

Corporate and Integrated Reporting: A Functional Perspective

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Abstract

In this paper, we present the two primary functions of corporate reporting (information and transformation) and why currently isolated financial and sustainability reporting are not likely to effectively perform these functions. We describe the concept of integrated reporting and why integrated reporting could be a superior mechanism to perform these functions. Moreover, we discuss, through a series of case studies, what constitutes an effective integrated report (Coca-Cola Hellenic Bottling Company) and the role of regulation in integrated reporting (Anglo-American).

Keywords: corporate reporting, integrated reporting, information, investing, sustainability, accounting

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1. The Functions of Corporate Reporting

Capitalist economies, where the means of production are controlled by private owners rather than by the State, are characterized by a large number of market transactions. These market transactions provide price signals, a central feature of the capitalist system. However, for individuals and organizations to participate in the economy they need decision-useful information. Better information makes it more likely that individuals and organizations will participate in economic transactions, deepening the liquidity of markets. Moreover, the incorporation of such information in the decision making process of economic agents yields price signals that accurately reflect individual preferences.

Corporations are the central economic agents in a capitalist system. In most countries, they create most of the economic growth, provide employment opportunities, deliver useful products and services, and ultimately lead to better social outcomes. Corporations need a number of resources in order to produce and deliver their products and services. For example, they employ people, utilizing their skills and knowledge, and they obtain financial capital to finance their investments. They market their products to customers creating brands and forming a reputation. Finally, they obtain licenses from regulators to conduct business. In each one of those transactions, the counterparty to the corporation (i.e., employee, investor, customer, or regulator) seeks to obtain information about the corporation in order to enter into an exchange of goods and services. Corporate reporting aims to provide all of these counterparties with the information they need in order to transact with a company. This can be called the “information function” of corporate reporting. Corporate information that is more decision useful is more likely to encourage all of these counterparties to transact with the company and, all else equal, to transact with a company on better terms. For example, a vast literature in accounting shows that firms with better disclosure or accounting quality receive financing on more favorable terms (Botosan 1997; Francis, Nanda and Olsson 2008).

Corporate reporting serves another function, what can be termed the “transformation function.” While the information function assumes no feedback from counterparties, the transformation function relaxes this assumption, allowing for engagement and activism from the counterparties. The

counterparties receive and evaluate the information. Where they see opportunities to influence corporate behavior to their benefit, and potentially to the benefit of the corporation, they actively try to bring about change. This engagement, activism, and change process enables a company to transform. The transformation function does not assume that the information function is performed effectively. In many cases, counterparties engage and bring change under conditions of incomplete information. For example, NGOs like the Global Reporting Initiative (GRI) and Transparency International (TI) engage with corporations to improve disclosure. Their engagement efforts are frequently exerted with incomplete, if any, information. It is natural to think, though, that counterparties will spend their efforts more productively if they are better informed.

In the case of the company itself, the information and transformation functions can be combined. External reporting can influence internal decision making, with revenue recognition and earnings management being two of the most commonly studied examples in financial reporting. Those advocating sustainability reporting see this act as also influencing internal decisions by virtue of the fact that the company is now tracking its performance on other metrics, reporting its performance externally, and perhaps even committing to targets—as many companies do. This influence on internal decision making can occur even without stakeholder engagement that results in the transformation function. We will refer to this as the “internal transformation function,” but our main focus will be on the external one which we will simply refer to as the “transformation function.” It should also be noted that the transformation function can apply to financial reporting as well. Investors unhappy with a company’s financial results may initiate engagement, such as through proxy voting, that are intended to improve financial performance, such as by replacing board members or separating the role of Chairman and CEO. As we will argue below, integrated reporting could result in both internally and externally-driven transformation.

With those primary functions in mind, one could question whether the current corporate reporting regime is effective in performing those functions. We turn to section 2 to analyze whether the current reporting regime satisfies these two functions. While the analysis can be performed for any counterparty,

we concentrate our discussion on investors since they are a primary consumer of information provided by corporate reports.

2. The Adequacy of Separate Financial and Sustainability Reporting

Currently, many large public companies around the world issue separate financial and sustainability reports. There is some variation in this by region, with the proportion of European companies issuing sustainability reports being higher than that in the U.S. and Asia (Eccles, Serafeim and Andrews 2011). The financial reports are shaped by accounting standards, while the sustainability reports are not but often comply with voluntary reporting standards, such as those created by the GRI. Moreover, while financial reporting is geared towards investors, sustainability reporting is geared towards stakeholders including employees, customers, suppliers, local communities, and NGOs.

Criticisms of how well financial reporting performs the information function have become more frequent over the past 20 years. With the economy becoming more knowledge- and information-based and less based on machinery and physical properties, many of a firm's assets are not captured on the balance sheet. The growing base of intangible assets that are not measured on the balance sheet is frequently cited as a failure of financial reporting to perform its information function (Amir and Lev 1996; Eccles et al. 2001). As a result, empirical research papers have shown a deterioration of the value relevance of accounting numbers, although the specifics remain a contested terrain (Francis and Schipper 1999).

Recently, an increasing number of investors have become interested in sustainability information in the form of environmental, social, and governance (ESG) data (Eccles, Krzus, and Serafeim 2011; Ioannou and Serafeim 2014). Indeed, recent research suggests that ESG disclosure and performance affect corporations' access to finance (Cheng, Ioannou, and Serafeim 2014). This interest in ESG performance information is driven for some investors by moral or ethical reasons; for other investors it is driven by economic reasons since these data could improve the risk-return profile of a portfolio (UNEPFI 2006). Whatever reason an investor is interested in the data, the fact remains that financial reporting fails to

provide information on ESG performance. While sustainability reporting aims to fill this vacuum, critics highlight that it does so incompletely because the information provided lacks credibility, timeliness, and relevance. The data that are included in a sustainability report are frequently not audited and, even when they are, the report receives negative assurance rather than the more investor-useful positive assurance. One of the major reasons for this is that ESG data lack the rigorous measurement and reporting standards that exist for financial information, although organizations like the GRI and the Sustainability Accounting Standards Board (SASB) are working to change that. Moreover, sustainability reports tend to be published with a lag of several months compared to financial reports, making the information included in them less valuable. Finally, and perhaps most importantly, information contained in sustainability reports is rarely presented in the context of the business model and the strategy of an organization, making it difficult for investors to understand how ESG performance relates to financial performance and how sustainability issues affect the value creation process in an organization.

The discussion so far suggests that the current corporate reporting status quo performs the information function incompletely. The same can be said about the transformation function. With poor information, investors are ill-equipped to monitor and engage with a company on areas where performance could be improved. The same is true for stakeholders, especially those interested in a holistic view of a company's performance and the trade-offs it has to make across shareholders and stakeholder groups, at least in the short term (Waygood 2013). Stakeholders who take a more holistic view are likely to be more effective than those who focus on a single issue since they will be able to engage with the company in a way that recognizes the conflicting pressures the company is under. But getting this holistic view requires that the company provide information to stakeholders in a holistic way that shows the relationships between financial and ESG performance. We turn to section 3 to discuss the concept of integrated reporting and whether it can be a potential solution to the shortcoming of the current reporting landscape in terms of both the information and transformation functions.

3. What is Integrated Reporting and Why it Could be Functionally Superior

Integrated reporting has a short history, its meaning is still evolving, and only recently has a framework been developed that can provide companies guidance on what constitutes an “integrated report.” Like other new management concepts, integrated reporting first started in practice. The first companies to produce an integrated report were the Danish enzymes company Novozymes (in 2002), the Brazilian cosmetics fragrances company Natura (in 2003, one year before its IPO), and the Danish pharmaceutical company Novo Nordisk (in 2004).¹ The Danish companies were a single entity until their demerger in 2000 and so the similar timing of the two is not surprising. And while we cannot prove this, it seems unlikely that a Brazilian company in a completely different industry was familiar with Novozymes’ 2002 integrated report, saw it as a good idea, and copied it. As in science, paradigm-changing ideas often occur independently and simultaneously once an “idea’s time has come.” So it would seem to be with integrated reporting.

The introduction of integrated reporting by these companies was visionary at the time because sustainability reporting was itself only in its early stages, having started in the early 1990s with only about 500 companies issuing sustainability reports in the late 1990s on a worldwide basis.² All of these companies, for some similar and different reasons, were early believers that sustainability was something companies should take seriously or they were under intense pressure from outside stakeholders to become more transparent about their environmental and/or social impacts. Stakeholder engagement began to emerge as corporate practice in order to ascertain which ESG issues were of greatest interest to them and of most potential impact on the company and its ability to create value for its shareholders over the long-term. Their premise behind integrated reporting was that it was the best way to communicate externally when ESG issues had been made core to the company’s strategy and operations, the information function of reporting. But early practitioners of integrated reporting were equally clear that it would lead to more

¹ *One Report: Integrated Reporting for a Sustainable Strategy* by Robert G. Eccles and Michael P. Krzus, John Wiley & Sons, Inc. Hoboken, New Jersey, 2010, Chapter 1.

² *Ibid.*, p. 97.

integrated internal decisions, aided by the input it would get from shareholders and other stakeholders who reacted to the information the company provided in its integrated report—the transformation function. That said, more emphasis was given to engagement for determining the content of the report—the information function—then to how it would enable stakeholders to engage with the company on a broader set of issues—the transformation function.

To our knowledge, the first publication about integrated reporting was in June 2005, itself a visionary act. Allen White, one of the co-founders of the GRI, begins by claiming that “A quiet renaissance in corporate reporting is gradually transforming its purpose, content and readership.”³ He rightly described integrated reporting as “embryonic” at the time in contrast to sustainability reporting which he refers to as being in the “pre-adolescence” stage since by then over 2,000 companies were producing sustainability reports, albeit by various names.⁴ While most of his discussion is focused more on nonfinancial (sustainability) reporting, White sees integrated reporting as the future of corporate reporting. Most of his focus is on the information function, but there is some discussion of the internal transformation function as well, more in terms of how an integrated report enables a company to transform itself since “cross-functional collaboration and learning...triggers conversations that otherwise would not occur, insights that would not otherwise surface, and innovations that would not otherwise materialize.”⁵

Two months later the Canadian sustainability consulting firm, Solstice Sustainability Works, published a report on integrated reporting that had been commissioned by Van City, a Canadian cooperative bank, and Citizens Bank. This report discussed both the information (“reporting that meets the needs of both statutory financial reporting and sustainability reporting”) and transformation (primarily internal) (“improved understanding of the links between sustainability and business strategy, consistent

³ “New Wine, New Bottles: The Rise of Non-Financial Reporting,” A Business Brief for Business for Social Responsibility by Allen L. White, June 20, 2005.

⁴ Ibid., p. 3.

⁵ Ibid., p. 4.

messaging, and improved decision making”) functions.⁶ Solstice also noted that “The vision of integrated reporting requires an articulation of the links between financial and sustainability performance and outcomes.”⁷

It is in showing these links or relationships, something still rare in most integrated reports due to a lack of understanding of what they are and still-emerging measurement and reporting standards, that the full value of the information function is achieved. It is how a company provides the information of interest to a certain class of investors and to stakeholders who want a holistic view of a company’s performance, with insights into its ability to create value over time. Knowing these relationships could enable a company to make better internal decisions. External reporting could further improve internal decision making through stakeholder engagement since “As companies realize the benefits of better decisions from higher levels of internal collaboration, they will naturally seek to obtain these same benefits from higher levels of external collaboration through stakeholder engagement in order to better understand their expectations, obviously useful for internal decision making.”⁸ Through this engagement, integrated reporting could effectively perform the transformation function.

The first U.S. company to issue an integrated report was United Technologies Corporation in 2008. Starting in 2011, all South African companies listed on the Johannesburg Stock Exchange were required to issue an integrated report or explain why they weren’t doing so. There is no clear way to measure the number of companies that are issuing integrated reports. Rather the practice of integrated reporting is a matter of degree. There are companies that are doing more or less integrated reporting and firms that practice to a certain extent integrated reporting while not describing their reports as integrated (Eccles and Serafeim 2011; Serafeim, 2014). However, through 2012 there were no well accepted guidelines on just what constituted an “integrated report,” with the exception of a brief document prepared in early 2011 by the Integrated Reporting Committee of South Africa. No formal guidance about

⁶ “Integrated reporting: issues and implications for reports,” by Solstice Sustainability Works, August 2005.

⁷ Ibid.

⁸ Eccles and Krzus, p. 151.

integrated reporting existed until the International Integrated Reporting Council (IIRC) published “The International <IR> Framework” (<IR> Framework) in December 2013.

The <IR> Framework explicitly notes the information and transformation functions of integrated reporting. The first sentence of the “Executive Summary” notes that “Integrated reporting (<IR>) promotes a more cohesive and efficient approach to corporate reporting and aims to improve the quality of information available to providers of financial capital to enable a more efficient and productive allocation of capital.”⁹ But the IIRC also notes that an integrated report can be of interest to others as well. “An integrated report benefits all stakeholders interested in an organization’s ability to create value over time, including employees, customers, suppliers, business partners, local communities, legislators, regulators and policy-makers.”¹⁰

The transformation function from an internal point of view is accomplished through “integrated thinking” which “is the active consideration by an organization of the relationships between its various operating and functional units and the capitals that the organization uses or affects.”¹¹ Integrated reporting and integrated thinking are a self-reinforcing cycle which will result in “efficient and productive capital allocation” and which will also “act as a force for financial stability and sustainability.”¹² Key to this cycle are measuring and reporting on all of the capitals a company uses to create value (financial, manufactured, natural, intellectual, human, and social and relationship) and the connectivity of information regarding how decisions about one type of capital affect the others (Figure I). The <IR> Framework also recognizes the external transformation function of integrated reporting since it notes that value is “created through relationships with stakeholders”¹³ and that “an integrated report should provide insight into the nature and quality of the organization’s relationships with its key stakeholders, including how and to what extent the organization understands, takes into account and responds to their legitimate

⁹ “The International <IR> Framework,” by the International Integrated Reporting Council, c. December 2013.

¹⁰ Ibid., p. 4.

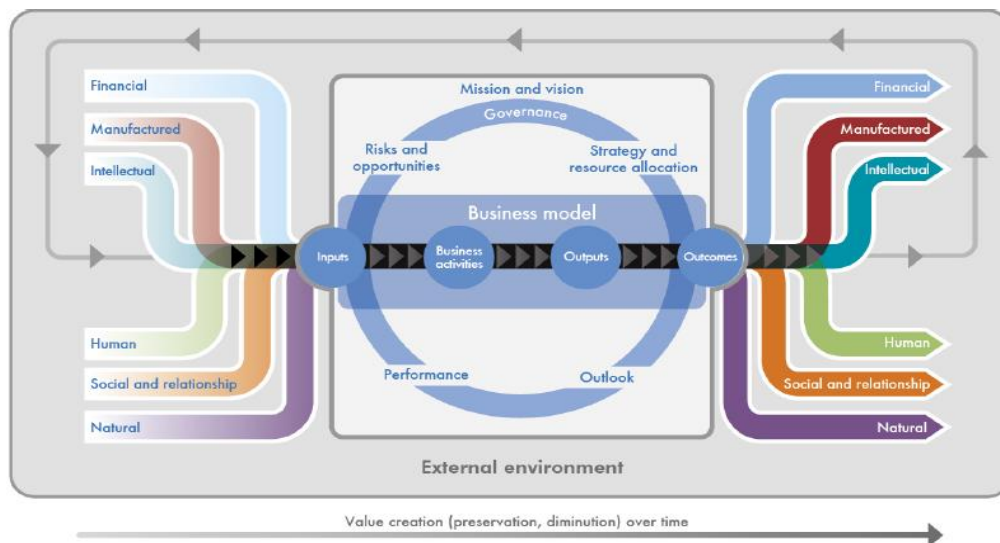
¹¹ Ibid., p. 2.

¹² Ibid.

¹³ Ibid., p. 10.

needs and interests.”¹⁴ Providing stakeholders with this information will make them more effective in performing the transformation function. They can “provide useful insights about matters that are important to them, including economic, environmental and social issues that also affect the ability of the organization to create value.”¹⁵ This is done through enabling the company to better understand how stakeholders perceive value, identifying trends the company may not be aware of but that are of increasing significance, identifying material risks and opportunities, identifying risks and opportunities and better managing risk, and providing useful input into the development and implementation of the company’s strategy.¹⁶

Figure I
Value Creation



An analysis of 124 reports issued by organizations that participate in the pilot program of the IIRC or are mandated to produce integrated reports because they are listed in the Johannesburg Stock Exchange provides an overview of the availability of information around the different forms of capital.¹⁷ Figure II shows for the different capitals the percentage of firms that provided no information (0), little

¹⁴ Ibid., p. 17.

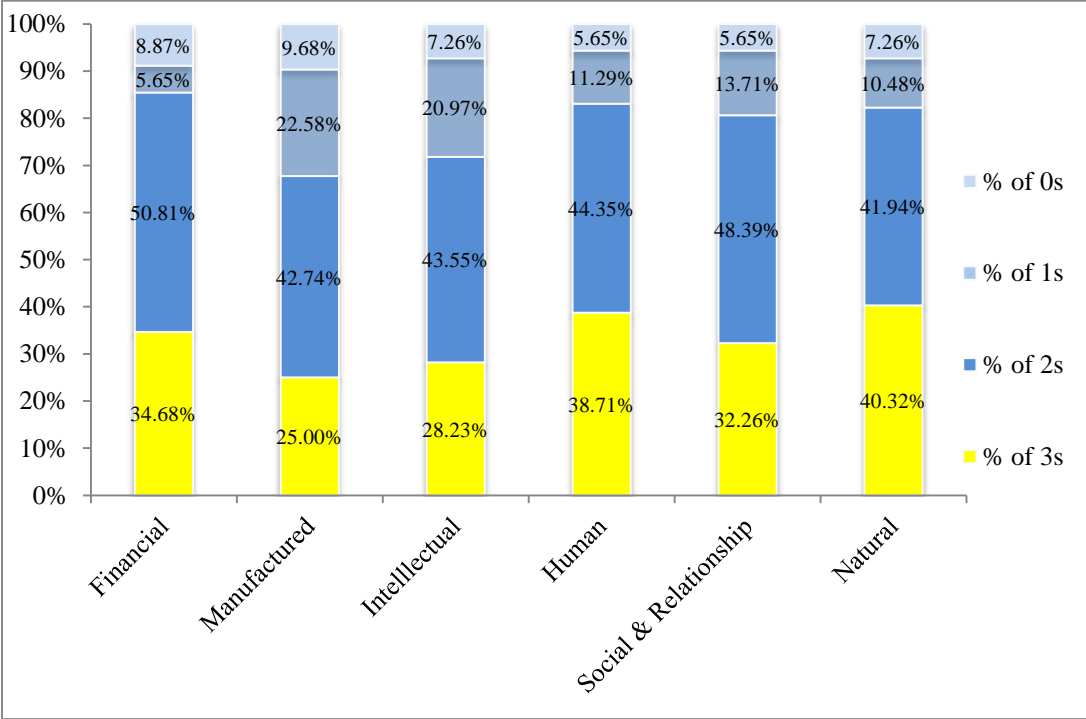
¹⁵ Ibid.

¹⁶ Ibid, pp. 17-18.

¹⁷ See Serafeim (2014) for a description of the sample.

information (1), moderate information (2), and detailed information (3). Across capitals, one can observe that companies are providing less information about manufactured and intellectual capital. While the relative deficiency of information about manufacturing capital could be attributed to the relative decline in importance of manufacturing assets in the knowledge economy, the deficiency of intellectual capital information is puzzling. Intellectual capital in the form of innovation capabilities and outcomes are important value drivers for many businesses now days. The capitals that companies report more information about are natural and financial capital. The first could be explained by the rising pressure on companies to improve their environmental performance. The latter by the longstanding emphasis of corporate reporting on financial issues. In general, one could argue that there is a fair amount of information about the different forms of capital in these corporate reports. However, a significant number of companies are still providing little capital-specific information even though these companies are considered leaders in integrated reporting.

Figure II
Percentage of Companies Reporting Capital Specific Information



While it is clearly too soon to claim that many companies and investors are reaping the information and transformation benefits of integrated reporting, that is clearly the intent of companies that are its early practitioners, people who have written on the subject, and the new <IR> Framework. In the next section we conduct a case study on a company that is practicing integrated reporting to promote the efficient performance of the information and transformation functions.

4. Integrated Reporting for Real: Coca-Cola Hellenic Bottling Company

Coca-Cola Hellenic Bottling Company (Coca-Cola HBC) is the second largest bottler of Coca-Cola products in the world and published its first Integrated Report in 2012. We believe that the report issued by Coca-Cola HBC represents a best case example of IR, as of 2013, since it takes into account all guiding principles and includes all of the content elements outlined by the IIRC (Figures III and IV). It clearly outlines risks and opportunities and the strategic and operational actions Coca-Cola HBC will take to address them.

Figure III Guiding Principles

GUIDING PRINCIPLES

The following Guiding Principles underpin the preparation of an integrated report, informing the content of the report and how information is presented:

- *Strategic focus and future orientation:* An integrated report should provide insight into the organization's strategy, and how it relates to the organization's ability to create value in the short, medium and long term, and to its use of and effects on the capitals
- *Connectivity of information:* An integrated report should show a holistic picture of the combination, interrelatedness and dependencies between the factors that affect the organization's ability to create value over time
- *Stakeholder relationships:* An integrated report should provide insight into the nature and quality of the organization's relationships with its key stakeholders, including how and to what extent the organization understands, takes into account and responds to their legitimate needs and interests
- *Materiality:* An integrated report should disclose information about matters that substantively affect the organization's ability to create value over the short, medium and long term
- *Conciseness:* An integrated report should be concise
- *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: (a) on a basis that is consistent over time; and (b) in a way that enables comparison with other organizations to the extent it is material to the organization's own ability to create value over time.

Source: <IR> Framework, IIRC

Figure IV
Content Elements

CONTENT ELEMENTS

An integrated report includes eight Content Elements that are fundamentally linked to each other and are not mutually exclusive:

- *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?
- *Business model:* What is the organization's business model?
- *Risks and opportunities:* What are the specific risks and opportunities 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?
- *Performance:* To what extent has the organization achieved its strategic objectives for the period and what are its outcomes in terms of effects on the capitals?
- *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 future performance?
- *Basis of presentation:* How does the organization determine what matters to include in the integrated report and how are such matters quantified or evaluated?

Source: <IR> Framework, IIRC

The rich content of the report, as well as the connection of initiatives to concrete goals, KPIs, and the value creation process are key to the effective performance of the information function of corporate reporting. For example, the company has identified “Community Trust” as a major pillar of each strategy. Coca-Cola HBC identifies managing the impact of its supply chain, prioritizing safety, responsible sales and marketing, supporting active lifestyles, partnering with local communities, wellbeing of employees, and managing waste as initiatives to ensure building of community trust. Relatedly, the company reports KPIs around safety, carbon footprint, water footprint, and inclusion in sustainability indices to track performance on those initiatives. Moreover, the connection of each material issue to stakeholders affected and to initiatives the organization undertakes to address each issue provides the platform for engagement and, as a result, enable the transformation process. Every stakeholder can identify the impact that the company is having on her and what the company is doing to mitigate the negative impact and magnify the positive impact.

To provide a better understanding of some of the strengths of the report, we briefly describe below how the Coca-Cola HBC integrated report follows some of the guiding principles. Before we do that, we highlight that the reporting roadmap that is included in the report that allows the reader to understand what are the material issues, the initiatives the company undertakes to manage them, the KPIs that are used to track performance, the main areas of risk, the stakeholders affected, and how they affect the value creation process. Importantly, the report graphically illustrates the value creation process inside the organization (Figure V). In just one figure the reader is able to understand the business model and strategy of the organization.

Strategic focus and future orientation

- The report clearly outlines the organization's strategic framework and how each key performance indicator (KPI) is relevant to its strategy. Four strategic priorities have been identified: Community Trust, Consumer Relevance, Customer Preference, and Cost Leadership. Each priority relates back to the value creation inside Coca-Cola HBC and the company reports for each priority what are the initiatives that are pursued in order to improve performance.
- It graphically illustrates the use of all forms of capital and how they enable the value creation process (Figure V).

Connectivity of information

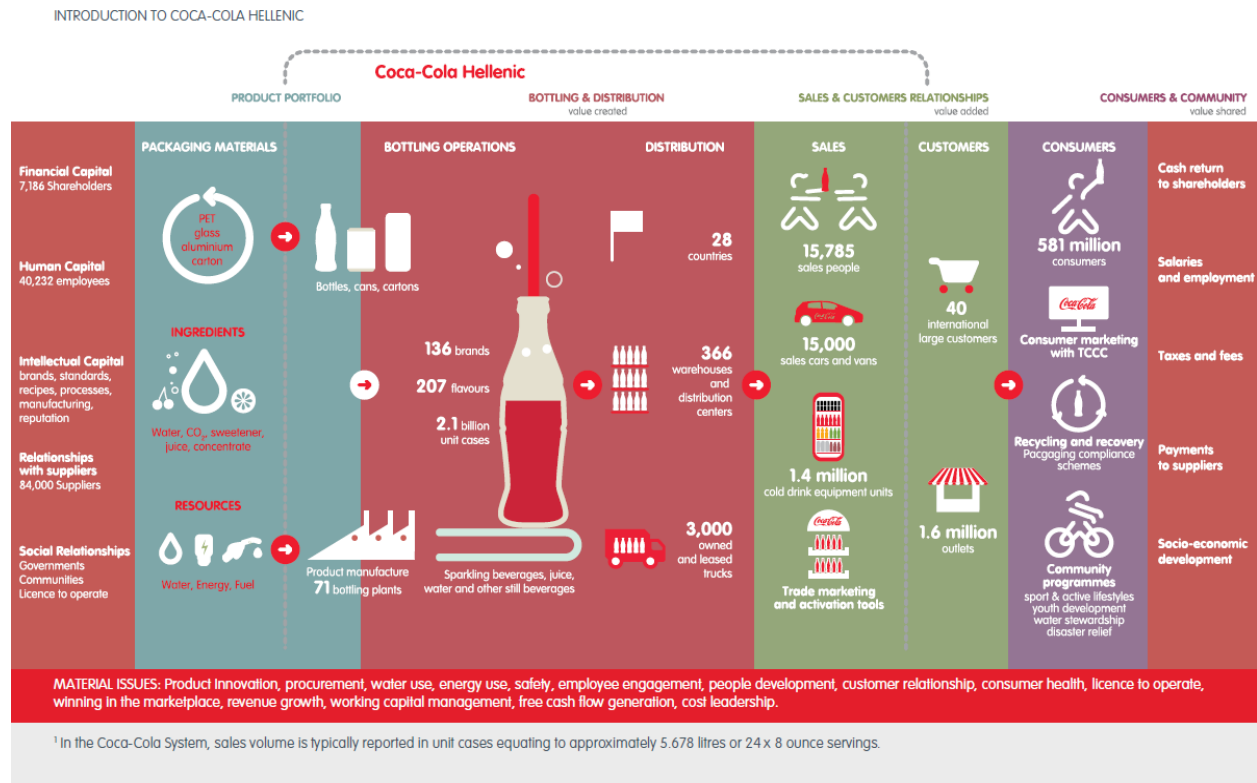
- The report describes the relationships and issues that are material to the organization and how they interact to create value over time. The report flows seamlessly from one section to the next and shows the coherence of each organizational choice with the following sequence: business model → strategy → external environment → operations → performance → risks and opportunities → governance

Materiality and conciseness

- The report identifies the most material issues across the Coca-Cola HBC value chain and ties them back to the company's ability to create value. The information provided is concise yet substantive with the report consisting of just 68 pages.

- The report makes heavy use of infographics, keeping the information concise, and communicating the key messages in a way that is easy for the reader to understand.

Figure V
Value Creation at Coca-Cola HBC



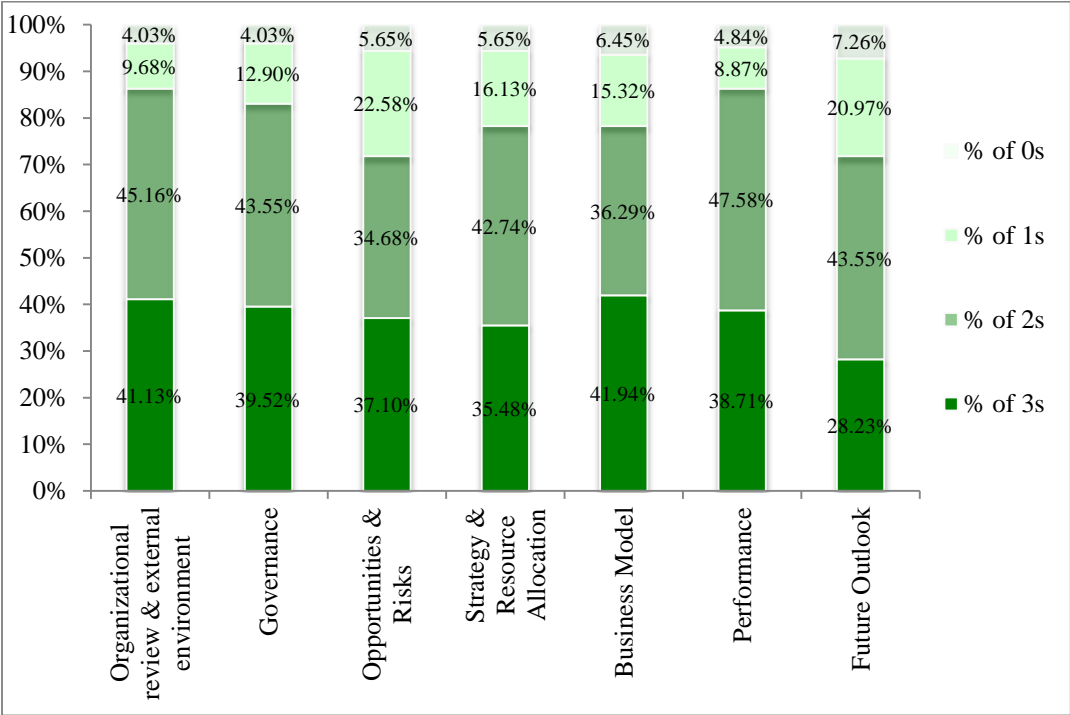
Source: Coca-Cola HBC 2012 Integrated Report

The case of Coca-Cola HBC represents a promising example of the future of integrated reporting. However, one should remember that integrated reporting still lacks regulatory support and the monitoring and enforcement that regulatory bodies provide to ensure accurate and reliable corporate reporting. A large literature has shown the importance of enforcement and monitoring and enforcement in enhancing the reliability, credibility, accuracy and, as a result, the decision usefulness of accounting information (Leuz 2010). We discuss the role of regulation in integrated reporting in the next section by studying the case of Anglo-American.

Before we proceed to the next section we provide an overview of the current landscape of integrated reporting by presenting summary statistics on the percentage of companies that provide information about the different content elements of integrated reporting. Figure VI shows that performance and organizational review are the two most well reported content elements. In contrast, information about opportunities and risks and future outlook are the two least well reported content elements. Both content elements require a higher degree of subjectivity and involve more uncertainty presumably increasing the reluctance of organizations to report such information. Traditional financial reporting is more backward looking with its emphasis on historical cost accounting. Thereby providing information on future outlook is something that companies are still struggling with although such information is traditionally communicated through earnings and other types of guidance.

Figure VI

Percentage of Companies Reporting Content Element Specific Information



5. Integrated Reporting and Regulation: The Case of Anglo-American

Integrated reporting is a corporate practice that has evolved over time shaped by market forces rather than regulation. Even in South Africa, where integrated reporting is mandatory, there are no strict guidelines, rules or standards about what a company should include in an integrated report. One could question whether such standards should exist, an incredibly difficult question to answer given the complexity of the associated cost-benefit analysis. We do not attempt to undertake such a cost-benefit analysis here to be able to answer the question of regulation. However, we observe that in every country with a developed or developing capital market, corporate reporting is regulated and guidance exists that shapes the content, timeliness, and credibility of corporate reporting.

One fundamental benefit of reporting regulation is enhanced comparability of information. For example, when accounting standard setters mandate the disclosure of information around pension liabilities, this ensures that interested parties have access to that information from all firms that are subject to the regulation and across time for the same firm. Some firms cannot choose whether or not to disclose this information and the same firm cannot choose to disclose a value relevant and important piece of information one year and not the next.

We already see how the lack of regulation of IR limits its usefulness. Even among the firms that practice IR, there is significant variation across firms on what they include in an IR. The same is true for what firms include in an integrated report over time. With IR receiving increasing attention and investors beginning to use data from IR reports into their capital allocation decisions, the potential for strategic disclosure from the part of management is higher. Because corporate management has an interest in increasing the stock price of the firm to increase executive compensation through stock option and bonuses or to receive financing in more favorable terms, the preference to reveal good news while hiding bad news is economically rationale. Indeed, research has documented that managers tend to withhold bad news and releases good news (Kothari, Shu, and Wysocki 2009).

An interesting case is Anglo-American, the largest firm in the world in the platinum industry. In 2012 the firm experienced landmark market disruptions (price declines) and severe labor unrest in South

Africa. Profits plummeted with mines being shut down and violence erupting in several locations. The firm published an IR both in 2011 and 2012. We found that the IR was about 50 pages shorter in 2012 and one of the most useful elements, in our opinion, in the 2011 report, the ESG scorecard that summarized in one place the most important KPIs, was completely removed. While financial performance had significantly declined, most of the ESG metrics that the firm chose to keep in 2012 did not show a similar deterioration. Overall, the 2012 report seems to be a rather traditional financial report with a few pages of the sustainability report stapled in. While these trends do not necessarily mean that the company is not reporting the optimal amount of information, it showcases how variability in reporting practices can inhibit the comparability of reported information.

Significant variability in the type of information reported across firms or by a firm over time is an impediment to both the information and transformation function of corporate reporting. Outside parties that cannot benchmark a company's performance against its competitors will find it difficult to make a choice across companies on how they allocate their resources. Moreover, not being able to make comparisons across firms and over time makes it more difficult for outside parties to form expectations and engage with the company to start the transformation process. While we see the lack of regulation of IR being reflected in low comparability of information reported in them, this is just one piece of the puzzle in a cost-benefit analysis of regulation. There can be many costs associated with regulating IR and we actually note that, perhaps paradoxically, the IR of Coca-Cola HBC, which we see as a best practice example, is a completely voluntary action from the part of the management, while the IR of Anglo-American, which exhibits shortcomings in terms of comparability, is mandated by stock exchange regulations on a 'comply or explain approach.'

6. Conclusion

In this chapter we have argued that corporate reporting plays two functions. The first is an "information function" which enables investors to make capital allocation decisions across companies, at least in the same sector. Companies themselves can benefit from the information function by benchmarking their

performance against peers, thereby informing internal resource allocation decisions. The second is a “transformation function” which is the result of a company engaging with stakeholders to get their input on the company’s resource allocation decisions. We have also argued that in today’s world with a variety of social and regulatory trends raising the importance of sustainability issues (broadly defined in terms of environmental, social, and governance), separate financial and sustainability reports are no longer adequate for performing either function. Investors need a better understanding of how companies are managing the relationships between financial and nonfinancial performance. Companies themselves need integrated reporting in order to make sure that they are having the appropriate forms of stakeholder engagement, starting with the preparation of the report itself and using the report as the basis for further engagement, in order for the transformation function to be as effective as possible.

The two functions vary in terms of how important the role of regulation is. The example of Anglo-American illustrates that regulation is extremely important for an effective information function in the same way that regulation is necessary to establish accounting standards. Regulation could be less important for the transformation function and, some would argue, can actually inhibit it. The high-level, principles-based framework of the IIRC enables companies to determine the most material issues through stakeholder engagement and then to continue the engagement process. If regulation is more prescriptive and “rules-based,” the risk is that integrated reporting becomes more of a compliance exercise.

This raises an important question for future research. Financial reporting is more focused on the information function and sustainability reporting on the transformation function. Integrated reporting is an attempt to accomplish both. Can it do so or are the tradeoffs between the extents to which these two functions are achieved inevitable? It is hard to address this question in an empirical way since so far there is no country that has well-defined regulations on just what constitutes an “integrated report.” However, some preliminary insights could be gained by in-depth case studies to determine if companies see these functions as representing tradeoffs or if they are looking for ways to get the best of each. Such insights would usefully inform any future regulations so that the information function is not achieved at the total sacrifice of the transformation function.

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