Volume : 2 | Issue : 4 | April 2013 • ISSN No 2277 - 8160

Research Paper | Accountancy

Integrated Reporting: Challenges and Opportunities

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ABSTRACT *Integrated Reporting brings together material information about an organization's strategy, governance, performance and prospects in a way that reflects the commercial, social and environmental context within which it operates. It provides a clear and concise representation of how an organization demonstrates stewardship and how it creates and sustains value. In other words, Integrated Reporting refers to the integrated representation of a company's performance in terms of both financial and non-financial results. Integrated reporting provides greater context for performance data, clarifies how sustainability fits into operations or a business, and may help embed sustainability into company decision making. Some companies that report in an integrated manner also report additional sustainability information, often online, for specific stakeholder groups.*

KEYWORDS: INTEGRATED REPORTING

❖ What is Integrated Reporting?

Integrated Reporting brings together material information about an organization's strategy, governance, performance and prospects in a way that reflects the commercial, social and environmental context within which it operates. It provides a clear and concise representation of how an organization demonstrates stewardship and how it creates and sustains value. In other words, Integrated Reporting refers to the integrated representation of a company's performance in terms of both financial and non-financial results. Integrated reporting provides greater context for performance data, clarifies how sustainability fits into operations or a business, and may help embed sustainability into company decision making. Some companies that report in an integrated manner also report additional sustainability information, often online, for specific stakeholder groups.

❖ An International Framework

The International Integrated Reporting Committee (IIRC) is developing an International Integrated Reporting Framework that will facilitate the development of reporting over the coming decades. The core objective of the Framework is to guide organizations on communicating the broad set of information needed by investors and other stakeholders to assess the organization's long-term prospects in a clear, concise, connected and comparable format. This will enable those organizations, their investors and others to make better short and long-term decisions.

The initial focus is on reporting by larger companies and on the needs of their investors. The Framework will help to elicit consistent reporting by organizations, provide broad parameters for policy-makers and regulators and provide a focus for harmonizing reporting standards.

❖ Reasons Why Integrated Reporting can be a Game Changer

All you need in order to understand why integrated reporting is so important to the future of sustainable business is to read a truly integrated report. After reading one and comparing with a regular sustainability report you won't need any further explanation. *Here are five reasons why, including the challenges that each one presents:*

❖ Integrated reporting can spur actions, not just display them

According to Eccles, right now "many, if not most, sustainability reports are more window dressing than substance and so aren't very effective at influencing the company's resource allocation decisions." He believes there's a much greater potential in reporting, both externally and internally, and integrated reporting is the way to take a full advantage of it.

It means that integrated reporting doesn't only demonstrate the linkages between an organization's strategy, governance and financial performance and the social, environmental and economic context within which it operates, as the IIRCdefines it, but is also an integrator of sustainability into a company's core business.

Challenge: Enhancing the role of an integrated report from a greenwash gatekeeper into a sustainability driver isn't easy at all. It's clear that an integrated report can help spot dishonesty or incoherence, but can it really be an eye opener and a driver for change for a company?

❖ Integrated reporting will help developing the metrics everyone is waiting for

One of the main problems in the sustainable business space today is the lack of clear metrics, translating social and environmental issues into business language, i.e. figures. The GRI standards, the most common framework used by companies for reporting hasn't been able to fill this void yet. Integrated reporting is supposed to change it by including ESG metrics, like the ones that companies like Puma are experimenting with these days. It's going to be an important step for investors and other stakeholders as well as a way to encourage competition between companies over who is more sustainable.

Challenge: First, creating valuable yet simple metrics. No one really did it to date. Second, how you compare apples to apples? As Eccles mentions in the interview, there's still a debate between setting a generic set of standards applicable across all industries, or sector-specific. "That would be a fundamental, strategic decision. On the one hand, it's good to have a set of metrics that are applicable to any circumstances, so that you can compare apples to apples. On the other hand, when you get into the sustainability, nonfinancial measures, ESG metrics, whatever you want to call them, what's important tends to vary by sector," he said.

❖ Integrated report to sustainability report is like shared value (CSV) to CSR

In other words, integrated reporting reframes the whole idea of value creation, providing an alternative to an existing model that provides very little value. Integrated reporting is also offering a better alternative to what we have now, which Eccles describes as ineffective and invaluable system. It's no wonder there's a clear similarity between the way Porter describes shared value and the way Eccles describes the opportunity in integrated reporting: "Good companies will see integrated reporting as an opportunity to communicate on and implement a sustainable strategy, which I define as one that creates value for shareholders over the long term while contributing to a sustainable society."

Challenge: Both integrated reporting and CSV sounds great in theory and have some solid examples from companies that already implement them, yet the substance behind their promise is not clear yet, and it's also not that obvious that the majority of companies will truly benefit from implementing them.

❖ Creating a global regulated sustainability reporting system

So far all the frameworks we have, from Global Reporting Initiative (GRI) reportsto Carbon Disclosure Project (CDP) surveys are voluntary. Thousands of companies use these frameworks, but a greater number of companies don't. As Eccles mentions, to achieve the goals behind integrated reporting at a global scale means "that integrated reporting needs to be a mandatory, not voluntary, exercise." There's just no other way to do it.

Challenge: Who will be the regulating body? Will it be done through stock exchanges, such as the Securities and Exchange Commission (SEC), making it a listing requirement? Should it pass through legislation or maybe developed by a global body like the U.N. that will set up the standards?

❖ Integrating a third-party audit requirement to ensure quality

Right now the majority of reports are not audited, which is one of the reasons why the data presented is many times questionable, not to mention the latest criticism on many mistakes found in unaudited reports. Clearly, the addition of third-party verification will make Environmental, Social and Governance (ESG) data much more trustworthy and therefore more valuable.

Challenge: Creating an auditing system that will be accepted on all the involved parties. Since we're talking about accountants here, it won't be simple. Let's just hope it won't take too long.

❖ Opportunities and Challenges in Integrated Reporting

The opportunities and challenges for a CFO undertaking a more integrated reporting approach are:

❖ OPPORTUNITIES

1. Embarrassment avoidance- the scale& frequency of voluntary multi-channel sustainability disclosure from the sustainability silo has now reached a tipping point. The CFO/CIO need to take charge to avoid embarrassing disclosure of duff data.
2. Greed is good- sustainability is a driver not only of risk avoidance but for innovation towards new revenue streams. Just take a look at GE, Philips, Unilever Nestle & Nike to name a few. However, CFOs & CIOs must put a sound information platform under sustainability led business transformation initiatives to guide them towards their objectives.
3. Cost savings - some firms are spending upwards of $500k annually on sustainability reports between data collection, design, audit etc. Effective sustainability reporting is getting too expensive not to consolidate & leave in the silo.
4. Innovation of process - sustainability reporting provides an additional lens for senior management to gain insight on performance. It also provides insight on non-financial capital on which the firm depends and how to better and manage these factors. Management of water, air quality, climate, talent is now or will be a competitive advantage for the future for some or all firms.
5. Innovation in reporting - the IIRC vision does help the CFO get beyond compliance disclosure and focus engagement on and with the key stakeholders that are impacted or can impact the firm. Expect this to be a two way process not a monologue.

❖ CHALLENGES

1. Sustainability strategy or a sustainable strategy? - An integrated reporting approach presupposes the firm has an integrated strategy. Presently, a truly integrated strategy for sustainability is still rare for all but a few leaders.
2. Overstretched CFO - in the midst of economic turbulence the CFO is already well stretched to become more effective and more efficient so sustainability risks falling off the table or worse - become way too diluted in the integration. IBM CFO Survey in 2010 showed that although integration was a high priority for CFO's, they felt they fell short on capability to deliver it.
3. Overcoming fragmentation- CFO's already have difficulty in integrating data currently spread across geography, hierarchy, systems and various finance disciplines including accounting, internal audit, governance, risk & compliance. Add to this the complexity of retrieving data from across the value chain and relating to items that have been traditionally uncosted externalities.
4. Immature systems and standards - while the IIRC outlines a good framework for reporting, the reality is that many firms have not yet built the robust information architecture to support sustainability reporting to the same level of quality as currently achieved by financial reporting. This will take time and investment. The same for standards bodies. By the way, given the multi stakeholder claim on an integrated report, we must see much more in the way of social media integration in reporting than is currently the case.
5. Vested interests - the corporate sustainability professionals must stand out of the way and allow operational and financial professionals take the lead on sustainability. Will they do so quickly and quietly? The same challenge is posed for some of the standards bodies for reporting and assurance. On the flip side, integration could see the Big 4 consolidate their influence over the development of sustainability reporting and assurance standards. Not everyone would agree this would make for ideal stewardship.

❖ Conclusion

In other words, Integrated Reporting refers to the integrated representation of a company's performance in terms of both financial and non-financial results. Integrated reporting provides greater context for performance data, clarifies how sustainability fits into operations or a business, and may help embed sustainability into company decision making. Some companies that report in an integrated manner also report additional sustainability information, often online, for specific stakeholder groups. Research has shown that reporting influences behaviour. Integrated Reporting results in a broader explanation of performance than traditional reporting. It makes visible an organization's use of and dependence on different resources and relationships or "capitals", and the organization's access to and impact on them.

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