Federation of European Accountants

INTEGRATED REPORTING <IR>

Enhancing transparency and value:
From the Non-Financial Information Directive to Integrated Reporting

FEE – IIRC event on Corporate Reporting

6 April 2016, Brussels

Summary

Following a welcome by **Olivier Boutellis-Taft (CEO, FEE), Paul Druckman (CEO, IIRC)** delivered a keynote address focused on how the information needs of capital markets are changing. Druckman pointed to several recent examples of innovation, including GE’s new integrated summary report and the call by Larry Fink, BlackRock’s CEO, for executives to reveal more strategic information about how they create value over time. Druckman argued that the capital markets system must change to respond to this growing demand.

Turning to the Non-Financial Information Directive (NFI Directive), Druckman pointed to the European Commission’s view that Integrated Reporting <IR> is “a step ahead”. <IR> is a step ahead in two ways, he said. First, because the six capitals model embraces a greater breadth of the value created by an organization. Second, it achieves greater depth by applying the principle of connectivity, ensuring that data and information are connected to the strategy and business model.

Richard Howitt (Member of the European Parliament) spoke both as an originator of the NFI Directive and as an IIRC Ambassador. He said the discussion had reached a point where it was “no longer a question of whether, but how” <IR> is adopted. <IR> will become the “new norm”, he said, and companies have a choice, whether to shape this emerging practice or wait. How companies account for themselves is changing, and the *Corporate Reporting Dialogue* (involving the corporate reporting standard setters and framework providers) is doing much to bring greater cohesion to the reporting landscape.

Howitt highlighted the growing international support for <IR>, and pointed not only to individual markets like Japan where <IR> is mainstream, but also to initiatives such as the *Financial Stability Board Task Force on climate-related financial disclosures*, a growing number of *Stewardship Codes* and the *Sustainable Development Goals*. These developments, and the NFI Directive itself, are a significant step towards <IR> and Howitt expressed his gratitude to the European Commission. The NFI Directive, he said, is “principles-based and enabling”, which enables the adoption of <IR> in its implementation.

He concluded by urging businesses to “get started, learn by doing, and don’t wait for someone else to make you do it”.

Erik Nooteboom (Head of Accounting and Financial Reporting, European Commission) said that "the future is some kind of integrated report that will be referred to as corporate reporting". He spoke of corporate reporting catching the public's imagination, and it would play a big role in the Juncker Commission's proposals on tax transparency.

We are living through an era of electronic reporting with a much more sophisticated understanding of technology – consideration must be given to how these developments are relevant to <IR>. Is there an opportunity to make corporate reporting more efficient and focused? From the European Commission's perspective, the NFI Directive must be implemented and applied. Responses to the Commission's consultation will provide the basis for guidelines for the implementation of the NFI Directive.

Nooteboom reflected on the discomfort within the business community about the number of ad hoc initiatives in the corporate reporting field. He asked whether all these separate elements should be put together in one readable, understandable, and workable document. He suggested looking at corporate reporting over a 20-year time-frame and consider issues such as the accessibility of information.

He concluded by saying, "…personally, I think <IR> is a necessity, it is unavoidable and it will come" because it forces companies at board level to consider the messages they wish to convey to the outside world. In an age of transparency, this is essential.

Mark Vaessen (Chair, FEE Corporate Reporting Policy Group) provided insights on the current Federation's consultation on its paper *The Future of Corporate Reporting.* He linked the relevance of information to the relevance of the accountancy profession. Corporate reporting has a growing audience reflected in the needs of different stakeholders. He asked whether corporate reporting should serve the interests of a broader stakeholder constituency.

The Federation's discussion paper starts from the perspective of the information needs of capital markets. The paper introduces the concept of *CORE and MORE*. Vaessen said that the reputation of corporate reporting had suffered due to an excess of "clutter". The idea explored in the paper is that the key elements that drive the business should be explained in the *CORE* report, while the additional *MORE* information could be enabled by technology.

Vaessen asked how innovation in corporate reporting could be encouraged and said that technology could be a driver of change, providing greater access to information as well as enabling feedback from stakeholders. He made clear that the *CORE and MORE* concept was not intended to compete with <IR> and he described <IR> as "the most developed and promising initiative". <IR> could become the *CORE* report if it is done well, he said.

Vaessen concluded on his theme of encouraging experimentation in reporting. He said that the *Financial Reporting Lab* in the UK had been a good innovation, led by the *Financial Reporting Council*. He asked whether there would be merit in establishing a similar initiative at a European level.

Jyoti Banerjee (Leader of IIRC Technology Initiative) introduced the concept of integrated thinking - <IR>, he said, is "the outcome of a process of integrated thinking". The <IR> *Technology Initiative* is designed to explore whether technology can bring clarity to integrated thinking.

Banerjee said that long-termism is causing a change to the kind of information required by companies. The increasing visibility of non-financial information means that investors are making judgements based on other kinds of issues.

We are also witnessing an exponential growth in the volume of data, with the Panama papers the latest example of transparency. We are also living through an era where disruptive business models are becoming the norm, for example in the banking sector, where non-banks are entering the sector. The problem is the CEOs lack access to the information they need. Data solutions are provided in silos creating a "messy environment". So the CFO toolkit to be released shortly by the <IR> *Technology Initiative* will equip CFOs with the questions they need to ask of Chief Information Officers: is our data stuck in silos? How do we harness the power of big data? Should we not be analysing our own information before others do?

Banerjee highlighted the example of Indra, a company that had demonstrated how integrated thinking had been embedded through the organization. The capitals introduce a new dimension. They help to abolish the notion of "non-financial information", because all the capitals are connected. It is this connectivity across the capitals that makes the difference. Frameworks are the enabler of this change, Banerjee concluded.

Chris Zerlaut (Director, Solution Management, Sustainability Performance Management, SAP) provided a practical case study, telling the story of SAP's evolution in corporate reporting from 2007 onwards, when the company produced its first sustainability report.

At first sustainability issues were managed in a silo, separate from the rest of the company. A change in CEO brought a new perspective and sustainability was integrated into the office of the CFO. It was at this point that SAP started on its <IR> journey. In SAP's case the evolution of the integrated report led to integrated thinking. Sustainability reporting was the benchmark, and it helped to explain the business culture as well as the confidence the business had in its future strategy. Then the company explored the financial impact, and developed the link through metrics and measurement.

SAP developed its integrated story KPI by KPI, starting with employee retention, developing a methodology for understanding the financial impact of employee retention. The business then looked at employee engagement, business health culture and carbon emissions, and found that a one per cent change in any of these KPIs had a significant financial impact. <IR> is, therefore, a framework for understanding the business better. It helps SAP to understand the financial impact of non-financial KPIs.

Zerlaut's advice to any business aspiring to practice <IR> is to learn how to write good business cases – the board will take an interest when you can connect the non-financial issues to financial performance.

Massimo Romano (Head of Group Integrated Reporting, Generali) spoke of his belief in integrated thinking. Generali had been a participant in the IIRC's *Pilot Programme* from 2011 onwards and had worked to improve their annual integrated report over that time, for example by leveraging infographics to provide a better understanding of the business to stakeholders.

Romano said that <IR> had led to greater simplification of the reporting suite, rationalising the way information is presented to the market. Generali has reduced the volume of interim reports, improving the effectiveness without losing any of the information to the market.

<IR> had also assisted in supporting improves internal communications. Romano described corporate reporting as a "puzzle", with lots of disconnected reports, and information in silos. <IR> helps to make sense of the puzzle, with the annual report now becoming the "core engine of corporate disclosure", explaining how the business uses its capitals to drive performance.

Romano said that the NFI Directive provides an opportunity to provide better information to markets. The risk is that the implementation is viewed as a compliance duty with pre-defined formats – this would deliver little value but an additional burden. Instead, the market should embrace an approach that enhances market transparency, break with tradition and adopt a smarter, simpler solution.

Olivier Boutellis-Taft (CEO, FEE) made the concluding remarks, thanking the speakers for their participation. He said the event had helped to articulate the role of corporate reporting in the transparency agenda. Corporate reporting innovation is "critical for doing business, for our civilisation and the sustainability of the planet", he concluded.