Integrated Reporting for a Good Corporate Governance

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Abstract

Corporate governance has been developed due to financial crisis, climate change and globalization. Corporate governance plays an important role in order to restore trust in business and to rebuild relationships with investors and other stakeholders. In parallel with this trend, integrated reporting also has become common. The integrated reporting is a new form of corporate reporting aims to provide a holistic picture of an organization's performance.

The origin of integrated reporting lies in corporate governance, as a solution to demands on corporate leadership regarding the sustainability, strategy, performance and risks.

This help a company to reporting how its governance structure supports the organization's ability to create the value in the short, medium and long term and the integrated report can be used as a corporate governance tool. The aim of this discussion paper is to describe these new concepts and also, relationship between these.

Key words: corporate reporting, integrated reporting corporate governance
J.E.L. Classification: M40, M41

1. Introduction

Corporate governance, integrated reporting, corporate reporting and responsibility are terms that have increased significantly in importance over the last decades in the world of business. This increased attention has been motivated by the financial crisis, the increased incidence of environmental disasters and accounting scandals. Corporate governance is a term frequently used by researchers, practitioners, the media and the general public focusing on control mechanisms as answer to these changes.

Against this background, stakeholders, investors and regulators has changed requirements for corporate reporting. As a result, the business reporting has become similarly complex. All information needs from investors and other key stakeholders are continuously changing. The value of a company reaches beyond the historical financial aspects. Business partners, managers, investors and other stakeholders nowadays have an increasing need for full picture of company health in order to have a clear understanding of company's global performance and make the better decision.

Based on this, companies are being forced to reporting their financial information and non-financial information to stakeholders, as clear, concise and transparent as possible. Also, corporate reporting has been changed, it must included additional matters in order to give investors or other stakeholders the critical information they need to value their investments.

Because traditional financial reporting cannot provide full picture of corporate, elements such as corporate social responsibility, information on environmental, carbon emissions, health and labor rights, must be included in reporting on total business performance. This is the moment when integrated reporting comes into play.

First of all, integrated reporting describe the company's global performance based on connectivity between financial and non-financial information, governance and remuneration, environmental and social matters and other relevant 'business-impacting' factors. Secondly, integrating reporting means is based on integrated thinking and follows the strategy and targets set by companies.

The purpose of this article is to describe integrated reporting and corporate governance as well as identifying mutual relationships between. The article presents the author's considerations regarding the corporate governance as element of integrated reporting based on literature review and using the deduction method. In order to follow this purpose, we examined the content and structure of the published annual reports of the top 20 companies listed on BSE. The reports examined are related to years 2012 – 2014.

2. Literature review

The financial crisis, followed by recent corporate scandals around the world due to fraud and insufficient systems of control have one common feature - the credibility of corporations and failing corporate governance. All these events contributed to an increase in focus on corporate reporting and corporate governance. The need of practices of corporate governance arises due to conflicts between two categories of interests: the interests of managers and the interests of shareholders. This is due to the separation of management and ownership control in the company. Corporate governance is an internal rule which is framed to safeguard the values of corporate shareholders' interests. Corporate governance knows many definitions. O'Donovan defines the corporate governance: "an internal system that includes processes, policies and people that serve the requirements of shareholders as well as other stakeholders by controlling and directing activities by the firm's management with good business objectivity, savvy and integrity". (O'Donovan, 2003).

The Organization for Economic Cooperation and Development (OECD) Principles of Corporate Governance, referred to in the EU Commission's Action Plan on Company Law and Corporate Governance defines the corporate governance as "a set of relationships between a company's management, its board, its shareholders and other stakeholders". (OECD, 2004:11)

According to Enquist et al., corporate governance defines important issues that integrate social, environmental values and company's business operations. (Enquist et al., 2006)

As improving corporate governance is the European Commission adoption by the European Parliament of the Directive on disclosure of non-financial and diversity information by large companies and groups officially titled Directive 2014/95/EU. According this, the companies will need to disclose information on policies, risks and results as regards environmental matters, social and other aspects regarding the employee, anti-corruption, respect for human rights and bribery issues, and diversity on boards of directors.

A critical part of good governance is good reporting. Parallel of this trend, the concept of integrated reporting has become more complex and common. The recent change of corporate reporting, integrated reporting, is driving at a global level by the IIRC (International Integrated Reporting Committee).

International Integrated Reporting Committee-global coalition of companies, investors, regulators, standard setters, accounting and finance professionals and NGOs aims to build consensus between businesses, investors, authorities, governments and accounting bodies on the future shape of corporate reporting practice.

According to IIRC, integrated reporting describe the non-financial information about organization's strategy, performance, governance and prospects in a way that reflects the social, commercial and environmental context within which it operates. It provides a clear and concise picture of how an organization creates value, now and in the future. (IIRC, 2011)

For long term vision, corporate reporting must be based on integrated thinking which is part of integrated report will sustain good corporate governance. Integrated thinking will take into account the interdependencies and connectivity between all factors that affect an organization's ability to create value in the future based on your strategy, your reporting business model and risks and opportunities it faces. Integrated reporting is defined by the IIRC, "a process founded on integrated thinking that results in a periodic integrated report by an organization about value creation over time and related communications regarding aspects of value creation". (IIRC 2013a, p.4).

According to The King Report on Governance for South Africa 2009 (King III), integrated reporting is "a holistic and integrated representation of the company's performance in terms of both its finance and its sustainability". (IIRC 2011, p. 3)

3. Corporate governance as part of integrated report

Because that many companies, stakeholders and governments have already recognized the importance of governance information, social, environmental as part of annual report, a new model for reporting is needed. This is the integrated report that can providing a full picture of performance, structured around the business model, governance and organization's strategic objectives including the financial information and non-financial information. According to IIRC, integrated report is: "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". (IIRC, 2011)

In other words, integrated report is an important document by which the organization communicates current position (business model, performance), where it's going (future outlook) and how it intends to get there (strategy). It tells us the organization's value creation story in understandable way. So, the integrated report tell to stakeholders the business model, activities, the strategy, risks and opportunities, the ability to create and maintain value in the short, medium and long term. The IIRC not prescribed the structure of integrated report. It suggested the most important elements and guiding principles referring to information which is interconnected. Based on this, the elements defined by the IIRC are:

- "Organizational overview and business model: What does the organization do and how does it create and sustain value in the short, medium and long term?
- Operating context, including risks and opportunities: What are the circumstances under which the organization operates, including the key resources and relationships on which it depends and the key risks and opportunities that it faces?
- Strategic objectives and strategies to achieve those objectives: Where does the organization want to go and how is it going to get there?
- Governance and remuneration: What is the organization's governance structure, how does governance support the strategic objectives of the organization and how does it relate to the organization's approach to remuneration?
- Performance: How has the organization performed with respect to its strategic objectives and related strategies?
- Future outlook: What opportunities, challenges and uncertainties is the organization likely to encounter in achieving its strategic objectives and what are the resulting implications for its strategies and future performance?" (IIRC, 2011)

So, given the above, one most important content element of according to IIRC (International Integrated Reporting Committee) and to International Integrated Reporting Framework focuses on governance as a solution to demands on corporate leadership to ensure adequate focus on strategy, risk, performance and sustainability.

4. Relationship between corporate governance and integrated reporting

The companies need to create sustainable values in addition to the financial gain they already create for themselves, their shareholders, and the society and also to present non-financial information to their stakeholders.

Corporate governance as part of integrated reports has been developed in order to rebuild the trust the stakeholders and to create a feeling of trust that the interest of manager is in line with the interest of owners.

Generally accepted the most important principles of corporate governance are:

- transparency
- fairness
- responsibility
- accountability

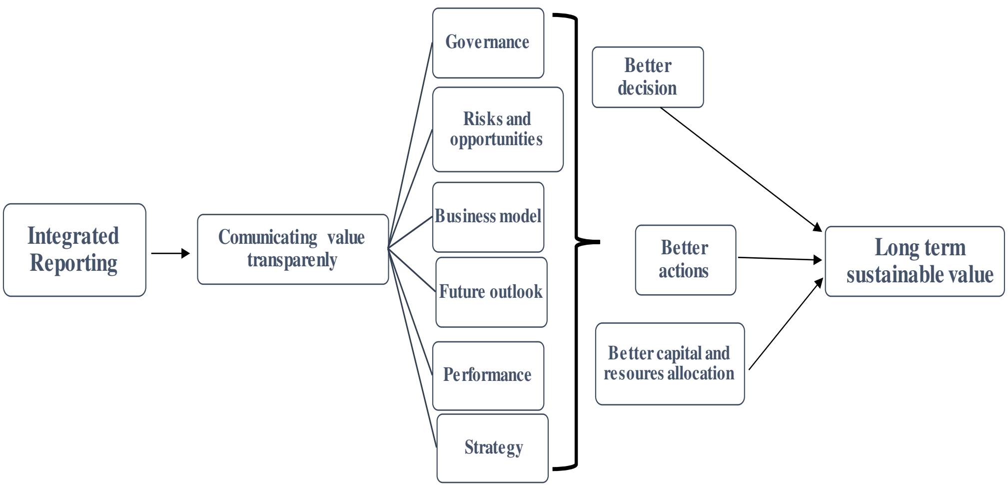
Accountability is a principle that emphasizes the business responsibility on the impact on the environment. Transparency refers to reporting these effects from the external environment to the non-business stakeholders.

According to IIRC, the guiding principles are:

- “Strategic focus
- Connectivity of information
- Future orientation
- Responsiveness and stakeholder inclusiveness
- Conciseness, reliability and materiality” (IIRC, 2011)

The research methodology used for this paper in order to describe the relationship integrated reporting and corporate governance is empirical analysis of the structure and content of the published reports by the top 20 companies listed on Bucharest Stock Exchange (BVB), period 2012-2014. The annual reports are available on the website of the companies studied. In order to collect the information regarding the integrated reporting and corporate governance we used the observation method. We classified the 20 companies studied in four categories, as follows: 6 companies in the sector "Food & drink", 7 companies the "Textiles & clothing", 3 companies in the "electricity electronics" and 4 companies in the" transport equipment". To this effect, we studied the manner in which companies listed on BVB embrace the integrated reporting and how can this help the companies for good corporate governance. The results of our analysis describe that the information provided in annual reports or administrator reports of the Top 20 companies listed on BVB (Bucharest Stock Exchange), additional to financial statements even it is mainly non-financial and strategic information regarding to environment, human resource, governance, good governance. From this study it can be concluded that governance disclosures are increasing in annual report meaning that the majority the studied companies mention the different aspects presented in the <IR> framework’s content element governance. Based on this and based on literature review analysis of company reporting development we can present the relationship between integrated reporting and corporate governance, presented in figure 1:

Figure 1.Integrated reporting for good governance



Source: Author’s compilation

Firstly, integrated reporting is based on integrated thinking and promotes emphasis on internal processes for understand the needs and interests of different investors/stakeholders. The companies which use the integrated report for reporting are better able to communicate the company’s global performance. Secondly, the connectivity of financial information and non-financial information, including those looking towards the future, embedded in integrated reporting can enhance corporate governance. Because the focus on connectivity is part of integrated reporting, it will help for better decisions, better actions and better capital and resource allocation by those in order to create and sustain long term sustainable value. Thirdly, integrated reporting can help to identify opportunities and risks for the organization and, more importantly, how these are addressed rather than merely articulating them. Such an approach facilitates better risk management. So, given the above, integrated reporting describe the information better aligned with investor needs for better decision and actions, for better capital and resources allocation. Above all, integrated reporting is a good toll for better corporate governance.

5. Conclusions

Corporate reporting has been changed due to the evolution of the stakeholders’ information needs. Today, the interest of investors, employees, non-government organizations, local communities and customer increasingly turn to shareholders and company’s management asking if its governance structures meet the expectations of society and if its business model take in consideration environmental and social dimensions of its activities. Due to those changes, the integrated reporting has been developed. The integrated reporting brings together company’s global performance, governance, strategy, and future outlook that will help to the creation of value over the short, medium and long term.

The literature review and empirical research regarding trends in corporate governance describe the advantages as being the reduced information asymmetry and capital cost and the gained legitimacy. We believe that integrated reporting can help corporate governance through enhanced accountability, clear performance management, greater transparency and effective leadership and more effective risk management. Also, for better decision-making which takes into account long-term as well as shorter-term outcomes.

6. References

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