The Institute of Chartered Accountants in England & Wales

Corporate Governance

The 21st Century Annual Report

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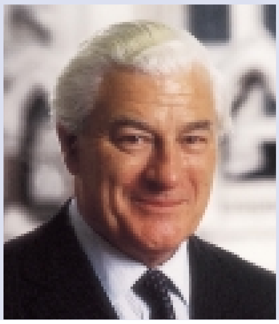
21 Century Performance Communication 21st Performance

SIR BRIAN JENKINS | **Chairman, Corporate Governance Group**
Chairman, Woolwich plc

“We must now begin without delay to focus more clearly on the issues of what information should be provided and the ways in which it can best be transmitted to fulfil the needs of the 21st century capital markets.”



Effective communication with a company’s shareholders and other stakeholders is a vital constituent of good governance and it is essential that interested parties be given a clear and balanced view of a company’s performance.

Until a few years ago, the annual report was very much a set menu with no choices. The one report was the primary document given to all shareholders. The focus was on financial information and by and large continues to be so although the Operating and Financial Review has been a very worthwhile innovation.

Then, summary financial statements were introduced. Many more companies have started to introduce them in recent years, especially those such as mine with a very large shareholder register.

With technology, a whole new vista of opportunities is, however, opening up and we are in the world of à la carte with potentially infinite alternative menus of information able to be given to users of financial data. The principal limitation will be companies’ ability or willingness to provide additional disclosures.

Whilst technology is an enabler, if its potential is to be realised, many businesses will need to change their approach to providing information, moving away from primarily seeking statutory compliance and towards meeting market needs. And there is a variety of different markets including, for instance, financially sophisticated investors who may have large or small holdings, those more interested in non-financial performance information and users primarily interested in social accountability issues.

There will undoubtedly be challenges to be faced in the new era such as deciding how to strike the balance between transparency and not giving away too much competitively sensitive information as well as determining how frequently information should be updated. These issues must be addressed but they are not reasons for staying where we are.

In this new world, the notions of what information should be included on performance measures will also be subject to substantial change with more sought on non-financial performance indicators and on, for example, the value of a company’s intangible assets, including its human resources and customer satisfaction ratings, the key drivers of wealth in many companies.

We must now begin without delay to focus more clearly on the issues of what information should be provided and the ways in which it can best be transmitted to fulfil the needs of the 21st century capital markets.

SIR BRIAN JENKINS

TOWARDS A MARKET-LED REPORTING MODEL

EDITORIAL

Corporate reporting has traditionally been regulation-led with innovations arising principally from new accounting standards and, less frequently, changes in legislation. A strong theme to emerge from this year's third governance conference held at the Institute in September, the edited proceedings of which form the basis of this report, is that the voice of the market-place is going to be far more influential in the future.

The table opposite highlights that this shift towards users having a greater say in the information presented by companies is part of a major shift in reporting that is already underway. As Alan Benjamin succinctly put it: 'The annual report of the 21st century will not be annual and it will not be a report: it will be an up to date informative, permanent dialogue.'

Reporting changes are being driven by globalisation, new technology and increased notions of accountability by corporations, professions and others. If we are to develop a successful new reporting model to meet the needs of the 21st century a number of questions will need to be answered. Chris Swinson, the Institute President, struck at the heart of the challenge when he asked: 'What are the real permanent sustainable needs which require a real sustainable answer?'

Mrs Justice Arden suggested we should ask, 'What is the company for?' before seeking to determine the interests of the various stakeholders. Whilst it may be difficult to reach a consensus on this issue we may be able to move forward from a pragmatic base which recognises that all principal users require information on a company's performance and viability. What is different, however, compared to, say, a decade or so ago is what many understand by these terms. The concept of performance and viability being measured in purely financial terms is giving way to broader measures of success. Chris Fay, chairman and chief executive of Shell UK, wholeheartedly embraced this change when he commented that: 'We are clearly at the start of a long and difficult journey towards a new type of business reporting which takes full account of economic, environmental and social performance.'

There are also demands for more information on expected future performance. Should a forecast or projection be provided or, alternatively, information allowing others to make their own judgements?

Other issues that need to be addressed include whether traditional audited financial statements take sufficient account of, for example, intangible assets and environmental liabilities and expenditure. Should more assets and liabilities be measured at their fair values rather than their historical costs? If they are, what criteria need to be satisfied if we are to be comfortable that the valuations are verifiable by the auditors? What information should be disclosed on intangible assets and the assumptions underlying their valuation if readers of the financial statements are to gain a proper understanding of them? On the other hand, are we discriminating against intangibles in our accounting system since the valuation of properties, work in progress and provisions for doubtful debts, to name but three, can also be very subjective.

Turning to the wider annual report, it is arguable that not enough attention has been given to the disclosures that are needed in addition to those in the audited financial statements. An exception to this is the Accounting Standard Board's introduction of the Operating and Financial Review (OFR). More recently, we have seen the introduction of the new narrative statement explaining how the principles in the Combined Code on Corporate Governance have been applied. Matters to be considered if more information were to be provided on environmental, employee and social issues or, indeed, on intangibles and other 'soft' assets often not recognised in the accounts, would be who should set the standards, the authority they should have and how compliance should be monitored.

Reporting in a period of change

The 'old' system		The 'new' system
Shareholder focus	➔	Stakeholder focus
Paper based	➔	Web based
Standardised information	➔	Customised information
Company controlled information on performance and prospects	➔	Information available from a variety of sources
Periodic reporting	➔	Continuous reporting
Distribution of information	➔	Dialogue
Financial statements	➔	Broader range of performance measures
Past performance	➔	Greater emphasis on future prospects
Historical cost	➔	Substantial value-based information
Audit of accounts	➔	Assurance of underlying system
Nationally orientated	➔	Globally based
Essentially static system	➔	Continuously changing model
Preparer-led regulations	➔	Satisfying market-place demands

The implementation of changes to the reporting model made possible by new technology is currently at an early stage. Companies are still essentially using a paper-based model and then transmitting their accounts via the Internet. But David Pinches' presentation offers an insight into the future shape of reporting. If, or rather when, it becomes primarily Net-based there will, as Sir Brian Jenkins said, be potentially limitless access to data stored by the company. The regulators will have to decide who should have access and whether it should be at different levels for different stakeholders depending on the nature of their relationship with the company.

Reporting is likely to move over time from being periodic to continuous with different segments of information being updated at different intervals, again rendering present notions of annual and interim reporting out of date. Against this background, users are likely to want assurance from auditors about the integrity of the underlying system that generates the information on the Internet, instead of, or as well as, an opinion on the financial statements at a given date. Analysts and others will also press for information to be in a standard format to enable it to be easily transferred to a spreadsheet and used for comparison with the performance of other businesses around the globe. Eventually, transmittal of information on the Internet or via digital television into stakeholders' homes or offices will surely count as fulfilling the obligation to communicate with them, replacing the need to post the annual report.

To enable the market place to be a successful catalyst for innovation in corporate reporting, we will need to consider what are the best mechanisms by which this can be achieved. Enhanced relevance in disclosure must not be seen as primarily an issue for a few leading-edge companies, far greater diffusion is needed. And last, but by no means least, any changes in the reporting model in any one country must take full account of developments in the international reporting arena.

CHRIS SWINSON

President, Institute of Chartered Accountants in England and Wales
Senior Partner, BDO Stoy Hayward

“The time is ripe for issues of corporate reporting to be the subject of a formal and broad review. We ought to be hard-nosed and calculating about what are the real permanent sustainable needs which require a real permanent sustainable answer on the form of the corporate reporting system in this country.”

CHRIS SWINSON

Many people are beginning to talk about the efficiency and the effectiveness of corporate reporting. It is easy at times not to think about what other people are saying about us accountants and to shut our eyes to the siren voices, some of which may lead us onto the rocks but some of which would improve what we are actually doing.

Earlier this year there was an article in the New Statesman, a journal not known for its absorption in accounting matters, which speculated that financial reports by companies must become broader and more useful and concluded that accounts should not remain the reserve of accountants.

Just before that, The Times published a spoof annual report for a period some twenty years hence from a Chartered Institute of Performance Measurement which crowed over the demise of the old-fashioned accountants who dealt with old-fashioned reports and praised the achievements of the Institute in developing new ideas on performance measurement.

Both of these articles sprang from ideas that were canvassed in this year’s PD Leake lecture which commented on academic research in the United States, suggesting that the relationship between stock market prices and reported profits was becoming more distant. The lecturer was suggesting that the stock market is increasingly taking account of sources of information other than annual accounts.

Nearer to home, Ken Wild, a member of the Accounting Standards Board, has been heard to speculate that future annual reports must answer the market’s call for more information. He mused that ways must be found to provide more information about a business’s future trading prospects, a business’s value or the value of its intangible assets, information which will inevitably be broader than that which we have been attempting to provide so far. Perhaps most controversial is the new book *Cannibals with Forks* by John Elkington of SustainAbility. Elkington identifies a series of revolutions in the corporate environment in which companies operate which, he argues, lead to concerns about the accountability of companies.

There are common threads to these events. Unhappiness with the usefulness of historical cost financial reports lies behind all of them and has led to the market being interested in alternatives.

Like many things in this country, the origins of company reporting can be traced back to Mr. Gladstone. As a member of a Mercantile Law Commission in the 1850s, he appears to have been instrumental in drafting the recommendations on which the statutory framework of company accounts was based. That framework was intended to safeguard the capital of a company by ensuring that dividends could not be declared imprudently.

The framework of historical cost financial reporting has served us well. Shareholders have been provided with information which has assisted them in judging the performance of their company and its directors. Some of the excesses of imprudent dividend declaration have been avoided. The public filing of historical cost accounts has enabled those not directly with the company to answer many of the questions that they need to answer.

There is no point in accountants working overtime to produce more and more accounting standards which serve simply to over-specify an old technology

However, accountants have long known that historical cost financial statements do not provide direct answers to all of the questions which every user of accounts might ever ask.

What is a company worth? Accountants all know that a balance sheet is not a guide to value. What are a company's prospects? All accountants know that a historical profit and loss account is not necessarily a guide to sustainable earnings. What risks does a company face? Accountants all know that accounts do not deal explicitly with risks. What are a company's intangible assets (let alone what are they worth)? Accountants know that accounts do not speculate about such matters.

The long and the short of this is that accountants have long known that historical cost financial reports do not attempt to meet the information needs of all users of accounts. Yet, for all this, the market-place has gone on using those financial reports.

Why should we now pay more attention to complaints about the usefulness of corporate reports? The answer to this may be that the assets and risks not measured by historical cost accounts appear to be becoming more important as determinants of a business's future success. Neither human capital nor intellectual capital is valued in historical cost accounts and many businesses' accounts give almost no indication at all of the nature and possible extent of their environmental obligations.

In addition, there are inequities in the way in which information is provided – privileged analysts rely on direct briefing from companies themselves – and in this country at least, thanks in some ways to Mr. Gladstone, the principle has always been that information should be equitably and freely available.

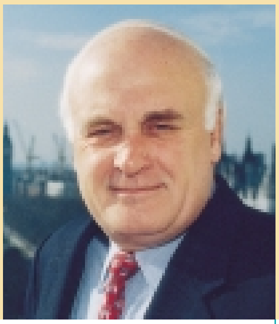
The changes in technology present us with an opportunity which we, as accountants, can either view proactively and take advantage of or let the market run away with us whilst we try to catch up as professionals.

We ought to ask how we can encourage financial reporting to meet the changing information needs of business and society. It is not that we should reject historical cost financial reporting but that we are not serving anyone if we do not pay attention to calls for change. There is no point in accountants working overtime to produce more and more accounting standards which serve simply to over-specify an old technology.

The time is ripe for issues of corporate reporting to be the subject of a formal and broad review. We ought to be hard-nosed and calculating about what are the real permanent sustainable needs which require a real permanent sustainable answer on the form of the corporate reporting system in this country. I would suggest that we learn from experience of the past.

It is now more than twenty years since the accountancy profession's *Corporate Report* surveyed the ways in which corporate reports should develop. Not all the recommendations of that report were implemented but it was influential in setting the grounds for debate. Such a review should include all parties with an interest in the subject – not only accountants, but also radical thinkers, companies, market regulators and other stakeholders.

CHRIS FAY | Chairman and Chief Executive, Shell UK Limited



“Environmental reporting should be seen as part of an effective long-term business strategy and not something to be conveniently pigeon-holed under PR or communications strategy.”

CHRIS FAY

We have reached a significant milestone in the story of business reporting in the United Kingdom. We recognise that industry's reporting achievements in the past were simply just the beginning. We are clearly at the start of a long and difficult journey towards a new type of business reporting which takes full account of economic, environmental and social performance.

We are, in a very real sense, at the corporate reporting crossroads, but one thing is certain, you can't make a U-turn at a crossroads.

However, two words of caution. First, we should remember that not all companies have even made it to the reporting starting grid. We are some way off a level playing field in this area and it may well be that in the end a level playing field proves clearly impossible to attain.

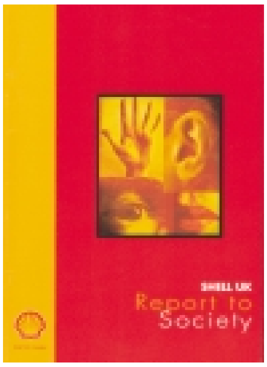
Second, the assumption that it is both possible and desirable to construct objective indicators for measuring a company's social performance may be overly optimistic. It is my view that while the world wants black and white answers in this area, we may in fact be dealing with different and shifting shades of grey. Decisions about community investment programmes, for example, may have more to do with the subjective feeling that this is the right thing to do than any objective measurement of their impact on the bottom line.

The Government DETR leaflet on environmental reporting says ‘Environmental reporting should be seen as part of an effective communications strategy and not just a public relations exercise.’ There is nothing wrong with that but we should go one stage further. Environmental reporting should be seen as part of an effective long-term business strategy and not something to be conveniently pigeon-holed under PR or communications strategy.

Many of the changes that we have already adopted in Shell's *Report to Society* feature heavily in the *Prototype plc* core company report.

The *Report to Society*, which clearly complements the 1998 Shell Group's report *Profits and Principles*, emerged from Shell's long-standing commitment to the core principles of honesty, integrity and respect for people. These principles were first codified and published over 20 years ago in 1976 and have been revised several times since.

Today, the latest Shell *Statement of General Business Principles* underpins all of our work. It underlines our commitment to sustainable development, high standards of service, community investment, social concern and perhaps, above all, to protecting the working conditions of our staff.



Shell UK Report to Society

For all that, the first Shell UK *Report to Society* clearly represents a major step forward, not least in our engagement with the outside world. The crucial point here is that in the past, Shell maintained health, safety and environmental (HSE) information in a large variety of forms. But, this was aimed very much at an internal company audience.

it is quite wrong to suggest that in some way the economic, environmental and social bottom lines are mutually exclusive

The emphasis on the importance of external audiences began modestly in the early 1990s. It has since developed through two stand alone HSE reports in 1996 and 1997 to an expanded report to stakeholders and wider society.

Changing Expectations

- Companies no longer judged solely on economic performance and wealth creation
- Wider responsibilities to the environment, local communities and broader society
- Shell UK's social responsibilities form a fundamental part of our business
- Public now demands highest standards of ethical and environmental responsibility
- 21st century company report must recognise profound and permanent changes in social attitudes

No one in Shell is under any illusion about the size of the task which still lies before us. The first Report to Society is actually the easiest. The true test lies in where companies go next and the extent to which they are able to build on a solid first platform. It is for that reason that there were some who urged me not to let the 'cat out of the bag' and go forward with that first HSE report in 1996 and now the first *Report to Society*. There were those who argued that such reports inevitably take our eye off the wealth creation ball.

To them I say two things. First, we all know that the world has changed. The days when companies were judged solely in terms of economic performance and wealth creation have long disappeared. Today, companies have far wider responsibilities to the environment, to local communities and to the broader society. These are not optional extras. They are not the 'icing on the cake'. I believe that Shell UK's wider social responsibilities form a fundamental and integral part of the way in which we do our business. They are vital to our long-term economic performance.

It is not just the outside world that has changed. Profound changes in working practices and culture have already taken place within Shell UK and throughout the Shell Group but these changes invariably do take time. Nowhere is this more obvious than in the automatic and central role that concern for safety now plays in all of our day-to-day operations. Safety is everyone's responsibility.

No one argues any more that 'it's not my job' or that safety should be left to others. If you were to go to an off-shore platform today most people would be absolutely amazed at how seriously safety is taken as a natural and normal way of life. Our challenge is to ensure that the same degree of individual ownership and commitment is extended to our environmental and social responsibilities.

Equally, when we talk about HSE reporting, it is often easy to overlook the importance of occupational health. Traditional HSE reports have strangely tended to overlook the H part of the equation. That is why I insisted in the *Report to Society* that we included a major section on people giving their best, which underlined the importance of a systematic approach to preventative healthcare in the workplace. Future social reports will clearly need to develop health reporting still further.

We know that public expectations are not going to go away or stand still. Sometimes, it is very easy to be cynical about public opinion, but I happen to be someone who believes that customer behaviour is affected by social, ethical and environmental concerns.

The public demands the highest standards of ethical and environmental responsibility from us and they are right to do so. That is why this process is far more than just about accurate reporting and especially reporting only financial figures. It is actually about the type of business Shell and other companies must become in the 21st century. It means that while oil and gas remain essential to the health and wealth of modern economies, real progress towards viable renewable projects and exciting new ventures including fuel cell technology is being made.

The 21st century company report will inevitably have to take into account these profound and permanent changes in social attitudes and the society in which we all live and work.

21st Century Bottom Line
Beyond Financial Reporting

- Challenge – to find commonly accepted ways of benchmarking environmental/social performance
- Need for accurate indicators but...
- Environmental/social commitments must be built into long-term business strategy
- Be open and transparent – tell it like it is

Second, I believe it is quite wrong to suggest that in some way the economic, environmental and social bottom lines are mutually exclusive. I am sceptical about the extent to which these issues can be neatly packaged into separate boxes of the 'triple bottom line'. Nor do I share the view that the choice which lies before industry is either to develop a set of clearly defined indicators or to engage in meaningful stakeholder dialogue. We should and must continue to do both while accepting the practical limitations of the reporting process.

I would also challenge the rather blinkered view that concern for the environment or community involvement in some way damages companies' underlying financial performance. Or, to put it another way, we don't have to make a choice between profits and principles.

Our challenge is to find commonly accepted ways of benchmarking individual companies' environmental and social performance and of accurately measuring and accounting for different facets of the bottom line. Without that, Shell and other companies' commitment to a more sustainable future will become increasingly difficult to quantify. Short-term financial demands can inevitably place enormous pressure on the scale of a company's environmental and social commitments. When jobs are on the line, or investment has to be cut, some companies may be tempted to push long-term environmental and social commitments to the margin of the decision-making process. My job at Shell UK is to ensure that these commitments are built into our everyday thinking and that we don't forget our broader long-term strategy for a sustainable future and new way of doing business.

In part, this is actually a question of openness and transparency and simply telling it like it is. It is about meeting the expectations of what I term now a 'show me' rather than 'tell me' society. That is why we accepted in our *Report to Society* and I quote: "We still have some way to go before we can clearly demonstrate that environmental and social factors are automatically built into our business strategy."

Our challenge is to find some consistent way of fully integrating social and environmental factors into day to day business decision-making. This is the measure of the distance that all of us in industry still have to travel. But this is one journey which companies should think very hard about postponing to a later date and can ill afford to ignore all together.

At the launch of the Shell UK *Report to Society* in May, I made it very clear that for us the report marked the beginning of an important new phase in our relationship with the outside world. We hope that the report set new benchmarks for openness and accountability. We know from feedback and continuing dialogue with stakeholders that it has been generally welcomed as a significant step forward but no one within or outside Shell is suggesting by any means that we have finished the job. No one, least of all Shell, can afford to rest on their laurels and assume that yesterday's successful report will satisfy tomorrow's stakeholders.

Our challenge is to find some consistent way of fully integrating social and environmental factors into day-to-day business decision-making.

For us, stakeholder opinion represents an important guide and continuing catalyst for new thinking and fresh approaches to these issues. Indeed, we have our stakeholders to thank in part for the evolution of environmental and social reporting in Shell UK. After publication of our second annual environmental report in 1997 we held a major dialogue event and that confirmed the widespread interest in a publication of a wide-ranging report to stakeholders and to wider society.

I have to say that it confirmed what many of us within Shell UK had already concluded privately. Namely, that the successful company of the future will need to demonstrate, year on year, progress towards greater openness and the involvement of key stakeholders and, above all, tangible progress towards external verification of financial, environmental and social performance.

So, where are we today? The Shell UK *Report to Society* provides detailed and verified environmental and safety data but it also sets out our position on a wide range of topical issues including air quality, equal opportunities, sustainable development and serving the customer. For the first time, we include a detailed chapter on staff and employee issues and we acknowledge that future reports must contain more concrete data in this area. It is my view that a staff opinion survey should form a fundamental part of our reporting strategy in the future.

Future Challenges

- How do we achieve greater environmental benchmarking across different industries?
- Oil and gas industry needs to ensure consistent and accurate data
- Hard work needed to get industry-wide comparisons of performance and improvement
- Continue to develop a set of commonly accepted indicators to measure social bottom line
- How do we represent the sum total of a company's social contribution?

As we look ahead to the publication of future reports, we are under no illusion about the reporting challenges of the future. One of those is how to achieve greater environmental benchmarking across different industries. This is an enormous task which may in the end prove fruitless.

In my own industry, we need to do more to ensure that data used are consistent and accurate. There will inevitably be variations in reporting criteria between companies and in the way we set performance targets and, inevitably, there will be a conflict between commercial confidentiality and a commitment to greater openness in this area.

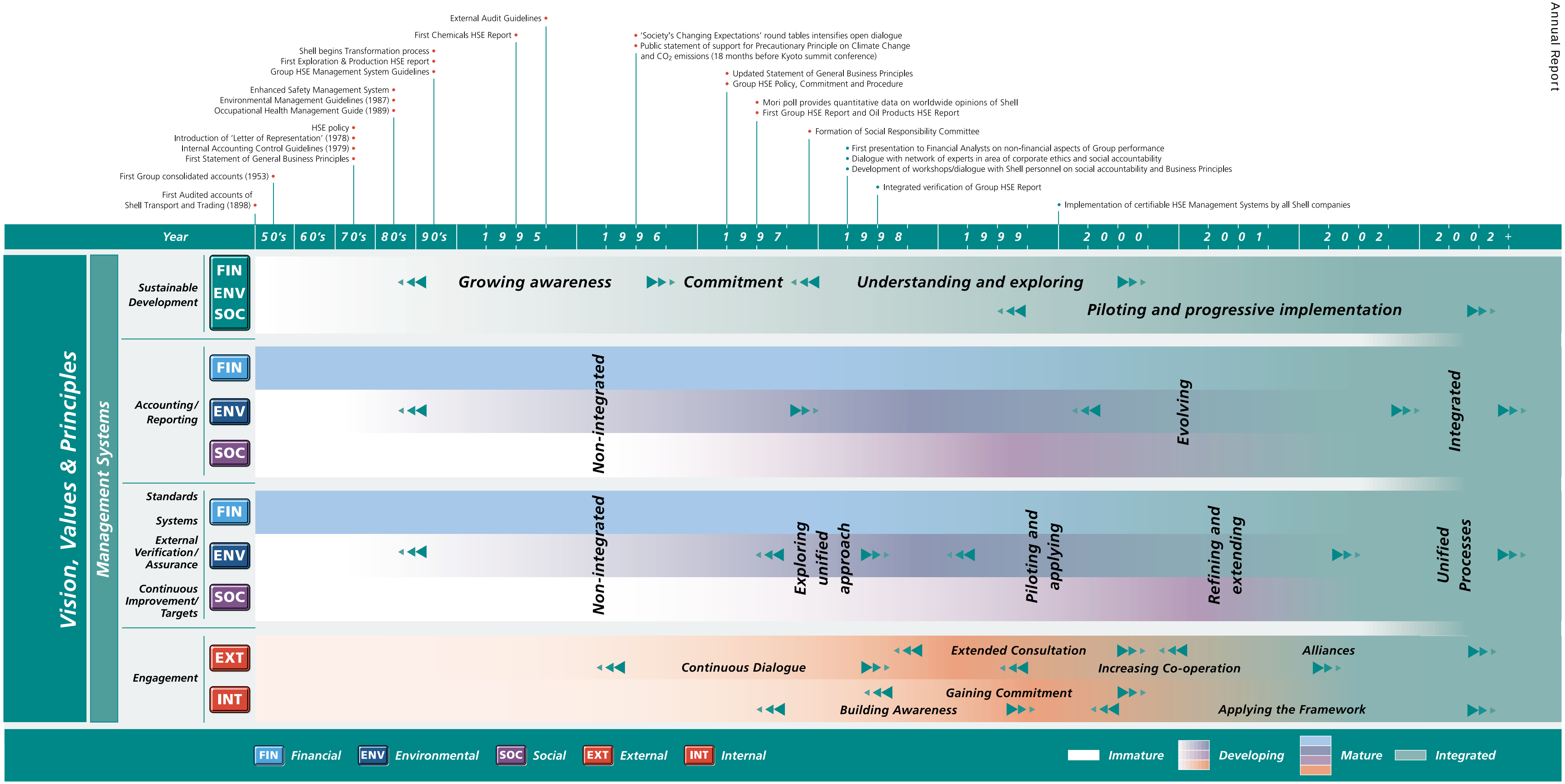
The more difficult challenge lies in attempting to accurately measure a company's social contribution to the bottom line. We are dealing here with a combination of factors which may prove impossible to quantify in any meaningful sense.

The first issue is a simple one: What do we include? Community investment programmes are an obvious place to start but quite clearly they don't adequately represent the sum total of a company's social contribution. Headline figures may tell us what a company is spending, for example, but nothing about the impact of specific projects in the community or the level of active staff involvement.

For a true measure of social contribution, we really ought to think about going back to the basics of employment, the way in which we treat our staff and even the social benefits, for example, of company taxation.

In 1997, Shell UK paid over £380 million in direct taxes, enough to provide four new hospitals or 20,000 new teachers. In addition, we collected £3.8 billion in royalties, VAT and other indirect taxes for the Government.

SHELL ROAD MAP



The other issue here is the question of resources. It is relatively easy for someone in my position to support measures which will bring hour after hour of lucrative work for an army of consultants, advisers, PR people and accountants. But auditing and verification demand significant resources, skills, management time and capabilities which may simply be lacking in smaller organisations. We have to be realistic, therefore, about the pace of change and the capacity of some companies to deliver real change in the short term.

We must be realistic about the role of stakeholders and the unbelievable continuing demands placed on them by companies like my own. Large set piece dialogue events with a broad range of stakeholders serve an important but increasingly limited purpose. If we are not careful, our stakeholders are going to start suffering from terminal cases of dialogue fatigue.

There is enormous scope, however, to develop a more sophisticated stakeholder dialogue process. This could involve external audiences in addressing real dilemmas and business problems rather than the general direction being adopted by individual companies. That, in the end, is precisely what we did with Brent Spar. There is scope for making better use of new technology and, in particular, the World Wide Web.

Ultimately, the best prepared and most beautifully presented reports are meaningless unless the promises they contain can be matched with clear, demonstrable progress where it matters – in the workplace. That is why the Shell Group's commitment to sustainable development and social accountability is so important. That sets the parameters for our strategic planning and for ensuring that broad commitments are translated into concrete decisions and the daily conduct of our business.

I am immensely proud of Shell's first *Report to Society*, but I also know that it is not an end in itself. Over the last few years we have moved quickly from publishing HSE data to full environmental reports and on to our first *Report to Society*. None of us knows where this process will lead us over the next decade. None of us can accurately predict the concerns of tomorrow's stakeholders. All we do know is that the evolving *Report to Society* will continue to adapt to new demands, emerging social trends and unforeseen events. Now the real work begins.

ALAN BENJAMIN OBE | Chairman, QSP Holdings plc

“Competitiveness requires companies to be proactive, very focused, open and informative. The ability to hold a dialogue with a company will be a feature of competitiveness and access to information will indicate confidence.”

ALAN BENJAMIN

As we enter a new century, we must be receptive to review and change. The well-established rules and regulations, those fixed positions, are now ready for scrutiny. There are new values emerging in society that suggest the need for new approaches to reflect and measure them and offer fresh opportunities for accountants.

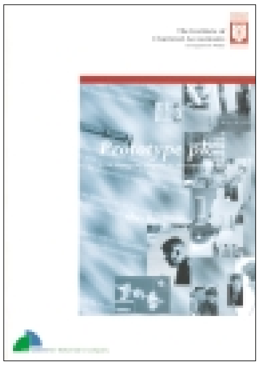
Prototype plc – a fictitious company – brings together some years of thinking, debate and argument about the company report of tomorrow. There were several drivers behind the development and shape of the *Prototype plc* report.

Yesterday’s Drivers

- Recognition and measurement of intangible assets
  Software industry’s experience
  Coopers & Lybrand Report 1990
- Tomorrow’s Company (RSA Inquiry)
  Inclusiveness and stakeholder recognition
- Growing irrelevance of conventional reports for risk management

Back in the early 1960s it was impossible to finance software companies. Those of us in the business had no acceptable assets: a wife, a cat, a home is what we could offer to the banks. Most of it was turned down. We only had people and their skills. It is different today. Microsoft has a balance sheet, certified true and fair, where the net assets represent 5% of the company’s market capitalisation. So what has changed?

In 1990, Coopers & Lybrand brought together a small group of interested people, among whom were Sir Bryan Carsberg, Sir Brian Jenkins and me, to consider the treatment of intangible assets in accounts. We published a report which showed the way forward and recognised first of all some of the fallacies applying to existing tangible asset valuations as well as forecasting the importance of intangibles.
The RSA Inquiry *Tomorrow’s Company* was also inspirational in its campaign for inclusiveness based on new values in society. It proposed that a wider range of stakeholders has a legitimate interest in companies’ activities than just those companies’ shareholders.



Prototype plc

It was also clear to me, particularly in my then business of building mission-critical systems, that conventional accounts, and certainly ours, did not address the many risks inherent in the business, and as I studied this in other industries it became, for me, a serious failure of the accounting status quo.

Today’s Drivers

- Competitiveness
- Technology
- Governance
- Stakeholder consciousness

Competitiveness requires companies to be proactive, very focused, open and informative. The ability to hold a dialogue with a company will be a feature of competitiveness and access to information will indicate confidence.

The arrival of the Internet has changed the way we work, the work we do and the world we live in. The World Wide Web and the coming merger of information technology and television, together with digital broadcasting, has created new tools and given people outside the company access to information which was unimaginable just a few years ago.

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Legislation and regulation have altered the reporting landscape and, for good reasons, made the issues of behaviour, accountability and responsibility of companies very visible.

All these influences and the rise of so many single issue groups, exploited or supported by the media, have raised the consciousness of stakeholders other than shareholders – but not excluding them – whether it is on the exploitation of child labour; genetic engineering of food; transportation of animals; or the pollution or cutting down of forests. Many companies have felt this wind of change.

The 21st Century Annual Report

- Basic Framework
- Structured by stakeholder to recognise key relationships
- Recognises and measures intangible assets as real wealth creators
- States its success model

In order to respond to some of these developments and get closer to reality, companies can create a new framework for their annual reports. This framework can be structured to recognise key stakeholder relationships. *Prototype plc*, for instance, categorises and describes its stakeholders as either direct or indirect.

The report of the future will also recognise intangible assets as real wealth creators. New York University research reveals that US manufacturing industry is investing $200 billion a year in intangible assets, equal to its investment in plant. We are beginning to realise that what we have always written off as cost does in fact constitute real value and should be acknowledged as such.

The report can also declare that its success model is based upon the interests of all its stakeholders. *Prototype plc* briefly outlines what constitutes success for each stakeholder group. The setting and disclosure of these targets describes the management challenge and the inauguration of the stakeholder dialogue.

As a 21st century annual report, *Prototype plc* was affected and will continue to be affected in its development by the Centre for Tomorrow's Company's proposition, emerging from the RSA Inquiry *Tomorrow's Company*, of a core report to be published with the preliminary results and issued sooner, sharper and simpler than the complex documents of today.

The deputy chairman of The Hundred Group of Finance Directors recently commented, 'The accounts of companies are so complicated, they are unreadable.' Professor Baruch Lev of New York University, a long-time researcher in this subject has said, 'Traditional accounting has had its day, it is no longer relevant.' Peter Knight wrote recently in the FT, 'People want all the news, good and bad, not just the company's view.'

The Centre for Tomorrow's Company also proposes that the core report is supplemented by other fuller reports which address in detail the financial, sustainability, people and value chain aspects of a company. These are described in full in the Centre's publication *Sooner, Sharper, Simpler* but are briefly outlined below:

- the financial report is the same as the current model
- the sustainability report will comment on community and environmental impacts, compliance with corporate governance codes, health and safety
- the people report will cover training, employment, contracting, outsourcing, morale, remuneration policy and pensions
- the value chain report will comment on sales, customer satisfaction and retention, product performance and purchasing and payment policies.

Clearly more investment in this presentational format will be required than might be the case today but new technologies will soon substantially reduce these costs while delivering much more.

The 21st century annual report will reflect the financial, social and environmental aspects of a company's activities, to give a better balanced view of the company. Yet we must not make the mistake of regarding the non-financial aspects as unimportant. Any analysis of existing and proposed European Directives should persuade us otherwise. For example, any study of the landfill tax legislation will reinforce this importance. It will provide financial and non-financial measures and will be integrated into a company's Web site as part of its continuous dialogue with stakeholders.

A research project has been undertaken by the University of Sunderland Business School in partnership with QSP and private and public corporations. The project is investigating a new generation of intelligent information systems which will enable companies to recognise, audit and manage their stakeholder relationships by quantifying and auditing intangible assets and quantifying and managing the corporate knowledge base.

The goals for the university in this project are to build models of the key performance measures for stakeholder relationships; to create and assemble the software tools to manage knowledge in the business; and, to create software to exploit the World Wide Web as an information repository.

The goals for QSP are simply to test our current architecture to see how it can handle non-financial data – it already handles financial data – and also to find intelligent system components to build an effective information flow between the company and its stakeholders.

The goals for the public and private corporations include becoming aware of these 21st century key performance measures, to understand the 21st century system implementation issues and to discover the sources of non-financial data.

Thus far, the project has discovered that different key performance measurement models emerge for large companies, small and medium-sized enterprises and, indeed, for companies in the public sector where, for example, the Audit Commission has already required them of local authorities. We are discovering the architecture and technology gaps in our system and also issues of data collection and where in companies those data lie.

The research has shown that there seems to be little organised effort anywhere to address these issues, excepting current discussions in Australia, the United States and the Netherlands.

The challenge inherent in the core report lies in what to put in and what to leave out. Although the stakeholder structure helps by establishing what is important to each stakeholder group, perhaps the way to establish what is important is to ask them directly.

Providers of Capital

Shareholders are generally satisfied with the company's ability to provide a competitive overall rate of return on their investments. Prototype's bankers have indicated that they do not believe it takes sufficient advantage of borrowing facilities which are available compared with some competitors' activities. They suggest a rebalancing of our financial sourcing in the coming year.

Source: Prototype plc – Core Company Report 31 December 2000

Prototype plc features comments by stakeholders on the company: customers have raised price issues; employees highlighted training gaps; local communities stressed local purchasing; bankers criticised the financial sourcing balance. You will find no stakeholder dialogue of this type of any size or shape in today's company reporting.

These data are shown as having been collected and collated by an independent firm, and some extremely helpful and important points have been made by the stakeholders. These comments are useful in assessing

the challenge inherent in the core report lies in what to put in and what to leave out

the stewardship of the company and the managers' responses are found in their own commentary in the management dialogue section.

Customers	**Target**	**Achievement**	
Percentage of customers retained	95%	81%	↓
Share of available market	3%	8%	↑
Quality of ratings	90%	81%	↓
Support services ratings	95%	79%	↓
Innovation ratio	16%	10%	↓

Source: Prototype plc – Core Company Report 31 December 2000

Prototype plc also features some indicators which relate to targets and achievements within the success model. Tables relating to customers for instance show that few of the targets have been met – 81% of customers have been retained against a target of 95% – but then the targets are very high and the achievements are substantial. It is argued that disclosing this information somehow assists competitors. A response to that criticism is, perhaps, to ask why competitors do not publish the data and whether they have even set such targets themselves.

Forward-looking information is provided in the section on summary financial results which is complemented by a short description of actions taken and future plans.

Providers of capital	**Results 1999**	**Results 2000**	**Actions Taken**	**Future Plans**
£000s				
R&D	1,700	1,860	More academic links	Customer inspired product innovation programme
Training	1,194	1,910	Distance learning programmes inaugurated	Focus on technical & skills and in telelearning courseware

Source: Prototype plc – Core Company Report 31 December 2000

Unusually, research, development and training are highlighted as being 'revenue investments'. The information immediately invites future comparison causing some companies great concern that critics in the future will be quick to highlight that they have not achieved stated targets.

The summary financial information is, of course, also supplemented by the full financial and economic report. It values intangible assets and provides a basis of measurement for those values. In this context, the criticism often made is that these intangible values are subjective.

However, on the basis of today's accounts and the size and shape of takeover bids in relation to the audited balance sheet values, a coach and horses can be driven through many tangible values as stated. What does all the goodwill paid for these companies mean? How is it locked up? What is it represented by? Subjective valuations are fine if they are properly described, disclosed and measured consistently.

Prototype plc invests money in research and development, in training and product branding. It suggests that these investments, as they have been described, should yield new ideas, products and services, i.e. innovation. The company relates such spending to the value added in the business each year by its people. It chooses to call the result the 'innovation ratio' and has created a measured objective (reported as not having been achieved yet).

Innovation Ratio

Management measures the ratio of its expenditures on research, development, training and product branding to the value added by employees. The goal is to reach, by the year 2004, value added equal to 20 times such expenditure.

£000	**1999**	**2000**
Total expenditure	5,000	7,600
Value added	73,290	77,290
Innovation Ratio	14.6	10.2

Source: Prototype plc – Core Company Report 31 December 2000

Communicating this measure helps to describe the business risks and some companies might not choose to do so. But it is, in fact, easily calculable and Prototype plc considers this to be one of the key performance measures.

It believes that it is critical to review the knowledge assets of the company. This becomes a much better basis for employee trust and progress because employees are involved in the establishment of these knowledge assets and their valuation. Any tool that measures, manages and audits a company's knowledge bank is a strong indicator of the company's sustainability.

Using the approach of a core report supported by supplemental reports, the stakeholder structure and the measurement of intangibles will help to measure all the risks in the business: technological, political, social and financial. It will also help the company to communicate effectively with all its stakeholders, thus generating a much fuller picture of its reputation, position in the market, risk profile and competitiveness.

There is a new and strong future for accountants in this scenario. They understand disciplines and standards and can look across industries and for the reality behind the measures. There is now an incredible opportunity for accountants to expand their horizons. Using their existing professional training, they can create a new professional skill in researching and studying, proposing standards and designing company reports which are far more relevant to the 21st century and which reflect users' changing needs for information. New measures are, of course, required both internally and externally by companies.

The Institute of Chartered Accountants in England and Wales should lead the way in Europe and conduct sustained research into 21st century corporate information in a stakeholder framework and into the impact of electronic communications upon reporting. I forecast the need for new skills in Web management and the rise of a chief information officer in the management hierarchy, all driven by the imminent merger of information technology and television.

Communicating

- The Web site will be the prime communications vehicle of the 21st century – largely interactive
- Stakeholder structure will assist clarity and use
- The Web site will be a key competitive asset and warrant board level management

The Web site will become the prime communications vehicle of the 21st century and will be largely interactive. It will host a permanent dialogue as the gateway to the company and, therefore, needs structure, standards and security. The stakeholder structure will assist this process by creating a framework for information to be organised and, critically, for navigation to be easy.

The Web site will become a competitive weapon and warrant board level responsibility. For example, today, ADP Systems in New Jersey runs a service for companies which distributes an electronic version of the annual report to shareholders in e-mail form at a cost to the company of 50 cents per shareholder. It is unadorned but contains all the relevant data. The company will also electronically collect proxy votes for annual general meetings for 3 cents each. Six hundred thousand people currently subscribe to this service.

any tool that measures, manages and audits a company's knowledge bank is a strong indicator of the company's sustainability

the annual report of the 21st century will not be annual and it will not be a report: it will be an up to date, informative, permanent dialogue

The key characteristics of a World Wide Web site are that it will be:

- information-rich
- always up to date
- interactive
- the vehicle for electronic commerce
- a competitive weapon entailing major organisational responsibility

The corporate report has moved from the philosophy proposed by the Royal Society of Arts and the Centre for Tomorrow's Company's initiative to a model in which *Prototype plc* demonstrates the principles and ideas for discussion in seeking to break new ground, to one of the first manifestations of some of these ideas in practice coming from Shell UK's *Report to Society.*

The model proposed, that of *Prototype plc*, may not be the first of a new type of annual report: it may be the last. The annual report of the 21st century will not be annual and it will not be a report: it will be an up to date, informative, permanent dialogue.

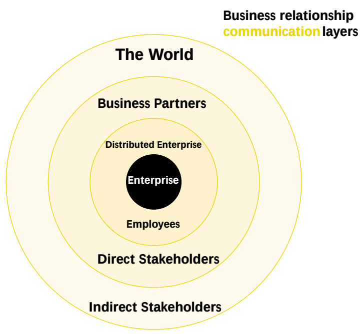
DAVID PINCHES | Director, QSP Holdings plc

"What used to be a fragmented communications system can now be brought together under a common infrastructure as an enabler of business processes. There is now only one geography."

DAVID PINCHES

Web technology and the Internet have enjoyed enormous hype in recent times. Some of it is justified, quite a lot is not, but there are fundamental truths that are emerging as the technology matures which will deeply affect the way in which we do business.

All organisations are diverse. Any one enterprise may have many different layers of communication encompassing a variety of different types of people and organisations. Beyond the immediate core of an enterprise lies its distributed self in terms of external offices and employees. Those offices may be distributed worldwide and the employees increasingly mobile. There is a pattern representing the communications infrastructure around an enterprise. A computer network is an inherent feature of an enterprise's system: this could include staff with laptops out on the road or in the distributed locations.



Included in the category of business partners or direct stakeholders, are suppliers, customers and shareholders who all have their own methods of communication within their own networks, individual computer or e-mail systems, financial and manufacturing systems. The world in the diagram above is represented by, for instance, new dealers for a company's services or the local community around its plant and offices, each of which requires different methods of communication, be it telephone, face to face or via a PC (though they may not be connected to an on-line service).

What connects all these discrete patterns is one technology, the Internet, which is acting as an agent of change. Typically, the UK is six to nine months behind the United States in its application and Continental Europe twelve to twenty four months behind. What the business world is starting to grasp is that in terms of a computing and communications infrastructure, the Internet presents a truly global network.

The development cycle in this technology can be as little as three months. Programmers build systems that take no account of where the users of the software are. Use may be on a machine in a private house, in a cable inside the infrastructure of a company or on the end of a global satellite telephone. These technologies assume that the world is wired in one common way. This means that what used to be a fragmented communications system can now be brought together under a common infrastructure as an enabler of business processes. There is now only one geography.

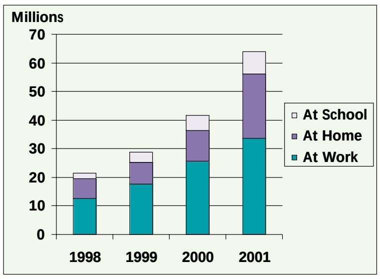
Web sites can now bring in customers which enterprises did not know existed since they did not have the ability to trade with them before such access took place. There now exists one continuous time zone: as one customer or supplier closes down, another opens up in a different part of the world. For instance, it is now possible for suppliers, from the luxury of their laptop or their PC, to link directly to a company's stock system and supply items on a just-in-time basis from anywhere in the world.

Currently in the United States, business-to-business transactions are moving wholesale onto the Internet. Already it is possible for preferred customers not only to look up products that they want from another business and order them but also to access that business' internal financial system.

On-line business commerce to consumers is starting to take off as well: it is no novelty for consumers to order books, videos or CDs over the Internet. Financial services on-line, however, are a relatively new area. Investigation is underway on how insurance policies could be sold on-line. Already there are banks in the United States that offer on-line loans of up to $10,000 with no human contact necessary: an inquiry is made, the credit check is forwarded to a credit agency and a response received, all on-line.

Other stakeholders are coming on-line such as investors and employees who are likely to be using both the company's intranet and the Internet.

European On-line Population



Source: Forrester Research Inc.

How many people are on-line? Research indicates that in Europe 12 million people currently have access to the Internet from their place of work, a figure which is estimated to almost triple by 2001. There is a similar growth pattern in on-line access from homes and schools. The estimate of 60 million on-line users in 2001 will represent 13% of the European population by that time. The equivalent in the United States it is estimated will be 98 million individual users, representing 33% of the population.

This is the arena into which a Web-published annual report is launched. For a company, Web publishing means that the annual report:

- is open to global access
- can be as up to date as liked
- may feature alternative media, i.e. not just text and pictures but more graphics or video and audio presentations
- can be an interactive communication with stakeholders who are able to be highly selective about the information they access, drilling down to more in-depth information that is not available in the paper-based report
- can be linked across to other reports elsewhere on the site
- is a medium for dialogue with stakeholders which can be designed to encourage them to provide feedback
- may be personalised to take account of individual stakeholder groups' needs (possible through the use of intelligent software which registers who the stakeholder is, what pages and type of information he accesses, and can generate pages accordingly).

Prototype plc, a fictitious company, has Web-published a version of its annual report which has been specially designed to demonstrate the enhanced communication possibilities brought about by the most up to date technology of the Internet. To enable meaningful dialogue with its stakeholders and allow a company to target its individual information needs, Prototype plc has categorised its stakeholders in one of two ways:

Direct Stakeholders	Indirect Stakeholders
• Customers	• Local Communities
• Employees	• Environmental Interests
• Providers of Capital	• Education
• Suppliers	

The integration of technology enables a high degree of interactivity and personalisation to facilitate the provision of information to highly segmented audience profiles, to individuals and organisations, on-line and in any time zone anywhere in the world. The cost of these systems is both less than the cost of paper-based systems and can add a lot more value to business in terms of customers, service, stakeholders and interaction.

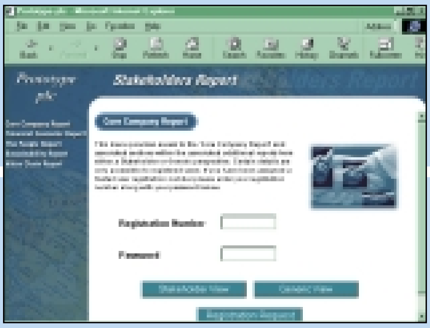
The following pages provide a brief glimpse of Prototype's core report in its Web-published, interactive form.

FEATURES OF THE PROTOTYPE WEB-PUBLISHED ANNUAL REPORT 2000

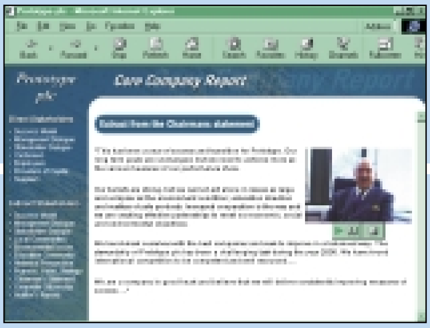
Start here

THE PROVIDER OF CAPITAL
The home page of the Prototype annual report site features a menu that contains many of the usual categories on a corporate site but, in addition, also has the option of accessing the Stakeholders Report. A direct stakeholder, a provider of capital for instance, who could be anywhere in the world, could log onto the site and via the **Stakeholders Report** button would reach a screen asking him to register.

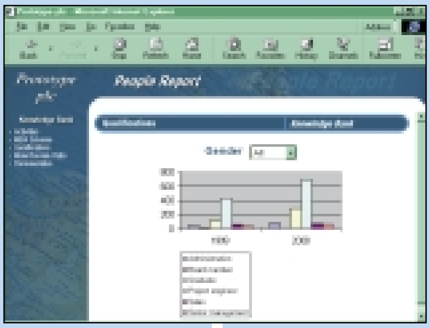
Any sensitive information on the site or access to internal computer systems is restricted at this point by asking the user to register: only those users who have been assigned trusted user status will have unrestricted access. The core company report has two views: generic or stakeholder. The generic view is very much as laid out in the paper-based report whereas the stakeholder view allows access to information tracks based on what type of stakeholder the user is. Having registered, the trusted user presses the **Stakeholder View** button at the bottom of the screen of the core company report and moves to an extract from the chairman's statement.

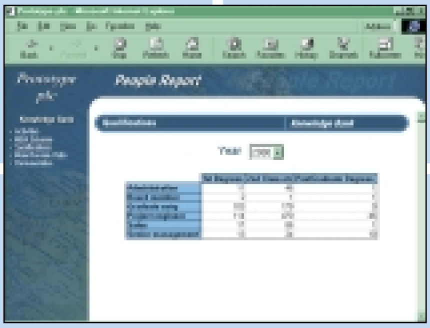


The statement is accompanied by leading-edge up to-the-minute technology on the Web, namely RealPlayer™ video, enabling on-line streamed video using downloadable software from the Internet. The video is heavily compressed compared to normal formats enabling it to be put onto a dedicated Web server. The current viewing quality of the video is not on a par with existing broadcast media but will dramatically improve with the advent of digital television. It can be viewed by anyone anywhere in the world whose PC or network has the capacity to download the software and includes an audio facility for those with multi-media equipment. The trusted user is likely to be interested in any one of the menu options but chooses the Direct Stakeholders **Success Model** option.

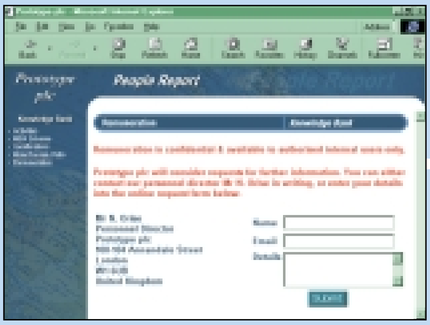


The graphical form of a breakdown for all employees shows an overall year on year increase in the knowledge bank of the company.





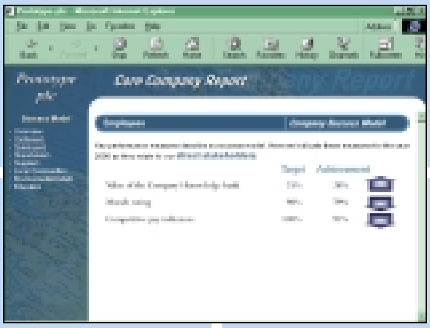
Accessing the **Qualifications** option on the left-hand menu calls up a table listing employees for the year 2000 by category with type of qualification (historic figures are also available).



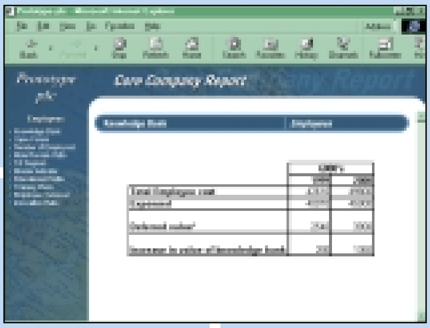
An attempt to look into the **Remuneration** of employees results in a notice that remuneration information is confidential and available to authorised internal users only. The user is invited to send an on line request form to the Personnel Director.

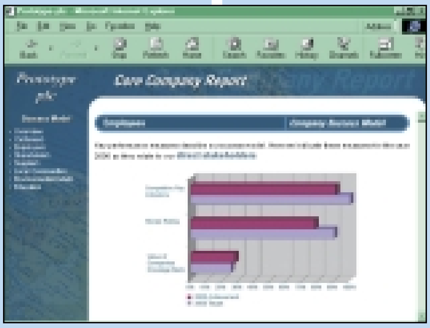
This screen describes how the company segments its stakeholders and how it intends to enhance the value of its relationships with them. The provider of capital reads what the company says about employees being part of the success model and, wishing to know more about the knowledge bank of employees, can access the **Employees** button on the menu.

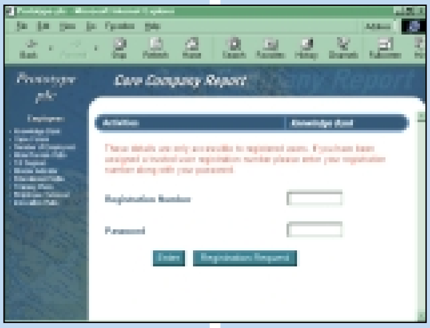
The information on this screen is lifted straight from the printed report on the value of the company's knowledge bank. Because this data is on the Web, it can be accessed and displayed in different formats simply by clicking on the screen. A click on the table enables the user to look at the information in graphical form if desired or switch back to tabular form by clicking again. A click on the **Value of the company's knowledge bank** in the table itself accesses data not available in the printed form of the core report.



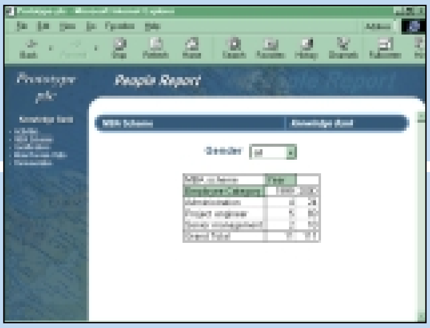
This information called up could be fed into the table on a weekly, daily or even hourly basis, if desired, directly from internal management systems. The figure for total employee cost is shown not only as expensed but also as a deferred value for succeeding years. The algorithmic and accounting debate continues on these matters but it is obvious that this kind of information could be made readily available on the Web. The figures show that there has been an increase in the value of the knowledge bank and pressing the title **Increase in value of knowledge bank** enables the user to drill down further.



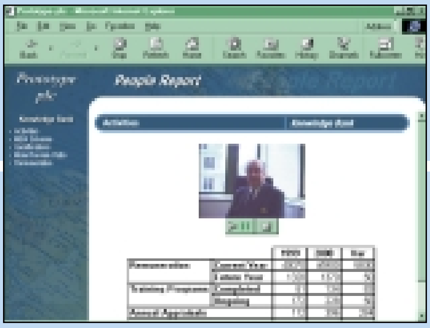




At this point, a security feature has been in-built to bar any non-trusted user from accessing sensitive or confidential information.



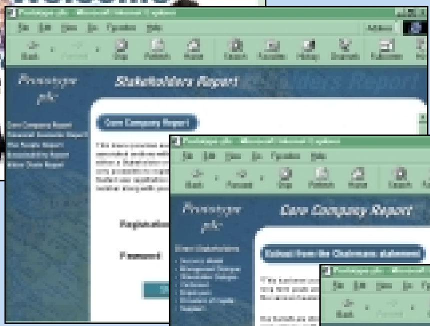
The information is shown by employee category over the previous two years. Using the underlying databases, the figures can be looked at in different ways including breakdown by sex of employee and also in graphical format.

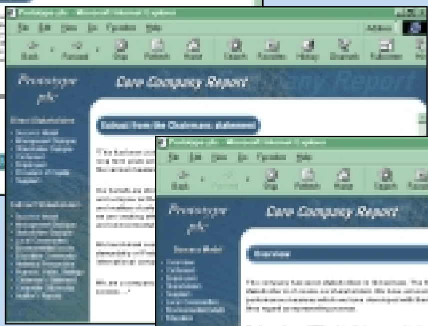


Having registered, the trusted user enters the People Report and finds a more detailed picture of how the company's knowledge bank is constituted. This is accompanied by a video of the chairman talking about the company's policies on, for instance, remuneration, training and appraisals, all items listed on the table on the screen. For this particular schedule there is no further breakdown available. The menu on the left-hand side, however, has changed and the user may choose the **MBA Scheme** button.

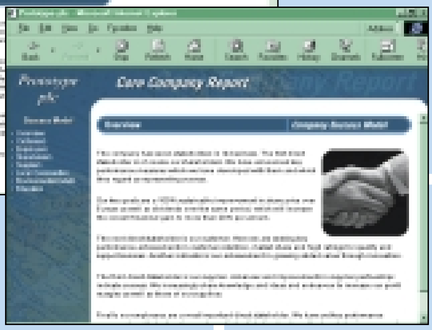
FEATURES OF THE PROTOTYPE WEB-PUBLISHED ANNUAL REPORT 2000

Start here

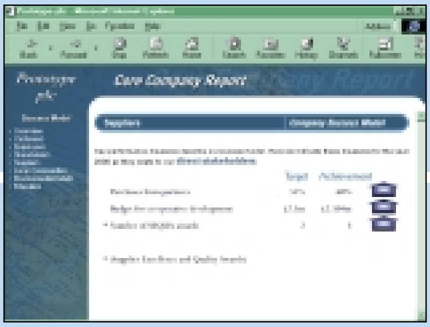




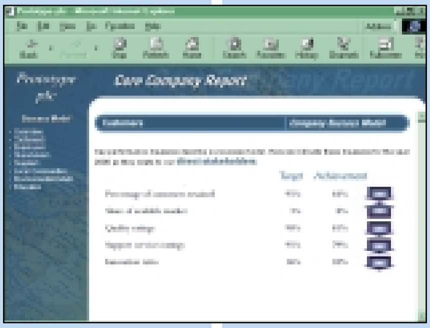
LOCAL GOVERNMENT
A different information track might be shown using the example of the user as a project officer in the local development agency, whose area includes one of the company's plants, wishing to understand something of the company's effect on the local community and how much of what it supplies is sourced locally. He reaches the Core Company Report and Extract from the Chairman's Statement, and accesses the **Direct Stakeholders Success Model** track. Via the Core Company Report Overview of the Success Model, the project officer chooses **Suppliers** on the left hand menu.

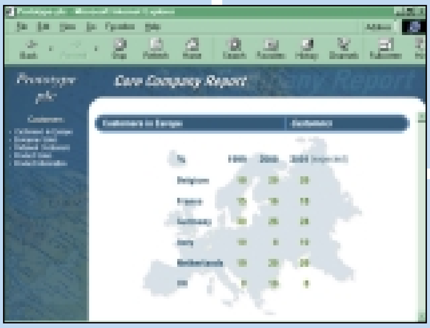


This screen lists key performance measures relating to direct stakeholders including details of relationships with trusted business partners. A click on the table itself leads to the next screen.



THE CUSTOMER
A customer, having chosen the Direct Stakeholder **Success Model** option in the Core Company Report, chooses the **Customer** button on the subsequent Overview screen. The table, as in the printed report, lists key performance measures which describe the success model: percentage of customers retained, quality ratings and support services ratings for instance. It is possible to drill down by clicking **Percentage of Customers Retained** in the table to a breakdown of customers by country.

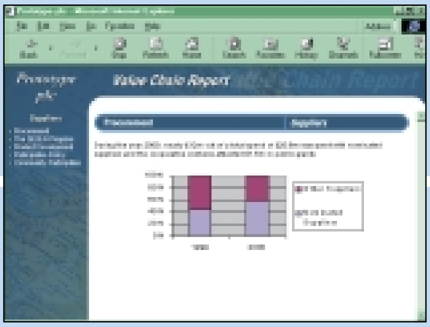




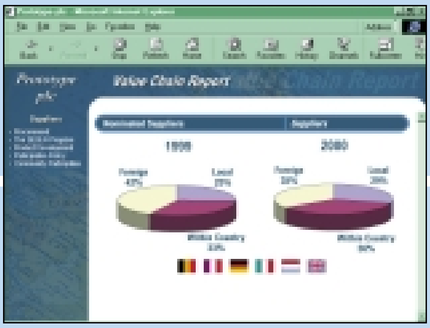
Of particular interest to the Customer may be the distinctions Prototype makes in its relationships with focused customers across geographic boundaries. Whilst the percentage of focused customers in other countries is forecast to remain static or increase, the figure for the UK is set to drop. A click on **UK** on the table calls up more information.

A prospective customer in the UK can see that it is the focused customers with whom Prototype wishes to deal in the future, knowledge which may help him to form his own relationship policy with the company. A focused customer can expect to have the same ability as a preferred supplier to access the company's internal financial system and look up her own account directly via the Internet.

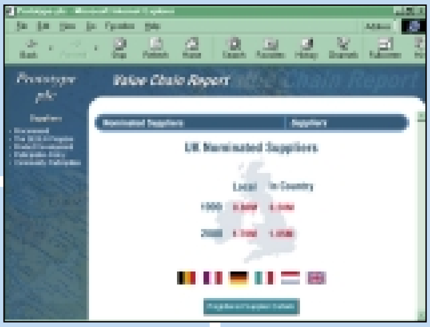
The information track leads into the Value Chain Report. The screen which appears is the same as that in the printed report but can be viewed in different ways. The statement the company has posted makes clear that a substantial amount of their business, £12m of a total spend of £20.6m, was spent with nominated suppliers during the year 2000. The local government officer can look up how much of that business was actually done with local businesses again by clicking on the table itself.



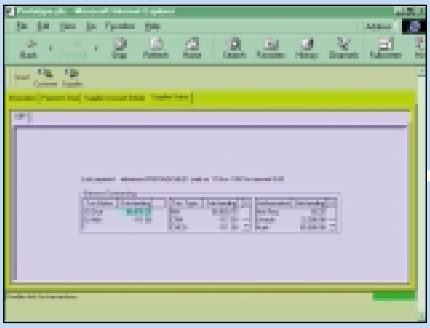
The pie charts called up show the nominated suppliers and compare those who are foreign, local and within the country (UK) over the last two years: the company has been using fewer foreign suppliers. A click on the pie chart drills down further.



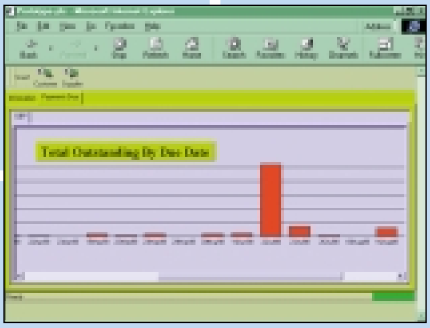
The screen provides a breakdown of the amount of money spent by Prototype with its UK suppliers in the last two years. The option is available for other countries by clicking on the flags. Still more in-depth information is possible, dependent on how much the company wishes to disclose and can be targeted most specifically on a secure basis to the different types of users.



The button at the bottom **Registered Supplier Details** is a secure feature accessible only to those who have an existing relationship with the company such as the nominated supplier who must register on the form called up (not shown here) to enable further access.



Having clicked on one date in the graph, the supplier can drill down precisely to the finer detail behind the graphic representation: the current status of all invoices including age of debt category, type and balance outstanding. In addition, he can call up a final summary status report of the up to date status of the company's entire account with him. This technology presents a fast and efficient financial communication facility, preventing the hundreds of telephone calls that accounts departments often receive.



THE NOMINATED SUPPLIER

The supplier may wish to reassess his relationship with Prototype and decide whether to strengthen or terminate it. The integration of technologies has now progressed so far, that it is possible to link directly to a company's internal financial system, through a secure fire wall, directly via the Internet. The supplier is able to link directly to his own page on the financial system and see payments owed to him by Prototype (completely up to date).


Sir Brian Jenkins


Mark Goyder


Chris Fay


Roger Davis

DISCUSSION

MARK GOYDER
Director, Centre for Tomorrow's Company

There are certain key areas that need to be looked at in the development of the annual report of the future: technology, audiences, content, consistency and timing. These areas are central to the report *Sooner, Sharper, Simpler* produced by a working party at the Centre for Tomorrow's Company.

Addressing the issue of technology first: is the whole debate really about technology per se? I don't believe it is. Technology offers marvellous opportunities but what exactly are we going to do about them?

Secondly, the audiences. I believe that technology enables the messages about a company that are aimed primarily at the shareholder audience to be integrated to encompass the stakeholder audience. Without skillful use of technology a company cannot know whether, when somebody is visiting the corporate Web site, they are accessing it with the hat of a customer, shareholder, supplier or possibly all three. It now becomes a nonsense to packet different messages for different audiences.

This brings us to consistency. If the core values are inconsistent, this very quickly becomes apparent. For instance, when we assess some of the annual reports against the scorecards mentioned in *Sooner, Sharper, Simpler,* one of the classic things that emerges is the chairman thanking people for the terrific year that the company has had whereas the chief executive studiously ignores people throughout the operational review.

In one example, I have seen a seven page operational review covering tasks and targets and figures but containing nothing about the people involved in the business. I believe that anyone reading a document like that would get a feeling of inconsistency and wonder about the sincerity of the original statement by the chairman.

There are two issues concerning consistency: that of consistency against values and that of consistency over time. One of the best ways of identifying weaknesses in a company is to look at successive reports and see what has *not* been consistently measured over time, often when times are tough. Disciplined frameworks against which business performance can be measured, based on set time-frames, may be waylaid or set aside. Expectations in terms of consistency can only increase.

A success model means, simply, the ingredients in the success pie. How can we understand the meaning of figures in the annual report if we cannot actually understand what recipe a company thinks it is working to in generating good results? It seems increasingly that the future annual report will fail if it does not make explicit how a company intends to achieve success and then measures consistently against this.

Finally, the issue of timing is critical when it comes to the importance of the preliminary results. Analysts will tell you that it is the preliminary results that they are interested in: the annual report is rather an anti-climax.

Sooner, Sharper, Simpler suggests two things: one is that a company needs to reduce the key message that it wants to communicate to any audience into a core document like *Prototype plc.* The other concerns timeliness. For a publicly quoted company, the core document needs to come out at the same time as the preliminary results and be less of an afterthought. I would urge companies to use the scorecard in *Sooner, Sharper, Simpler* to score themselves and find out how inclusive they actually are.

MRS JUSTICE ARDEN
Chairman, The Law Commission

I react very positively to the merging communications network. But technology is not going to make traditional accountancy irrelevant. It will, however, make the information more accessible. I see that as a


David Pinches


Alan Cook


Mrs Justice Arden


Alan Benjamin


Sir Sydney Lipworth

separate issue from the issue of reporting to stakeholders. On that, I do not have quite the same enthusiasm at this point in time. Indeed, I would say I see certain amber flashing lights starting to show up on this matter.

First of all, on a purely legal level, I would be concerned to make sure that there was sufficient regulation of what was being said in the stakeholder report. The information must be capable of being monitored and it must be meaningful. There is also a danger of misstatement, particularly where information is repeated as of the present time in videoclips.

My further concern, from a company law perspective, is that the debate on stakeholder reporting is assuming answers to the questions: 'What are the duties of directors?' and 'What is a company for?' We do not currently have the answers to those questions. The Companies Act states that it is the duty of directors to take account of the interests of employees but it is not clear how far the Act extends the general law which provides that directors owe their duties to 'the company'.

It seems to me that we have to have a debate on those questions first – before one starts equating the interests of the various stakeholders. At the present time, the law would probably favour an 'inclusive' approach, i.e. an approach in which what directors do is justified in terms of the interests of the company. It would not seem to favour elevating all the stakeholders' interests on to the same level. Thus, there has to be a certain amount of caution here.

These are my personal views but I should also like to mention that in the last couple of days, the Law Commissions have issued a consultation document in which we have suggested that there should be a statement of directors' duties in simple form which should be inserted into the annual accounts. We seek consultees' views on that and other questions. Now, we have not gone into the stakeholder issue because that was outside our remit. For the purpose of the stakeholder report, it is necessary to clarify the duties of directors, so that people understand what those duties are rather than to make certain assumptions and widen the practice of reporting on the basis of those assumptions.

Once we have got through that barrier, then (as I have said) I think we have to consider whether this information is meaningful. So far as I am concerned, to make it meaningful you have got to be able to measure it. Unless you can measure it, you can't compare performance and the primary function of accounts in my view is to make sure you can monitor what the directors are doing. So, it has to come down to a question of measurement and it has got to be in terms of a unit which you can compare with what they said last year and with what other companies in the same industry are saying.

So, it seems to me that the questions discussed today are very futuristic matters. A great deal of work has got to be done in clarifying the legal basis for stakeholder reporting and in clarifying the way in which these matters are going to be measured.

SIR SYDNEY LIPWORTH

Chairman, Financial Reporting Council

The types of issues that are being suggested for inclusion in companies' annual reports of the future are essentially matters for companies internally. It is probably far more important to develop a culture and an ethos internally where there is concern for the interests of the community, the environment, health and safety, and good ethical standards than to report on them in detail externally. That is where I would place primary emphasis. But, that said, clearly we are moving in the direction of greater openness and transparency externally so that people outside can see what the company is all about, how it behaves and what its particular standards are.

Moreover, these steps are coming about not through any legislative pressure but through greater public awareness and the fact that technology is enabling greater openness. However, I think there is still a long way to go and there are several concerns to be addressed.

The first of these is the burden of detail that investors, shareholders and other stakeholders currently receive in addition to essential financial information. I would be worried about adding to that burden with detailed non-financial reporting, and we should ask how far should one go, who needs it, and what do they actually need? Furthermore, how do you measure it and how do you get common standards that you can apply across companies?

I would be very slow to introduce any form of regulation or compulsion into this area. It is now a matter of responding voluntarily to public awareness and concern, but, if made compulsory, it would be very difficult to define using the same criteria as apply to financial reporting, which in itself is difficult. The issues are wide and I think one should move fairly slowly down the route of regulation and enforcement – I would avoid prescription in this area.

CHRIS FAY

Chairman, Shell UK Limited

I think that we must be careful to separate out information which is provided on a daily basis from that provided annually or biannually. Shell's annual report and other information is available internally via the company's intranet. It is an old saying but information itself used to equal power whereas today, because everybody has information, it is what you do with it that matters. Gathering information is fine but one should be very careful to differentiate between the reason for gathering it and the ability to then quantify it.

It currently seems to be difficult to verify anything more than simple accounts particularly as regards the verification of health, safety and environmental information. Social accounting will present interesting problems and the necessity of having no rules in this area is very clear: this is a grey rather than black and white game, one open to interpretation rather than fixed rules.

That is going to be very difficult for a profession that is built up on a two plus two equals four mentality. We are actually in a world where two plus two is maybe not quite four. I welcome technology but to me it is about on-line, up to date information rather than something that is static. It is not enough to audit an organisation and say 'that is the company' because by the time it has been audited it has already changed and moved on.

It is easy enough for a large company like Shell to use technology efficiently because, in many ways, it is the only way that it can bring information together as a whole. A smaller company is going to be much more reliant on simpler and perhaps less quantifiable things and one must be very careful to differentiate between SMEs and other companies.

ALAN BENJAMIN

Chairman, QSP Holdings plc

I don't think that there will be a problem with the indiscriminate disclosure of information: the horses may want to charge away but the reins will be applied. The word 'caution' will be used almost as frequently as the word 'stakeholder'. However, it is a fact that companies are not the determinants of what information people require about them. It is the stakeholders themselves who are saying that they need to know more about companies for their own purposes. Companies must ask stakeholders what information they require and how it can be provided and then present it in a properly manageable form.

ROGER DAVIS

Head of Professional Affairs, PricewaterhouseCoopers

I believe that if something is publishable then it must be verifiable in some way. I would not like to see the type of audit profession that thinks, 'Well, it is OK to give this information to the shareholders and other stakeholders but I'm afraid we cannot comment.'

If one goes back 20 or 25 years, the auditing profession was actually quite good at commenting on subjective information and using its judgement. The profession has become much more regimented over the last 10–15 years through accounting standards and the need to put figures in the right boxes. I think it would make for a very healthy auditing profession for it to start coming back out of those boxes and giving honest opinions on information as to whether or not it is fair. I am not saying those opinions will be infallible any more than the information is itself but management has to make a judgement as to whether that information can be put into the public domain and it is verifiable in that context. I do not at all see why the auditors should not be able to make that judgement. However, the problem of liability would need to be cleared up before too much progress could be made.

ANNE JENKINS

Director, ATC Professional Training Ltd

Since technology can enable stakeholders to drill down into a corporate Web site and even access the company's management accounting system to look up their own details, it must surely be possible then to drill down through the audit files to the detailed level of audit working papers and to see exactly what it is that the auditors have done. Perhaps auditors can now also start to adopt the new technologies and use the possibilities presented.

BARRY SPAUL

Lecturer, University of Exeter

It would be easy to run away with the idea that new technology is all about presenting much more information. Should we not also be thinking about technology being used to filter information in the same way that, for instance, a head-up display in a modern military jet filters and presents a tremendous amount of information in a relevant way to a pilot every second? For pilot read stakeholders.

ALAN BENJAMIN

Chairman, QSP Holdings plc

I think that the filtering of information should best be left to the stakeholder. In the case of a fighter pilot, some of the information relates to outside influences such as missiles arriving or enemy planes in sight. Those are stakeholders. Refining information to make it relevant and useful is a task done by technologists and managers and the technology has the capacity to do it. Over time, people will avoid deluges of information by pre-selecting what they need and having it filtered for them but it is the person who wants the information who has that role, the stakeholder.

DAVID PINCHES

Director, QSP Holdings plc

Technology is now at a stage whereby filtering can be done either by an organisation, dependent on how it perceives the profile of its groups of stakeholders or individuals, or by the inquirer himself. Furthermore, technology is developing at such a rate that information can then be pushed from the enterprise to that individual against certain mutually or individually pre-set criteria. In fact, the technological infrastructure is already available.

MARK GOYDER

Director, Centre for Tomorrow's Company

The point about filtering is a very important one. Barry Spaul's report *Corporate Dialogue in the Digital Age* clearly highlighted the capabilities of intelligent agents in enabling the user of information to specify the kind of report he requires. I believe, however, that we are in fact facing two issues: filtering information not only for the user or stakeholder but also for companies. Companies should be squaring up to this challenge. Given that there exists a need for both voluntary and compulsory disclosure and that more disclosure is likely to be required in the future, companies will help themselves if they think about the total pattern of disclosure that they want. Then, as the voluntary becomes compulsory, it causes fewer sleepless nights because a framework and reporting model are already in place. That is the conceptual task to be undertaken now.

CHRIS FAY

Chairman, Shell UK Limited

Our experience with stakeholder dialogue is that giving some basic information actually satisfies the vast majority of stakeholders. Giving more detail often results in a smaller number of stakeholders engaged in that dialogue: a one-to-one discussion with a non-governmental organisation (NGO) results in a far more reasoned debate than talking with 15 NGOs.

Shell's stakeholders suggest that the frequency of Shell's reports to society should actually be every two years not one, the simple reason being that one year is not long enough to accurately show real change. I think we have got to understand what stakeholder dialogue really means as opposed to stakeholder information. Dialogue fatigue sets in when people already have the basic information but no meaningful contact with the companies concerned. It is interesting that the first two or three sessions of meetings with stakeholders are really devoid of information until you reach the real dialogue when it is amazing how quickly there is actually a communality of thought as to the way forward.

HILARY SUTCLIFFE

Managing Director, Addition Public Relations

What sometimes gets lost in the debate about reporting is that the whole point behind financial and performance measures is to find qualitative information about a company, about what makes it tick and to gain an understanding of the company. This is what is totally invaluable but tends to get lost when we look at how we respond to the demands of stakeholders. It is how we run the company that is important rather than how we respond to the people who want to know about us.

DAVID PHILLIPS

Partner, Value Reporting, PricewaterhouseCoopers

The debate is about the inside looking out rather than the outside looking in. Companies are increasingly having to understand better what it is that creates value in their organisations. The better-run companies are noticeable in the way they manage themselves; they have, for instance, balanced score-cards which they use to determine how they should take management decisions.

What we are really talking about is the need for greater transparency. Arguably, the management model has changed in that companies no longer rely just upon financial information to run themselves and there is a plethora of management reporting now used which has to be reported in slightly more expansive ways to the outside world.

I believe the capital markets will not have to gather information from all sorts of sources which technology now enables them to do. A telecoms analyst a few weeks ago told me that he had spent the previous week speaking to 20 suppliers around the world to a company that he was researching to try to understand what was going on in the business. The information is freely available today. Companies believe that they can keep their cards close to their chests. I think they are misguided. Both companies and society benefit from greater transparency but it is something that should really be happening today in managements themselves.

ALAN COOK

Technical Director, Accounting Standards Board

I welcome the need for a much broader base of information in reports on a company but I think it is useful to distinguish between two different types of information. There is a whole gamut of experimental information that needs to be developed and encouraged but people also need to see that it is experimental. On the other hand, there is a very different kind of information of which the prime example perhaps is audited information but which is now developing, for instance, in the area of environmental reports. We need to know where we stand on this. We should not confuse the two.

The genesis of the very strict financial reporting regime that we now have across the world today emerged as a result of the Wall Street crash which occurred because companies were hyping themselves up on information that had no factual or audited basis which was fed into stock prices. We need to develop techniques that will enable us to move from the experimental to the factual and the standardised.

If you try and quantify and add the knowledge base into the assets of a company it is rather like putting a kind of black box in there. Nobody knows what was the basis for those figures. It would be better for the company to talk in general terms about how it sees the development of its employees. Let us always have some kind of modesty about the extent to which we can quantify information. Let us try to quantify where we can but not pretend that quantification can always be achieved.

Companies should think even harder than they do at the moment about what they are putting into their simplified financial statements. This is something that the Accounting Standards Board is currently looking into since it believes it is very important to raise the present degree of financial awareness, something which really should be done through simplified statements rather than the huge annual reports that companies are sending out.

JOHN PLENDER

Chairman, PIRC Ltd

It is encouraging, in a world where competitive advantage derives increasingly from intangibles, that there are pioneers who have been prepared to experiment and, as far as the integrity of financial information is concerned, the genie is out of the bottle. Companies will see advantage in more frequent disclosure. We will be seeing multiple interim disclosure and it seems impossible that auditors will be able to respond to that information in the way they have in the past. It would be costly. The audit profession may well be in the same position as a central banking supervisor, where the risk profile of a company it supervises changes minute by minute. You simply cannot supervise in those circumstances. Possibly one way of dealing with this would be a different approach in the London Stock Exchange Listing Rules which stipulate how this information is released. Another approach would be for auditors to examine the bases from which the information is derived and to report more widely about the integrity of a company's reporting approach in the auditor's report.

ROGER DAVIS

Head of Professional Affairs, PricewaterhouseCoopers

The auditing profession has no choice but to adapt to the changing business environment and we have only seen the surface of how communication is going to change over the next ten years or so. Historical accounts are a declining proportion of the total communications package and, if the auditing approach is to remain relevant, it has to adapt to a concept of auditing in a framework within which this information is put out.

I think companies should be experimenting with new information: the balance sheets are increasingly less relevant than they were 20 years ago. In another 20 years' time, there are not going to be many smoke stacks left to put on balance sheets: the only assets that a company will have will be the soft assets. Either the world moves to just cash flow accounting (because accruals accounting will not mean anything anymore if you do not have the assets on the balance sheet) or we have to experiment with new models of accounting. The auditing profession has been innovative before and can be again.

CHRIS FAY

Chairman, Shell UK Limited

We are now a 'show me' not a 'tell me' society. People want to be shown what companies are doing and that is at the root of the matter. I am pleased at the way the environment is now a part of the everyday thought process in our culture.

This extends down to an operator doing something with a valve who will instinctively take a drip tray as part of what he is doing. Societal aspects also will become more natural in everyday thinking processes but this may also need a return to the classroom. The idea of the triple bottom line will be in-built into the totality but will not happen overnight.

MARK GOYDER

Director, Centre for Tomorrow's Company

It is obvious that most people want to see innovation born of good practice rather than regulation although in reality this puts terrific pressure on those who have a role in leadership. At the heart of the task of innovation is what The Centre for Tomorrow's Company has been calling the 'search for a common language'. This is not a tidy process that results in a definitive bottom line. It involves a shifting dialogue. We have also found a duality in measurement: not everything can be benchmarked.

The paradox for every company is that there are some things which can be compared across that company (not only against others) and be benchmarked. These must be sought out and defined, i.e. the common language. There are other things that are unique to individual companies and people who use company reports want to hear about them. To me it is a bit like the game of golf: you play not only against the course and your opponents but also against yourself. I do not think this duality should ever be forgotten.

In our work we have found that measurement performs two different functions. One is to observe reality, to know where you really are. But the other, equally important, is to signal where you want to get to and what you believe to be important.

BIOGRAPHIES

SIR BRIAN JENKINS GBE

Sir Brian Jenkins is chairman of Woolwich plc and of the Charities Aid Foundation (CAF). He was a senior partner with Coopers & Lybrand until 1995, Lord Mayor of London in 1991-92 and president of the Institute of Chartered Accountants in England and Wales in 1985-86.

Sir Brian has been appointed by the Governor of the Bank of England to the Financial Law Panel. He is a director of The New Millennium Experience Company Limited and past president of the London Chamber of Commerce and Industry (1996-98) and the British Computer Society (1997-98).

He serves as a government appointed member of the Commission for the New Towns and The Architectural Heritage Fund.

CHRIS SWINSON

After reading PPE at Wadham College, Oxford, Chris Swinson qualified as a Chartered Accountant in 1974. He joined Price Waterhouse in 1970, initially as an articled clerk and later as audit manager.

He became a partner at Binder Hamlyn in 1981, acting as the firm's UK technical partner and later as national director of accounting and auditing. He was the firm's national managing partner from 1989 to 1992. He became a partner in BDO Stoy Hayward in January 1993 and was appointed the firm's senior partner from 1 July 1997.

He became a fellow of the Institute of Chartered Accountants in England and Wales in 1980. He has been a member of Council since 1985 and became president of the Institute in June 1998. He is chairman of the Institute's Executive Committee and chairman of the Regulation Review Implementation Working Party. He was appointed as trustee to the Greenwich Foundation for the Royal Naval College in February 1997.

CHRIS FAY

Chris Fay became chairman and chief executive of Shell UK Limited on 1 November 1994.

After gaining a PhD in civil engineering, Chris Fay joined Shell International Petroleum Company Limited in 1970. He went to The Hague in the Netherlands as an offshore design engineer, and in 1971 was posted to the Shell BP Development Company in Nigeria. Between 1971 and 1974 he held several posts, starting as drilling services engineer and finishing as chief civil engineer.

For the following four years he was head of engineering, planning and design and offshore construction for Sarawak Shell Berhad in Malaysia.

From 1979 to 1981 he was development manager of Dansk Undergrunds Consortium in Copenhagen, Denmark, on secondment from Dansk Shell. In 1981 he became technical manager of Norske Shell Exploration and Production at Stavanger, Norway, and was appointed director of exploration and production in 1984.

In 1986 he became general manager and chief executive of the Shell companies in Turkey with responsibility for Shell's integrated oil, gas, coal and chemical activities. From 1989 until his current appointment he was managing director of Shell UK Limited.

Chris is a Fellow of the Institute of Engineers, the Royal Academy of Engineering, the Institute of Petroleum, the Royal Society of Edinburgh and a Companion of the Institute of Management.

ALAN BENJAMIN OBE

In 1963 Alan Benjamin founded one the of the first software companies in the UK, Systems Programming Ltd.

He became ICL's director of communications in 1979 and joined the board of Cap Group Plc in 1981, responsible for all overseas business. He was part of the team that in 1988 conducted the merger with Sema Metra of France to form the SEMA Group, one of the world's largest software companies.

He retired in 1990. Currently chairman of QSP, he was chairman of IT 82, the very successful information technology year which was a major national multi-event programme throughout Britain to create interest and participation in the new information technologies. He was awarded the OBE in January 1983.

He was a board member of the London Docklands Development Corporation from 1984 to 1990, and is now a member of council of City University and a director of the London Symphony Orchestra.

As a co-founder of the 100th Livery Company of the City of London, the Worshipful Company of Information Technologists, he was its Master in its first Livery year in 1991/2.

DAVID PINCHES

After gaining a degree in computing and mathematics, David Pinches joined the Mars Group of companies. In 1984 he joined Lotus Development UK becoming UK marketing manager at a time when the company's spreadsheet package Lotus 123 was fuelling the growth of PCs within the business world. He went on to join the US-based software house, Software Publishing Corporation, as international marketing manager for computer graphics and database products.

In 1993, he moved to The Sage Group plc (the world's largest supplier of PC-based accounting software) and set up a new division in the UK, becoming the UK marketing director in 1995.

In 1997, David took on the role of group marketing director for QSP and was instrumental in the formation of QSP NetConsulting.

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