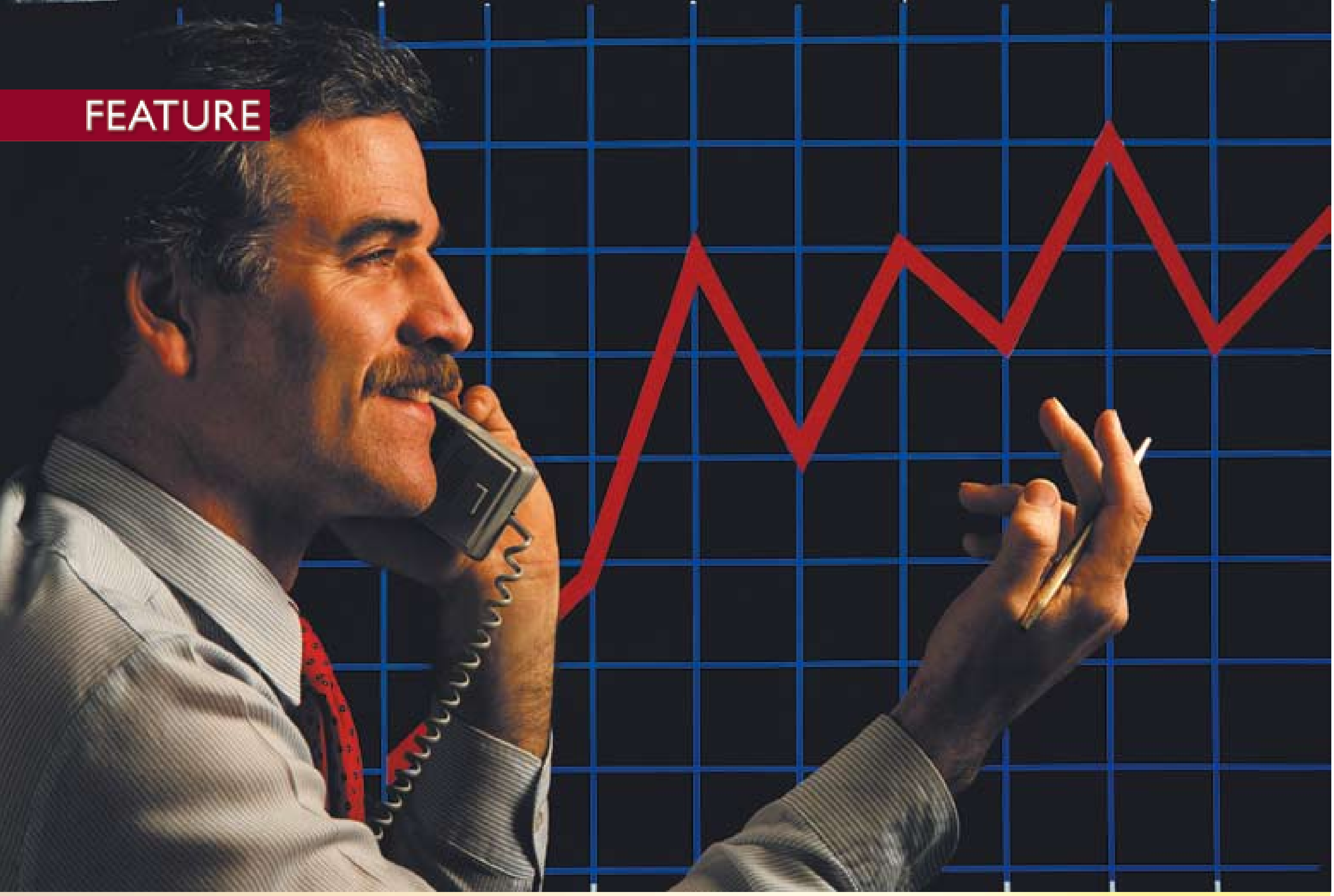
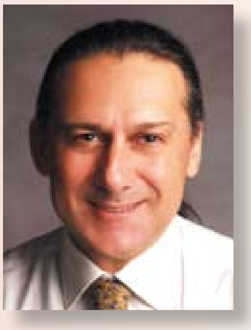


FEATURE

The Relationship Between Triple Bottom Line Reporting and Corporate Governance



By Paul Zaman of Qualvin Advisory, an organisation that provides advisory services to the Board, CEO and CFO of unlisted companies in S.E. Asia

Corporate Governance is often misunderstood. A strict and simple interpretation is creating long-term shareholder value. Often the focus is upon the risks and potential legal consequences of not having good corporate governance. Also Directors are reluctant to include additional information requested by investors due to the threat of exposure to legal risks often identified by the legal advisors.

Investors simply need information to make informed investment decisions. They seek information on the corporate goals, strategy and execution operational and financial track record. Investors always have alternative choices. If governance is poor they will invest elsewhere.

Long term investors, also increasingly value those corporates that undertake what is termed "triple bottom line reporting", because the corporate's sustainability and social report coupled with the annual report demonstrate that good corporate governance and planning is in place. Corporate sustainability, corporate social responsibility, the global reporting initiative and triple bottom line reporting are names for broadly the same issues – they all pertain to a company's reporting about its financials, stakeholder interests and the broader environmental impact of the business.

The triple bottom line is not a club sandwich, but very serious stuff. It involves the reporting of the strategy and operational performance of a company within the three primary dimensions of the financial, stakeholder and environmental performance. These reports are indication that robust planning is taking place in the company.

A company selects the most important and key issues to be in their triple bottom line plan and report. This is usually included in the reports submitted for the annual general meeting. The financial statement falls within the company's standard annual report, and the stakeholder and environment statements often within a company sustainability report. All have historic reporting on operational parameters. Many have triple bottom line planning goals and strategy statements on how to improve performance.

The stakeholders include the owners, plus banks, employees, suppliers, customers and other key people closely involved. Social issues include quantifying equal opportunities and labour usage in undeveloped countries, both directly and via suppliers. The environmental dimensions cover areas like usage of reusable energy, carbon dioxide emissions, resource recycling and pollution control.

Remember that value creation comes from planning not reporting.

Corporate Social Responsibility – Entrepreneurial Businesses, Start Young!

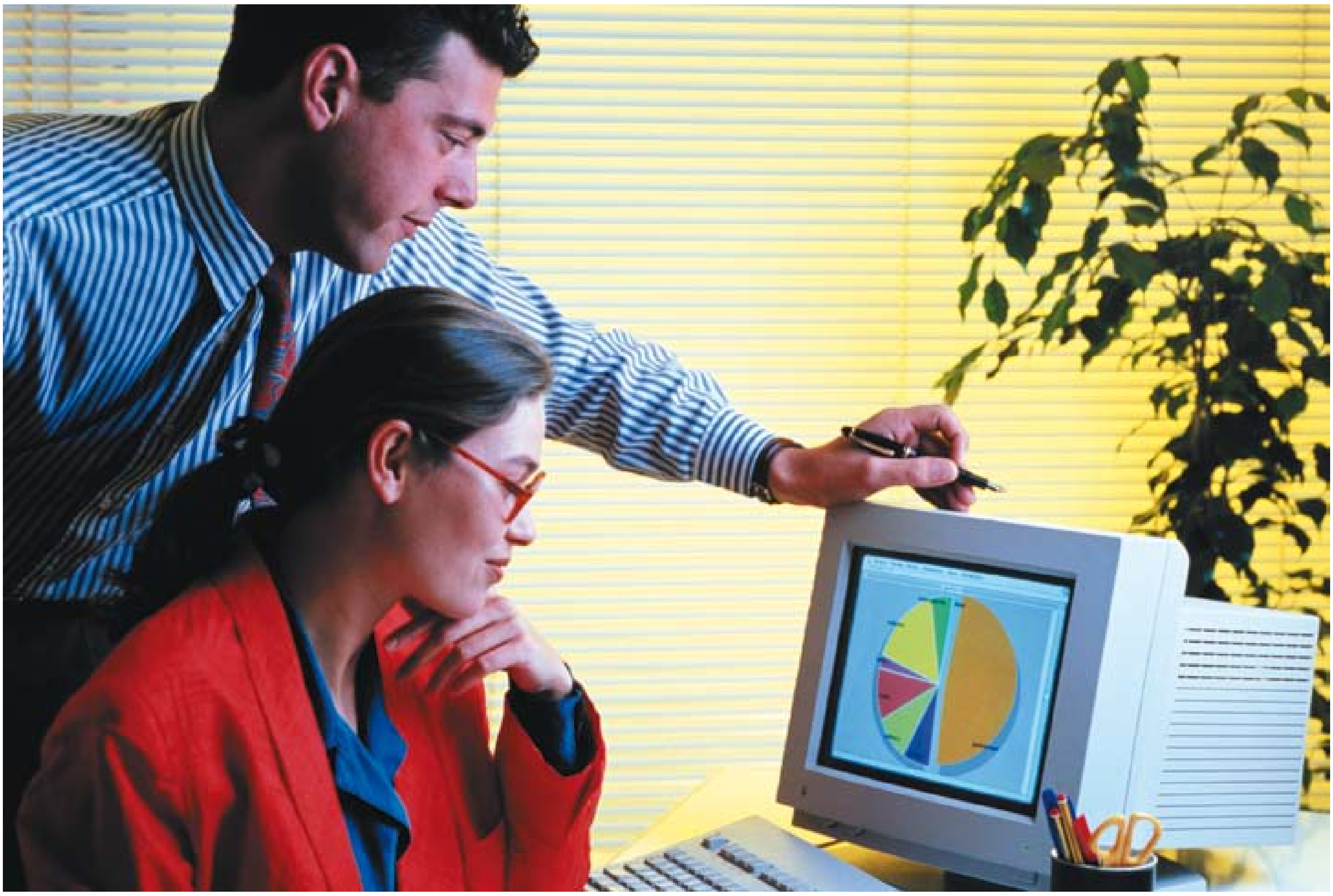
How does an entrepreneurial company embrace and execute corporate social responsibility? There are two major global initiatives on CSR reporting, also known as triple bottom line reporting. The Global Reporting Initiative (GRI) sponsored by both the United Nations and the Institute of Social and Ethical Accountability a not for profit institution set up in 1995.

AccountAbility focuses upon assurance, which means the process of reporting and the audit role. The GRI focuses on a process of identifying and reporting upon key relevant CSR issues. The GRI has a scheme for small businesses called High Five. This is actually a fantastic way for any size business to start CSR reporting. GRI has over 600 users and AccountAbility over 300 users. Each is growing fast and is just the tip of the iceberg.

Many large multinational companies are doing CSR including Sony, Canon, Microsoft, McDonalds, Telstra, Heineken, Hewlet Packard, Lend Lease, Phillips, TNT, and Westpac. There are many more companies that use these guidelines, yet do not formally submit reports back.

The Benefits of Corporate Governance and Social Responsibility Reporting

Proper corporate governance provides for two systemic outcomes that benefit the shareholders in terms of lower



risk and better investment returns. The internal perspective means improved operational performance. The external perspective gives a lower cost of capital. That is, lower interest rates and better terms for raising debt, as well as often a high quality group of sophisticated equity investors. Pension funds are increasingly active in voting on governance issues and rewarding a company with good governance by remaining a long-term investor.

The Key Point is...

With corporate governance we must also ask the question: Whom are we being transparent for? Ticking a compliance list of key processes to say that the annual report has disclosure against a prescribed list of items largely misses the point. The key point is to ensure that the shareholders are getting the level of ongoing disclosure that they need to support their ongoing investment decisions in the company. Some investors are transient, while others are major global unit trusts and pension funds with a wealth of investment experience and corporate governance experience. Surely then, the sensible pragmatic measure of corporate governance and transparency is to watch what institutional investors are doing with their money.

There have been many studies of institutional investors and fund mangers focusing on the correlation between a company's equity market value and good corporate governance. The findings indicate that companies with good corporate governance are rewarded with an approximate 20 percent increase in value compared to those with inferior governance. In the emerging equity markets, this premium for good governance can be much higher. However, opaqueness does not necessarily mean that corporate mis-governance is occurring.

Another benefit of the CSR Report is making corporate social initiatives more meaningful. Corporate social initiatives differ from corporate philanthropy in that they are aligned with the company's vision and the CSR strategic issues. This means that a company's social sponsorship affects the key community stakeholders that the company is involved with and these stakeholders recognize the power of your intention and commitment. The CSR Report is a critical window on management's claim of being socially responsible. It means that corporate sponsorship makes sense to all that witness it and that this sponsorship becomes justifiable and sensible to all owners and beneficiaries.

How to Undertake Triple Bottom Line Planning and Reporting for a Business

In my view, the Global Reporting Initiative (GRI) has a focus on the financial, management and operational key performance indicators that make it easy for a business person to get great results. AccountAbility has a focus on auditing the process and dialogue with the stakeholders to verify the voracity of the data. I like to stay focused upon creating shareholder value, which means the GRI five-step process is a great starting point. GRI also, although a CSR tool is aligned to triple bottom line planning and reporting.

STEP 1: Get Board and Senior Management and owner sponsorship.

STEP 2: Using the business vision, objectives, strategies, activities and plan identify the stakeholders and map out the company relevant key interest areas.

STEP 3: Identify from the GRI the relevant type and nature of indicators to report upon that match with the key interest areas. Collect and collate historic data on these areas and candidate indicators. Identify the historic relevant management activities in these areas and determine what enhancements and new activities could be undertaken.

STEP 4: Verify data quality with internal and external stakeholders. Engage in dialogue with key external NGOs whom are respected surrogate representatives of the external stakeholders. Set targets, management activities and accountabilities for the forward-looking years of the CSR. Write, finalise and distribute the first report.

STEP 5: Collect feedback from the report in areas of improvement in triple bottom line reporting performance. Plan the next steps of the triple bottom line strategy and execution. Get recognition from management, staff, suppliers, and customers for the triple bottom line awareness and commitment.

Developing a corporate sustainability report, like most business wide projects, requires the support and commitment of top management. Within a small business, this support and commitment is required from the entrepreneur owner and founder. Much of the necessary information to develop the report will already be in the company. It just will simply lie in different areas, awaiting collation.

An initial step is setting the context and significance of CSR reporting for the company. There must be real benefits in reporting, such as enhanced reputation, increased profit, improved access to capital, improved access to information, new market opportunities, improved relationships and increased staff motivation. Reviewing CSR reports by industry peer companies will help. This will help identify the major environmental sustainability and integrity issues and the social welfare and human rights issues affecting your industry sector. These can then be listed, profiled and ranked for importance.

Like an annual report and financial statement, there are a few guiding principles on what to report. These include materiality, comprehensiveness, inclusiveness and transparency. The quality and reliability of reporting is based upon reproducibility and accuracy. The CSR report is intended for senior management to make informed

decisions about how to improve the business performance, and so strategy and execution plans. The CSR reporting must be timely and relevant for management action. Lastly, the process for data gathering should be auditable to demonstrate that the underlying information and report is fair and true.

One of the initial dilemmas is identifying whom your company's key stakeholders are. Candidates include: employees, family, community leaders, owners and equity investors, banks, financial analysts, suppliers, customers, end users, NGOs, labour associations, licensing bodies and environmental inspectors. Once established, you then map the key CSR issue areas to each stakeholder and rank the level of stakeholder's interest.

The next stage is dialogue with a representative set of stakeholders to verify their level of interest and understand their expectations for your business. This could be by a town hall meeting, one to one meeting or even an email questionnaire. With this feedback, you can gauge if you are satisfying the key stakeholders' interests.

The CSR report areas can now be formulated along three themes. The economic theme impacts typically affect customers, suppliers, employees and owners. The Environmental theme typically impacts materials, energy, water, pollution, compliance, transportation, and your products and services. The social theme relates to labour practices and conditions, human rights, community at large, and product responsibility.

The next step is to choose core performance indicators. Industry peers CSR reports will guide you in the selection. It is key to select the core indicators relevant to your business and your CSR areas of interest. Formal sources of information are the financial accounts, utility bills, human resource records and supply chain contracts. The focus is on setting objectives, strategies and action for improvement. Like all planning, iteration and consultation is required.

To capture the economic benefits of the CSR initiative, some results need to be published and disseminated. For small businesses, this could be via notice boards, web pages, newsletters, meetings, press releases, presentations, or industry conferences. The communication method can be matched to the stakeholder groups identified to ensure that you get your company's message out there. Naturally, senior management needs to do a final review before distribution of the CSR report.

Conclusion

The correct perspective for corporate governance is the focus upon increasing long-term shareholder value. The often held view, of a legalistic perspective upon the risks of fulfilling Director's duties and obligations is misleading.

Investors need information to make ongoing informed investment decisions. This is the requirement that drives the ongoing disclosure policy for a company. It is a key role of the Board and the investor relations officer, it is a key duty and not a burden and risky activity.

Investors want to understand the corporate goals, strategy and execution track record, to make informed investment decision. This is detailed financial and operational data which a financially astute investor relations officer can help support the Board and CEO deliver. If a company fails to provide financial and operational information then there are plenty of other higher quality and lower risk investment opportunities.

Increasingly, investors favour companies that undertake triple bottom line reporting as these companies have higher quality corporate governance. For listed companies this is often rewarded with much higher valuations. ■