Curtis C. Verschoor, CMA, CPA, Editor

Integrated Reporting Lags in the U.S.

An increasing number of companies around the globe are using integrated reporting as part of their annual reports, but the initiative is making slow progress in the United States.

Efforts have been under way for years to make the reporting of corporate performance in both financial and nonfinancial terms more understandable and useful to all stakeholders. This is becoming even more difficult in today's business environment. Factors such as the growing complexity of doing business in a worldwide economy, the increased legal exposure of businesses in meeting regulatory requirements, and the move toward harmonizing accounting standards globally while still addressing the needs of local jurisdictions and regulatory agencies combine to create additional challenges in communicating performance results. And that's before you even factor in the growing popularity of corporate responsibility reporting and the expanded definition of a company's stakeholders.

In recent years, an initiative known as Integrated Reporting (IR), has focused on combining financial reporting with responsibility reporting concerning social issues, governance, and the environment. This movement is led by the International Integrated Reporting Council (IIRC), which issued the *International Integrated Reporting Framework* (IIRF) in 2013 to set guidelines for reporting. According to the IIRC, "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."

IR aspires to greater benefits for all stakeholders whose companies adopt the practice. The IIRC believes it "is 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." Because of its future orientation and emphasis on value creation, investors should be able to better understand company strategies and how effectively they work, resulting in lower costs of capital for the organization over the long term. Internally, a common focus on creation of long-term value with consideration of environmental and social issues should eliminate thinking in silos and result in a more effective and efficient execution of long-term strategies.

The IIRC published a summary of progress in 2012-2013 reported by the 100 companies in the Pilot Programme—companies that volunteered to implement the principles of the Framework. Its "Business and Investors Explore the Sustainability Perspective of Integrated Reporting" report found that businesses in the IIRC Pilot Programme are tackling key interconnected areas of IR: the use of capitals, the creation of value, and the definition of the organization's business model.

According to Mervyn E. King, chairman of the IIRC, "Integrated Reporting is playing a role in meeting the world's two great challenges—financial stability and sustainability. The participants in the IIRC Pilot Programme have made and continue to make an important contribution to sustainable capitalism."

IR in the U.S.

Historically, the emphasis of corporate reporting in the United States has been on meeting quarterly earnings expectations and satisfying shareholders. The movement to address stakeholders beyond investors is gaining strength, but it still lags behind other countries. Consistent with that trend, only seven of the companies in the IIRC's Pilot Programme have their corporate headquarters in the U.S. In an online search, I was only able to find integrated reporting information for two of those companies.

The first company is Jones Lang LaSalle Incorporated (JLLI), a global financial and professional services firm specializing in commercial real estate services and investment management. JLLI's 2013 Annual Report to the Securities & Exchange Commission (SEC) on Form 10-K contains a paragraph stating the company intended the report to satisfy the requirements of the IIRF, presumably by combining both financial and sustainability reporting. Nevertheless, JLLI published both a 2013 Sustainability Report and a 2013 Transparency Report. This limited coverage doesn't seem to be a ringing endorsement of actually integrating corporate responsibility reporting with financial reporting.

The second company is Clorox Corp., a multinational manufacturer and marketer of consumer and professional cleaning/household products. Of the U.S. companies in the IIRC's Pilot Programme, Clorox has made the most substantial effort at integrated reporting so far. But a look at the results shows that more progress is needed.

Clorox Corp.'s Integrated Report

An August 1, 2014, press release presented Clorox's fiscal year 2014 financial results. This document followed usual public company practices and wasn't prepared as an integrated report. A separate press release on October 13, 2014, announced the publication of Clorox's 2014 Integrated Annual Report. Yet the release contained no financial information or integrated disclosures. It highlights the four factors helping Clorox achieve its fiscal year 2014 business and corporate responsibility objectives—Engage Employees, Innovate Every Day, Expand Our Brands, and Fund Growth—which are contained in the context of the company's 2020 Strategy:

- "Engage our people as business owners"—Using consulting firm data for workforce attitudes and reported U.S. government safety experience, Clorox has empowered its employees to streamline operational processes and make decisions faster. Its safety record is world class.
- "Increase brand investment behind superior value and more targeted 3D innovation"—This year, the company saw sustainability improvements in 15% of its products, and promotional efforts emphasized value.
- "Grow in profitable new categories, channels and countries"—Expansion plans during the year targeted new products and new markets.
- "Fund growth by reducing waste in our work, products and supply chain"—This was the 11th consecutive year that Clorox had cost savings in excess of $100 million. The company reduced its greenhouse gases by 12% and its waste sent to landfills per product unit by 34%.

Clorox's 2014 Integrated Annual Report is presented in a digital format that utilizes the forward-looking principles of IR. It uses the context of Clorox's 2020 Strategy to measure the company's performance in the current year in terms of financial, environmental, social, and governance factors. The strategies are repeated under the general caption of the Integrated Business Model—Goal, Mission, Objective, and Commitment.

The Integrated Annual Report has a Scorecard section containing five subcategories and a company profile that gives a short summation of the report. Each subcategory has quantitative measures of 2014 achievements, several of which have review-level negative assurance by Clorox's independent public accounting firm, Ernst & Young.

The Performance (or financial) subcategory of the report contains four measures based on Generally Accepted Accounting Principles (GAAP) and three non-GAAP measures. A footnote page explains the non-GAAP measures: EBIT (earnings before interest and taxes), Economic Profit, and Free Cash Flow. The other subcate-

continued on page 61

For guidance in applying the *IMA Statement of Ethical Professional Practice* to your ethical dilemma, contact the IMA Ethics Helpline at (800) 245-1383 in the U.S. or Canada. In other countries, dial the AT&T USA Direct Access Number from www.usa.att.com/traveler/index.jsp, then the above number.

Ethics

continued from page 14

gories are Products ("Making responsible products, responsibly"), Planet ("shrinking our environmental footprint while growing our business"), People ("Engaging our people as business owners and promoting diversity, opportunity and respectful treatment"), and Our Impact ("Safeguarding families with our Be healthy, Be smart and Be safe initiatives").

Clorox's Financial Reporting

The Clorox 2014 Annual Report to the SEC on Form 10-K appears straightforward and has the same regulatory format as other U.S. public companies, but it excludes a great deal of financial information that many companies would include. Clorox has an Appendix in its Proxy Statement containing the Management's Discussion and Analysis of Financial Condition and Results of Operations, audited financial statements, the independent auditor's opinion on the financial statements and internal control over financial reporting, and other selected financial information. These separate documents are required disclosures that most companies put in their 10-K, not in their Proxy Statement. There was no mention of Integrated Reporting in either Clorox's 2014 Proxy Statement or its Annual Report on Form 10-K. A reconciliation schedule explained the differences between GAAP income and economic income, but the heading didn't mention GAAP. Neither was there any mention of the other two non-GAAP financial measures reported in the Clorox Integrated Annual Report.

The end result is two separate reports describing Clorox's performance for the year. The major goal of IR is to align various frameworks for nonfinancial reporting and integrate them or connect them directly to financial measures to better inform investors and other market constituents about the long-term, sustainable value-creation capability of the organization. Having two unconnected, distinct reports doesn't seem to fulfill that goal.

IR and Ethical Behavior

In this column, I have long advocated that companies that behave ethically generally report better results, and the evidence continues to support that notion. One element of behaving ethically is the consideration of other key stakeholders beyond the company's shareowners. This includes the employees; the cities, towns, and other locales in which the company operates; and the environment. As seen in Clorox's 2014 Integrated Annual Report, an important aspect of IR is corporate responsibility and/or sustainability reporting. Thus, companies that embrace IR would appear to be moving in the right direction of ethical behavior by establishing a company culture that looks to long-term growth and sustainability and values the needs of all stakeholders over short-term gains.

Unfortunately, the examples from two of the U.S. companies in the IIRC's Pilot Programme appear to fall short of meaningful Integrated Reporting. The creation of two different reports—one that gets filed with the SEC and another that's published separately—raises the question of whether IR is possible within the regulatory environment. Are other solutions, such as reducing the excessive disclosures required by regulators, needed before IR can gain a stronger foothold in the U.S.? **SF**

Curtis C. Verschoor is the Emeritus Ledger & Quill Research Professor, School of Accountancy and MIS, and an honorary Senior Wicklander Research Fellow in the Institute for Business and Professional Ethics, both at DePaul University, Chicago. He also is a Research Scholar in the Center for Business Ethics at Bentley University, Waltham, Mass., and chair of IMA's Ethics Committee. He was selected by Trust Across America-Trust Around the World as one of the Top Thought Leaders in Trustworthy Business–2014. John Wiley & Sons has published his latest book, Audit Committee Essentials. *His e-mail address is curtisverschoor@sbcglobal.net.*