CRO A
Corporate Responsibility Officer Association

CROA Input on IIRC Integrated Reporting Discussion Paper

The World has Changed – Reporting Must Too (page 5 of the Discussion Paper)

Q1. (a) Do you believe that action is needed to help improve how organizations represent their value creation process? Why/why not?

Yes, action is needed because:

- Currently the reporting focus is primarily on profitability and delivering return to shareholders, whereas it needs to support a wider perspective of the value companies bring to society. There are very few organizations today that do a good job of representing their value creation process through their reporting.
- The 10K in the U.S. and equivalents elsewhere do not provide the context or the narrative for anyone other than the most astute investors to comprehend the business model. Meanwhile, CSR Reporting detached from considerations of financial risk and other governance issues does not provide anything more than an isolated snapshot of a firm's "good works." A more standard integrated model would be useful.
- Too often, material environmental and social impacts are left out of financial reporting. At the same time, many sustainability reports give only a cursory discussion of the key drivers for their business. To ensure that externalities (i.e. the significant external factors that affect an organization) are included in the regulated disclosure for the business, the key will be showing the connections between financial, governance, environmental and social issues and how they affect the ability of the company to sustain itself over time.
- Organizations should have an efficient and consistent way to provide information to their various stakeholders on how they create value over time. If action is not taken, each stakeholder will continue to layer additional reporting and disclosure requirements on organizations. Over time, this just adds cost without providing additional transparency.

Q1. (b) Do you agree that this action should be international in scope? Why/why not?

Yes, this action should be international in scope because:

- This accounts for globalization and today's environment of global value chains– otherwise not comprehensive or accepted – but also retains an appropriate level of local focus to reflect the needs and resources of national organizations.
- The majority of the firms that would be affected by such a change are multinational in scope and operations.

- Ideally, there would not be different views of what value creation means based on what country you live in; although, if international consensus impedes the development of Integrated Reporting, could pursue a more phased country approach.

Towards Integrated Reporting (page 6 of the Discussion Paper)

Q2. Do you agree with the definition of Integrated Reporting on page 6? Why/why not?

Largely agree with the definition of Integrated Reporting because:

- It captures well the different stakeholders an organization services and the different components of value that an organization creates. It also highlights the importance of connectivity between those components.
- It includes all the necessary attributes and, most importantly, includes the benefit of practicing integrated reporting – which is to demonstrate the connectivity between both financial and non-financial reporting.

Take exception with some parts of the definition of Integrated Reporting as follows:

- Emphasis is on the report itself, indicating that a single report is the specified main output. Rather, focus on a tight and clearly defined relationship between components of reporting and recognition of the priorities of different stakeholder groups to reflect the relative importance of the various components of that value (impact on economy, society and environment) for them. While it is critical to Integrated Reporting that the various components of reporting are tightly connected and related to each other, different stakeholders require and expect different reporting in terms of both content and style.
- Concept of “value creation” may be a bit abstract as opposed to a simpler notion of what the company does and what service it provides or products it makes.
- There is a need to provide a clear definition of materiality as Integrated Reporting places added emphasis and strain on this concept. It asks a company to marry two definitions of materiality – the financial definition and the CSR definition. For example, many more companies report on GHG emissions in their sustainability report than in their financial reports. Why is that? Both reports are presumably using materiality to be the filter for what is included in disclosure, yet you get very different outputs. To avoid this, make the concept of materiality clearer when defining Integrated Reporting.
- Caution saying that effective integrated reporting will help stakeholders understand an organization’s future resilience as lawyers may object to this statement.

An International Integrated Reporting Framework (page 8 of Discussion Paper)

Q3. Do you support the development of an International Integrated Reporting Framework? Why/why not?

Yes, we support development of an International Integrated Reporting Framework because:

- A framework provides the ability for comparison and standardization. Setting expectations in this way enhances the understanding across all stakeholders of their own priorities and the interdependence of those on the priorities of other stakeholder groups. If well structured it would provide organizations headquartered in and operating in different countries with a common mechanism to balance the sometimes conflicting and sometimes complementary demands of different stakeholder groups
- A Framework guides organizations through the first time process of Integrated Reporting. Without a framework to follow, organizations make up their own interpretation of "integrated."
- A Framework allows stakeholders to consider this as they look at reporting and disclosure requirements and gives them the ability to compare apples to apples when reviewing reports.

One caution is that the integrated approach is likely to take years if not decades to be broadly accepted because of internal resistance to the idea that so-called "soft" concepts are as material as "hard," i.e. purely financial performance metrics. Given this, integrating the two – although ideal – may be difficult to achieve.

Q4. (a) Do you agree that the initial focus of Integrated Reporting should be on reporting by larger companies and on the needs of their investors? Why/why not?

We agree that it makes sense for the <u>initial</u> focus to be on reporting by larger companies for the following reasons:

- Larger companies have the resources to contemplate a project of this scope and have a greater impact on sustainability and therefore can command greater opportunity for both risk and benefit. Their stakeholder groups are broadly dispersed so the pressure to comply with such a proposal might be most efficiently applied from external stakeholders.
- The reality is the early adopters will be the larger companies, where small- and medium-sized companies will likely wait to see case studies for how companies are doing this to see if it makes sense for them.
- Large companies will look at other large companies as their competitive set for doing this, which will help create a significant impetus for doing this and generate momentum.
- Caution that the large company focus not crowd out the creativity and innovation that flourished under the more open GRI standards. Also, look at meeting the needs of supply chain partners and regulators in obtaining the information that they need by implementing standards that reduce the burden and costs of reporting and disclosure.

However, we disagree that the initial focus should be on the needs of their investors because:

- The discussion paper leads with very powerful and important statements about recognizing the needs of all stakeholders, so it is inconsistent to then focus in on needs of investors; it loses the value of this broader perspective.

- One of the primary purposes of Integrated Reporting is to create a tight knit relationship between the reporting needs of a diverse range of stakeholders across social and environmental, as well as economic needs. This includes policy makers, civil society, customers and governments. While there is a benefit in confining early efforts rather than boil the ocean, the primary purpose of integrated reporting is to integrate reporting needs across a much broader group of stakeholders than just investors, so it would undermine the purpose to focus on a specific stakeholder.
- To some extent the drive for separate sustainability reporting has arisen from the narrower and shorter term perspective of investors. So predicating foundational integrated reporting principles on that stakeholder group would be counterproductive.
- To date, investors have been largely apathetic towards sustainability reporting. As a result, capital markets are failing to utilize the full power of sustainability information and sustainability leaders are not rewarded with the capital and credit their performance deserves. The investor community certainly warrants attention to help change this mindset, but should not be the only stakeholder group addressed.

Q4. (b) Do you agree that the concepts underlying Integrated Reporting will be equally applicable to small and medium enterprises, the public sector and not-for-profit organizations?

Although the answer to this question will become clearer as there are more examples of how these concepts are put into practice in real integrated reports, we generally feel that yes , the concepts underlying Integrated Reporting certainly could be equally applicable to small and medium enterprises and not-for-profit organizations, as well as to both private and publically owned companies.

Not-for-profit organizations may well be a good litmus test for the non-financial principles. While not-for-profits do not deliver value through traditional investors, they bring value to society in different ways. In general we would expect a not-for-profit to be bringing more value in non-financial areas than in financial, and a for-profit vice versa. However, the principle that organizations bring value across more components than just returns to investors, should allow for a reporting structure applicable across both. These concepts may just drive different behaviors in these different types of organizations.

Business Model and Value Creation (page 11 of the Discussion Paper)

Q5. Are: (a) the organization's business model; and (b) its ability to create and sustain value in the short, medium and long term, appropriate as central themes for the future direction of reporting? Why/why not?

Yes, focusing on an organization's business model is appropriate as a central theme since it is paramount to that organization's sustainability. Giving equal weighting to the short, medium and long term value is important and is clearly a missing component in current analyst conversations. However, there is a danger that discussion of business model and value creation will be seen by some investors as detracting from their ability to judge such more fundamental concepts as cash flow, profit margin, and the like. Also, creating this much flexibility in the definition of business model may make it difficult to provide consistent reporting parameters; it asks each organization to define what is meant by "short," "medium" and "long term."

Q6. Do you find the concept of multiple capitals helpful in explaining how an organization creates and sustains value? Why/why not?

Generally we agree that yes, multiple capitals is helpful in explaining how an organization creates and sustains value, although this may be more meaningful to those involved in the investment and financial communities. These are important central themes in a world where so many firms are participating in activities that draw on all of these different capitals to compete. It more equitably distributes importance to a broader set of company inputs.

- External factors
- Downstream impacts such as indirect impacts of products and services.
- Upstream impacts of the supply chain

Recommend providing additional information in the integrated reporting document to adequately explain this concept as some may not think it is helpful. "Capital" tends to have a financial connotation to it, and some may argue that you can't measure an organization's value just on financial measures alone.

Guiding Principles (page 12 of the Discussion Paper)

Q7. Do the Guiding Principles identified in the Discussion Paper provide a sound foundation for preparing an Integrated Report – are they collectively appropriate; is each individually appropriate; and are there other Guiding Principles that should be added? Why/why not?

Overall, the Guiding Principles seem like a sound foundation for preparing an Integrated Report. However, it will be important to distinguish how this is different from the status quo as most of them already exist within financial reporting. Suggest the discussion paper do a better job of highlighting where Integrated Reporting is pushing the expectations for reporting and where it is validating existing approaches. As an example, while the paper articulates the building blocks of operation of the business in detail, it would be equally important to articulate three other key areas.

1) Other stakeholder groups and their likely priorities
2) The component of the key areas of non-financial reporting (predominantly societal and environmental). While these are mentioned they are presented within the context of their importance to the investor rather than their value to other stakeholders as a valid audience in their own right.
3) Further explore the role of Government and Public Policy; value in providing insight on what will truly help practitioners develop long term sustainable economies by identifying

how and where value is being created. This insight should help formulate Government policies to encourage rather than inhibit long term prosperity and sustainability.

Content Elements (page 15 of the Discussion Paper)

Q8. Do the Content Elements identified in the Discussion Paper provide a sound foundation for preparing an Integrated Report– are they collectively appropriate; is each individually appropriate; and are there other Content Elements that should be added? Why/why not?

The Content Elements are framed by the business model and so provide a sound foundation for preparing that component of Integrated Reporting to meet the needs of the enlightened investor. But they do not explicitly address the needs of policy makers, civil society, customers, vendors etc. and as such miss the primary purpose of Integrated Reporting. Suggest Government and Economies need be called out more explicitly in this section.

Also note that the Content Elements seem similar to the GRI framework. Distinguish how an Integrated Report will be substantively different than a sustainability report based on the GRI. It will be hard to judge its effectiveness until there are some actual reports created using this framework as it feels like a fairly open framework that can be interpreted many ways; one of the weaknesses of the GRI model. The challenge is the balance between flexibility and the desire to create a consistent report that analysts can use to guide their investment decisions.

What Will Integrated Reporting Mean for Me? (Reporting organizations – page 21 of the Discussion Paper)

Q9. (a) From your perspective: Do you agree with the main benefits as presented in the Discussion Paper? Why/why not?

By and large, we agree with the main benefits as presented; Integrated Reporting would provide an effective way to better demonstrate an organization's long term sustainability and benefits to stakeholders. However, one potential downside is that reports will be constrained to fit a very tight framework, they will all begin to look the same, and lose a potential for innovation and creativity of presentation as a result. Additional areas to explore include:

- Why does Integrated Reporting lead to more accurate non-financial information? Is this based on the assumption that including financial information in the report will force better rigor behind the non-financial information? Does this assume that reports will be assured by a third party?
- Why does this lead to lower cost of capital? The assumption is that this will provide a more accurate picture of cost, which in some cases will raise the cost of the different capitals? Or if this was this only referring to financial capital, then suggest making that clear as the discussion paper created a specific definition of capital.
- More emphasis on the benefits to the organizations themselves: (1) reduced costs of reporting, and (2) government policy development that supports long term value creation.

Q9. (b) From your perspective: Do you agree with the main challenges as presented in the Discussion Paper? Why/why not?

Yes, we agree with the main challenges as presented but would add the following:

- Buy-in: The difficulty in convincing large organization's management of the need/benefits of Integrated Reporting. It will be an easier task in Europe but potentially an uphill battle in the US.
- Status Quo – Ensuring that this framework leads to actual improvement in the reporting space, as it feels similar to the approaches that already exist.
- Reduced Disclosure – Ensuring that this process does not diminish the amount of information that companies disclose. With limited space in a single report, there might be the tendency to only report on a few core subjects (or maybe that is good!).
- Political Environment: Government agencies, regulators, and the many tax authorities will all have varying sacred cows in this change.

Q9. (c) From your perspective: Do you agree that Integrated Reporting will drive the disclosure of information that is useful for integrated analysis (from the perspective of investors)? Why/why not?

We believe that this will take time to be accepted, particularly in the U.S. where CSR Reporting in general is only beginning to gain widespread recognition as a viable contributor to reputation and value; for the two to be integrated will be seen as an outlier for some time. An additional challenge is how companies discuss the interconnectivity between the different capitals, as there is a whole spectrum of ways to interpret this guidance which would impact its usefulness. Consider that a compelling goal for this is creating long term prosperity and sustainability.

Future Direction (page 25 of the Discussion Paper)

Q10. (a) Do you agree that the actions listed in the Discussion Paper should be the next steps undertaken by the IIRC? Why/why not? Are there other significant actions that should be added?

Yes. We, as a reporting community, need more examples of integrated reports. In discussions, most people agree with the idea behind Integrated Reporting, but it is the practical application of it that is more ambiguous. "Harmonization" is a critical element of success. This should not be viewed as an additional compliance requirement forcing additional burden and costs on organizations.

Q10. (b) What priority should be afforded to each action? Why?

All the actions are important, but the Pilot Programme should be a high priority as it will be very important to understand how this is actually put into practice. It will be important to show other organizations that this can be successfully applied and lead to greater explanation of performance than traditional reporting.

Q11. Do you have any other comments that you would like the IIRC to consider?

As a point of clarification, it would be helpful if you were more explicit about whether the Integrated Reporting initiative is meant to drive towards the adoption of one single report for all stakeholders or whether the end result may be multiple reports for multiple stakeholder groups that are tied together by a consistent approach/formulation. This is currently unclear.

Additionally, while the U.S. is so dominant in so many areas, it is not out in front of this trend. There are valid reasons why Integrated Reporting will be seen by some as threatening to vested interests and established ways of doing things. The question remains what central international authority will drive this change. As it stands now, between CDP and GRI and other reporting initiatives, the chief challenge is likely to be to achieve consensus among the NGO community before attempting to achieve a consensus in the business, financial and investor communities. More insight into the thinking here would be helpful.