Integrated Reporting – A Challenge for Corporate Reporting and Academics?

Richard Howitt
CEO, IIROC

IAAER World Congress
University of Sydney, Abercrombie Business School
Sydney, 8th November 2018
THE NEED FOR A NEW REPORTING MODEL
Value is more than financial

COMPONENTS of S&P 500 MARKET VALUE

SOURCE: INTANGIBLE ASSET MARKET VALUE STUDY, 2017
The Australian contribution on Intangibles

- Before IFRS implementation in 2005, in Australia and New Zealand internally generated intangible assets (such as brands) were recognised on the Balance Sheet.

- In September 2008, the International Association of National Standard Setters (NSS) released a document authored by the Australian Accounting Standards Board (AASB) to deal with intangibles in financial reporting.

- In 2005, the Society for Knowledge Economics (SKE) was established with the aim to develop more innovative, fulfilling and high performing workplaces.
The reporting mismatch

- **Reporting Content**
  - Strategic Issues
  - Forecasts/Plans
  - Past Performance

- **Business Value**
  - Strategy and Governance
  - Implementation Plans
  - Business as usual
The story is lost in details

103,484 words, 257 pp

(95,356 words)

(76,944 words)
The Issue of Connectivity

• Piecemeal addition of “bits” of information

→ Explosion of unconnected, and sometimes immaterial, information

• An integrated report should “tell a story”
THE INTERNATIONAL <IR> FRAMEWORK
Fundamental Concepts

• Value Creation for the organization and for others
• The Capitals
• The Value Creation Process

Guiding Principles

• Strategic focus and future orientation
• Connectivity of information
• Stakeholder relationships
• Materiality
• Conciseness
• Reliability and completeness
• Consistency and comparability

Content Elements

• Organizational overview and external environment
• Governance
• Business model
• Risk and opportunities
• Strategy and resource allocation
• Performance
• Outlook
• Basis for preparation and presentation
The Centrality of Business Model

Business model

Inputs

Business activities

Outputs

Outcomes

Mission and vision

Governance

Strategy and resource allocation

Risks and opportunities

Performance

Outlook

External environment

Value creation (preservation, diminution) over time

Financial

Manufactured

Intellectual

Human

Social and relationship

Natural

© International Integrated Reporting Council
The Capitals

- Financial capital
- Manufactured capital
- Intellectual capital
- Social and relationship capital
- Human capital
- Natural capital
The Value Creation Concept

Value Creation → The increases, decreases or transformations of the capitals caused by the organization’s business activities and outputs

That value has two interrelated aspects → Value created for:
• The organization itself, which enables financial returns to the providers of financial capital
• Others (i.e., stakeholders and society at large)

(International <IR> Framework, 2013)
The largest Centre for Refugees Asylum Seekers in Europe (C.A.R.A. of Mineo, Italy) has released 2015 and 2016 Integrated Reports to explain its value creation story.
Integrated thinking

- **Integrated thinking** is the active consideration by an organization of the relationships between its various operating and functional units and the capitals that the organization uses or affects.

- Integrated thinking leads to integrated decision-making and actions that consider the creation of value over the short, medium and long term.
“integrated thinking is a symphony of the 6 Capitals”

Mervyn King
THE INTERNATIONAL INTEGRATED REPORTING COUNCIL (IIRC)
Who is the IIRC?

- Investors
- Companies
- NGOs
- Regulators
- Standard setters
- Accounting
The IIRC’s vision is to align:
- capital allocation, and
- corporate behaviour
to wider goals of:
- financial stability, and
- sustainable development
through the cycle of:
- integrated reporting, and
- integrated thinking.
Integrated reporting in regulations/ codes

Integrated reporting adopted by 1,600 organizations across 65 countries including every G20 economy

<IR> networks
2,000 participants including 500 in Brazil

Mainstream adoption in South Africa and Japan

Academic evidence
shows that integrated reporting improves conditions for long-term investment, reduces cost of capital, improves performance and improves liquidity
Australia

- <IR> referenced in draft ASX CG Principles (Draft 4e)

- The <IR> Pension Fund Network is based in Australia where leading funds are adopting Integrated Reporting

- Business Reporting Leaders Forum active towards Integrated Reporting
The Academic Movement

• Over the years increasing interest also by academics and academic research (ca. 400 research works on <IR> since 2010)

• Probably well known to many of you the paper by Barth et al. on Accounting Organization and Society on the economic consequences associated with integrated reporting quality

• More recently, Stubbs and Higgins (Journal of Business Ethics, 2017) found that according to the Australian stakeholders interviewed “IR will become the reporting norm over time if left to market forces as more and more companies adopt the IR practice”
WHAT’S NEW IN THE <IR> SPHERE?
The corporate perspective

Launch of Three Special Interest Groups (SIG):
• Strategy and Integrated Thinking
• Financial Institutions
• Hidden Capitals

Increasing interest by Universities <IR>

How does higher education create and demonstrate value?

Role of CIO in <IR> development

Technology primer for integrated reporting
A Chief Information Officer guide
From an institutional perspective

IIRC welcomes appointment to IASB Management Commentary Consultative Group

“The Corporate Reporting Dialogue Is Looking for Alignment, Not for One Common Framework”

Launched on November 7th

IIRC appointed to 2018 B20 Task Force

CFA Institute and IIRC in new global partnership to promote integrated reporting in financial analyst community
In terms of research

Launch of the <IR> Academic Network Oversight Body
- 5 international universities involved (incl. Deakin University from Australia and University of Auckland from New Zealand)

The <IR> Academic Database

http://www.iracademicdatabase.org/
Aligning SDGs with the value creation process
Today we launch the creation of two special sections on the <IR> Academic Database on:

- SDGs
- Public Sector
WHAT’S NEXT?
Implementation guidance

Materiality

Outputs and outcomes

Conciseness

Statement from those charged with governance

Stakeholder needs and interests
Calls for Research

- Use of narrative and non-financial info by providers of financial cap.
- Corporate reporting developments & Incentives and barriers
- Implementation by SMEs, public sector and not-for-profit
- Disclosing stakeholders’ needs and interests
- Connectivity and decision making
To conclude

• The implementation of <IR> is a journey

• To change the way an organisation “thinks” represents a real transformation → a new theory of the firm?

• <IR> should not to be conceived as an additional reporting requirement → focus not only on the integrated report, but also on the process of “Integrated Reporting and Thinking”

• Integrated Reports are not intended to substitute for financial statements or sustainability reporting → sustainability is an integral part of a wider value creation process represented in <IR>
THANK YOU!
richard.howitt@theiirc.org