

Tell your story, warts and all

CR reporting means defining company values and communicating them as inclusively and transparently as possible, says **Mark Goyder**

Although corporate responsibility has been embraced by the business community, there is a danger that in some countries, including the UK, people working within the sector could lose sight of what it really stands for.

To put it simply, there are two sides to running a successful business. On one side is the hard stuff: performance, sales, turnover, efficiency and incentives. On the other, the soft stuff: behaviour, social impact, sustainability, reputation, values and ethics.

The soft stuff is the most difficult to get right. Get the performance side wrong and, provided your reputation and track record is strong, investors will think you worth another chance. Get the responsibility part wrong and it could permanently tarnish your reputation. You may be pursued through the US courts, and fall into a vortex of hostility from the media and your stakeholders.

I am particularly suspicious of companies that boast about having 'corporate responsibility values' – the implication being that values are there to be wheeled out on Sundays and special occasions when the focus is on the company's responsibility, and not linked to the business's operations as a whole.

Values are the bedrock of any organisation, and CSR is simply one part of the whole process by which a company imparts its values.

It is the job of leaders to ensure that values are widely understood and applied. In any well-led organisation, no one, however technically competent,

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deserves to stay in their job if their perceived behaviour is inconsistent with what the organisation stands for – as Paul Wolfowitz discovered earlier this year. It is no accident that at Marks & Spencer, the group monitoring its 'Plan A' has not been named the 'CR' committee but the 'How do we do business' committee.

Which brings us to the process of CR reporting. It is, for the same reasons, a mistake to start planning the reporting of your company's CR without first having a clear mandate from the CEO that links what you are doing to the values and strategy of the organisation.

One of the best ways to understand this is to see it as part of the 'virtuous circle of governance' (see below).

The first thing a well-led organisation does is to establish why it exists (its purpose) what it stands for (its values) and how it is going to be successful in its strategy or success model.

THE VIRTUOUS CIRCLE OF GOVERNANCE



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This in turn depends on being clear about all the relationships that can make or break the organisation, and having mapped these out, identifying key performance indicators that best reflect success with your customers, your employees, your suppliers and all the communities upon which you depend or have impact. You can only start to report when you know what success looks like, how it will be measured, what your targets are, what your values are, and how you intend to monitor your success in upholding them.

This brings us to the question of materiality. Put simply, there are two overlapping areas of focus for corporate reporting: the enterprise and society. The primary focus for your shareholders and the experts who inform their judgments is the enterprise. Does it have solid performance and good prospects? The primary focus for society is the nature of your contribution to economic and social wellbeing and the environmental sustainability of the world around you. What are your negative impacts and how are you mitigating them?

Brown: abolished the OFR in favour of the 'Enhanced Business Review'

Because of risk and opportunity, these concerns overlap. The risk of you not mitigating your environmental impacts is that it could lead to a community or regulatory backlash, and so to litigation, compensation claims and reputational damage. Equally, stakeholders who enjoy no direct dividends from your performance will still want to know about your financial performance – if you are about to go out of business, they stand to lose in all kinds of ways.

It is against this background that those operating within the UK need to understand the evolving practice of corporate reporting, and the breakthrough represented by the Operating and Financial Review (OFR), which Gordon Brown abolished, then quickly reinstated in the guise of the 'Enhanced Business Review'.

It was in 1995 that a group of business leaders involved in the original Tomorrow's Company Inquiry suggested a change in the definition of directors' duties. This change was effected in the Companies Act 2006. Without compromising the accountability of directors

to shareholders, the law makes it clear that directors can only fulfil their duty to the company if they take full responsibility for their relationships with all stakeholders.

This inclusive approach, which has been championed by Tomorrow's Company, was also the basis for the OFR. In 1998, Tomorrow's Company followed up its recommendation on directors' duties by advocating inclusive reporting. 'Sooner Sharper Simpler', first published that year, sets out a vision for the annual report of the future, comprised of a concise 'core report' with supple-

mentary reports on remuneration and social impacts branching off it.

The reform process that culminated in the 2006 Companies Act applied this inclusive logic to the duties of directors and of reporting. If shareholders are to hold companies to account, it reasons, then the company should take a more inclusive approach to reporting. The urgency of this reform was underlined by the reporting failures at Enron and WorldCom in 2002.

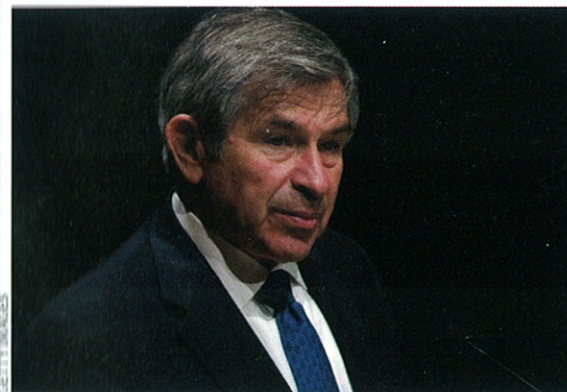
The OFR was designed to improve transparency of corporate governance and, therefore, business performance.

HOW DO YOU GO ABOUT REPORTING?

- Set out your purpose, values success model and strategy, and make a 'core' of reporting that covers your shareholder and your CR Report.
- Map your stakeholders.
- Think about the distinction between stakeholders as contributors to your success, and stakeholders as audiences (eg the need to report on employee retention). Do not assume that the 'social' audience only want the 'social' report. Staff, suppliers and many other stakeholders want to read more about the total story of which they are a part.
- Ensure that your company has an inclusive approach to its Business Review/OFR/ Core report.
- Work out which of your CR indicators are material to future financial performance and ensure these are covered in your Business Review.
- Have a set of core messages common to all audiences and then decide what you tailor on top of this for each key stakeholder group – this must include a core of purpose, values, and key business performance and responsibility data.
- Use trends: show performance over a number of years. The real relevance of indicators is that they are a guide to inform the readers' overall judgement, and most judgements cannot be made on one year in isolation.
- Explain variation from target honestly: do not drop inconvenient indicators. Acknowledge failure.
- Warning: the customary division of reporting into 'financial' and 'non-financial' categories is misleading. Revenues, earnings, dividends, costs and other financial metrics are measurable financial outcomes of business activity, but so-called 'non-financial' factors such as poor employment conditions or pollution incidents can have a significant impact on a company, including on its financial results.
- To be credible, reporting on social and environmental issues has to be undertaken with equivalent rigour to conventional financial reporting and as part of an integrated framework that recognises that these factors are connected to financial and operational performance.
- Cover good and bad news – what different stakeholders want to hear about and not just what the company wants to talk about. In this way, the company demonstrates that it is living up to its values and its definition of success.
- Set up the opportunity for dialogue so that you are able to learn from your stakeholders and improve next year's communication as a result. Companies that enter into public dialogue with critics can rapidly identify and then challenge unrealistic public expectations.

It was intended to focus directors' and shareholders' assessments on all internal and external issues affecting that performance.

Although its repeal was described as leaving a significant 'policy vacuum', it was soon replaced by the EU's 'Business Review'. This was part of the EU's 2003 Accounts Modernisation Directive, and required annual reports published after 1 January 2006 to evaluate risks and uncertainties to an unprecedented level. Although this legislation does not go as far as the OFR in requiring companies to report on strategy and busi-



ness prospects, it has had a much wider impact than the OFR, affecting more than 37,000 unquoted as well as quoted companies in the UK. The OFR would only have applied to a group of quoted companies, and has now been replaced for this group by the 'Enhanced Business Review', which has many of the same features.

At the same time, in January 2006, the Accounting Standards Board issued its legal 'Reporting Standard' for OFR almost verbatim as a 'Reporting Statement'. This provided a clearly defined 'statement of best practice on OFR' for any company that wished to follow it, irrespective of whether or not there was a legal requirement to do so. The most recent research by Tomorrow's Company suggests that, in practice, the ill-fated attempt to abolish the OFR has made little difference, apart from spreading

confusion: almost half of all the FTSE 100 firms appear to have gone ahead with an OFR regardless.

The public are often bitterly critical of large companies, particularly global companies, fearing that they are only interested in making money. It is crucial that a company breaks through this cynicism by demonstrating the part that its values play in its success (one of the recommendations made by global leaders involved in the Tomorrow's Global Company inquiry). It is important to get companies telling their own story, in their own language, while remaining free to use their own chosen communication methods.

Over time, we will begin to develop a common language that helps the reader compare one report against another. It has taken financial accounting 500 years to reach its present, incomplete, state of harmonisation. Although there are sterling examples, such as Novo Nordisk, integrated reporting is still some way off.

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 that merely asks, what do we have to do now?. The challenge of regulation is not to work out what the regulator wants, but to work out what the company wants and then find a way of achieving that within the framework laid down by the regulator.

Companies that use what I have outlined to define clearly why they are reporting, and the principles they intend to 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 answered by their reporting are the same questions being asked by their boards.

Mark Goyder is founder director of Tomorrow's Company. Further information about the publications mentioned and its latest inquiry, Tomorrow's Global Company, can be found at www.tomorrowscompany.com.

Wolfowitz:
his perceived
behaviour was at
odds with World
Bank's image