LEADING PRACTICES IN

Integrated Reporting

Management accountants will guide their companies on the journey to value creation.

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

Integrated Reporting (IR) is making the leap from promising concept to powerful practice. Released at the end of 2013 by the International Integrated Reporting Council (IIRC), a global coalition of regulators, investors, companies, standards setters, the accounting profession, and nongovernmental organizations (NGOs), the IR Framework has been robustly tested and piloted in 25 countries. As we described in the article “Redefining Corporate Accountability through Integrated Reporting” (Strategic Finance, August 2013) and in our book Integrated Reporting: Concepts and Cases that Redefine Corporate Accountability (Springer, 2013), the Framework was co-created with business and investors and provides an “open” platform for IR to move toward the mainstream. To shed light on the way in which IR is currently being adopted and reflect on the possible opportunities ahead for management accountants and finance professionals, we will explore some leading examples of integrated reporting at Lawson, Inc.; Eni; and SAP.
In Search of Competitiveness and Sustainable Growth

Competitiveness and sustainable growth are fundamental goals that contemporary organizations and societies are urged to achieve in the short, medium, and long term. The recent financial crisis and the growing disparities across societies have led many analysts and observers to describe the global economic system as busted and to lump business and finance among potential causes of social, environmental, and economic problems. Can businesses and societies succeed in striking a balance between the need for competitiveness and sustainable growth? How can value be defined, managed, and measured over time? From what and for whom do businesses create or destroy value?

These issues recently have fueled the macroeconomic and political debate across the globe with a significant demand for a move beyond Gross Domestic Product (GDP) measures. Some people maintain that GDP ignores social costs, environmental impacts, and income inequality. Therefore, the world needs a better understanding of what sustainable well-being means, how to measure it, and how to achieve it. This movement is gaining momentum in public opinion and is well aligned with the call for civil society and business organizations to cooperate globally to achieve the United Nations Sustainable Development Goals: a set of objectives, which are to be released in 2015, for fighting poverty, promoting sustainable development, and improving global well-being.

A paradigm shift is required if businesses intend to contribute toward a more sustainable society. This change calls for the introduction of an innovative perspective of integrated management that’s able to combine multiple dimensions of analysis and sustain—in practice—the ongoing search for competitiveness.

The combination of Integrated Thinking and Integrated Reporting seems to offer a pragmatic solution to the existing concerns and outstanding needs. Integrated Thinking marks a change in the way in which companies envisage, design, and run their business. In parallel, IR provides an opportunity to understand and question the business holistically: looking beyond the financial representation to include an overview of strategies, operations, risks and opportunities, future outlook, governance, and more. The need for such an innovative and integrated vista seems to offer an interesting opportunity to management accountants and finance professionals, who are called on to leverage their existing skills and acquire new ones as the adoption of Integrated Thinking and Integrated Reporting continues over time. Next, before focusing on some of the leading practices in IR, we offer a snapshot of the IR Framework released by the IIRC (see www.theiirc.org for more).

The IIRC Integrated Reporting Framework

Integrated Reporting results in a periodic, concise integrated report about how an organization’s strategy, governance, performance, and prospects—in the context of its external environment—lead to the creation of value in the short, medium, and long term (visit www.theiirc.org/international-ir-framework). Although providers of financial capital are the primary intended 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 tangible and intangible capitals and promote understanding of their interdependencies.

In December 2013, the IIRC released the first version of its IR Framework to be used as guidance for voluntary adoption of IR. This Framework is currently inspiring a large number of companies across the globe (Microsoft, PepsiCo, Southwest Airlines, Unilever, Danone, Eni, Coca-Cola, Volvo, BASF, HSBC, Natura, SAP, and Repsol, to name a few) as they pioneer the adoption of IR across different industries and regions (see p. 25 for the current list of pilot companies). The IR Framework was designed to offer a balance between flexibility and prescription. It provides the fundamental concepts, guiding principles, and content elements that should be featured in an integrated report. Ultimately, the IR Framework represents an “open space” to be filled in a meaningful and reliable way to communicate the unique value-creation story of the company.

Representing Value Creation as Capitals Engages with the Company Business Model

The fundamental concepts of IR are represented by the capitals that an organization uses and affects, as well as the process of creating value over time. That value is embodied in the capitals—sometimes also referred to as resources and relationships. (The IR Framework refers to “capitals” instead of “capital,” so we continue that use here.) The assessment of an organization’s ability to create value depends on an understanding of the connec-
Companies that Have Piloted the IR Framework

**BASIC MATERIALS**
- AkzoNobel NV, Netherlands
- AngloGold Ashanti, South Africa
- BASF SE, Germany
- Cliffs Natural Resources, United States of America
- Gold Fields, South Africa
- MASISA SA, Chile
- Solvay, Belgium
- Teck Resources, Canada

**CONSUMER GOODS**
- The Clorox Company, United States of America
- The Coca-Cola Company, United States of America
- Danone, France
- Industria de Diseño Textil SA (Inditex), Spain
- Marks and Spencer Group plc, United Kingdom
- Natura, Brazil
- Sainsbury’s, United Kingdom
- Showa Denki Co. Ltd., Japan
- Unilever, United Kingdom
- BRF S.A, Brazil
- PepsiCo, United States of America

**CONSUMER SERVICES**
- Edelman, United States of America
- Meliá Hotels International, Spain
- New Zealand Post, New Zealand
- Slater & Gordon Lawyers, Australia

**FINANCIALS**
- Achmea (formerly Eureko), Netherlands
- AEGON NV, Netherlands
- Association of Chartered Certified Accountants, United Kingdom
- bankmecu Limited, Australia
- BBVA, Spain
- BNDES, Brazil
- The Chartered Institute of Management Accountants, United Kingdom
- CNDCEC, Italy
- The Crown Estate, United Kingdom
- DBS Bank, Singapore
- Deloitte LLP, United Kingdom
- Deloitte Netherlands, Netherlands
- Deutsche Bank, Germany
- Deutsche Börse Group, Germany
- Ernst & Young Nederland LLP, Netherlands
- Ernst & Young ShinNihon LLC, Japan
- Generali Group, Italy
- Grant Thornton UK LLP, United Kingdom
- Grupo Segurador Banco Do Brasil E Mapfre, Brazil
- HSBC Holdings plc, United Kingdom
- Itaú Unibanco, Brazil
- Jones Lang LaSalle, United States of America
- KPMG International, Switzerland
- National Australia Bank Limited, Australia
- PricewaterhouseCoopers Advisory, Italy
- PriceWaterhouseCoopers N.V., Netherlands
- Prudential Financial, Inc., United States of America
- Stockland, Australia
- Strate, South Africa
- Uralsib, Russian Federation
- Vancity, Canada
- CPA Australia, Australia
- Garanti Bank, Turkey
- FMO, Netherlands
- Singapore Accountancy Commission, Singapore

**HEALTH CARE**
- NHS London, United Kingdom
- Novo Nordisk, Denmark
- Takeda Pharmaceutical Company Limited, Japan
- Sanofi, France

**INDUSTRIALS**
- AB Volvo – Volvo Group, Sweden
- Atlanticia SpA, Italy
- BAM Group, Netherlands
- CCR SA, Brazil
- Diesel & Motor Engineering PLC, Sri Lanka
- Flughafen München GmbH, Germany
- Freund Corporation, Japan
- Interserve Plc, United Kingdom
- Kirloskar Brothers Limited, India
- NV Luchthaven Schiphol, Netherlands

**OIL & GAS**
- eni SpA, Italy
- NIAEP, Russian Federation
- Petrobras SA, Brazil
- Repsol SA, Spain
- ROSATOM, Russian Federation
- Rosneft, Russian Federation
- Sasol, South Africa
- SNAM SpA, Italy

**TECHNOLOGY**
- ARM Holdings plc, United Kingdom
- Indra, Spain
- Microsoft Corporation, United States of America
- SAP, Germany

**TELECOMMUNICATIONS**
- SK Telecom, South Korea
- Telefónica SA, Spain
- Vivendi, France

**UTILITIES**
- AES Brazil, Brazil
- CLP Holdings Limited, China
- CPFL Energia, Brazil
- ENAGAS SA, Spain
- EnBW Energie Baden-Württemberg AG, Germany
- Enel SpA, Italy
- Eskom Holdings SOC Limited, South Africa
- Terna SpA, Italy
tivity between a wide range of internal and external factors in its business model. (See Figure 1 for an overview of the value-creation process as presented in the IIRC IR Framework.)

As illustrated in the IR Framework, organizations depend on six different types of capitals, which are stores of value that, in one form or another, become inputs to an organization’s business model. They are: financial, manufactured, intellectual, human, social and relationship, and natural. The IR Framework doesn’t require organizations to adopt them, so they should be used as a benchmark to ensure an organization doesn’t overlook a capital that it uses or affects.

Value is created or destroyed through the capitals within a company’s business model, which represents the chosen system of inputs, business activities, outputs, and outcomes that aims to create value over the short, medium, and long term. Since these capitals and their value change over time as they are 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 (see Figure 1).

The Ingredients of IR: Content Elements and Guiding Principles
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, risks and opportunities, strategy and resource allocation, business model, performance, and future outlook (see Figure 1). By linking content across these elements, an integrated report illustrates the value-creation story from a basic description of the business model through the external factors affecting the business, including 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.

Because the intention is to offer an appropriate balance between flexibility and prescription, the IR Framework is principles based rather than rules based. The idea is to recognize the wide variation in individual circumstances of different organizations yet enable a sufficient degree of comparability across organizations to meet the relevant information needs. For this reason, the IR Framework
doesn’t focus on rules for measurement, disclosure of individual matters, or even on the identification of specific key performance indicators (KPIs). Rather, the Framework is driven by Integrated Thinking, which will lead to integrated decision making and execution toward the creation of value. The rationale 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, business 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.

Next, to illustrate and discuss some of the key features of Integrated Reporting, we’ll draw on leading examples from Lawson, Inc.; Eni; and SAP.

**Lawson, Inc.: Connecting Business and Society**

Lawson, Inc. is a convenience-store franchise chain based in Japan. The store originated in the United States in Cuyahoga Falls, Ohio, but today it’s a Japanese company and is the second-largest convenience-store chain in the country behind 7-Eleven. In 2013, Lawson, Inc. produced its first integrated report that combines its previous Annual Report and Corporate Citizenship Report to incorporate financial and nonfinancial information in one volume. Lawson’s “Integrated Report 2013” (http://lawson.jp/en/ir/library/pdf/annual_report/ar_2013_e.pdf) opens by identifying the key stakeholders of the company. Among them are local communities, which Lawson places at the center of the corporate philosophy, business model, and action plan. The one-page message from the CEO further emphasizes this by highlighting how the company strives to create value and to respond to the dynamically diversified needs of the local communities while existing in harmony with society.

From the start, the report illustrates how the company’s business model is tied to possible solutions to the social and environmental challenges of the local communities. For example, **key challenges** in the local communities include issues arising from changes in society, such as gender balance, an aging population, few jobs for young people, escalation of national medical costs, and increase in lifestyle-related diseases. Global environmental changes include power shortages, climate change, increasing waste, and long-term depletion of natural resources. Both

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**Figure 2: Lawson, Inc. Capitals and Business Model**
the local and global issues are connected to the multiple actions that Lawson, Inc. has implemented as part of its mission to realize a sustainable business growth in harmony with society and the environment. The response to these challenges characterizes the company’s business model and approach to value creation (see Figure 2).

Figure 2 represents Lawson, Inc.’s “Corporate Value Creation Cycle.” This representation, which mirrors the IIRC Framework in Figure 1, builds on the capitals as inputs and outcomes of the cycle. Both “visible” and “invisible” capitals are included. According to Lawson, Inc., “Visible capital is goods and money depicted in financial statements. Invisible capital is what is not shown, such as human capital.” The “Integrated Report 2013” offers a powerful view of the company’s business model and capitals.

Eni, the Italian energy giant, has moved one step further by identifying the stocks of capitals, how they have been used within the company’s business model, and their impact on the company and its stakeholders. Eni’s innovative approach is presented next.

**Eni: Mediating across Capitals and Stakeholders**

Eni is the sixth-largest integrated energy company in the world by market value, is active in 90 countries, and has approximately 78,000 employees. Its net sales from operations are €127 billion. The company boasts a strong position in the oil-and-gas value chain from the hydrocarbon exploration phase to product marketing. In 2010, after having issued a series of environmental and sustainability reports, Eni realized that, although the numbers were allowing a true and fair review of the company’s performance, operations, and management, they weren’t necessarily relevant to the stakeholders or able to hint at the sustainability of the business. Also not relevant per se was the simple act of reporting data. What was missing was a broader process of analysis and communication that was able to put performance in context and to represent the strategic leverages the company was using to build and maintain its ability to produce value in the long term. For this reason, Eni began the process of integration in corporate reporting.

At Eni, sustainability isn’t a specific area of activity, instead, it represents a business approach and is a lever to support long-term value creation while managing political, operational, and financial risks. This approach has been embedded in the company’s culture since its foundation when Enrico Mattei, Eni’s first chairman, pioneered a way to become more competitive by managing relations between international oil companies and producing countries based on long-term cooperation, on the transfer of knowledge and skills, and on mutual development. Eni adopts Integrated Thinking that starts from planning and integrated risk management. Business opportunities are defined by taking into account the multiple capitals that could be leveraged by the operations, and risks are evaluated considering all possible impacts that could be generated.

Within this context, Eni’s “Annual Report 2013” is an integrated report that innovates in terms of contents by highlighting the different capitals, resources, and relationships that are part of the company’s value-creation process. The main capitals Eni uses (financial, manufacture, intellectual, natural, human, social and relationship) are classified in line with the indications offered in the IIRC Framework (see Figure 3). They represent the stocks and their value, which is increased or transformed through Eni’s activities. Each capital is associated with the main actions that will create value for the company and all stakeholders.

For example, for the natural capital, stocks include oil and gas reserves, water, biodiversity and ecosystems, air, and soil (see Figure 3). Eni’s main actions related to this capital include investments in new businesses, such as biorefinery and green chemistry; investment in technological and process upgrades; and remediation activities. Among the results for Eni are growth of hydrocarbon reserves, reduction in operational expenses, mitigation of operational risk, license to operate, and stakeholders’ recognition. Regarding the impact on external stakeholders, the report highlights the reduction of gas flares, reduction of oil spills and blowout, preservation of biodiversity, containment of water consumption, and energy efficiency.

From the upstream operations to marketing activities, Eni’s “Annual Report 2013” (www.eni.com/en_IT/attachments/publications/reports/reports-2013/Annual-Report-2013.pdf) attempts to make the connections that exist between integrated activities and business strategies.
Figure 3: Eni’s Main Capitals
(Source: Eni “Annual Report 2013,” p. 5)

<table>
<thead>
<tr>
<th>stock of capital</th>
<th>Eni’s main actions</th>
<th>value creation for Eni</th>
<th>value creation for Eni’s stakeholders</th>
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<tr>
<td>• Financial structure</td>
<td>• Cash flow from operations</td>
<td>• Going concern</td>
<td>• Yields</td>
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<td>• Liquidity reserves</td>
<td>• Bank loans</td>
<td>• Lower cost of capital</td>
<td>• Share price appreciation</td>
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<td>• Bonds</td>
<td>• Reduction of working capital</td>
<td>• Social and economical growth</td>
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<td>• Maintaining strategic liquidity</td>
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<td>• Hedging</td>
<td>• M&amp;A opportunities</td>
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<td>• Dividends</td>
<td>• Mitigation of market volatility</td>
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<td>• Onshore and offshore plants</td>
<td>• Technological upgrade</td>
<td>• Returns</td>
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<td>• Pipelines and storage plants</td>
<td>• Process upgrade</td>
<td>• Enlarging asset portfolio</td>
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<td>• Liquification plants</td>
<td>• Investment in new businesses</td>
<td>• Increase assets value</td>
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<td>• Refineries</td>
<td>• (bio-refinery, Green chemistry, car sharing)</td>
<td>• Reduction of operational risk</td>
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<td>• Distribution networks</td>
<td>• Maintenance and development activities</td>
<td>• Energy and operational efficiency</td>
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<td>• Power plants</td>
<td>• Increase environment certifications (ISO 14001, ISO 50001, EMAS, etc.)</td>
<td>• Reputation</td>
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<td>• Chemical plants</td>
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<td>• Availability of energy sources and green products</td>
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<td>• Buildings and other equipment</td>
<td>• Competitive advantage</td>
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<td>• Partnership with centres of excellence</td>
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<td>• Development of proprietary technologies and patents</td>
<td>• Performance</td>
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<td>• Application of procedures and systems</td>
<td>• Licence to operate</td>
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<td>• Technologies and intellectual property</td>
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<td>• Corporate internal procedures</td>
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<td>• Corporate governance system</td>
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<td>• Integrated risk management</td>
<td>• Development of proprietary technologies and patents</td>
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<td>• Management and control systems</td>
<td>• Application of procedures and systems</td>
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<td>• Knowledge management</td>
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<td>• ICT (Green Data Center)</td>
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<td>• Health and safety of people</td>
<td>• Safety at work</td>
<td>• Performance</td>
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<td>• Know-how and skills</td>
<td>• Recruiting, education and training on the job</td>
<td>• Efficiency</td>
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<td>• Experience</td>
<td>• Promotion of human rights</td>
<td>• Competitiveness</td>
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<td>• Engagement</td>
<td>• Eni’s people engagement</td>
<td>• Innovation</td>
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<td>• Diversity (gender, seniority, geographical)</td>
<td>• Knowledge management</td>
<td>• Risk mitigation</td>
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<td>• Eni’s thinking</td>
<td>• Welfare</td>
<td>• Reputation</td>
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<td>• Leveraging on diversity</td>
<td>• Talent attraction</td>
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<td>• Enhancing individual talents and remuneration in accordance to a merit system</td>
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more evident. In particular, the report identifies a certain number of KPIs that capture the financial performance and sustainability performance as well as the results of the use of different forms of capitals (see Figure 4).

Eni’s goal is to continue refining its Integrated Thinking and Integrated Reporting by capturing and highlighting the connections among the multiple capitals. This should lead to a better understanding of the impact of the heterogeneous sustainability drivers on the business objectives and financial results. This is something that is featured in the SAP integrated report.

**SAP: Connecting the Dots**

SAP is a German multinational software corporation that produces enterprise resource planning (ERP) applications to manage operations and customer relations. This year, for the second time, SAP has published an integrated report by linking contents from its traditional Annual Report and Sustainability Report into one cohesive document ([www.sapintegratedreport.com/2013/en](http://www.sapintegratedreport.com/2013/en)). One of the key attributes of the SAP “Integrated Report 2013” is the attention drawn to the connections between financial and nonfinancial performance of the business. The purpose of the report is to illustrate the features of SAP integrated strategy by offering a holistic picture of all possible impacts. Notably, SAP’s four global corporate goals (objectives) reflect this balanced view: Two focus on the company financial performance (revenue and margin) and two on nonfinancial performance (customer loyalty and employee engagement).

The inclusion of a wider set of economic, social, and environmental measures is essential, but it isn’t sufficient. Exploring the interdependencies is often the key. Actions taken in one area affect another area, and these connections hold the potential for the company to increase value creation by responding more effectively to the business landscape of today and tomorrow. For these reasons, the SAP “Integrated Report 2013” explores the cause-and-effect relationships between the financial and nonfinancial indicators. In doing so, IR represents a platform for connecting the dots across the company’s business model and offers a space to explore the company’s ability to create value over time.

In particular, the report presents a map of the specific activities SAP has undertaken to first change employee behavior, subsequently impact company performance, and finally influence financial results. Describing such a chain is part of a strategy that should lead to assessing the consequences of nonfinancial performance in financial terms. To create and validate these chains of cause and effect, SAP turned to internal and external stakeholders. It started with those inside SAP, meeting in small groups that examined the cascade of impacts from activities related to each of the nonfinancial indicators. Next it engaged external stakeholders, including academics, financial investors, and peers, to evaluate the key findings.

SAP’s goal is to estimate the impact of the nonfinancial drivers of the business on corporate objectives and financial results. Understanding integrated cause-and-effect chains within the process of value creation that characterizes the SAP business model helps the company manage processes and activities in a more effective way and, most importantly, build awareness of the heterogeneous capitals, resources, and relation-
ships used and affected. Although this attempt is still in progress, the search for connectivity and quantification is already providing tangible results. Earlier in 2014, while seeking to design calculations with deeper cause-and-effect links behind them, SAP introduced two new non-financial performance indicators related to innovation and productivity.

The example presented in Figure 5 refers to the SAP Business Health Culture Index (BHCI). This index assesses the health of SAP employees and the health of the SAP organizational culture, which the company says are interrelated. The chain in Figure 5 starts with activities that support health at SAP, from flexible work arrangements to leadership development to global health and innovation awareness weeks. Each of these strengthens SAP organizational culture and helps employees manage stress, achieve work/life balance, feel empowered in their roles, and perform at their best. Moving from left to right, the diagram shows the impact of these activities. Flexibility, for example, enhances stress resilience and work/life balance, which leads to greater employee engagement. Supported by specific analysis, the report suggests that a company culture with engaged employees enhances SAP employer ranking, helping the company attract top talent, which spurs innovation and ultimately boosts revenues. In parallel, leadership development leads to a stronger work culture, which increases productivity as well as employee retention, resulting in a higher operating margin.

Figure 5: Integrated Cause-and-Effect Value Chain for the BHCI at SAP
(Source: SAP “Integrated Report 2013”)

Figure 6: Strategy and Business Model—Integrated Performance Analysis for the BHCI
(see www.sapintegratedreport.com/2013/index.php?id=354&L=1)
The “Integrated Report 2013” offers readers and users the opportunity to learn about and question SAP works in progress with Integrated Reporting. By visiting www.sapintegratedreport.com/2013/index.php?id=354&L=1, you can learn about SAP key performance indicators and see the connections among them. The report offers readers the opportunity to explore the chains that enable intangibles to become tangible. When you click on one of the boxes, arrows appear and point to other boxes that are their connections (see Figure 6 regarding the Business Health Culture Index). This way, users have the potential to learn and challenge the assumptions underpinning the links among the KPIs and corporate objectives (boxes with an asterisk in Figure 6 are corporate objectives). Significantly, the website calls for participation: “What do we know about the relations between our financial and nonfinancial indicators? Challenging ourselves to go beyond our assumptions, we looked into the connections and came up with the illustration below. We know that we do not have all the answers yet, so we invite your feedback as we continue to work on improving our performance.”

Opportunities for Management Accountants within IR

The journey of Integrated Thinking and Integrated Reporting starts at the core of any organization: its business model. Resources, activities, output, and outcomes represent the foundation of any business. Strategy formulation, action planning, governance, and risk management put the company’s model for value creation in motion. As seen from the examples of Lawson, Inc.; Eni; and SAP, the need to master the connections across the multiple drivers of the value chain puts management accountants at the forefront of value creation. No one knows the business model better than management accountants because they have a holistic and unique perspective of a company’s strengths and weaknesses. For these reasons, they will find themselves at the heart of the drive to Integrated Reporting, leveraging their Integrated Thinking. Accountants and controllers need to be prepared for that drive—they need to be ready and equipped to take advantage of the opportunities to lead that will definitely flourish in this space.

Once more, Integrated Reporting is making the leap from promising concept to powerful practice throughout the world. Add on Integrated Thinking, and management accountants have the opportunity to lead these new practices, acting as designers and leaders of a space where companies are continuously searching for a pragmatic balance between competitiveness and sustainable growth in practice. They can be designers because Integrated Thinking and Integrated Reporting represent an open platform that requires imagining and understanding the business model rather than rigid compliance with standards. They can also act as leaders because this process needs direction since it requires mediating the connections and trade-offs between the different drivers of value creation. These opportunities are available, and it’s up to management accountants and finance professionals to take advantage of them.

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