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Financial Reporting Council
8th Floor
125 London Wall
London, EC2Y 5AS
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RE: A Matter of Principles, The Future of Corporate Reporting

Dear Sir Jon,

IFAC welcomes the opportunity to comment on the FRC's Discussion Paper (A Matter of Principles, The Future of Corporate Reporting, "the DP" or "Discussion Paper"). We applaud the FRC's leadership in prompting this important conversation about the future of corporate reporting. IFAC supports including a broader range of information in corporate reporting so that organizations can communicate more effectively—and stakeholders can better understand—prospects for longer-term value creation.[1] Our most recent points of view are presented in our policy paper on ***Enhancing Corporate Reporting***, our call-to-action for a new sustainability standards board—***The Way Forward*** (issued in September 2020), and our response to the IFRS Foundation Consultation on Sustainability Reporting. We believe our views are broadly consistent with those of the five leading integrated and sustainability reporting organizations, as set out in joint papers they have issued in 2020.[2]

As the global voice of the accountancy profession, IFAC represents over 170 Professional Accountancy Organizations in 130 jurisdictions, thereby representing over three million professional accountants. As such, our goal is to bring an international perspective to these conversations and encourage the identification of areas of alignment between jurisdictions. We believe the accountancy profession has an important voice in advocacy for initiatives that enhance communication between companies and their stakeholders.

In this context, we address some of the key issues raised in the Discussion Paper.

Overview

It is IFAC's view that corporate reporting should capture all relevant information about organizations. We acknowledge that investors and other stakeholders are demanding more, higher-quality information and insights about company performance, risks, opportunities, and long-term prospects than are available from the conventional financial reporting process.[3] These themes are consistent with many of the underlying challenges identified in the DP—that stakeholder expectations have changed, that the annual report is

[1] For example, IFAC's long-standing partnership with the International Integrated Reporting Council demonstrates our support for reporting that brings together the relevant information about a company, provides a holistic picture of performance, and provides insights on an organization's ability to create sustainable value over time.

[2] CDP, CDSB, GRI, IIRC, and SASB ("The Five"). See their joint Statement of Intent to Work Together Towards Comprehensive Corporate Reporting and their open letter to IOSCO.

[3] Enhancing Corporate Reporting | IFAC

serving multiple audiences, that the interests of investors has broadened, and that non-financial reporting has evolved.[4]

For corporate reporting to be decision-useful to stakeholders, the information reported (financial and non-financial) must be relevant, reliable, and comparable.[5] Therefore the benefits of contemplated reforms such as the Reporting Network, must be considered in context of clarity and comparability for investors and other stakeholders. This should be the case through initial implementation, over the longer term, and across industries and national boundaries. Sufficient clarity is needed so that organizations can implement new reporting requirements with understanding of i) what is required, ii) what is voluntary, iii) how various components of the reporting network connect (vs. overlap or duplicate), and iv) what is the cadence of interim reporting.

We also note the preeminent role of the annual report in jurisdictions around the world. While we welcome the FRC's consideration of the future value of annual reports to investors and other stakeholders, it is also important to reflect on the risk of regulatory fragmentation that could result from its reform. IFAC looks forward to this ongoing discussion about improving the relevance and focus of how companies communicate with stakeholders while maintaining sufficient reliability and comparability for the benefit of all users.

In this context, IFAC conducted extensive outreach in 2020 with its stakeholders around the world (i.e., regional round table sessions and bilateral interviews in jurisdictions across Asia-Oceania, Africa, the Caribbean, Europe, Latin America, and North America) on the role and nature of sustainability-related reporting—an important aspect of broader corporate reporting. We spoke out—in various public consultations—and called for the IFRS Foundation to create a new sustainability standards board alongside the IASB.[6] We strongly believe that the public interest is best served by a harmonized global system, rather than a fragmented, jurisdiction-specific approach. Below we address some of our key findings with relevance to the DP.

Non-Financial Reporting

The Discussion Paper's significant focus on non-financial reporting is appropriate. We note many similarities with the views that IFAC voiced in The Way Forward towards a ***global*** approach to reporting sustainability information and in our comment letter to the IFRS Foundation's recent consultation. We

[4] Figure 1 – Future of Corporate Reporting.
NOTE: As stated in IFAC's Enhancing Corporate Reporting policy paper, we view "non-financial" information to include measures derived from the financial statements (i.e., "non-GAAP" or "non-IFRS" measures), other "Key Performance Indicators" connected to financial performance, and broader information related to value creation (including intangibles), sustainability or environmental, social, and governance factors. "Sustainability" information is therefore somewhat narrower in scope—typically understood to focus most on environmental, social, and governance factors. This said, we believe that many of the same underlying principles for high-quality corporate reporting apply to both terminologies and that much of the broader information needed to address a wider stakeholder base are majorly captured by the various sustainability frameworks of CDP, CDSB, GRI, IIRC, and SASB. Therefore, we view "sustainability" and "non-financial" as being somewhat interchangeable within the context of this letter.

[5] Enhancing Corporate Reporting

[6] IFAC Response to Consultation on Interconnected Standard Setting – Accountancy Europe

IFAC Response to WEF Consultation: Toward Common Metrics and Consistent Reporting of Sustainable Value Creation

IFAC Response to the European Commission Review of the Non-Financial Reporting Directive

IFAC Perspective on Proposed Rule Governing ESG Information in US Pension Plan Investment Decisions

The Way Forward

agree with the FRC's assessment that "a multitude of voluntary frameworks…creates a confusing landscape for companies and results in a lack of relevant, reliable, comparable, and balanced information for users." Global standards ***are*** needed for sustainability and broader non-financial reporting.[7]

In supporting the establishment of a new sustainability standards board under IFRS (i.e., an "SSB"), we recognize that harmonization, consolidation, and evolution of a global reporting system that includes both financial and non-financial information on equal footing is a journey. We agree that the leading voluntary frameworks and standards are "building blocks towards the long-term vision."[8] The collaborative work of The Five provides standards and frameworks that serve as a starting point for a new SSB. Their work also provides the architecture for reconciling differing materiality preferences. We believe that the "Building Blocks" detailed in IFAC's The Way Forward are consistent with the FRC's view that stakeholders require information about "both how the ecosystem in which it [a company] operates can have an effect on the sustainability of the company's business model, and how the company's business model is affecting this ecosystem."[9]

We support an approach that both accommodates the need for investor-focused reporting requirements, while allowing multi-stakeholder-focused requirements (e.g., those of GRI) to progress in parallel. We encourage the FRC to remain focused on the role of sustainability/non-financial reporting—and alignment with the emerging global system—as you continue to contemplate the future of corporate reporting.

Materiality

In the context of including information other than traditional financial information and addressing the information needs of multiple stakeholders, IFAC agrees that the future of corporate reporting will not necessarily rely on a single, conventional, definition of materiality. The recent collaborative work of The Five adopts the concept of "dynamic materiality," which goes beyond both traditional investor-focused materiality, as well as the static "double materiality" contemplated in the European Union's ongoing work. In this new framework, matters (sustainability-related) can transition from being important to an enterprise's positive/negative impacts on economy, environment, and people; to being important to the enterprise's value creation (for economic decisions); to being material under the definitions applied to the enterprise's

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[7] See Section 6.4 of A Matter of Principles

[8] See Section 6 of A Matter of Principles – "We welcome the moves towards coalescence of voluntary frameworks in this area and consider that some of the existing voluntary frameworks could be building blocks towards the long-term vision.

[9] See Section 6.6 of A Matter of Principles.

IFAC's The Way Forward outlines three components—Building Blocks—of the system for setting standards for non-financial information such as sustainability information.

BLOCK 1: The SSB should establish a core set of standards addressing sustainability through an investor-focused lens—requirements for material non-financial information focused on company performance, risk profile, economic decisions and "enterprise value creation." This information will be of interest to investors, is consistent with the work of the IASB, and will attract global support.
BLOCK 2: The SSB should also collaborate with respect to reporting requirements primarily designed to address broader, material sustainable development and company impacts on economy, environment, and people. These requirements may ultimately be incorporated or endorsed into SSB standards.
BLOCK 3: A global system must anticipate some jurisdictions-specific requirements that support local public accountability. For example, societal goals or policy initiatives like the European Union's Green Deal may drive country/region-specific regulatory reporting requirements on sustainability factors above and beyond global norms for such requirements—meaning specific, additional metrics or disclosures, not changes to or customization of standards otherwise in Blocks 1 or 2.

This explanation of a 3-block approach is consistent with the recommendations of The Five as expressed in their joint, open letter to IOSCO. (September 30, 2020) primary financial statements.[10] We believe that dynamic materiality is consistent with the IFAC Building Block approach (see footnote 9) and aligns with the FRC's focus on linking materiality to the specific objectives of each report in the proposed Reporting Network.[11] IFAC encourages embedding dynamic materiality into the future of corporate reporting to accommodate a multi-stakeholder context and to align with the evolving work of The Five and a new SSB.

Objective-Driven Reporting

We have highlighted important areas of alignment between innovations presented in the DP and the evolving global framework for reporting sustainability information. However, dynamic materiality reflects the fact that "distinctive materiality concepts are supported by distinctive standard-setting processes." In other words, the objectives of different users have driven demand for enhancing corporate reporting and supported multiple, alternative standard-setting activities.[12]

The recently announced combination of SASB and the IIRC to form the Value Reporting Foundation (with the possibility of also incorporating CDSB) suggests that various value creation-focused reporting initiatives could ultimately reside within one entity.[13] Consistent with this consolidation, the recently revised <IR> Framework continues to be primarily investor-focused, while also recognizing the value of information in an integrated report to other stakeholders.[14] The proposed objective of the Business Report aligns well with such value creation-focused reporting requirements.

While we agree that the needs of different user groups are not mutually exclusive,[15] we caution that the proposed Network Reports, based on their different ***communication*** objectives, might misalign with the evolution taking place in the integrated and sustainability reporting ecosystem. Specifically, the Business Report may better deliver on its objectives if investor-focused (not neutral), while the Public Interest Report may do likewise if focused on broader stakeholders. Maintaining a primary user focus (i.e., providers of capital in the Business Report and multi-stakeholders in the Public Interest Report) should not be presumed to obfuscate the value of information presented and may better drive sufficient clarity to preparer organizations about what, where, and how to report information. Further, various elements comprising the

[10] See Figure 1, page 5 of Statement of Intent to Work Towards Comprehensive Corporate Reporting.

[11] See Section 4.3 of A Matter of Principles.

[12] See page 10 of Statement of Intent to Work Towards Comprehensive Corporate Reporting

Also, SASB's 2020 Conceptual Framework Exposure Draft (See page 24) explains The Five's materiality analysis by saying that "…perspectives on the materiality of sustainability information vary by user and use case. Some users are primarily interested in how sustainability issues impact a company's financial performance and contribute to enterprise value creation; other users are interested more broadly in how a company's actions impact society and contribute to sustainable development. Some users are interested in both perspectives."

[13] IIRC and SASB announce intent to merge in major step towards simplifying the corporate reporting system

Also see response to question 5 of the Climate Disclosure Board's (CDSB) response to the IFRS Foundation Consultation Paper on Sustainability Reporting.

[14] "The primary purpose of an integrated report is to explain to providers of financial capital how an organization creates, preserves or erodes value over time. It therefore contains relevant information, both financial and other. An integrated report benefits all stakeholders interested in an organization's ability to create value over time, including employees, customers, suppliers, business partners, local communities, legislators, regulators and policy-makers." Page 11, section 1C, International Integrated Reporting Framework.

[15] See Section 2.1 (Objective-driven reports) of A Matter of Principles.

In IFAC's comment letter to the IFRS Foundation (page 12, question 9), "We acknowledged that some aspects of multi-stakeholder-focused reporting requirements [e.g., under GRI] can also inform investor decisions."

Reporting Network (i.e., the mandatory reports plus any voluntary reports) should present an interconnected (not siloed) picture of financial performance, business model, prospects for value creation, etc.

Other

Ecosystem: In ***The Way Forward***, IFAC highlights important changes that are needed to complete a future-fit, global ecosystem for corporate reporting—including the assurance of non-financial information, enhanced skills for professional accountants, digital readiness, corporate controls and data systems that can deliver new types of high-quality information, enhanced corporate governance over expanded reporting obligations, among others. We encourage the FRC to also consider these important, necessary changes as it refines proposed changes in U.K. corporate reporting. As IFAC engages with stakeholders and speaks out on in the coming months on these important topics, we encourage and welcome the FRC's input.

Assurance: IFAC believes that assurance is critical to confidence in corporate reporting. IFAC supports additional work towards the evolution of assurance practice with respect to non-financial information and we urge the FRC to consider the assurability of future reporting requirements. Alignment of jurisdiction-specific corporate reporting requirements with the work of standard-setting bodies (such as the SSB and members of The Five) and an agreed global reporting framework will support the International Audit and Assurance Standards Board's work to ensure there is a robust, international framework for the assurance of non-financial information.[16]

Proportionality: IFAC notes the critical role of SMEs in the global economy—representing over 90% of the business population, 60-70% of employment, and 55% of GDP in developed economies.[17] From this perspective, their collective economic contribution suggests that their relevance to sustainability factors, especially sustainable development and impacts, should not be overlooked. However, their aggregate economic weight is not representative of their individual limited resources. Therefore, the cost to SMEs of compliance with reporting requirements warrants consideration by regulators. We support the FRC taking a pragmatic, proportionate approach to requirements for the Business Report and Public Interest Report, subject to clear/appropriate metrics for defining small versus medium-size entities.

Technology: We agree with the approach of the DP that puts questions around technology at the heart of the discussion. Initiatives like the European Single Access Point demonstrate that we are on the verge of radically new ways in reporting data. This follows the digitalization of how users consume reported information that has occurred in the past decades. Any changes to reporting requirements must be designed to best leverage the technology of today, but also nimbly pivot to best leverage the technologies of tomorrow. This will require active engagement with a diversity of users, reporting entities and technology providers. At the same time, "traditional" users of reported information must not be left behind.

Timeliness: The pace of change in non-financial reporting requirements (i.e., in the European Union, in the U.S., in Korea, in New Zealand and other jurisdictions) and the evolving global ecosystem suggest that the intended benefits of proposed changes in U.K. corporate reporting are timely. The current environment affords an opportunity for the FRC to align its efforts with the IFRS Foundation and play a leading role in rational, systemic changes to the future communication between companies and their stakeholders.

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[16] See International Standard on Assurance Engagements 3000 (Revised), ***Assurance Engagements Other than Audits or Reviews of Historical Financial Information***, as well as the IAASB Consultation on Extended External Reporting (EER) Assurance.

[17] World Trade Report 2016, Levelling the trading field for SMEs.

Conclusion

Thank you again for bringing these issues into the public arena for analysis and discussion. IFAC stands ready in its capacity as convener and voice of the global accountancy profession to provide any future assistance. We would welcome continuing discussion with the FRC on these and other important matters.

Sincerely,

Kevin Dancey, CEO