

Summary of comments on the 2011 Discussion Paper's coverage of the capitals

Supporting document to Background Paper "The Capitals" www.theiirc.org/resources-2/framework-development/background-papers

Statistics for responses to questions 6 in the IIRC's 2011 Discussion Paper can be summarized as follows:

	Agree	Agree with qualification	Disagree	Other*
Q6. Do you find the concept of multiple capitals helpful in explaining how an organization creates and sustains value? Why/why not?	70% (149)	6% (13)	2% (5)	22% (47)
	76% (162)			

* These respondents did not directly answer the questions, were undecided, or answered in a manner that was unclear whether they agreed or not.

This Appendix focuses on the issues and concerns that respondents raised with respect to the Discussion Paper's coverage of the Capitals. It does not claim to give a balanced view of respondents' comments and pays little attention to those comments that reinforced or elaborated on, in a consistent way, the coverage in the Discussion Paper. When reading this Appendix, therefore, it should be remembered that the figures above tell a reasonably convincing story of strong majority agreement from those who answered these questions directly with most of the Discussion Paper's coverage of the Capitals.

Summarized below are the reasons given for disagreement or for specifically qualifying agreement, as well as other significant concerns and issues noted by respondents:

- i) *Taxonomy and definitions: There were many comments on both the taxonomy used to categorize the capitals and the definitions of various capitals, including whether the categorization should meet the criterion of being "mutually exclusive and collectively exhaustive" which it does not currently do. Comments included:*
 - a) *The taxonomy differs from other better known ones (e.g., Adam Smith's classification, and SIGMA Guiding Principles) which may not be justified and may even cause confusion.*
 - b) *"We classify Intellectual Capital (IC) into three categories: Human Capital, Structural Capital and Relational Capital".*
 - c) *"Not sure how helpful the distinctions are between financial and manufactured and also between human, intellectual and social capitals".*
 - d) *"Under the heading of "Human capital" ... there is no discussion around leadership".*
 - e) *"We don't think the distinction between "Manufactured" and "Natural" Capital works well".*
 - f) *"Under Social Capital, the narrative talks about 'an organisation's social licence to operate'. We think that many businesses would fail to see how to address this and might consider it to be a value judgement on their activities".*
 - g) *"Capability, which means skills to use resources (sum of procedure and professional knowledge of a firm to produce products and services) is not covered, even though it is very critical to some organizations to create and sustain value".*
 - h) *"Why human and intellectual capitals are separated. Should they not be integrated".*
 - i) *"It may be useful ... to make a distinction between those (capitals) that can more easily be ascribed a value e.g., can be bought or sold, as opposed to more*

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- intangible capital such as reputation or employee skills and experience".*
- j) *"the six types of capital identified are clearly very different in terms of, for example, whether they are resources that belong to the business and whether they are measurable".*
 - k) *"further types of capitals, such as cultural capital, could be included in the existing categorization".*
 - l) *"need to separate intellectual capital from technological capabilities in the operating context".*
 - m) *"the 'three capitals' (social, natural and economic) has the advantage of simplicity, and roughly equates to People, Planet & Profit (triple bottom line mnemonics)".*
 - n) *"some capitals are at the macro-economic level (e.g., natural capital) and others at the organizational level (e.g., human and financial capital). In addition, some capitals appear to have been excluded (e.g., reputational capital)".*
 - o) *"the Discussion Paper appears to overlook the organization's own values and how those contribute to its performance and value creation"*
 - p) *"It must be noted that the silent stakeholder are still left out: animals, future generations, etc".*
- ii) *Untoward connotations, e.g., "... it does not provide an accurate view of the world, which cannot be reduced to a set of 'capitals' that exist to provide inputs to corporations. The notions of 'human' and 'natural' capital are particularly reductive. Human beings, human communities and ecosystems are not merely forms of capital provided to companies in order to be drawn down or built up. They have inherent value that cannot be quantified, and harm to them cannot be justified according to a financial materiality analysis. These realities are implied by the Discussion Paper's use of the terms 'human rights', 'stewardship' and 'eco-system health.' Nevertheless, conflicting messages are sent by the notion that natural capital, for example, is merely "an input to the production of goods or the provision of services." Also, "There is an implication from this approach that all capitals are of equal standing and equally important in the sustainability of an organisation. However, it could be argued that natural capital underpins other "capitals" and so a depletion or impact on natural capital can have a greater impact on long-term sustainability than depletion of other capitals."*
- iii) *Measurement and monetization:* Quite a few respondents commented on measurement and/or monetization: some assumed/suggested/questioned whether measurement of the capitals was necessary for the model to work, some assumed/suggested/questioned whether the IIRC would introduce KPIs/metrics, some questioned whether measurement was possible/practical/necessary/desirable, and some specifically commented on measurement in terms of money value (monetization or economic value). There was no strong, consistent theme coming through with respect to these comments, but it is clearly an issue that needs to be clarified.
- iv) *Control/ownership:* A number of respondents noted the fact that an organisation uses capitals that it does not own or control, which raises complex and significant issues, such as how to assess stewardship and performance, and how to determine materiality and boundaries (upstream and downstream).
- v) *Competitive disadvantage, e.g., "I am not sure (about the capitals) from a competitor standpoint. It would be good from an investor standpoint as well as risk*

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disclosure, but being transparent may force revealing sensitive information (on) which competitors may be able to capitalise." A number of other respondents mentioned competitive advantage as a hurdle that <IR> will need to jump.

- vi) *Economic connotations: "The challenge with 'multiple capitals' is its association with economic thinking and the danger of falling back into framing corporate reporting in terms of an economic conceptual framework. As the IIRC paper rightly shows, the most striking aspect of corporate balance sheets over the last few decades has been the growth of intangible assets. In economic theory this is described as 'total factor productivity' but is in fact a residual category, i.e. how to explain economic growth when all other factors have been taken into account. As long as 'multiple capitals' is used in this weaker, residual sense then it is of (limited) help in explaining how organisations create and sustain value. The central thrust of the IIRC project must be to encourage and respect multidisciplinary approaches to corporate reporting."*
- vii) *Capital v income: "The concept can be enhanced by considering the relationship between "capital" and "income", which illustrates the kind of product/service each kind of capital provides". A number of other commentators also noted the opportunity to explain the capitals in terms of "stocks" and "flows".*
- viii) *Flexibility, e.g., "the concept of multiple capital might be useful but should not be a straitjacket to bind each and every corporate to have to document how each type of capital is addressed". Several respondents also specifically agreed with the comment in the Discussion Paper that "the extent to which different organizations use or impact each of these capitals varies: not all capitals are equally relevant or applicable to all organizations".*
- ix) *Entrenching silos, e.g., "even with this division of capitals, we still run the risk of maintaining the segmentation of topics (financial, economic and social) without actually making the report integrated." A number of respondents also mentioned the importance of recognising the interdependence of the capitals and some specifically mentioned this in context the need to recognise trade-offs.*
- x) *Practicality, e.g., "I find the concept of multiple capitals intellectually helpful but practically confusing. It is of little or no interest to sell side market outside of pending liabilities/fines in conjunction to the five capitals use. I believe the use of capitals will not provide the envisioned breakthrough for developing or using reporting information". Similarly: "The capitals discussion, while interesting and used elsewhere in the past ... does not easily and intuitively translate into a vision of reporting that current reporters could readily embrace." Quite a few other respondents raised issues on the practical aspects of how the capitals concept would manifest in an integrated report. Interestingly, a number of respondents commented along the lines that the concept of the capitals "within business are universal, well understood and should be easy to apply within a common consistent framework", but a similar number made a contradictory claim, e.g., "As this concept of multiple capitals is not widely accepted or applied currently it would need to be clearly defined and explained so that directors understood their disclosure duties".*