

Putting non-financial data TO WORK

If companies are to be held accountable for how they are managing their material issues, there is much to do to improve the standard of indicator-based reporting. The question remains: when will non-financial data translate into business intelligence?

The call for improved disclosure in sustainability and integrated reports is inextricably linked to the quality of the non-financial data that these reports are built on. As they heed this call, companies confront a daunting array of frameworks and measurement protocols aimed at clarifying data gathering and reporting expectations and processes. But despite their intentions, these frameworks are not a panacea; reporters and audiences are still confused. And where confusion exists, achieving the ultimate goal – using non-financial data as a valuable decision-making tool – remains elusive.

By defining scope, boundaries and materiality differently, companies limit readers' ability to compare performance across different businesses and sectors. Even common and well-recognised issues lack this comparability. For example, a measure that seems as straightforward as staff turnover is calculated in nearly as many ways as there are companies

MULTIPLE FRAMEWORKS TO GUIDE – OR CONFUSE – REPORTING?

Although they are intended to help, the broad range of reporting frameworks can also detract from comparability as reporters apply different treatments or take varying approaches. And with no clear winner in the standards war, the burden is on the reporters to select the frameworks most appropriate to their situation.

Frameworks range from high-level, principle-based guidance to more explicit measurement protocols. But even within the second category, the degree of prescription varies. The Global Reporting Initiative (GRI) and Sustainability Accounting Standards Board (SASB), two of the more instructive internationally-recognised frameworks, provide a clear example of this.

- GRI: A popular framework offering a combination of principle- and indicator-based guidance in general and sector-specific terms. Its latest iteration, the G4 guidelines, places greater emphasis on materiality and enables companies to select the indicators they consider most relevant to their business. Although this flexibility is sensible in that it encourages organisations to choose relevant measures, it risks detracting from comparability between companies.
- SASB: Guidance designed by American accountants for required Securities & Exchange Commission (SEC) submissions such as 10-K and 20-F forms (as opposed to broader sustainability and integrated reporting). This framework emphasises materiality at a sector level through a series of industry-specific indicator guidelines. While the level of required detail is commendable, its uptake is perhaps the greatest obstacle to enabling comparisons between companies.

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on the Johannesburg Stock Exchange (JSE). Should the figure include voluntary and involuntary departures? Should it be calculated as a percentage of the average workforce size or headcount at year-end? What about part-time employees?

Though many bemoan the lack of standardisation, the end result – when balanced with the need for relevance and tailorability – compromises the reader’s ability to benchmark performance, or improve their understanding of the company’s unique dynamics.

Meaningful data

Data on its own is not worth much. Data as an outcome of a management process is. If there is one thing all reporting frameworks and audiences can agree on, it is the need for businesses to reduce the clutter and focus on what is material. This applies to the reports companies produce as well as the way they manage the issues contained in those reports.

Items measured and reported should be embedded in performance management systems at individual, functional, divisional and group levels. Too often, companies haphazardly scrape together data on sustainability topics just weeks before the reports go to print. Issues important enough to be reported on should be important enough to be robustly managed, and vice versa. A clear business purpose should be articulated and a simple test applied: no purpose, no data.

Data as a decision-making tool

Meaningful data requires interrogation from the provider and the end user. Many would argue

that progress in South Africa’s sustainability arena has been driven primarily by a need to conform to standards, rather than a demand for sensible data by stakeholders. As a result, the outcome has been volumes of reported data that is not applied to internal or external decision-making. If data is not interrogated, questioned or benchmarked, sloppy reporting will go unnoticed and will not be a suitable decision-making tool. A vicious cycle forms.

Data as a tool for driving change

Management should actively use data to drive internal efficiencies and improve business performance. These prospects alone should justify the effort of generating this data – conditional, of course, on the materiality of the issues. Again, if an issue is not important enough to be managed, do not waste time tracking and reporting it. On the other hand, if it has the potential to materially impact on business performance, it should be embedded into management systems, including executive and divisional key performance areas. In reality, few internal decision makers are at the point where they are willing or able to use the data meaningfully. However, certain pockets of promise exist. In some areas, such as mining safety and customer satisfaction in retail sectors, data is already actively used to drive performance. Nevertheless, many powerful non-financial indicators continue to fall outside performance management systems.

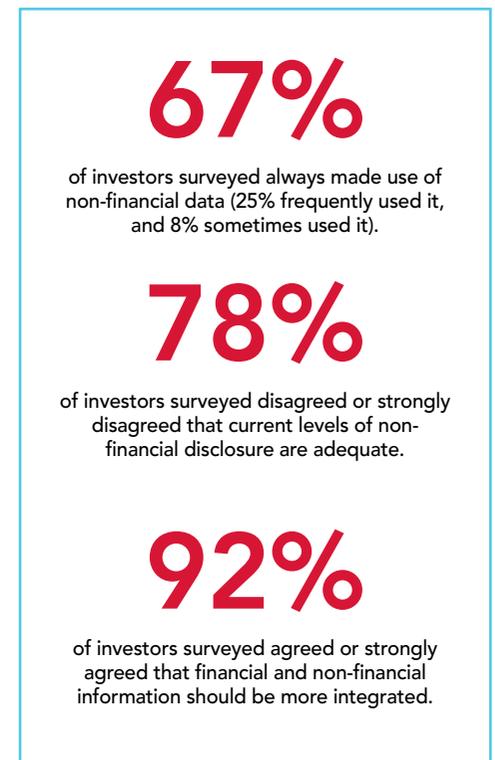
Data as a tool for investment decisions and tracking special interests

Potential external users of comparable datasets

include investment analysts and interest groups concerned with particular issues. Analysts are looking for comparative performance information, yet struggle to incorporate reliable data into their models. This is partly because they cannot determine (or they are not being informed about) how the data impacts on performance and risk management.

While analysts are being led into this space by the need to comply with investment standards, the business rationale remains lost to most. Are they interested in insisting on improvements in reporting, or would they be if the data was better to begin with? In this chicken-or-egg scenario, it seems that, ultimately, much of the non-financial data is produced at great cost and effort, presented publicly but not used to affect decision-making.

In the investment domain, sustainability agreements such as the United Nations Principles for Responsible Investment (UNPRI) and the Code for Responsible Investing in South



Source: “What do investors expect from non-financial reporting?” survey by the Association of Chartered Certified Accountants (2013), conducted with 94 analysts and investors from 18 countries.

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Africa (CRISA) are moving the needle on interest in environmental, social and governance (ESG) issues. However, significant variation exists in analysts’ ability to use the data. Approaches range from ‘not at all’ to complex proprietary evaluation tools. Some third-party firms, Trialogue included, are developing tailored tools to support the investment community in meeting their UNPRI, CRISA and Regulation 28 obligations.

Other external stakeholders do refer to data by exception, picking up on hot issues such as executive pay. However, the media and other stakeholders are not fully engaging the data or questioning the business on what data is presented. This is probably due to apathy and a disconnect between the stakeholders’ interests and the data shared.

Ultimately, end users should be asking themselves if the data makes sense and is believable. At present, too many are taking reports at face value, and this can lead to significant oversights. Analysts need to learn how these issues can be collectively applied to their risk-adjusted financial models and call for the right data. If analysts cannot figure out how carbon reduction translates into lower costs, mitigated risk or improved access to markets – they should not ask for it.

Assurance is driving data robustness

Although non-financial data is not traditionally subject to the same level of inspection as financial statements, it is still beginning to benefit from closer scrutiny in certain areas. While the non-financial assurance

field is struggling to find the same degree of robustness and replicability as financial assurance, it is a dynamic, ever-evolving field. A panellist at the Trialogue EY Sustainability Forum on non-financial assurance likened it to building a plane while it’s taxiing down the runway.

▲ *See the summary of Trialogue EY Sustainability Forum discussions, page 40.*

The annual process of verifying a company’s Broad-based Black Economic Empowerment (BBBEE) credentials, for example, means that a wealth of data related to employee diversity, ownership, procurement, skills development and socio-economic development is exposed to independent examination. This lends an extra degree of credibility to these areas and is helping to strengthen companies’ processes around measuring non-financial performance. Assurance can cover a combination of processes and/or indicators. While the latter is more directly tied to the quality of non-financial data, it is important to note the correlation between sound processes for managing and communicating sustainability and the quality of the data demonstrating performance.

However, independent verification comes at a cost and companies should carefully consider the needs of the business as well as its stakeholders when deciding what indicators to assure. Companies at the early stages of non-financial assurance find it helpful to engage internal auditors before bringing in external assurers. These trial runs can help accustom the company to data collection and the assurance process in a non-threatening way.

Where do we go from here?

While there are improvement opportunities for compilers, communicators and end users of non-financial data, progress is evident. Growing public interest and regulatory oversight of certain issues is already forcing scrutiny of the quality and comparability of associated data. This includes issues that feature prominently in public discourse, such as fatalities, strike days or lost production in the mining sector. And as the quality of internal metrics improves, so too will companies’ ability to meet external scrutiny with meaningful data.

As the link between sustainability and financial performance is solidified in stakeholders’ minds, a wider range of issues is likely to be managed, measured and reported. Assurance of this data will be more targeted and relevant as companies are held accountable for their performance against such issues.

Will there be a winner in the ‘standards battle?’ With a growing emphasis on the key reporting frameworks complementing – rather than competing with – each other, reporters will hopefully converge on a more consistent treatment. Ultimately, this will improve readers’ ability to compare performance over time and between companies and sectors. Hopefully, pressure from the providers as well as users of data will continue to push the remaining frameworks towards more sophisticated and complementary processes, ultimately resulting in more meaningful and useful data.

With time and repetition, data collection and reporting become more routine and robust. It’s worth noting that companies are on a journey and as they become more comfortable with capturing, combining and communicating data, the end result is likely to become more credible. As stakeholders, we stand to benefit from this improvement process. We should respond with tools that have been improved to ensure they’re capable of realising the data’s potential as business intelligence. ►