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The Adoption of Integrated Reporting and Changes in Internal Mechanisms in Japanese Companies

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Abstract

Integrated reporting (IR) is a new reporting framework established by the International Integrated Reporting Council (IIRC) that proposes the integration of financial and non-financial information in a single report. This study investigates the approaches and internal mechanisms early adopters use to implement IR, and examines whether it drives organizational change at this early stage. Data were gathered through semi-structured interviews and e-mail exchanges with the managers and employees responsible for developing integrated reports in Japanese companies with the best IR practices. The content analysis results did not uncover radical, transformative changes to reporting processes, but rather incremental changes to processes and structures that previously supported sustainability reporting. As Japanese companies traditionally hold long-term business perspectives and practices to create sustainability reports, the adoption of IR is seamless, but it may not cause radical changes to their internal mechanisms. This study contributes to IR research that focuses on internal mechanisms in the context of IR. This research also has practical implications as it highlights the best practices of IR in Japan.

Key words: Integrated reporting, Sustainability reporting, Organizational change

1 Introduction

The debate around corporate social responsibility (CSR) and sustainability in corporate information disclosure has been diversifying recently. Until now, companies published CSR and sustainability reports, and the number of companies publishing integrated reports based on the International Integrated Reporting Council (IIRC) framework is increasing. Against this backdrop, regulatory authorities and accounting professionals, in addition to the IIRC, are advocating the application of integrated reporting (IR) (de Villiers et al., 2017).

IR 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" (IIRC, 2013, p. 33). Integrated thinking is "the active consideration by an organization of the relationships between its various operating and functional units and the capital that the organization uses or affects" (IIRC, 2013, p. 2). Integrated thinking "leads to integrated decision-making and actions that consider the creation of value over the short, medium and long term" (IIRC, 2013, p. 2). 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" (IIRC, 2013, p. 4). Based on this objective, IR is a new framework for information disclosure that combines financial and non-financial information in a single report. It incorporates new ideas that could change how companies disclose information, improves investors' ability to evaluate firms' prospects, and provides solutions to address the oft-repeated criticisms of traditional accounting reporting models (de Villiers et al., 2017).

The increase in companies' use of IR has led to an increase in academic interest in the subject. Most early IR research argued for or against the idea and engaged in a normative discussion of application methods (Atkins & Maroun, 2015; Serafeim, 2015; Stent & Dowler, 2015). On the other hand, research on IR from an internal corporate perspective is limited, with the focus being on theoretical research and case studies (de Villiers et al., 2017; Jensen & Berg, 2012; McNally & Maroun, 2018; Stubbs & Higgins, 2014).

These research tendencies are the same for Japan, with no studies along the lines of Stubbs and Higgins (2014) and McNally and Maroun (2018), which were carried out in Australia and the Republic of South Africa immediately after the initial adoption of IR. Specifically, these studies investigate perspectives such as the reasons companies apply IR, the methods and use of internal mechanisms, and organizational change as a result of IR (Koga, 2015). As the IIRC states that the aim of IR is to "support integrated thinking, decision-making and actions that focus on the creation of value over the short, medium and long term" (IIRC, 2013, p. 4), we can expect its application to result in changes to organizational decision making and behavior.

However, there is a lack of research on Japanese companies in terms of the kinds of organizational changes that occur due to the application of IR given the changing state of companies and markets. As managers decided to apply IR, there is still plenty of room to discuss the effect of IR on organizational change in the context of the move from traditional performance measures that focus on financial outcomes to a more comprehensive set of indicators that express how companies manage diverse capital in the creation of sustainable returns (de Villiers et al., 2017; McNally & Maroun, 2018; Stubbs & Higgins, 2014).

In this context, we interview and exchange e-mails with the managers and employees who create integrated reports to learn the approaches and internal mechanisms their companies employ in the application of IR. We aim to determine the current organizational changes that are driven by IR. This study thus contributes to the growth of IR research that focuses on the internal aspects of the organization. By focusing on companies with best practices in IR, this study specifically contributes new knowledge on changes driven by the application of IR. The practical significance of this study is that by focusing on companies that exemplify the best practices, we may provide value for companies not only in Japan, but also worldwide.

The structure of this paper is as follows. Section 2 presents a review of the existing literature. Section 3 discusses the methods used and Section 4 presents the findings. Section 5 discusses the findings and the final section offers the study's conclusions, significance, and future research directions.

2 Literature Review

2.1 Internal Mechanisms of IR

In this section, we review the research on IR from an internal corporate perspective. Through an interview study of managers responsible for the application of IR in Australia, Higgins et al. (2014) find that such managers were cognizant of changes in the format, but not the quality of the reports. Managers understood IR as a form of storytelling that would provide system-level benefits. Higgins et al. (2014) point out that IR clearly does not influence changes in corporate norms. Similarly, Stubbs and Higgins (2014) find that the introduction of IR by early adopters in Australia did not necessarily lead to innovations in disclosure mechanisms. Their study demonstrates that no fundamental and innovative changes in reporting processes occurred; rather there were incremental changes to the structures and processes that previously supported sustainability reporting.

Prior studies also discuss the benefits of IR as an extension of sustainability reporting. For example, Parrot and Tierney (2012) discuss the case of AEP (American Electronic Power) and argue that in shining a light on the difficulty of balancing not just the profits of multiple stakeholders, but also the financial and environmental, social, and governance (ESG) aspects, the long-term perspective that IR provides can help managers accept the difficulty of balancing multiple dimensions. Further, Knauer and Serafeim (2014) find that engaging in integrated thinking and reporting supported by increases in transparency and ESG performance attracts long-term investors in their case study of Shire PLC. Furthermore, IR can lead to the formation of an organizational structure that integrates economic, social, and environmental responsibility. McNally and Maroun (2018) show that financial and non-financial accounting processes can expand the scope of existing accounting systems and promote broader management controls, as well as a more integrated conception of 'value' in reporting, even in cases in which the individuals involved in the creation of such reports did not support the changes at the early stage of its adoption.

While, as noted above, IR has both limitations and benefits, the expansion of corporate information disclosures until now shows that it holds the potential to broaden the scope of the function of financial reporting, develop a new sphere of responsibility for the organization, and transform business thinking (Gray et al., 1995; Adams & Frost, 2008; Stubbs & Higgins, 2014). Existing research focuses on the management and application of new approaches by early adopters of IR (McNally & Maroun, 2018; Stubbs & Higgins, 2014), but the numbers involved are limited (de Villiers et al., 2017; McNally & Maroun, 2018). Moreover, no studies focus on Japanese companies or companies with the best IR practices. We consider the lack of knowledge in this field and apply Laughlin's (1991) model of organizational change to investigate changes in internal mechanisms in Japanese companies that resulted from the application of IR, as in the existing literature (McNally & Maroun, 2018; Stubbs & Higgins, 2014).

2.2 Laughlin's (1991) model

Laughlin (1991) states that the process of organizational change is due to a disturbance in the external environment. Laughlin (1991) conceptualizes the organization as consisting of two intangible components and one tangible component. These components are the interpretative schemes (beliefs, values, norms, and mission/purpose related to the organization's culture), design archetypes (structures, processes, and systems), and tangible sub-systems (buildings, people, behavior, machinery, and finances) of the organization.

The assumption is that these three components are in a coherent state with a certain degree of balance, with organizational norms being the inertia that works to maintain the status quo once a balance has been achieved (Laughlin, 1991). Another assumption of the model concerns the relationship between the organization and its external environment. Under normal circumstances, the organization acts to stay in balance with the external environment; however, the environment changes periodically, which acts as a disturbance to the organization. Laughlin (1991) points out that we can observe organizational change when such a disturbance occurs.

The first-order change (morphostasis) that the disturbance causes results in changes to the original design and subsystems. It does not change the core (i.e., the DNA) of the organization, but is a transition. The second-order change (morphogenesis) affects all components. This change permeates the DNA of the organization. Laughlin (1991) posits four pathways of change: two first-order changes (rebuttal and reorientation) and two second-order changes (colonization and evolution).

The rebuttal pathway of the first-order change may include small changes to the design archetype, but the organization resists the disturbance, the design archetype returns to its original form, the relationships with the existing interpretive schemes remain, and the organization returns to its pre-disturbance state. In the reorientation pathway, the organization internalizes the environmental disturbance, which leads to a change in the design archetype and sub-systems. However, the disturbance has a limited effect on the subsystem during reorientation, meaning that the interpretive schemes at the core of the organization are not fundamentally affected.

In the second-order change, colonization occurs, whereby the design archetype and sub-systems change as a result of the disturbance and then flow on to the interpretive schemes, which a small group will force upon the organization. While a new current (the new foundation for the whole organization) forms at this stage, the organization can either welcome (evolution) or resist (colonization) the changes in the interpretive schemes. Evolution can include the reformation of the design archetype or subsystems and significant changes to the interpretive schemes. However, in contrast to colonization, the changes chosen and accepted by the organization overall are not enforced.

This classification of change is useful, for example, to classify companies that introduced environmental accounting to address changes in the external environment, such as environmental problems. The field of environmental accounting has a similar debate (Gray et al., 1995; Adams & McNicholas, 2007). Environmental accounting research of this type describes how companies change during the process of addressing environmental problems, specifically the question of whether the environmental accounting leads to changes in the design archetype or sub-systems, or further, to the interpretive schemes (da Silva Monteiro & Aibar-Guzman, 2010; Gray et al., 1995; Larrinaga-González & Bebbington, 2001; Larrinaga-González et al., 2001).

McNally and Maroun (2018) and Stubbs and Higgins (2014), as discussed above, also employ Laughlin's (1991) model to investigate the organizational changes driven by IR in the context of the move from traditional performance measures that focus on financial outcomes to a more comprehensive system that expresses how companies manage diverse capital in the creation of sustainable returns (McNally & Maroun, 2018).

In line with previous research, we employ Laughlin's (1991) model to investigate the approaches and internal mechanisms companies adopt in the application of IR to investigate whether organizational change occurred in Japanese companies at this early stage.

3 Methodology

We used data collected during detailed semi-structured interviews as well integrated reports, websites, and internal documents provided at the time of the investigation[1] to check the details of the interviews. We created an interview report, which we then had checked by the interviewee. This process strengthened the validity and reliability of the study.

We referred to awards won for IR practices as reported by Nikkei and WICI Japan to select the participant companies to ensure that our sample included companies with the best practices in IR. All companies were in the early stages (between three to five years) of the application of IR.

Table 1 presents the details of the investigation. The interviewees belonged to a range of departments, including public relations, CSR, and corporate planning, but are identical in that they were involved in the creation of integrated reports and embedding them within their companies. In the case of Company C, we also exchanged two emails

[1] The Investor Relations Department of Company B provided the meeting materials. These materials included information on the concept behind and content of Company B's integrated report.

and have their replies in addition to the interviews[2]. Company D permitted only email interaction, with one email sent and one reply received.[3]

Table 1: Interview Summaries

	Industry Type	Date	Interview Duration (min)	Division and Department	Interviewee (s)
Co. A	Retailing and Finance	March 7, 2019	120	General Affairs Division (Public Relations Department)	1. General Manager 2. Chief Leader
Co. B	Parts Manufacturer	March 27, 2019	90	1. Investor Relations Department 2. CSR Office	1. General Manager 2. Lead
Co. C	Public Sector	March 28, 2019	75	Financial Planning Division (Investor Relations Department)	Senior Manager
Co. D	Food Manufacturer	March 12, 2019	-	Corporate Planning Department	Senior Manager

We used the interview reports and e-mails from interviewees for the data analysis. We applied the content analysis method, which is a systematic coding and categorization technique for unobtrusively examining large amounts of text to determine the words and phrases, their frequencies, and their relationships, structures, and communication and discourse from the perspective of the research question (Vaismoradi et al., 2013). This method can be employed to describe the characteristics of the content of a text by investigating "who" said "what" to "whom," and with what kind of effect (Vaismoradi et al., 2013). In the case of exploratory research of a relatively little-known phenomenon, content analysis is appropriate to uncover the common themes in the data in a simple fashion (Vaismoradi et al., 2013; Stubbs & Higgins, 2014). As previous related studies employ content analysis (McNally & Maroun, 2018; Stubbs & Higgins, 2014), we can consider it as an appropriate method for this study. We used Nvivo 12 (QSR International, Burlington, MA, USA) for the analysis. Following McNally and Maroun (2018), we analyze the data by focusing on

[2] We sent a request for participation on January 29, 2019, and exchanged e-mails about the appointment and IR on January 30 and 31, 2019 prior to the interviews.

[3] We sent a request for participation on March 5, 2019; however, in place of an interview, we received an email response from the group senior manager for corporate strategy in the corporate planning department.

the issues the interviewees discussed and the changes in the organizational processes that are noted in previous studies[4].

4 Findings

From the analysis, we derive six themes related to changes in organizational processes as applications of IR. The following presents the findings for each theme.

4.1 Background to the application of IR

The case study companies adopted IR to meet the environmental changes that it faced and to present how the company intended to employ its strengths to achieve both short and long-term goals to external actors. Company B, for example, discussed environmental change and information disclosure as follows:

> *For example, the direct mechanism was The UN Sustainable Development Goals (SDGs) and the question of how to disclose how future business risks and chances were understood and how that understanding would be applied in the operations at management level was in the background. The fact that there was a demand for reporting on how companies were going to move from social responsibility to sustainability can be considered as the background of the move to IR.* (Company B, CSR Office, Lead, March 27, 2019)

More detailed background information was also provided. Company A, for example, decided to apply IR because in addition to recovering the company's performance going forward, there was a demand for information about management policy from a long-term perspective.

> *Up until now, our company considered it a virtue not to blow our own trumpet, but there was a demand from investors to know what kind of management practices were behind our results. ...This is because there is a trend for stakeholders, including investors, to desire management that takes a long rather than short-term approach.* (Company A, General Affairs Division, General Manager, March 7, 2019)

[4] In addition, a student provided support by checking the interview reports and results of the analysis.

Furthermore, Company D adopted IR as part of a move to strengthen its group values in their pursuit to realize social and economic value.

> *After the change in company President in 2016, the new President set out a new policy to significantly strengthen Company D's Creation of Shared Value (CSV) as a core value of our various activities. Company D's CSV is a way of thinking that aims to address social issues and co-create social and economic value through business operations and refers to Company D's group values that have been cherished since its inception. The co-creation of social and economic value is, in other words, the integration of non-financial and financial aspects, and the first integrated report was published in 2016.* (Company D, Corporate Planning Department, Senior Manager, March 12, 2019)

In addition, the management principles of Japanese companies may influence the application of IR. Company B, for example, discussed the past positions of Japanese companies and the corporate values they prioritized in relation to the publication of integrated reports.

> *During the bubble, Japanese companies were on top of the world in terms of their finances and stock prices, but they declined afterwards. In that situation, the intangible assets that were the strength of Japanese companies were incomprehensible. This was true of the contribution of intangible assets to value creation. IR discloses the activities related to financial data and financial performance. It is also an effective tool to explain that corporate values and non-financial strengths and initiatives in a broad sense, such as ESG, CSR, and sanpo-yoshi[5], lead the sustainable growth of the company and*

[5] *Sanpo-yoshi* "is a managerial philosophy and creed established by the Ohmi merchants—who were active from the Edo period to the end of the Meiji period (17th–19th century)—through their daily business activities (Ohmi is a region in Japan)" (Tanimoto, 2013, p. 2107). It "translates as 'good for three parties', meaning the seller, buyer, and society. Broken down, *sanpo* refers to *urite* (= seller), *kaite* (=buyer), and *seken* (≒ society), while *yoshi* means 'good' in Japanese" (Tanimoto, 2013, p. 2107).

society in terms of value creation. (Company B, Investor Relations Department, General Manager, March 27, 2019)

Company C also noted the concept of "*sanpo-yoshi*," which was important in Japanese-style management and stated that the application of IR did not result in changes to company values.

Many company presidents and managers in Japan have been with the same organization for their entire careers, and we are at the stage now where the importance of external directors is finally becoming recognized. While the important thing is whether or not value creation is sustainable, over half of the companies worldwide with a history of over two-hundred years are Japanese companies. Actually, it is my belief that the spirit of 'sanpo-yoshi' plays the greatest part in sustainable growth. ...IR was not the trigger for changes to corporate philosophy and beliefs, it is something that has finally manifested over space-time and many generations. (Company C, Financial Planning Division, Senior Manager, January 31, 2019)

Similarly, the origin of IR in Company D was its past, and its application was a method to present its current and desired future state to investors.

I view it as a valuable communication method that invigorates dialog with institutional investors in order to sustain robust growth together by delineating the spirit and values that underpin the company (also known as its DNA), its current form as seen through financial and non-financial activities from the past to the present, its desired future state, and the course to take to realize it. (Company D, Corporate Planning Department, Senior Manager, March 12, 2019)

As illustrated above, the companies did not adopt IR because it can bring about new value. Rather, as each company had a past imbued with the principles from their time of inception, they adopted it as a concrete framework for explaining to external parties how the company will create value from a long-term perspective.

4.2 The role and value of integrated reports

Integrated reports have two roles. The first is to disclose financial and non-financial information concerning how the managers intend to run the business to create value from a long-term perspective to external investors. Company B, for example, discussed the role of IR as a method to disclose the company's strengths to those outside of the company.

> *In the context of the changing times in society and various companies starting to produce integrated reports, it was suggested, at the practical business level, by the Investor Relations Department to the executive level. There was no directive from the top. Up until then, we had expressed Company B's strengths in our annual reports, but I believe that, in accordance with the times, it become necessary to use a framework, such as the IIRC's, to express our strengths.* (Company B, Investor Relations Department, General Manager, March 27, 2019)

Second, the companies use integrated reports to cultivate employee understanding of the company's direction from a long-term perspective. Company A, which discussed this aspect in detail, uses the integrated report to create a sense of unity within the company.

> *In movements driven by "centrifugal forces," such as the move to a pure holding company system and the various operating companies in industries such as retail and finance increasing their own strengths, there was a need to for the group as a whole to also possess a "centripetal force" to increase company value.* (Company A, General Affairs Division, General Manager, March 7, 2019)

4.3 The relationship between CSR/sustainability reports and integrated reports

Integrated reports are not necessarily superior to other types of reports. They supplement the content of CSR and sustainability reports. As the target audience differs, the content of the reports differs accordingly. Rather than the integrated report being comparatively superior, each type of report has a role for its intended audience.

For example, Company A issues an integrated report and a sustainability report annually and presents the sustainability results in the integrated report. In addition, the content that it cannot include in the integrated report is included in the sustainability report.

Company A's IR is issued once a year (September) and its sustainability report is issued once a year (December). For example, the items left out of the integrated report are incorporated into the sustainability report, and the sustainability reports are incorporated into the integrated report. (Company A, General Affairs Division, General Manager, March 7, 2019)

Company B states that the reports have different readers and describes the relationship between the integrated report and the CSR report as follows.

Since the readers of the two reports are different, we issue the integrated report and the CSR report separately. The primary readers of the integrated report are investors. We issue the CSR report to a wider range of stakeholders, including employees. (Company B, Investor Relations Department, General Manager, March 27, 2019)

Company C mentioned the relationship between the CSR, environmental, and integrated reports in terms of their contents. While the CSR and environmental reports disclose only non-financial information, integrated reports are positioned to show how non-financial information and strategy are integrated.

Non-financials have been reported through the CSR report and the environmental report and shifted to reporting on ESG activities with a view to the SDGs. It is characteristic of the integrated report. (Company C, Financial Planning Division, Senior Manager, March 28, 2019)

Finally, Company D states that integrated reports are a superior way to show the picture of corporate management itself based on financial and non-financial information.

We practice non-financial and financial corporate communication using the integrated report as a gateway. For this reason, it is excellent and it is the simplest microcosm of corporate management that summarizes the essentials *of corporate management that lead to sustainable growth.* (Company D, Corporate Planning Department, Senior Manager, March 12, 2019)

4.4 The creation of integrated reports

The creation of integrated reports was smooth and carried out systematically without hinderance. Specifically, the companies created the reports after collecting all information from the relevant departments by the department in charge (e.g., Investor Relations Department).

Company A is a characteristic example. We can surmise that for Company A, this process was made smoother by the strong commitment of the company president to the creation of the integrated report and Company A's unique human resources system.

> *It is formulated as a project that works across departments. Specifically, the participants include the company president, corporate planning department, investor relations department, sustainability department, general affairs department, financial department, and ESG development department. Additionally, the reporting consultancy company participates from outside the company. The publication of the report was initiated as a coherent whole, including the corporate planning department, ESG development department, and the company president, while still maintaining a diversity of perspectives. The creation of the report in a collaborative way that traverses departments, is characteristic of the Company A group. ... A characteristic of the publication of our integrated report is that all employees involved are committed to the task. In the background to this is an atmosphere in which employees feel they can freely talk with one another, enabled by the company-wide support of job rotation and the fact that many of our employees know one another by sight. In these ways, the group company, departments, inter-departmental cooperation, information sharing, and commitment from the company president came together to enable the smooth creation of the integrated report in Company A.* (Company A, General Affairs Division, General Manager, March 7, 2019)

Additionally, Company D established a system for the creation of the integrated report. Characteristic of Company D is that the people responsible are closer to the development and execution of strategy. The support of people in these types of roles may drive the practice of IR.

> *The global corporate headquarters was launched in 2017 by consolidating the management responsible for the creation of the integrated report in the global public relations department, investor relations department, and corporate planning department under one managing director (executive in charge of financials). The director was responsible for the creation of integrated reports and for the design of the medium-term corporate strategy. Thus, the company established a structure by which both financial and non-financial information were coordinated in the process of the work being carried out.* (Company D, Corporate Planning Department, Senior Manager, March 12, 2019)

4.5 The relationship between IR and official mechanisms

The integration of the content disclosed in the integrated report with strategic and corporate planning is progressing. Rather than setting new Key Performance Indicators (KPIs) in line with the application of IR, all the companies in this study continued to employ CSR and sustainability related KPIs that they were already working towards.

Additionally, they set new targets and KPIs based on things noticed during strategic and corporate planning or IR, which they then reflect in the integrated report. The setting of KPIs related to the SDGs, which is recently attracting attention, was mentioned in the interviews. This does imply implementing completely new KPIs, rather that new KPIs that apply to important aspects that existing KPIs do not cover. Company C, for example, was integrating the content of the integrated report into the medium-term corporate plan, as described below.

> *The medium-term corporate strategy has a 5-year period set towards 2022. With regard to financials, non-financials, and the quantitative and qualitative analysis of the KPIs for such, if we think ten, twenty, or even one hundred years into the future, then non-financials are indispensable. The aim is to integrate non-financials into the medium-term corporate strategy, make contributions with other companies in the same industry, and ultimately, contribute to the SDGs. ...The ES of the ESG were already practiced in the past, with KPIs set and conformance with the medium-term strategy.*

Governance is particularly important within the ESG. For example, an indicator relating to governance is set for external directors, but the indicator is not a target; its ultimate purpose is the realization of our principles. (Company C, Financial Planning Division, Senior Manager, March 28, 2019)

However, this situation is different for each company. Company D, for example, is pursuing cutting-edge initiatives. Specifically, they are moving toward integrating the content and strategy disclosed in their integrated report with the medium-term corporate plan and objectives management.

Company D's CSV was first expressed in 2014, when the current President was in office, and from the 2014-2016 medium-term corporate plan, which started in that year, non-financial indicators (ESG-related) linked to departmental evaluation have been set for all departments within the company. It is also compulsory to have a CSV indicator set as one item (which is not linked to evaluation) in the objectives for individual employees. (Company D, Corporate Planning Department, Senior Manager, March 12, 2019)

In contrast, while Companies A, B, and C integrated the content disclosed in their integrated reports with their medium-term corporate plans and set companywide KPIs, there was a need to change official systems to make all employees aware of non-financial aspects and move them to act.

The KPIs in the medium-term corporate plan are mainly financial indicators. These KPIs are employed as long-term indicators. They are also linked to executive remuneration. …While ESG-related KPIs are reported for the entire group, currently their practice has not filtered throughout the group company, sub-organizations, and individual employees. This could be because it is difficult to see how they relate to one's everyday work, but going forward, the ideal is to set KPIs and apply them so that initiatives, including ESG, become more familiar. (Company A, General Affairs Division, General Manager, March 7, 2019)

Additionally, Company B in particular saw the question of how to set non-financial KPIs and roll them out through the entire company as a challenge.

In addition to information disclosure, there is a need to develop concrete initiatives. Last year and the year before, the position on the SDGs was limited to simply respecting them, but from April, it was decided that the new medium-term corporate plan will include seven SDG-related indicators that will be directly linked with our operations. …Until now, responsibilities have differed across the company as a whole, functional divisions, and operations departments, but there is a need to allocate authority for the seven areas across all organizations and set KPIs that can be responsibly achieved. The setting of KPIs to accompany each objective is under discussion, but I expect that the responsibilities and departments responsible for development will depend on the respective objectives. Of course, there are initiatives that are already under way that were selected according to the SDGs. It is not the case that all initiatives selected via the SDGs will result in the setting of new objectives. (Company B, Investor Relations Department, General Manager, March 27, 2019)

4.6 The penetration of and challenges for integrated thinking

All companies made use of the integrated report to disseminate the long-term management philosophy and integrated thinking presented in the report. A characteristic initiative that was observed was the selection of employees to participate in information sessions on the medium-term corporate plan. It was believed that having motivated employees participate would help the management's thinking disseminate to all employees in the field.

Additionally, we try to develop an understanding of the company direction through participation in the medium-term corporate planning development meeting. All employees can participate in this meeting. We put out a call for contributions and have employees write papers, with selected employees from each rank being able to participate. It is not always the case that employees in higher positions can attend these meetings. Sometimes, the store manager cannot attend, and a general employee attends in their place. Employees who participate in the meetings have a high desire to understand the company's direction and proactively share it in the field. (Company A, General Affairs Division, General Manager, March 7, 2019)

Even so, there is a gap between the IIRC ideals and the actual situation. In contrast to the high level of penetration reported by Company D, the other companies were striking in that they recognized the importance and necessity of embedding integrated thinking, though faced challenges to achieving this outcome. Specifically, managers and employees in the field tend to prioritize their core tasks, and thus the companies must work harder to address the situation. For example, Company A distributes the integrated report to all employees and ninety percent of them read it (at least in part). However, the degree to which the company's philosophy that reflects integrated thinking penetrates the organization differs. The reasons for this outcome include differences in the amount of information for each organization, differences in the temperament of each generation, and differences in thinking about companies and employment.

> *The degree of penetration of Company A's concept of integrated thinking differs depending on the organization. This is affected by differences in the amount of information. For example, there is a disparity in penetration and understanding between the head office, stores, and group companies. It also differs for each generation.* (Company A, General Affairs Division, General Manager, March 7, 2019)

As in Company B, some managers and employees have an interest in integrated thinking and the content of the integrated report, though it takes time for these ideas to take root in the form of organization-wide values.

> *The expansion of everyday operations based on integrated thinking is still in progress. Specifically, the link between integrated thinking in the form of CSV-type ideas and business strategy is still under development. As the company needs to aspire to a form where it can guarantee and reinforce the sustainable growth of the world, society, and company (i.e., sustainability), the integrated report does not represent the state of our company at this point in time. As a future-focused company, it will have little meaning without sustainable activities that are connected with increases in the value of the company and the strengthening of such links.* (Company B, Investor Relations Department General Manager, March 27, 2019)

Similarly, the characteristics of Company C's business make the spread of integrated thinking throughout the company difficult due to the need for balance with everyday operations.

> *Our staff in the field place the utmost priority on the short-term safety of the customers right in front of them. In such a situation, the question of how to link what they prioritize in the short term with a longer-term perspective in order to realize our principles is a challenge.* (Company C, Financial Planning Division, Senior Manager, March 28, 2019)

5 Discussion

Despite the four companies having different objectives for introducing IR, they used similar reports to disclosure to investors how they plan to use the company's strengths to meet their objectives from a long-term perspective. Furthermore, from an internal standpoint, the results show that the companies published integrated reports for the purpose of nurturing employee understanding of the direction that the company needed to take.

We did not observe the obstacles that McNally and Maroun (2018) note, such as resistance from employees responsible for producing the reports and problems with information collection systems. Conversely, incremental changes to the processes and structures that support CSR and sustainability reporting were apparent (Stubbs & Higgins, 2014).

Company A, for example, has a structure that involves the active participation of the company President in the multi-department project and the production of integrated reports. Further, Company D also designed a system with a modified reporting structure in which the employees involved with strategic planning and execution were appointed to positions of responsibility (Burke & Clark, 2016). We can think of this structural development and improvement as promoting the application of IR (Stubbs & Higgins, 2014).

Additionally, each company integrated the content of the integrated reports into the medium-term corporate strategy and plans, with KPIs set and modified to ensure that the disclosed information was credible. The companies are currently at the stage where they are aiming to set specific KPIs to deploy across the company to create medium- and long-term value (Stubbs & Higgins, 2014). As seen in Company D, companies can link integrated thinking to management by objects in order to induce individual employees to work for medium- and long-term value creation.

As the above shows, despite incremental changes to processes and structures, the application of IR did not result in changes to organizational values (interpretive schemes) (Stubbs & Higgins, 2014). Consequently, as is the IIRC ideal, the companies need to target changes in employee behavior to improve report content.

Taking our analysis into account, our results the findings of Stubbs and Higgins (2014) that only small changes to the design archetype occurred because the companies were already engaged in activities related to IR out as an extension of sustainability and CSR reporting. Furthermore, while initiatives to shift the companies' values toward creating value from a long-term perspective were underway, they were limited to only some managers and regular employees. In cutting-edge companies (like Company D), which not only set KPIs, but also changed formal mechanisms like management by objectives and even established the infrastructure to embed integrated thinking, we can suppose that the spread of such values, as in McNally and Maroun (2018), are progressing smoothly.

Management practices (*sanpo-yoshi*, CSR) that take a long-term perspective are a tradition in Japanese companies and for the background to our findings. Since the Meiji Period, which saw a rebirth of Japanese industry, the company was regarded as a social institution, and in 1956, the Japan Association of Corporate Executives declared the company to be a public institution and that company management has a duty of stewardship towards the society in which it operates rather than its stockholders (Demise, 2006). In addition, several practices[6] stress the importance of taking a long-term perspective on the relationship between the company and its stakeholders (Eweje & Sakaki, 2015; Fukukawa & Moon, 2004). Until now, there was no means for Japanese companies to express their internal practices that take a long-term perspective to contribute to society to outsiders, and that the aim of IR should be its application. With the dawn of CSR in 2003 (Fukukawa & Teramoto, 2009) paving the way, all of the sample companies engaged in environmental, CSR, and sustainability reporting as part of their CSR and environmental management practices, which may explain why the application of IR was smooth but did not result in any significant change.

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[6] For example, the system of lifetime employment, which maintains a long-term relationship between the company and employee; the *zaibatsu* form of conglomerate, which procures funds mainly from banks rather than stockholders; and the *keiretsu*, which maintains cooperative and long-term relationships between major companies and their suppliers (Fukukawa & Moon, 2004).

While it appears that Japanese-style company values, historical aspects, and practices to create CSR and sustainability reports coalesced to enable the smooth creation of integrated reports, there is still a need for various internal reforms, as the IIRC points out because companies must still embed integrated thinking into their organizations. If managers and employees fail to understand integrated thinking and the corporate direction outlined within the integrated report, and put them into practice, then the quality of the disclosed information will be affected (Burke & Clark, 2016). Going forward, it may be necessary to consider the degree of integration between the content of the report and management control systems (MCSs) for motivating managers and their subordinates (de Villiers et al., 2016; Fasan et al., 2016; Kerr et al., 2015).

6 Conclusion

This study investigated the approaches to and internal mechanisms employed in the application of IR and the resulting organizational changes in Japanese companies with the best IR practices. While companies adopt IR for many reasons, we did not find the same resistance and barriers reported in previous studies in this research. We can hypothesize that these companies could adopt IR practices smoothly based on existing practices because the concept of integrated thinking that forms the basis of IR is close to traditional Japanese-style management. However, we see that all sample companies recognized the importance and necessity of embedding integrated thinking in all levels of companies to put it into practice for value creation over time.

The theoretical significance of this study is that it contributes to the growth of the IR research that focuses on the internal aspects of companies. Specifically, this study provides new knowledge on the changes driven by the application of IR by focusing on companies that have the IR practices. Additionally, we set our study in Japan, a country for which research on IR is lacking. Furthermore, in terms of practical significance, by focusing on the companies with best practices, we can offer valuable insights for companies in Japan and worldwide.

Finally, this study has four limitations. First, the sample size is limited to four companies. To reach generalizable conclusions, following Stubbs and Higgins (2014), future research should continue interview studies to provide cross-industry investigations, and adopt other research methods such as surveys.

Second, bias is unavoidable in this study because the interviews focused on the managers responsible for creating the integrated reports. Accordingly, interviews with other managers involved in the practices of IR are required. Further, as Stubbs and Higgins (2014) note, it is necessary to interview external stakeholders.

Third, the results represent only a specific point in time. As such, there will be a need to conduct future interviews, perhaps with the subjects of this study, on a regular basis. Further, case studies are required to delineate the details of the processes of change attributable to the application of IR.

Fourth, the relationship between ESG and the SDGs in the integrated reports and MCSs has not been sufficiently examined. As MCSs are essential to realize these targets, future studies should investigate how to integrate MCSs and the contents of integrated reports, as well as the possible effects on the behavior of managers and employees.

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