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Integrated Reporting

The journey to better business reporting

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IN THE HEADLINES

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> “We applaud the work of the IIRC and urge regulators, investors and governments to actively drive for change for better business reporting which can help ensure future financial stability.”
>
> – Alan Buckle
> Deputy Chairman, KPMG International

Looking beyond short-term earnings – The future of corporate reporting?

The Integrated Reporting (IR) Framework is an ambitious attempt to reshape the direction and focus of corporate reporting, aiming to provide investors with a more complete picture of business value by extending reporting beyond historical financial performance. The International Integrated Reporting Council (IIRC) has invited comments on the Framework, issuing a consultation draft on 16 April 2013.

Although the Framework is aimed at the production of an ‘Integrated Report’, the approach described is also relevant to those who simply want to improve the focus of their corporate reporting. The proposals are likely to be of particular interest to those companies already looking to improve the quality of their narrative reporting as a basis for a better dialogue with their investors.

A principles-based framework for more relevant information

Rather than specify detailed disclosures and measurement bases, the IIRC has defined a principles-based framework that would leave businesses to tell their story on their own terms, rather than through a checklist of disclosures.

Cultural shift

Report preparers would need to undergo a cultural shift if companies were to use this approach to better communicate the value they are creating. Preparers would need to recognise their reporting suite as a platform to explain what drives the underlying value of the business and how management has acted to develop and protect this value. They would need to ask themselves what the reader needs to know, rather than what they are required to tell the reader.

The increased business relevance that this could bring to the report should be welcomed, but it would be challenging for those who have come to regard the annual report as a compliance-led regulatory burden rather than a basis for better shareholder dialogue.

Relationship with other frameworks

IR would not replace other reporting frameworks. The IIRC’s vision is that preparers would incorporate relevant information produced under other more detailed reporting frameworks – e.g. IFRS – as building blocks for an integrated report.

Explaining how long-term value has been developed and protected

IR is a relatively new concept, and has been subject to a variety of interpretations – some of which are more closely linked to sustainability reporting. The IIRC has provided greater clarity over a number of areas, including the following clarifications.

- **Investors are the focus of an integrated report**. Information would only be included in an integrated report if it is considered material to an investor’s assessment of the business.
- **The purpose of an integrated report is to explain value creation in the short, medium and long term to investors**. It does not set out to value the resources controlled by the business.

These two areas in particular should help companies to narrow down the range of information that IR might require them to provide.

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Telling the business's story

IR is built around seven components of content:

- business model;
- organisational overview and external environment;
- opportunities and risks;
- strategy and resource allocation;
- performance;
- future outlook; and
- governance.

The IR Framework would not require the content elements to be discrete sections in the report. Rather, they should be seen as a high-level check to ensure that the report covers the relevant aspects of the business story.

Linking the components

By linking content across these components, an integrated report could build the story of the business from a basic description of the business model, through the external factors affecting the business and management's strategy for dealing with them and developing the business. This would provide a foundation to discuss the performance, prospects and governance of the business in a way that focuses on its most important aspects.

The linkage across the content elements would help to determine what should and, importantly, what should not be included in the report. For example, if a central part of the business strategy involves developing a particular market, then the logic of IR implies that the company should report on its progress in developing that market.

Focusing on the key drivers of business value

The result should be a report focused on the key drivers of business value – typically built around a thread of five or six key issues that run throughout the report. These should be the same issues that management is focused on in the day-to-day operation of the business, and the same issues that should be driving investors' decision-making.

Reporting the information most relevant to each business

The approach proposed by the IIRC means that the information relevant to each business would be different. Broadly, we would expect IR to result in the following outcomes.

- **More operationally focused measures of performance**, with the aim of helping readers to understand progress in implementing strategy, developing business assets and creating new income streams – i.e. leading indicators of performance, rather than lagging ones.
- **Greater focus on explaining key business assets – e.g. customer base, intellectual property and reputation** – with the aim of helping to explain how these assets have been managed and enhanced in line with the business strategy and changes to the external operating environment.
- **More emphasis on explaining factors driving future performance**, with the aim of helping readers to understand the factors driving future performance – including risks and opportunities – so that they could form their own views on how they might impact on future performance.

This should lead to reports that are more aligned with investors' own cash flow valuation models – in particular, providing a clearer picture of how management's plans and changes in the operating environment are likely to affect medium-term returns, and also helping investors to assess the substantial element of value that is typically locked up in the 'terminal value' element of their models.

Next steps

The IIRC has requested comments from all stakeholders. The comment period is open until 15 July 2013.

> "Integrated Reporting provides an opportunity to re-align corporate reporting with investor decision-making. It is an opportunity to shift reporting focus from short-term financial performance to long-term value creation."

– David Matthews
Leader, KPMG's Integrated Reporting team

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About the IIRC

The International Integrated Reporting Council (IIRC) is a global coalition of regulators, investors, companies, standard setters, the accounting profession and non-governmental organisations. It is leading the development of a global framework for Integrated Reporting, and is promoting the adoption of the IR Framework by regulatory bodies.

Find out more

You can download a copy of the consultation draft from the IIRC website.

For further information, please visit our Integrated Reporting homepage or speak to your usual KPMG contact. You can also download the following publications.

Integrated Reporting: Addressing the reporting gap provides a brief introduction to Integrated Reporting.

The future of corporate reporting: towards a common vision tests the premise that fundamental reforms are needed by interviewing ten international leaders in the field.

Timeline

November 2012:
Prototype Framework published

16 April 2013:
Consultation draft published

15 July 2013:
Consultation period closes

December 2013:
Initial version of the International IR Framework published

Ongoing development of the International IR Framework

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