A Vision for Integrated Thinking and the Role of Finance Professionals

Integrated thinking is the critical foundation of integrated reporting. Without it, the ultimate objective of sustainable organisations, markets, and societies cannot be achieved. The chicken and egg analogy can be applied to integrated thinking and integrated reporting: while reporting can lead to a journey of greater transparency and, hopefully, behaviour change within an organisation, leadership on integrated thinking is the key to unlock a change of mindset and purpose. The International Federation of Accountants (IFAC) has published Creating Value with Integrated Thinking: The Role of Professional Accountants to highlight the important role accountants play in integrated thinking.

Integrated thinking and reporting provides a means and additional incentive for CFOs, and their finance teams, to focus on the information and decisions that matter to the organisation and its potential success. For finance teams that have begun to shift toward business partnership within their organisation, the principles and concepts of integrated thinking and reporting are a natural progression on their journey.

Stathis Gould

(The author is Head of Professional Accountants in Business and Integrated Reporting, IFAC)
Comments can be sent to eboard@icai.in

The IFAC publication *Creating Value with Integrated Thinking: The Role of Professional Accountants* sets out a vision and framework for integrated thinking and explores what professional accountants working in the public and private sectors can do in practical terms to facilitate it in their organisation, regardless of whether their organisation is planning to publish an integrated report. The report identifies five key elements, which, if implemented, can lead to more effective

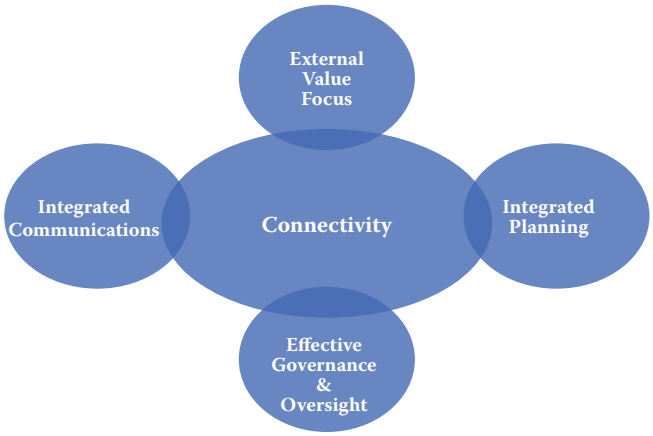
organisations and ultimately provide the basis for shifting from today's financially oriented reporting to integrated reporting.

The benefits of integrated thinking are already having an impact. *Realizing the Benefits: The Impact of Integrated Reporting,* published by the International Integrated Reporting Council (IIRC) and Black Sun, provides evidence of the nature of the benefits of integrated thinking. The IIRC's Pilot Programme, which ran for three years, yielded a great deal of research from participating organisations. This research and first-hand experience shows that many organisations captured the benefits of integrated thinking, including a range of strategic and operational benefits. Results from the Programme include, for example:

- 71% of participants experienced strategic benefits, the most important being a change in conversations between the board and management;
- 79% reported improvements in management information and decision making; and
- 96% experienced a positive impact from connecting departments and broadening perspectives.

Integrated thinking is also addressed in Mervyn King and Leigh Robert's *Integrate: Doing Business in the 21st Century,* which usefully provides a clear purpose to integrated thinking.

- Financial and nonfinancial performance are no longer separated, and the entire organisation accepts that one affects the other.
- The organisation's strategy is shared by all functions and divisions.
- Decision making is carried out with a longer-term view on value creation.



The IFAC's thought paper explains that integrated thinking is sparked by a connected approach. Connectivity supports the other four key areas of integrated thinking: an external value focus, integrated planning, effective governance and oversight, and integrated communications. An external focus is a critical starting point for identifying and articulating how value is created and destroyed. As a finance professional, it will be difficult to add value to this process without a broader connection to, and understanding of, the industry, business environment, and stakeholder perceptions.

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External Focus

An external focus is a critical starting point for identifying and articulating how value is created and destroyed. Identifying and understanding relevant matters for decision-making involves bringing together information and analysis from various sources, including trends in the business environment and market; understanding the impact their products and services have on society and on markets; understanding what impacts the organisation's reputation and public perception; and the overall customer experience.

As a finance professional, it will be difficult to add value to this process without a broader connection to, and understanding of, the industry, business environment, and stakeholder perceptions. This awareness and understanding is the basis of facilitating an understanding and assessment of the relevant drivers of value.

Integrated planning

Integrated planning—that is, the insights gained from an external value focus form the basis of integrated planning—should incorporate a comprehensive process of identifying and managing significant matters affecting value creation over the short, medium, and long term. Integrating relevant and material matters throughout the planning and management process involves an integrated approach to risk management, budgeting, and performance

management. The integrated planning process ensures that the necessary information and analysis is presented in a manner that allows managers at all levels to use it to make effective decisions. Furthermore, this level of integration encourages all parts of an organisation to have a common view of what is important and the measures of success.

Effective governance and oversight

Effective governance and oversight leads to credibility among stakeholders in the data, information, and insights provided. Appropriate governance and oversight structures ensure effective processes and accountabilities for all organisational initiatives and, ultimately, lead to better performance. For example, the importance and credibility of non-financial data, or data that has not previously been subjected to the oversight of the board and its audit committee can lack robustness and credibility. CFOs and their finance functions can begin to educate and train other parts of organisations about how to ensure their non-financial data achieves the same quality and credibility as financial data.

Integrated Communications

To achieve integrated communications, the organisation needs to communicate effectively on the full range of issues impacting value creation across the six capitals underpinning the value creation model in the *International <IR> Framework*. This is a new perspective for many organisations, and the shift from a financial focus requires communication by leadership in ways that significantly influence the organisation's behaviour, and that flow naturally from an integrated planning approach.

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The thought paper reflects integrated thinking as we understand it today, given that this is a period of experimentation for many organisations.

Integrated Reporting and Climate Change: A Perfect Marriage

The climate risk tsunami is still out in the ocean but the timing and force of its landfall is uncertain. Attention from investors is increasing as they do more to understand climate risk, and increasingly flex their muscles to help ensure fossil fuel companies respond. Part of the climate risk problem is rooted in the age-old challenge of transparency—transparency over the potential risk and opportunity of climate change and, in the case of fossil fuel companies, the risk that fossil fuel reserves might cease to be considered as assets in the future.

As should be the case in a market system, investors are getting active. Some ExxonMobil investors recently proposed a resolution to publish an annual assessment of long-term portfolio impacts of public climate change policies. And other investors across industries and sectors are taking similar actions.

This is a transparency problem that integrated reporting is designed to fix. An integrated report is largely forward looking, and linked to strategy and business models. It ultimately demonstrates how a company is creating value over time.

Unfortunately, the Association of Chartered Certified Accountants' *Filling the Information Black Hole: How Are Fossil Fuel Companies Reporting on the Stranded Asset Risk?* found that integrated reporting has not appeared to result in greater disclosure in relation to carbon related "stranded assets". The ACCA research covered 11 fossil fuel companies for the 2014 reporting season.

Given that the International Integrating Reporting Framework was only released in December 2013, the ability of integrated reporting to have already influenced the way these companies report on stranded assets and related matters is limited. This is not to say that these companies are not disclosing any information on the risks and opportunities of climate change. The problem is that often these disclosures are not delivered in the context of the organisation's strategy, governance, performance, and prospects. Integrated reporting should lead

to material disclosures on climate risks—ones that affect the organisation's ability to create value in the short, medium, or long term.

This reporting problem is down to a lack of transparency, and where there is disclosure it is *ad hoc* and fragmented and not clearly linked to the business model reality of the company. Consequently, climate related disclosure comes across as specious to some investors and stakeholders.

Integrated reporting responds to the challenge of transparency and inaccessible reporting. Where climate risks are linked to trends and issues in the external environment, and to the strategy and business model of the company, stakeholders can make their own judgment call on how well they think climate risk and opportunity is being dealt with.

The position of the fossil fuel companies seems to be based on a premise that energy demand will continue increasing and fossil fuels, particularly gas and oil, will be needed to support global economic growth, at least in the medium term. This transition phase is seeing many of the largest fossil fuel companies investing in energy efficiency and solutions based on new technology. The energy demand from society is arguably not the fault of the fossil fuel companies. The point is that integrated reporting, if done well and based on integrated thinking, will greatly help influence the allocation of market capital and credit.

Integrated reporting's premise is that it requires integrated thinking, which leads to better decisions not just better reporting. Integrated reporting arose out of concerns about corporate behaviour, sustainable development, and the resilience of organisations. Integrated thinking involves a changed mindset, purpose, and multi-capital approach. Ultimately, mainstream investors and others will be looking at a company's capacity for integrated thinking.

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A country should be defended not by arms, but by ethical behaviour. - Vinoba Bhave