Fostering Integrated Reporting in Indian Corporate Sector

Dr. (Mrs.) N. V. Kavitha
HOD, Commerce Department, St. Ann’s College for Women, Hyderabad (India)

Mrs. N. Suma Reddy
2nd Lecturer, Commerce Department, St. Ann’s College for Women, Hyderabad (India)

Abstract: Integrated Reporting “Provides a holistic method for explaining how the organization is doing, and how the management team thinks it will do in the future... It takes into account the connectivity and interdependencies between the range of factors that have a material effect on an organization’s ability to create value over time.” by Bob Laux, Senior Director of Financial Accounting and Reporting at Microsoft Corporation. In today’s globalized economy there has been an emergent concern of social, environmental and ethical reporting along with financial reporting. Integrated Reporting is a complete financial and non-financial information disclosure which is an essential for the effective operation of any corporate enterprise. The paper makes an attempt in understanding the rationale of integrated reporting along with the various benefits and need for fostering integrated reporting in Indian corporate sector. Businesses require an evolution in the system for reporting, facilitating and communicating mega-trends without the complexity and inadequacy of current reporting requirements. Currently, there are significant information gaps in reports, with the organizations such as the World Bank and IMF calling for a greater focus on aspects such as risk and future development. Fostering integrated reporting is the only answer for Indian Corporate sector.

Keywords: Integrated reporting, transparency, corporate reporting, financial and non financial information, disclosure.

I. INTRODUCTION

“Integrated Reporting helps the company manage processes and activities in a more effective way and, most importantly, build awareness of the heterogeneous capitals, resources, and relationships used and affected.” By Jonathan Labrey, Chief Strategy Officer, International Integrated Reporting Council, London.

Integrated reporting (IR) is a process which builds up the linkages between an organization’s strategy, governance and financial performance and the social, environmental and economic context within which it operates. The aim of the integrated report is to give the stakeholder a realistic view of the company, its future and how it creates value. The two essential concepts of integrated reporting are capitals and the value creation process.

Integrated reporting is being adopted or explored by companies throughout the world. An increasing number of social reporting requirements driven by local regulatory bodies and stock exchanges have played a key role in continuing this momentum. In the IR the capitals are the stores of value (or relationships) that are input into a company's business model. The IR framework has six categories of capital an organization need to use as a benchmark while preparing their report. The following are the six capitals identified to be included in IR:

- Financial (i.e., the pool of funds),
- Manufactured (i.e., manufactured physical objects, not necessarily owned by the organization),
- Intellectual (i.e., organizational, knowledge-based intangibles),
- Human (i.e., peoples' competencies, capabilities and experience, and their motivations to innovate),
- Society and relationship (i.e., relationships within and between communities, groups of stakeholders and other networks, and the ability to share information to enhance individual and collective well-being), and
- Natural (i.e., renewable and non-renewable environmental resources and processes that provide goods or services that support past, current or future prosperity of the company)

II. LITERATURE REVIEW

As corporate reporting is the current burning issue, several researches were conducted on this area. The literature review mainly focused on huge untapped areas and emerging trends in the reporting practices. Corporate reporting has been proved in the literature to be an important promoter of economic growth. Wallman (1995) proposes a piecemeal, partial solution to the critical issues faced by financial reporting, including additional reporting of soft assets and business risks and on-line access to large sections of the company’s management information system. The Royal Society for Arts, U.K. (1995) proposed a more inclusive, non-adversarial approach to both business practices and financial reporting, intended to support sustainable success. To achieve this, it is argued that there is a relatively greater need to use of non-financial performance measures. Kaplan and Norton (1996) revealed that in recent years, management practices have embraced the use of a balanced scorecard, which recognises that corporate value depends on a range of critical success factors, with accounting measures lagging behind non-financial
performance indicators. Wright and Keegan (1997) explained that the International Accountancy Firm Price Waterhouse (PW) proposes enhanced and voluntary disclosure of future-oriented information covering both financial and nonfinancial performance measures. The Institute of Chartered Accountants in England and Wales (ICAEW), 1997 has suggested a framework for the comprehensive reporting of risk and has considered the implications of digital technology. Accounting Standard Board, UK (1999) identified seven legitimate user groups, such as employees, customers and suppliers. Despite this, investors are currently viewed as the ‘defining class of user’. Lodhia (2006) has defined corporate environmental reporting (CER) as a process through which “companies often disclose environmental information to their stakeholders to provide evidence that they are accountable for their activities and the resultant impact on the environment.” Cooper (2007) pinpointed that financial information is critically important, it provides only one part of the picture of overall business performance, and has a built-in bias towards recording the short-term results of companies, giving too little emphasis to their longer-term value potential. Leuz and Wysocki (2008) provide a comprehensive survey of research on the economic consequences of financial reporting and disclosure regulation. Also, Kothari, Ramanna and Skinner (2009), as part of a larger discussion on what GAAP should look like, provides an in-depth discussion of the origin and consequences of regulating standard setting. They argued that the objective of accounting standard setting is to promote the efficient allocation of capital; they conclude that competition between standard setting organizations is likely to be the most effective means of achieving this objective. Nayak (2012) observed that not only investors benefit from full disclosure, as they do not have to bear the uncertainty caused by lack of corporate disclosure, the company also gains because an upward move in the share prices reduces its cost of capital and also helps in resource mobilization. Adhikari and Bhusan Dey (2012) viewed that banks are to contribute to sustainable development by way of their compliance of integrating environmental, social and corporate governance aspects into their business strategy.

III. OBJECTIVES OF THE STUDY

Fostering integrated corporate reporting practices is the need of the hour in Indian Corporate sector, so as to reduce information asymmetry between investors and management thus enhancing the performance and risk that is essential for rational and high quality decision-making. The present paper makes an attempt:

- To analyze the benefits of integrated reporting practices.
- To explore the challenges and opportunities of integrated reporting practices.
- To examine the disclosure of integrated reporting in Indian corporate sector.

IV. METHODOLOGY

In order to accomplish the above objectives, secondary sources, available literature, reports and data have been used. The data has been obtained from various journals, reports, magazines and websites. The data pertaining to the study has been analyzed and interpretation of data is based on rigorous exercises aiming at the achievement of the study objectives and findings of the existing studies and it is more on qualitative terms than on quantitative terms.

V. EVOLUTION OF CORPORATE REPORTING

India's business and investment communities are beginning to recognize the benefits of sustainability reporting and organizational transparency.

Source: Adapted from IIRC, Towards Integrated Reporting: Communicating Value in the 21st Century, September 2011
VI. FOSTERING INTEGRATED REPORTING IN INDIAN CORPORATE SECTOR

Businesses require an evolution in the system for reporting, facilitating and communicating mega-trends without the complexity and inadequacy of current reporting requirements. Currently, there are significant information gaps in reports, with the organizations such as the World Bank and IMF calling for a greater focus on aspects such as risk and future development. Thus fostering integrated reporting is the only answer for Indian Corporate sector.

VII. IS INTEGRATED REPORTING A BETTER TOOL FOR CORPORATE REPORTING?

“IR Framework is a tool for the better articulation of strategy, and to engage investors on a long-term journey to attract investment that will be crucial to achieving sustained, and sustainable, prosperity.” By Professor Mervyn King, Chairman, IIRC

Integrated Reporting is an evolution of corporate reporting, with a focus on conciseness, strategic relevance and future orientation. As well as improving the quality of information contained in the final report, makes the reporting process itself more productive, resulting in tangible benefits. Integrated Reporting requires and brings about integrated thinking, enabling a better understanding of the factors that materially affect an organization’s ability to create value over time. It can lead to behavioral changes and improvement in performance throughout an organization.

Businesses have reported breakthroughs in understanding value creation, greater collaboration within their teams, more informed decision making and positive impacts on stakeholder relations. IR has been created for any organization that wants to embrace integrated thinking and progress their corporate reporting.

VIII. SOME OF THE BENEFITS OF IR ARE

• More effective capital allocation – The more meaningful communication brought about through Integrated Reporting will support more effective capital allocation across the economy generally and, to the extent that Integrated Reporting supports capital flowing to those organizations that are responding most effectively to future challenges, can encourage the investment necessary to respond to issues such as energy security, food scarcity and climate change.

• Harmonization of approaches and reduced “red tape” – Reporting is shaped by a patchwork of laws, regulations, standards, codes, guidance and stock exchange listing requirements, described in a recent report as “a jigsaw in pieces”. 10 Integrated Reporting offers a platform for policy-makers, regulators and standard-setters, working together, to: – integrate reporting requirements within a jurisdiction; – harmonize advances in reporting that have been achieved in different jurisdictions; and – approach new reporting issues on a consistent basis as they emerge across jurisdictions.

• Economic and market stability – The recent global financial crisis has made it clear that risks can develop, be harberoude and be transmitted through market participants and practices that fall outside the traditionally prudentially regulated institutions. One important tool in addressing these risks is greater transparency of market participants, which Integrated Reporting can facilitate. This linked with the better internal decision making and behaviors that Integrated Reporting encourages, as well as the longer term perspectives that it enables, may well deliver lower volatility in markets. Moreover, it permits policy-makers and regulators to identify such risks as they emerge so that they can be dealt with in a timely way, thus adding to greater economic and market stability.

• Stewardship of common resources – Because of the broader perspective required by Integrated Reporting, both in terms of the resources and relationships that it takes into account and the longer timeframe over which value creation is considered, it leaves organizations better placed to act, and be more accountable, as stewards of the community’s common resources, in particular human, natural and social capital.

• Access to information – Integrated Reporting, by providing decision-relevant information, can support effective action by policy-makers and regulators as users of that information.

  ✓ Positive benefit in relations with institutional investors and analysts.
  ✓ Common understanding of value creation process, including short, medium and long term value.
  ✓ Improved data quality, resulting in better management information and decision-making.
  ✓ Breaking down the silos through integrated thinking, fostering internal buy-in to strategic objectives.
  ✓ Enhanced quality of corporate communications.
  ✓ Opportunity to review and align operational processes.
  ✓ Embedding corporate responsibility and sustainability into business as usual.
  ✓ A new lens for thinking about your business, particularly identifying non-financial value drivers.

IX. WHY THERE IS A NEED FOR CHANGE?

“As the world begins a long shift toward a higher share, of market- based financing, effective disclosure become even more important. In the future, IR may well play a bigger role.” By David Wright, Director General, IOSCO.
Globalization and interconnectivity mean the world’s finances; people and knowledge are inextricably linked, as evidenced by the global financial crisis. In the wake of the crisis, the desire to promote financial stability and sustainable development by better linking investment decisions, corporate behavior and reporting has become a global need. The following are some of the reasons found for change in reporting practices in Indian Corporate Sector.

- **Overcoming silos** – current reporting often shows a lack of connectivity, perhaps reflecting the reality of organisational behaviours and diverse information sets. Better connection between different internal departments is seen as a key benefit of integrated thinking and reporting.

- **Looking to the future** – many reports adopt the ‘rear view mirror’ approach, focusing on the last year’s performance. An integrated report should have forward-looking elements, using current information to shape strategic insight over the long term.

- **Describing value creation** – many companies’ reports lack insight into how dependent they are on key relationships and resources outside the organisation to create value. And it’s rare to get a clear sense of how the dynamics of their risks and opportunities are evolving. Integrated thinking and reporting encourage a broader perspective, better understanding of the wider impacts and how these factors feed into the business model and drive sustainable value creation.

- **Measuring performance** – current reporting remains largely focused on financial performance. Measuring the impact an organisation has beyond traditional reporting boundaries and across multiple “capitals” is at the heart of the value of integrated thinking and reporting.

- **Measurement and reporting practices**
  - **Regulation** – Many components of Integrated Reporting are the subject of existing local regulations which vary between jurisdictions. Progress towards Integrated Reporting is, therefore, likely to evolve at different speeds in different countries. International consensus on the direction taken will be important, in particular for organizations operating across jurisdictions.
  - **Directors’ duties** – The fiduciary and other duties of those charged with governance are not consistent across all jurisdictions. Consequently, the focus of an Integrated Report may differ, in particular in relation to the users to whom the Integrated Report is addressed.
  - **Directors’ liability** – Because the scope of Integrated Reporting will cover new and evolving subjects, with a greater focus on the future, concerns about the liability of those charged with governance will need to be addressed. This might be achieved through the adoption of globally accepted and harmonized “safe harbours” or a broad business judgement rule.
  - **Commercial confidentiality** – Organizations will need to provide a more strategic focus and, in some cases, information not currently subject to mandatory disclosure requirements in their Integrated Reports. They will, therefore, need to balance the benefits mentioned above with the desire to avoid disclosing competitive information.
  - **Capacity building** – Building knowledge and experience across the reporting system will be essential to long-term success. The IIRC Pilot Programme (see page 24 for more details) will help to build this capacity, with the learning captured and disseminated by the IIRC for all to access. An online forum will also be created to encourage knowledge sharing.
  - **Information systems** – Organizations will need to establish or strengthen information systems for capturing and aggregating information.
  - **Outreach** – Conduct regional roundtables and other engagement and communication activities to raise awareness of Integrated Reporting among investors and other key stakeholders, and to encourage organizations to adopt and contribute to the evolution of Integrated Reporting.
  - **Harmonization** – Explore with national, regional and global policy-makers, regulators and standard-setters, opportunities for harmonizing reporting requirements within and across jurisdictions, and help to develop a compatible regulatory landscape.
  - **Governance** – Develop, through public consultation, institutional arrangements for the ongoing governance of Integrated Reporting.

### X. INTEGRATED REPORTING – STEPS IN IMPLEMENTATION

In spite of genuine apprehensions and concerns about Integrated Reporting, companies must realize that the benefits far outweigh the efforts and the stumbling blocks. Following is a suggestive approach for implementation of Integrated Reporting

1. Top management must constitute an Integrated Reporting committee with cross functional representation.
2. Clearly communicate that the committee shall own the process of compiling Integrated Report
3. Lay down materiality thresholds for reporting information on Economic, Social and Environmental aspects
4. Involve professional content writer for clarity and conciseness in Integrated Report
5. Involve a credible agency for assurance of Integrated Report
6. Adopt a fair approach towards positive and negative aspects of in Integrated Reporting
7. Set a time line for compilation of Integrated Report
8. Look at the journey of other companies in the process of compiling Integrated Report and imbibe learnings
9. Acknowledge and reward the efforts of the Committee in compiling Integrated Report

Integrated Reporting is not a matter of choice. The stakeholders will in future demand information on Social and environmental aspects of business and companies which rise to the challenge shall be rewarded with higher valuations and enhanced corporate image.

XI. CONCLUSION

In a rapidly changing and evolving global marketplace, it is imperative for the management of organizations to keep abreast of changes effecting both specific industries and the marketplace overall. Accounting and the financial services profession in general, is undergoing a radical transformation. Integrating advances in technology and balancing increases in marketplace demands for real-time information have resulted in an entirely new lens through which financial services operate. Linking together governance, stakeholder requirements, other non-traditional demands, and integrated reporting requires real-time, flexible information. These three pillars, linked together by both market demand and synergistic connections, appear to have a very significant impact on the way businesses operate and report results to market participants.

IR has been created to enhance accountability, stewardship and trust as well as to harness the information flow and transparency of business that technology has brought to the modern world. Providing investors with the information they need to make more effective capital allocation decisions will facilitate better long-term investment returns.

REFERENCES

1. Integrated Reporting- the future of corporate reporting-www.pwc.de
2. Integrated Reporting-Performance insight through better reporting –www.kpmg.com
3. The Landscape of integrated reporting- reflections on next steps – Robert G. Eccles & others