XBRL

By Brad Monterio

Sustainability Reporting and XBRL—Part 2

At the Global Reporting Initiative (GRI) conference in Amsterdam last May, I had a chance to sit down with two recognized experts in the area of environmental, social, and governance (ESG) and integrated reporting to discuss the concept of integrated reporting, its challenges, and its opportunities.

Mike Krzus, CPA, is a partner with Grant Thornton in its Public Policy and External Affairs Group and is the firm's global expert on improving corporate reporting. He is coauthor of *One Report: Integrated Reporting for a Sustainable Strategy*.

Robert Eccles is a professor at Harvard Business School, coauthor of *One Report* with Krzus, and coauthor of *The Value Reporting Revolution: Moving Beyond the Earnings Game* and *Building Public Trust: The Future of Corporate Reporting*.

"No corporation can have long-term viability unless they mitigate ESG risk," Krzus began. Just ask the BP executives or analysts covering the oil sector. The lack of a common *lingua franca* around a generally accepted ESG reporting standard presents a significant obstacle to effective risk management. Can you truly manage that which you don't fully understand—or that around which you don't have universal agreement? A strong advocate for integrated reporting, Krzus identified some of the challenges, opportunities, and benefits of an integrated reporting approach.

One of the important challenges surrounds the quality and reliability of CSR/ESG information. "Corporate Social Responsibility information isn't always considered to be of the same quality or reliability as financial information," he says. "That's because, as least in the U.S., we have things like Sarbanes-Oxley and various control structures in place to protect the quality of financial information. That doesn't necessarily exist for information gathered by environmental or human resources systems. So one of the first challenges is how do we improve the control structure and rigor of the process that we use to gather CSR/ESG information." CFOs and management accountants can help companies overcome this hurdle as they innately understand controls and processes around information. "CFOs have an opportunity to work alongside the sustainability team and help elevate the quality of ESG information to the same high standards as that of financial information," Krzus adds.

Which leads to another challenge and opportunity: understanding the relationships and tradeoffs between information and how they impact financial performance. CFOs and the investor relations team already have well-established dialogue and interaction with analysts and investors. But this isn't enough. CFOs and management accountants can help their company engage a broader stakeholder community such as NGOs (nongovernmental organizations), associations, consumer groups, community groups, and others to better understand what they truly value, what's important to them, and what's material to them in terms of nonfinancial information. The result is a stronger focus by the CFO on control and process improvements to elevate the quality and reliability of ESG/CSR information and better relationships with internal and external stakeholders.

Krzus also highlighted other benefits of an integrated reporting approach:

- Greater clarity of information relationships helps companies understand tradeoffs of that information—for example, understanding how a cut in CO_2

emissions affects electricity consumption and what impact that has on internal stakeholders (e.g., employees) and external stakeholders (e.g., a happy public).

◆ Sustainability is about long-term viability of an organization. It doesn't matter how "green" a company is—if it doesn't have a good business plan in which sound ESG practices (with appropriate controls and processes in place) are integrated, it can't be viable because it can't mitigate risks of those things it doesn't understand or know.

◆ Greater clarity and quality of information leads to more informed decision making. As management teams allocate limited resources, they are better informed about the relationship of information, the tradeoffs that will be necessary, and the impact of those tradeoffs on society and the environment.

Integrated reporting improves overall reputational risk management strategy for companies. Engaged dialogue with stakeholders can often build up credibility with those stakeholders, giving companies "a little more cushion," Krzus offers. "Beginning to see how the world sees you and your corporate impact on society gives you a better idea of what risks to mitigate."

Birth of a Global Integrated Reporting Standard

Financial reporting is a mature, known entity. International Financial Reporting Standards (IFRS) have been developed and are being promulgated around the world to help companies report financial information in a comparable, consistent manner. Such isn't the case with ESG reporting… yet.

Robert Eccles discussed hurdles to overcome in order to achieve integrated reporting around the world in our lifetime, chief among them a lack of a uniform, global integrated reporting standard that incorporates both financial and ESG information. This lack of a "Generally Accepted Framework for Integrated Reporting (GAFIR)," as he calls it, is really a significant opportunity for innovation in disguise.

"Companies will have to create a framework for themselves, but there are a few leading companies whose practices they can examine and learn from. This is actually good because experimentation and innovation by companies will supply very useful insights into what a GAFIR should look like. Since all 450 listed companies in South Africa have to file integrated reports starting on June 1, 2010, within one year there will be a large number of cases to learn from. I'm also hoping that my idea of a 'voluntary filing program for integrated reporting' will take hold in some major countries like the U.S., the U.K., Brazil, Netherlands, and China. We will learn a lot from this as well."

In late May 2010, the Johannesburg Stock Exchange (JSE) announced that all of its listed companies must file integrated reports as a condition of listing. As Eccles indicated, the lack of an existing framework opens up the possibilities for a creative solution to the collaborative efforts of the entire market. Innovation will teach the standards setters, whoever they may eventually be, a lot about how this standard might be developed. He notes that, although we lack "globally accepted standards for nonfinancial metrics [although the GRI has made a big contribution here], what we really need is enough companies using the same standards over a period of time so that we have the necessary data to do research."

This research will be conducted by the recently formed International Integrated Reporting Committee (IIRC), a global body composed of global CEOs of the Big 4 accounting firms, investors, companies, NGOs, accountancy bodies, standards-setting bodies, and Eccles himself, to develop a GAFIR by 2020 for the world's companies.

Also at the GRI conference, Mervyn King, a world-renowned corporate governance expert, called on all large and medium-sized corporations to file integrated reports within the next five years. King worked with the JSE, the Association for Savings and Investment SA, the Institute of Directors SA, Business Unity South Africa, and the South African Institute of Chartered Accountants on their program to require all 450 listed companies on the JSE to file integrated reports as a condition of listing. South Africa is the first country to require integrated reports, and similar developments are under way in China, India, and, with the recent Securities & Exchange Commission (SEC) guidelines document on environmental reporting issued, perhaps the U.S. as well.

Accountants need to be prepared. Companies and CPA firms are already adding domain experts to their teams, including scientists and sustainability and environmental experts. CFOs and accountants should heed Eric Israel's advice (Part 1) to learn about carbon and sustainability accounting and disclosure, and they should seize the opportunities Krzus outlined to elevate the quality and reliability of ESG information, better

continued on page 61

XBRL

continued from page 57

engage stakeholders, and understand risks related to ESG practices.

"Novo Nordisk is at the cutting edge of integrated reporting," King added. The company has been providing integrated reports since 2004–clearly an early trailblazer and shining beacon of best practice. Susan Stormer, Novo Nordisk's VP of Global Triple Bottom Line Management, indicated that producing integrated reports wasn't easy but that now was the time to begin "experimenting" even without an established reporting standard. She stressed that this would lead to innovation and creativity in the process, thereby helping companies come up with creative solutions to managing and monitoring ESG practices. This meshes well with Eccles' view.

XBRL's Role in Interactive Integrated Reporting Data

"As with financial reporting, XBRL has an essential role to play in making the information in an integrated report as accessible and useful to as many stakeholders as possible," Eccles notes. "Taxonomies exist for both financial and nonfinancial data (e.g., for the GRI G3 Guidelines), so the step towards a taxonomy for a GAFIR will be pretty easy in the near future. The harder steps are the taxonomies for the metrics based on standards and standards for nonfinancial information."

With financial information already tagged in XBRL in the United States, China, and Japan (and under way in many other countries), it isn't a large jump to see that ESG data tagged in XBRL will make the combined data set fully machine-readable over the Internet and readily available at the click of a mouse—or the touch of an iPad or iPhone—for auditing, analysis, benchmarking, or other decision making and planning. And not just for analysts, regulators, and institutional investors but, rather, for a broader stakeholder group including NGOs, community and consumer groups, retail investors, and others.

Even in the absence of XBRL-enabled, digital ESG data today, there are some leading-edge companies already sharing their ESG information with a broader world of interested parties. Rabobank, a large cooperative bank based in the Netherlands, has a digital ESG report available on its website. This is a harbinger of things to come, but it isn't quite there yet. ESG reports on a corporate website aren't quite the same things as a fully integrated report being produced by a company with ESG processes integrated into its business practices. But it's progress.

Once there's an agreed-upon XBRL taxonomy for ESG information and we achieve Eccles' vision for a GAFIR, the value of digital ESG data will improve, allowing for real-time or near real-time ESG information to be available alongside financial data and eliminating the gap or disconnect between the two. Similar to how XBRL helped unlock financial information from historical, backwards-looking paper- or PDF-based presentation formats, XBRL will also help release ESG data trapped in outdated models and formats that until now have been simply unreported or, at best, stapled to company financial reports.

This movement will shift us from an historical view of outdated, limited-use information—around which assurance is somewhat meaningless—to a real-time, forward-looking view with a strong degree of assurance and reliability around digital, interactive financial and ESG information. This could be used for 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.

XBRL and its ability to connect with source documentation or a reporting standard, paired with the assurance of a CFO or accountant trained to gather, use, and report such structured information, will bring much-needed trust to ESG data and integrated reports. **SF**

Brad J. Monterio is managing director and founder of Colcomgroup, Inc. and managing director and founder of CMH Partners LLC. He is a member of the IMA XBRL Advisory Committee and chairs its Outreach Working Group. You can reach him at bmonterio@colcomgroup.com.