

## ANALYSIS OF FRAMEWORK

### CHAPTER 2: FUNDAMENTAL CONCEPTS – BUSINESS MODEL (Section 2C)

#### OTHER

Question 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).

**NOTE:** This objective analysis includes only the most prevalent, significant or controversial issues as far as they relate directly to the content of the Consultation Draft of the International <IR> Framework<sup>1</sup>, for the attention of the Working Group and therefore not all matters raised in submissions are referenced in it.

Drafting this analysis involved considerable judgment in deciding how to categories comments into issues/themes and how to summaries the underlying positions. Statistics have been included to provide a snapshot and starting point for analysis. Although the statistics indicate the prevalence of different views, due consideration will be given to the substance of all positions expressed.

In total the IIRC received 359 submissions to the Consultation Draft. 352 are included in this analysis. The remaining 7 submissions (of which 6 were late and one was in too complex for collation) are being reviewed separately.

#### CONTENTS

A – Overview

B – Key / Major Issues

C – Other Issues Raised

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#### A – OVERVIEW

- A1 Of the 352 total comment letters received by the IIRC, only 133 (38%) of the respondents provided a feedback to Question 9.
- A2 Because question 9 asked for any additional feedback on any aspect of Sections 2C and/or 4F related to the discussion of an organization's business model, this question does not lend itself to a statistical analysis of those who were in favor (or opposed) to a particular concept. As such, the following analysis serves to highlight the major issues/observations raised by respondents, with particular focus being placed on common responses that were echoed by a number of respondents (Section B), and some other comments that were frequently repeated (Section C).

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<sup>1</sup> <http://www.theiirc.org/consultationdraft2013/>.

## B – KEY/MAJOR ISSUES

B1 Paragraphs 4.21 and 4.22 of the Consultation Draft introduce the concept of **'Resilience'**. This concept garnered a significant number of responses, as reflected by the following representative feedback:

- *"With regards to 4.21 of 4E: It would be interesting if greater clarification was provided in terms of resilience to what - Economic crises? Political conflict/unrest? Environmental crises? New legislation? Climate change? Resilience can be explored in a number of facets."*
- *"Too much emphasis is done on the word "resilient", which is especially important in downturns in the economic cycle but less so in periods of relative prosperity. We would favour integrated reporting also mention the "agility" and "dynamism" of the business model."*
- *"Requiring an entity to report generally on the resilience of its business model is not likely to be very helpful and risks boiler-plate statements instead of meaningful information. Instead, what might be helpful is to supplement the discussion of risk and opportunities in 4C with any further information which might assist users of the report to make their own assessment of resilience."*
- *"4.21 would require organisations not only to describe their business model, but also to say how resilient it is. We think that it will be very difficult for organisations to provide a useful answer on resilience, and so the temptation will be for them to give bland assurances that they are indeed resilient. Perhaps more fundamentally, it is the business's resilience that is important rather than that of its business model. Business models are constantly changing in response to changing circumstances and opportunities; this is an important part of how a business stays resilient."*
- *"The question of resilience overlaps with the financial reporting and auditing question of 'going concern'. This is currently under consideration in the UK, largely as a result of the financial crisis... Directors are able to take a clear view on their company's short term liquidity and solvency but the future is inherently uncertain. The longer the assessment period, the less confident directors can be.' Any reporting on resilience would face similar limitations."*

B2 Organizations with multiple business models (4.24 - 4.25) was another major topic of discussion in the comment letters. Many respondents stated a request for additional information and/or application guidance that will enable certain organizations (large, complex, multi-national, conglomerates, etc) to apply the Framework appropriately in their evaluation of business model(s).

- *"Paragraphs 4.24-4.25 provide useful comments on organizations with multiple business models. We suggest including a reference to multiple business models in the initial discussion/ definition of business model in 2.26."*
- *"If conciseness is a goal U.S. businesses are uncertain how the framework will be used when a company has complex and multiple business models and geographies. The framework needs to address this in the body of the text even if addressed in standalone documents."*
- *"We understand that the presentation of all business models on the Integrated Reporting does not fit with the concepts of relevance and materiality contained herein. We suggest that the other business models should be briefly presented and any additional information can be found on the external links."*

**B3 Focus on reporting at the corporate centre:**

- *"Paragraph 4.25 needs to address the needs of investors more clearly. We agree that an integrated report by a conglomerate should report on the business model of the corporate centre; however, disclosure relating to the business model alone may be insufficient in addressing all material risks facing the entity."*
- *"Our experience has shown that many such diversified or holdings companies have inadequate disclosure of information regarding its various business operations. ESG information is rarely disclosed and it is often difficult to find anything beyond the basic operational information. If the integrated report focuses only on the business model of the corporate center, we have a concern that this would perpetuate that problem."*
- *"Paragraph 4.25 should be tightened. I agree that for corporate centres acting primarily in investment management activity, the relevant business model is likely to be that for the corporate investment management rather than all the underlying investments. However, I believe the provision is a bit loosely defined and may leave some organisations to misinterpret it to avoid being transparent about their business models. I believe the provision is and should be an exception to the main provision in paragraph 4.24 and should only be available for truly diversified investment management vehicles."*

**B4 Respondents highlighted a concern that some of the guidance in the Consultation Draft that would enable an organization to demonstrate its 'resilience' could potentially lead to the disclosure of commercially sensitive information.**

- *"Increasingly detailed disclosure in areas like product differentiation and market segmentation, as may be expected by integrated reporting, could result in commercially sensitive information being released."*
- *"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."*
- *"While we would resist the disclosures in paragraphs 2.32 and 2.45 which could expose the organization to competitive harm, we recognize that, in the overview to the draft, relief is provided from disclosures that may cause such harm."*
- *"One of the biggest obstacles to companies adopting <IR> is concern that they will be giving away competitive advantage. Guidance is needed on how to report per <IR> objectives without losing competitive advantage."*
- *"We do not agree with disclosing how an organization differentiates itself in the market place if this could jeopardize their competitive position."*

**B5 Respondents commented that they would appreciate further development of the interaction between 'business model' and 'business strategy'.**

- *"An area of debate, on which the framework is relatively silent is on how the business model interacts with other content elements, particularly strategy, e.g. which comes first the strategy or the business model? In our experience many companies familiar with reporting on strategy find it difficult when adding an additional level of disclosure around business model. We would therefore encourage the inclusion of some guidance on the interaction between strategy, business model and other content elements."*
- *"There should be greater emphasis that strategy flows from business model; this will serve to increase understanding of the differences. Accordingly, in section 4E the order should be first business model and then strategy."*

**Question 9 – OTHER COMMENTS ON BUSINESS MODEL**

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B6 Respondents requested additional clarity regarding the incorporation of the Capitals into the discussion of 'business model' in an integrated report.

- *"The Framework should clearly state, on what grounds should a company include capitals in its business model. Taking into account the concept of "collective ownership", it cannot be based only on property right, which would be understandable. Thus, specific criteria are necessary."*
- *"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."*
- *"The Framework could usefully be enhanced by a discussion of the need to explain the inter-relationships of the separate elements of the business model as well as a focus on the related flows."*

B7 The respondents provided feedback on the use of figures/diagrams in the Consultation Draft, re: Figure 2 and Figure 3. In general, the feedback noted that some diagrams were confusing and, in some cases, seemingly inconsistent with the guidance in the Framework.

- *"Figure 3 is a synthesis of Figure 2 (the capitals) and the business model. However, it is positioned in the framework (on page 11) much earlier than the actual explanation of the business model in the text (page 14)."*
- *"Figure 3 introduces two new columns on either side that represent the organization, whereas in the previous figure this space was part of the external environment. Also, paragraph 2.9 says "Some of the capitals belong to the organization, while others belong to stakeholders or to society more broadly" (identified as society in Figure 3). However, Figure 3 seems to portray an exchange or transfer between the organization and society from all capitals."*
- *"The pictures in Figures 2 and 3 and the relevant discussions might create the perception that capitalism is something of the past, and that socialism now has the upper hand. It might be noteworthy to still discuss entrepreneurship and leadership and the provision of financial capital as prerequisites for the business model to work and for the creation of value /wealth through the processes."*

**C – OTHER ISSUES RAISED**

C1 Disclosure Requirements should be presented in a single section:

- *"It appears to contain a number of embedded disclosure requirements (e.g. paragraphs 2.29, 2.33 and 2.34). These requirements are both difficult to identify and add unnecessary detail to this section. Any disclosure requirements relating to the business model should, in our view, be included only in section 4E."*

C2 All presentation guidance should be included in Section 5:

- *"As for (4.23), the content presented in this item is related to presentation, thus, inappropriate to be included in Content Elements. If this content is really necessary, it should be moved to Chapter 5."*

## Question 9 – OTHER COMMENTS ON BUSINESS MODEL

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### C3 The use and discussion of innovation:

- *"The effect of innovation or the choice of technology in the Business Model is not really discussed. Those factors have a large role in the efficiency of any operations."*
- *"Point 2.33, about innovation, seems to assume that innovation is always good. Of course it is true that a lack of it would probably be a very bad idea. But change isn't always positive; what is important in integrated reporting is not only describing the company's approach to innovation and responsiveness to change, but how that innovation or change contributes to or detracts from sustainability."*

### C4 <IR> places a high reporting burden on report preparers:

- *"In the last bullet point to paragraph 2.28 the reporting entity is to 'explain how secure the availability...of natural capital is'. This asks a lot of an entity in the context of broader environmental, economic and political factors that may affect the supply of clean air, water, biological assets and land. However an entity can be reasonably asked to disclose its key assumptions and the basis for them about the availability of components of natural capital."*
- *"On 2.36: To start reporting on outcomes that are not influenced or controlled by an organization would be strange. It would only make sense if there is an outcome that is eventually recorded somewhere else in the value chain, but can still be directly linked to a particular business activity of the organization (and if the outcome would not exist without the organization's involvement). Otherwise it would almost be similar to governments reporting, next to reports on education, healthcare and law enforcement achievements, also on the number of sunny days in a country in a given year."*
- *"While the discussion is useful and appropriate to assist entities to develop more comprehensive business models, the cost may well outweigh the benefits in the short term."*

### C5 Are business models static or dynamic? Respondents shared differing views about the usefulness of annually disclosing information about an organization's business model in an integrated report.

- *"... note that the business model should be stable even for the long term and certainly not change every year. Therefore this content should probably become reference information on a website in support of all public reports and audiences, rather than forming a significant section of an annual stand-alone <IR>."*
- *"For most organisations, business models don't change radically annually. Should IIRC acknowledge that in year-on-year reporting forthcoming IRs may simply repeat if there are no significant changes in business model that have occurred during the last year?"*
- *"It would be good to include something about development and review of business models in this section. In conversation with people throughout our business and externally, the perception is sometimes that once a business model is agreed it is set in stone rather than the evolving process that it is."*