Integrated Reporting Newsletter

First Edition, 2021

By the
Integrated Reporting Council of Sri Lanka (IRCSL)

Foreword by the Chairman of the Integrated Reporting Council of Sri Lanka

Corporate reporting has hitherto evolved progressively responding to market driven requirements, building on the existing foundation of financial reporting, and adding on, non-financial information such as sustainability reporting. This process did not historically address the fundamental short comings in the context, content, connectivity, and complexity of corporate reports. In addition, it did not address information asymmetry in the context of the interest of wider stakeholder groups fundamental to the success of the business. Integrated Reporting has endeavored to bring in a new paradigm of corporate reporting.

IIRC elaborated that Integrated Reporting has been created to enhance accountability, stewardship, and trust as well as to harness the information flow and transparency of business enabled by technology, providing investors with the information they need to make more effective capital allocation decisions.

The IIRC Framework on Integrated Reporting was first issued in 2013 and a few public listed Companies in Sri Lanka voluntarily adopted the framework in the same year. In response to that, CA Sri Lanka launched an award titled “Award for Integrated Reporting” in the said year at CA Sri Lanka Annual Report Awards competition. Progressively, the number of Companies adopting Integrated Reporting has increased over the past years to over fifty in number. The IIRC has now issued the revised Framework on Integrated Reporting which came into effect from January 2021.

IRCSL has issued three publications over the past several years to support preparers, practitioners, and other interest groups. These are;

1. A Preparer’s Guide to Integrated Corporate Reporting
2. A Supplement to a Preparer’s Guide to Integrated Corporate Reporting
3. Handbook on Integrated Corporate Reporting

In furthering its objectives, IRCSL planned to issue this newsletter to engage and update those interested in Integrated Reporting on new developments and thought leadership. This newsletter consists of three articles in Integrated Reporting, the first article is contributed by the ICAEW Sustainability Faculty titled “*Non-Financial Reporting: Ensuring a Sustainable Global Recovery”* and the second article is written by Dr. Nuradhi Jayasiri, an academic at University of Colombo in “*Integrated Reporting Reaching Maturity in Sri Lanka”.* The third article depicts the key changes brought into the 2021 revision of the IR Framework.

I hope this newsletter would be informative. I also encourage those interested in sharing articles to reach out to us.

Asite Talwatte

Chairman
Integrated Reporting Council of Sri Lanka
16th February 2021

Content

Non-Financial Reporting: Ensuring a Sustainable Global Recovery

By ICAEW (UK)

Overview

ICAEW is proud to work alongside CA Sri Lanka as both institutes are part of Chartered Accountants Worldwide, a global network representing over 1.8m chartered accountants and students. In addition, ICAEW is delighted to be implementing a joint student and membership scheme and Pathways agreement with CA Sri Lanka.

Founded in 1880, ICAEW now has 186,500 members and students across the globe. It has a long history of serving the public interest and continues to work with governments, regulators and business leaders around the world to develop the Profession. As a regulator, it supervises and monitors over 12,000 firms, holding them, and all ICAEW members and students, to the highest standards of professional competency and conduct.

ICAEW believes that chartered accountancy can be a force for positive change. By sharing our insight, expertise and understanding we can help to create strong economies and a sustainable future for all. It has technical faculties on financial services, audit and assurance, corporate governance, financial reporting, sustainability, ethics, among many others, which offer a wealth of articles, reports and webinars to support Chartered Accountants in using opportunities and addressing challenges facing this evolving Profession.

Below is a summary of an example article on *Non-Financial Reporting: Ensuring a Sustainable Global Recovery*, and the full article is available here.

There is a pressing need to expedite the sustainable rebuilding of economies. The COVID-19 pandemic has battered human, social and economic capital across the globe. For change to happen, business has to respond. In responding to the virus and charting a post-coronavirus recovery path, we cannot lose sight of the wider unfolding picture of climate emergency, massive biodiversity loss and increasing inequality. Improved reporting on environmental and social issues is central to efforts to encourage system change. Businesses need to better understand the strategic value nature and society has for them – and they need to recognise and be accountable for the impact of their activities.

ICAEW has put together a report here on the importance of non-financial reporting to ensure a sustainable global recovery.

Our recommendations:

- We strongly encourage all efforts to move towards the establishment of a single principles-based and internationally recognised global framework providing comparability and consistency for non-financial reporting.
- We believe in the longer-term goal of a global corporate reporting structure, encompassing both financial and non-financial reporting.
- Current moves to consolidate existing standards, guidelines and frameworks need to be accelerated and made more open and transparent.
- High quality standards need to be based on a shared understanding of the goals and purposes of reporting. Next steps must also address the urgent need to define and agree a solid conceptual framework for non-financial reporting.

What is the current state of play?

Enhanced non-financial reporting can play a critical role in the transition towards more sustainable and resilient societies and economies. Even more so in the aftermath of the COVID-19 crisis, businesses need to both understand the implications for their activities of environmental and social factors and be accountable for their impact on the nature, people and the economy.

Broadened non-financial disclosures also provide key information needed by shareholders, regulators and other stakeholders on the overall performance and impact of companies and other organisations. It is unsurprising that the demand for enhanced and more accessible corporate financial and non-financial information has continued to grow over the years, driven by investor needs, societal expectations and regulatory demands.

The result has been the emergence around the world of a wide range of non-financial standards, guidelines and frameworks that can be applied by companies. This proliferation of initiatives has, over time, led to a confusing landscape which risks undermining the overall usefulness and credibility of non-financial reporting. It is now time to come together to find a solution to the demand for improved non-financial reporting.

What is the end goal?

The coronavirus pandemic and the climate emergency are global challenges and call for global responses. Equally, capital markets participants call for global reporting standards enabling greater transparency, comparability and consistency. The IFRS experience indicates that a universal reporting language can offer many potential economic and social advantages. We believe the same holds true for non-financial reporting.

ICAEW has been a persistent champion of the creation of a single set of high-quality global accounting standards and their application by publicly traded and other companies around the world. When it comes to non-financial reporting, our ultimate goal is also that of a single set of high quality, authoritative standards that have international resonance. Given the pressing urgency of the challenges, such standards must be available in the mid-term, not the long term.

At international level, this calls for the establishment of an independent non-financial reporting standard-setting body overseen by an authoritative, internationally recognised umbrella body, which can represent relevant public organisations, to coordinate activities globally and help cement a common viewpoint on the desired direction of travel. We strongly encourage all efforts in this direction.

We believe that this could ultimately take the form of a global corporate reporting structure along the lines of the model put forward in the Accountancy Europe Cogito paper, interconnected standard setting for corporate reporting, published in December 2019. The Cogito paper sets out a three-tier reporting structure, including a stronger and broader approach to public oversight through an enhanced monitoring body, the restructuring of the IFRS Foundation into a body with a broader corporate reporting mandate and the establishment of a new International Non-Financial Reporting Standards Board (INSB) responsible for formalising non-financial reporting standards.

What is happening elsewhere in the world?

Governments across the globe are expressing their intention to achieve climate neutrality by 2050 and to restart economic activity post-COVID-19 by building on the Green agenda, particularly in the run up to COP-26.

As an example, we support the approach taken to date by the EU to mandate non-financial reporting by setting out essential requirements in legislation, leaving technical details to standards, while ensuring a strong enforcement regime. This mirrors the IFRS model whereby standard-setters create the standards but adoption is determined by governments.

How to move forward?

We believe it is time to consider some practical steps to enable economies to move ahead rapidly while also supporting the end goal of a global corporate reporting structure. We note that activity to consolidate existing standards, guidelines and frameworks is starting to take place. This may lead to the restructuring of the IFRS Foundation to enable the emergence of a single INSB. The pace, buy-in and eventual outcome remain uncertain. Action, if framed in an innovative, outward looking and collaborative way, can make an important contribution to a global solution.

High quality standards need to be framed by agreed over-arching ‘rules of the game’, providing a shared understanding of the goals and purposes of reporting. A solid, high-level ‘conceptual framework’ enables a consistent approach to the development, interpretation, and application of detailed standards. This is currently lacking for non-financial reporting and is needed urgently. It would provide a critical grounding for the standards, setting out fundamental concepts. Looking further ahead, consideration should be also given to the development of a broader conceptual framework for connected reporting, paving the way for an interconnected standard-setting approach for both financial and non-financial reporting.

Next steps could also lead to a ‘bridged’ approach to setting non-financial reporting standards in the mid-term, and setting international alignment and the establishment of a new corporate reporting framework.

What does a ‘bridged’ approach to standard setting look like?

We believe that a ‘bridged’ approach could lead to development of international standards, provided that they meet local legislative and market requirements. A focus on international standards would also encourage jurisdictions to take an interest in the development and adoption of such standards. Such an approach could be based on an understanding, potentially laid down in legislation, that departures from international non-financial reporting standards would be minimised, objectively justified and preferably temporary.

In practical terms, we consider that the next steps could therefore include the following:

- Explicit recognition in legislation of a preference for international non-financial reporting standards while providing a route for the development of local standards for which need has not been recognised or is not pressing at international level.
- Changes to governance, resources and working processes to ensure that the local body can call upon the best international expertise.
- A collaborative approach international frameworks and initiatives to urgently move ahead with the definition of a globally acceptable conceptual framework for non-financial reporting. This could eventually feed into the development of a global conceptual framework for connected reporting.
- Establishment of a new way of working that is open to building on standards developed by individual jurisdictions, as part of a global suite of standards.
- Agreement on a collaborative development of standards. This could refer to the ability of individual jurisdictions to request work on specific standards and/or the countries to take a ‘lead’ in certain circumstances.

How to enhance cooperation between international bodies?

Assuming that a new international non-financial reporting standard setter is set up within a broader corporate reporting framework, we think it is possible to envisage an enhanced form of working between the two bodies to ensure:

- transparency of work, with the possibility of both sides being able to input into the content of standards under development – with cooperation being ensured through respective internal rules of procedure;
- avoidance of duplication of work, enabling expertise to be focused and used in an efficient manner;
- a more rapid process of development and maintenance of standards, by establishing early consensus; and
- shared commitment to ensure the appropriate involvement of all relevant interested parties and stakeholders.

Specific steps to encourage enhanced technical cooperation, could include:

- regular exchange of information, including on draft proposals;
- mutual representation at technical working level;
- clarity over likely future work programmes, including an overview of the standards which are deemed necessary;
- annual assessment of global alignment efforts, with reference to new, agreed standards, as well as an overview of the collaborative working arrangements in practice; and
- provision for a mechanism to flag issues of concern.

What are the implications of a 'bridged' approach to standard setting?

Importantly, the potential implications of a more 'bridged' approach to non-financial reporting standard setting could include the following -

- Acceptance that jurisdictions can make formal requests to an international non-financial reporting standard setter for the development of specific standards that should be responded to positively or negatively.
- An understanding that if there is not sufficient interest and/or urgency at the international level, then the standard-setting process at a local level can kick in.
- A willingness to consider and/or build on local standards that are authoritative, of high quality and globally relevant as international standards.
- Recognition that such an approach would require closer working with other individual jurisdictions' authorities and stakeholders, as well as the establishment of more structured feedback mechanisms.

Our next steps - contributing to the debate:

Now is the time to act. This is demanded by the nature and urgency of the combined challenges posed by the COVID-19 pandemic, the climate and biodiversity emergencies and increasing inequality within societies. Requiring better non-financial disclosures can help organisations to deliver meaningful change with the urgency and scale required.

While we believe that active steps need to be taken immediately to start the process of developing a global corporate reporting structure, achieving effective and sustainable international change will take time. We can play a critical role in catalysing and supporting international efforts in this direction as well as pursuing change globally. Moreover, in recognising the momentum for action, we hope that the practical, short to medium-term steps that we have set out in this report can further encourage a phased yet aligned international approach towards interconnected standard setting.

IR “Reaching Maturity” in Sri Lanka

By Nuradhi Jayasiri, University of Colombo

In the wake of economic, social and environmental challenges, especially the global economic crisis of 2007, there has been a call for more transparent reporting, urging a clear global need for greater coherence in corporate reporting. Integrated reporting (IR) arose with the desire to promote and deliver market resilience through financial stability and sustainable development needs. IR is intended to underpin both of these corporate reporting needs of the 21st century. As stated in the IR framework by IIRC, the heart of IR relies on financial factors and a wide range of non-financial factors in order to create and sustain value for the organisation itself and for other stakeholders.

The trend analysis below gives the overall picture as to how IR has been adopted by the Sri Lankan listed companies over the nine-year period from 2010 to 2018.

Table 1: IR adoption in Sri Lanka (SL)

Sector	**No. of listed companies adopted IR**								
	2010	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**
Bank Finance and Insurance		1	2	8	17	22	25	24	25
Beverage Food and Tobacco						2	5	7	9
Chemicals and Pharmaceuticals						1	1	0	0
Construction and Engineering				1	2	2	2	2	2
Diversified Holdings			2	3	5	5	5	6	7
Footwear and Textiles						1	1	1	1
Health Care					1	1	2	3	3
Hotels and Travels			1	1	2	4	4	4	6
Investment Trusts								0	1
Land and Property								1	2
Manufacturing					1	2	6	9	12
Motors		1	1	1	1	1	1	1	1
Plantations				2	3	3	4	4	5
Power and Energy					1	1	3	4	4
Services						1	1	3	3
Telecommunications				1	1	1	1	1	1
Trading							1	1	2
Total IR adopted companies	0	2	6	17	34	47	62	72	84

As in Table 1, IR is well taken by Sri Lanka, for example, in 2011, while only 2 companies had started to adopt IR, in the following year, the number of IR adopters rose to 6 and then to 17 by 2013. Then that number doubled to 34 in 2014 and then rose to 47 in 2015. In 2016, the number of IR adopters further proliferated to 62. 10 more companies in 2017 and then 12 more companies in 2018 boarded on IR while mounting to 72 and 84 adopters in 2017 and 2018 respectively. It is also noted that among the IR adopters, nearly or more than 50% of them were found in the 'bank, finance an insurance' sector, while the remaining represented other sectors. This is shown in Figure 1 as well.

When identifying the early adopters of IR, it should also be noted that the official proclamation of the IIRF took place in December 2013, although several drafts of the framework have been issued since 2011. Academic scholars claimed that these early adopters were most likely to be companies that already had sustainable strategies and so for them IR was the logical way to report on these strategies.

Table 2 gives an understanding of the level of adoption of IR in each year out of the total number of listed companies in CSE since 2010.

Table 2: IR adopters out of total listed companies

No. of companies	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**
Total CSE listed companies	241[1]	272[1]	287[1]	289[1]	292[1]	296[1]	295	295	298
Total IR adopters	0	2	6	17	34	47	62	72	84
% of adoption	0	1	2	6	12	16	21	24	28

As shown in Figure 1, the percentage of adoption level out of the total listed companies grew from 1% in 2011 to 21% in 2016 over five years. In 2011, only 2 out of 272 listed companies adopted IR (1%) and gradually the percentage of adoption increased to 2% in 2012 and then 6% in 2013. The percentage of adoption increased two-fold from 2013 to 12% in 2014 with the 34 timely adopters of IR out of 292 listed companies. Out of 296 listed companies, only 47 companies adopted IR in 2015 with a 16% of adoption level, in 2016, it moved up to 62 out of 295 listed companies with a 21% of level of adoption. By 2017, one quarter of CSE listed companies have adopted IR. Although the overall level of adoption shows an increasing trend as shown in the line graph in Figure 1, the total adoption in 2018 was 28% of the total listed companies in CSE.

[1] Based on past studies

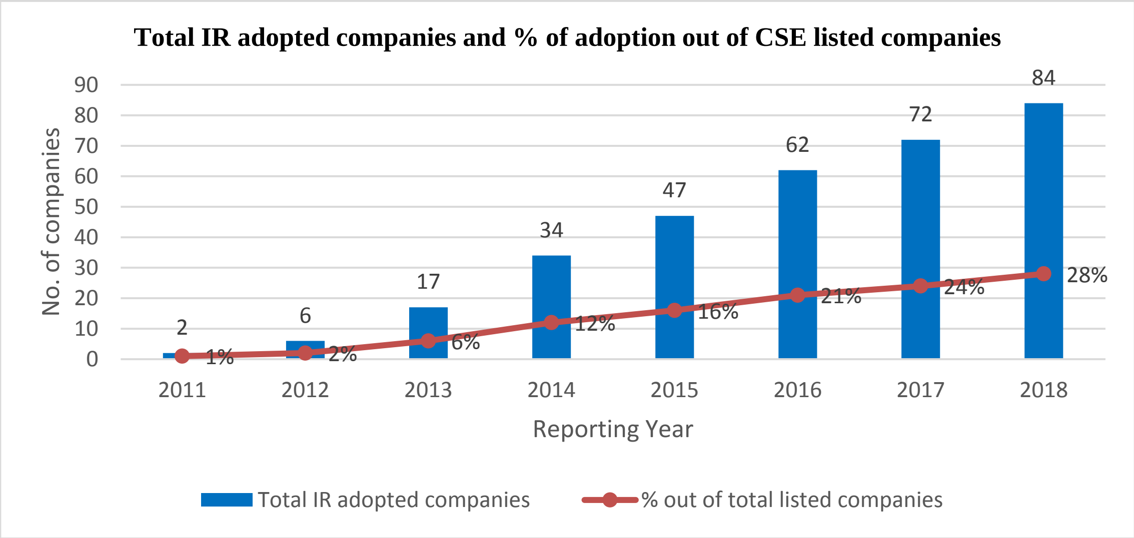

Figure 1: Trend of IR and level of adoption of IR out of total listed companies in Sri Lanka (Source: Author)

Further evidence is in Figure 2 showing how IR has grown sector-wise[2]. In 2014, half of the adopters represented the 'Bank, finance and insurance' sector while 5 companies in 'Diversified holdings', 3 from 'Plantations', 2 each from 'Construction and engineering' and 'Hotels and travels' and, one company represented 'Healthcare', 'Manufacturing', 'Motor', 'Power and energy' and 'Telecommunications'. Similarly, it was also found that majority of the companies registered in IIRC's IR Examples Database have represented 'Financial Services' sector. This majority has not dominated by high environmental impact industries while drawing out the idea that this is quite different from what is claimed in the literature where companies with a high environmental and social impact tend to report more on non-financial or social and environmental reporting.

[2] This sector-wise analysis has carried out prior to the GICS classification at CSE.

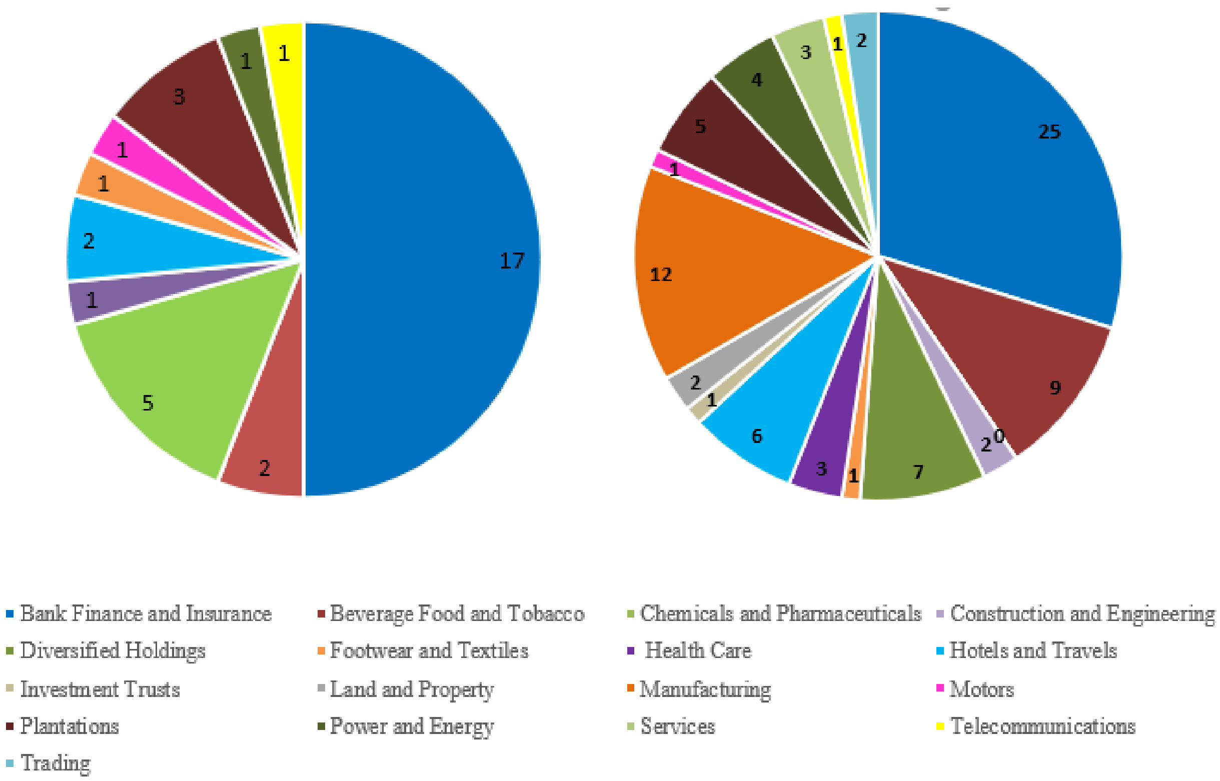

Figure 2: Comparative Sectoral analysis of IR timely adopters in 2014 and 2018 (Source: Author)

The majority in 2018 were also from the 'Bank, finance and insurance' sector followed by 15 other sectors as shown in Figure 2. This provides the conclusive idea that IR adopted Sri Lankan listed companies are widespread in different sectors.

Figure 3 depicts the trend of the number of adopters of IR and the number of companies which followed the IIRF through the period 2010 to 2018 in Sri Lanka. In December 2013, the IIRC proclaimed the IR framework (IIRF) to assist the companies in preparing their integrated reports

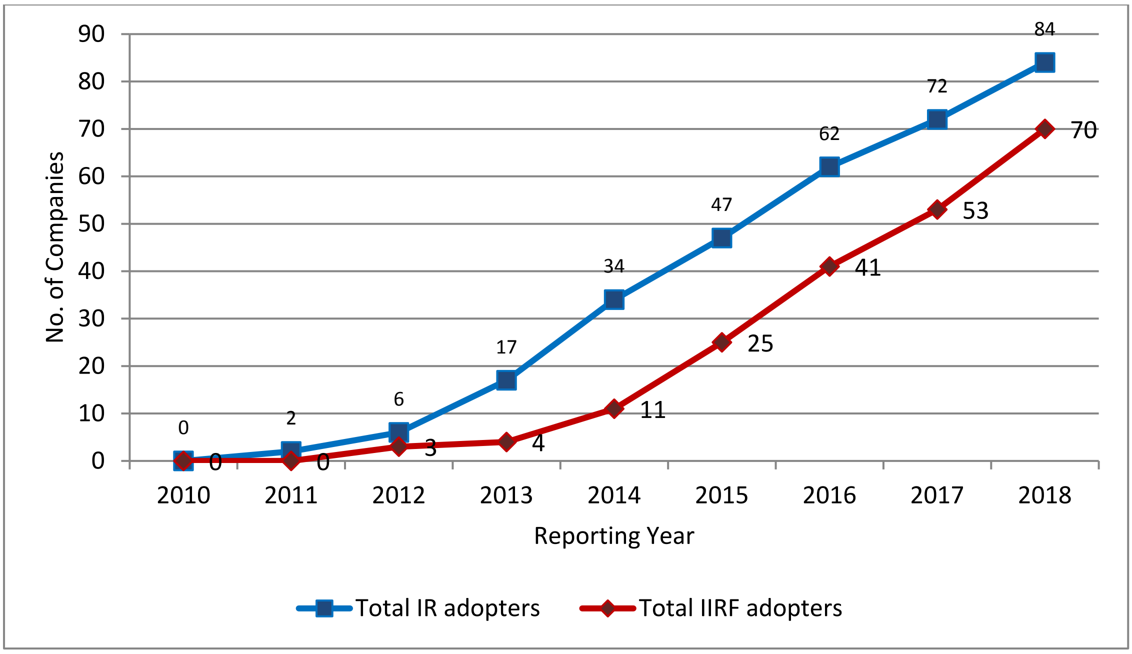

Figure 3: Adoption of IR and IIRF by Sri Lankan listed companies (Source: Author)

Figure 4 also shows the total number of adopters and non-adopters of IIRF among the total number of companies who embraced IR over the nine-year period together with the percentage of IIRF adoption out of the total number of companies who prepared integrated reports. Non-adopters of IIRF are the ones who have not stated of IR framework (IIRF) in their integrated/annual reports.

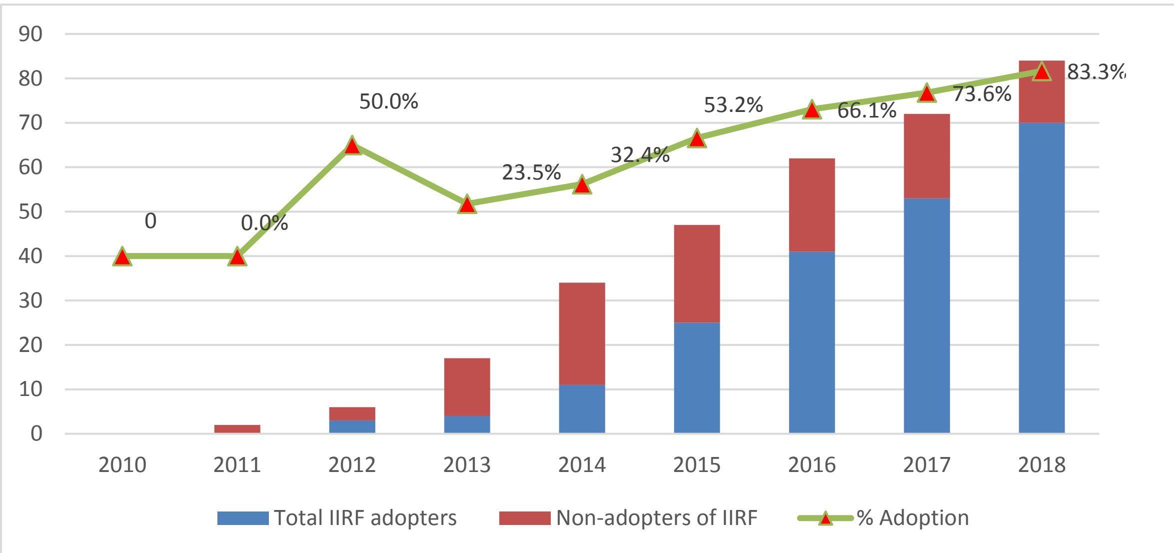

Figure 4: Total number of adopters and non-adopters of IIRF and % of adoption (Source: Author)

The Former CEO of IIRC stated that “the worldwide shift for businesses to integrate their external relationships and resources into their financial reporting is now on the path to maturity in Sri Lanka”.

He continued stating that:

“Businesses wanting to meet the challenge of international competitiveness, better manage staff turnover and inclusiveness, and to embrace global sustainable development goals, can use integrated reporting as a tool for delivery. My message is that this delivers not just for individual businesses locally, but for the Sri Lankan economy as a whole. Whether it is for trade, for attracting investment, or simply for the reputation of having practices which reflect the best international benchmarks, integrated reporting can be part of Sri Lanka’s future economic success”.

Thus, with other fast-growing economies across Asia, IR can be a key driver for developing Sri Lanka’s capital markets, which itself leads to accelerated economic growth. This makes an urging need to adopt IR as a framework that provides a holistic view of the corporate value creation process in their capital market strategies.

International <IR> Framework Revision - January 2021

After an extensive consultation process with preparers, users and other relevant stakeholders, IIRC revised the International <IR> Framework in January 2021 and the International <IR> Framework (January 2021) supersedes the International <IR> Framework (December 2013). This latest version applies to reporting periods commencing 1 January 2022. Earlier application is encouraged. Significant revisions to the 2013 framework are listed below.

1. Responsibility for an Integrated Report - Part I Section 1G

An integrated report should include a statement from those charged with governance that includes:

- An acknowledgement of their responsibility to ensure the integrity of the integrated report.
- Their opinion or conclusion about whether, or the extent to which, the integrated report is presented in accordance with the <IR> Framework.

Where legal or regulatory requirements preclude a statement of responsibility from those charged with governance, this should be clearly stated.

Where an organization is in the process of adopting the <IR> Framework, it is appropriate to identify which requirements have not been applied and the reasons why.

In applying a statement from those charged with governance, the organization will take into account its own governance structure, which is a function of its jurisdiction, cultural and legal context, size and ownership characteristics. For example, some jurisdictions require a single-tier board, while others require the separation of supervisory and executive/management functions within a two-tier board. In the case of two-tier boards, the statement of responsibility is ordinarily provided by the body responsible for overseeing the strategic direction of the organization. It is important to consider the intent of a statement from those charged with governance, which is to promote the integrity of the integrated report through the commitment of the body responsible for overseeing the strategic direction of the organization.

In cases where legal or regulatory requirements preclude a statement of responsibility from those charged with governance, an explanation of measures taken to ensure the integrity of the integrated report can provide important insight to users. Accordingly, disclosures about the process followed to prepare and present the integrated report are encouraged. Such disclosures can include:

- Related systems, procedures and controls, including key responsibilities and activities
- The role of those charged with governance, including relevant committees.

Process disclosures are encouraged as a supplement to a statement of responsibility from those charged with governance as this information indicates measures taken to ensure the integrity of the integrated report.

2. Outcomes - Part 2 Section 4.19 and 4.20

An integrated report describes key outcomes. Outcomes are the internal and external consequences (positive and negative) for the capitals as a result of an organization's business activities and outputs. The description of outcomes includes:

- Both internal outcomes (e.g. employee morale, organizational reputation, revenue and cash flows) and external outcomes (e.g. customer satisfaction, tax payments, brand loyalty, and social and environmental effects).
- Both positive outcomes (i.e. those that result in a net increase in the capitals and thereby create value) and negative outcomes (i.e. those that result in a net decrease in the capitals and thereby erode value).

A simple example illustrates the distinction between outputs and outcomes, and the importance of a balanced consideration of outcomes.

An automotive manufacturer produces internal combustion engine cars as its core output. Positive outcomes include increases in financial capital (through profits to the company and supply chain partners, shareholder dividends and local tax contributions) and enhanced social and relationship capital (through improved brand and reputation, underpinned by satisfied customers and a commitment to quality and innovation).

Negative outcomes include adverse consequences for natural capital (through product-related fossil fuel depletion and air quality reduction) and reduced social and relationship capital (through the influence of product-related health and environmental concerns on social licence to operate).

An integrated report presents outcomes in a balanced way. Where practicable, it supports the organization's assessment of the use of and effects on the capitals with qualitative and quantitative information.

3. Value creation, preservation or erosion instead of Value Creation – Part 1 Section 2B

The new <IR> Framework replaces the terminology "Value Creation" by "Value Creation, Preservation or Erosion".

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