

IRC comments submission to the International Integrated Reporting Council (IIRC) – Implementation feedback on the International <IR> Framework

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(Online submission)

Multiple capitals

Q1a. What is your experience with the multiple capitals approach in integrated reports?

The capitals serve a very useful purpose in: (1) understanding the breadth of resources and relationships, beyond the financial, which are used and/or affected by an organisation, (2) highlighting the short, medium and long term resource needs of an organisation, and (3) they enable strategy and business model functionality and are a critical risk issue.

There are challenges and confusion, though, around the following:

- Some preparers think there is an expectation to structure their reports around the capitals.
- Some preparers mention the capitals in their reports because they assume this is a reporting requirement, however, as they don't use this terminology internally there is disconnect and confusion.
- The capitals should be reported from a capability and sustainability perspective in strategy and yet this is not always done.
- The concept of the stock and flow of capitals is poorly understood.
- Significant inputs, from the capitals, are stated in narrative form rather than quantified information despite the figures being available (for instance, the number of Kilolitres of water used in a year).
- The significant trade-offs between the capitals are not often disclosed and where they are it is usually in narrative form. Generally, there is some confusion about trade-offs and the link to the concept of maximising capital protection and growth.
- There is uncertainty on how to measure the outcomes (effects) on some of the capitals.

We support the continued use of the six capitals as a useful approach to achieving completeness when considering the resources and relationships used and/or affected by an organisation.

Q1b. What if anything should be done and by whom to improve this aspect of implementation?

The IIRC could offer guidance on the use of the capitals in a report. There ought to be emphasis on the capitals as a thinking approach and not necessarily as a reporting one. The guidance may be presented in a way that explains how the capitals interact with the business functions, the external environment, and with each other. In addition to the points noted above, the guidance may include:

- If a preparer chooses to use definitions and classifications different to those of the Framework, there should be suitable disclosure in the report. To increase

comparability, though, the IIRC might consider encouraging the use of the Framework's definitions.

- On the measurement of outcomes, a list of the global organisations currently doing work and research on the various capitals would be useful. Such a list could be cited as useful reference sources for preparers with a disclaimer of endorsement from the IIRC.
- Examples of indicators/ metrics to report against.

We refer the IIRC to the FAQ on the use of the six capitals in an integrated report on our website (www.integratedreportingsa.org).

Connectivity and Integrated Thinking

Q2a. What is your experience of connectivity in integrated reports as an indication of integrated thinking and/ or an enabler of enhanced decisions?

Connectivity of information in a report goes beyond cross-references and icons and is more about weaving a golden thread through the report in explaining an organisation's value creation story. Connectivity, however, cannot be a function of reporting and replace the connectivity of thinking in an organisation's value creation process to minimise or ameliorate negative outcomes and maximise positive outcomes.

It will be easier to show connectivity in a report if there is underlying integrated thinking in an organisation. While a report may demonstrate good connectivity, however, it cannot always be interpreted as integrated thinking in the organisation. For organisations starting out on their integrated reporting journey making the connections in their report can help to embed integrated thinking.

Connectivity can be enhanced through the development of the IR process around strategy and performance. Also, the governing body's approval of a holistic strategy – one that considers all significant capitals – can be a useful starting point to embed connectivity in the organisation's monitoring, measurement and review processes.

Q2b. What if anything should be done and by whom to improve this aspect of implementation?

Time, experience and commitment can work towards achieving better connectivity in a report. The IIRC's database, regularly updated, can assist preparers with leading practice examples and explanation of various aspects of connectivity. Embedding integrated thinking in an organisation is an important leadership issue and part of the governing body's responsibilities. The IIRC could look to issue guidance on integrated thinking and encourage research on this vast area.

Key stakeholders legitimate needs and interests

Q3a. What is your experience with the identification in integrated reports of key stakeholders' legitimate needs and interests and how these are considered and addressed?

Some preparers have good disclosure of their stakeholders' needs and interests and how these have been included in the materiality determination process, strategy process, and assessment of risks and opportunities. Others outline their stakeholders' needs and interests but don't disclose how they are responding or using the information – that is, the important feedback loop is missing.

Further, it is rare to find comment in reports on the quality of an organisation's relationship with each of its key stakeholders. This is significant information to future value creation.

Q3b. What if anything should be done and by whom to improve this aspect of implementation?

Practical guidance from the IRC in this area would be useful to preparers. It could cover how stakeholders' needs and interests can affect various areas of the organisation and why the feedback loop is important. There could also be consideration of current 'stakeholder hot topics' noting the views of different stakeholders, the potential effect on value creation, and actions taken by the organisation. Emphasis is warranted on the point that a lack of disclosure of stakeholders' needs and interests and the organisation's response thereto might be considered an indication of governance failure rather than a reporting failure.

Materiality and value creation

Q4a. What is your experience with the Framework's definition of materiality, in particular?

- **Application of the Value creation lens**
- **Use of different time periods to identify material matters**

The report is the story of the organisation and the Framework's definition is correctly phrased as what is material to the organisation's value creation process. The Framework's explanation of the materiality determination process ensures that stakeholders' needs and interests are considered.

The main weakness noted in some preparers' materiality determination process is that not all six capitals are considered thus rendering the process incomplete. Assessing the effect on value creation may also be difficult in the evaluation process. On the identified material matters, these may be out of line with the organisation's risks and opportunities and overly detailed information is sometimes disclosed.

The lens of value creation, as stated in the preamble to this question, could be misconstrued and push preparers to disclose only the positive consequences on the capitals as value created while ignoring the negative consequences. Value creation - as defined in the Framework - comprises all significant changes to the capitals (increase, decrease or

preservation). Some reports in South Africa reflect the misunderstanding outlined above and view value creation in the limited light of shared value. Other organisations see value created as the achievement of their desired goals (rather than the actual consequences), or as the Value Added Statement (financial value only), or as their inputs, while yet others define value in their own terms rather than disclosure of the actual consequences on the capitals.

On the different time periods, material matters are more often related to the reporting year and the immediate future than the longer term future or the past. Given the Framework's focus on long term value creation, the medium and long term value drivers and influencers should be included in the assessment of material matters.

Q4b. What if anything should be done and by whom to improve this aspect of implementation?

The existing useful guidance publication on materiality by the IIRC and IFAC could be updated and include the above points. Further, explanation is needed to highlight that the definition of materiality also refers to the level of information disclosed in the report (that is, high-level), as well as the influence of the other guiding principles (notably completeness and conciseness) and the boundary of the report.

Guidance from the IIRC on the value creation concept – what it is and what it isn't - is much needed. We refer the IIRC to our Information Paper *Disclosing Outcomes in the Integrated Report* on our website (www.integratedreportingsa.org).

Conciseness

Q5a. What is your opinion on the conciseness of integrated reports?

Generally, the reports of experienced preparers are slimmer than those of new preparers. This is because the experienced preparers are more willing to move detailed and compliance information to their website, their materiality determination process is more refined, and their reports have evolved into a comfortable format and structure thus limiting duplication of information. Organisations in South Africa have also found it useful to apply the octopus approach to their corporate reporting suite – that is, the integrated report is the head of the octopus and all other supplementary reports containing detailed information are seen as the arms of the octopus. Our view is that it is entirely possible that the reports of even complex organisations can be less than 80 pages.

Local regulations play a part in the length of integrated reports. For instance, a requirement allowing the full AFS to be accessible on the website enables organisations to include summarised financial information in their reports.

Q5b. What if anything should be done and by whom to improve this aspect of implementation?

It would be useful for the IIRC to inform on its expectations regarding conciseness, although not necessarily alluding to a precise number of pages, and of how this guiding principle can be applied with the others.

Specific guidance for beginners (a road map with milestones) that includes a simple structure and illustrative examples is useful to new preparers. We refer the IIRC to our Starter's Guide and FAQ on the octopus approach on our website (www.integratedreportingsa.org).

Business model - outputs and outcomes

Q6a. What is your experience with the reporting of business model information, particularly outputs and outcomes?

The lack of distinction between outputs and outcomes was observed in South African reports a few years ago. The IRC released an Information Paper *Disclosing Outcomes in the Integrated Report* in December 2015 and subsequently a general improvement in this differentiation has been noticed.

In South African reports the business model is often disclosed in graphic form, in line with the Framework's suggestion. Improvements can be made, however, especially in the disclosure of actual inputs in the reporting period and while the disclosure of outcomes has improved there is work to be done. Some organisations are finding it difficult to include all significant information in one graphic – their confusion is around including information on the reporting period as well as information pertinent to the business model in general.

Q6b. What if anything should be done and by whom to improve this aspect of implementation?

Practical implementation guidance from the IIRC will be useful to preparers. This could include suggestions on where best to disclose those outcomes directly related to performance in the reporting period and the broader, longer term outcomes arising from the business model in general. A useful suggestion too is that stakeholder information be included in the business model section of a report. Emphasis should be made of the fact that value creation and outcomes are one and the same.

We refer the IIRC to our Information Paper on outcomes for consideration.

Involvement of those charged with governance and identification of the Framework

Q7a. What is your experience with whether: (i) reports identify the involvement of those charged with governance, and (ii) indicate that they are presented in accordance with the Framework? What are the implications of excluding such information?

- (i) Many reports in South Africa carry a statement from the governing body acknowledging responsibility for the report. This is often upfront of the report and signed by members of the governing body. This statement, however, is not always in line with the wording in the Framework.
- (ii) In March 2014, the IRC advised the use of the Framework in preparing an integrated report and many reports in South Africa indicate that the report has been prepared in accordance with the Framework. The King IV Report states that organisations should follow the guidance of the IRC.

Given that the governing body is responsible for the organisation, the report should be seen as the 'voice of the board'. We regard it as extremely important that the governing body continue to be responsible for the integrity of the report, as stated in the Framework.

Q7b. What if anything should be done and by whom to improve this aspect of implementation?

In many jurisdictions the governing body of an organisation has a duty to ensure the integrity of reporting. The IIRC may need to remind preparers that the statement by the governing body is one of the requirements of the Framework and should be adhered to if the report is stated as being in accordance with the Framework.

If guidance is issued by the IIRC on the governing body's involvement and oversight this will necessarily have regard to different legal regulations and governance frameworks.

Other guiding principles

Q8a. What is your experience of the application of these remaining three guiding principles?

- **Strategic focus and future orientation**
- **Reliability and completeness**
- **Consistency and comparability**

Strategic focus and future orientation – Strategic-focused information is included in reports, however, further improvement is needed in cutting out detailed information. Future-oriented information (and the Outlook content element) tend to receive less attention in reports.

Consideration could be given to separating the two principles – strategic focus is critical in a report and while strategy is future-oriented any inclination by a preparer to avoid disclosing detailed forward-looking information may inadvertently result in insufficient disclosure of strategic information.

Reliability and completeness – The assurance process is generally disclosed in South African reports given the prevalence of the combined assurance approach recommended in King III and clarified further in King IV.

Some preparers note that achieving completeness is a challenge with the simultaneous application of the conciseness guiding principle. And on achieving balance in a report, this is proving to be a challenge for many preparers with the natural bias being to disclose positive information and avoid potentially negative issues. Consideration could be given to separating these two principles to heighten the importance of completeness.

Consistency and comparability – Some preparers note that it would be useful to have a clearer positioning from the IIRC on the role and relationship with other indicator-based initiatives or standards (such as the GRI and SASB). Clarity would also be useful on the IIRC's expectations as to the comparability of reports; specifically, with a principles-based Framework and the variable placement of the content elements which are phrased as

questions, overall comparability may be simply unattainable. An area where comparability can be achieved, however, is in benchmarking and sector analysis.

Other content elements

Q9a. The Framework identifies eight content elements (business model is mentioned above). What is your experience with how these seven remaining content elements are reported in reports?

Organisational overview and external environment – The importance of the external environment in setting the context for the organisation’s value creation story as told in the rest of the report is worthy of emphasis. Explanation of how these factors have influenced the organisation, including its business model, strategy and risks and opportunities, should be highlighted.

Governance – This is an area where improvement is needed in many reports. The information given is often detailed and compliance-oriented rather than a demonstration and assessment of the governing body’s role in the organisation’s value creation process and the decisions taken. The IRC is currently working on an Information Paper to assist preparers in this area and it is scheduled for release in December 2017.

Risks and opportunities – Many preparers have increased and improved their disclosure of risks over the years. Improvement is still needed, though, in the following areas: excluding detailed information in favour of material risks, better connectivity, and the consideration of all six capitals in the assessment process. Further, better alignment is needed with the identified material matters. The reporting of opportunities is often less advanced than risks and some leading practice examples in this area would be helpful to preparers.

Strategy and resource allocation – While disclosure has improved over the years, improvement is needed in disclosing targets and KPIs not only for the year ahead but also for the medium and long term. Further, preparers often neglect disclosure of their plans to access strategic resources needed in the future. The disclosure of the strategy to achieve their strategic objectives can also be minimal with some preparers regarding this as sensitive information. The trade-offs of the capitals in pursuing strategic objectives is also a generally neglected area with some preparers seeing this as commercially or politically sensitive information.

Performance – The areas for improvement include: some preparers do not link performance to their strategic objectives in their reports, or disclose the positive and negative outcomes related to performance in the reporting period. If the strategic objectives and targets are not adequately disclosed then the disclosure of performance falls short.

We refer the IIRC to our Information Paper *Disclosure of Performance against Strategic Objectives* on our website (www.integratedreportingsa.org).

Outlook – Generally, this is an area that needs to be more actively addressed by many preparers despite the progress to date. Some reports contain bland, boilerplate information rather than considered information. The IIRC could consider guidance in this area, as well as

leading practice examples on the IIRC database. Useful information to users of reports could include the longer term aspirations of the organisation and scenario analysis of the achievement of strategic objectives in the future.

Basis of preparation and presentation – The boundary of reports is sometimes not determined with as wide a view as set out in the Framework. The challenge to preparers is in determining the extent of the risks, opportunities and outcomes associated with external entities and stakeholders, and then seeking information thereon from external parties. Practical guidance from the IIRC will be useful to preparers, and particularly the report boundary's link to the identification of material matters.

Q9b. What if anything should be done and by whom to improve this aspect of implementation?

Practical guidance from the IIRC as noted in the answer above. The IIRC's database can also assist preparers.

Other quality issues

Q10a. Aside from any quality issues already raised in Q1 – 9, what is your experience with the quality of integrated reports?

The quality of South African reports has improved since the first reports were released in 2010/2011 following King III's recommendation to prepare an integrated report. Today, some excellent reports are released by organisations committed to better corporate reporting and improvements in their reports each year. These organisations are not only striving for high-quality integrated reports but also for deepening the integrated thinking in their organisations. This does not, however, hold true for all organisations and there are no doubt some which see the integrated report as a compliance chore rather than a useful management tool among many other benefits.

It should be noted that private-sector reports in South Africa are variably targeted at providers of financial capital (per the Framework), all the organisation's stakeholders, or there is no mention of the targeted audience with the report being the value creation story of the organisation. This varied treatment is due to King III, and now King IV, which have adopted a stakeholder inclusive approach to governance. The IRC's objectives include consideration of international developments in international reporting, such as the Framework, and the King Codes of Corporate Governance.

Q10b. What if anything should be done and by whom to improve this aspect of implementation?

It is suggested the IIRC could do more to emphasise the role of an integrated report, and the quality of the information contained therein, for example in enabling stakeholder engagement and interaction or being an effective 'gateway' for accessing more specific and detailed reported information, among others.

Other enablers, incentives and barriers

Q11a. What is your experience of other enablers, incentives and barriers to Framework implementation, not covered by other questions, including the extent to which they apply particularly to:

- **Specific jurisdictions?**
- **Large or small organisations?**
- **Private, public or non-profit sectors?**
- **Different stages of Framework implementation?**

The establishment of the IRC as a national body whose members include professional institutes, industry bodies, regulators and others has been a significant enabler in South Africa. The IRC promotes integrated reporting and develops the quality of integrated reports through technical Information Papers, FAQs, a website and conferences. The IRC's members in turn keep integrated reporting in focus with their respective members by passing on IRC technical information and including integrated reporting and integrated thinking in conferences and training, among others.

The initial impetus for integrated reporting in South Africa was its inclusion as a recommended practice in King III. The principles of King III were incorporated into the Listings Requirements of the Johannesburg Stock Exchange on an 'apply or explain basis' and this saw listed companies prepare their first integrated reports in 2010/ 2011. Since then, many large state-owned companies prepare reports as do some public-sector organisations, non-profit organisations and unlisted companies.

In King IV, there is a similar recommendation to prepare an integrated report. King IV is closely aligned with the Framework. King IV has five sector supplements aimed at specific sectors, including SMEs, retirement funds and non-profit organisations, and this is expected to significantly widen the number and type of organisations preparing integrated reports.

In South Africa there are three national integrated reporting awards and they have played a part in stimulating interest and ongoing improvement in reporting. There is also a well-established 'eco system' of consultancies and publishing houses that serve the needs of preparers.

Q11b. What if anything should be done and by whom to improve this aspect of implementation?

Some public-sector reporting frameworks in South Africa need to be better aligned with King IV (which will then align them with the Framework).

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