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South African Integrated Reporting Committee

### **COMMENTS ON THE DISCUSSION PAPER: FRAMEWORK FOR INTEGRATED REPORTING AND THE INTEGRATED REPORT DD 25 JANUARY 2011**

We refer to the request for comments on the above discussion paper.

As a consultancy active in the field of sustainability reporting, *Environmental & Sustainability Solutions* (ESS) wishes to submit its comments on the discussion paper for consideration by the IRC.

If you have any queries regarding our comments, or require further elucidation, please feel free to contact us.

Kind regards

Seakle Godschalk  
Executive Director

COMMENTS BY *ENVIRONMENTAL & SUSTAINABILITY SOLUTIONS* ON DISCUSSION PAPER: FRAMEWORK FOR INTEGRATED REPORTING AND THE INTEGRATED REPORT DATED 25 JANUARY 2011

1. **Introduction.**

*Environmental & Sustainability Solutions* (ESS) is a boutique consultancy specialising in all aspects of sustainability accounting, including sustainability reporting. ESS is one of only two certified training providers on sustainability reporting in South Africa for the Global Reporting Initiative (GRI) and has now also been approved to offer the GRI certified course in Zimbabwe in partnership with the Centre for Environmental Accountability based in Harare. One of the partners of ESS, Seakle Godschalk, is currently finalising his M Com study on *The relationship between environmental reporting and financial reporting in South African mining companies*. ESS respectfully offers some comments in order to contribute to the development of theory and practice relating to integrated reporting.

2. **Focus of our comments.**

Although we do have concerns about the inclusiveness of the process followed to develop the discussion paper<sup>1</sup>, the way its presentation may be interpreted as being a final guidance document, and the offering of paid information sessions by participants in the IRC, our comments will focus on the substance of the discussion paper.

3. **Discussion Paper or Draft Framework.**

From the document it is not clear whether it is a Discussion Paper for broader discussion of the topic of Integrated Reporting or a draft Framework for Integrated Reporting and the Integrated Report released for comments. It appears more to be the latter. In that case the headings for sections 1.2 – 1.4 are not appropriate and should refer to the Framework etc. For the remainder of this document we will refer to the document as the draft IR Framework.

4. **One or more reports.**

Our main comment revolves around the potential confusion surrounding the relationship between an integrated report (IR) and the two other most relevant reports, i.e. the financial report (FR) and the sustainability report (SR).

- 4.1. Many communications regarding integrated reporting tend to imply that the IR will replace the FR and the SR, especially the latter. Again and again, we stumble upon remarks such as *“An increasing number of companies now produce integrated reports*

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<sup>1</sup> Soon after the announcement of the establishment of the IRC, Seakle Godschalk offered to get involved based on his post-graduate studies, which directly addresses the integration of environmental and financial reporting, as well as the GRI certified training on sustainability reporting he is offering. He was informed that the workgroup was already closed. His offer to brief the workgroup on the results of his research relevant to the subject matter was not taken up.

*rather than separate financial and sustainability reports”<sup>2</sup>*, or words to that effect. Even the media release accompanying the release of the draft IR Framework adds to this confusion by unqualified statements referring to the IR replacing the traditional annual report. The use of such unqualified terminology adds to the confusion and misperceptions rather than defuse it.

- 4.2. Although for smaller organisations it may be possible to integrate their financial report and their sustainability report into one integrated report, for medium and larger organisations this would not be possible or even desirable given the purpose of the IR. The IFRS requirements for financial reporting and the GRI “requirements/expectations” for sustainability reporting do result in extensive and focused individual reports (FR and SR). To just combine them into one report would be impractical as well as defeat the whole purpose of integrated reporting. Therefore, the concept of an IR as a higher level strategic document that integrates the most material issues from the FR and the SR and the interrelationships between them, is strongly supported. In that sense the IR could be viewed as a replacement of the Annual Report.
- 4.3. The draft IR Framework does bring out the above-mentioned approach on several places, however, not clearly enough. The relationship between these three types of report<sup>3</sup> (IR, FR and SR) and the respective purpose of each one should be much more clearly discussed. Currently, it is hidden away in by-the-way remarks throughout the document. A dedicated discussion of this should be included early in the document to put the guidance provided in perspective. This will make the document much clearer and avoid any confusion readers may already have or develop when reading the document.
- 4.4. The clear distinction between these three types of reports does have substantial impact on the discussion of processes, principles, stakeholder engagement and assurance. Much of this discussion in the draft IR Framework tends to create the impression that the development of the IR is a separate process and that principles, stakeholder engagement and assurance involved in the IR are viewed in isolation. This should be addressed as the process involved in integrated reporting should be truly integrated process, not a third process on its own.

## 5. **Reporting principles.**

The first aspect where the incomplete discussion of the relationship between the various reports becomes evident is in the discussion of the reporting principles (chapter 2). The extensive discussion of all the basic reporting principles may reinforce the misperception that the IR process is separate from the FR and SR processes.

- 5.1. The relationship between the application of the reporting principles in the various reports should be the focus of this chapter rather than an extensive discussion of all the

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<sup>2</sup> GRI in its 2011 News Item on “Sustainability data hidden in online reports”

<sup>3</sup> Although other reports may contribute to the IR, the main contribution comes from the FR and the SR. Reports such as a Carbon Footprint, could even be regarded as sub-reports for the SR.

principles that are relevant to all the reports. In principle, there should not be any difference in the application of the basic reporting principles between the IR, FR and SR. However, the different nature and level of these reports may require a differentiated approach to the application of some principles, e.g. in terms of the level of materiality.

- 5.2. In principle, the boundary of the IR should be the same as the boundary for the FR and the SR, otherwise it would be difficult to talk about integrated reporting. If for some reason the boundary for the financial information and the sustainability information would be different, the implications thereof on the information provided should be explicitly disclosed.
- 5.3. In terms of the application of different levels of materiality between the FR/SR on the one hand and the IR on the other hand, some more guidance on how to determine appropriate materiality levels for the IR compared to the other two reports would be useful. This IR Framework should provide guidance on those aspects which are unique to IR.
- 5.4. It is not clear why the term Neutral was preferred above Balanced (the GRI name for this principle). Neutral implies in-between, not positive, nor negative. Balanced is a better description, including both positive and negative.
- 5.5. The Free from Error principle seems to be redundant. In respect of omissions it overlaps with the Neutral principle, whilst the concept of free from error reporting is obvious/self-evident and does not require a principle.

## **6. Reporting process.**

The reporting process outlined in Annex 2 could lead to misunderstanding of the IR process as a stand-alone process. The linkages between the FR and SR processes, which feed into the IR process, are not clearly described. It is suggested that the linkages between these processes be discussed in more detail and that appropriate guidance on this be provided.

## **7. Stakeholder engagement.**

The discussion of step 4 of the process once again seems to create the impression that a separate stakeholder engagement process should be implemented. If we assume correctly that the IR is based on the FR and the SR, it becomes even questionable whether stakeholder engagement should be discussed as an activity in the IR process at all, as the main stakeholder engagement should take place in the FR and in particular the SR process. As no new information should be addressed in the IR and the focus of the IR should be on the integration of financial and sustainability information, no additional or separate stakeholder engagement for the IR should be required.

**8. Assurance.**

- 8.1. The discussion on assurance is the fourth aspect which suffers from the lack of a clear understanding and discussion of the relationship between the IR, FR and SR. If we once again assume that the FR and the SR feed into the IR, and that the IR should not contain new information as such, but focuses on the integration of financial and non-financial information, the question can be asked what the role of assurance of the IR would be. The FR needs to be assured/audited in terms of legislation. The SR should preferably be assured – although not legally prescribed – as it contains all the detailed sustainability information. It appears as if assurance of the IR would result in a duplication of effort and a huge additional expense, with no obvious benefit, as the information and principles applied would already have been assured in the SR and the FR.
- 8.2. Although brief mention is made of the AA1000AS assurance standard, Chapter 4 seems to favour assurance based on ISAs, i.e. by auditors. If the content of assurance statements performed by the 4 big audit firms is compared with the content of assurance statements by specialist consultancies, this tendency in favour of an ISA based assurance can be questioned. Assurance statements by non-auditor consultancies are generally more comprehensive and useful to readers of the SR, than those by the audit firms. This is to a large extent based on the limitations applicable on audit professionals in what they can include in an assurance statement.
- 8.3. The so-called combined assurance approach mentioned in the King III Report, refers to combining the ISAE3000 and the AA1000AS methodologies, assuming that ISAE3000 refers to data assurance whilst AA1000AS would then refer to principles-based assurance. This assumption misses the point that an AA1000AS Type II assurance is exactly a combination of the principles-based assurance and an information/data-based assurance. AA1000AS is, therefore, more comprehensive and useful for assuring sustainability information than the ISAE3000 standard.
- 8.4. In Chapter 4 of the draft IR Framework, the concept of combined assurance is mentioned but in a different way than the King III Report. Paragraph 5 of this chapter seems to focus on a “combination” of various forms of audit with “any other external assurance provider, such as ISO certification and BEE verification” making up the tail-portion. This paragraph which seems to sum up the various components of a “combined assurance strategy” does not even refer to AA1000AS based assurance, whilst this is the most important form of assurance of sustainability information, and on a completely different level as ISO and BEE certification/verification which only address a very limited part of sustainability information. This is a major flaw and should be corrected.

**9. Determining materiality.**

The new G3.1 GRI Guidelines for Sustainability Reporting, which was released in March 2011, should be referenced in the box on page 20, in particular the Technical Protocol on Applying the Report Content Principles.

10. **King III's principles of integrated reporting and disclosure.**

The principles listed in the box on the bottom of Annex 1 are laudable but not contained in the King III Report. As far as we remember, these were the reporting principles in the draft King III Report but were replaced by the current principles 9.1-9.3 in the King III Report. The content of some of these principles are contained in the text of Chapter 9 of the King III Report, but not as principles anymore.

11. **Conclusion.**

The draft IR Framework contains laudable guidance for taking business reporting to a next level of integration. However, it suffers from a lack of clarity on the relationship between various reports and how they linked to each other. This affects much of the discussion in the document. It is recommended that the draft IR Framework be completely overhauled to start off with a clear discussion of the relationship between the FR, the SR and the IR, and that the subsequent guidance be tailor-made to support this relationship.