CHAPTER 2

The Integrated Reporting Framework: Revisions 2021

This article aims to:
Summarise new developments in the area of integrated reporting.
The space of corporate reporting has evolved tremendously over the years and covers a wide spectrum of topics including financial reporting, Environmental, Social and Governance (ESG) reporting and value creation for all stakeholders in the ecosystem. Regulators and standard setters across the globe recognise this growing attention towards transparent and good disclosures to meet investors' attention and expectations from the businesses.

Background

The International Integrated Reporting Council (IIRC) was formed in August 2010 with an aim to create a globally accepted framework for communication by an organisation about its value creation over time. The IIRC published the first version of its 'International Integrated Reporting <IR> Framework (<IR> Framework) in December 2013. Rather than laying down any specific detailed disclosures or measurement bases, the <IR> Framework takes a principle-based approach and establishes Guiding Principles and Content Elements that govern the overall content of an integrated report.

Over the last decade, more than 2,500 companies across 70 countries[1] have adopted the concept of integrated reporting as part of their sustainability reporting. Further, over 40 stock exchanges[1] globally make reference to the integrated reporting in their guidance. In India, the Securities and Exchange Board of India (SEBI) on 6 February 2017 had recommended the voluntary adoption of the <IR> Framework for annual reporting. Since then, more than 40 companies[2] across various sectors have adopted integrated reporting in India.

Recent developments in sustainability reporting

In its journey towards integrated reporting, the IIRC has covered several significant milestones. In September 2020, the IIRC along with four other standard setting global institutions namely the Climate Disclosure Standards Board (CDSB), the Global Reporting Initiative (GRI), the Sustainability Accounting Standards Board (SASB) and the Carbon Disclosure Project (CDP) issued a joint statement to show an intent to work together towards a comprehensive corporate reporting system. In December 2020, these five leading organisations published an illustration of how their current frameworks, standards and platforms, along with the elements set out by the Task Force on Climate-related Financial Disclosures (TCFD), can be used together to provide a 'running start' for development of global standards that enable disclosure of how sustainability matters create or erode an enterprise value.[3]

Revisions to the <IR> Framework

The primary purpose of an integrated report is to bring an improvement in the quality of information which is made available to various stakeholders in the ecosystem including investors, lenders, and public at large. The <IR> Framework lays down a set of fundamental concepts and includes guiding principles and content elements which govern preparation of an integrated report by a company. While the <IR> Framework continues to be relevant today despite various developments in the ESG and sustainability reporting space, the IIRC council endorsed for certain revisions to the existing <IR> Framework.

In January 2021, the IIRC in order to facilitate more decision useful reporting published revisions to the <IR> Framework. The revisions to the <IR> Framework focussed on a simplification of the required statement of responsibility for the integrated report, improved insight into the quality and integrity of the underlying reporting process, a clearer distinction between outputs and outcomes with examples and a greater emphasis on the balanced reporting of outcomes and value preservation and erosion scenarios.

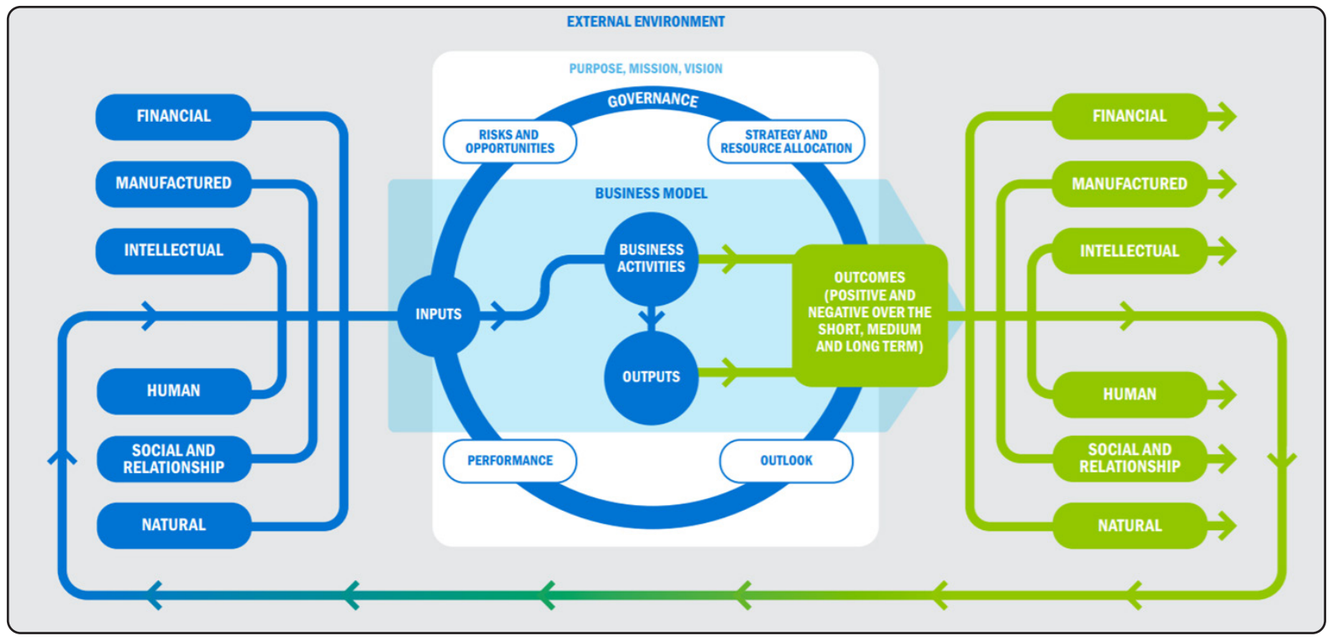
1. 'Celebrating our 10 Year Anniversary: Reflections from around the world', IIRC, 30 November 2020
2. 'Integrated reporting in India', Vrushali Gaud, IIRC, 12 September 2019
3. 'Global sustainability and integrated reporting organizations launch prototype climate-related financial disclosure standard', IIRC, 18 December 2020

Below is an overview of the key revisions made in the <IR> Framework:

- **Responsibility for an integrated report:** Under the revised <IR> Framework, an integrated report should include a statement from Those Charged With Governance (TCWG) that they acknowledge their responsibility to ensure integrity of the integrated report and that in their opinion and conclusion, the integrated report is presented in accordance with the <IR> Framework (earlier the <IR> Framework provided an option to not include such a statement). Each country may have stipulated laws and regulations defining the governance structure of the organisations, therefore, the revised framework clarifies that an organisation should consider such governance structure, the culture and legal context, size and ownership characteristics in order to access who is responsible for acknowledging this responsibility. In the revised framework, this is further explained by an example that in some jurisdictions a single board may be required whereas in others, separation of the supervisory and the executive/management functions may be prevalent in a two-tier board. In case of a two-tier board, the body responsible for overseeing the strategic direction of the company would issue the statement of responsibility.

  In jurisdictions where legal or regulatory laws preclude a company from issuing such a statement of responsibility from TCWG, this should be clearly stated in the integrated report. Further, in such cases, a company should make appropriate disclosures about the processes followed to prepare and present the integrated report. Such disclosures can include related systems, procedures and controls including key activities and responsibilities and the role of TCWG, including relevant committees.

- **Business model and value creation:** The fundamental of the <IR> Framework lies in the creation of value for the organisation itself which affects the financial returns to the providers of the financial capital and others including stakeholders and society at large. During the revision to the <IR> Framework, the IIRC recognised, that although all organisations aim to create value, the overall stock of capitals such as the financial capital, manufactured capital, human capital, intellectual capital, natural capital or social capital can also either undergo a net decrease or experience no net change. In such cases, value is eroded or preserved. Accordingly, a revision was made in the <IR> Framework to include in the integrated report how an organisation creates, preserves or erodes value over time. The IIRC believes that if companies adopt the new disclosure requirements of short term, medium term and long-term outcomes, the complete value creation story can be built. Greater emphasis on value preservation and value erosion will encourage more balanced reporting of outcomes. Consequential amendments were made in the process through which value is created, preserved or eroded as depicted in the diagram below:



Source: International <IR> Framework, January 2021

- **Clearer distinction between output and outcomes:** As illustrated in the diagram above, the <IR> Framework provides guidance on what is a business model. Section 4C of this framework defines a business model as 'an organisation's system of transforming inputs through its business activities into outputs and outcomes that aim to fulfil the organisation's strategic purposes and create value over the short, medium and long term.' Outputs are an organisation's products and services and include other outputs including any by-products and waste (e.g. emissions) which may need to be discussed and disclosed within the business model depending on the materiality. Outcomes are the internal and external consequences (positive and negative) for the capitals[4] as a result of an organisation's business activities and outputs.

The IIRC in a review of randomly selected integrated reports in 2016 observed that preparers of integrated reporting are often confused or fail to distinguish between outputs, outcomes and impacts. The IIRC acknowledged that differentiating between outputs and outcomes can be challenging and encourage organisations to decipher their business models and the impact on their activities. In the revision to the <IR> Framework in January 2021, the IIRC has included a simple example to illustrate the distinction between output and outcomes in Para 4.19 of the <IR> Framework as below:

'An automotive manufacturer produces internal combustion engine cars as its core output. Positive outcomes include increases in financial capital (through profits to the company and supply chain partners, shareholder dividends and local tax contributions) and enhanced social and relationship capital (through improved brand and reputation, underpinned by satisfied customers and a commitment to quality and innovation). Negative outcomes include adverse consequences for natural capital (through product-related fossil fuel depletion and air quality reduction) and reduced social and relationship capital (through the influence of product-related health and environmental concerns on social license to operate).'

The revised <IR> Framework encourages prepares to present outcomes in a balanced way. Where predictable, it supports an organisation's assessment of the use of and effects of the capitals with qualitative and quantitative information.

4. Stocks of value on which all organisations depend for their success as inputs to their business model, and which are increased, decreased or transformed through the organisation's business activities and outputs.

Way forward

The journey of integrated reporting which began in 2010 provided a reporting framework for companies to address the business reporting model. Over the years, much has changed including the way businesses are being conducted with globalisation, environmental concerns on the rise and growing expectations from the society on enhanced corporate reporting and accountability. Regulators and standard setters around the world have supported the vision of a comprehensive corporate reporting system to include a holistic disclosure of both financial performance as well as sustainability matters. By doing so, investors and other stakeholders such as customers, lenders, employees and society at large will be able to better understand and make investment decisions in organisations which tell the entire story of value creation, preservation and erosion of its enterprise value.

Even today, reporting requirements have evolved differently in different jurisdictions around the world. This has caused added burden and duplication of information on an organisation functioning in more than one jurisdiction. It also makes it difficult for various stakeholders such as investors to compare the performance of companies across jurisdictions.

The statement of intent issued by the five regulatory bodies i.e., the IIRC, CDSB, GRI, SASB and CDP to work towards development of a comprehensive corporate reporting system is a step in the right direction. This will enhance comparability and reliance of information sought by not only shareholders but all stakeholders in the eco-system across various jurisdictions.

Certain other prominent standard setters such as the International Accounting Standards Board (IASB) are evaluating their roles and responsibilities on setting up guidance and standards on sustainability reporting. The IASB recognises the growing and immediate demand globally towards improving transparency and comparability in sustainability. Accordingly, the IASB is looking to produce a definitive framework, including setting up a separate sustainability standards board by the end of September 2021[5]. The International Auditing and Assurance Standards Board (IAASB) in early 2019 rolled out a consultative paper to gather feedback from stakeholders in order to issue guidelines for assurance on Extended External Reporting (EER). The EER includes many different forms of non-financial reporting such as sustainability reporting, integrated reporting and other forms of ESG reporting by companies. The IAASB on its part proposes to draft a non-authoritative guidance for assurance practitioners applying International Standard on Assurance Engagements (ISAE) 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*, to EER assurance engagements[6].

Clearly, the thrust of the global standard setters is now on the non-financial reporting aspect which is an ask from the society today. Companies should keep a close watch on the areas of development in this space.

5. 'IFRS Foundation Trustees announce next steps in response to broad demand for global sustainability standards', IASB, 2 February 2021
6. IAASB consults on Extended External Reporting (EER) assurance, IAASB, 13 March 2020