

Redefining Corporate
Accountability through

Integrated Reporting

What happens when values and
value creation meet?

By Cristiano Busco, Mark L. Frigo, Paolo Quattrone, and Angelo Riccaboni

The landscape of corporate reporting is about to change considerably. The concepts, principles, and elements that characterize the way organizations report their annual performances are currently being questioned, debated, and redesigned throughout the world. This is happening as key elements such as capital employed, value creation, and accountability are redefined in practice. What are the types of capital that an organization uses and affects? In what ways is value created and distributed over time? To whom are organizations accountable? A possible answer to these critical questions is offered by Integrated Reporting (IR), a process that results in communicating—through an annual integrated report—value creation over time.

Background

In April 2013, the International Integrated Reporting Council (IIRC), a global coalition of regulators, investors, companies, standards setters, the accounting profession, and nongovernmental organizations (NGOs), released a Consultation Draft (CD) of the first Integrated Reporting Framework. The CD was developed based on an analysis of the responses to the 2011 Discussion Paper “Towards Integrated Reporting—Communicating Value in the 21st Century,” the publication of a draft outline in July 2012, and a Prototype Framework in November 2012. The CD focuses on how to create an integrated report and what to include in it.

An integrated report offers a concise, stand-alone communication about how an organization’s strategy, governance, performance, and prospects lead to the creation of value over the short, medium, and long term. In this article, we introduce the fundamental concepts, guiding principles, and content elements of IR. To illustrate these, we use the experience of Eni, a large multinational company in the oil and gas industry that has been participating in the IIRC’s IR Pilot Program to develop the Framework. Finally, as we reflect on the possible challenges ahead for the Integrated Reporting Framework, we speculate on the implications for management accountants of a wide adoption of IR’s concepts, principles, and elements. What could the role of management accountants be as values meet value creation?

Redefining Corporate Reporting as Values Meet Value Creation

In the aftermath of the recent financial crisis and corporate scandals, many people increasingly perceive the global economic system as busted, and they view business as one of the major causes of social, environmental, and economic problems. Issues such as huge national and individual debts, large unemployment rates, growing disparity across societies, persistent fraud and unethical behavior in managing public and private organizations, and increasing concerns for the environment have left large segments of contemporary society frustrated with the existing social and economic order, particularly with the logic, principles, and practices currently in place. Among others, the notion and functioning of capitalism, the ultimate purpose of the business, as well as personal and collective *values* systems and the concept of corporate value creation, have been questioned and placed under the spotlight.

In this context, the pressure on the private sector to

consider the social, environmental, and economic impact of its conduct has grown tremendously as corporate leaders and entrepreneurs are urged to take the lead in bringing business and society back together. Values (broadly defined as principles, beliefs, standards, and ideals that shape our feelings and emotions and help us decide how to act) help to shape perceptions of how value is created, distributed, and reported. Societal perceptions of value also help shape individual perceptions of value. Therefore, it isn’t surprising to see a number of entrepreneurs, corporate leaders, and organizations moving toward the hybrid ideal where the *values* embraced (economic, social, and environmental) influence and are influenced by the way in which *value* creation and distribution are accounted for and communicated within a company’s annual report.

This makes the values embraced and the value created fundamental concepts around which contemporary corporate reporting can be routed. Unfortunately, however, the logic, principles, and practices of corporate reporting currently in place have been transforming annual reports in complex, compliance-driven documents that mainly are useful for accounting experts only. Much of the information included in current corporate reports isn’t designed to offer forward-looking information about strategy, performance, and risk. There’s an increasing sense among stakeholders—investors, customers, citizens, and the community—that existing corporate reporting, which is characterized by a strong focus on financial performance and a lack of information about corporate strategy and nonfinancial performance, is becoming increasingly less fit for the purpose. Businesses are facing capital constraint from a broader range of resources than just finance. This needs to be accounted for, and communicated to, an expanding series of stakeholders who are eager to be informed about both values embraced and the value created.

Closing the Gap

To close this gap, over the last decade a large number of companies have voluntarily offered reports focused on sustainability and on corporate social responsibility. Also, a number of coalitions (such as the IIRC), councils, and NGOs focused on improving and broadening the contents of corporate reporting have emerged. Here we focus on Integrated Reporting as an example of contemporary managerial innovation where a number of initiatives, organizations, and individuals began to converge in response to the need for a consistent, collaborative, and

An integrated report is a concise communication about how an organization'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.

internationally accepted approach to redesigning corporate reporting.

Integrated Reporting: Principles, Concepts, and Elements

Integrated Reporting is a process that results in communicating—through the annual *integrated report*—value creation over time. On August 2, 2010, The Prince's Accounting for Sustainability Project (A4S) and the Global Reporting Initiative (GRI) announced the formation of the IIRC. The IIRC's mission is "to create a globally accepted integrated reporting framework which brings together financial, environmental, social and governance information in a clear, concise, consistent and comparable format" in order to "help business to take more sustainable decisions and enable investors and other stakeholders to understand how an organization is really performing." (For more information about the IIRC and Integrated Reporting, visit www.theiirc.org.)

According to the Consultation Draft, an integrated report is a concise communication about how an organization'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. Although providers of financial capital are the primary intended IR users, an integrated report should be designed to benefit all stakeholders—including employees, customers, suppliers, business partners, local communities, regulators, and policy makers—interested in an organization's ability to create value over time. The key objective of IR is to enhance accountability and stewardship with respect to the broad base of six kinds of capital, or "capitals" (financial, manufactured, intellectual, human, social and relationship, and natural), and pro-

mote understanding of their interdependencies. In doing this, the aim of IR is to support integrated thinking, decision making, and actions that focus on sustainable value creation for stakeholders. (The CD refers to "capitals" instead of "capital," so we continue that use here.)

The International IR Framework is being developed to assist organizations with the IR process. In particular, the purpose of the Framework is to establish fundamental concepts, guiding principles, and content elements that govern the overall content of an integrated report. This will help organizations determine how best to express their unique value-creation story in a meaningful and transparent way. Significantly, the IR Framework doesn't intend to set benchmarks for such things as the quality of an organization's strategy or the level of its performance. The intended report users will do these assessments based on the information in an organization's integrated report.

IR Principles

Because its intention is to offer an appropriate balance between flexibility and prescription, the IR Framework is principles based rather than being founded on a more rigid, rules-based approach. The idea is to recognize the wide variation in individual circumstances of different organizations yet, at the same time, to enable a sufficient degree of comparability across organizations to meet relevant information needs. For this reason, the IR Framework doesn't focus on rules for measurement, disclosure of individual matters, or even the identification of specific key performance indicators. Rather, the Framework is driven by integrated thinking, which, as illustrated in the CD, should lead to integrated decision making and execution toward the creation of value. The purpose of this approach is to stimulate the active consideration by

organizations of the relationships between their various operating and functional units and the kinds of capital that they use and have an effect on. Through the integrated thinking promoted by the IR Framework, organizations are stimulated to focus on the connectivity and interdependencies among a range of factors that have a material effect on their ability to create value over time (see “Principles of Integrated Reporting”).

PRINCIPLES OF INTEGRATED REPORTING

- **Strategic focus and future orientation:** An integrated report should provide insight into the organization’s strategy and how that strategy relates to the organization’s ability to create value in the short, medium, and long term and its use of and effects on its capitals.
- **Connectivity of information:** An integrated report should show, as 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.
- **Stakeholder responsiveness:** An integrated report should provide insight into the quality of the organization’s relationships with its key stakeholders and how and to what extent the organization understands, takes into account, and responds to their legitimate needs, interests, and expectations.
- **Materiality and conciseness:** An integrated report should provide concise information that is material to assessing the organization’s ability to create value in 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 and without material error.
- **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 value-creation story.

(Source: “Consultation Draft of the International Integrated Reporting Framework,” the International Integrated Reporting Council, April 2013, p. 6.)

IR Concepts

The fundamental concepts of IR are represented by (1) the six capitals that an organization uses and affects, (2) the organization’s business model, and (3) the creation of value over time. The business model is the vehicle through which an organization creates value. (See the IIRC report “Business Model—Background Paper for IR,” March 2013, for more.) That value is embodied in the capitals that the organization uses and affects. The assessment of an organization’s ability to create value in the short, medium, and long term depends on an understanding of the connectivity between its business model and a wide range of internal and external factors. These factors represent the elements disclosed in the integrated report.

IR Elements

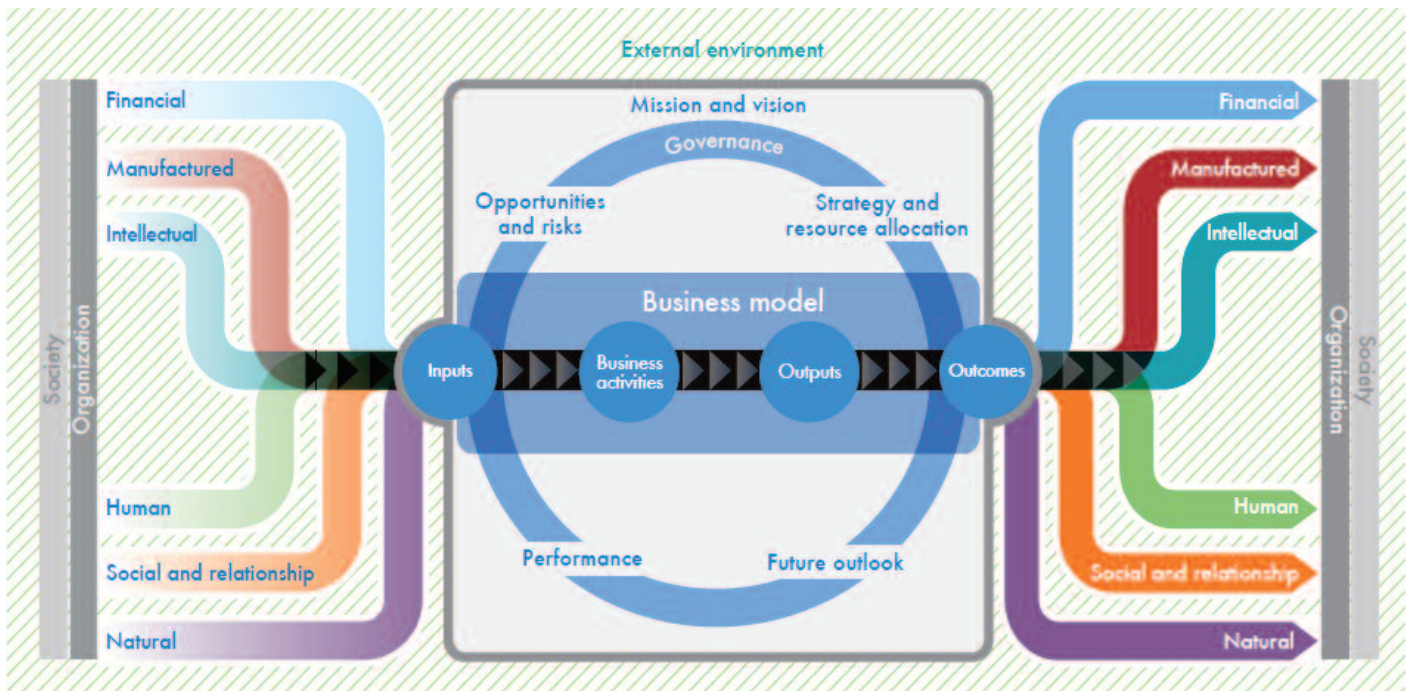
An integrated report is built around seven elements that define its content and communicate the organization’s unique value-creation story: organizational overview and external environment, governance, opportunities and risks, strategy and resource allocation, business model, performance, and future outlook (see “Elements of Integrated Reporting”). By linking content across these elements, an integrated report can 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 provides a foundation from which to discuss the performance, prospects, and governance of the business in a way that focuses on its most important aspects.

As emphasized by Brad Monterio in “Integrated Reporting and the Potential Role of XBRL” (*Strategic Finance*, June 2013), the IIRC recognizes that value isn’t created by or within an organization alone. Rather, as the CD explains, it’s *influenced* by the external environment (e.g., economic conditions, technological change, societal issues, environmental challenges), *created* through relationships with others, and *dependent* on the availability, affordability, quality, and management of various resources. Along this line, a representation included in the CD illustrates how a company interacts with its external environment and uses and affects the group of capitals to create value (see Figure 1, which summarizes the key concepts and the elements of Integrated Reporting). The CD clarifies that companies aren’t required to adopt this categorization of the capitals, which are shown in this way as a benchmark to help ensure that companies

Figure 1: Integrated Reporting:

The interaction between its fundamental concepts and content elements

(Source: "Consultation Draft of the International Integrated Reporting Framework," the International Integrated Reporting Council, April 2013, p. 11.)



don't overlook any of them.

According to the IIRC, the IR Framework leads to a broader explanation of performance than more traditional corporate reporting by describing, and measuring where feasible, the material elements of value creation and the relationships between them. In particular, the capitals are stores of value that become *inputs* to a company's business model. They can be increased, decreased, or transformed through the activities and *outputs* of the organization. It's also important to understand how the outputs affect *outcomes*, which represent the ultimate results of the outputs.

Integrated Reporting at Eni

Eni is a major energy company that's active in more than 90 countries, has approximately 78,000 employees, and has sales in excess of €127 billion. It maintains a strong position in the oil and gas value chain, from the upstream hydrocarbon exploration phase to the down-

ELEMENTS OF INTEGRATED REPORTING

An integrated report should answer the following questions:

- **Organizational overview and external environment:** What does the organization do, and what are the circumstances under which it operates?
- **Governance:** How does the organization's governance structure support its ability to create value in the short, medium, and long term?
- **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?
- **Strategy and resource allocation:** Where does the organization want to go, and how does it intend to get there?
- **Business model:** What is the organization's business model, and to what extent is it resilient?
- **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 its future performance?

(Source: "Consultation Draft of the International Integrated Reporting Framework," the International Integrated Reporting Council, April 2013, p. 7.)

stream product marketing. (For additional information about Eni, visit www.eni.com.) For Eni, being sustainable in the energy business means creating value for stakeholders and using resources in such a way as to avoid compromising the needs of future generations. In 2010, after publishing the fourth edition of its annual Sustainability Report, Eni began a process leading to the preparation of an integrated report according to the recommendations of the IIRC and the standards in GRI's 2006 "Sustainability Reporting Guidelines, version 3.0." In 2011, Eni was included in IIRC's Pilot Program for this.

Approved by its board of directors in May 2013, Eni's annual report for 2012 is an integrated report prepared in accordance with principles included in the prototype of

The added value represents the wealth the company generated in carrying out its activities. To reinforce this message, Eni says that being sustainable in the energy business means creating value for stakeholders.

the International IR Framework (www.eni.com/en_IT/sustainability/sustainability.shtml). It represents financial and sustainability performance, underlining the existing connections between competitive environment, group strategy, business model, integrated risk management, and the corporate governance system. Interestingly, right after the letter to the shareholders, the report opens with a summary of Eni's business model, which is arguably the fundamental content of any integrated report.

While illustrating and disclosing its business model in the 2012 integrated report, Eni says that the company's market position and competitive advantages derive from its strategic decision-making process, which is consistent with the long-term nature of the business and relies on a sustainable model founded on a consolidated and distinctive way of doing business in a framework of clear and straightforward rules of corporate governance and respectful of the highest ethical standards and rigorous risk management (see p. 12 of the 2012 Eni Integrated

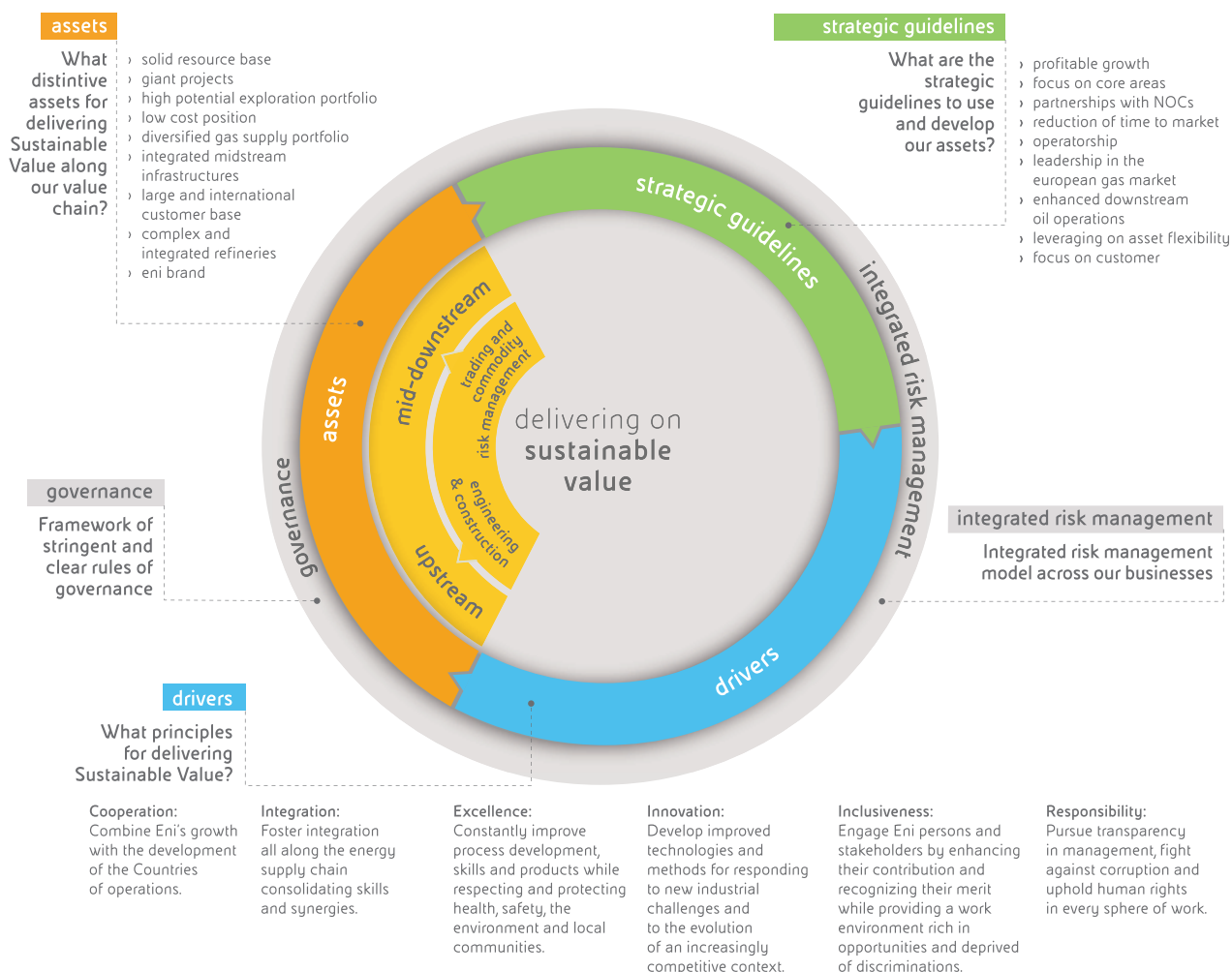
Annual Report). In 2012, this business model enabled Eni to lay the foundation for a new growth phase of its oil and gas production, one in which, according to the report, Eni promises to outperform the industry over the medium and long term. In the meantime, Eni communicates that it has started the reorganization of the downstream activities to manage the current European downturn. In the Chemical segment, for example, Eni suggests that it has progressed at repositioning the business to deliver sustainable results. The decision to produce an integrated report and open it with a discussion of the company's business model enabled Eni to note that the strategies, the decisions in terms of resource allocation, and day-by-day operations underpin sustainable value creation not only to shareholders but, more generally, to all its stakeholders.

The illustration of the internal business model is followed by an analysis of the external competitive environment. In particular, the integrated report identifies a number of industrial challenges and describes the actions and initiatives that Eni implemented during the year to face those challenges, the performance for the year, and the performance outlook at the end of the 2013-2016 business plan (pp. 14-15 of the report). For example, one of the most important challenges was the increasing competitive and regulatory pressure in the European energy market. The actions Eni implemented in 2012 were directed toward renegotiating long-term gas supply contracts in Europe, strengthening its position in the gas and liquefied natural gas (LNG) market outside Italy, relaunching efficiency programs at European industrial sites, selecting new initiatives in green refinery and biochemistry, and retaining and strengthening the customer base.

Next, Eni's integrated report continues by illustrating the strategy for the 2013-2016 four-year period, highlighting the priorities of profitably growing oil and gas production; recovering profitability in the downstream gas sector; improving efficiency in downstream oil, chemicals, and general services supporting business activities; and retaining global leadership in engineering and construction by focusing on the most technologically advanced and innovative segments. The IR suggests that, following some divestments, Eni has a more flexible financial structure and a business model more focused on upstream activities. The integrated report then offers additional details on the strategy at divisional levels across the oil and gas value chain: exploration and production, gas and power, refining and marketing, chemical, and engineering and construction (pp. 16-19 of the report).

Figure 2: Eni Business Model

(Source: Eni 2012 Integrated Report, p. 12)



The added value represents the wealth the company generated in carrying out its activities. To reinforce this message, Eni says that being sustainable in the energy business means creating value for stakeholders. The configuration Eni chose for its integrated report is that of overall added value net of amortization and depreciation. Net overall added value is divided among employees (direct remuneration consisting of wages, salaries, and provisions for termination benefits and indirect remuneration consisting of social welfare contributions); the Public Administration (income taxes); financial backers (medium-/long-term interest paid for availability of borrowed capital); shareholders (dividends distributed); and the company (quota of reinvested earnings). The net added value distributed in 2012 was €22,475 million and was divided as follows: 52% to the State and Public Administrations through taxes on the income of Italian

and overseas businesses, 22% to human resources, 18% to shareholders, 4% to the company system, and 4% to financial backers (p. 236 of the report).

Eni's Business Model

Within Eni, the creation of sustainable value is pursued through a business model focused on strategic assets and drivers distributed along the entire value chain, governed by good governance, by continual interaction with all the reference stakeholders, and by a way of working made up of six distinctive elements applied in all operating contexts. The combination of these six elements—integration, cooperation, innovation, excellence, inclusion, and responsibility—guides investment decisions and enables the company to achieve its strategic objectives. Eni's business model is shown in Figure 2.

The business model is governed by a system of rules

regulating all processes within the Eni Group. Eni's organizational model envisages that the sustainability unit will carry out coordination, guidance, and reporting duties and manage relations with stakeholders and the community. By analyzing the international scenario, stakeholders' needs, commitments made, and the company's performance, Eni defines sustainability priority targets and improvement areas, which are set forth in the multiannual strategic plan.

Eni's strategic plan incorporates the company's priority sustainability targets and develops them into concrete projects. Implementation of the projects relating to the priority targets is supported by economic incentives. Each sustainability target is pursued with projects and initiatives defined by the divisions and companies that Eni controls and is included in specific short-/medium-term action plans. To manage its impacts in a responsible and systematic manner, Eni has put in place a sustainability reporting system that regularly assesses the progress of projects and targets and the results achieved. The set of indicators is updated annually on the basis of analyses regarding: (1) significant aspects for sustainability in the energy industry; (2) the main international standards, sector guidelines, and sustainability indexes; and (3) common practices and best practices used by main competitors in the field of sustainability communication (pp. 227-254 of the report).

Eni's second year in the IIRC Pilot Program was 2012. In line with the "Prototype of the International Framework" that the Council published in November 2012, Eni has continued integrating financial and sustainability information, showing the relationship between elements of the scenario and competitive context, performance, and strategic direction within the Operating Review and Financial Review sections of the integrated report. Significantly, the final section of the report, Consolidated Sustainability Statements, contains the key performance indicators that, by summarizing the business model and the value-creation process of the company, will be monitored annually.

The Role of Management Accountants and the Challenges Ahead for IR

What is the role of management accountants regarding Integrated Reporting? In June 2013, IMA® (Institute of Management Accountants) sent a response letter to the IIRC about the Framework CD, saying "management accountants are not 'just technical accountants'—they are broad-based business thinkers who serve as trusted advisors inside organizations. Management accountants are

'at the table' on all issues involving strategy and sustainable value creation." For these reasons, concepts and content such as capitals, business models, future outlook, risks, and financial and nonfinancial key performance indicators, to name a few, call for the active participation and engagement of management accountants within IR.

In 2011, with a response letter to the IIRC paper "Towards Integrated Reporting: Communication Value in the 21st Century," IMA welcomed the development of the IR Framework as "an opportunity to modernize corporate reporting and corporate culture, unlock data from corporate silos and restrictive presentation formats, link operational, environmental, social and governance practices to financial performance, and make information relevant, meaningful and reliable for management and all stakeholders." Yet although the IR Framework represents a major development in the area of disclosures to better inform investors and other stakeholders as to the sustainable value-creation capacity and capability of the enterprise, the design of corporate reports where the values embraced are blended with the process of value creation still presents a number of challenges.

As highlighted within the IMA response letter to the CD, there are several issues and concerns that deserve further consideration in the development of the IR Framework. Among others, the compelling market need for a single integrated report from investors and other market stakeholders, as well as the cost/benefit of the process, aren't described or articulated in the CD. Second, in light of the increasingly complex, turbulent, and competitive global marketplace we are currently experiencing, it's questionable whether investors and other market stakeholders would want management teams to disclose (potentially) competitively sensitive information about their sustainable business model. Third (and this is really important), there's a real danger, especially in the early stages of IR development, that overregulation will stifle innovation, learning, and growth. Mandatory reporting standards for IR could hamper the development of the framework and, most importantly, could be inadequate. Are regulators really in the best position to determine the best metrics to measure and disclose sustainable value creation in contemporary, highly diversified global markets? The journey toward IR has just begun.

What role can management accountants play as values meet with value creation within new forms of corporate reporting? The demands placed on management accountants have grown significantly in recognition of social and environmental challenges. These demands require a rich

supply of information that's capable of informing corporate managers of the impacts of their decisions and enabling them to act. For these reasons, the linkages across the principles, concepts, and elements of IR call for management accountants to master their knowledge regarding the organization's business model to identify and leverage the key drivers of business value. We believe that, through their expertise, management accountants (at all levels) have the opportunity to actively integrate the operational, environmental, social, and governance aspects in place in their organizations with the financial performance of their organizations. But rather than simply prescribing specific indicators or measurement methods to be used in the annual report, management accountants can lead the process of communication and reporting by designing innovative documents that can capture the interest and attention of diverse stakeholders. We mean innovative reports where values and capitals integrate with strategy and business models to generate and distribute added

value in the short, medium, and long term. The innovation, learning, and growth needed in the continuing development of IR can benefit greatly from the active participation of management accountants. **SF**

Cristiano Busco, Ph.D., is established professor and chair of accounting at the School of Business and Economics of the National University of Ireland in Galway. Previously, he has held positions at Babson College, the Manchester Business School (U.K.), University of Southern California, and the University of Siena, Italy. You can reach Cristiano at cristiano.busco@nuigalway.ie.

Mark L. Frigo, CMA, CPA, Ph.D., is director of the Center for Strategy, Execution and Valuation and the Strategic Risk Management Lab in the Kellstadt Graduate School of Business and Ledger & Quill Foundation Distinguished Professor of Strategy and Leadership in the Driehaus College of Business at DePaul University in Chicago, Ill. He also is an advisor to executive teams and boards in the area of strategy development, innovation strategy, and strategic risk management. You can reach Mark at (312) 362-8784 or mfrigo@depaul.edu.

Paolo Quattrone, Ph.D., is professor and chair of accounting, governance, and social innovation at the University of Edinburgh Business School. Before joining Edinburgh, he was professor of accounting and management control at IE Business School, Madrid; reader in accounting at the Saïd Business School; and official student (i.e., fellow) of Christ Church at the University of Oxford. You can reach Paolo at Paolo.Quattrone@ed.ac.uk.

Angelo Riccaboni, Ph.D., is the rector of the University of Siena and professor of management control systems. He was visiting scholar at USC (Los Angeles), INSEAD, LSE, University of Wales at Bangor (U.K.), Columbia Business School, and DePaul University. Angelo is a member of the Leadership Council of the UN Sustainable Development Solutions Network and chair of Med Solutions, the UN SDSN Regional Center for the Mediterranean. You can reach Angelo at angelo.riccaboni@unisi.it.

Note: This article is a preview of an upcoming book *Integrated Reporting—Reflections on the Concepts, Principles, Elements and Case Studies that Are Redefining Corporate Accountability*, edited by Cristiano Busco, Mark L. Frigo, Paolo Quattrone, and Angelo Riccaboni. The book is published by Springer and will be available this fall.

Further Reading

Julie Battilana, Matthew Lee, John Walker, and Cheryl Dorsey, "In Search of the Hybrid Ideal," *Stanford Social Innovation Review*, Summer 2012, pp. 51-55.

Robert G. Eccles and Daniela Saltzman, "Achieving Sustainability Through Integrated Reporting," *Stanford Social Innovation Review*, Summer 2011, pp. 56-61.

Robert G. Eccles and Michael P. Krzus, *One Report: Integrated Reporting for a Sustainable Strategy*, John Wiley & Sons, Hoboken, N.J., 2010, pp. 146-156.

International Integrated Reporting Council, *Consultation Draft of the International Integrated Reporting Framework*, April 2013.

John Mackey, Rajendra S. Sisodia, and Bill George, *Conscious Capitalism: Liberating the Heroic Spirit of Business*, Harvard Business Review Press, 2013.

Nikos Mourkogiannis, *Purpose – The Starting Point of Great Companies*, Palgrave Macmillan, 2006.

Michael E. Porter and Mark R. Kramer, "Creating Shared Value: How to Reinvent Capitalism and Unleash a Wave of Innovation and Growth," *Harvard Business Review*, January/February 2011, pp. 62-77.