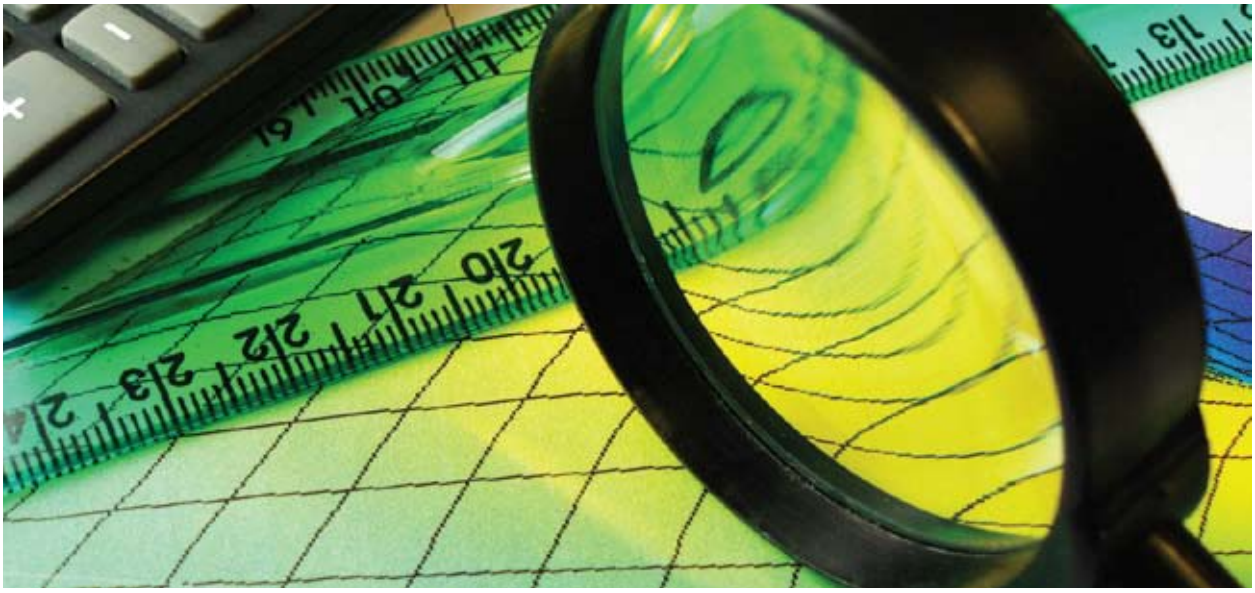
The Next Stage in the Evolution of Business Reporting – The Journey Towards an Interlinked, Integrated Report



As key stakeholders to any company, analysts and institutional investors today are sending a strong message to CEOs, CFOs, Finance Professionals and Boards of Directors that their non-financial performance is just as important in determining their attractiveness to the market as financial metrics. They are looking today for integrated reports – interlinked reports showing operational and ESG data. This is not simply the stapling together of an annual report and a corporate social responsibility (CSR) report or sustainability report; rather, this is about companies integrating best ESG practices within their operations and measuring and reporting on those integrated practices in an aggregated, machine-readable, XBRL format. The journey towards integrated reporting represents a fundamental shift in a traditional data paradigm in which accountants will play a central role as measurers and assurers of this information. Read on to know more.

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"Everything that can be counted does not necessarily count; everything that counts cannot necessarily be counted." - Albert Einstein

Until the last few years, typical historical, backward-looking financial reports were widely used and relied upon for much of the decision-making among executives, analysts, investors and regulators. But financial information alone is not the only indicator of a company's true performance, as we have come to find out with the increasing reliance on non-financial metrics as well as the advent of interactive data technologies such as XBRL that help us access information more easily and reliably.

The market place is increasingly paying more attention to non-financial information about organisations to better understand their performance, value and reputation – all one need do is look to the trillions in assets under management of the signatories of the UN Principles of Responsible Investing (UNPRI), or for that matter, to the number of private equity, venture capital and hedge funds dedicating significant portfolio allocations to companies that measure and report on their operations as well as their environmental, social and governance (ESG) practices. Companies that don't follow good ESG face reputation and financial risks, as evidenced by global brands such as Coke and Nike whose shares were dropped from the portfolios of asset managers in the last several years for failing to deliver upon their ESG promises.

As key stakeholders to any company, analysts and institutional investors today are sending a strong message to CEOs, CFOs, Finance Professionals and Boards of Directors that their non-financial performance is just as important in determining their attractiveness to the market as financial metrics. They are looking today for integrated reports – interlinked reports showing operational and ESG data. This is not simply the stapling together of an annual report and a corporate social responsibility (CSR) report or sustainability report; rather, this is about companies integrating best ESG practices within their operations and measuring and reporting on those integrated practices in an aggregated, machine-readable, XBRL format. This also is not just about the company's own operational and ESG performance, it's about that of the upstream and downstream supply chain participants. The journey towards integrated reporting represents a fundamental shift in a traditional data paradigm in which accountants will play a central role as measurers and assurers of this information. Accountants around the world are helping to define 'what counts' among operational and ESG information and helping organisations to develop integrated reports that accurately reflect performance and long term sustainability; as a result, they have an opportunity to help a company better relate to all stakeholders, not merely the shareholders. The use of XBRL to 'tag' operational and ESG data throughout the organisation will enable streamlined gathering, analysis and reporting of information for the integrated report.

The effort to report on operational and ESG practices is not without its challenges today. There are some key 'missing links' in the evolution to integrated reporting that must be addressed to help the market progress towards the ultimate integrated reports with user generated monitoring capabilities. If companies don't address the missing link, the stakeholders will… eventually.

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Key Missing Link: Non-Financial Information and Economic Value

Perhaps the greatest challenge is the lack of a clearly established link between ESG performance and financial or economic value. Often times, the concepts captured by ESG reporting are intangible… difficult to measure… and even more challenging to verify. Nevertheless, reliable, credible ESG information is essential to investors, regulators, governments, capital markets and the general public today. Recent headlines demonstrate this – for example, shares of oil giant BP plunged after its failure to eliminate the oil leak in the Gulf of Mexico, eliminating over $23 billion in market value in one day alone. This move by investors (both institutional and retail) to dump shares in the company provides insight into the linkage that has formed between ESG practices and financial performance. But the general marketplace has not fully grasped this linkage yet.

Previously less obvious to most investors, the capital markets and other stakeholders, this linkage is becoming part of the growing market evidence around the push for integrated reporting. Accountants have an important role to play in educating the market about this linkage. The profession will play a central role either as preparers or auditors of integrated reporting, as well as internal or external trusted advisors around ESG information and how it can be used alongside financial data for better decision making. As government mandates and private sector requirements for integrated reporting (e.g., Tata Group, Wal-Mart, P&G, Puma and others requiring thousands of their partners and suppliers to be fully sustainable) come into effect around the world, both public and privately held companies will be impacted. These best practice leaders have taken a "comply or die" approach where supply chain participants must meet their sustainability standards in order to remain a part of that supply chain.

As with the established reliability and credibility of financial reporting, there is a well understood concept of what is material in financial performance. With ESG performance, this again is murky at best. A company cannot report on everything in the ESG domains; they're simply too broad. This means that determining what is material in ESG performance will be absolutely essential to the process as the global framework for integrated reporting is established.

Accountants in industry and public practice will be at their sides as one of their most trusted advisors to help them meet many of these complex challenges.

Key Missing Link: Reliability and Market Credibility

Financial reporting has a relatively long history and reliability – there are fairly well-established standards for accounting and measurement, a trusted group of professional body of accountants to measure and assure that information, and clear oversight by established regulatory bodies. As a result, the market places trust and credibility in financial information as indicators – and predictors – of performance.

Contrast this with the area of ESG practices – a nascent area, the domains of ESG are not very well understood. There is currently no established global framework or reporting standard for ESG – in fact, there are so many competing frameworks that it is akin to total chaos from the accountant's perspective in picking which framework makes most sense. Without a clear framework and standard, there is also a severe lack of comparability and an understanding of what is good vs. bad ESG performance. The lack of a common 'lingua franca' around a generally accepted ESG reporting standard presents a significant obstacle to effective risk management. After all, can you truly manage that which you don't fully understand or that around which you do not have universal agreement? There is also no clear oversight body. As a result, the general market places less trust in ESG information than financial information today. The asset managers, analysts and regulators that 'get it' – such as in South Africa, the market with the world's first requirements for integrated reports by listed companies on the Johannesburg Stock Exchange – are true pioneers in showing the rest of the market the way towards reliable, credible ESG information and the ultimate integrated reports. With their guidance and leadership, as well as the creation of a uniform, global framework and standards for ESG reporting (as currently being undertaken by the International Integrated Reporting Committee based in London), the reliability and credibility of ESG data will grow to eventually be equal with that of financial reporting.

Key Missing Link: Materiality

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Key Missing Link: Do Accountants Get It?

The role accountants will play begs the question whether or not they understand ESG reporting. Some interested stakeholders feel accountants have much more to learn about the ESG domains in order to be seen as integrated reporting experts, whether as preparers (e.g., CFOs) or assurers (e.g., external auditors) around that information. In some cases, accountants in internal roles such as CFOs and Controllers may need to expand their body of knowledge and skill sets and collaborate with other industry experts such as engineers. Eric Israel, Managing Director at KPMG, addressed a 2010 gathering of concerned stakeholders in ESG in Amsterdam and called on CFOs to "learn more about carbon and sustainability accounting." When pressed by the audience on whether accountants 'get it' – whether they understand complex relationships between environmental, labour, social and governance issues and how to gather and report that information – Israel went on to say that the issue is more "how prepared accountants are, not if they get it." Nancy Kamp-Roelands with the European

Having worked with the XBRL standard for more than a decade, we see the significant potential XBRL can play in integrated reporting. With financial information already tagged in XBRL in the US, China, the UK, German, and Japan (and underway in many other countries, including India), it is not a large leap to see that ESG data tagged in XBRL will make the combined data set transparent, fully machine-readable over the Internet, and readily available literally at the click of a mouse or the touch of an iPad, for auditing, analysis, benchmarking or other decision making or planning.

Federation of Accountants' (FEE) Sustainability Group, remarked at that time that "we (accountants) can measure everything." Therein lays the challenge. And as Einstein's quote implies, the key to effective reporting will be to figure out which ESG elements are of value and should be counted, how they can be counted reliably and consistently, and how they should be reported so that those who make decisions based upon this information can readily uptake and understand it. Larger accountancy firms are adding domain experts, including scientists, consultants and engineers, to their sustainability teams. They recognise the opportunity – and missing link – here for the accounting profession.

The Carrot vs. the Stick – Can We Have Parallel Strategies?

The global company, Novo Nordisk, is at the cutting edge of integrated reporting. The company has been providing integrated reports since 2004 – clearly an early trailblazer and shining example of best practice. Susan Stormer, Novo Nordisk's VP of Global Triple Bottom Line Management, indicated during the 2010 GRI Conference that producing integrated reports was not easy, but that the time was now to begin 'experimenting' even without an established reporting standard. This is what leads to innovation and creativity in the process. The big stick of government mandates is not the only possible motivator to move companies along the evolutionary path to integrated reporting – large global brands have the power to drive best practices as well. The calls from corporate giants like Tata Group, Wal-Mart, P&G and Puma go a long way towards inspiring public and private companies to become more sustainable parts of larger supply chains.

Dynamic, Interactive, Integrated Reporting Data Through XBRL

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Even in the absence of widespread XBRL-enabled ESG data today, we already have evidence of how Web 2.0 and social media platforms are helping leading edge companies share their ESG information with a broader world of interested stakeholders. Rabobank, a large, cooperative bank based in the Netherlands has already produced a digital ESG report and made it available on its website. Rabobank only produces 50 print copies of its annual report, recognising the greater power of digital information to reach the masses. This is a good sign for things to come – once we have an agreed upon XBRL taxonomy for ESG information as well as a global framework for reporting, the value of digital integrated reports will improve manifold, allowing for real-time or near real-time ESG information to be available alongside financial data and eliminating the missing links. Similar to how XBRL helped unlock financial information from historical, backwards-looking, paper- or PDF-based presentation formats (that were essentially not useful to most stakeholders today since they need current information in digital format), XBRL will also help release ESG data from the prison of ineffective reports that up until now have been simply "stapled" to company financial reports.

Think about where this leads us… shifting from a historical view of outdated, limited-use information, around which assurance is somewhat meaningless, to a real-time and forward-looking view with a strong degree of assurance and reliability around digital, interactive financial and ESG information – the interactive, integrated report. This could be used for both external reporting to regulators, media, analysts and investors as well as for internal decision making for business planning, marketing, benchmarking, performance measurement, and predictive business intelligence, and supply chain management. XBRL and its ability to connect with various link-bases (e.g., back to source documentation or a reporting standard), paired with the independent assurance of an accounting professional trained to review such structured information, will bring much needed trust and confidence to ESG data. If it holds true that we fear what we don't know, XBRL can help us limit that fear, and assurance by accountants can improve trust and confidence in the things "that count." ■

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