Deloitte.

December 23, 2013
Volume 20, Issue 36

Heads Up

In This Issue:

The <IR> Framework reflects the IIRC's view that corporate reporting must evolve to communicate the full range of factors that affect an organization's ability to create value over time.

IIRC Releases the International Integrated Reporting <IR> Framework

Introduction

On December 9, 2013, the International Integrated Reporting Council (IIRC), a global coalition of regulators, investors, companies, standard setters, the accounting profession, and nongovernmental organizations, released the *International Integrated Reporting <IR> Framework* (the "<IR> Framework"), a principles-based framework for the preparation of an integrated report.

The <IR> Framework reflects the IIRC's view that corporate reporting must evolve to communicate the full range of factors that affect an organization's ability to create value over time, including traditional financial or manufactured capitals[1] as well as the equally important human, intellectual, social and relationship, and natural capitals needed to do business in the 21st century.

Integrated Reporting is not combined reporting. Therefore, an integrated report is not a report that combines the financial statements or annual report and any separate corporate responsibility or sustainability report into one report (see Form of Report and Relationship With Other Information below). Rather, it is "a concise communication about how an organization's strategy, governance, performance and prospects, in the context of its external environment, lead to the creation of value over the short, medium and long term."

The <IR> Framework is organized into two parts, each consisting of two chapters:

- Part I provides guidance on (1) using the framework and (2) the fundamental concepts of Integrated Reporting.
- Part II discusses Guiding Principles and Content Elements related to the preparation and presentation of an integrated report.

Parts I and II both include ***requirements in bold italic type*** with which any communication claiming to be an integrated report in accordance with the <IR> Framework should comply. Those requirements are listed in an appendix to the <IR> Framework and are also included in a table as an appendix to this newsletter.

Using the <IR> Framework

Purpose and Users of an Integrated Report

The primary purpose of an integrated report is to explain to providers of financial capital how an organization creates value over time. Integrated Reporting aims to:

- Improve the quality of information available to providers of financial capital to enable a more efficient and productive allocation of capital

[1] The <IR> Framework defines capitals as the "resources and the relationships used and affected by the organization." For more information, see The Capitals below.

- Promote a more cohesive and efficient approach to corporate reporting that draws on different reporting strands and communicates the full range of factors that materially affect the ability of an organization to create value over time
- Enhance accountability and stewardship for the broad base of capitals (financial, manufactured, intellectual, human, social and relationship, and natural) and promote understanding of their interdependencies
- Support integrated thinking, decision-making and actions that focus on the creation of value over the short, medium and long term.

Editor's Note: A stated aim of Integrated Reporting is to support integrated thinking and decision making. The <IR> Framework defines integrated thinking as "the active consideration by an organization of the relationships between its various operating and functional units and the capitals that the organization uses or affects." Just as Integrated Reporting engenders integrated thinking, so does integrated thinking engender Integrated Reporting; each is a function of the other.

Many of the businesses that participate in the IIRC's Integrated Reporting pilot program[2] are focusing initially on integrated thinking by applying the concepts of Integrated Reporting internally to adapt their information systems and decision making, before producing external integrated reports. For details and case studies, see the 2013 pilot program yearbook[3] on the IIRC's Web site.

Although the integrated report focuses primarily on providers of financial capital, it benefits all stakeholders that are interested in an organization's ability to create value over time, including employees, customers, suppliers, business partners, local communities, legislators, regulators, and policymakers. This is because how the organization interacts with the external environment and the capitals (financial, intellectual, human, social and relationship, and natural) affects its ability to create value over the short, medium, and long term.

Although the integrated report focuses primarily on providers of financial capital, it benefits all stakeholders that are interested in an organization's ability to create value over time.

Form of Report and Relationship With Other Information

Under the <IR> Framework, an integrated report is "a designated, identifiable communication" that differs from financial statements and sustainability reports. However, it may form part of another report prepared by an organization for compliance purposes, provided that the inclusion of information outside the scope of the guidance "does not obscure the concise information required by [the <IR>] Framework."

Editor's Note: The IIRC's vision is bold: ideally, integrated thinking and Integrated Reporting will become the norm, with the concepts of Integrated Reporting thoroughly embedded in all forms of business communication regardless of whether they are external (i.e., across the corporate reporting suite, from the statutory report to a quarterly investor presentation) or internal (i.e., management reports). Paragraph 3.7 of the <IR> Framework states, "The more that integrated thinking is embedded into an organization's activities, the more naturally will the connectivity of information flow into management reporting, analysis and decision-making."

Statement of Compliance

Any communication claiming to be an integrated report and referencing the <IR> Framework must comply with all of the requirements identified by the <IR> Framework in bold italic type except in any of the following circumstances:

- Reliable information is unavailable.
- Specific legal prohibitions preclude disclosure of material information.
- Significant competitive harm would result from disclosure of material information.

[2] IIRC Pilot Programme. For more information about the Integrated Reporting pilot program, see Pilot Program Networks below.
[3] *IIRC Pilot Programme Yearbook 2013.*

In the first two instances, the organization must indicate the nature of the information omitted and explain why it has been omitted. When reliable information is unavailable, the organization must also "identify the steps being taken to obtain the information and the expected time frame for doing so."

When disclosure could cause competitive harm, an organization should consider "how to describe the essence of the matter without identifying specific information that might cause a significant loss of competitive advantage." The <IR> Framework further states that the organization accordingly "considers what advantage a competitor could actually gain from information in an integrated report, and balances this against the need for the integrated report to achieve its primary purpose."

Role of Those Charged With Governance

To comply with the <IR> Framework, an integrated report should generally include a statement from those charged with governance that (1) acknowledges their responsibility for ensuring the integrity of the integrated report, (2) acknowledges that "they have applied their collective mind to the preparation and presentation of the integrated report," and (3) provides their "opinion or conclusion about whether the integrated report is presented in accordance with [the <IR>] Framework."

When disclosure could cause competitive harm, an organization should consider "how to describe the essence of the matter without identifying specific information that might cause a significant loss of competitive advantage."

If such a statement is not included, the integrated report is required to explain (1) the "role those charged with governance played in its preparation and presentation," (2) the steps the organization is taking "to include such a statement in future reports," and (3) the "time frame for doing so, which should be no later than the organization's third integrated report that references [the <IR>] Framework."

Editor's Note: The question of whether those charged with governance should provide a statement acknowledging their responsibility for ensuring the integrity of the integrated report was the single most contentious issue raised during the comment period, with just over 50 percent of respondents expressing support for the proposed requirement. Investor representatives in general deemed the statement necessary to give the integrated report credibility and avoid making the report appear to be a marketing document. The principal argument against requiring the statement came from respondents in countries such as Japan, where no such requirement exists in connection with financial statements and there is no evidence that investors view Japanese stocks less favorably as a result. By holding Integrated Reporting to a higher standard, the IIRC risks discouraging entities in those markets from adopting the <IR> Framework. Time will tell whether this proves to be the case.

Fundamental Concepts

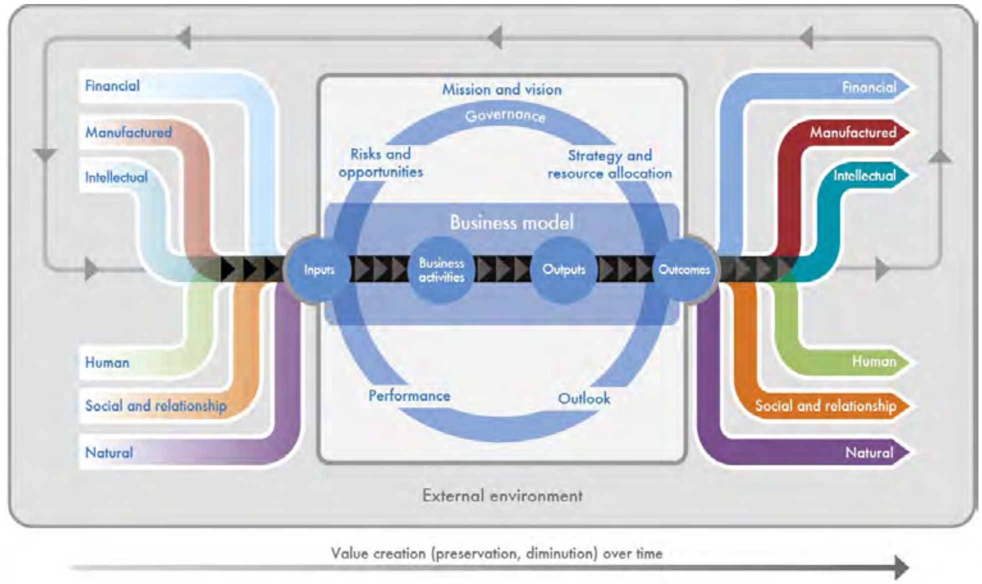
Integrated Reporting is predicated on three fundamental concepts:

- Value creation for the organization and for others.
- The capitals.
- The value creation process.

An organization's activities, its interactions and relationships, its outputs, and the outcomes associated with the various capitals it uses and affects influence its ability to draw on these capitals in a continuous cycle.

The <IR> Framework's value creation diagram (see Figure 1 below) links the fundamental concepts of Integrated Reporting to the Content Elements of an integrated report.

Figure 1 — The Value Creation Process (reproduced from the <IR> Framework with the permission of the IIRC)



Value Creation for the Organization and for Others

The <IR> Framework states that "[v]alue created by an organization over time manifests itself in increases, decreases or transformations of the capitals caused by the organization's business activities and outputs. That value has two interrelated aspects — value created for:

- The organization itself, which enables financial returns to the providers of financial capital
- Others (i.e., stakeholders and society at large)."

In addition, the <IR> Framework explains that providers of financial capital are interested in the value an organization creates for others "when it affects the ability of the organization to create value for itself, or relates to a stated objective of the organization (e.g., an explicit social purpose) that affects their assessments."

Editor's Note: The premise here is that whether an organization creates value for others materially affects the organization's ability to create value for itself — and whether an organization creates value for itself materially affects its ability to create value for others. This is why an organization's business model and value creation process benefit not only providers of financial capital but also all other stakeholders that are interested in the organization's ability to create value over time.

The value creation process diagram in the <IR> Framework (see Figure 1 above) effectively depicts this dynamic relationship: an organization's activities, its interactions and relationships, its outputs, and the outcomes associated with the various capitals it uses and affects influence its ability to draw on these capitals in a continuous cycle.

The Capitals

The capitals — i.e., the "resources and the relationships used and affected by the organization" — are categorized in the <IR> Framework as "financial, manufactured, intellectual, human, social and relationship, and natural." However, this categorization is only a guideline, which is provided to ensure that an organization does not overlook a capital it uses or affects. The <IR> Framework does not require organizations preparing an integrated report to adopt this categorization.

The <IR> Framework further defines the capitals as "stocks of value that are increased, decreased or transformed through the activities and outputs of the organization" and gives several examples (such as improving human capital through employee training, the related training costs reducing financial capital).

The <IR> Framework is explicit about not requiring an organization to quantify or monetize its use of, or effects on, all of the capitals; quantitative indicators are to be included in an integrated report only when it is practicable and relevant to do so. The guidance states that the "ability of the organization to create value can best be reported on through a combination of quantitative and qualitative information."

When preparing an integrated report, organizations should consider disclosing the important interdependencies or trade-offs between capitals or between components of a capital that influence value creation over time (e.g., creating employment through an activity that negatively affects the environment).

The <IR> Framework is explicit about not requiring an organization to quantify or monetize its use of, or effects on, all of the capitals; quantitative indicators are to be included in an integrated report only when it is practicable and relevant to do so.

Editor's Note: The <IR> Framework does not expect an organization's integrated report to cover every capital since the capitals will not be equally relevant to all organizations. An organization's interaction with some capitals may not be sufficiently important to disclose in its integrated report.

The Value Creation Process

Figure 1 above links the various components of the value creation process with all of the Content Elements in an integrated report (see below). The <IR> Framework's explanatory text links to the "Business model" Content Element in particular as follows: "At the core of the organization is its business model, which draws on various capitals as inputs and, through its business activities, converts them to outputs (products, services, by-products and waste). The organization's activities and its outputs lead to outcomes in terms of effects on the capitals" (underscoring omitted). The <IR> Framework further explains that "[o]utcomes are the internal and external consequences (positive and negative) for the capitals as a result of an organization's business activities and outputs."

Editor's Note: The <IR> Framework's value creation process diagram shows the linkage between an organization's business model (which should be dynamic, not static) and its ability to create value. The outcomes associated with the relevant capitals are as important as the organization's outputs (products and services) for enabling the organization to continue creating value for itself.

The Building Blocks — Guiding Principles and Content Elements

The table below lists (1) the seven Guiding Principles underlying the preparation and presentation of an integrated report and (2) the eight key Content Elements included in such a report.

Ultimately, the content of an integrated report will depend on the particular circumstances of the organization as well as the exercise of judgment by senior management and those charged with governance in applying the <IR> Framework's Guiding Principles and Content Elements.

The Content Elements of the integrated report need not be arranged in the order in which they are listed in the <IR> Framework. However, an organization is required to present the content in a way that clearly shows how those elements interconnect.

Guiding Principles	Content Elements
The following seven Guiding Principles underlie the preparation and presentation of an integrated report, informing its content and how information is presented: • Strategic focus and future orientation. • Connectivity of information. • Stakeholder relationships. • Materiality. • Conciseness. • Reliability and completeness. • Consistency and comparability.	An integrated report is required to include the following eight key Content Elements: • Organizational overview and external environment. • Governance. • Business model. • Risks and opportunities. • Strategy and resource allocation. • Performance. • Outlook. • Basis of preparation and presentation.

Editor's Note: Judgment will be required when there is an apparent tension between the Guiding Principles (e.g., between conciseness and completeness). The <IR> Framework does not provide additional guidance on how to make this judgment but notes that the "Guiding Principles are applied individually and collectively for the purpose of preparing and presenting an integrated report."

Key aspects of the Guiding Principles and Content Elements that offer guidance in making that judgment include:

- Looking to the medium and long term instead of focusing solely on the short term.
- In a manner reflecting the importance of relationships with key stakeholders, providing insight into the nature and quality of the organization's relationships with them, including how and to what extent the organization understands, takes into account, and responds to their legitimate needs and interests.
- Applying the materiality concept to determine the content of an integrated report by assessing those matters that substantively affect the organization's ability to create value over the short, medium, and long term. The organization's reporting boundary for an integrated report will be central to the application of the materiality concept in the context of the broader capitals considered under the <IR> Framework.
- Understanding the interconnectivity of information presented in the integrated report (e.g., the linkage between strategy, risks and opportunities, and performance, including financial and nonfinancial key performance indicators) and in the organization's other communications.
- Adopting a future orientation (e.g., by clearly articulating information about the availability, quality, and affordability of the capitals the organization uses or affects).
- Providing the basis of the report's preparation and presentation, including any other significant frameworks used to quantify or evaluate material matters for inclusion in the report, in addition to disclosure of:
    - "A summary of the organization's materiality determination process."
    - "A description of the reporting boundary and how it has been determined."

Judgment will be required when there is an apparent tension between the Guiding Principles (e.g., between conciseness and completeness).

Reporting Boundary for an Integrated Report

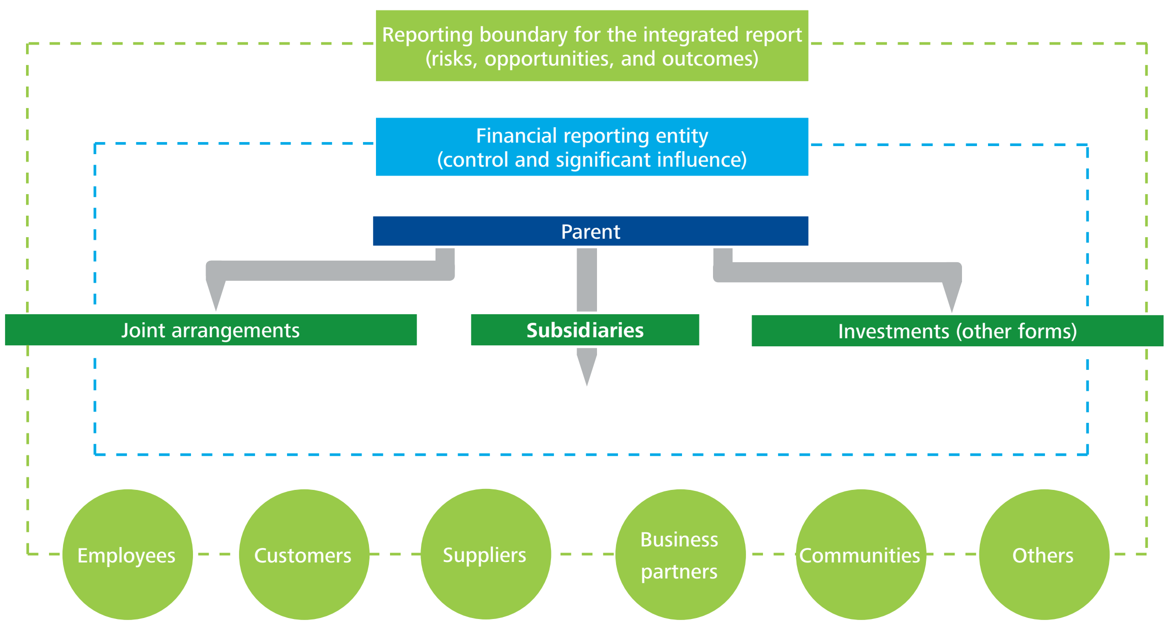
The <IR> Framework includes the concept of the reporting boundary as a component of the materiality determination process. Considering the organization's reporting boundary has two aspects:

- The financial reporting boundary, which identifies the subsidiaries', joint ventures', and associates' transactions and related events to be included in the organization's financial report and is determined in accordance with applicable financial reporting standards.

- A wider boundary beyond the financial reporting boundary to identify those risks, opportunities, and outcomes attributable to or associated with entities or stakeholders beyond the financial reporting entity that have a significant effect on such entity's ability to create value. The <IR> Framework states that although these other entities or stakeholders could be related parties for purposes of financial reporting, they "will ordinarily extend further." Examples given in the <IR> Framework's depiction of the reporting boundary for an integrated report include employees, customers, suppliers, business partners, and communities (see Figure 2 below).

Editor's Note: The entities or stakeholders beyond the financial reporting boundary reflected in the <IR> Framework's depiction of the reporting boundary may be those considered by organizations for purposes of stand-alone reports on corporate responsibility or sustainability.

Figure 2 — The Reporting Boundary (reproduced from the <IR> Framework with the permission of the IIRC)



Supporting Guidance and Documentation

Section 4I of the <IR> Framework, titled "General reporting guidance," includes further guidance on matters related to various Content Elements: (1) disclosure of material matters (including the characteristics of suitable quantitative indicators); (2) disclosures about the capitals; (3) time frames for short, medium, and long term; and (4) aggregation and disaggregation.

The <IR> Framework is accompanied by two documents, both of which are available on the IIRC's Web site:

- *Basis for Conclusions*.
- *Summary of Significant Issues*, which (1) discusses in greater detail how the IIRC addressed various issues raised in respondents' comments on the April 2013 Consultation Draft and (2) maps significant changes in structure and movements of text from the Consultation Draft to the <IR> Framework.

Pilot Program Networks

The IIRC maintains a pilot program[4] for Integrated Reporting that it describes as an "innovation hub." There are two pilot program networks, one for businesses[5] and the other for investors.[6]

Now in its third year, the pilot program for businesses serves a diverse group of more than 100 companies and other business entities from various regions and industries worldwide. Participants include Deutsche Bank, HSBC, Hyundai Engineering and Construction, Microsoft, National Australia Bank, PepsiCo, Tata Steel, and Unilever.

The IIRC maintains a pilot program for Integrated Reporting that it describes as an "innovation hub."

Participants in the pilot program for investors include AMP, Blackrock, Goldman Sachs, Government Employees Pension Fund of South Africa, Groupama, ING, Natixis, Nissay (of Nippon), Norges Bank, and State Street Global Advisors.

Emerging Integrated Reporting Practice

The IIRC's Web site features an emerging Integrated Reporting database of examples from various annual and integrated reports that illustrate specific Guiding Principles and Content Elements.

Emerging Integrated Reporting practice reporters referred to by the IIRC include Marks & Spencer Group plc (on governance), Lawson Inc. and Sasol (on the business model), Schiphol (on risks and opportunities), Gold Fields and New Zealand (on strategy), Nedbank Group and Stockland (on financial performance), and ARM Holdings plc and Novo Nordisk (on outlook).

4 See footnote 2.
5 IIRC Pilot Programme Business Network.
6 IIRC Pilot Programme Investor Network.

Appendix — Requirements Under the <IR> Framework

Below are the requirements related to the preparation of an integrated report that appear in the <IR> Framework in bold italic type.

Using the Framework	
1E. Form of report and relationship with other information	1.12. An integrated report should be a designated, identifiable communication.
1F. Application of the Framework	1.17. Any communication claiming to be an integrated report and referencing the Framework should apply all the requirements identified in bold italic type unless: • The unavailability of reliable information or specific legal prohibitions results in an inability to disclose material information • Disclosure of material information would cause significant competitive harm. 1.18. In the case of the unavailability of reliable information or specific legal prohibitions, an integrated report should: • Indicate the nature of the information that has been omitted • Explain the reason why it has been omitted • In the case of the unavailability of data, identify the steps being taken to obtain the information and the expected time frame for doing so. 1.20. An integrated report should include a statement from those charged with governance that includes: • An acknowledgement of their responsibility to ensure the integrity of the integrated report • That they have applied their collective mind to the preparation and presentation of the integrated report • Their opinion or conclusion about whether the integrated report is presented in accordance with this Framework or, if it does not, it should explain: • What role those charged with governance played in its preparation and presentation • What steps are being taken to include such a statement in future reports • The time frame for doing so, which should be no later than the organization's third integrated report that references this Framework.
Guiding Principles	
3A. Strategic focus and future orientation	3.3. An integrated report should provide insight into the organization's strategy, and how it relates to the organization's ability to create value in the short, medium and long term and to its use of and effects on the capitals.
3B. Connectivity of information	3.6. An integrated report should show a holistic picture of the combination, interrelatedness and dependencies between the factors that affect the organization's ability to create value over time.
3C. Stakeholder relationships	3.10. An integrated report should provide insight into the nature and quality of the organization's relationships with its key stakeholders, including how and to what extent the organization understands, takes into account and responds to their legitimate needs and interests.
3D. Materiality	3.17. An integrated report should disclose information about matters that substantively affect the organization's ability to create value over the short, medium and long term.
3E. Conciseness	3.36. An integrated report should be concise.
3F. Reliability and completeness	3.39. An integrated report should include all material matters, both positive and negative, in a balanced way and without material error.
3G. Consistency and comparability	3.54. The information in an integrated report should be presented: • On a basis that is consistent over time • In a way that enables comparison with other organizations to the extent it is material to the organization's own ability to create value over time.
Content Elements	
4A. Organizational overview and external environment	4.4. An integrated report should answer the question: What does the organization do and what are the circumstances under which it operates?
4B. Governance	4.8. An integrated report should answer the question: How does the organization's governance structure support its ability to create value in the short, medium and long term?
4C. Business model	4.10. An integrated report should answer the question: What is the organization's business model?

4D. Risks and opportunities	4.23. An integrated report should answer the question: What are the specific risks and opportunities that affect the organization's ability to create value over the short, medium and long term, and how is the organization dealing with them?
4E. Strategy and resource allocation	4.27. An integrated report should answer the question: Where does the organization want to go and how does it intend to get there?
4F. Performance	4.30. An integrated report should answer the question: To what extent has the organization achieved its strategic objectives for the period and what are its outcomes in terms of effects on the capitals?
4G. Outlook	4.34. An integrated report should answer the question: What challenges and uncertainties is the organization likely to encounter in pursuing its strategy, and what are the potential implications for its business model and future performance?
4H. Basis of preparation and presentation	4.40. An integrated report should answer the question: How does the organization determine what matters to include in the integrated report and how are such matters quantified or evaluated?

Subscriptions

If you wish to receive *Heads Up* and other accounting publications issued by Deloitte's Accounting Standards and Communications Group, please register at www.deloitte.com/us/subscriptions.

Dbriefs for Financial Executives

We invite you to participate in *Dbriefs*, Deloitte's webcast series that delivers practical strategies you need to stay on top of important issues. Gain access to valuable ideas and critical information from webcasts in the "Financial Executives" series on the following topics:

- Business strategy & tax.
- Driving enterprise value.
- Financial reporting.
- Financial reporting for taxes.
- Governance and risk.
- Sustainability.
- Technology.
- Transactions & business events.

Dbriefs also provides a convenient and flexible way to earn CPE credit — right at your desk. Subscribe to *Dbriefs* to receive notifications about future webcasts at www.deloitte.com/us/dbriefs.

Registration is available for this upcoming *Dbriefs* webcast. Use the link below to register:

- Managing the Risks of Financial Crime: An Integrated Approach (January 30, 2 p.m. (EST)).

Technical Library and US GAAP Plus

Deloitte makes available, on a subscription basis, access to its online library of accounting and financial disclosure literature. Called Technical Library: The Deloitte Accounting Research Tool, the library includes material from the FASB, the EITF, the AICPA, the PCAOB, the IASB, and the SEC, in addition to Deloitte's own accounting and SEC manuals and other interpretive accounting and SEC guidance.

Updated every business day, Technical Library has an intuitive design and navigation system that, together with its powerful search features, enable users to quickly locate information anytime, from any computer. Technical Library subscribers also receive *Technically Speaking,* the weekly publication that highlights recent additions to the library. For more information, including subscription details and an online demonstration, visit www.deloitte.com/us/techlibrary.

In addition, be sure to visit US GAAP Plus, our new free Web site that features accounting news, information, and publications with a U.S. GAAP focus. It contains articles on FASB activities and updates to the *FASB Accounting Standards Codification*™ as well as developments of other U.S. and international standard setters and regulators, such as the PCAOB, the AICPA, the SEC, the IASB, and the IFRS Interpretations Committee. Check it out today!