

Integrated Reporting: A Driver For Sustainable Development

Dr. Jayanti Ningombam

Associate Professor, Dhanamanjuri College, Imphal, Manipur

Submitted: 15-10-2021

Revised: 26-10-2021

Accepted: 28-10-2021

ABSTRACT

As integrated reports communicate about how an organisation's strategy, governance, performance and prospects lead to the creation of value over the short, medium and long-term representing company's performance in term of both financial and other value relevant information in short, it is very must necessary to study the Integrated Reporting for the Corporate sector. Again, Integrated Reporting provides greater context for performance data and clarifies how value relevant information fits into the operations of a business and helps the company in decision making more. Integrated Reporting benefits to a range of stakeholders and they are principally aimed at providing of financial capital allocation decision which ultimately extends towards the complete financial and sustainability reports. As a result, applied effective integrated reporting can be a catalyst for strategic change and a keystone of corporate sustainability leading to sustainable development to the organisation especially to the corporate sector. Considering the need for sustainable development, the paper analyses the impact of Integrated Reporting resulting to the 5mustainable Development of the corporate sector through value creation.

Key Word :Integrated Reporting, Sustainable Development, Strategic change andValue Creation.

I. INTRODUCTION

The global economic change has resulted to bring light over the link between disclosure, especially voluntary disclosure, and growth disclosing has become one of the main concerns of business houses. However, what should a company disclose? Then more questions must be addressed: financial and nonfinancial data. What rules should be applied, which shareholder and stakeholder, what are the strategic consequences and so on. Therefore; the best option to use a frame work that has been already engaged in various economic sectors and successfully applied which ultimately

leads to sustainable development through value creation.

This was one of the reasons behind a new concept integrated reporting. Considering the need, in 2009, The Prince of Wales convened a high level meeting of investors, standard setters, companies, accounting bodies and UN representative including The Prince's Accounting for Sustainability Project, International Federation of Accountants (IFAC), and Global Reporting Initiative (GRI), to establish the International integrated Reporting Committee (IIRC), a body to oversee the creation of a globally accepted Integrated Reporting framework. In November 2011, the committee was renaming as the International Integrated Reporting Council (IIRC).

The International Integrated Reporting Council (IIRC) has issued in March 2013 a prototype framework as a starting point for companies which want to make use of an integrated report, and instrument useful to communicate periodically to the different shareholder, the value created path that an organization taken. And, it can support the strategic development and financial sustainability (Integrated Reporting Organization 2013).

Considering the need the paper aims to define and present the concept of integrated reporting in connection to the business sector, the place where it has started. Again, it evaluates the need for integrated thinking in the integrated reporting.

Next, the paper studies the relationship between value creation and sustainable development through business model. Further, the article studies the six capitals that are employed when carrying integrated reporting and the tries to find out the advantages and disadvantages of this business model.

Finally, the paper analyses the challenges of integrated reporting, conclusions and the future research.

II. CONCEPT OF INTEGRATED REPORTING

Business firms create customers and provide goods and services that they value. In the process, they create value for partners in the value chain, employees, investors and others who are involved in the value creation process. They use variety of capitals, which represent resources and capabilities, in the value creation process. Some capitals that firms use is internal in the sense that those are owned or controlled by them, while others are external. An example of external capital is public goods, such as, fresh air and knowledge. Other examples of external capital are natural capital and infrastructure being created by the government for common use. Draft Integrated Reporting Framework, issued by International Integrated Reporting Council (available at www.theiirc.org/consultationdraft2013) on April 16, 2013, classifies capital into financial capital, manufactured capital, intellectual capital, human capital, social and relationship capital and natural capital.

There is interplay between capitals. For example, the value of the goods produced by using plant and equipment depends a lot on the ability of the firm to manage corporate and product brand, customer relationships and relationships with networking and supply chain partners. In the value creation process firms consume or add value to capitals. For example, in the process of delivering value to customers in the form of products and services, firms consume manufactured capital (e.g. plant and equipment) and natural capital, while increasing the value of financial capital and social and relationship capital.

Business models of firms impact external capitals either positively or negatively. Negative externalities destroy value of natural capital. For example, when a firm pollutes the fresh air through its operation, it destroys value air. A firm adds value to public goods by creating positive externalities. Firms through its operations create knowledge and skills that might be available for general use for the benefit of the society as a whole. For example, many innovations in the famous Bell Lab are being used for creating goods and services across the globe for social benefits.

For long, firms have taken a narrow view of capital. They ignored consumption of or value addition to external capital while measuring success of their business models. Traditionally, they measure net profit, which is the surplus available to shareholders, for a particular period at

the difference between the value of internal capital at the end of the period and that at the beginning of the period. Theoretically, distribution of surplus does not impair the earning capacity of the firm. However, in practice, it is not true because of two reasons. One is the difficulty in measuring the value of capital accurately. The second is that while measuring surplus, accountants ignore those capitals whose cost or value is not auditable.

For example, internally generated intangible assets, except software, are not counted in measuring the surplus. These drawbacks are significant. But, the most important drawback of financial reporting is that it does not provide information on firm's use of external capital.

Value of a firm is determined in the capital market. It is estimated, based on the forecasted cash flows that the firm will generate over long term and risks associated with that cash flow stream. Accounting numbers in financial statements might not have any direct correlation with the value of the firm. For example, although human capital, and social and relationship capital do not find place in the balance sheet, financial analysts, while estimating the value of a firm, consider the firm's ability to manage the same.

They also consider all other relevant factors that might affect future cash flows. Therefore, some may argue that integrated reporting, which tells the complete value creation story and explains how each type of capital will impact short-term, medium-term and long-term performance of the firm, might not improve valuation of firms in the capital market. The argument is weak. Disclosure will help financial analysts to identify and assess the risks to which the firm is exposed and thus will improve the accuracy of value estimation.

The most important benefit of integrated reporting is that it will enforce accountability of firms towards the society. Firms are expected to minimise negative externalities, maximise positive externalities and optimise the use of natural capital. But till now there is no mechanism to evaluate their performance in using external capitals. Integrated reporting will bridge this gap. It will force firms to develop business models that are sustainable. It will also enlighten the consumers how their consumption habits affect the community, natural capital and public goods. Integrated reporting is in sync with the 'responsible business' paradigm which can be seen from value creation and sustainable development through business model.

III. VALUE CREATION AND SUSTAINABLE DEVELOPMENT THROUGH BUSINESS MODEL

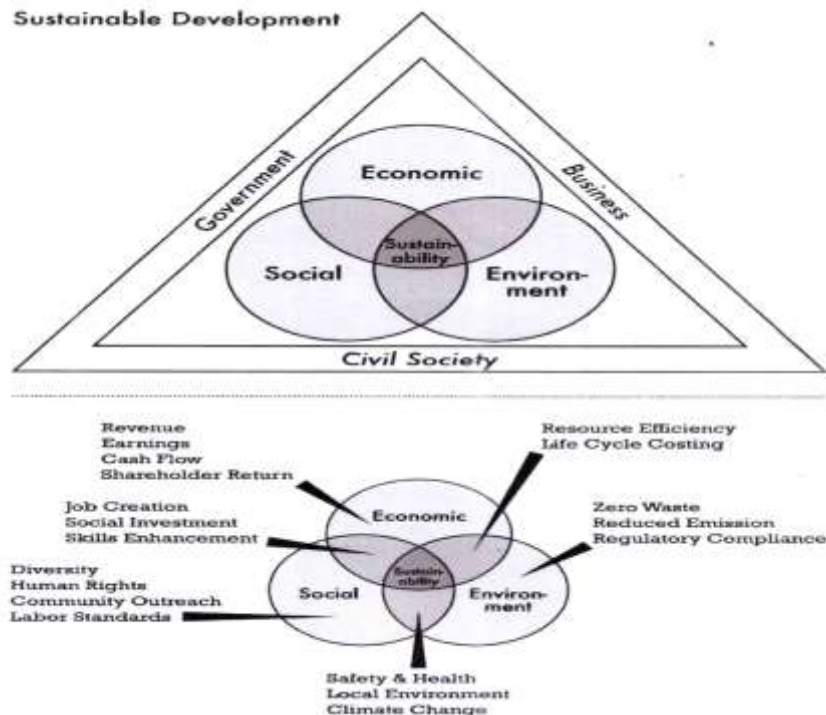
"Sustainable development is the adoption of strategies and activities that meet the needs of the enterprise and its stakeholder today while protecting, sustaining and enhancing the human and natural resources that will be needed in the future."

International Institute for Sustainable Development The conceptual model below captures the essence of how firms can embrace sustainable development consistent with their overall business strategies. The diagram shows the interactions of the economic, social, and environmental systems and gives examples of measurable business variables that reflect the natural interdependencies between the systems. The triangle bordering the "interdependent systems" indicates the influence different sectors of society can have on the firm's ability to operate sustainably. For example, government provides such things as regulatory oversight, incentives, and the legal license to operate. Firms also may face conflicting messages from different parts of government (from agencies charged with environmental protection, consumer safety, and so

forth) and different levels of jurisdiction (local, state, national and inter-governmental). Similarly, civil institutions are many and varied, and often at odds with each other in terms of what they want from a firm (environmental protection versus job creation). In addition, the actions of an individual firm are often shaped by others within their industry, acting through trade associations, industry principles of conduct, and so forth.

The extent to which sustainability will move from the margin of business practice to the mainstream of business strategy will depend upon its ability to create value for an enterprise. While there has been a good deal of discussion social, environmental, and economic metrics, the fact is that a private sector business is ultimately held accountable based on a single bottom line: profitability. Hence, what firms must come to recognize (and an increasing number have) is that strategic environmental and social actions can enhance profitability through environmental stewardship and through promoting social equity in ways that serve both shareholders and the larger public good. When that occurs, the value of a firm is increased through enhanced reputation, performance, and brand image among key stakeholders.

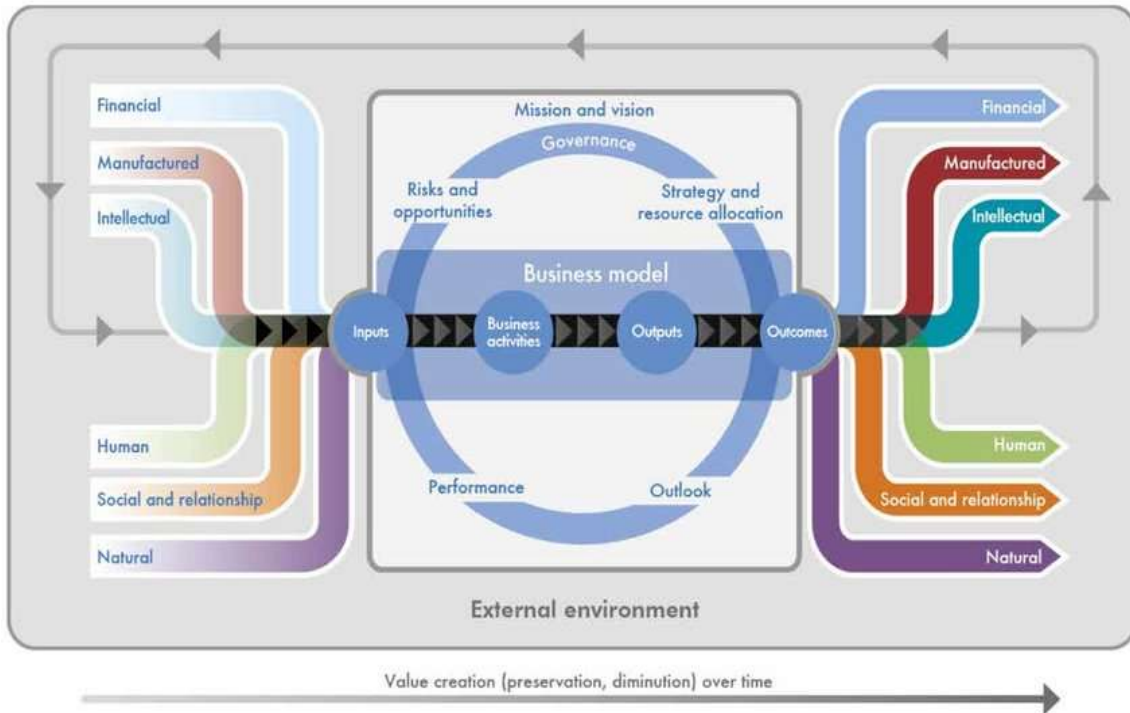
Figure II: Overall business Strategies and Sustainable Development



On the other hand value creation is also one of the most important strategy for sustainable development of a business house. Without creating value of the firm, it become a difficult task to

sustain over a long period of time. So, there is a close relationship between value creation and sustainable development (cl continuous one) which can be seen from figure

Figure II: Value Creation process and Sustainable development through Business model



As integrated reporting is consistent with a focus on by communicating about the value creation and the value creation process, it extends to the - benefit to shareholder, preservation and diminution of value role of social environmental externalities in increasing or decreasing the value created by organization, availability stewardship of multiple capital, trade - off in relation to use of capital, implication of evolving societal expectations and resource shortages as planetary limit and the so on. Which ultimately leading to articulate how the continued availability, quality and affordability significant capital contributes to the organization's ability to achieve its strategic objective in the future and create value. Again, from the above diagram one can see the six capital i.e. - financial, manufactured capital, Human capital, Intellectual capital, Natural capital, Social and

Relationship capital as 'stores of value' and the interconnection and interdependence of each other, a business can create value of the firm and ultimately leading to sustainable development of the firm.

IV. SIX CAPITALS FOR A BUSINESS MODEL:

As the Figure III shows, the capitals are interconnected and therefore they are interdependent on each other. For example, a decision to invest in' manufactured or human capital increases this capital but_ diminishes the financial capital. Considered as input factors, capitals' role is to contribute to the future growth of the company. However, depending on the specific activity some of them may be more or less important than others, in which case they add too little to the value creation processes therefore being "immaterial for reporting" (IIRC, 2013).

Figure III: Interconnection and interdependence of Six Capitals



A significant obstacle when trying to promote and enforce a new reporting framework is the measurement. Used to quantitative indicators and metrics nowadays it has become obvious that this is not enough. For many components of the capitals this is not possible - human capital incorporates experience, reputation or loyalty; can these be monetary evaluated? Others are measured better by accounting their effects and by making use of narratives instead of figures. But IR offers is a benchmark system against which an organization can start evaluating and reporting all its capitals. This means that there will be capitals which are not covered by the six capital theory but can be included if necessary for achieving the goals of an integrated report.

Following, the paper presents each type of capital according to a Background paper on IR that aims at detailing the six capitals theory, corroborated with information from Deloitte, Ernst & Young, and ACCA.

Financial Capital represents the "pool of funds" available and used by a company in the production process. It comprises the debt, equity and grants, interacting with the other capitals by the way it transforms itself to value. The financial capital is a means for acquiring other forms of capital - investing in the personnel qualifications by training decreases the financial capital but it increases the value of the human capital. Still the perspective of IR on the financial capital is oriented towards the sources of funding and not on the acquisition process.

Manufactured Capital is defined as "material goods and infrastructure owned, leased or controlled by an organisation that contribute to production or service provision, but do not become embodied in its output" (The Sigma Project), such as buildings or infrastructure. A characteristic is that it combines both tangible elements as well as intangible, which are associated of intellectual capital like patents for a machine.

The next is **Intellectual Capital**, whose definition is still under construction. The notion has most often been defined by its three components - human capital, structural (organizational) capital and relational component, but for reporting

purposes this could cause confusion (Human capital and Social and Relational Capital). There are also subtle aspects to be analyzed: intellectual capital has both intangible assets and liabilities (intellectual liabilities) yet unaccounted for; the intangibles must possess certain futures so they can be reported - "durably and effectively internalized and/or appropriated" (IIRC, 2013) by the company. At last, reporting must make the distinction between intellectual capital and intellectual property which are not the same. The latter is only a part of IC over which the company has legal rights.

Because of these reasons the next three capitals are separately reported and disclosed though under debate as they are strongly connected to IC.

Human Capital is represented by individual employees who have the skills, abilities, loyalty and experience, all required for the duties specific to the company for which they work. This implies that the organization is in control as it is responsible for the selection procedure of the human resources.

On the other hand, the **Social and Relationship Capital** is embedded in the networks a firm has, both internal and external ones. Obviously it is linked also to the Human Capital but it refers mainly to social aspects, functioning as a complement to it and to IC.

Finally, Natural Capital includes the natural resources that are vital to performing any economic activity, renewable and not renewable, such as water supplies, soil, minerals or air, all necessary to produce goods and services.

In short, integrated reporting is linked to integrated thinking which can be seen from of significance of integrate reporting to the business sector.

V. SIGNIFICANCE OF INTEGRATED REPORTING TO THE BUSINESS SECTOR

Integrated reporting fosters "integrated thinking" resulting to –

- Resource allocation decisions which take account of all "six capitals" and their effects on each other

- Greater collaboration throughout the company
- More effective engagement with significant audiences
- A better managed company

More relevant and reliable data Better decisions Long-term sustainable value

- Demonstrates to investors the company's ability to create value over the long term
- Makes clear how the company is supporting the government's policies for sustainable development

Considering the importance's of integrated reporting while communicating about the organization's strategy, governance, performance and prospect leading to the creation of value over the short, medium and long term representing the company performance in term of both financial and non-financial information one should analyse the challenges of integrated reporting for an effective implementation.

VI. CHALLENGES OF INTEGRATED REPORTING

Strategically, integrated reporting needs the

- Understanding how <IR> can support the company's strategy
- Being willing to be one of the first
- Seeking competitive advantage rather than waiting for external validation
- Recognizing that integrated reporting is a journey, not an outcome Again, tactically also integrated reporting is necessary to analyse–
- Inadequate IT and internal management and control systems
- A new reporting process needs to be created
- Lack of standards for nonfinancial information

VII. CONCLUSION

In short, integrated reporting elicits the organization's material information, about their strategy, governance, performance and prospect in a clear concise and comparable format by reflecting the development in financial, nonfinancial, management, governance and sustainability. However, this benefit must be weighed against the potentially onerous data collection. And validation needed to compile reports and risks around "ultimately raising stakeholder expectation of multi-faceted performance".

Considering the importance of integrated reporting, for an effective application over coming of the challenges is also initiated through - full support of CEO, Board; and the being clarity about the role of the company in the society etc.

Lastly, further research about integrated reporting and the way of its applying by the

corporate sector is necessary to analyse for further action accordingly.

REFERENCES

1. Abeysekera, I. (2013). A template for integrated reporting, Journal of Intellectual Capital, Issue 14, Vol. 2, pp. 227-245
2. ACCA (the Association of Chartered Certified Accountants) (20 2). Reporting pre- and post-King III : what's the difference?, [Online], Available at: <http://www.accaglobal.com/content/dam/accaglobal/PDF-technical/integrated-reporting/tech-tpwtd.pdf>
3. Accounting for Sustainability, A4S Reporting guides and examples, [Online], Available at: <http://www.accountingsustainability.org/connected-reporting/connected-reporting-a-how-to-guide>
4. Association of Chartered Certified Accountants (ACCA), Jones, H. (2012). "Sustainability reporting matters. What are national governments doing about it?", [Online], Available at: <http://www.accaglobal.com/content/dam/accaglobal/PDFtechnical/sustainability-reporting/tech-tpsrm.pdf>
5. Deloitte Global Services Limited (2011). "Integrated Reporting. A better view?," [Online], Available at: http://www.deloitte.com/assets/Dcom-MiddleEast/Local%20Assets/tDocuments/Services/ERS/me_ers_integrated_reportingsept11.pdf
6. Ernst & Young (2013). "The concept of 'capital' in Integrated Reporting" [Online], Available at: [http://www.ey.com/Publication/vwLUAssets/The_concept_of_capital_in_Integrated_Reporting_-_July_2013/\\$FILE/EY%20'Capital'%20in%20Integrated%20Reporting%20July%202013.pdf](http://www.ey.com/Publication/vwLUAssets/The_concept_of_capital_in_Integrated_Reporting_-_July_2013/$FILE/EY%20'Capital'%20in%20Integrated%20Reporting%20July%202013.pdf)
7. Global Reporting Initiative (GRI), [Online], Available at: <https://www.globalreporting.org/reporting/reporting-framework-overview/Pages/default.aspx> <http://www.sap.com/about.html>
8. International Integrated Reporting Council (IIRC), <http://www.theiirc.org/>
9. PricewaterhouseCoopers Africa (2013). King III Report, Chapter 9: Integrated reporting and disclosure, [Online], Available at:

- <http://www.pwc.co.za/en/king3/integrated-reporting-and-disclosure/index.jhtml>
10. SAP Integrated Reporting 2012, [Online], Available at:
<http://www.sapintegratedreport.com/2012/en/nd-about-this-report/about-this-report.html>
 11. Solomon, J., Maroun, W - ACCA (the Association of Chartered Certified Accountants) (2012). "Integrated reporting: the influence of King III on social, ethical and environmental reporting", [Online], Available at: <http://www.accaglobal.com/content/dam/acca/global/PDFtechnical/integrated-reporting/tech-tp-iirsa.pdf>
 12. The Sigma Project (2006). Manufactured Capital, [Online], Available at: