Integrated Reporting: Literature Review and Its Practice in India and Abroad

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Abstract: *This paper has reviewed the recent literature in the field of integrated reporting (IR) to study the progress of IR research and opportunities for future research. The IR practice in India and abroad have been discussed to find out the challenges and opportunities. Corporate reporting over the years has witnessed paradigm shift to meet the information needs of the stakeholders and it continues to evolve from traditional financial reporting to sustainability reporting to more recently, Integrated Reporting. Integrated reporting is a vehicle for long-term value creation for and by the business itself. It is a concise communication about how an organization's strategy, governance, performance and prospects lead to creation of value over short, medium and long-term. IR is expected to bring greater transparency on corporate commitment to sustainability by showing the links between financial and sustainability performance in single document. It aims at connecting different functions to form a holistic view of the business, recognizing the value, risks, and opportunities. It takes a wider view of the six 'capitals', i.e., financial, manufactured, intellectual, human, social and relationship, and natural capital. IR is emerging as an innovative reporting tool for companies for integrating environmental and social thinking into their business. Many countries and their regulators (Japan, India, South Africa, UK and many European countries) have taken initiatives to implement integrated reporting. SEBI, in consultation with industry bodies and stock exchanges, asked top 500 listed companies to voluntarily adopt IR framework from the financial year 2017-18.*

Keywords: *Corporate Reporting, Sustainability Reporting, Integrated Reporting*

Introduction

'Change' is believed to be the only constant in today's world. We have seen revolutionary changes in 20th and 21st century.In line with the emerging changes, corporate reporting over the years has witnessed paradigm shift to meet the information needs of the stakeholders. Corporate reporting practices continue to evolve from traditional financial reporting to sustainability reporting to more recently, Integrated Reporting(IR).

"The accounting profession has challenged the traditional financial reporting model, arguing that it does not adequately satisfy the information needs of stakeholders for assessing a company's past and future performance" (Flower, 2015). "Organisations are increasingly disclosing financial and nonfinancial performance as they are encouraged to become more accountable and transparent to the providers of capital, and towards other interested parties (Camilleri, 2018). "Initially, the idea of managing, measuring and reporting the three elements of an organisation's social, environmental and economic impacts gained prominence during the late 1990s and early 2000s (Dumay et al., 2016). However, these reports, known as sustainability reports, often suffer weaknesses as they appear disconnected from the organisation's financial reports and fail to make a link between sustainability issues and the organisations core strategy (Clayton et al., 2015). IR, the latest development in corporate reporting reform, promises to address criticisms and shortcomings of sustainability reporting (Stubbs & Higgins, 2018).

The International Integrated Reporting Council (IIRC) released the International IR Framework in December 2013, following multi-stakeholders input. The International IR Framework aims to simplify company reporting and improve its effectiveness by focusing on value creation "as the next step in the evolution of corporate reporting" (IIRC, 2015). In the words of Richard Howitt, CEO of the International Integrated Reporting Council (IIRC), "Integrated reporting is a vehicle for long-term value creation for and by the business itself. It helps them think, plan and report the story of their business" (ET, Jan 17, 2018).

Integrated reporting in corporate communication is a new model of corporate reporting. It is a concise communication about how an organization's strategy, governance, performance and prospects lead to creation of value over short, medium and long-term(Wikipedia). It is an integrated representation of a company's performance in terms of a company's financial and other value relevant information, which helps stakeholders in their decision-making. IR aims at connecting different functions to form a holistic view of the business, recognizing the value, risks, and opportunities represented in the long-run. It takes a wider view of the six 'capitals' with which it operates and applying the reporting to the core business model and strategy of the organization. IR is emerging as an innovative reporting tool for companies for integrating environmental and social thinking into their business.

Background

The two main objectives of any business organization are financial stability and sustainability. The global financial crisis in 2007 brought into focus that a wide range of factors determine the value of the organization.The focus was on end product rather than the process or system. Sustainability was not embedded with business model. The tangible or financial factors are easy to account for in the financial statements. But intangible factors like intellectual capital, competition, energy security, employee engagement, reputation and stakeholder relationships are very complex phenomena and also very difficult to report in specific terms.

The idea of managing, measuring and reporting the three elements of organizations social, environmental and economic impacts gained prominence during the last 1990s and early 2000s. In 2002, Novozymes, a Danish enzyme company, which was spun off from Novo Nordisk in 2000, prepared the first corporate integrated report. The discussions and debates regarding IR continued after that in many forums. In 2009, the Prince of Wales convened a high level meeting of investors, standard setters, companies, academic bodies, UN representatives, representatives of IFAC and GRI to establish International Integrated Reporting Council (IIRC), a body to oversee the creation of a globally accepted integrated reporting framework. On December 9, 2013, the draft of the internationally recognized integrated reporting framework was released.IIRC has prescribed guiding principles for preparation of an IR, specifying the content of the report and how information is to be presented. The objective of merging conventional financial reports and reports on environmental, social and corporate governance (ESG) into one integrated report is to improve information available to investors qualitatively.

Many countries and their regulators (Japan, India, UK and many European countries)have taken initiativesto implement integrated reporting. South Africa is the only country which made IR mandatory for all listed companies in the Johannesburg Stock Exchange.

Objectives and Methodology

The specific objectives of this article areas follows:

- To critically examine the research papers to find the progress of IR research and opportunities for future research.
- To study the IR practice in India and abroad to find out the challenges.

The study is mainly dependent on secondary data. A number of recent research articles have been reviewed to find out the progress in IR research and opportunities for future research. Content analysis of annual reports of Sensex 30 companies has been undertaken in this research study to find out the IR practices in India.

Literature Review

A structured review of literature in the area of 'Integrated Reporting has been undertaken to develop understanding into how IR research is progressing.The research papers have been critically examinedto find out the opportunities for future research.

Robert G. Eccles and George Serafeim of Harvard Business School in their research paper on "Corporate and Integrated reporting: A Functional Perspective" presented two primary functions of corporate reporting (information and transformation) and described why IR could be a superior mechanism to perform these functions.They have also discussed, through a series of case studies, what constitutes an effective integrated report.

Clayton, et al. (2015) made a comparative study on integrated reporting and sustainability reporting for corporate responsibility in South Africa. The content analysis of the corporate reports revealed that the key drivers of sustainability and integrated reporting were regulatory requirements, industry of the company, the environmental and social impact of the company, and stockholder perceptions and pressure. It is disclosed that the actual drivers of sustainability reporting and integrated reporting did not differ significantly from the King Code II sustainability era (up until 2010) to the King Code III integrated reporting era (post 2010).

Lai et al. (2016) studied whether the decision to adopt IR stems from the need to repair legitimacy threats. They found out that legitimacy pressures did not play a role in explaining IR adoption. Overall, their evidence suggested that corporate engagement in IR was not a matter of strategic legitimation.

Humphrey et al. (2016) studied the emergence of International Integrated Reporting Council (IIRC) and its attempts to institutionalize IR as a practice that is critical to the relevance and value of corporate reporting. They observed that the IIRC has been swift in establishing itself as a globally recognised body.

Dumay, et al. (2016) reviewed the field of integrated reporting to develop insights into IR research and outline future research opportunities. They observed that there is little research examining IR practice. They argued that the 'eco-system approach' to researching IR is important because the IIRC (2013, p. 2) advocates leveraging "financial, manufactured, intellectual, human, social and relationship, and natural" capital as part of creating value.

Faria (2016) analysed the evolution of IR and discussed arguments in favour and against IR. It was concluded that there are several advantages above the disadvantages that need to be improved to disseminate the guidelines of doing IR all over the world.

Perego, et al. (2016) studied IR and observed that IR has fast emerged as a new accounting practice to help firms understand how they create value and be able to effectively communicate this to external stakeholders. The study has contributed to this field by reframing the existing implementation challenges of IR into promising and inclusive research opportunities that align the priorities of both academia and business.

Maniora (2017) examined the impact of IR on the integration of environmental, social and governance (ESG) issues into the business model and the related economic and ESG performance changes. The research paper provided empirical evidence using three matched samples of companies from around the world for the sample period 2002-2011, that contradicts the general notion of IR as a superior reporting mechanism, as the benefits of IR are driven by several factors.

Mervelskemper and Streit, (2017) studied the effectiveness of a firm's strategy to report on its ESG (environmental, social and governance) activities, and whether following the current IR trend is worth the effort. They observed that IR is associated with superior outcomes compared with a standalone report for composite ESG and corporate governance performance.

Stubbs and Higgins, (2018), in their exploratory study of the preferences of users of non-financial reporting for regulatory or voluntary approaches to IR, found more support for voluntary approaches to IR. They suggested that IR will become the reporting norm over time if left to market forces as more and more companies adopt the IR practice. However, half of the investors supported mandatory IR because, in their experience, voluntary sustainability reporting has not led to more substantive disclosures or increased the quality of reporting.

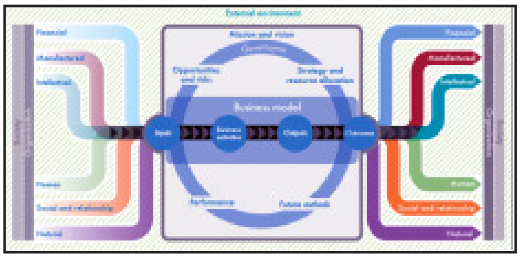
Camilleri (2018), in his research on the integrated reporting of financial, social and sustainability capitals, found out that organisations are increasingly disclosing financial and non-financial performance as they are encouraged to become more accountable and transparent to the providers of capital, and toward other interested parties. He inferred that there is both costs and benefits for using IR framework.

Integrated Reporting: A Conceptual Study

Features of IR

- IR is an integrated representation of a company's performance in terms of both financial and other value relevant information.
- It provides a holistic view of the business by connecting different functions.
- It recognizes the value, risks and opportunities of the organisation.
- It is a transition from sustainability reporting to IR.
- It links the sustainability of a company's activities and company's financial performance.
- It takes a wider view of six 'capitals' used by the organisation.
- Six Capitals:
- IR framework categorises the resources and relationships, an organization uses as the following six capitals:
- Financial Capital: The pool of funds available to the organization.
- Manufactured Capital: Manufactured physical objects as distinct from natural physical objects.
- Intellectual Capital: Intangibles that provide competitive advantages.
- Human Capital: The skill and experiences of people and their motivations to innovate.
- Social and Relationship Capital: Community, stake holders and other networks to enhance individual and collective well-being.
- Natural Capital: Water, land, minerals, forests, bio-diversity and ecosystem health.

Figure I: Interaction between the six capitals



Source: R.G. Eccles and George Serafeim, Harvard Business School

Guiding Principles of IR (Morros, 2016, 345-346):

- Strategic Focus and Future Orientation:
- Connectivity of Information
- Stakeholder Relationships
- Materiality and Conciseness
- Reliability and Completeness
- Consistency and Comparability

The process of producing an IR requires companies to actively measure environmental, social and other non-financial impacts and embed these factors into corporate decision making- a process referred to as 'integrated thinking'. (www.accountingforsustainability.org). The key aspect of integrated thinking is that companies must measure and report on all of the various "capitals" a company uses to create value, rather than focusing solely on financial capital. IR also includes a company's expectations about the future, including information about future prospects and uncertainties. The report should include all material matters, both positive and negative.

Elements of IR

Common reporting format for companies following IR has the following elements:

- Organizational Overview
- Governance
- Business Model
- Risk and Opportunity
- Strategy and Resource Allocation

- Performance
- Outlook
- Basis of Presentation

Relevance of IR

IR is a change from siloed reporting to integrated reporting. Its focus is on integrated thinking and management of various types of capital. It's a more efficient and effective reporting for both users and preparers of this report. It provides a complete picture of both internal and external environment. As sustainability is embedded within the every business model, the risks of long term failures are reduced. Integrated reporting is a big shift from financial capital market system to inclusive and sustainable capital market system. IR focuses on the process/system rather than the end result or outcomes. It provides a better understanding of the performance of the organization and its value creation.

IR is expected to bring greater transparency on corporate commitment to sustainability by showing the links between financial and sustainability performance in a single document. IR provides insight into firm'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 an effect on capital (www.integratedreporting.org).IR stimulates innovative reporting practices by reducing the number of reports. Finally the stake holders get a strong company narrative and a more joined-up story regarding the organization.

IR: Cost-Benefit Analysis

Costs:

- Initial efforts to integrate:Afirm's strategy, governance, performance, prospects, as well as the contents within which it operates should be integrated.
- Design the reporting process and its review: The organisation has to designs an efficient system of collecting information, simplifying relevant information and putting it in concise, consistent and in comparable format. All areas of organizational performance should be presented in a connected reporting way.

Benefits

- IR will provide better quality of information available for stakeholders.
- It develops a culture for departmental collaboration srequired to produce the reports combining financial with non-financial reporting.
- There is enhanced accountability for six capitals.
- Better corporate reporting leads to better reputation and goodwill in the market.

IR Practices

The evolutionary phase of IR was from 2002 to 2013, which is presented briefly as follows:

2002: The first company to prepare IR is Novozymes, a Danish enzyme company (Spun off from Novo Nordisk in 2000).

2009: High level meeting was conducted by Prince of Wales to establish IIRC.

2009: South Africa became the first country where IR became mandatory for all listed companies.

2013: IIRC designed the IR framework and many companies participated in the IIRC pilot programme.

Kirlosker Bothers Ltd. is one of the first companies in India to prepare IR since 2013-14. At present, many large companies in India have already adopted IR. SEBI, in consultation with industry bodies and stock exchanges, asked top 500 listed companies to voluntarily adopt IR framework from the financial year 2017-18. After this declaration, IR in India is gaining momentum. This move by the market regulator is aimed at providing stakeholders relevant information that is useful for making investment and other decisions. SEBI said that information related to integrated reporting should be provided in the annual report separately or by incorporating in 'management discussion and analysis' or by preparing a separate report. The companies can also host the IR on their website and provide appropriate reference to the same in their annual report. To avoid duplication of information, if the firm has already provided the relevant information in any other report prepared, it should provide appropriate reference to the same in its IR.

Tata Steel, Reliance Industries Ltd, Tata Motors, HDFC Bank, Wipro, HDFC Ltd. and Induslnd Bank have prepared integrated reports in the last financial year. RIL aligned the sustainability report content to principles of International Integrated Reporting Framework laid down by IIRC and prepared its IR. HDFC Ltd. has prepared IR which gives holistic view of the long-term strategy and financial performance of the company along with benchmark standard with respect to human rights, sustainability, environment, society, governance and CSR.

Yes Bank is the first bank to release the IR in line with IIRC since 2015-16. The report explains bank's dependence and impact on the various forms of capital that are fundamental to its ability to create long-term value.

Tata steel is preparing IR since 2014-15. The IR for financial year 2016-17 has been recognized as Asia's best integrated report by Asia Sustainability Reporting Awards. Wipro is also preparing IR for last three years providing information on six types of capitals and their interdependence.

Observations and Conclusion

There is need for an IR movement/ mission in India to comply with international best practices. Significant transformation in approach and thinking leading to innovative reporting is the need of the hour. Strategy and pressure groups can play an effective role for reforms in corporate reporting. Regulators, academics and professionals have to play their role in enriching corporate reporting for the benefit of stakeholders. The main challenges for IR are value identification, its creation, measurement, preservation and reporting. Another challenge is the complexity of measuring and quantifying non-financial matrices. There is need for harmonization of IR standards and regulations.Technology enabled reporting system is essential for the corporates. Audit and Assurance services are requiredfor the reported data in IR to check reliability, materiality and completeness.

The current system of voluntary disclosers has created an uneven playing field, with some companies clearly informing investors and others under-reporting, over-reporting, green washing, or otherwise producing misleading propaganda. IR should be comprehensible, credible and comparable. Guidelines based on best practices would be the most constructive way forward.

IR is a radical transformative change in the field of corporate reporting. It has significant potential for future research.The SEBI, ICAI and Ministry of Corporate Affairs have to play an active role for the promotion of integrated reporting.

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