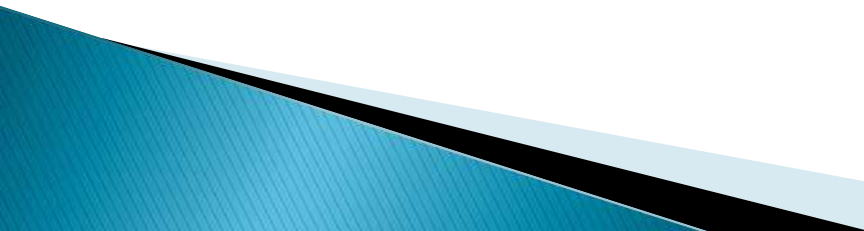


Communicating Value in 21st Century

Prashant Saran



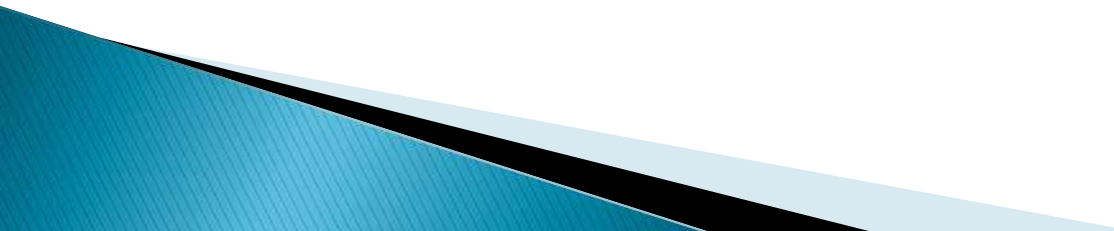
Accounting seen as manner of Communication of Value

- ▶ Accounting has been in vogue since time immemorial
 - ▶ Early accounts served mainly to assist the memory of the businessperson and the audience for the account was the proprietor or record keeper alone.
 - ▶ 15th Century Italy– Bigger Ventures needed multiple investors.
 - ▶ Simple recording of transactions did not make sense to investors
- 

Double Entry Accounting

- ▶ 1494 –Luca Pacioli– *Summa de arithmetica, geometria, proportioni et proportionalità*
- ▶ Pacioli is often called the "father of accounting" because he was the first to publish a detailed description of the double-entry system, thus enabling others to study and use it.

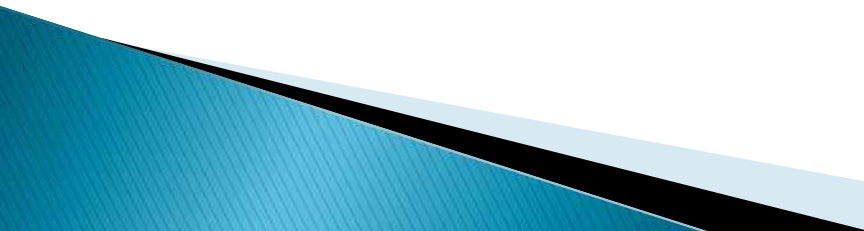
Traditional (British) Approach

- ▶ Personal account: Debit the receiver and credit the giver
 - ▶ Real account: Debit what comes in and credit what goes out
 - ▶ Nominal account: Debit all expenses & losses and credit all incomes & gains
- 

American System

- ▶ **Assets = Liabilities + Capital**
 - **Assets Accounts:** debit increases in assets and credit decreases in assets
 - **Capital Account:** credit increases in capital and debit decreases in capital
 - **Liabilities Accounts:** credit increases in liabilities and debit decreases in liabilities
 - **Revenues Accounts:** credit increases in incomes and gains and debit decreases in incomes and gains
 - **Expenses Accounts:** debit increases in expenses and losses and credit decreases in expenses and losses

Other Accounting Concepts that communicated true value

- ▶ Communicating stock and flow
 - ▶ Depreciation
 - ▶ Cost Accounting
 - ▶ Transfer pricing,
 - ▶ Overhead allocation to each product
 - ▶ Cash/ Fund Flow Statements
 - ▶ Present Value – Discounted Cash Flow
 - ▶ Zero Based Budgeting
 - ▶ Spread Sheets– What if scenarios
- 

Fair Value Accounting



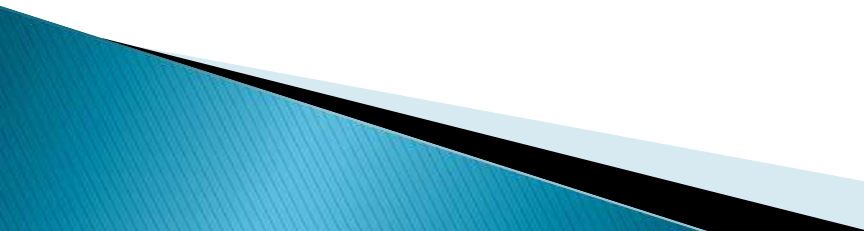
Definition–Fair Value

▶ IAS 39

- Fair Value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction”

▶ IFRS 13

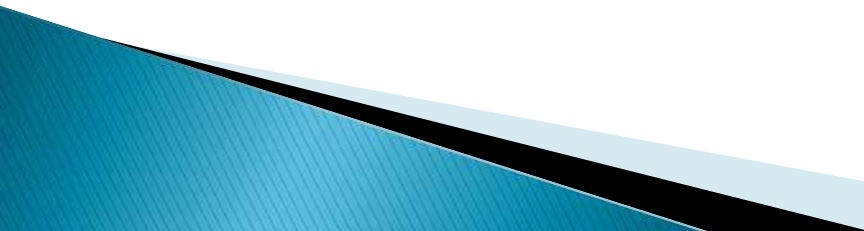
- The price that would be received to sell an asset or paid to transfer a liability in an **orderly transaction** between **market participants** at the measurement date”
- Emphasises that fair value is a market based measurement, not an entity specific measurement
- No distress sale

- ▶ Own Credit Risk in measurement of liability
 - Settlement basis under IAS 39
 - Transfer settlement
 - ▶ Derivatives
 - Adjustment for CVA or DVA
 - $CVA = \text{Potential Future Exposure} \times PD \times LGD$
 - ▶ Hedge Accounting
 - Adjustment of own credit risk for hedge effectiveness
 - ▶ Mid market pricing
- 

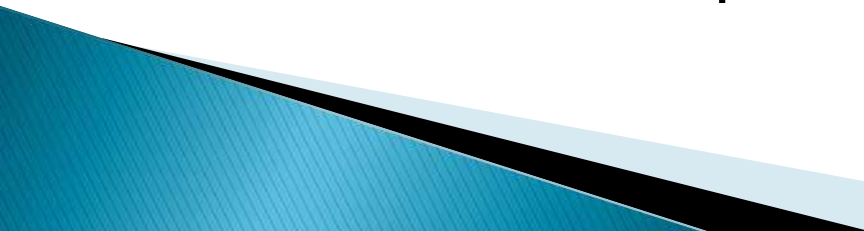
Fair Value Hierarchy

Level	Description
Level 1	Quoted Prices (unadjusted) in active markets for identical assets or liabilities
Level 2	Inputs other than quoted prices included within Level 1 that are observable for asset or liability, either directly (i.e. as a price) or indirectly (i.e. derived from prices)
Level 3	Inputs for the asset or liability that are not based on observable market data (UNOBSERVABLE INPUTS)

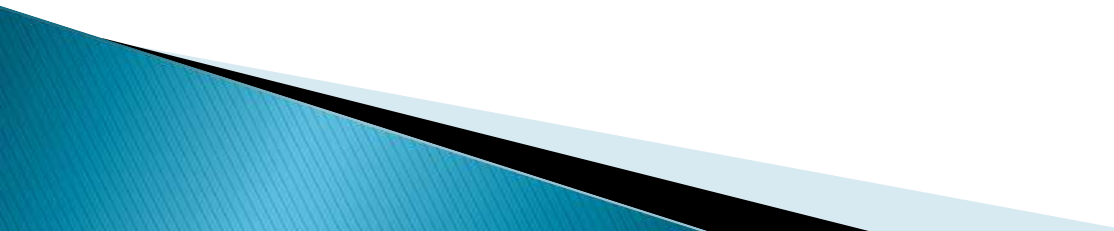
Arguments for Fair Value

- ▶ Provides relevant information
 - ▶ More accurate, timely and comparable than amounts reported under existing alternative accounting approaches
 - ▶ Updated on a regular and ongoing basis
 - ▶ Results in income figures which are of enhanced value – both in terms of stewardship and predictive value
 - ▶ Helps bring accounting and risk management in alignment
 - ▶ Greater transparency
- 

Arguments against fair value

- ▶ Unreliable as may not be based on arm's-length transactions
 - ▶ Developing reliable methods of measuring that investors trust is critical and may be a challenge
 - ▶ Market inefficiencies, behavioural biases and investor irrationality may reduce the usefulness
 - ▶ Pressures on management to mitigate the effects of fair value
 - ▶ Distinction between fair value gains and losses occasioned by the activities of the management and those otherwise occasioned may be difficult
 - ▶ Difficulties in separation of windfall gains
- 

Arguments against Fair Value

- ▶ Volatility
 - ▶ Reporting losses could be misleading if they are temporary and may reverse as markets return to normal
 - ▶ Communicating with stakeholders the effect of fair value accounting is challenging
 - ▶ Contagion effect
- 

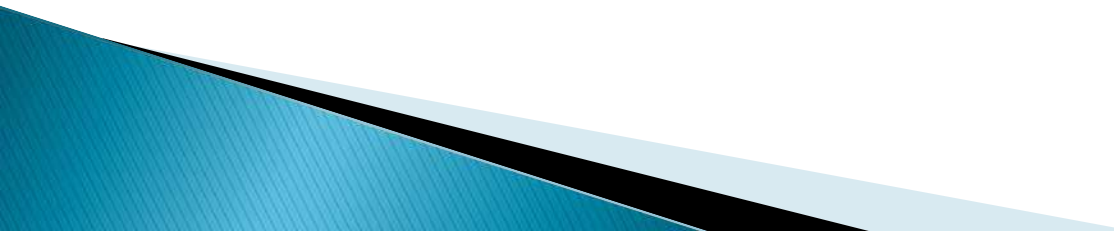
Sustainability Reports



Communicating Value Beyond Money

- ▶ 23 BC – The Deeds of the Divine Augustus
- ▶ It quantified his public expenditure
 - distributions to the people,
 - grants of land or money to army veterans,
 - building of temples,
 - religious offerings,
 - theatrical shows and gladiatorial games.
- ▶ The aim was not to account to anyone but convey Emperor's munificence

National Voluntary Guidelines

- ▶ Released by MoCA in 2009 revised in 2011
 - ▶ Applicability to all irrespective of size, sector or location
 - ▶ All principles are equally important and indivisible and to be adopted comprehensively
 - ▶ Reporting framework made on Apply or Explain basis
- 

Principle 1: Businesses should conduct and govern themselves with Ethics, Transparency and Accountability

Revenue growth and market access	New Customers, Business Partner of Choice
Cost savings and productivity	Reduced cost of ambiguity Reduced litigation
Access to Capital	Attractive to investors, banks Attractive to financial markets
Risk Management and License to Operate	Positively seen by communities, NGOs, local governments, regulators
Human Capital	Attract and retain employees
Brand Value/ Reputation	Positively seen by customers, regulators, media

Principle 2: Businesses should provide goods and services that are safe and contribute to sustainability throughout their life cycle

Revenue growth and market access	New customers Customer loyalty
Cost savings and productivity	Efficiency gains across the value chain –procurement, production distribution, after–sales
Access to Capital	Investors feel assured that liability issues are minimized. Sustainable Production attracts
Risk Management and License to Operate	Reduced risk of action from regulators and NGOs
Human Capital	Employee morale is high due to working to improve the quality of life of customers/community
Brand Value/ Reputation	Better brand identity New found USP

Principle 3: Businesses should promote the wellbeing of all employees

Revenue growth and market access	Business partner of choice
Cost Saving and Productivity	Increased productivity High morale Less absenteeism
Access to Capital	
Risk Management and License to Operate	Improved Labour Relations leading to less disruptions
Human Capital	Attracts and retains employees. Reduces tardiness and absenteeism
Brand Value/ Reputation	Employer of Choice

Principle 4: Businesses should respect the interests of, and be responsive towards all stakeholders, especially those who are disadvantaged, vulnerable and marginalised

Revenue growth and market access	Customer demand– market share increase and long term ability
Cost Saving and Productivity	Efficiency gain across value chain, procurement, production and distribution
Access to Capital	Attractive to banks and financial market
Risk Management and License to Operate	Positively seen communities, NGOs, governments and regulators
Human Capital	People drawn to work for a sensitive employer
Brand Value/ Reputation	Positively seen by customers, media and regulators. Enhances corporate cache

Principle 5: Businesses should respect and promote human rights

Revenue growth and market access	Business Partner of choice
Cost Saving and Productivity	Minimized litigation
Access to Capital	Attractive to investors, banks and financial markets
Risk Management and License to Operate	Positively seen by communities and NGOs. Lessened chance of non compliance
Human Capital	Talent attracted to a corporate which upholds dignity of all
Brand Value/ Reputation	Positively seen by customers, regulators and media

Principle 6: Business should respect, protect, and make efforts to restore the environment

Revenue growth and market access	sustainability oriented buyers will prefer to deal with organization
Cost Saving and Productivity	Less Danger of externalities emerging as liabilities
Access to Capital	Attractive to investors, banks and financial markets
Risk Management and License to Operate	Positively seen by local governments, NGOs and regulators
Human Capital	Talent is attracted to the company
Brand Value/ Reputation	Positively seen by customers, Media and regulators

Principle 7: Businesses, when engaged in influencing public and regulatory policy, should do so in a responsible manner

Revenue growth and market access	Growth stimulated due to openness and trust
Cost Saving and Productivity	Blunt the possibility of others using policy to stymie business.
Access to Capital	Openness will attract investors committed to good governance
Risk Management and License to Operate	Positively seen by civil society
Human Capital	People drawn to working in an open firm
Brand Value/ Reputation	Positively seen by customers, regulators and media

Principle 8: Businesses should support inclusive growth and equitable development

Revenue growth and market access	New Customers, Market Expansion Innovative thinking stimulated
Cost Saving and Productivity	New models will emerge to effect cost savings
Access to Capital	New sources of funding such as social venture funds
Risk Management and License to Operate	Enhanced governmental and stakeholder support conducive to business growth.
Human Capital	Potential source of new employees
Brand Value/ Reputation	Positively seen by customers, regulators and media

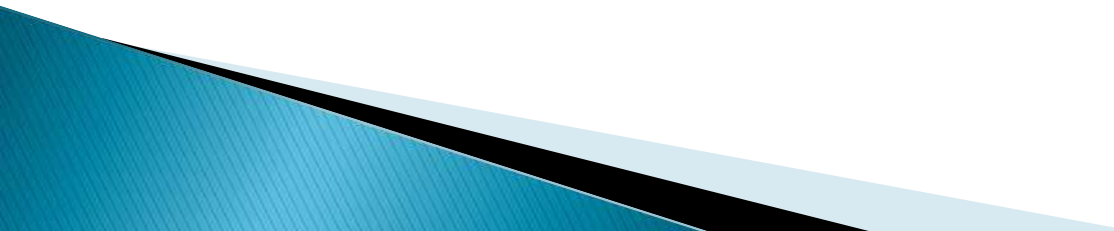
Principle 9: Businesses should engage with and provide value to their customers and consumers in a responsible manner

Revenue growth and market access	New Customers and customer loyalty
Cost Saving and Productivity	New markets brought into fold
Access to Capital	Investors back a growing firm
Risk Management and License to Operate	Lower risk of consumer action
Human Capital	Talent will be drawn to a growing firm
Brand Value/ Reputation	Customers conceive the brand favourably

Reporting Structure

- ▶ A–General Details
- ▶ B–Principle–wise details
 - Board/Committee structure
 - Recyclable Materials, Energy Efficiency, Copyrights
 - Contract Labour/Women/Disabled/Least Wage/Skill
 - Identify and have a dialogue with stakeholders
 - Policy on Human Rights
 - Percentage of Recycled raw material, Energy consumed greenhouse gases, Renewable energy, effluents
 - Policy Advocacy Statement
 - Community Investment and Goals
 - Labeling and Customer Complaints
- ▶ C–Negative Consequences and Goals

SEBI Guidelines

- ▶ Mandated NVG for top 100 listed companies
 - ▶ Those submitting International Reports not to have separate reports but only map
 - ▶ Guidelines for reporting
 - Principle wise reporting is a little more specific and detailed
 - Top 3 products where design as incorporated ESG concerns
 - Reduction in use of resources
 - Local Procurement etc.
- 

Integrated Reporting



Integrated Reporting

- ▶ Promoted by International Integrated Reporting Council (IIRC)
 - ▶ IIRC is a global coalition of
 - Regulators
 - Investors
 - Companies
 - Standard Setters
 - Accounting Professions
 - NGOs
 - ▶ More than 1000 companies are reporting
 - ▶ Many Indian Companies such as ITC joined
- 

Integrated Reporting

▶ Applicability

- Unless unable on a/c of laws or competition ,omit but tell
 - What has been omitted
 - Why it has been omitted
 - If due to lack of data what is being done

▶ Objectives

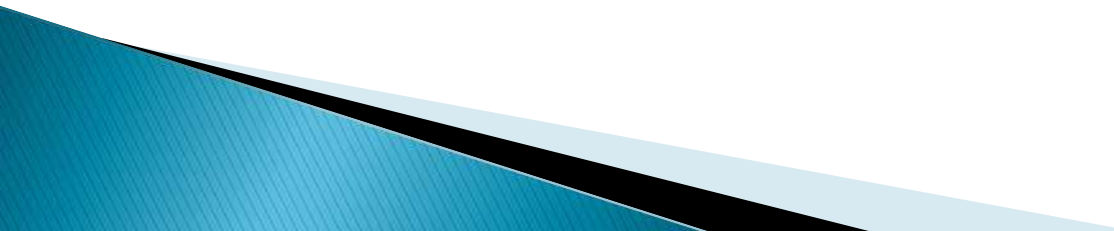
- Capture Creation of Value over time
- Accountability for use of various capitals
 - Financial
 - Manufactured
 - Intellectual
 - Human
 - Social and Relationships
 - Natural
- Support Integrated thinking

Integrated Reporting

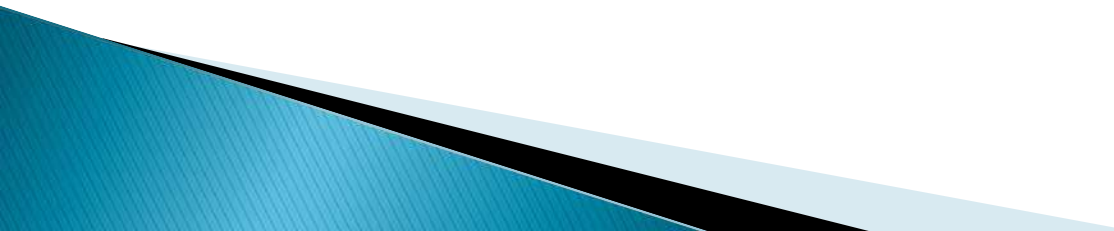
▶ Audience

- Primarily for providers of financial capital
- Also for
 - Employees
 - Customers
 - Suppliers
 - Business Partners
 - Local Communities
 - Legislators
 - Regulators
 - Policy Makers

Various Types of Capitals that are inputs and outputs of a business

- ▶ Financial
 - ▶ Manufactured
 - ▶ Intellectual
 - ▶ Human
 - ▶ Social and Relationship
 - ▶ Natural
 - ▶ Past Present and Future Value Creation depends upon these Capitals
 - ▶ Some inputs/outputs belong to organization and other to stakeholders
- 

Transformation of Capitals

- ▶ Business Models converts into products, services, by-products and waste
 - ▶ Enhanced – Profits, training, Patents, Reputation
 - ▶ Consumed– Oil
 - ▶ Modified– Pig Iron turns into steel
 - ▶ Destroyed–Environment
- 

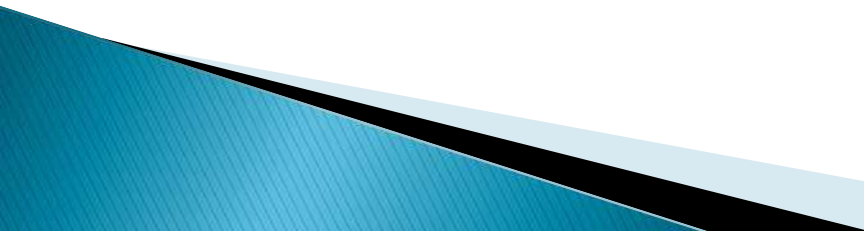
Financial Capital

- ▶ The pool of funds that is:
 - – available to an organization for use in the production of goods or the provision of services
 - – obtained through financing, such as debt, equity or grants, or generated through operations or investments.

Manufactured Capital

- ▶ Manufactured physical objects (as distinct from natural physical objects) for use in the production of goods or services, including:
 - – buildings
 - – equipment
 - – infrastructure (such as roads, ports, bridges, and waste and water treatment plants).
- ▶ Manufactured capital is often created by other organizations, but includes assets manufactured by the reporting organization when they are retained for its own use.

Intellectual Capital

- ▶ Organizational, knowledge-based intangibles, including:
 - – intellectual property, such as
 - patents,
 - copyrights,
 - software,
 - rights, and
 - licences
 - ▶ “organizational capital” such as
 - tacit knowledge,
 - systems,
 - procedures and protocols
 - ▶ intangibles associated with the brand and reputation that an organization has developed.
- 

Human Capital

▶ People's

- competencies, capabilities and experience
- motivations to innovate,
- alignment with and support for an organization's governance framework, risk management approach, and ethical values
- ability to understand, develop and implement an organization's strategy
- loyalties and
- motivations for improving
 - processes,
 - goods and services,
- ability to lead, manage and collaborate.

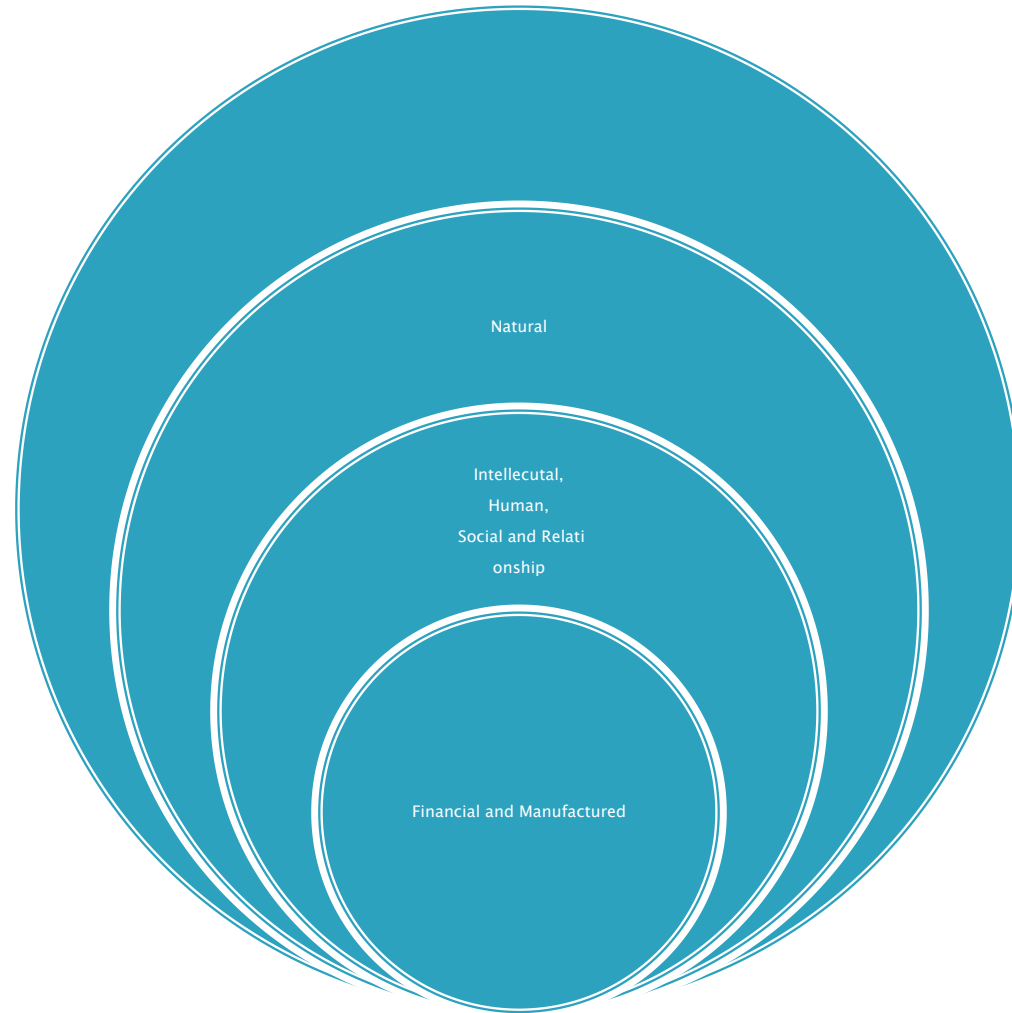
Social and Relationship Capitals

- ▶ The institutions and the relationships within and between communities, groups of stakeholders and other networks
- ▶ the ability to share information to enhance individual and collective wellbeing.
- ▶ Social and relationship capital includes:
 - – shared norms, and common values and behaviours
 - – key stakeholder relationships, and
 - – the trust of external stakeholders, such as
 - customers,
 - suppliers,
 - business partners,
 - local communities,
 - legislators,
 - regulators, and
 - policy-makers
 - – an organization's social licence to operate.

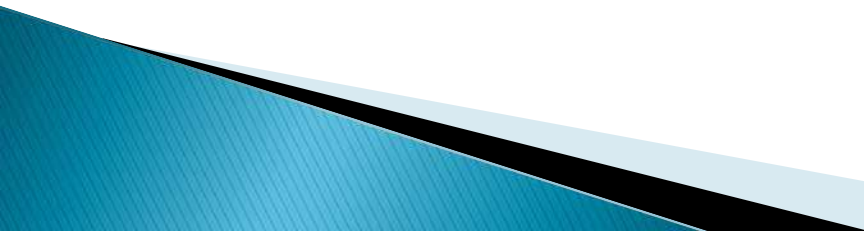
Natural Capital

- ▶ All renewable and nonrenewable environmental resources
- ▶ It includes:
 - – air, water, land, minerals and forests
 - – biodiversity and eco-system health.

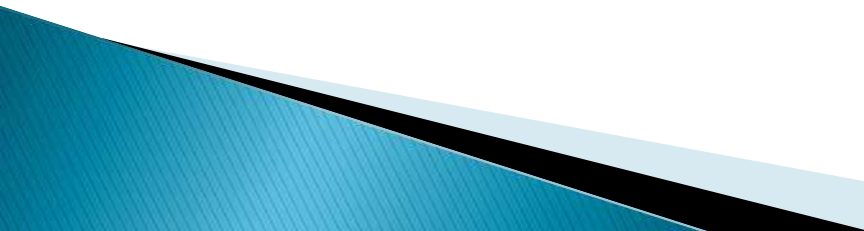
Relationships between Capitals



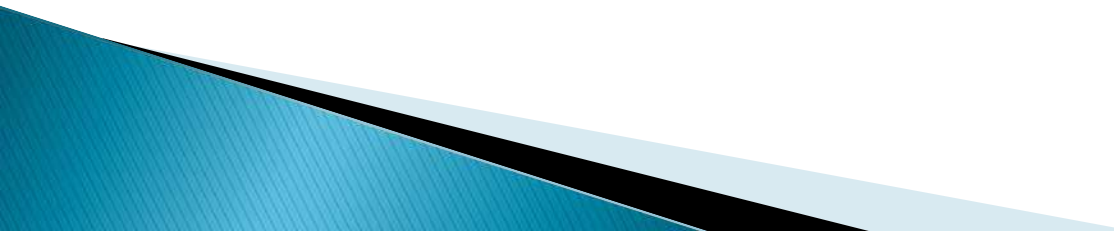
More About Capitals

- ▶ May or may not be owned by the organization
 - ▶ Quantitative Information will be useful but not essential
 - ▶ There are complex interdependencies and trade-offs between capitals
 - Creating Employment while harming environment
 - Over time i.e. choosing a course that will give a payoff later
 - Capital owned by organization and others
- 

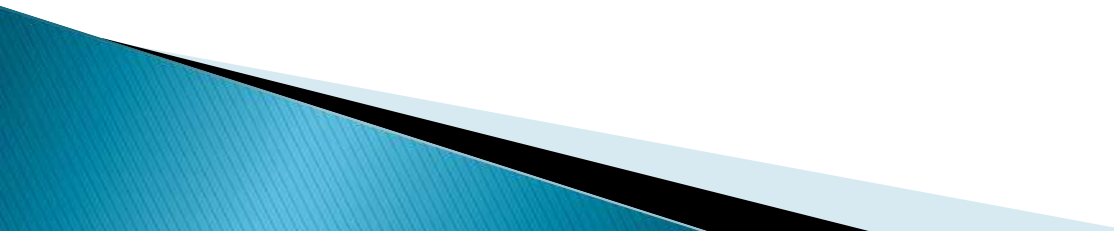
Business Model

- ▶ Sits at the Core and is the chosen system of
 - Inputs
 - Business Activity
 - Planning, Design and manufacture of products/services
 - How the organization distinguishes itself
 - Innovation culture
 - Outputs– products, services, by–products, waste
 - Outcomes– positive or negative
 - Internal – Employee Morale
 - External–Products, local community, environment
- 

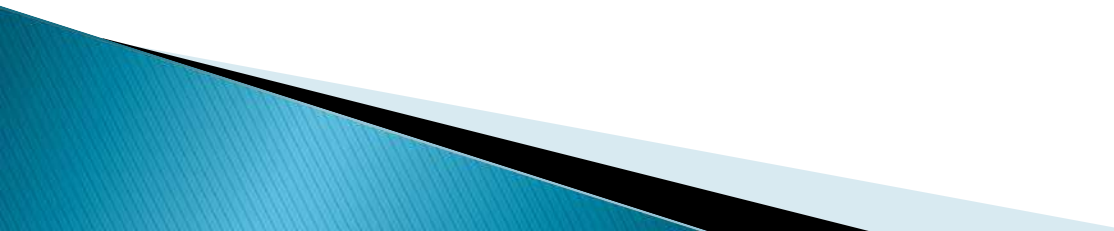
Value Creation

- ▶ Traditionally Value is Present Value of Future Cash-flows
 - ▶ In <IR> sense it is all the capitals taken together
 - ▶ Value Creation for providers of financial capital over long time will also depend on how other capitals perform
 - ▶ There may be positive or negative externalities
- 

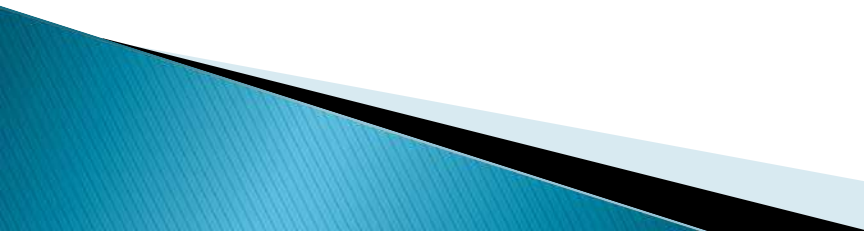
Value Drivers

- ▶ Financial drivers, such as
 - growth in sales or market share,
 - pricing strategy,
 - operational efficiency,
 - brand equity, and
 - the cost of financial capital
 - ▶ Customer relations, responses to societal expectations
 - ▶ environmental concerns,
 - ▶ innovation
 - ▶ corporate governance
 - ▶ Integrity and Trust
 - ▶ Teamwork
- 

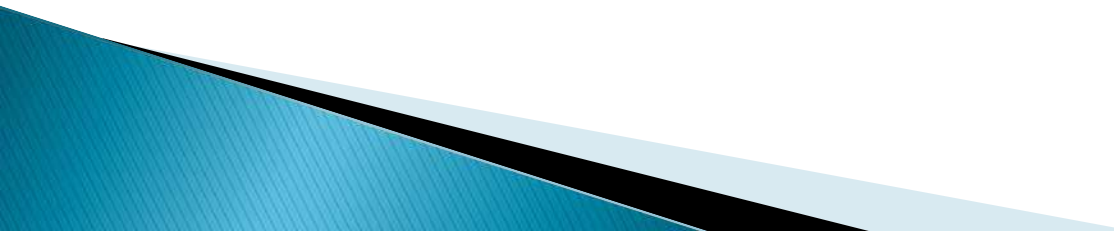
Guiding Principles of Integrated Reporting



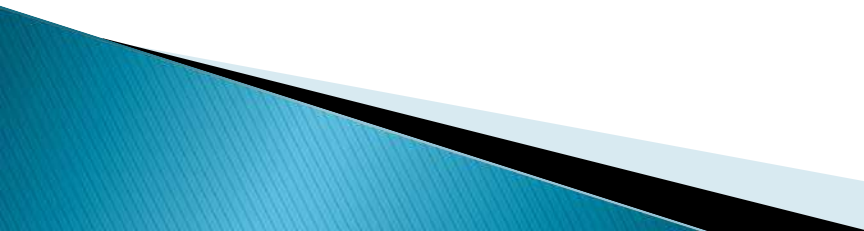
Strategic Focus and Future Orientation

- ▶ Tell Opportunities, Risks and dependencies flowing from market position and business model
 - ▶ Tell about availability, quality and affordability of various capitals
 - ▶ Avoid boilerplate disclosure
 - ▶ Unlike usual reporting, here we are reporting an uncertain future and not definite past
- 

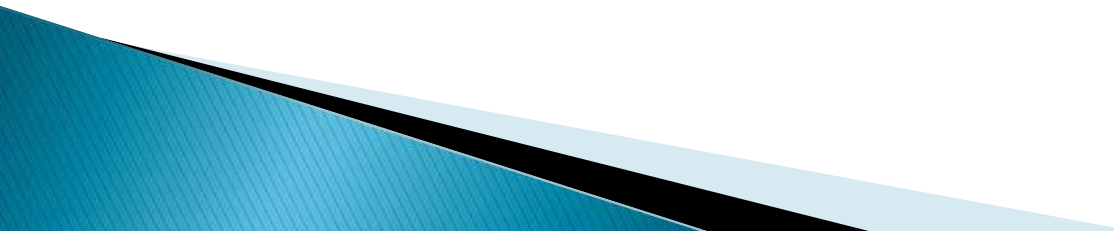
Connectivity of Information

- ▶ Tell the Comprehensive Value Creation Story with reference to content element viz.
 - external environment,
 - governance,
 - opportunities and risks,
 - strategy and resource allocation,
 - business model,
 - performance and
 - future outlook.
 - ▶ Tell how user can understand the future of organization
 - ▶ Facilitate the user to drill down and connect information
 - ▶ Tell how financial information and other information are connected
 - ▶ Give Both Quantitative and Qualitative Information
- 

Stakeholder Responsiveness

- ▶ provide insight into relationships with its key stakeholders and how the organization
 - understands,
 - takes into account and responds
 - ▶ to their
 - legitimate needs,
 - interests and
 - Expectations
 - ▶ This responsiveness may be day to day or occasional e.g. with community while planning a new plant
- 

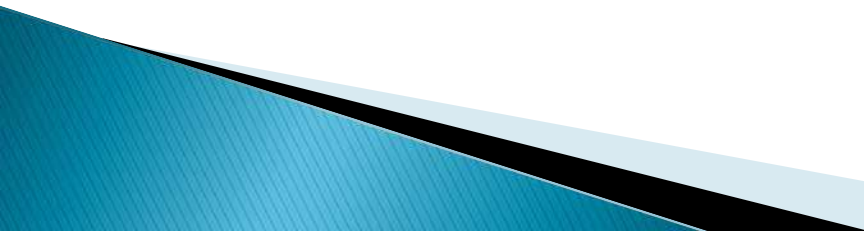
Materiality and Conciseness

- ▶ Material if likely to influence user's view of ability to create value by affecting positively or negatively
 - Strategy,
 - Business Model
 - One or more of Capitals
 - ▶ Avoid redundancy
- 

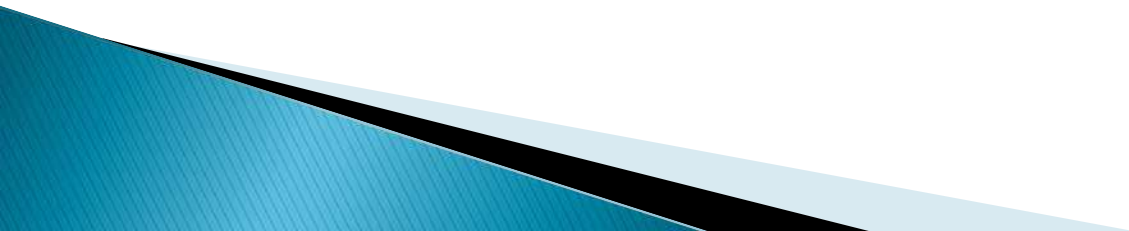
Reliability and Completeness

- ▶ Balance –
 - No bias in selection of information
 - Give equal weight to both increment and decrease in capitals
 - Report against previously reported targets and forecasts
 - Free from material error
- ▶ Completeness
 - Evaluate cost/benefit of detail and specificity of information
 - It does not mean that Competitive Advantage should be thrown out


Consistency and Comparability

- ▶ Consistency
 - Use same Key Performance Indicators
 - Explain reasons for change
 - Should reconcile with information available elsewhere
 - ▶ Comparability with others to emphasize its unique value creation story
 - Give Benchmark data
 - Present information in ratios
 - Use Common quantitative indicators
- 

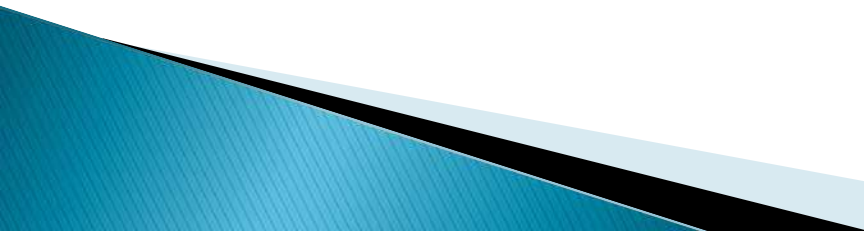
Content Elements



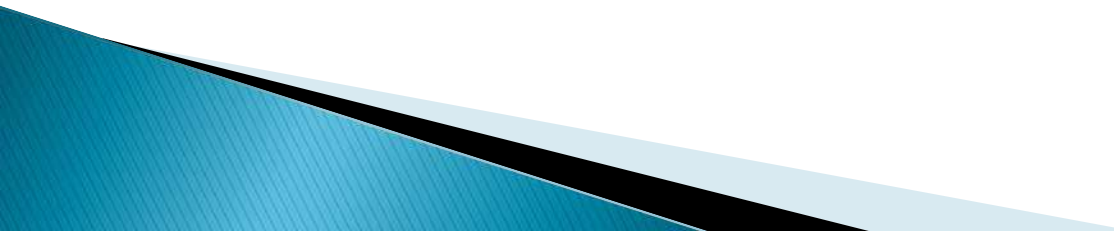
Overview and External Environment

- ▶ Overview of
 - Culture, Ethics and Values
 - Ownership and operating structure
 - Principal Activities, products and markets
 - Competitive landscape and market positioning
 - No. of employees, revenue, presence
 - ▶ External Environment
 - Macro and Micro Economic Conditions
 - Market forces
 - Technological Change
 - Societal Issues
 - Environmental Challenges
 - Legislative and Regulatory landscape
- 

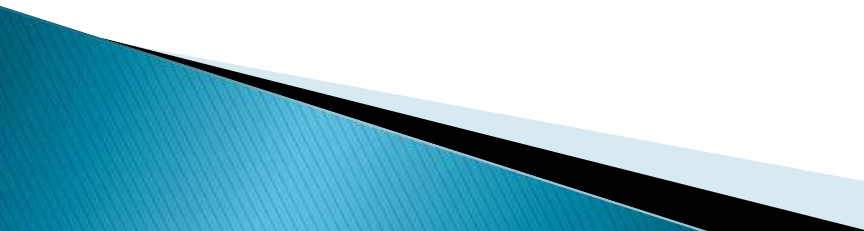
Governance – How it supports Value Creation

- ▶ Leadership Structure
 - ▶ Specific Process used to make strategic Decisions
 - ▶ How Culture, Ethics and Values are reflected in use of capitals
 - ▶ What are best practices beyond legal requirements
 - ▶ How incentives affect value creation
- 

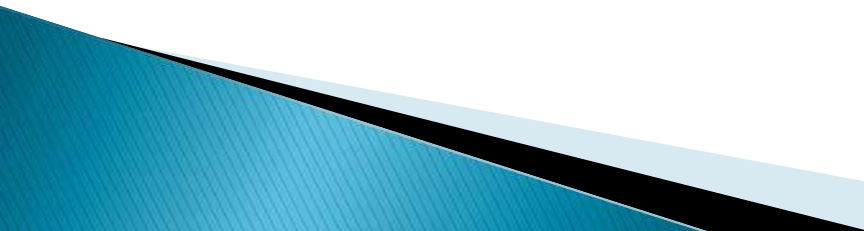
Opportunities and Risks

- ▶ Specific Source of Opportunities and Risks
 - ▶ Assessment of likelihood
 - ▶ Steps being taken to create value from opportunities and to mitigate risks
 - ▶ Risk Appetite– which risks are fundamental to create value
 - ▶ Catastrophic Risks
- 

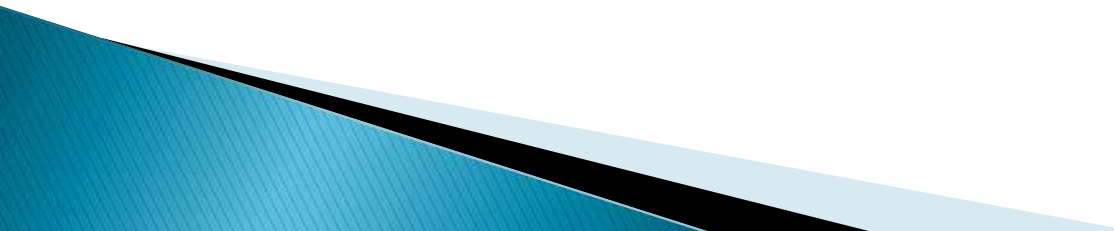
Strategy and Resource Allocation

- ▶ Where organization wants to go?
 - ▶ How does it intend to get there?
 - ▶ Linkage between strategy and Resource allocation
 - ▶ How it gets competitive advantage from
 - Innovation
 - Intellectual Capital
 - Embedding of Environmental and Social considerations in strategy
- 

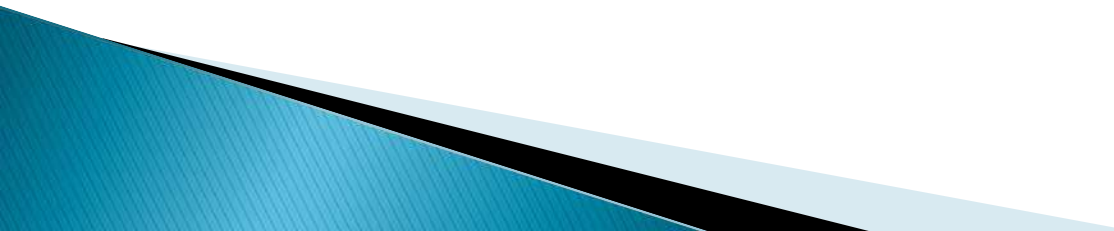
Business Model

- ▶ Key Inputs
 - ▶ Key Business Activities
 - How the organization differentiates itself
 - Revenue Generation after Point of Sale
 - ▶ Key Outputs
 - Products and Services
 - By-products
 - Waste
 - ▶ Key Outcomes
 - Internal – revenue and cash flows
 - External – customer satisfaction, brand loyalty, tax
- 

Performance

- ▶ Quantitative Indicators
 - ▶ Effect on Capitals
 - ▶ State of key stakeholder relationships
 - ▶ Linkage between current performance and future outlook
- 

Future Outlook

- ▶ Expectations from External Environment
 - ▶ How it will affect the organization
 - ▶ How the organization is equipped
- 

Thank You

