PROFIT TO VALUE CREATION

WHY? & HOW?

OF INTEGRATED REPORTING

RSM

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WHY INTEGRATED REPORTING?

- IMPERATIVE
- SEBI CIRCULAR

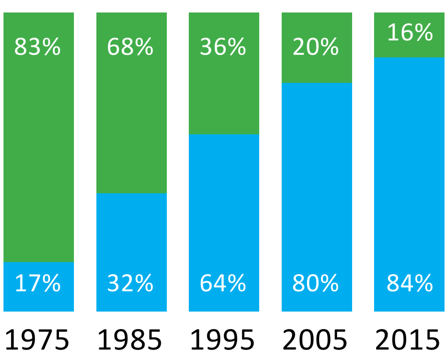
WHY?

INTEGRATED REPORTING IMPERATIVE

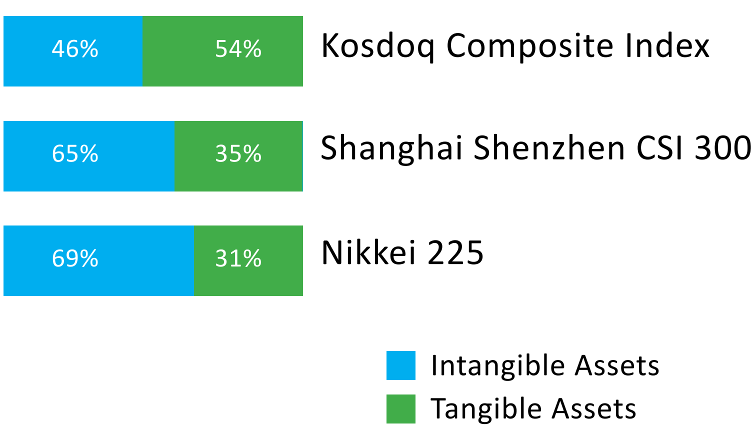
Enhance Business Reporting

Business disclosures often present the information which is insufficiently strategic and sector specific. Hence, many investors continue to struggle to integrate all the relevant risk factors that contribute to value creation over time into investment decisions. As a result, there is a risk that capital is not being directed efficiently towards those companies that have robust business models. By disjointed view of non-financial from financial performance, one would miss what most CEOs and boards already know well – that these two are not isolated, but interconnected. For example, labour standards, employee satisfaction, customer health & safety, community relations and compliance records are fundamental to the success of the business and its "license to operate". It is important to enhance the business reporting framework so that the business provides the context alongside its strategy and business model and discloses more holistic view of the performance.

Components of S & P 500 Market Value



The share of intangible assets has grown from 17% in 1975 to over 84% of total market value in 2015 for S&P 500 companies. That means, current financial accounting standards are not capturing massive proportion of an organization's true value. This calls for urgent reality check for business reporting.



Further, current practices of corporate reporting is disjointed in communicating financial accounts (in annual report) and nonfinancial information (in sustainability report/ business responsibility report) which do not provide adequate information to their existing and potential financial stakeholders. Reporting must evolve to address the information needs of business decision makers within this changed business dynamic.

SEBI CIRCULAR

Securities and Exchange Board of India (SEBI) through its circular on 6 February 2017, advised the top 500 listed companies to voluntarily adopt Integrated Reporting (<IR>), in addition to the existing Business Responsibility Reports (BRR) mandate. <IR> has been made applicable from FY2017-18. SEBI in its circular mentions that adoption of Integrated Reporting is in keeping with regulation 4(1)(d) of SEBI LODR which states "*the listed entity shall provide adequate and timely information to recognised stock exchange(s) and investors*" and IOSCO Principle 16 which states "*there should be full, accurate and timely disclosure of financial results, risks and other information that is material to investors´ decisions*".

The information related to Integrated Reporting, as per SEBI circular can be

- Provided in the annual report separately
- Incorporated in Management Discussion & Analysis
- Provided in a seperate report

In case, the company has already provided the relevant information in any other report prepared in accordance with national/international requirement / framework, SEBI's circular provides for appropriate referencing to the same in its Integrated Report so as to avoid duplication of information.

ABOUT
INTEGRATED REPORTING?

- INTEGRATE
- GUIDING PRINCIPLES
- CONTENT ELEMENT
- AT THE CORE
- CORPORATE REPORTING FOR INTEGRATED PERFORMANCE
- EVOLUTION OF INTEGRATED REPORTING

INTEGRATE

IIRC- International Integrated Reporting Council

(previously the International Integrated Reporting Committee) was formed in August 2010 with an objective to create a globally accepted framework for a process that results in communication by an organization about the value created over time.

The IIRC brings together a cross section of representatives from corporate, investment, accounting, securities, regulatory, academic and standard-setting sectors as well as civil society. Post extensive consultations with various stakeholder groups, IIRC released the Integrated Reporting framework in 2013 and followed it up with promotion to increase the scale and pace of Integrated Reporting adoption.

Integrated reporting (<IR>) brings together material information about an organization's strategy, governance, performance and prospects in a way that reflects the commercial, social and environmental context within which it operates. It provides a clear and concise representation of how an organization demonstrates sustainability and creates value. The International Integrated Reporting Framework sets out the guiding principles and content elements of an integrated report.

An integrated report may not necessarily include quantified values of an organization at a point in time, but may include a combination of both quantitative and qualitative information which best explain how an organization creates value over time. The Framework requires the integrated report to include a statement from those charged with governance, acknowledging their responsibility for integrated reporting by no later than the organization's third integrated report that references the <IR> Framework.

While adopting <IR>, it is important to note that it is not just about reporting but about incorporating the <IR> processes connected with - Renovation of Value Creation, Business Model, Materiality, Risks and Opportunities and hence Governance.

NOT EVERYTHING THAT COUNTS, CAN BE COUNTED AND NOT EVERYTHING THAT CAN BE COUNTED COUNTS.

- ALBERT EINSTIEN

GUIDING PRINCIPLES

The following Guiding Principles underpin the preparation of an integrated report, informing the content of the report and how the information is to be presented:

Strategic Focus and Future Orientation:
An integrated report should provide insight into the organization'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 and effects on the capitals.

Stakeholder Relationships:
An integrated report should provide insight into the nature and quality of the organization's relationships with its key stakeholders, including how and to what extent the organization understands, takes into account and responds to the legitimate needs and interests of the stakeholders.

Conciseness:
An integrated report should be concise.

Consistency and Comparability:
The information in an integrated report should be presented:

- on a basis that is consistent over time; and
- in a way that enables comparison with other organizations to the extent it is material to the organization's own ability to create value over time.

Connectivity of Information:
An integrated report should show a holistic picture of the combination, interrelatedness and dependencies between the factors that affect the organization's ability to create value over time.

Materiality:
An integrated report should disclose information about matters that substantively affect the organization's ability to create value over the short, medium and long term.

Reliability and Completeness:
An integrated report should include all material matters, both positive and negative, in a balanced way.

CONTENT ELEMENTS

Organizational Overview And External Environment
What does the organization do and what are the circumstances under which it operates?

Strategy And Resource Allocation
Where does the organization want to go and how does it intend to get there?

Governance
How does the organization's governance structure support its ability to create value in the short, medium, and long term?

Business Model
What is the organization's business model and to what extent is it resilient?

Opportunities And Risks
What are the specific opportunities and risks that affect the organization's ability to create value over the short, medium, and long term, and how is the organization dealing with them?

Performance
To what extent has the organization achieved its strategic objectives and what are its outcomes in terms of effects on the Capitals?

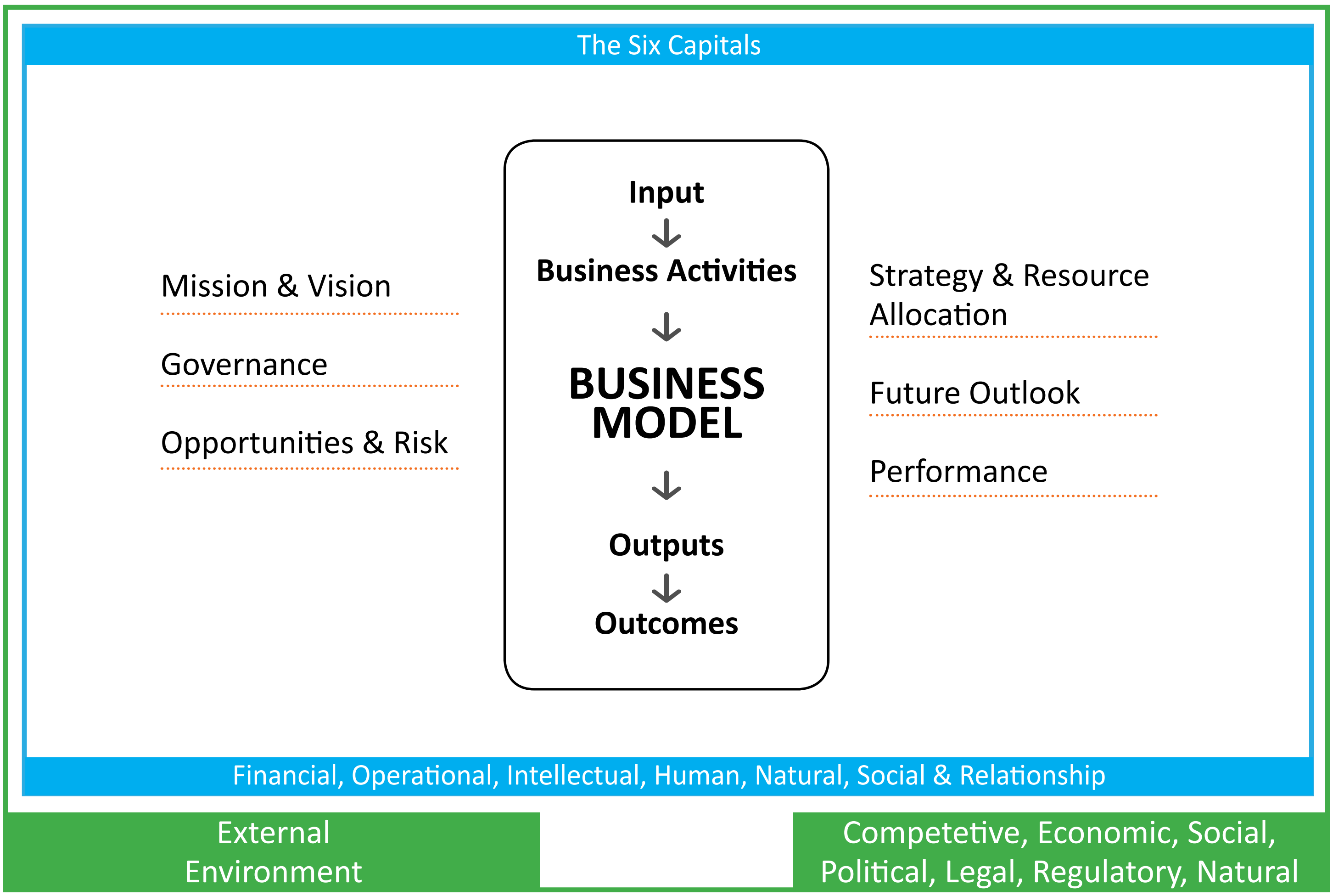
Future outlook
What challenges and uncertainties is the organization likely to encounter in pursuing its strategy, and what are the potential implications for its business model and future performance?

AT THE CORE

The Business Model

The business model, as per <IR> framework is its "system of transforming inputs, through its business activities, into outputs and outcomes that aim to fulfill the organization's strategic priorities and create value over the short, medium and long term."

THE BUSINESS MODEL, SITS AT THE HEART OF THE ORGANISATION, WITHIN THE CONTEXT OF THE EXTERNAL ENVIRONMENT



There is need to understand the business model at both the tactical and strategic levels within an organization. At the strategic level, it is imperative for the board to understand how their organization creates value through its chosen business model and the risks it faces. At the tactical level, the focus is on imperatives of improved customer experience, cost leadership, management of external resources, limiting the effect of competitor activity etc. At any level, the focus should be on value creation leading to long-term business success through enhancing and reinforcing the value-creating opportunities and the minimization of value-limiting factors.

CORPORATE REPORTING FOR INTEGRATED PERFORMANCE

Prince's A4S (Accounting for Sustainability) project, AICPA (American Institute of Certified Public Accountants), WICI (World Intellectual Capital/Assets Initiative), EBR (Enhanced Business Reporting) consortium and others have highlighted addressed some gaps in business reporting.

Effective March 2010, King Code authored by Professor Mervyn King applies to all companies listed on the Johannesburg Stock Exchange (JSE). King III requires companies to file an integrated report that encompasses economic, social and environmental performance. Denmark also requires public companies to file integrated reports. In Brazil, the Sao Paolo stock exchange requires that listed companies must report or explain their approach towards corporate responsibility. The Shenzhen and Hong Kong stock exchanges introduced CSR reporting guidelines for listed companies. In US, SEC regulations S-K viz., form 10K and 20F require non-financial information.

External reporting in most jurisdictions around the world is a complex mosaic of requirements. Many of the content elements of the proposed integrated reporting framework are already encompassed by one or more existing requirements, allowing companies to draw upon existing disclosures in the preparation of <IR>.

Evolution of Integrated Reporting

1999

- Value reporting framework 1999 (Corporate Reporting Framework) was created

2002

- Novozymes first 2002 intergrated report
- Institute of Direction of Southern Africa(KING II): Governance code on ESG

2003

- Business impact review 2003 group
- Indicators that count
- Magna Rautenbach: Integrated sustainability Accounting, Assurance and Reporting (ISAAR)

2004

- Sustainability
- Enhanced Business Reporting consortium (EBR360)

2007

- The Prince's accounting 2007 for sustainability project (A4S)
- World Intellectual Capital Initiative (WICI)

2008

- Sustainabilty:GRI readers' choice
- Corporate Register first annual award for best integrated report

2009

- Preliminary foundation of IIRC
- International corporate gorvernance network (ICGN) recommends IR
- European commission workshops on ESG disclosure
- KING I II (South Africa)

2010

- Official formation of IIRC
- South Africa established integrated reporting committee

2011

- Integrated reporting discussion paper
- IIRC pilot programme

2012

- Prototype of the framework
- Emerging IR database

2013

- Consultation Draft of the International IR framework
- International <IR> framework published

"Despite an increase in the volume and frequency of information made available by companies, access to more data for public equity investors has not necessarily translated into more comprehensive insight into companies. Integrated reporting addresses this problem by encouraging companies to integrate both their financial and ESG performance into one report that includes only the most salient or material metrics."

AL GORE AND DAVID BLOOD, A MANIFESTO FOR SUSTAINABLE CAPITALISM

HOW INTEGRATED REPORTING?

- DEVELOP
- WHERE WE ARE?
  WHAT IS THE WAY FORWARD?
- ROAD AHEAD

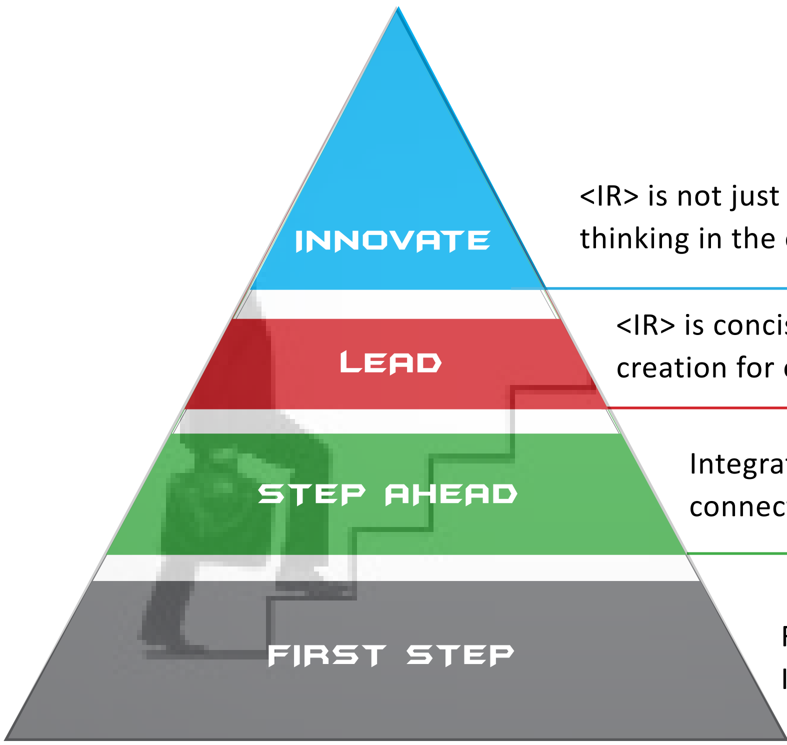
DEVELOP

Integrated Report

The Integrated report is expected to be future oriented with firm focus on strategy, business model and value creation. The report should present a comprehensive value creation story, the combination, interrelatedness and dependencies between the components that are material to the organization's ability to create value over time. This greater cohesion in the reporting process promotes integrated thinking as a way of breaking down internal silos, reducing duplication and driving positive behaviors focused on long term success.

While it is desirable to first establish integrated thinking and in phase-wise manner graduate to Integrated Reporting (as in Fig. below), it is important to take a pragmatic view of existing business requirements, processes in practice, variety of public and limited disclosures and management accounting and other documentation in an organization for developing first Integrated Report and then gradually strengthening the process of Integrated Thinking.

One could clearly discern four kinds of <IR> practitioners suggesting the steps in the journey towards best <IR> practice.



<IR> is not just a report, it is the reflection of integrated thinking in the organization

<IR> is concise and is connected with the focus on value creation for organization's today and tomorrow

Integrated Reporting with strategic focus, still the connectivity of information is limited

Reporting non-financials, few elements of the International <IR> framework are visible

Organizational journey towards Integrated Reporting would differ from entity to entity depending upon strategic clarity, processes and systems which are already in place. Organizations with experience in sustainability or non-financial reporting for significant number of years or with robust internal management accounting, business excellence or balance score card deployment, may find Step Ahead is their First step or in some cases whatever they are already doing may require recast to become the leader. Hence first step in <IR> journey is to determine -

WHERE WE ARE?
WHAT IS THE WAY FORWARD?

Constituting cross functional <IR> champions team and understanding <IR> principles and practice

Assess the status of organizations' systems and practice (Non-Financial Reporting, Management Accounting, ISO, Business Excellence or Manufacturing Excellence systems/ practices, Balance Score Card, Internal Audit practice) vis a vis <IR> principles and guidance on "Scan of External environment, Value Creation Model, Risks and Opportunities, Strategy and Resource Allocation, KPIs and Outlook"

Position yourself on <IR> practice pyramid
(you could chose to follow RSM tool)
and develop a road map ahead.

ROAD AHEAD

The road ahead will depend on

-Where you are today?
-Where you want to be tomorrow?
-How swiftly you want to reach your target?

Typically, in view of SEBI’s circular and related other developments, it is desirable that organizations begin integrated reporting in FY 18 and have increasingly mature integrated reporting practice in the next three years by FY 20.

FIRST STEP

CAPTURE

Capture As-is “Scan of External environment, Value Creation Model, Risks and Opportunities, Strategy and Resource Allocation, Outlook”.

DEVELOP

Develop KPIs to monitor and measure, to the extent feasible, Value Creation in terms of <IR> capitals, impact due to evolving environmental changes, progress and effectiveness of strategies - limiting to the indicators that are being monitored presently as a part of financial, management and sustainability accounting.

PREPARE

Prepare Integrated Report as a part of Sustainability Report or as a separate extension but bounded with the Annual Report.

STEP AHEAD

DISCUSS

Discuss in a workshop of cross functional <IR> team the findings of "Scan of External environment, Value Creation Model, Risks and Opportunities, Strategy and Resource Allocation, Outlook" developed from available organizational information. Obtain information for further refinement.

MAP

Conduct strategy mapping and fill in Value creation worksheet (following a robust method/tool) for the business. Also collate measures (may incorporate limited new measures) to measure/assess state of value creation factors and deployment of strategy for the relevant <IR> capitals.

VALIDATE

Conduct internal and external strategic stakeholder engagement to validate value creation model and strategy map.

MEASURE AND RECORD

Set up data gathering processes for new KPIs and collate relevant financial and non-financial data for the relevant capitals.

LEAD

REFINE AND RESTATE

Based on the outcome of strategic stakeholders engagement, the <IR> champions team set up a task force and work towards refining and restating:

- Value creation model and indicators for tracking value creation processes and value created in terms of various capitals (inputs, outputs/outcome).
- Business model: Positioning value creation model within its strategic framework, showing how company's values, purpose, and strengths form the basis of the value created for different stakeholders.
- Risks and opportunities: What are the specific risks and opportunities that affect the organization's ability to create value over the short, medium and long term and how is the organization dealing with them?
- Strategy and resource allocation: Where does the organization want to go and how does it intend to get there? Understanding social, commercial and environmental context in which company operates and its response to challenges for short, medium and long term growth. Demonstrating clear link between risks/opportunities, strategies and business performance.
- Outlook: What challenges and uncertainties is the organization likely to encounter in pursuing its strategy and what are the potential implications for its business model and future performance?

TARGET AND DATA MANAGEMENT

- Identify the indicators which are not tracked as part of compliance, sustainability and management reporting or otherwise and set up systems to track and record with data controls.
- Set targets for select indicators that are critical in tracking the effectiveness of deployment of strategy to preserve and enhance value creation ability and are in line with vision, mission and objectives.
- Work with <IR> champions team to develop a road map to achieve target.

INTERNAL AUDIT

Review the <IR> processes and content against <IR> principles and of progress on road map for identified indicators

DEVELOP IR

Collect data on additional KPIs and collate available financial and non-financial information and develop the integrated report content to be dovetailed into Annual Report, possibly as a part of Management Discussion and Analysis.

INNOVATE

REVIEW AND REFINE

Review and refine of value creation model, business model, risks and opportunities, strategy and resource allocation and outlook against the criteria.

Develop KPIs to demonstrate interconnectedness and deploy systems of internal controls to improve credibility of data and information that are inputs to KPIs.

Conduct review and audit of additional (other than the items audited and assured as per statutory requirements) information following robust guidelines and standards e.g., ISAE 3000.

Develop Integrated Report and assign review and audit (to an independent agency) with scope that includes checks against criteria viz., connectivity of information, stakeholder relationships, materiality, conciseness, reliability and completeness, consistency and comparability, strategic focus and future orientation.

THE GROSS NATIONAL PRODUCT ...MEASURES.... NEITHER OUR WIT NOR OUR COURAGE, NEITHER OUR WISDOM NOR OUR LEARNING, NEITHER OUR COMPASSION NOR OUR DEVOTION TO OUR COUNTRY, IT MEASURES EVERYTHING IN SHORT, EXCEPT THAT WHICH MAKES LIFE WORTHWHILE.

- ROBERT F. KENNEDY

<IR> practice is led by **Rambabu Paravastu**, Chief Executive Officer of RSM GC Advisory Services Pvt. Ltd, an affiliate of RSM Astute Consulting group, offering advisory services in Energy and Sustainability.