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company

a future for business  
which makes equal sense  
to staff, shareholders  
and society

## The Future of Corporate Reporting

'State of Play - February 2007'

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## Preface

The key to long-term success is the quality of leadership and its influence on all a company's relationships. Communication - alongside strength of character and strategy - is in turn at the heart of good leadership and relationships. Reporting is in its turn one aspect of strong communication, and a particularly important part in creating a sense of confidence in a company.

Over the last decade Tomorrow's Company has played a significant role in charting the course taken by leaders in their companies' communication to their many stakeholders, and also in clarifying what these different stakeholders need and can expect. In *'Restoring Trust'* (2004) we described the value chain that links the ultimate investor to the company, and suggested how transparency and rewards could be better aligned along that chain. *'Sooner, Sharper, Simpler - A lean vision of an inclusive Annual Report'* (1998 and republished 2006) formed the basis for the mandatory Operating and Financial Review (OFR) and outlined a number of principles we believe should be followed by companies, regulators, investors and stakeholders in the UK.

Regulations are becoming more global - with all the complications that brings - and there has been a growing worry about class actions against companies based on what they say about the future. But, in our view this does not change the principle of good communication. This publication reviews where UK-based companies now think that they are and suggests what they should be preparing for as the fog clears after the regulatory confusion of 2006.



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## The Future of Corporate Reporting 'State of play - February 2007'

### Introduction

When Gordon Brown overturned the planned introduction of the UK's OFR in November 2005 it was because of the "extra administrative cost" that a "gold-plated regulatory requirement" would impose on businesses<sup>1</sup>. But investors, accountancy bodies, trades unions and environmental groups immediately attacked the decision, saying it would "damage information to shareholders"<sup>2</sup>.

Whatever the rights and wrongs of that decision, the next six months saw the Accounting Standards Board (ASB) publish almost all of the planned OFR as its "statement of best practice" for narrative reporting<sup>3</sup>. And for annual reports published after 1 January 2006, the 2003 Accounts Modernisation Directive from the European Union (EU) came into force - legislation with a much wider impact than the OFR, requiring more than 37,000 unquoted as well as quoted companies in the United Kingdom to disclose much of what the OFR would have required, in a new-style 'enhanced Business Review'<sup>4</sup>.

Just over a year on from the Chancellor's decision, where do we find ourselves? Have companies avoided OFR-type narrative reporting because of the cost? Have they rushed to embrace it as best practice, even though there is no legal requirement to do so? Or are they caught between differing UK and EU requirements, unsure what to do?

This short report looks at how companies have changed their reporting style, both before and after the introduction of the enhanced Business Review. It examines the reasons behind their actions, and makes predictions for how we should expect this area to evolve in the upcoming reporting season following the year ends in December 2006.

## Was there a problem with reporting?

The roots of the OFR lie more than 10 years in the past, when there was a drive to change Company Law to achieve three major things: to clarify directors' duties, to encourage shareholders to exercise more control, and to improve transparency and accountability. With the reporting failures at Enron and WorldCom in 2002, the government decided to move faster on the third of these priorities, and so the OFR was born.

The intention of the OFR was to "improve transparency of corporate governance and hence business performance." In doing so it would "focus both directors' and shareholders' assessment on all internal and external issues affecting that performance."<sup>3</sup> No wonder, then, that a number of groups described its repeal as leaving a significant "policy vacuum."

But the 2003 EU Accounts Modernisation Directive also requires companies to prepare an enhanced review of their business. It requires them to report on risks and uncertainties to a level not previously experienced in the UK<sup>4</sup>. Although it does not go as far as the OFR in requiring companies to report on strategy and the prospects for the business<sup>4</sup>, the January 2006 decision by the ASB to issue the planned legal 'Reporting Standard' as a 'Reporting Statement'<sup>5</sup> provided a clearly-defined 'statement of best practice on OFR' for any company that wishes to follow it - irrespective of whether or not there is a legal requirement to do so.

The fear in some quarters was that narrative reporting would not be as good as it would have been with compulsory OFRs<sup>6</sup>. But rather than a reduction in quality across the board, it seems more likely that this will create a divergence in what companies do. Some companies may only conform to the minimum; others will continue to push back the frontiers.

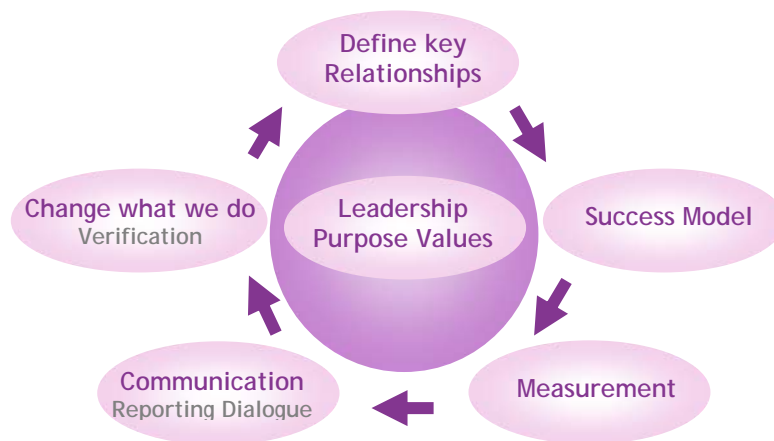
The key question in determining whether or not this causes a problem, and whether or not it is useful to publish an OFR, is 'what does the company want to achieve by publishing its annual report?'

## Why do companies produce annual reports?

For Tomorrow's Company, the annual report is part of the whole virtuous circle of governance for a business (see Figure 1). Whatever the legislative environment, there is something deeply natural about the directors giving an account of their stewardship. We all need to be accountable to be effective, and the annual report and the Annual General Meeting (AGM) are the axles which drive this accountability.

But the focal point which determines the quality of the annual reports produced is the perceived self-interest of the companies that create them. What do they see as the purpose of creating an annual report?

Figure 1: Governance - A Virtuous Circle



The virtuous circle of governance is a joined-up way of thinking about success. It means linking together every conversation about business planning, measurement, and the boardroom agenda, with the production/audit of the annual report (and other reports), the annual meeting, and stakeholder dialogue - all as part of the same logic.

Reporting on performance provides verification of whether or not the company has achieved what it set out to do. This in turn allows it to understand whether or not it has correctly identified its key relationships and success model, and to change these as necessary. This allows it to define how to measure its success model, so that it can be communicated.

There is also another set of impacts that flow in the opposite direction. Communicating (for example through an annual report) forces the company to define what measures it is going to report on. This in turn forces it to be clear about what is its success model, and what are the key relationships that enable that model to succeed. This also forces the company to be clear about what it means by success: what it is setting out to achieve.

This is why companies find non-financial reporting difficult - because it forces them to be explicit about the success they seek and what drives it. It also explains why those that choose to grasp the nettle gain so much benefit from doing so.

A recent study<sup>7</sup> by the design agency Bostock & Pollitt found that companies have two main reasons for producing an annual report. The first is to meet the government's regulatory requirements. The second is to market the company to key stakeholders.

*"[The annual report] provides a balanced overview of our results and financial position at the end of the year and satisfies all regulatory requirements."*

*"It achieves the primary regulatory purpose when signed off by the auditors and regulators."*

*"It achieves our statutory obligation for filing."*

*"It is a legal requirement but it also enables you to get your message out to key stakeholders ... It forms a branding exercise also."*

*"The purpose of the Annual Report is to give stakeholders a view of business, what drives it, what affects it, how we measure ourselves going forward."*

*"It is a communications piece to stakeholders raising the key issues for the business and addressing how management will address these issues going forward."*

Who are these groups of stakeholders? The same survey gives us some insights into the breadth and variety of different audiences that companies feel they need to communicate with (in priority order):

*"Institutional investors, analysts and media."*

*"Institutional investors; private investors; the industry; competitors; communities; 'punters'; government; employees; the media."*

*"Shareholders and potential investors; sell side analysts; public affairs and media audiences; corporate responsibility and community partners; customers; staff; competitors."*

*"Shareholders form the primary audience, but also opinion formers are important, namely government and press in UK and overseas; financial analysts; financial reporters; existing and potential investors and clients."*

## What do the different stakeholder groups want from the annual report?

These varied and diverse groups are likely to be interested in very different aspects of the company. Each group will want to see its own interests reflected in the annual report.

A series of polls carried out by Ipsos-Mori in 2005 and 2006<sup>8</sup> asked people what factors they considered most important when making a judgement about a company. It found that different groups of people thought very different things were important:

	General public	MPs	City	Business + Financial Press	Captains of industry
Financial performance	12	37	42	93	58
Treatment of staff	16	42	n/a	24	7
Customer service	24	16	n/a	37	12
Quality of management	13	n/a	76	75	44
Image and reputation	n/a	n/a	n/a	38	34
Quality of products	20	n/a	n/a	37	23
Social responsibility	n/a	34	n/a	10	n/a
Corporate strategy	n/a	n/a	n/a	63	15
Market share	n/a	15	19	51	n/a
Accessibility/openness to enquiries	n/a	n/a	n/a	44	n/a
Comms/info provided	n/a	n/a	n/a	34	n/a
Honesty/integrity	28	n/a	n/a	n/a	19
Long established	13	n/a	n/a	n/a	n/a
Valuation	n/a	n/a	28	n/a	n/a
Cashflow	n/a	n/a	25	n/a	n/a
Sector/industry in which they operate	n/a	n/a	20	n/a	n/a
Environmental responsibility	n/a	18	n/a	n/a	n/a

"What are the most important factors you take into account when making a judgement about a company?"  
(Spontaneous, top two factors for each group highlighted)<sup>8</sup>

For companies, as we saw, the primary stakeholder group is overwhelmingly the existing shareholders and potential investors. What do these people want from an annual report? The Bostock & Pollitt survey<sup>7</sup> found consistent views:

*"We want a document that presents a good investment case, details of the business drivers and strategy put in the context of the marketplace, and a description of any risk factors that might face that company."*

*"Investors want an open, frank, honest view of the company and evidence that it is well managed."*

*"Critical are accurate figures, accessibility and reliability, as well as material that is well signposted and which hangs together coherently."*

Companies try to meet these needs, but at the same time they include material to meet the needs of customers, employees and media audiences:

*"We use the annual report as an advertising medium for our products. We focus on the brands and on the new collections."*

*"The annual report ... forms a branding exercise also."*

*"The Report and Accounts tries to be so many things to so many people. It is often the main marketing document for the Group, but it is also a statutory document."*

*"We attempt to give a full and frank overview. Our report and accounts now run to 130 pages, very lengthy."*

Perhaps not surprisingly, the result is often in conflict with what investors want to see:

*"Too much narrative dilutes the message."*

*"PR spin... glossy pictures ... detract from the annual report."*

*"I detest reports that waste pages on environmental garbage. Environmental statements are all the rage but ... it's not useful or meaningful information. CSR statements are often bland and meaningless."*

As one company recognised:

*"The Report and Accounts tries to be so many things to so many people. Hence it clearly will not fulfil all of those roles as well as it might."*

What is the solution? Can the circle of differing needs be squared within a single annual report?

## What is the solution?

Companies want to meet their legal requirements. They also want to communicate with their key stakeholders. The law provides a framework within which companies are free to find their own solutions. The ability to report online will make this task easier.

From early 2007, the proposal is that UK companies will be legally allowed to use the internet and email as the default option for sending information to shareholders, sending paper copies of annual reports and other information only to shareholders who request them<sup>9</sup>. The DTI estimates that this will save UK-listed companies over £47 million a year. But the main benefit of online communication, surely, is not that it reduces cost but that it allows companies to develop detailed, targeted communications and relationships with each of the major stakeholder groups that can impact the business performance. It is business-criticality and materiality that is key.

For investors and investment analysts, the annual report is already somewhat of a non-event<sup>10</sup>, since by the time it is published they have often already received far more in-depth information from other sources throughout the year. For them the annual report is already "a supplement to give context."<sup>7</sup>

Wider use of the internet should allow companies to develop similar strong relationships and communications with their other major stakeholder groups. This should improve the quality of their relationship with each constituency, and hence lead to improved business performance.

All this is positive. But it raises the question: what role remains for the annual report? If new technologies allow better communication with key stakeholders by other means, has the annual report had its day? Is its only remaining role to meet the company's legislative requirements?

At Tomorrow's Company we believe that the annual report has a far more positive role to play in the whole process of governance and accountability. If companies are to fulfil both their legal and wider communications responsibilities effectively, they need to be very clear about their objectives. They also need to understand where the annual report fits as part of their total communications approach.

But before we look in detail at what we believe that role is, let us first examine the changes that companies have actually made to their annual reports over the last 12 months. These are the annual reports for the year-ending December 2005 (when companies would have been readying themselves to comply with the OFR) and for the year-ending April 2006, when the enhanced Business Review was required for the first time.

## How companies have changed their reporting

When the corporate reporting agency Black Sun analysed the FTSE-100 annual reports published for the year ending December 2005<sup>11</sup>, they found evidence of significant change:

- \* 95% of companies discussed their corporate strategies, up from 75% a year before
- \* 40% provided business objectives or targets, up from 16%
- \* the percentage of firms discussing values and principles rose from 30% to 66%
- \* the proportion disclosing Key Performance Indicators (KPIs) almost doubled from 19% to 36%.

The report concluded, "A preliminary review of the first season of enhanced narrative reporting confirms that despite the confusion and uncertainty, companies are beginning to find new ways of reporting that deliver business benefit."

But was this actually because companies had been expecting to have to comply with the OFR? Now the legislation had been repealed, would standards slip?

In August 2006 Black Sun published a follow-up report<sup>12</sup> that looked at the annual reports published by the FTSE-100 companies with April year-ends. Although the expected OFR had not come into force, these companies were the first to have to comply with the new EU legislation and publish an enhanced Business Review. Although this legislation was seen as less demanding than the OFR, some firms were found to be "struggling to meet the more challenging aspects", while others "demonstrated how to use the opportunity to communicate - with conviction and commitment - meaningful information about what is driving their performance."

Interestingly, despite the fact that the mandatory OFR had been repealed, nearly half the companies (48%) still felt it meaningful to describe their narrative as an 'OFR'. Of those companies, half (26%) explicitly said that they had prepared their reports in accordance with the voluntary principles of the OFR Reporting Statement issued by the ASB.

At a high level, then, a significant proportion of Britain's largest companies are stating that they find value in the OFR.

Looking in more detail at the basic building blocks of the Business Review:

- \* risk and uncertainties
- \* forward-looking information
- \* financial and non-financial KPIs

the report found evidence of further change.

The Black Sun study of December 2005 year-end reports had shown little change in the first of these elements. ("The increasing importance and profile of risk has had little impact on

the development of reporting in this area.”<sup>11</sup>) But under the new EU legislation this now became the area of “greatest improvement”<sup>12</sup>.

Companies were found to be “going beyond traditional risk reporting...generating confidence that systems are in place to protect the revenues which will deliver market expectations.”

At the other extreme, companies found talking about their future prospects “most challenging”. This reticence was “not surprising given the uncertainty surrounding the detail of the safe harbour provision in the Company Law Reform proposals<sup>12</sup>.” Presumably we can expect greater disclosure in this area, once directors’ responsibilities have been clarified by the new companies act formulation of their duties.

Part-way between these two extremes of reporting performance are the financial and non-financial Key Performance Indicators (KPIs). Only around half the companies in the survey specifically identified their financial KPIs. Given that companies must surely have well-established financial reporting systems in place this seems surprisingly low. We can only guess at the reasons for non-disclosure. But given that as many as half the companies felt able to disclose their financial KPIs, competitive sensitivity cannot be the stumbling block that some once thought.

As might have been expected, however, non-financial KPIs were described as “an area where companies struggle.” Companies were often found to be focusing “on what is easily reported, avoiding the main issues.” But the survey also found “a few leadership companies... integrating their financial and non-financial thinking and decision-making, signalling a better understanding and management of both.”<sup>12</sup>

This, surely, is what holds the key to the value of the narrative reporting and to the future role of the annual report itself.

In September 2006, creative consultants Radley Yeldar published similar findings in a review of the most recent annual reports for all FTSE 100 companies, covering year-ends in December 2005 and April 2006<sup>13</sup>.

They, too, found evidence of major changes in company reporting, with some areas still proving challenging:

- \* 83% included “some form of upfront strategic content or discussion”
- \* 43% called their narrative content an OFR, despite the switch to the Business Review legislation
- \* 37% made a “reasonable attempt at explaining their marketplace”
- \* KPIs were “getting better”, with 14% “fully defining or explaining their KPIs”

Forward-looking information was also considered a problem, with only a quarter (26%) giving a clear indication of what the future might hold, and only half of those descriptions (10% of companies) were considered to be ‘in depth’.

## The future role of the annual report

Companies want their annual reports to achieve two goals: to fulfil their legislative requirements and to communicate with stakeholders.

Adequate communication with stakeholders can no longer be achieved by publishing a single report each year. Investors are already used to receiving information in a variety of different forms throughout the year. Through the use of the Internet companies are now building similar ongoing relationships with other groups of stakeholders. Investors receive quarterly announcements, *ad hoc* briefings, and the detailed reports required by different stock exchanges. The audiences interested in Corporate Responsibility (CR) or Corporate Social Responsibility (CSR), for example, are finding that a number of companies now publish separate CSR reports, as well as putting information online:

*"A couple of pages [on CSR] are included in the annual report, broad coverage online."*

*"[CSR reporting] will become more complex as the environmental impact becomes more complex. Also online for CSR should be huge since one can do so much more... [It] will eventually be as voluminous and frequent as financial reporting."*

*"This year was different in that we have moved away from a distinct CSR report or section because it has become so embedded in what we do."<sup>7</sup>*

These changes are moving all stakeholder communication away from being a one-off 'event' into more of an ongoing process or relationship, and we expect this trend to continue.

This points the way to a clearer role for the annual report.

At Tomorrow's Company, we believe that successful companies achieve this by the 'five plus one' approach. In this the 'five' are the strong relationships (with customers, suppliers, staff, shareholders, and society) and the 'one' is leadership that aligns them to a common purpose.

Companies, as we have seen, are already building relationships in depth with each of their five stakeholder groups. The role of the annual report is to enhance the sixth element: leadership.

The annual report cannot and should not focus on every single issue that is relevant to every single stakeholder. The annual report should focus on the issues that are material to the business as a whole, and bring them together in a single, coherent story. It should reveal the 'value proposition' of the total business.

Communications and accountability are the hallmarks of good leaders, and that is the role of the annual report: to summarise all the critical issues that affect the success of the business, explain how they have created the past year's results, forecast how they might

pan out in the future, and explain what is being done to ensure the company's future success in that environment.

In doing so (see Figure 1 'Governance - A Virtuous Circle') management's understanding of the business is also enhanced, and so leadership is improved. This is reflected in the comment above about how CSR has shifted from a separate, reporting-focused activity to becoming "embedded in what we do".

As we know, investors also want this viewpoint. They want an annual report that:

*"...gives a good investment case, details of business drivers and strategy, puts this in the context of the marketplace and describes any risk factors that might face that company."*

*"...[provides] a basis by which a reader can understand what is happening, the market the company is in...the company's strategy to compete in that marketplace, how it is managing critical assets and resources in order to deliver on that strategy..."<sup>7</sup>*

And this is exactly what the OFR and the enhanced Business Review set out to do.

Little wonder, then, that as understanding of the OFR and narrative reporting has grown, so opinion amongst the investment community has moved strongly in favour of these reporting frameworks.

A study published by IR Magazine in June 2006 showed that 78 per cent of fund managers and analysts believed companies should publish a full OFR. As a stand-alone figure, this is high. But it is even more striking when you realise that it is almost twice the number who had shared that view a mere eight months earlier. An Ipsos-Mori poll quoted to the Chancellor in October 2005 showed only 41 per cent of fund managers supporting the compulsory OFR<sup>14</sup>.

As they gain experience and understanding of narrative reporting, companies and investors are both finding benefits from the approach.

As one investment analyst put it recently: "We might not be particularly interested in every specific issue mentioned in a CSR report. But the presence of good CSR reporting tells us there is good CSR management. And that tells the company as a whole is well-managed."<sup>15</sup> Viewed in this light, the quality of the annual report becomes a proxy for the quality of the management team.

Narrative reporting is a developing area. All companies are learning. But some companies are clearly taking a lead and developing emerging best practice in different areas<sup>11, 12, 13</sup>. Better reporting not only has the potential to create better relationships between the company and the external constituencies that matter most. It also improves the internal leadership of the business by focusing decision-makers on the real drivers of enduring success. That is the self-interest that is driving some companies to extend their performance in this area.

Other companies should watch the leaders, and apply whatever innovations are most useful to their own situations. The results would then not only be improved dialogue and performance for individual businesses, but also the creation of an environment in which less regulation is needed - because good accountability increases self-regulation and regulation by stakeholder accountability. This is part of the package, along with 'comply or explain' and a strong media, which makes for robust governance and reduces the need for imposed regulation.

We hope and expect to see this trend continuing in the annual reports published for the December 2006 year-ends.

### Sooner Sharper Simpler

In 1998 we published our report '*Sooner, Sharper, Simpler: A lean vision of the inclusive annual report.*' This was intended to challenge companies to re-examine and improve their approach to communication.

It identified a number of key principles that still hold true, and continue to be a foundation for the work of Tomorrow's Company in the field of reporting. It also offers companies a scorecard by which to assess their own reports and benchmark themselves against others.

Those principles are:

- 1. Improve company decision-making**  
Report on the key drivers of long-term value and thereby focus the minds and priorities of senior management
- 2. Put judgement before compliance**  
Create frameworks which allow companies the flexibility to exercise and then explain their judgement in promoting the success of the company, and lift their sights beyond merely complying with an external standard.
- 3. Improve investor decision-making**  
Enable investors to compare the prospects and performance of companies, and thereby focus the financial system on long-term value creation to the benefit of the entire economy and those who have a diversified exposure to it.
- 4. Make reports more accessible**  
Liberate companies to convey information with the minimum of repetition, and allow them to cross-refer readers to other information, so that they can create a core narrative which captures, in one place, all the key information and context that is needed to form an overall assessment of the company.
- 5. Improve communication and trust**  
Without compromising the accountability of companies to shareholders, help employees, the community, regulators and all stakeholders to form a total picture of the company, what it stands for, and where it is going.

## The world is moving on

The repeal of the mandatory OFR has forced companies to endure a period of significant public policy confusion. One year on, however, the fog is clearing.

The introduction of the EU's Accounts Modernisation Directive now means that more than 37,000 quoted and unquoted companies in the UK must produce an enhanced Business Review. This does not go as far as the OFR in requiring companies to report on prospects for the business, but many firms are choosing to go beyond the minimum, by complying with the original full OFR. As the ASB put it recently, "While narrative reporting is still evolving, and whatever name is given to the narrative sections of the annual report, the overall impression is that there appears to be a willingness among many companies to go beyond strict legal requirements and to move towards best practice reporting."<sup>16</sup>

The Association of British Insurers (ABI) have also recently sort to reflect, and influence, some of the changes that are taking place by updating and replacing their Socially Responsible Investment (SRI) guidelines with their Responsible Investment Disclosure Guidelines<sup>17</sup>. The changes to the guidelines highlight aspects of responsibility reporting on which shareholders place particular value, and reflect the emerging policy framework resulting from the enhanced Business Review.

We can see two main reasons why any company should stretch itself towards best practice reporting. The first, in an increasingly competitive world, is to improve relationships with key stakeholders by demonstrating that the management team understands and can manage its business better than competitors. The second is that clearer reporting requires clearer understanding, and so better reporting can actually help to improve internal management and performance.

In addition, the fact is that corporate reporting is currently going through a period of radical change which shows no sign of slowing. Given that rate of change, and given the impact which reporting can have, even companies that do not want to be at forefront will want to be able to manage this agenda, rather than have it manage them.

Looking forward, some of the major issues that companies will need to deal with over the next few years include:

1. **Safe harbour**

One of the reasons cited for resisting the mandatory OFR was the need for directors to have a 'safe harbour' in case their predictions of the future turned out to be wrong. The fact that so many leading companies have managed to produce good reports despite this, means it is probably not as big a stumbling block as some people have suggested. (Predictions will always turn out to be wrong, so it is the coherence of the explanation of performance that matters, rather than the accuracy of the prediction.) The Companies Act 2006 has now established the principle of protection, but we await DTI guidance on implementation.

## 2. Electronic reporting

From early 2007, it seems likely that UK companies will legally be allowed to use the internet and email as the default option for sending information to shareholders, sending paper copies of annual reports and other information only to shareholders who request them. This is likely to cause issues during the transition phase, mainly around the need to communicate the changes to shareholders. But companies will also need to develop new processes to handle the online materials, whilst maintaining the old-style paper reports for those who want them.

As firms need to provide more information to more people in more forms than ever before, it is likely that there will be a shift to new models for gathering and managing 'parcels' of information, and disseminating them in different ways to different audiences. The annual report, as the key strategic and operational summary of the business, is likely to remain central to those developments.

## 3. Global developments

The current trend is towards more international harmonisation of accounting standards, beyond the EU's enhanced Business Review. The International Accounting Standards Board (IASB) has set out a roadmap for the convergence of the International Financial Reporting Standards (IFRS) and the US Generally Accepted Accounting Principles (GAAP) between 2006 and 2008, and has committed not to introduce any new standards before January 2009. In addition, its proposed management commentary offers the opportunity to equip global markets with a regime of corporate reporting and accountability that is both forward-looking and pragmatic.

For multinational companies no longer having to prepare accounts to meet multiple different standards, the cost savings could be considerable. So could the benefits for analysts wishing to compare performance. But as well as the obvious surface differences between accounting standards, there are also differences in the underlying philosophical approaches followed in different regions of the world, especially the conflict between a rules-driven and a principles-driven approach. Harmonisation will prove difficult, and even apparently minor changes could have a major impact. In the meantime, narrative reporting provides the opportunity to clarify any confusion caused by reporting numbers under different conventions.

## 4. Changes from the major accounting firms

The recent call by the major accounting firms for a radical change to the current financial reporting model would have an even more significant impact on corporate reporting than the changes we have just seen. The firms have called for quarterly financial reporting statements (with a historic perspective on performance) to be replaced by real-time, internet-based reporting that would encompass a wide range of financial and non-financial performance measures. This, they suggest, would provide a more valuable indication of company value and its future prospects than current reporting. It seems unlikely that these changes would happen quickly. But the shift from providing historic to real-time

information, and the associated shifts in systems, processes and relationships with external auditors, would be so fundamental that this is an issue no Finance Director can afford to ignore.

#### 5. Improving business performance

It makes no sense to have two separate processes for gathering and reporting information: one for external audiences and one for the managers of the business. As the focus of management information shifts away from measures of past/current performance towards indicators of future performance, it is common sense that external reporting systems will become more closely linked to those used for internal reporting. At one level this will include the identification, tracking and integration of financial and non-financial key performance indicators (KPIs). At another, it could extend to measuring how well corporate values are put into practice (since values drive behaviour, and behaviour drives results). Ultimately though, these changes will be about improving the board's understanding of its business model, improving its ability to manage that business model, and enabling it to develop more robust business models for the future.

Corporate reporting is currently undergoing a period of significant change; one that can be expected to continue. What is important during times of external change is to be clear about objectives and stick to them. When new regulation comes along, it is essential to hold to these objectives and reject the compliance mentality which merely asks "What do we have to do now?". The challenge of new regulation is not about working out what the regulator wants. It is working out what the company wants and then finding a way of achieving that within the framework laid down by the regulator. Companies which use what we have said here to define clearly why they are doing reporting, and the principles they will use to achieve those aims, will have a strong compass to guide them, no matter what regulatory regimes may arise, and they will continue to find that the questions which their reporting answers are also the questions that their boards should be asking all the time.

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Other Tomorrow's Company publications include:



- \* Originally published in 1998 and re-published in 2006
- \* Report focuses on a number of key principles, and played a vital role in developing the DTI's guidelines for its mandatory OFR
- \* Much of what is detailed in this report still holds true today, and continues to be a foundation for work by Tomorrow's Company in the field of reporting



- \* The second in a series of publications examining the challenges and choices facing tomorrow's global company
- \* It outlines the issues of climate change and then examines the efforts made, to date, to create a global framework for action, before looking at how companies feature in the potential solutions
- \* Published in 2006
- \* Free to members of Tomorrow's Company



- \* The third in a series of publications examining the challenges and choices facing tomorrow's global company
- \* It is a brief summary of some current practice and thinking - and a stimulus to further discussion and research around corporate purpose and value
- \* Published in 2006
- \* Free to members of Tomorrow's Company

## Background to Tomorrow's Company

Tomorrow's Company is a not-for-profit research and agenda-setting organisation committed to creating a future for business which makes equal sense to staff, shareholders and society. Its business-led programme of publications, events and activities focuses on three issues fundamental to the future of business:

- \* an improved investment system
- \* an inclusive approach to leadership and governance
- \* closing the gap between business and society.

For more information about becoming a member and the work of Tomorrow's Company please visit [www.tomorrowscompany.com](http://www.tomorrowscompany.com)