

<IR> Framework Exposure Draft Response

*Submitted online in a survey format to IIRC August 14, 2020 by The IIA and Richard F. Chambers, CIA, QIAL, CGAP, CCSA, CRMA
President and Chief Executive Officer
The Institute of Internal Auditors*



TESTING <IR> FRAMEWORK REVISIONS

Open feedback

The IIA recognizes the valuable role the <IR> Framework plays as organizations operationalize sustainability and business risks related to ESG issues, and the practical guidance it provides for governing bodies and management.

To that end, The IIA encourages the IIRC to position the Framework more strongly as a tool for internal audiences, especially the governing body. The tool is a way not just to publish an external report, but also – and more importantly – to build a comprehensive, long-term, and integrated picture of the organization, its performance, its prospects, its impacts on and by the external environment, and how all of this supports or frustrates strategic goals.

An internal integrated report would provide the governing body the overarching and objective view it needs to exercise effective oversight, an essential step prior to any thoughts of external disclosures.

Such an internal integrated report would require an organization to evolve its mindset and practices consistent with “integrated thinking.” Many sources of information need to be drawn together, requiring independent and objective assurance to ensure credibility that can be most usefully provided by internal audit. Internal audit’s authoritative knowledge of the organization, together with its independence from management and from the responsibilities of management, allow it to provide confidence and to create a more complete and integrated picture. The internal audit positioning, mindset, and approach are very much in tune with “integrated thinking.”

Statement of responsibility for an integrated report

Q1: Do the adjustments to paragraph 1.20 simplify the statement of responsibility in an effective way?

Paragraph 1.20 is simplified with the removal of the required commentary on the application of a collective mind and plans for a future statement of responsibility. However, it does not go far enough to provide transparency to the audience, because there is no mention of establishing confidence in and credibility for what is included in the integrated report. Internal audit is ideally positioned to convey both and is routinely tasked with providing assurance to the governing body on all aspects of the organization’s activities. We believe this function is an important addition to the <IR> Framework, and there should be disclosure of the efforts made to provide assurance.

Q2: Does the framing of process disclosures meet the goals of promoting accountability and integrity while still providing flexibility?

Accountability and integrity require transparency. This section needs to include the role internal audit plays throughout the organization, providing assurance on data collection processes and on the reliability of data used in the report.

The statement referenced in Paragraph 1.20 from “those charged with governance” acknowledges their “responsibility to ensure the integrity of the integrated report.” Paragraph 1.20 goes on to say: “This statement is enhanced by supplementary disclosures on the process followed to prepare and present the integrated report. These disclosures can include, for example:

- “Related systems, procedures and controls, including key responsibilities and activities
- “The role of those charged with governance, including relevant committees, in the process of preparing and presenting the integrated report.”

We believe this is an opportunity to modernize the Framework by specifically describing the role of internal audit as an integral part of effective governance and a major contributor to the improvement of disclosure reporting by assuring the accuracy and completeness of information for the governing body.

Internal audit provides a tool for organizations to share information that has been verified and to build trust.

Q3: Does the Consultation Draft strike an appropriate balance between maintaining a principles-based approach and usefully informing preparer considerations?

It would be useful to include principles of good governance, and specify that the head of audit provides integrated assurance to the organization. The global International Professional Practices Framework (IPPF) specifies that the head of audit should share information, coordinate activities and consider relying upon the work of other internal and external assurance and consulting service providers to ensure proper coverage and to minimize duplication of efforts.

Those charged with governance

Q4: Does the Glossary sufficiently clarify the potential inclusion of management personnel in the scope of those charged with governance?

To clarify the phrase “those charged with governance,” we believe it is important to shift to discussing “a system of effective governance.” Clarification in this way will improve the Framework by introducing the concept that a system of effective governance includes the critical roles played by the governing body, executive management, and an independent internal audit function. Governance is strongest when these three roles are performing their responsibilities effectively and are sufficiently aligned. Grounding the Framework in The IIA’s [Three Lines Model](#) of governance — accountability, actions (including managing risk), and assurance, all aligned — is most effective and widely recognized.

Q5: Do paragraphs 1.21 and 1.22 sufficiently recognize variations in governance models?

Paragraph 1.22 is an appropriate place to not only recognize variations in governance models but to connect readers with internal audit’s indispensable role in governance. The paragraph clearly states the intent of 1.20 is “to promote the integrity of the integrated report through the commitment of the highest oversight or decision-making body.” Internal audit is an independent role able to provide insight to management and the governing body on organizational risks.

We believe the Framework should ask that organizations that publish integrated reports indicate the extent to which internal audit has played a role in evaluating or monitoring internal systems and controls over the content of the report, including, and especially, nonfinancial matters.

By definition, internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization achieve its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, controls, and governance.

This can be added to amplify section 3F Reliability and Completeness, where the Framework states that reliability of information is "enhanced by mechanisms such as robust internal control and reporting systems, stakeholder engagement, internal audit or similar functions, and independent, external assurance."

Internal audit's role in providing independent assurance should be spelled out specifically and separately as a key benefit. This has precedent in the United States, where internal audit typically tests internal controls over financial reporting before they are subject to external assurance by the financial auditors. External assurance providers are limited by statutory, regulatory, and professional standards for what they can (and cannot) do, and what they can (and cannot) sign. Internal audit takes a more holistic risk-based approach.

Business model considerations

Q6: Does paragraph 4.19 sufficiently differentiate outputs from outcomes?

Yes. However, it should be noted that measuring outcomes is potentially very complex. It is difficult enough to do so for financial capital and much more so for nonfinancial capitals. In financial reporting, it is not at all common to try to report outcomes (or impacts). Without sufficient clarity on how it can be achieved, it is a significant difficulty for implementation of the Framework.

Q7: Does Figure 2 effectively distinguish outputs from outcomes and link outcomes to value creation, preservation or erosion?

No, it does not effectively distinguish outputs from outcomes. As an illustrative example, Figure 2 is too complex to be helpful, and doesn't make clear the expression "value creation." Because the word "value" is not in the figure, and appears only outside the figure in the title, it could be confusing as a standalone.

Q8: Does the final sentence in paragraph 4.19 sufficiently encourage evidence-based reporting of outcomes?

Providing evidence to back up claims and conclusions is in the spirit of the Framework, but it introduces significant complexity that is not required for financial reporting, nor by other nonfinancial reporting frameworks (e.g., GRI).

Q9: Does the increased emphasis on value preservation and value erosion encourage more balanced reporting of outcomes?

Yes. While it seems logical that "value creation" is generally understood as a net positive change in capital, one can talk of zero value creation (i.e., preservation) or negative value creation (i.e., erosion).

Treatment of impacts

Q10: Does the closing sentence of paragraph 4.20 sufficiently address the coverage of impacts under the term ‘outcomes’?

Yes, the addition of positive and negative effects and looking at the organization’s wider impacts could encourage more balanced reporting. However, impacts on society and nature do not cover the full range of the six capitals, so it is important to broadly reference impacts.

CHARTING A PATH FORWARD

Purpose of an integrated report

Q11: Should paragraph 1.7 extend beyond providers of financial capital alone to include providers of other forms of capital?

We suggest the entire reference to audience be deleted and the definition rewritten to read: “The primary purpose of an integrated report is to explain how an organization impacts capitals in its pursuit of value over time.”

This change supports the shift from a financial capital focus to multi-capitalism, and removes the emphasis of investors above those of other stakeholders. It helps lead to a much broader view of value impact, which can be positive and negative, rather than using the term “create value,” which implies positivity.

This also better matches the language used to explain the purpose of an integrated report elsewhere in the Framework. For example, 2.2 reads: “An integrated report explains how an organization creates value over time.” We suggest this be changed to “impacts value.”

External reporting standards and frameworks

Q12: Do you support the creation of a resource outside the <IR> Framework (e.g. an online database) to showcase authoritative sources of indicators and methodologies across the capitals? If yes, to which standards, frameworks or initiatives should the resource point?

Yes, but its creation would have to be carefully considered, as this resource would require a dedicated manager and constant upkeep. To be valuable, it should point to all standards, frameworks and initiatives available.

Integrated thinking

Q13: Should the IIRC address the concept of integrated thinking more deeply? If yes, what additional guidance is needed?

Yes, and internal audit has an important role in this space given its responsibilities within organizations. The internal audit profession looks beyond financial reporting to provide transparency and insight into all facets of an organization’s governance, controls, risk management, and, ultimately, the integrity of the nonfinancial information it provides.

It is important to provide guidance that the communication of nonfinancial information does not begin and end with the report. The IIA believes that, for nonfinancial information to be valuable, it requires an organization to think, plan, operate and communicate with sustainability in mind at every step.

Internal audit is a key partner for external auditors tasked with sustainability reporting because it typically has made the whole “integrated thinking” journey with the organization, and is therefore the resident expert to provide independent and objective assurance on all the structures and processes needed to gather, validate, analyze, and report nonfinancial data.

The COVID-19 pandemic has amplified the interconnectedness of organizations, and internal audit’s expertise and unique role has proven valuable in helping organizations move from crisis management, to issues management, to short-term risk management, to long-term risk management in order to find success.

If external audit practitioners focus exclusively on assurance of the external report, with no account of the preparation and stages an organization needs to go through to be ready to even think about making such disclosures, the practitioners may struggle to deliver a service to the client organization in the most effective and efficient manner.

Technology

Q14: Should the IIRC explore the role of technology in future corporate reporting as a priority? If yes, what technology considerations should be addressed?

Technology will continue to have a major impact on data gathering, analysis, and reporting, as it creates opportunities to leverage huge amounts of data, deploy continuous monitoring and assurance techniques, and communicate rapidly to multiple stakeholders in customized ways.

An increase in the role of technology raises questions about the ethical use of data and the need for greater control and security over personal information. One might like to consider that data is a kind of capital. Certainly, intellectual and financial capital may be captured, stored, processed, and transmitted digitally.

Changes in the way people consume data will need to be recognized and accommodated. Continuous monitoring and continuous reporting will become common, and can be embraced through innovations in risk management. The ability for instant communication and the collection of massive amounts of data daily mean the technology must handle everything from 24/7 updates and dashboards for online viewing of timely data to the potential intrusion of social media trolls and the demands of strict data privacy laws.

The Framework should emphasize the connectivity of information to communicate how value is created over time, and how outcomes are supported by innovation and automation.

It is most important to embed the idea of long-term value and sustainability in the everyday strategy of the organization and at the front end of new technology to capture data points for appropriate use. Sustainability doesn’t work as a stand-alone, it must be everyone’s job every day. Much like managing risk, an organization doesn’t manage operations then manage risk. It must do it all at once.

Open feedback

Q15: Please provide any other comments not already addressed by your responses to Questions 1 – 14.

See introduction.