INTEGRATED REPORTING - THE FUTURE OF FINANCIAL REPORTING

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Abstract

From investors' point of view, financial results are not sufficient to offer an overview of a given business. To provide an overview on the activity of an entity, reports will need to include both the traditional financial and non-financial part to provide information on sustainable development, the impact of the activity on the environment, and social responsibility.

The main purpose of this article is to ascertain the current state of social responsibility concerns and integrated reporting entities, given the need for a more comprehensive reporting system, showing how the activity of large companies affects the public interest, environment and society.

Keywords: corporate social responsibility, integrated reporting.

JEL classification: M14, M41, O47

1. Introduction

Accounting information plays a critical role in our contemporary world. As part of economic data, accounting information has seen its share of progress, and the circuit of accounting data has been permanently brought up to date by changes taking place at a global level. As it follows, accounting information must adapt to capital markets throughout the world, thus turning the science of accounting into an "internationally spoken language" that all users can understand.

The development and adjustment of the accounting system used in our country, in keeping with the trends observed at a European and international level, are aimed at creating a shared framework for preparing and presenting accounting data, which would provide credible and relevant information for all users. This development of the national accounting system can significantly help improve accounting data in that which concerns the amount of information, with the aim of increasing the trust of both internal and foreign investors, as well as that of credit institutions and of the capital market

However, the actual performance of a given entity is established based not only on the financial data provided by the accounting records, but also on several qualitative elements (the quality of the resources used: technological, material, human) that play a decisive part in determining its size, therefore such elements must be taken into account when establishing the performance of said entity.

The effects of the global economic recession have raised questions about the reliability of financial reporting and have made it obvious that a more comprehensive reporting system is needed, one that can show how the activity carried out by large companies influences public interest, the environment, and society.

Integrated reporting means a new step of corporate reporting, given that, in order to provide a comprehensive picture of the activity carried out by a given corporation, this type of reporting will include both the traditional part – the financial data – and a non-financial part presenting information about sustainability and long-term development, as well as the impact of the activity on the environment, human capital and social responsibility.

At the moment, the corporate environment sees a dramatic increase of the moral requirements it is subjected to, due to the increase of the social influence of business units as a result of their growing economic force, which, in its turn, leads to the apparition of a certain set of moral obligations that said units must commit to. This is known as the social responsibility of entities, specifically corporate social responsibility (abbreviated, in that which follows, as CSR). Social responsibility entails disclosing both the positive and the negative impact of the company's operations on the work standards, on the environment, on economic development and human rights.

Several organizations [such as KPMG and ACCA] have conducted studies regarding reporting trends in the field of CSR, both at a European and at a national level, as well as regarding investors' expectations from corporate reporting. There are also articles providing an analysis of how important integrated reporting appears in the eyes of investors [Couldridge D., 2014, Shital Jhunjhunwala, 2014]. Several authors discuss and assess the provisions of the Integrated Reporting Framework drafted by the IIRC, while also analyzing the information that an integrated report must provide [Shital Jhunjhunwala, 2014, Graham Terry, 2014, Bunea Stefan, 2013].

2. Research methodology

In that which regards the research methodology, the research method of choice for this paper was that of document analysis, since analyzing bibliographic sources allowed for insight into the content of the subject chosen. This article is a piece of descriptive research, aimed at describing the current state of the concerns regarding integrated reporting, a type of reporting that is particularly important for the relationship between corporate governance elements and environment elements, respectively subjects dealing with the social and human capital. Such factors as economic globalization, the domination of multinational enterprises, and the development of the capital market have led to an increase in the demand for complex information capable of reflecting the commercial, social, and environmental context in which organizations operate. Throughout the research, the method chosen was that of qualitative analysis, the aim being that of establishing value judgments and summarizing the most important conclusions drawn from consulting specialized documentation.

3. Corporate Social Responsibility (CSR) – concept and trends

Although there is no clear and specific definition for the social performance of a given business unit, such performance may be equaled to the unit's concerns regarding various social aspects such as: encouraging ethical practices in its employment policy, contributing to the development of the community in which it carries out its activity, complying with the requirements of sustainable development, investing in social infrastructure, maintaining the environment as clean as possible, and so on and so forth.

The three pillars of sustainable development are as follows: economic, social and environmental development; in conjunction, they form the concept of sustainability. Assessing and following social performance is important because of the interaction between the three aspects of global performance [Pintea O. M, 2011]. According to empirical research conducted on the American market [quoted by Pintea O. M, 2011], it has been proven that a positive relationship exists between financial performance and the various aspects of social performance, in particular in that which concerns employees, customers, and the civil society. Thus, business units that stand out through an improved social performance can expect to obtain a sustainable financial performance.

At the moment we are witnessing an increase in the number of business units that are interested in this type of triple performance, which means they also aim to obtain a good environmental performance by mitigating the environmental impact of their operations through a series of environment protection measures and by advertising such performance to the public.

The efficiency of social and environmental commitment relative to the ultimate purpose of sustainable development translates into an increase of the company's value, consolidation of its reputation, improvement of its financial performance, and a reduction of the cost of capital [Bunea Stefan, 2013].

KPMG, which analyzed the trends in reporting, with regards to CSR, for companies included in G250, as well as for another 3,400 companies throughout the world, all of them national leaders in 34 countries and 15 industrial sectors, found that almost half of the G250 companies claimed an increase in their financial value following the initiatives taken with regards to CSR. Corporate responsibility has thus moved from a moral imperative to a critical business imperative.

Reporting social responsibility practices does not constitute a priority for the Romanian business environment. Most Romanian companies adopted social responsibility policies only when they went public at the Bucharest Stock Exchange, forced by its Corporate Governance Code. Such policies were also adopted by Romanian subsidiaries of foreign companies which, to a large extent, had already integrated social responsibility in their corporate culture and already had significant experience in reporting social responsibility practices.

However, a survey of the local market, conducted by KPMG in Romania and which analyzed the companies included in N100 at a national level based on their income in 2010, indicated a significant increase, up to 54% of the companies in N100 providing reports on social responsibility, as compared to a level of only 24% in 2008. This significant progress reflects an improvement of the awareness concerning the importance of reporting for non-financial information, as well as of the financial benefits that such voluntary reporting may produce for the reporting companies. A survey of the main reasons why Romanian companies choose to report CSR aspects found that brand reputation and economic benefits are chief among them, which serves to show the companies' significant concern with their image on the market and with the need to improve relationship with stakeholders, but also awareness of the financial benefits entailed by disclosing non-financial information.

Although the number of Romanian companies that have adopted social responsibility reporting is still low, this is expected to change in the near future because, since November 2014, Romania saw the coming into effect of the EU Directive 2014/95/EU that makes it compulsory for large companies (those with over 500 employees) to report on a yearly basis a series of aspects concerning their social and environmental performance.

However, the European Parliament and the Council of the European Union have not enforced a standard reporting format for such information.

Therefore, at the level of the European Union, about 6,000 companies will find themselves forced to disclose non-financial information. In Romania, companies with over 500 employees total about 720. In that which regards the costs incurred by companies for non-financial reporting, they have been estimated to reach some Euro 5,000 per year. However, the companies that fall in this category are allowed to choose the aspects to include in their reporting, as well as the reporting format. The companies may choose to include the information they consider relevant either in their yearly financial statement or in a separate CSR report. In the future, to make reporting easier, the Commission wishes to draft a set of reporting guidelines, based on the most frequently used international standards.

4. Integrated reporting

Given that financial reporting alone cannot provide all the information needed for decision-making, several international organizations are currently working together to create an international framework for integrated reporting, so as to best ensure a connection between financial and non-financial information.

The general framework for integrated reporting accepted at global level, drafted and implemented by the International Integrated Reporting Council (IIRC), completed in December 2013, provides an innovative impulse for corporate reporting.

The International Integrated Reporting Council, set up in 2009, is a powerful representative of corporate leaders, regulators, financial markets, academic environment, standardization bodies, accounting professionals and NGOs. The aim of this framework is to create an integrated conceptualization, to establish the Guiding Principles and the Elements that regulate the general content of an integrated reporting system, as well as to explain the fundamental concepts that the system is based on.

"The integrated report is a brief communication on how the strategy, governance, results, and prospects of an organization, in the context of its external environment, lead to the creation of value on a short, medium and long term". [General Framework for Integrated Reporting, International Integrated Reporting Council].

The General Framework for Integrated Reporting is based on the concept that the value a company creates depends on how said company uses its capital, as well as on how it interacts with the external environment. The company's activities and results lead to an increase, a decrease, or a transformation of the capital. Value is created for the entity when value is created for other stakeholders [Shital Jhunjhunwala, 2014].

The benefits of integrated reporting are summarized by Philippe Peuch-Lestrade, Deputy CEO of the International Integrated Reporting Council, who shows that financial information is critical, but not sufficient, and that integrated reporting proposes a change of focus on the true forces behind the development of a business activity. Another benefit stands in the fact that, beyond the integrating concept, it becomes possible to provide a more clear explanation of what the financial market calls the "value of intangibles". Integrated reporting is a strong supporter of the "less is more" concept, which means the company must have a complete and holistic vision of its business activity, but also be able to present it as briefly and succinctly as possible, to make it easy to read and comprehend.

An integrated report explains how an organization creates value over time. But it's not the organization alone that creates value; it is also influenced by the external environment, through the company's relationships with the stakeholders and depending on various resources. Therefore an integrated report attempts to provide insights with regards to the following:

- the external environment that affects the organization;
- the resources and relationships used and affected by the organization, which are also known as capitals and are classified as financial, manufactured, intellectual, human, social, as well as relational capital and natural capital;
- how the organization interacts with the external environment and the capitals in order to create value in the short, medium, and long term.

Integrated reporting means an opportunity to present to investors and other stakeholders the organization's longer-term prospects, as well as the motivation and explanation of its vision, of the organization's strategies and results, thus contributing to decision making with regards to resource allocation in view of creating value in the long term, in particular for limited and non-renewable resources.

A survey conducted by the ACCA (Association of Chartered Certified Accountants), which was aimed at discovering the changes that took place in the investment environment after the global economic recession, inquiring about what investors expect from corporate reporting and how the companies, through their chief financial officers, respond to the ever changing needs of the investors, found that investors want more transparency from the companies and an integrated reporting system that should include both financial results and business decisions; however, companies are still reluctant to adopt integrated reporting. Thus, 93% claim to be in favor of companies adopting integrated reporting. From the investors' point of view, yearly financial results, or even quarterly financial results, are no longer sufficient to provide an overall picture of a given business unit.

What investors want is to understand how the company will generate sustainable value within the environment in which it carries out its operations:

* What is the chosen business model?
* What are the risks and opportunities?
* What is the governance system?

Investors who place their money in a company's capitals have limited rights – the right to vote, the right to sit in the General Meeting of Shareholders, and the right to receive dividends, if such is the case. Given that the investments are geared towards an uncertain future, it is important for the investors to make an assessment as accurate as possible and to understand the company's governance system [Couldridge D., 2014].

At the same time, the ACCA survey shows that, while open to the concept of integrated reporting, finance professionals are still reluctant to become pioneers of this model. However, most of them claimed that they were planning to adopt integrated reporting in the near future, whereas only 10% said they were not interested in adopting this model, which also provides investors with non-financial information, because of the risks entailed: high costs, the risk of prematurely disclosing key information to the competition, and the risk of influencing the quality of the reporting process because of the need to speed up the reporting.

The survey indicates that most of the respondents are aware of how providing complete and transparent information improves the company's relationships with the investors. Some 40% of those surveyed are either planning to or have already taken steps towards adopting integrated reporting, a type of reporting that takes into account information available from various departments and attempts to provide a complete image of the company's performance.

Among the benefits of integrated reporting, the respondents mentioned the following:

• the competitive advantage entailed by the image of sustainable company that provides a complete and transparent reporting of its activity;

• the ability for an improved management of both opportunities and risks;

• the possibility of accurately identifying the factors that lead to a successful performance;

• improving relationships with the investors.

5. Conclusions

Integrated reporting is the answer to the ever increasing demands of those investors who are looking for a more profound insight into the company's vision, by bringing together both financial and non-financial information and combining internal and external reporting, all of which, ultimately, translate into improved efficiency, transparency and consistency.

Observing results only from a financial point of view is no longer sufficient, which applies not only to external corporate reporting, but also to how organizations are governed. Also, an important role in the future reporting system will be assigned to accounting professionals and auditors, which is why the accounting profession will have to undergo the progress required by this new concept.

We believe that integrated reporting will add to the measures taken in recent years in view of ensuring comparability for the information produced and disclosed by corporations and multi-national companies, and will help with making decisions regarding the allotment of resources so as to create value in the long term, in particular in that which concerns limited and non-renewable resources, thus supporting sustainable development.

On the other hand, we agree with some authors [Graham T., 2014] who believe that integrated reporting is a very new concept and it will be many years before it reaches its maturity. The integrated frame of mind is even newer and will require quite some time before it is fully understood, but the organizations that are already using it are creating a significant competitive advantage for themselves.

ACKNOWLEDGMENT

This paper has been financially supported within the project entitled ***"Horizon 2020 - Doctoral and Postdoctoral Studies: Promoting the National Interest through Excellence, Competitiveness and Responsibility in the Field of Romanian Fundamental and Applied Scientific Research",*** contract number POSDRU/159/1.5/S/140106. This project is co-financed by European Social Fund through Sectoral Operational Programme for Human Resources Development 2007-2013. **Investing in people!**

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