued tension between the requirement for an integrated report to provide concise (paragraph 3.29) yet complete information, specifically as it relates to the statement that "*In achieving conciseness, additional detailed information can be provided separately, and linked to, other forms of communication, such as the organization's website*".

    b) The Guiding Principles do not include the notion of assurability (i.e., verifiability) as a qualitative characteristic of information, although paragraph 5.21 indicates that the Framework provides reporting criteria against which organizations and assurance providers may assess a report's adherence to the Framework. Some information (e.g., some future orientated information) may be more difficult to assure than information disclosed under traditional reporting frameworks. By excluding assurability as a qualitative characteristic of information, the Framework may inadvertently exclude the provision of assurance on the process followed by management to prepare the information (rather than on the information itself).

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?

We agree with the way reliability is formulated in the Framework. We believe that the organization's own view of reliability and completeness should be disclosed in the report. Further, we believe that those charged with governance (or senior management) should take explicit responsibility for the integrated report, although we recognize that management might be hesitant to take responsibility for forward-looking information in the integrated report.

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

The Framework states that, to help ensure that all material matters have been identified, the preparers should consider what organizations in the same industry are reporting on, as certain matters within an industry are likely to be material to all organizations in that industry. Although we agree that industry benchmarking is appropriate, sometimes this might not suffice, and the organization could also use external international benchmarks prepared by organizations such as the World Business Council for Sustainable Development (WBCSD) and the International Labor Organization (ILO).

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

No further comments.

Chapter 4: Content Elements

16. Please provide any other 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).

No further comments.

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, we believe that it is important to demonstrate accountability and transparency for the integrated report. In order for an assurance provider to assure the report or a part of it, the assurance provider would require a party (such as senior management) to take responsibility for the information being assured.

Paragraph 5.18 could form the basis of any additional requirements related to the responsibility of those charged with governance in respect of integrated reporting.

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

The definition of those charged with governance is not consistent with those commonly used by other authoritative international organizations, such as IFAC or ICGN. This may create confusion among preparers and users of an integrated report, and therefore we suggest that the IIRC consider aligning the definitions.

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?*

As we discussed earlier in our letter, this is an area that we believe requires considerable further research and poses significant challenges for assurance providers. Although the ultimate aim might be that assurance should be provided on the integrated report as a whole, we recognize that this is not achievable at present.

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.*

No further comments.

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).*

No further comments.

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?*

As we have explained in our letter, the content of the Framework overall is a helpful starting point. However, it needs to be underpinned by methodologies and measures that will help, over time, to provide a practical foundation for integrated reports. We believe that this will require taking the best of evolving practice among the Pilot Program participants and further developing it to provide robust standards for integrated reports.

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?*

a) Developing a common language, definitions, and consistent measurement principles and metrics by working together with IASB and GRI, i.e., further refining and providing more depth to the Guiding Principles. It is also important for organizations to have guidance on the Content Elements, to help them apply the <IR> Framework.

b) Demonstrating how an integrated report itself creates value for an organization and the providers of financial capital (i.e., the "business case") – convincing and educating the providers of financial capital is very important for the success of <IR>. We believe that the providers of financial capital are not yet completely convinced of the business case for integrated reporting, and are not therefore driving demand for integrated reports. Integrated reporting has gathered considerable momentum over the past two years, but it is important to maintain this momentum by continuing to demonstrate the soundness of the business case.

c) Assurance – please refer to our letter for our discussion on assurance.

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

No further comments.