NEED TO GET UP TO SPEED ON INTEGRATED REPORTING?

LEIGH ROBERTS EXPLAINS THE 101 OF INTEGRATED REPORTING

Q: Who should prepare an integrated report?
A: There are many reasons that an organisation would – and should – prepare an integrated report. There's absolutely no doubt that the integrated report – with its emphasis on conciseness, strategic focus and future orientation, connectivity of information, and the capitals and their interdependencies – is a huge improvement on the traditional annual report. Also, responsible institutional investors (the signatories to the Code for Responsible Investing in South Africa, or CRISA, and the Government Employees Pension Fund, among others) want to read a quality integrated report to inform their investment decisions (see article by David Couldridge on page 32). Other stakeholder groups such as employees and suppliers like to read the integrated report because it offers a holistic view of the organisation, its future, and how it creates value over time. (The publication *Realizing the benefits: the impact of integrated reporting* available on www.theiirc.org lists other benefits experienced by organisations.)

In South Africa, companies listed on the JSE are obliged to apply the principles of King III – which include that of integrated reporting – or to publicly explain why they are not applying a principle. In my view, even newly listed companies would find it hard to reasonably explain away the lack of an integrated report. The larger parastatal companies such as Eskom and Transnet prepare integrated reports as a mark of good governance and reporting, as do some small organisations such as SAICA and the Independent Regulatory Board for Auditors (IRBA).

One could say that integrated reporting is becoming the norm in South Africa – and the rest of the world is just catching up.

Q: Which guidance should an organisation use?
A: While the Integrated Reporting Committee (IRC) of South Africa in January 2011 released the world's first discussion paper on a framework for an integrated report, things have moved on – and indeed the local paper fed into the subsequent international iterations. In December 2013, the International Integrated Reporting Council (IIRC) released the International <IR> Framework (Framework). The Framework is now used by organisations in Japan, Malaysia, Singapore, the United Kingdom, the European Union, Canada, and in many other countries. One could call it the de facto international "standard".

In March 2014 the IRC of South Africa endorsed the Framework as guidance on how to prepare an integrated report.

Local organisations may wonder at how the Framework fits with the principles of King III. The King III Practice Note (available on www.sustainabilitysa.org) helps out by reconciling the two. It states that while King III covers the principles, the Framework addresses the "how to" of an integrated report and if an organisation believes a principle of King III is not being met by applying the Framework, then it should explain this (because King III is on an apply or explain basis). The Framework is flexible enough to allow for regulation differences in different countries. This is largely through section 1E and caters for the main differences to King III being the "audience" and form of the report (long or short?) covered later in this article.

The IRC has a useful information paper *Preparing an integrated report – a starter's guide*, which sets out the planning and processes to be considered by new preparers based on the wisdom of some of some of South Africa's experienced reporters (available on www.integratedreportingsa.org from early December 2014).

Q: What's the difference between the terms integrated report, integrated reporting and integrated thinking?
A: The Framework's definition of an integrated report is: "a concise communication about how an organisation's strategy, governance, performance and prospects, in the context of its external environment, lead to the creation of value over the short, medium and long term".

The Framework's definition of integrated reporting is: "a process founded on integrated thinking that results in a periodic integrated report by an organisation about value creation over time and related communications regarding aspects of value creation".

The Framework's definition of integrated thinking is: "The active consideration by an organisation of the relationships between an organisation's various operating and functional units and the capitals that the organisation 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."

So, the integrated report (which most commonly appears annually) tells the holistic picture of the organisation and results from the integrated reporting process of preparing the report. This process rests on the integrated thinking in the organisation. Integrated thinking means considering the implications of decisions and business activities for all the key capitals used or affected by the organisation (the Framework's six capitals are financial, manufactured, environmental, intellectual, social and relationship, and human). The reason is that, if nothing else, the current effect an organisation has on its key capitals today affects their future availability, quality and affordability – and that influences the organisation's future.

Integrated thinking is hot right now because in the connected world of the 21st century how can anyone focus only on financial capital knowing full well that other capitals key to that business impact on the organisation's future? (See article on integrated thinking by Graham Terry on page 42.)

In February 2015, SAICA will release a thought leadership paper on integrated thinking based on a survey of the Top 40 listed companies, the larger parastatals, and some nonexecutive directors (this will be available on www.integratedreportingsa.org).

Q: How does the integrated report fit with other reports such as the annual financial statements?
A: The integrated report can easily fit into the existing structure of corporate reporting. Many larger companies already produce a plethora of detailed reports covering particular information and aimed at different stakeholder groups. In describing how the integrated report fits with these, the octopus can lend a hand.

The head of the octopus can be seen as the integrated report. The head is connected to the multitude of arms with each arm representing a detailed report or communication, such as the annual financial statements, sustainability report, governance report, remuneration report, regulatory reports and so on. The integrated report connects the different type of information, including the financial to the non-financial, and in so doing explains how the company creates value and how it can continue to create value in the future.

Q: Should the annual financial statements be included in the integrated report?
A: The Framework makes no mention of this. Section 1E, however, offers flexibility to including other information in the integrated report provided that such other information "does not obscure the concise information required by the Framework". So, while the Framework's requirement is for the integrated report to be a "designated, identifiable communication", other information can be latched on to it under the conditions of section 1E.

A rising trend among the larger JSE-listed companies is for abridged financial statements to be included with the integrated report, with the full annual statements available elsewhere (usually on the company's website).

Q: What is value creation?
A: It's more than financial value and more than the value added statement.

See it more in the line of the following: an organisation draws on inputs from its capitals, these churn through its business model activities and are spewed out as products, services and waste – and also as various consequences on the input capitals and any other capital affected by the organisation. These material consequences are termed "outcomes" in the Framework and should be disclosed in the integrated report with qualitative and/or qualitative information.

For example, a pharmaceutical company makes vaccines (its product) which it sells to make profit for itself and shareholders (thus increasing financial capital) with the vaccine helping customers and improving the company's reputation (thus increasing social and relationship capital); the production process relies on the patent (intellectual capital) and uses water and other natural resources (thus decreasing environmental capital). The total value created by the organisation of being in business over time is all of the above positive and negative consequences for the capitals. The consequences are not required to be quantified in the integrated report – but if not, use narrative to explain them so that readers can make an informed assessment of the company, how its run, and its ability to create value in the short, medium and long term.

As the Framework states, the company's value is created for the organisation and for others: "the ability of the organisation to create value for itself is linked to the value it creates for others ... [T]his happens through a wide range of activities, interactions and relationships ..."

Value creation and the six capitals are the two underlying concepts of the Framework. Understand these and you understand integrated reporting. Building on these concepts in the Framework are seven guiding principles (that guide on the preparation and type of information) and eight content elements (akin to information areas in the report). Also, there are 18 requirements (based on the guiding principles and content elements) which must be met if the integrated report is said to reference the Framework.

Q: What to call the report?
A: South African organisations variously use the terms Integrated Annual Report, Annual Integrated Report, or Integrated Report. My preference is for either of the last two (to pave the way for the future Interim Integrated Report).

Q: Can an organisation prepare an integrated report if integrated thinking is not embedded in the company?
A: It can and it should start the integrated reporting process. There's no doubt, though, that a report from an organisation that has embedded integrated thinking will be of much higher quality.

Embedding integrated thinking takes time and needs to happen at three levels: the board, senior management and employees. It necessitates a mindset change from thinking about the short-term financial only to considering the implications of decisions and activities for all the key capitals in the short, medium and long term, and the resulting effect on the organisation. So, don't delay – start your integrated reporting process. Organisations that have gone this route say that integrated reporting significantly helped embed integrated thinking and helped lead to more informed decision-making, among other benefits. Well-run organisations will probably already have a level of integrated thinking in their business.

Q: What is the Integrated Reporting Committee of South Africa?
A: The IRC was formed in May 2010 under the chairmanship of Professor Mervyn King. Its objectives are to develop and promote guidance on good practice in integrated reporting in South Africa. The IRC has a Working Group comprising various individual experts.

The current organisational members of the IRC are the Association for Savings and Investment South Africa (ASISA); the Banking Association of South Africa (BASA); the Batseta Council of Retirement Funds for South Africa, previously known as the Principal Officers Association (POA); Business Unity South Africa (BUSA); Chartered Secretaries Southern Africa (CSSA); the Financial Services Board (FSB); the Institute of Directors in Southern Africa (IoDSA); the Institute of Internal Auditors (IIA); the Government Employees Pension Fund (GEPF); the Johannesburg Stock Exchange (JSE); the Finance Union (SASBO); and SAICA. The individual members are Dr Gavin Andersson, Dr Bob Scholes, Ansie Ramalho, and Leigh Roberts (as chairperson of the Working Group) (see www.integratedreportingsa.org).

The IRC holds regular networking events aimed at information-sharing and discussion of topical issues around integrated reporting. If you would like to be added to its database, please send an email with your contact details to the IRC secretariat at lynettek@saica.co.za.

The IRC undertakes technical projects through its Working Group. The 2014 projects were the information paper Preparing an integrated report: a starter's guide and a research paper, Scan of research on integrated reporting in South Africa (January 2010 to June 2014) and identification of future research opportunities. The latter is a valuable resource on past research (summaries of 116 documents dated from January 2010 to June 2014 are housed on www.integratedreportingsa.org) and highlights areas where research is needed.

Q: What is the International Integrated Reporting Council?
A: The IIRC is a global coalition of regulators, investors, companies, standard setters, the accounting profession and NGOs. Together, this coalition shares the view that communication about businesses' value creation should be the next step in the evolution of corporate reporting. A link to the International <IR> Framework can be found on *www.theiirc.org* (or *www.integratedreportingsa.org*). Professor Mervyn King is the current chairman of the IIRC.

Q: Does the integrated report need a specified audience?
A: Actually, it's a bit old-fashioned to talk about audience these days. The Framework re-stated its previous slant on audience to focus on the purpose of the report – which is to explain to providers of financial capital how an organisation creates value over time, noting that the report will be of interest to all stakeholders interested in the organisation's ability to create value.

King III is based on an inclusive stakeholder approach, which implies the integrated report should be addressed to key stakeholders. But as the King III Practice Note states, the Framework offers flexibility in section 1E such that local organisations are free to address their reports to all stakeholders (but read section 1E for the conditions). It's a choice. So, if an organisation wishes it can address its integrated report to all its stakeholders in line with King III, provided it meets the Framework's conditions.

Q: Should the integrated report be long or short?
A: The Framework calls for a concise report. King III refers to a long report which can then be summarised into a shorter report (bets are on that sense will prevail in the next King Code). Once again, section 1E offers flexibility to companies on the format of their report. It's a choice.

Q: Are directors responsible for the integrated report?
A: In many jurisdictions it's likely that directors are responsible for corporate reporting. The Framework is firm on the board, or other highest governance body, acknowledging responsibility for the integrity of the integrated report. So much so that a statement to this effect is required to be included in the integrated report (however, there is an easing-in period until no later than the organisation's third integrated report referencing the Framework).

Q: Can (and should) the integrated report be assured?
A: This is a hot international topic (see the articles by Mark Hoffman and Linda de Beer **in this issue**). The IIRC in August 2014 released two papers on assurance (available on www.theiirc.org) which are open for public comment until 1 December 2014. As assurance is not the remit of the IIRC, it plans to hand things over to the International Auditing and Assurance Standards Board (IAASB). And indeed, the IAASB now has a project group looking at the matter.

It's worth reading the above papers to get a grip on the challenges of assurance on the integrated report with its connectivity of information, call for completeness, and future-oriented information. In my view, it's just a matter of time, though, before this is commonplace. Some experts say it's already do-able. Be aware of the term "integrated assurance"– it's gaining international and local airtime and is about to make "combined assurance" look like yesterday's story while placing even greater importance on an organisation's head of internal audit.

Q: What is SAICA's involvement in integrated reporting?
A: SAICA is a proud founding member of the IRC of South Africa. It serves as secretariat and the chairperson of the Working Group is from SAICA. As secretariat, it's responsible for carrying out the objectives of the IRC, including organising and finding sponsors for IRC networking events, and running the IRC and its Working Group. In addition, SAICA is a member of the IIRC's Working Group and as such was involved in the development of the International <IR> Framework.

One of SAICA's key focus areas is integrated reporting, hence its large role in the IRC on behalf of members. SAICA believes the integrated report is the natural domain of the CFO and finance function given the CA(SA) training in reporting and systems.

SAICA also offers members training courses (notably the one-day workshop on how to prepare an integrated report, which will again be run in 2015), it co-sponsored an eight-part TV series *Integrated Reporting Made Simple III* in 2014 (see www.businessdaytv.co.za for the webcasts), and there are regular information updates via the weekly standards newsletter and the website www.integratedreportingsa.org. ❐

NOTES
1 The International <IR> Framework – Glossary.
2 The International <IR> Framework – Glossary.
3 The International <IR> Framework – Glossary.
4 Mervyn King and Leigh Roberts, *Integrate: doing business in the 21st century*, Cape Town: Juta, 2013, 72.

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Innovations in finance today relate to the changing role of the CFO, the processes used, the IT that enables them, and how this relates to the current business environment. In this article, SYSPRO, the ERP (enterprise resource planning) vendor that simplifies your success, discusses this issue.

THE BUSINESS ENVIRONMENT
Mega-trends shape how and where we work in the 21st century:
- Capital crises (banks and Wall Street): the erosion of capital value
- The climate change crisis: the effect of carbon footprints
- The natural resources crisis: we consume these faster than nature replaces them
- Radical transparency: driven by consumer activism
- Marikana: the effect on labour activism
- Stakeholder activism: not just shareholders at the AGM

These factors must be top of mind for all boards while making decisions to ensure their company value meets the "triple bottom line" (a phrase coined by John Elkinson) measuring financial, social and environmental performance. Gone are the days of a few wealthy shareholders focusing on their returns. Company assets are now 80% intangible and only 20% financial.

Capital has also changed. Today, six capitals have to be watched by the CFO: financial, manufacturing, human, intellectual, social and relationship, and natural.

Other global conditions need to be factored in: growing cross-religion confrontation globally; fury of the "middle classes" against the perceived "owning classes"; and ageing populations. These all affect our trading world, products, services, prices, and behaviour as global citizens.

Innovation must be central to your business. Create a new product every year, live your brand, and still be the cheaper alternative. With an ambivalent government, over-regulated departments, and banks that will not lend, our economy needs a vibrant industrial sector full of entrepreneurial spark driving innovation, jobs and GDP.

RIGHT PRACTICES FOR TODAY'S CFO
The CFO's domain is no longer limited to capital expenditure, financial reports, tax, and cost management. These must be managed, but today the role of the CFO is to advise the board using clear, relevant, balanced information providing business insights to enable effective decision-making.

Integrated reporting (IR) is a fundamental innovation for company reporting starting with King III and now, in its third year, companies and leading CFOs accept it as the norm. IR covers financial and non-financial value, earnings, and appropriate use of resources for a sustainable organisation.

IR deals with the six capitals and offers a balanced insight into company affairs. Alas, some companies still believe more is better. This "thud factor" thinking produces poorer reporting. Condensed reporting is an objective of IR.

Augmented by more pervasive and predictive business analytics, information systems aid new CFO demands. CFOs have become more familiar with the realities of managing manufacturing, supply chains, customer service, technology, and executive needs in far more than financial terms. The CFO needs to be a business generalist who helps guide and coordinate company execution to agreed strategy. In short, the CFO must make the organisation more effective and efficient.

INNOVATIONS IN IT
As a support function, finance must renew departmental processes reducing cost and people while increasing productivity and skills. This requires strong but intuitive information systems.

The aim of IT for CFOs and organisations is to enable accurate and auditable transaction processing, typically using an ERP system. It also provides the information needed to simplify running the business. However, ERP alone is inadequate. Business intelligence – not just reporting – fuelled by analytics helps process and present complex information in a digestible way for people to react to, thus increasing their effectiveness.

Back to integrated reporting – where we started. If you are using spreadsheets for IR, it means your reporting has no life and it is time to implement an ERP system. IR uses transactional data inside and outside the company. It requires structured and unstructured information and can demand insights from "Big Data".

With all these innovations hitting us, a final sobering thought: "The largest room in the world is the room for improvement."