PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers
ABN 52 780 433 757

Darling Park Tower 2
201 Sussex Street
GPO BOX 2650
SYDNEY NSW 1171
DX 77 Sydney
Australia
www.pwc.com/au
Telephone +61 2 8266 0000
Facsimile +61 2 8266 9999

Committee Secretary
Parliamentary Joint Committee on Corporations and Financial Services
Department of the Senate
Parliament House
Canberra ACT 2600

10 October 2005

Dear Sirs

Inquiry into Corporate Responsibility

Thank you for the opportunity to provide a submission to your inquiry on corporate responsibility. PwC supports the development of a reporting framework that delivers a simplified reporting environment for corporate Australia, and greater transparency for all relevant stakeholders.

The key points of our submission are that:

- Current annual reports are excessively long and detailed, have a diminishing readership, and any further legislation on environmental and social matters using the current reporting framework will only burden corporate Australia with little value being added for stakeholders.
- Our research indicates that 'less is more'. Corporate reporting should be simplified, more focused and more relevant. Furthermore, capital markets tend to ignore disclosures on corporate social responsibility unless there is a clear linkage to corporate strategy.
- Consistent with the above finding and the work of the World Economic Forum and Business in the Community, we advocate linking initiatives on corporate responsibility with corporate strategy and related business performance drivers
- However, reporting corporate responsibility against corporate strategy and related business performance drivers requires a robust and coherent framework, and at present such a framework is not available through existing triple-bottom-line reporting 'guidelines'.

- The framework proposed in our submission assumes that economic, legal and ethical responsibilities to shareholders are primary, but that long-term sustainable value is only realised if the interests of all relevant stakeholders are understood, addressed and reported.

We look forward to further consultation and to providing any assistance on this important matter. With that in mind, if you should have any questions regarding the content of our submission please do not hesitate to contact Nick Ridehalgh on 02 8266 4899, or myself, on 02 8266 3317.

Kind regards

Tony Harrington
Chief Executive Officer

Submission to the Parliamentary Joint Committee on Corporations and Financial Services

Inquiry into corporate responsibility

This submission is in response to the Committee's Terms of Reference and addresses point (f) "The appropriateness of reporting requirements associated with these issues". As we understand it, 'these issues' refers to corporate responsibility and triple-bottom-line reporting for incorporated entities in Australia.

For the purpose of this submission, we have adopted a definition of corporate responsibility from the 'business in society' literature. This definition recognises that a corporation's (social) responsibility[1] includes economic, legal and ethical responsibilities, as well as discretionary activities. Further information on this definition is presented in Attachment A.

We define triple-bottom-line reporting as 'statements about the economic, environmental and social aspects of an organisation's performance'.

The key points of our submission

- Current annual reports are excessively long and detailed, have a diminishing readership, and any further legislation on environmental and social matters using the current reporting framework will only burden corporate Australia with little value being added for stakeholders.

- Our research indicates that 'less is more'. Corporate reporting should be simplified, more focused and more relevant. Furthermore, capital markets tend to ignore disclosures on corporate social responsibility unless there is a clear linkage to corporate strategy.

- Consistent with the above finding and the work of the World Economic Forum and Business in the Community[2], we advocate linking initiatives on corporate responsibility with corporate strategy and related business performance drivers.

- However, reporting corporate responsibility against corporate strategy and related business performance drivers requires a robust and coherent framework, and at present such a framework is not available through existing triple-bottom-line reporting 'guidelines' (refer to footnote 6).

- The framework proposed in this submission assumes that economic, legal and ethical responsibilities to shareholders are primary, but that long-term sustainable value is only realised if the interests of all relevant stakeholders are understood, addressed and reported.

---

[1] The reference to 'corporate (social) responsibility' and 'corporate responsibility' within this submission is referring to a 'corporation's responsibility to society'.
[2] For further information on Business in the Community go to www.bitc.org.uk

1. The current corporate reporting framework

Our view, like many others', is that corporate reporting needs to focus on a more transparent and credible disclosure mechanism that helps to rebuild public trust in corporations. The current corporate reporting framework does not meet the relevant information needs of users today.

The framework was originally developed to account for physical assets in a manufacturing environment. It is no longer ideal in today's business environment, where corporate value is largely dependent on intangible assets, and where the Corporate Social Responsibility (CSR) agenda is becoming increasingly more important.

Coupled with the framework's structural shortcomings is its increasing complexity, much of which stems from regulators' reactions to recent accounting scandals and reporting abuses.

Regulators face a huge challenge in their ongoing efforts to rebuild public trust and are therefore adding additional layers of mandatory disclosure. In so doing, regulators do not appear to have a formal review process for reconsidering current rules and regulations and discarding those disclosures which may no longer be relevant or required by users of corporate information.

As a result, current annual reports are excessively long and detailed to ensure compliance, and further legislation on environmental and social matters using the current reporting framework will only further burden corporate Australia.[3]

In addition to these 'compliance' reports, many companies are producing additional publications in an attempt to meet the expectations of specific-user groups (CSR reports, customer charter performance reports, environmental reports and other forms of triple-bottom-line reporting).

Some of these reports are very informative, others look like marketing documents. Either way, our research indicates that capital markets tend to ignore them unless there is a clear linkage to corporate strategy.

2. A proposed framework for reporting corporate responsibility

In delivering greater transparency against economic, legal and ethical responsibilities, and discretionary activities, companies need to organise and align information in a manner which facilitates effective internal management and reporting, and which can be consistently applied to external communications to shareholders and other stakeholders. After all, stakeholders are not data miners – they require and deserve clear, logically presented information.

For nearly a decade PwC has been researching and codifying corporate reporting (ie information in annual reports, sustainability reports, company websites, etc), and testing its presentation with

[3] Attachment B at the end of this submission provides an overview of specific environmental and social obligations relevant to corporate reporting.

key stakeholders in and around capital markets.[4] This work has emphasised the importance of reporting performance against key strategies and related business performance drivers, both financial and non-financial.

Reporting performance against key strategies and related business performance drivers is not unique. The World Economic Forum and Business in the Community both encourage the design and reporting of corporate responsibility initiatives against drivers that help to improve business performance. For example, the World Economic Forum has published eight business performance drivers (value drivers) for corporate responsibility[5]:

- reputation management
- risk profile and risk management
- employee recruitment, motivation and retention
- investor relations and access to capital
- learning and innovation
- competitiveness and market positioning
- operational efficiency
- licence to operate.

We are strongly in favour of linking initiatives on corporate responsibility with business performance drivers recognised by capital markets. Indeed, many of Australia's largest companies have started to embed these business performance drivers into their sustainability reporting (see, for example, sustainability reports by BHP Billiton, IAG and Westpac).

However, we believe that reporting corporate responsibility against economic, legal and ethical responsibilities, and discretionary activities, using drivers linked to business performance requires a robust and coherent framework, and that at present such a framework is not available through existing triple-bottom-line reporting 'guidelines'.[6]

---

[4] This research is documented each year in the PwC publication titled 'Trends – good practices in corporate reporting*'. Details of our research program and certain findings and reports are available at www.pwc.com/au/valuereporting . PwC's research, which includes surveying over 3,000 CFOs and investment professionals, identifies and acknowledges the growing number of companies that are steadily moving towards more transparent reporting, and provides practical examples of how this is being achieved. We have enclosed hard copies of the 2005 publication with this submission.

[5] Roberts, S., Keeble, J. and Brown, D. 'The Business Case for Corporate Citizenship', World Economic Forum website

[6] Over the past 15 years numerous international and national guidelines have been issued to assist companies reporting their social and environmental performance. Examples of international guidelines include the Valdez Principles (1989), the WICE (World Industry Council for the Environment) guidelines (1993), the PERI (Public Environmental Reporting Initiative) guidelines (1994), and the GRI (Global Reporting Initiative) guidelines (1999, 2002). There are also numerous national guidelines.

2.1 A framework based on a 3-tier model

The framework we are proposing for reporting corporate responsibility is grounded in the following model:

- Tier one: generally accepted accounting principles

  Any framework will need to be built on a number of underlying principles, the key ones being transparency and consistency. It will need to recognise that corporate responsibility information (financial and non-financial) is demanded by all stakeholders and not just investors. While investors might have primacy, the needs (including information) and societal expectations of all relevant stakeholders must be addressed if corporate value is to be optimised longer term.

  The framework should also assume that information needs to be communicated consistently across all mediums, with a particular focus on both historic trends and forward-looking information and associated assumptions.[7] This is not about providing profit forecasts, but about being transparent on high-level targets, milestones and non-financial information that provides confidence to all stakeholders.

- Tier two: industry-specific standards

  Our ongoing empirical analysis shows that reporting should be tailored according to the specific dynamics of each industry. This is also a highly significant finding in the vast majority of the corporate social accountability literature.[8]

  What this means, for example, is that performance measures for *innovation* rank highly in the pharmaceutical sector, *risk and financial management systems* feature prominently in the banking sector, and *environmental performance* is a critical success factor for the mining sector. The contents of any framework should be tailored to reflect industry dynamics, using standard definitions in key non-financial areas developed by industry associations and participants.

- Tier three: company-specific information

  Any framework for reporting corporate responsibility will also need to focus on company-specific information, based on their own unique strategies and performance metrics with associated definitions. In order to gain comfort with the sustainability of current corporate performance, investors and managers alike demand a body of information that considers both the external environment in which the company operates,

---

[7] International Financial Reporting Standards have started to introduce consistency in financial measures, and also provide a platform for principles relating to non-financial information.

[8] The term ‘corporate social accountability’ is used to describe the broader philosophical issues concerning organisational accountability to society, which includes the process of reporting environmental, social or economic information concerning corporate activities, services or products to multiple stakeholders (society).

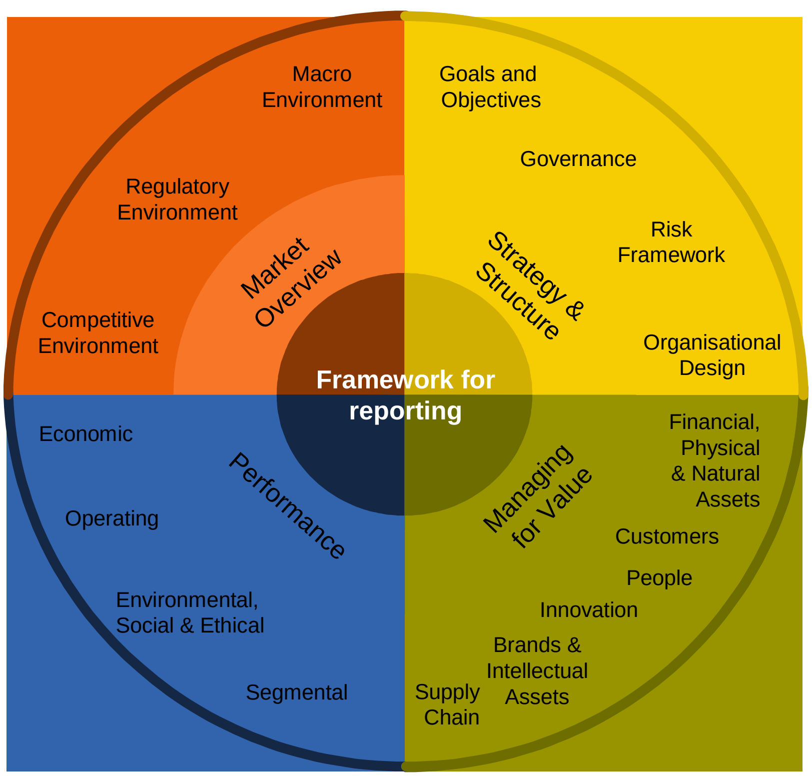
and the resources and competencies that management can harness to execute its strategy.[9] The ultimate success of these endeavours will be measured in terms of economic and operational performance.

2.2 Four categories of information

Our research indicates that a framework for reporting corporate responsibility grounded in the above model can be presented using four basic categories of information, which we have called:

- Market overview
- Strategy and structure
- Managing for value
- Performance.

Together they create a coherent and complete medium to longer-term picture of a business, against which short-term performance (both financial and operational) can be explained. The framework assumes that economic, legal and ethical responsibilities to shareholders are primary, but that long-term sustainable value is only realised if the interests of all relevant stakeholders are understood and addressed.



[9] This body of information could be organised so that standing data (governance frameworks, directors' details, remuneration contracts, accounting policies and other details which do not change regularly) is held and updated 'on-line' via the internet, with updates being notified to shareholders and other stakeholders in the performance report.

The four categories of the framework link to and build upon one another. For this reason, the framework should not be viewed as a static medium for presenting discrete bits of information. Used properly and integrated into internal management processes, it becomes a dynamic tool for assessing and monitoring all key aspects of performance and for communicating publicly a company's economic, legal and ethical responsibilities, as well as discretionary activities.

3. The framework in practice

A closer examination of each of the four categories provides additional insight into how companies can put the framework to practical use.

3.1 Market overview

Logically this represents the starting point for any analysis and presentation of performance in regard to economic and legal responsibilities, as factors in the external marketplace typically constitute a dominant force in determining a company's current performance and medium to long-term sustainability.

However, in our experience this is an area less understood and communicated by companies than one might expect. This is surprising given its fundamental importance in regard to the rationale and logic for the chosen strategic direction, and thus its role in evaluating a company's current performance and medium to long-term sustainability.

In meeting their economic and legal responsibilities corporate managers should communicate their views on areas such as:

- the opportunity space in which the company is competing
- the company's position within the competitive landscape
- the macro economic environment
- the regulatory challenges facing the company.

3.2 Strategy and structure

Corporate economic and legal responsibility also includes the need for management to clearly articulate its strategy for competing within its particular marketplace, ideally supported by quantified medium-term targets and relevant milestones.

Any strategy should be based on an understanding of the key areas in which a company has competitive advantage. Accordingly, the company's success in creating value will depend on management's ability to invest in resources in these areas and manage them to deliver the sustainable financial performance investors expect.

In meeting their economic and legal responsibilities corporate managers should communicate:

- the overall mix of risk (eg cost of capital), return (eg cash flow) and growth that management has chosen for the business
- the mix of risk and return according to each business segment, as well as for the corporate centre
- the portion of their growth strategy that will be achieved organically versus the portion requiring acquisitions
- how the company's underlying organisational and governance structures, systems, and processes and risk management frameworks are aligned with strategy.

3.3 Managing for value

Having communicated a well-defined strategy that includes the goals and objectives for those activities that drive value and provide competitive advantage, management should specify at a more detailed level the complex web of assets, relationships, capabilities and processes it has in place for executing the strategy.

By reporting on how it is enhancing areas of business activity linked to strategy and related performance drivers, and by providing a sense of the company's health through metrics and other information, management can help the investment community and other relevant stakeholders assess both current performance and the company's likely longer-term sustainability.

However, it is our experience that the information appearing in many boardrooms remains predominantly financial in nature. Without non-financial information management and the board are partially flying blind – and when financials tell them there is a problem, they have already missed the optimal point for taking corrective action.

This complex web of assets, relationships, capabilities and processes must be carefully communicated to provide clarity to all relevant stakeholders on how the organisation strives to meet its economic, legal and ethical responsibilities. This includes:

- the ability and commitment of their people to deliver against strategy
- stewardship of financial, physical and natural assets
- the degree to which customers trust their products or services
- relationships and accountabilities with a wider stakeholder group
- capacity to share knowledge, to learn, to adapt, to innovate
- the protection and enhancement of the value of its brands and intellectual assets.

All of these value-creating activities are common to most companies, although their relative importance will differ based on industry dynamics and corporate strategy.

This message is consistent with the World Economic Forum's recommended application of eight business performance drivers (value drivers) for corporate responsibility – they are all relevant, but some are more relevant than others depending on industry dynamics and corporate strategy.

3.4 Performance

This category is, of necessity, a key focus both internally and externally. It is the test of whether a company has delivered results in line with expectations and, implicitly, of how well management has understood its market, executed its strategy, and managed its value-creating resources and relationships. It is here that the elements of risk, return and growth come together in the form of performance outputs.

Historically, reporting on performance has been about reporting financial numbers. While financial performance remains at the heart of corporate reporting, it needs to be expanded. It is our view that performance should be reported in a more holistic way by including:

- economic measures (ie market growth, share of market, sales growth, weighted average cost of capital, etc)
- operating results (ie customer satisfaction, average revenue per customer, revenue from new products, etc)
- management of economic, legal and ethical responsibilities relevant to the company's strategic objectives (including performance in managing environmental and social risks[10])
- important aspects of performance by major individual business segments.

A framework that reports in this way would provide greater transparency against corporate economic, legal and ethical responsibilities, as well as still placing an appropriate level of emphasis on reporting financial performance.

[10] For example, climate change risks affecting the insurance and finance sector, labour standard risks affecting supply chains in the retail sector, and environmental rehabilitation risks affecting future access to land in the mining sector.

4. The benefits to corporate entities in Australia

Our research indicates that capital markets tend to ignore disclosures on corporate social responsibility unless there is a clear linkage to corporate strategy. This was a key finding from a series of focus groups designed to determine whether capital markets reward organisations that practise better disclosure of non-financial information (including information relating to economic, legal and ethical responsibilities).

Over the last few years we have conducted geographic and industry-specific research to highlight the economic and reputational rewards to those who were perceived to practise fuller disclosure of non-financial matters. These perceived rewards included:

- increased share value
- increased management credibility
- improved access to new capital (and potentially a reduced cost of capital)
- increased number of long-term shareholders
- reduced volatility in the capital markets.

We have since conducted additional research to determine if those perceived benefits would actually materialise, and whether investors would truly reward companies that practised greater transparency. In a partnership with Schroders Asset Management, a major UK fund manager, we have been able to show the economic and reputational benefits of non-financial reporting and in particular that:

- more focused and relevant reports generate greater certainty over future economic prospects of the company and a less volatile stock
- a strong relationship exists between corporate reporting and the value placed on a company
- financial data with boilerplate disclosures alone are insufficient to evaluate corporate performance with any degree of accuracy.

5. Conclusion

Our view is that 'less is more' and any initiatives by Government and standard-setters in regard to reporting corporate responsibility should aim to simplify the reporting activities of Australian entities. Current annual reports are excessively long and detailed, and any further legislation on environmental and social matters using the current reporting framework will only burden corporate Australia.

The reporting of corporate responsibility goes beyond the scope of the current CSR debate and includes matters regarding economic and legal responsibility. As such, corporate Australia should be encouraged to report their corporate responsibility against key strategies and related business performance drivers – an approach also advocated by the World Economic Forum.

However, we believe that reporting corporate responsibility against key strategies and related business performance drivers requires a robust, coherent and simplified framework, and that at present such a framework is not available.

With this in mind, Government and standard-setters should:

- recognise that the existing reporting framework was originally developed to account for physical assets in a manufacturing environment and is no longer ideal in today's environment where corporate value is largely dependent on intangible assets

- recognise that current annual reports are excessively long and detailed, and that in addition many companies are producing additional reports in an attempt to meet the expectations of specific-user groups, and that any further initiatives should reduce the volume of material currently being presented

- focus on a robust and simplified framework for reporting corporate responsibility grounded in a 3 tier model that includes underlying principles (the key ones being transparency and consistency), industry dynamics and company information based on specific strategies and performance metrics.

Furthermore, clarification is needed on a definition for corporate responsibility that recognises an organisation's goal to balance economic, legal and ethical responsibilities, and discretionary activities, with the demands on all relevant stakeholders.

Attachment A - Definitions used in our submission

Corporate responsibility

The term 'corporate responsibility' has been extensively discussed for over 100 years in the 'business in society' literature. This history is carefully documented in a number of academic and business publications and frequently defines corporate responsibility using the following model:

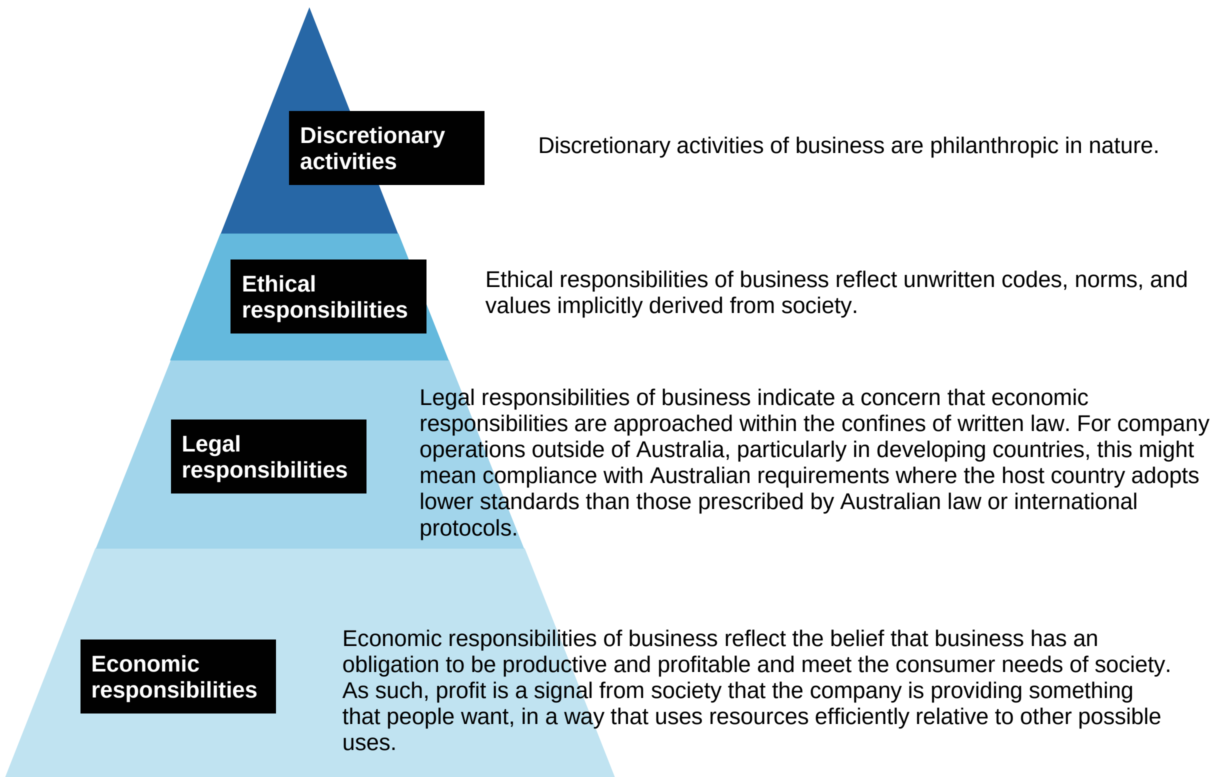


Figure 1: Defining corporate responsibility – framework sourced from the 'business in society' literature

Triple-bottom-line

The term 'triple-bottom-line' was coined by John Elkington and made popular in his publication *Cannibals with Forks: The Triple Bottom Line of 21st Century Business* (1998). It encourages corporate reporting on matters regarding economic, environmental and social performance. However, the notion of a triple-bottom-line has been explored in the corporate social accountability literature for the last 30 years using themes relating to corporate behaviour against social and environmental 'bottom-lines', with monetary disclosure against these same themes to define the economic 'bottom-line'. For example, disclosure against *lost time injuries* would be a component of the social bottom line, and disclosure regarding the monetary implications of *lost time injuries* would be a component of the economic bottom line.

Attachment B – Current reporting requirements

In 2002, PwC explored the triple-bottom-line reporting practices of 150 companies in Australia, Singapore and South Korea and found that in Australia the legal requirements displayed in Table 1 influenced how companies reported environment and social matters. This observation was drawn after a comprehensive review of Australian company laws, accounting standards, stock exchange listing rules and generally accepted accounting principles.

Category and (theme)	**Summary of information to be disclosed**	**Where to be disclosed**	**Originated in**	**Activated in**	**Current extant - AIFRS**
Environment (restoration)	Amount of restoration obligations, accounting methods, significant uncertainties, assumptions and judgements.	Financial accounts	UIG Abstract 4	1995	AASB 137
Environment (pollution control)	Compliance with particular and significant environmental regulation	Directors' report	Company Law Review Act, 1998	1998	Corps Act s.299(1)(f)
Social (employee entitlements)	Nature and amount of employee entitlement assets and liabilities; comparative information with previous year.	Financial accounts	AASB 1028, AAS 30 (Employee entitlements)	1994	AASB 119, AASB 124 & AASB 101
Social (share ownership)	Description and nature of scheme; price, number and type of shares; total market value; accounting policy, etc	Financial accounts	AASB 1028, AAS 30 (Employee entitlements)	1994	AASB 2
Social (super-annuation)	Aggregated accrued benefits; net value of the plan assets; accounting policy. AIFRS introduces specific rules for recognising and measuring superannuation and other post employment benefits, and additional disclosures relating to amounts recognised.	Financial accounts	AASB 1028 AAS 30 (Employee entitlements)	1994	AASB 119
Social (super-annuation)	Details of accounting policy, contributions and liabilities regarding superannuation contribution surcharge.	Financial accounts	UIG Abstract 19	1998	UIG Abstract 19

Table 1: Legislation affecting the reporting of social and environmental matters

Further reporting requirements similar to those above is not something that we would advocate. Our opinion is that any initiatives by Government and standard-setters should aim to simplify the reporting activities of Australian entities and focus on disclosures against key strategies and related business performance drivers, both financial and non-financial.