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why the IASB is focusing
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Man with a plan
Hans Hoogervorst tells us
why the IASB is focusing
on better communication

Burning issue
Why companies are feeling
the heat on climate-related
financial disclosures
Dear readers,

Corporate social responsibility (CSR) is no longer an optional extra in the growing list of management initiatives. It’s a strategic priority for global companies, and one that will have a significant impact on reporting requirements. The effects of globalization, concerns over climate change and calls for greater sustainability have put CSR center stage. Users of financial reports are looking for assurance that goes beyond the numbers, and involves demand for data on environmental, social and governance (ESG) issues.

This demand comes in many forms, as this latest issue of Reporting shows. It involves mandatory compliance with legislation, such as the European Union Directive on Nonfinancial Information. But a number of voluntary initiatives are also creating a wind of change.

We look at two such initiatives in these pages – those formulated by the International Integrated Reporting Council (IIRC) and the Task Force on Climate-related Financial Disclosures (TCFD).

Richard Howitt, the IIRC’s CEO, describes integrated reporting (IR) as a “global movement” that allows companies to focus on long-term value (page 23). Around 1,500 companies are already using or referencing IR, and Howitt is expecting many more to come on board.

Meanwhile, the TCFD has published an analysis promoting a new reporting framework. We interview two members of the Task Force – Mary Schapiro, former Chair of the US Securities and Exchange Commission, and Graeme Pitkethly, Unilever CFO (page 08). Schapiro suggests that pressure from investors, lenders and insurers for “decision-useful” climate-related financial information has reached a critical point.

Regulators and standard setters are aware of the trend. Hans Hoogervorst, Chairman of the International Accounting Standards Board, tells us that nonfinancial information is “complementary to the statements” (page 14). However, he accepts that there are some challenges on integrated reporting: “There is progress, but there is not the beginning of a single set of global standards, and I think it is very hard for preparers to figure out exactly what they need to do.”

There is certainly still work to be done here – both in consolidating competing frameworks and in producing robust standards that can be endorsed as generally accepted. But the direction of travel is clear, and the importance of nonfinancial information in corporate reporting will inevitably grow in the months and years ahead.

I hope you enjoy this issue of Reporting, which also includes features on the role of the CFO in cross-border acquisitions and Vietnam as an emerging market. Don’t forget that you can also find online-only features and videos on the Reporting insights hub at ey.com/reporting.

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Taking up the challenge

Crashing commodities, roller coaster share prices and labor disputes: Christine Ramon, CFO of South African mining company AngloGold Ashanti, has successfully dealt with all these and more in a career filled with challenging roles, as Adam Oxford discovers.

Christine Ramon has been described as the most powerful female business executive in South Africa. It may be hard to quantify such a title precisely, but she certainly has a strong claim to it. For the past two years, Ramon has been the CFO at AngloGold Ashanti, the world’s third-largest gold producer, which owns 17 mines in nine countries across Africa, Australia and South America.

Given South Africa’s historical reliance on the fortunes of the mining industry, and the dominant position of AngloGold in the sector, that position alone would guarantee Ramon’s status as a force to be reckoned with. But her career has seen her take senior positions in the country’s most important industries, always at a time when their future seemed most in flux and when their fortunes and those of the young democracy were most intertwined. Ramon has always been at the eye of whatever storm is blowing through South Africa’s often turbulent business community.

AN INSPIRING EXPERIENCE

As a young accountant who began her career with Coopers & Lybrand, Ramon’s first job in the new, post-apartheid South Africa was a secondment to the Independent Electoral Commission (IEC) for the 1994 general election that put Nelson Mandela and the African National Congress in power.

“It was an inspiring experience, but maturing at the same time,” recalls Ramon. “I was involved in setting up offices in nine provinces and it was truly satisfying for me to be involved in the first
democratic elections. It was also very trying, because we had bomb scares and strikes to deal with, and we still had to run a smooth election.”

Her experiences at the IEC convinced her that she wanted to play a role in the commercial growth of the new country, and she rapidly rose to the position of Finance Director and, later, CEO of media giant Johnnic Holdings. This was during a critical period of transformation for the press and entertainment sector through the Black Economic Empowerment policies of the time.

She left Johnnic to take up the role of CFO at South Africa’s most important petrochemical firm, Sasol. This was a period of massive expansion and diversification for a company that was transforming itself to fit the new economic and political life of the country.

At AngloGold, meanwhile, she finds herself in a mining sector that has been battered by volatile commodity prices, the unstable value of the rand and divisive labor issues as firms struggle to modernize amid rising costs and harder-to-reach resources. As if that wasn’t enough, Ramon is also a Non Executive Director at telecommunications giant MTN, which itself has been through a tough period of labor unrest, management changes and a US$1.7bn fine from the Nigerian Government.

It’s perhaps an indication of her character that, when asked about her uncanny ability to pick industries in turmoil, she simply says with a smile: “I guess I’m the type of person who enjoys a challenge.”

HOW TO TALK TO SHAREHOLDERS
To demonstrate how she rises to those challenges, Ramon describes how she took over as CFO at AngloAshanti at a tough time for the company.

“When I joined, one of our challenges was having a very highly leveraged balance sheet,” she says. “The shareholders didn’t want to put equity in the company, so we had to focus on self-help measures, and that entailed focusing on cost reduction to drive operational efficiencies in the business. It was a particularly low gold price environment, so our focus was to keep the long-term growth optionality in the business, even while looking at keeping the costs down.”

Just two years on, Ramon’s tight financial management has left the group looking decidedly healthier. Net debt is down by 32% and free cash flow has more than quadrupled to US$161m. The company is even considering a return to dividend payments in early 2017 – something that hasn’t happened since 2013. “Cutting debt by a third was a significant achievement,” says Ramon. “It was quite tough deciding which assets to dispose of, but it was the right thing to do; the important thing was communicating and getting buy-in from the operators as regards the decisions we had to make. The benefit of reduced debt then resulted in improved free cash flow generation in the group. The credit ratings agencies have moved us to a positive outlook and our share price has more than doubled.”

Ramon has, of course, had plenty of experience talking to shareholders, and she’s been tasked with delivering both good and bad news in the past.

“It’s very important for a CFO to be honest and transparent in communication with shareholders, as well as with other stakeholders,” she says. “Shareholders are interested in hearing about the challenges the business faces, whether it is related...
to the commodity price, regulatory developments or other challenges. They’re interested in hearing how management is dealing with these issues, and articulating transparently how you’re doing so does inspire more confidence in management.”

Being clear about future plans is also vital to gaining that confidence, she adds. “It was very important for us to undertake the cost-cutting initiatives without prejudicing the longer-term growth objectives,” she says. “That’s important for shareholders, because they do look at the longer-term value proposition of the company.”

**DRIVING NEW STANDARDS**

Ramon is as passionate about the wider world of financial reporting as she is about her day job. She is a past member of the Standards Advisory Council of the International Accounting Standards Board, and today she is Deputy Chair of the Financial Reporting Standards Council (FRSC) in South Africa and Chair of the national CFO Listed Companies Forum.

The FRSC is a particularly interesting place to work, as South Africa’s unique history means that corporate reporting is stringent: the Johannesburg Stock Exchange insists on integrated reporting, and rules around good governance and corporate social responsibility are arguably better defined than anywhere else in the world as the country continues on its long journey toward economic equality for all.

Ramon says that adopting the integrated reporting principles laid out by the International Integrated Reporting Council and the King Code of Governance hasn’t just kept AngloGold compliant, it’s also been an influence on company culture at all levels. “Having to produce an integrated report allows for more integrated thinking,” she explains. “It allows for functions and the business to come together as one and focus on the key messages that we need to deliver to shareholders.

“The integrated report has been a key report that allows us to capture succinct messages to shareholders, to employees, to broader stakeholders. It’s allowed us to pull together all the key objectives of the company, and the key deliverables as well.”

**BEYOND THE OFFICE**

Gaining experience beyond her day job has been a hallmark of Ramon’s career. In 2007, she was nominated as a Young Global Leader by the World Economic Forum (WEF), which opened up a global network of connections and influences.

“It created an opportunity for me to attend the WEF in Davos,” she recalls, “and also to participate in a number of different forums across the world whereby we, as a global community, could get a more in-depth understanding of some of the sustainability issues we face. And I experienced some of the solutions that worked effectively in certain environments, and that I could then take back to my own environment.”

As for that environment, Ramon doesn’t shy away from the sad truth that, as a woman of color, she’s still an unusual presence in the boardroom of a global company (although 27% of AngloGold Ashanti’s board of directors are female). That’s something she wants to change, and she has worked hard to direct the companies she’s worked for toward policies such as gender equity in pay and developing a culture that encourages and supports women as they are building careers in traditionally male industries such as mining and petrochemicals.

“Women who are leaders have got a key role to play,” she insists. “It’s important to be an executive in order to be able to drive these changes, and to refine recruitment processes to attract and fast track women with high potential to senior leadership positions.”

Significantly, Ramon can talk directly to the experiences of women living in the remote and poor areas where AngloGold typically operates and recruits. “I recently took part in a program on SABC [the South African national broadcaster],” she says. “I wanted to say, ‘Look, I’m a woman, I grew up in the Transkei and this is what I’ve done, and you can do the same. These are the challenges I’ve faced and this is how you deal with it.’”

Of all the subjects she talks about, this, she says, is the one that is the most important for her to get her point across. “In South Africa, only 25% of management positions are filled by women,” she says. “At the top, just 2.4% of CEOs are women, so we need to make a lot of inroads.”

To change that situation, you could hardly wish for a better role model than Ramon.
CHRISTINE RAMON: CV IN BRIEF

- Earns a BCompt degree in accounting and auditing from the University of South Africa in 1989.
- Works as an Audit Manager for Coopers & Lybrand for 10 years, both in South Africa and in Verona, Italy.
- Seconded to the South African Independent Electoral Commission in 1994 as Deputy Director, Finance, to help oversee the general election.
- In 1995, joins Johnnic Holdings as Senior General Manager, Finance, rising to the position of Finance Director in 2003 and then to CEO in 2004.
- In 1999, completes the Senior Executive Program at Harvard University in the US.
- Becomes CFO at Sasol Ltd in 2006.
- In 2009, is named Most Influential Woman in the Petrochemical Sector by CEO Magazine.
- Serves as Chairman of the CFO Listed Companies Forum in South Africa from 2011–13.
- Joins AngloGold Ashanti as CFO in October 2014.

View video

go.ey.com/RamonVideo
Awareness of the huge potential impacts of climate change has been spreading for at least 25 years. However, until recently, there has been no commonly accepted reporting framework that companies can use to make climate-related disclosures to their key stakeholders. Partly as a consequence, the degree to which they report on these issues varies considerably and, in many cases, disclosures are limited. The report from the Task Force on Climate-related Financial Disclosures (TCFD), published in December 2016, aims to change all that.

The Task Force was asked to do this work in late 2015 by the Bank of England Governor and Financial Stability Board Chair Mark Carney at the request of the G20 Finance Ministers and Central Bank Governors. Its 32 members were drawn from a wide variety of industries, as well as banks, asset owners, asset managers, ratings agencies, insurers and consultants. The aim was to create a broad, flexible framework that would meet the needs of both the companies making climate-related disclosures and their stakeholders.

Mary Schapiro (pictured on page 10), former Chair of the US Securities and Exchange Commission Chair and Unilever CFO Graeme Pitkethly are two key members of the Task Force on Climate-related Financial Disclosures. Andy Davis talks to them about reporting the effects of climate change, the need for a voluntary approach and how a new framework could help.
Commission and a special adviser to Michael Bloomberg (who chairs the TCFD), argues that demand from investors, lenders and insurers for “decision-useful” climate-related financial information has reached a critical point.

The report sets out 11 recommended disclosures grouped under four headings – governance, strategy, risk management, and metrics and targets – that deliberately follow the approach companies use already for other types of disclosure (see panel, below). The TCFD also offers both general and sector-specific guidance for financial and nonfinancial companies.

**RISKS AND OPPORTUNITIES**

According to Schapiro, the proposed framework represents a single solution to three separate problems. First, businesses need a coherent reporting framework that is efficient and cost-effective. Second, asset owners, investors and financial intermediaries need concise, reliable information that allows meaningful comparisons between companies and enables better decision-making about capital allocation and the assumption of risk by lenders and underwriters. Finally, Schapiro says, regulators and policy-makers need a better view of “the risks that are building in the financial system stemming from climate-related impacts – and, frankly, the opportunities too, which is one of the novel things about the framework we’ve developed.”

The intention is that the financial disclosures the TCFD calls for should form part of companies’ mainstream financial filings, as this is where discussion of other material risks takes place. “Over time,” says Graeme Pitkethly (pictured below), Vice-Chair of the TCFD and CFO of Unilever, “their adoption should promote better dialogue about material risks between companies and their stakeholders that leads to more accurate pricing of the business’ securities. Ultimately, we’re trying to

### The main recommendations

#### Governance

Disclose the organization’s governance around climate-related risks and opportunities.

**Recommended disclosures:**

- Describe the board’s oversight of climate-related risks and opportunities
- Describe management’s role in assessing and managing climate-related risks and opportunities

#### Strategy

Disclose the actual and potential impacts of climate-related risks and opportunities on the organization’s businesses, strategy and financial planning.

**Recommended disclosures:**

- Describe the climate-related risks and opportunities the organization has identified over the short, medium, and long term
- Describe the impact of climate-related risks and opportunities on the organization’s businesses, strategy and financial planning
- Describe the potential impact of different scenarios, including a 2°C scenario (i.e., one where the rise in global temperatures following the industrial revolution is restricted to no more than 2°C), on the organization’s businesses, strategy and financial planning

#### Risk management

Disclose how the organization identifies, assesses and manages climate-related risks.

**Recommended disclosures:**

- Describe the organization’s processes for identifying and assessing climate-related risks
- Describe the organization’s processes for managing climate-related risks
- Describe how processes for identifying, assessing and managing climate-related risks are integrated into the organization’s overall risk management

#### Metrics and targets

Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities.

**Recommended disclosures:**

- Disclose the metrics used by the organization to assess climate-related risks and opportunities in line with its strategy and risk management process
- Disclose Scope 1 (direct), Scope 2 (energy indirect) and, if appropriate, Scope 3 (other indirect) greenhouse gas emissions and the related risks
- Describe the targets used by the organization to manage climate-related risks and opportunities and performance against targets
allow fair valuation and pricing that is appropriate to the level of risk and opportunity."

The Task Force held more than 120 individual meetings with interested parties and reviewed and catalogued the near-400 existing initiatives on climate-related impacts. It aimed to incorporate this huge body of previous work but, in doing so, to produce a set of recommendations with a different and very distinct focus. “Lots of frameworks focus on how companies impact the environment; we focused on how climate change and the environment impact companies from a financial standpoint,” Schapiro explains. “That’s an important differentiator.”

The need to offer a clear path through the thicket of climate-related initiatives was also critical; faced with so many competing demands, it is easy for companies to “throw up their hands and say ‘This is just too complicated’,” says Schapiro. “These recommendations provide them with a coherent, informative framework for disclosure.” Instead, companies that use the TCFD’s recommended reporting framework can be confident that it synthesizes the existing work into a single source of guidance and best practice on climate-related financial reporting.

A FLEXIBLE FRAMEWORK
Pitkethly argues that the reporting framework had to be flexible rather than prescriptive because companies vary enormously across sectors and will therefore be affected very differently by the two major categories of climate-related risks the TCFD identified: the physical effects of climate-related events, and the risks (and opportunities) for their business of making the transition to a lower-carbon economy.

He believes Unilever, as a fast-moving consumer goods company with two billion customers each day in 190 countries, has more exposure to physical than to transition risk; but that, even so, most physical impacts do not have a great effect, because they are localized and Unilever’s operations are dispersed so widely around the world.

However, its recent experience in Brazil has shown how exposed companies are to water scarcity. Brazil is a major market for Unilever’s Omo laundry brand, and São Paulo, a city of 12 million people, has been hit by water shortages. “If people can’t wash their clothes because there’s no water, you get a sense of the impact – it goes into the tens of millions of euros,” says Pitkethly. “These are climate-related risks and opportunities for businesses that are definitely material and that need to form part of our dialogue with stakeholders.”

For companies in other, more carbon-intensive industries, such as energy or mining, the physical and transition risks are likely to be much more concentrated on particular locations and specific, major aspects of the way they operate. The TCFD’s framework tries to accommodate these differences by taking a flexible and pragmatic approach to the

Scenario analysis
A central element of the TCFD’s recommendations is that companies should consider using scenario analysis to support their strategic and financial planning, and that they should report the results and their proposed responses. It suggests that the base scenario should assume that the rise in global temperatures following the Industrial Revolution is restricted to no more than 2°C, but that a range of other scenarios “that covers a reasonable variety of future outcomes, both favorable and unfavorable” should also be planned and reported.

Scenario analysis is already commonly used in industries, such as energy and mining, which have significant exposure to climate-related impacts, but its use elsewhere is much more patchy. The TCFD acknowledges that, for many businesses, scenario analysis will be a more qualitative exercise than for many existing users, but argues that this does not render it irrelevant.

Graeme Pitkethly says Unilever does not currently use scenario analysis extensively, but adds: “What my time on the TCFD highlighted is the benefit of scenario analysis in helping businesses to think and talk internally about the impacts of climate change, both physical and transitional. I think we will start to use it in a more qualitative sense to help our internal decision-making and long-term strategic choices.”

“ We focused on how climate change and the environment impact companies from a financial standpoint.”
Mary Schapiro
job of setting out the reporting framework. An important element of this flexibility is the TCFD’s intention that companies should be able to use the framework as a starting point to develop their own approach to reporting on climate-related financial impacts, and that this should not involve excessive additional costs. The Task Force believes that the approach companies take will evolve from a more qualitative one at the beginning toward an increasingly quantitative set of disclosures as they develop their processes for climate-related reporting.

“While there will be some [additional] costs, these are largely costs that will be incurred in any event as companies meet their existing disclosure obligations. Investor demand for this information continues to grow,” says Schapiro.

She also suggests that, as climate-related reporting becomes more mainstream, tools and analytical techniques will be developed that will help to reduce the compliance costs that companies face.

**VOLUNTARY ADOPTION**

Both Schapiro and Pitkethly acknowledge that the TCFD’s framework has some overlaps with others, including the EU Directive on Non-Financial Reporting, which came into effect from January 2017, and the International Integrated Reporting Council’s (IIRC) framework. However, there is little direct duplication, as both these initiatives are concerned with a wider set of issues than just climate-related financial impacts.

“I think many large companies will be well advanced in being ready to adopt the new requirements;” says Pitkethly, “which shows that the market is already moving in the direction of more and better disclosure. My only concern is that companies should have the flexibility to report their own story in their own words, and I think the TCFD framework provides that.”

Unlike the EU directive, though, the TCFD’s framework is voluntary and will depend on its acceptance by companies to achieve widespread adoption. This was why the Task Force sought such a wide range of input from companies and financial intermediaries, Schapiro explains: “We knew our approach had to be practical and pragmatic for companies, because our goal is to have them adopt it without a regulatory mandate. As a result, business input was critical.”

Pitkethly argues that compulsion would lead to “a proliferation of unhelpful, boilerplate disclosures” and that the voluntary approach is therefore best, although he acknowledges that this requires both “a push and a pull” for information; companies and their stakeholders alike need to understand the benefits of disclosure in promoting better dialogue and more efficient price discovery.

If companies choose not to engage because the framework is voluntary, he says, the solution will again be increased dialogue. The onus will be on stakeholders to ask: “Why do you believe you don’t have material risks in this area?”

The TCFD began a 60-day consultation on its recommendations on 14 December 2016. The consultation period will be followed by a report back to the FSB, and the TCFD Recommendations report will be presented at the G20 Summit in July 2017.

So how will its success be judged? Schapiro believes this will become apparent over the coming year or two in the quantity and quality of disclosures of climate-related financial impacts that start to appear in companies’ public filings. “It will be something that will evolve over time,” she says. “But hopefully not a very long period of time.”
**My wish list**

**Edgar Ernst** currently heads three audit committees and is President of the Berlin-based Financial Reporting Enforcement Panel. He believes that companies in other countries could learn some valuable lessons from the German system of corporate governance.

**GIVE YOUR EMPLOYEES A VOICE**

Germany’s two-tier system, with separate management and supervisory boards, is often underestimated. Non-Germans think it’s complicated and time-consuming, but I’m a big supporter of it.

One of the main advantages is that, classically, German supervisory boards have employee representatives. This means that, even in difficult situations like restructurings, employee representatives are part of the decision-making process from the start. They have a chance to influence companies’ decisions and make sure they are organized in a socially responsible manner.

That’s one of the reasons that hostile, mutinous strikes rarely occur in Germany. Giving employee representatives the chance to shape the company’s strategy means they are held accountable and incentivized to think about its future as a business. I think that’s a good way to get outcomes that both sides feel comfortable with.

**WORK CLOSELY WITH YOUR AUDITORS**

In Germany, the head of the audit committee of the supervisory board hires the external auditors. I’m in this position at three listed companies and I’ve always made sure that auditors understand that I work with them in a close, trusting relationship. They are an invaluable resource if you want to know what’s going on in the different departments of your company.

I expect auditors to get in touch with me if they feel the accounting is too aggressive – if goodwill tests are too loose, the business plan has too many positive assumptions baked in, or write-offs aren’t properly accounted for. If management and auditors disagree on issues like these, they can talk to the audit committee. I don’t want any secret meetings – that would damage the relationship with management – but I think the audit committee should be involved if there are doubts. In the long run, it’s in the best interests of the company and its stakeholders.

**FOCUS ON STRATEGY**

Bad supervisory boards consist of “yes men” who agree with whatever management says. Ideally, both sides have a critical, open and trusting relationship and use meetings as opportunities to bounce ideas off one another – whether about new markets to enter or new businesses to acquire.

Strategy talks are an essential part of the supervisory board’s work and, in my experience, separate meetings to discuss strategy...
are a good way to focus on these issues without short-term distractions such as quarterly reports. I'm aware that this trusting relationship between management and supervisory boards doesn't always exist. In Germany, the supervisory board appoints the management board, which can lead to power struggles. A trusting relationship is something both sides have to work at.

**ENFORCEMENT IS IMPORTANT**

Every year, the Financial Reporting Enforcement Panel (FREP), which I'm the President of, checks the annual reports of around 100 listed German companies on a sample basis.

I like to think our work has made a positive impact on financial reporting in Germany. Our institution was founded in 2005 and has an unusual structure. In most European countries, it's up to the authorities to control the companies' reports, but in Germany we have a two-tier system. There's the FREP and then there's the Federal Financial Advisory Authority (BaFin), which is a government agency. If we find a fundamental mistake in a report, we get in touch with the company and ask it to publish a correction. But if the company disagrees, we hand the case over to the BaFin, which looks at the books again and makes its own assessment.

For me, the advantage of this procedure is that it gives a window into the company from two different angles. Whereas the BaFin deals with a company's books from a legal, administrative perspective, we try to read them like an economist would. Accounting isn't an exact science and there are a wide range of interpretations. That's why it's important to have that second approach, and that's what we provide.

Statistics show that we have made a positive impact. When we started, we found significant mistakes in 25% of the reports we checked; today it's only 13%. Ultimately, our work increases the trust in Germany's capital markets.

**BEING A BOARD MEMBER TAKES COMMITMENT**

In recent years, independent directors and supervisory board members have had to deal with a stream of regulatory changes. Some colleagues complain about that, and it's true that it means more work for everyone. But I also think it's an inevitable part of the professionalization of our job. The days are long gone when it was enough for supervisory board members to show up at a few meetings every year and get paid handsomely just for doing that.

Today, being a board member requires constantly keeping up to date with the company's news and the regulatory environment, preparing for the next meeting or working on new reports. And that's a good thing, because it helps us to do our job.

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**PROFILE**

Since 2011, Edgar Ernst has been President of the Financial Reporting Enforcement Panel (FREP), a government-appointed but privately organized institution in Berlin that controls the accounting practices of listed companies in Germany. Prior to that, he worked for 15 years as CFO on the management board of Deutsche Post DHL and its state-run predecessor, Deutsche Bundespost Postdienst. He currently serves on the supervisory boards of DMG Mori, TUI, Vonovia and Deutsche Postbank and heads the audit committees of the first three companies. Since 2006, he has also been an honorary professor at the Otto Beisheim School of Management in Vallendar, near Koblenz.
In November 2016, the International Accounting Standards Board published its work plan for the next five years. Christian Doherty talks to the board’s Chairman, Hans Hoogervorst, to find out how they intend to keep improving the standards.

Last year was a memorable one for International Accounting Standards Board (IASB) Chairman Hans Hoogervorst. As the public face of the accountancy regulatory community, he spends much of his time persuading countries around the world to adopt International Financial Reporting Standards (IFRS). So far, more than 120 countries have done so.

As he looks back on a tumultuous year for the global economy, Hoogervorst says 2016 represents a pivotal moment in the evolution of the IFRS project. “There is generally a feeling among our constituents that we should give them a chance to fully implement the new standards we’ve created in the last couple of years, and not look at starting on a new set of big changes.”

In November, the IASB issued its new five-year plan, setting out its priorities for the period up to 2021. The main takeaway is the announcement of the end of the era of writing major new standards and a new focus on improving existing standards and guidance. In practice, that means completing work on the final remaining standard
on insurance, as well as refining what has already been agreed as part of the decade-long IFRS project. But Hoogervorst insists there is still a lot of work to be done to improve the effectiveness of financial statements, explaining that the next phase of work will fall under a new theme entitled “Better Communication.”

**CLARIFYING MATERIALITY**
That label covers everything from the format of financial statements to how best to use technology (and what to avoid). Hoogervorst’s view is that, now that the standards are written and agreed, the board must focus on improving how they are understood and applied.

Take materiality, an area where Hoogervorst admits more clarity would be useful. “Materiality is part of the Better Communication program,” he says, “because we believe that a lot of disclosures are being made using checklists that satisfy auditors and regulators, but not necessarily investors or companies themselves.

“So we have set out to clarify the materiality concept and how to use it. By adjusting IAS 1 (the standard that sets out the guidelines for presenting financial statements), we have made it much clearer that if something is not material, not only do you not need to include it in the financial statement – it is actually better not to do so.”

The IASB is also working on a materiality “practice statement” to make it easier for preparers to avoid clutter, streamline their financial statements and enhance the effectiveness of their disclosures. “That’s beneficial both for preparers and for investors,” Hoogervorst notes, adding that work to simplify and streamline financial statements will continue as part of Better Communication.

**THE TECHNICAL CHALLENGE**
The next few years will see the IASB focus on achieving a clearer format for income statements, something that will inevitably involve a more proactive approach to technology. Hoogervorst acknowledges that this may be overdue.

“We do recognize that, given the changing nature of the consumption and dispersion of financial information, we have to adjust as well,” he says, pointing out that developments in technology – not only data mining and analytics, but also the coming wave of cognitive computing and artificial intelligence – make accounting standards even more critical.

“I am not worried about the relevance of the IFRS statements; they continue to be the anchor for most investors,” he says. “But you do see concern about disclosure overload and the voluminous nature of financial statements. You also see concern about the proliferation of non-GAAP measures, and you see that a lot of investors think the financial statements do not depict the financial performance of a company sufficiently clearly.”

To illustrate that concern, Hoogervorst recalls a recent speech he delivered in Washington, DC, on the impact of the new insurance standard, which has given rise to the situation where the same company can give wildly differing financial statements depending on which GAAP it uses. “I said that technology is great, but all the artificial intelligence in the world could not figure that out. So the need for solid accounting standards remains essential.”

**THE INSURANCE STANDARD**
Hoogervorst identifies completing work on the insurance standard as the IASB’s most important task in the short term: an effort that (speaking in December) he expected to intensify in the early months of 2017.

“We are close to the finish line,” he says. “Our staff have already written a draft and refined that further. We made some more last-minute refinements in November, but we are ready to finish and publish the standard in the next few months.”

However, Hoogervorst doesn’t expect the hard work to end there. “I’m not sure if the endorsement of the new standard will happen within a year, and I know that it’s going to be a rough ride, because all insurance companies will have to change their accounting; that often means that you also have to adapt your business model a little bit, so there could be last-minute hiccups. But I am optimistic, because the necessity is so obvious that I cannot imagine that, for example, Europe will say: ‘This is too big a change. Let’s leave it as it is.’”

A similar determination has driven the work behind IFRS 16, the leases standard. While many feel the reforms are overdue, it is a project that has caused consternation in certain quarters, with some observers fearing a raft of unintended consequences. Earlier in 2016, reports suggested the new standard would bring US$2.8t back onto corporate balance sheets.

The accounting advantage of leases will disappear (at least in the sense that companies will no longer be allowed to keep leases off the balance sheet), as will the difference between operating leases and finance leases. However, Hoogervorst insists that the intention of the standard is not to dissuade companies from considering leases as a financing option – far from it.

“I think it will lead companies to make better decisions,” he explains. “I don’t think leasing is going to disappear at all, because leases have the huge advantage of removing the risk of ultimate ownership. And you have a lot more flexibility, although it is usually more expensive than simply buying and financing.

“Whereas in the past, people would perhaps go for the more expensive solution simply because the balance sheets would look a little bit better, that advantage will disappear and they will make better economic decisions,” he continues. “It will not mean a huge shift from leases to buying, but there will definitely be some shift.”
BEYOND THE NUMBERS

Of course, long-term value creation is not entirely confined to financial growth. Nonfinancial measures have gained currency in the past decade as sustainability concerns, risk reporting and scrutiny of corporate governance have risen up the agenda. While some market observers (and preparers) have chosen to cast the issue as an either-or question, Hoogervorst views the integration of nonfinancial measures as a vital part of the bigger picture.

“Nonfinancial information has always been important, and is gaining in importance at the moment, so we do not see that as a problem or as competition,” he says. “In fact, we see that as complementary to the statements and we take a constructive approach.”

However, he does see some challenges ahead for the integrated reporting movement. “At the moment, there is too little streamlining of activity,” he argues. “There is progress, for sure, but there is not the beginning of a single set of global standards and I think it is very hard for preparers to figure out exactly what they need to do.”

Hoogervorst points out that the IASB is a member of the International Integrated Reporting Council (IIRC) and is debating whether it should take a more proactive approach to engaging with it in the future. Its work with the IIRC mirrors other ongoing partnerships and fits squarely with the board’s determination to spread the IFRS message beyond its current constituency.

GLOBAL, NOT LOCAL

However, that expansion into new territories will not involve the development of locally accented standards adapted for individual territories. “We are not supportive of ‘local dialects,’ because they tend to evolve into local languages if you’re not careful,” says Hoogervorst. “It’s not something we would encourage or would turn a blind eye to. For the ideal of a single set of global standards to materialize, everybody has to have some self-discipline and avoid the temptation to make local deviations and adaptations.”

It’s a firm line that belies Hoogervorst’s instincts as a natural conciliator. That collaborative approach, he believes, has informed the IASB’s attitude to the world in which it operates. And despite a year when global institutions and the notion of international cooperation have come under intense pressure, Hoogervorst retains his faith in the value of collaboration, compromise and progress.

“In spite of all the political upheaval, the adoption of IFRS in the rest of the world has continued to grow,” he insists, giving the example of Saudi Arabia, where all listed companies will have to use IFRS for financial periods beginning on or after 1 January 2017. “So it’s still on the increase, despite all the tension in the world and the economic problems.

“I still believe that our product basically sells itself, and most countries see the benefits. By the way,” he adds, “if you adopt IFRS, it’s a voluntary position. You can always pull back if you want; there is absolutely no loss of sovereignty, and that’s why most countries feel very comfortable adopting it.”

Ensuring the smooth progress of the IFRS project is a difficult task; Hoogervorst acknowledges that further challenges await and sees each incremental step as a cause for celebration. “It’s not that easy, but generally the mood in the world is still very receptive,” he reflects. “I hope that our accounting constituents don’t get infected by all the tension in the world and the retreat from globalization, and that we can continue with our good work.”

PROFILE

Hans Hoogervorst has been Chairman of the IASB since 2011 and says he intends to fulfill his second five-year term, which ends in 2021. Before joining the IASB, he held a series of senior positions in the Government of the Netherlands, including that of Minister of Finance. His career as a regulator gathered pace when he took over as Chairman of the executive board of the Netherlands Authority for the Financial Markets (AFM), following a stint as Chairman of the Technical Committee of the International Organization of Securities Commissions. Those roles came about as a result of his success as Co-Chair of the Financial Crisis Advisory Group, a high-level group of business leaders with experience of international markets, set up to advise the IASB and the FASB on their joint response to the financial crisis.
In a global economy where organic growth is increasingly rare, M&A activity continues to be a significant factor. Indeed, despite political and economic uncertainty, EY’s 15th Global Capital Confidence Barometer reveals that 2016 was one of the best years ever for dealmaking. While the deal value globally – US$3.5t – was down 17% compared with 2015, that was a record year; overall, 2016 was up 9% against 2014. Significantly, 37% of that deal value was made up of cross-border acquisitions; Chinese buyers alone were responsible for deals totaling US$210b. In short, while M&A may not be the only game in town, it’s arguably the biggest.

For most CFOs, acquisitions present both an opportunity and a challenge: the opportunity to add value to their company by buying new businesses, and the challenge of finding the right target, getting the deal done and making sure the acquisition delivers the intended benefits. Acquisitions are as much an art as a science and require a range of skills from the CFO, including diplomacy, persistence, strategic vision and leadership.

STRATEGY COUNTS

Mark Okerstrom (pictured on page 2, top left) has more experience than most when it comes to acquiring companies. As CFO and Executive Vice President, Operations of US travel company Expedia, Inc., he has overseen more than US$8b of acquisitions and divestitures, and he emphasizes
that every deal is underpinned by a clear alignment with corporate strategy.

“We examine 50–100 possible transactions a year,” he says. “Every year, we take a close look at where we want this company to be in the next three to five years. We look at our organic prospects and the trajectories that all of our businesses are on and we see gaps – places where we want to either fill in white space in our existing portfolio, or we want to accelerate some of our capabilities or growth prospects. We fill those gaps with M&A.”

Naturally, there isn’t a one-size-fits-all model. “Every deal is different,” says Okerstrom, who explains that he has learned to address each potential acquisition on its own merits.

“If you take a deal like trivago (in which Expedia acquired a majority stake in the German hotel search company for US$570m in 2013), the thesis was: this is a great company which has phenomenal growth prospects. Yes, our global scale and our presence in the US – a market they wanted to enter – was helpful, but really the base thesis was that we had the opportunity to create a huge amount of shareholder value.”

Okerstrom contrasts that with the more recent acquisition of global online travel company Orbitz for US$1.3b. “There, we had a very clear deal thesis around the ability to realize significant cost synergies, at the same time as actually making the consumer product better and therefore driving revenue synergies. In that respect, it’s the complete opposite of trivago. With Orbitz, it was all about leveraging the Expedia platforms to create the value.”

THE ACID TEST

Reeza Isaacs (pictured right) is the CFO of South African retailer Woolworths, a role that has seen him handle a number of acquisitions, most recently that of Australian clothing brand David Jones for approximately US$2b. For Isaacs and his team, once the process of identifying a suitable target has been completed, the spotlight falls on interrogating the rationale behind the deal. “I would typically ask: does the acquisition bring with it, for example, substantial EBITDA? Is it immediately earnings-or value-accretive to shareholders?” he says.

In the Woolworths model, once the basic assumptions have been ratified, the CFO’s role focuses on asking some key questions, as Isaacs explains: “What is the strategic rationale, and how can we as a group leverage our scale, either in terms of product or support services or other expertise, that would generate additional value for the group and for shareholders?”

Answering those questions can be especially tricky when it comes to acquiring overseas companies. Isaacs has (like Okerstrom) been a key player in finding and completing deals with foreign targets. Woolworths has been involved in two Australian acquisitions since Isaacs became CFO and he says that, while the due diligence process is broadly similar, some different arrangements are required in terms of financing.

“We take a view that if we acquire in a particular jurisdiction, then we match the cash flows in that jurisdiction to the financing requirements in the country,” he explains. “We ensure that we aren’t exposed from a forex fluctuation perspective; obviously, we are exposed from a pure currency translation point of view from earnings, but from a cash flow point of view, we don’t hedge.”

Yi Sun is Leader, EY Greater China Business Services in Germany, Switzerland and Austria. She echoes Isaacs’ point about the need for the CFO to address and reduce complexity in cross-border acquisitions.

“Normally there are five different work streams: financial, tax, legal, environment and commercial,” she says. “The CFO should work closely with the rest of the

“Exposing yourself to different approaches and management styles broadens your horizons.”

Mark Okerstrom, Expedia
INTEGRATION INSPIRATION
Of course, Wang recognizes that achieving synergies — and the attendant long-term shareholder value — will largely depend on how well the acquirer integrates the target into the group. Neglecting the integration phase is a mistake many businesses have made, as Okerstrom points out.

“If one piece of the deal thesis involves benefits around integration, then you’d better be sure that you get your integration team involved in vetting the assumptions you’re making,” he says. “That way, when you close the deal, they can hit the ground running.”

Recent research from Harvard Business Review revealed that between 70% and 90% of mergers fail to realize the declared benefits post-deal. These sobering statistics support Okerstrom’s reflection that the worst deals are those that are either ill-conceived from the start, or, even worse, ill-conceived and then handed off to a team that has not been involved in the transaction. “When the CFO simply says, ‘Here, integrate this,’ it’ll end up being a difficult transaction,” he says.

That is especially true of cross-border acquisitions, where cultural differences can delay or even derail a successful integration. “Culture is a factor that has to be considered, especially when it involves the different habits and ways of those people involved in the business,” says Sun.

“Trust, respect and open communication will make everything happen.”

Yi Sun, EY

MAKING SYNERGY COUNT
As a veteran of numerous acquisitions, Robin Wang (pictured above), VP and CFO of Fosun Group, a Shanghai-based investment group, has become an expert in identifying and tracking synergies — often the stimulus for an acquisition, but notoriously difficult to measure, let alone achieve.

Acquisitions are central to Wang’s role at Fosun Group, and Fosun Pharma recently completed a US$1.2b deal to buy Gland Pharma in India. In that acquisition, as in others, identifying and achieving synergies was a key driver.

“Before we decide to go forward with a deal, we have to discuss synergy, and we look for that across a range of areas: innovation, technology, data exchange, collaboration and so on,” Wang explains. “Then we look at KPIs for the investment managers, so once the deal is done, we can monitor the synergies that are being created.”

Under Wang’s guidance, Fosun has introduced a detailed mechanism for monitoring and improving the synergy performance of every acquisition. While not every deal is a synergy play, “for the big deals, we’re always focused on them,” Wang says. “We’re trying to create an ecosystem rather than a conglomerate. That’s why synergy targets are important.”

THE MORNING AFTER
As Isaacs points out, whatever euphoria may accompany the successful completion of a deal, “at the end of the day, the executive is accountable to the board and shareholders for delivering on the plan. Once your advisers, banks and lawyers move off, the hard part begins. Despite all the due diligence you’ve done, there will be surprises that pop out.”

Given all that, discipline is key in the immediate aftermath of deal completion; the discipline to stick by the guiding principles that led to the deal in the first place and the discipline to remain focused on its success.
So, to achieve the best possible outcome, Woolworths insists on the formation of what Isaacs calls a “group transformation management unit” in order to bring governance to integration. “This body effectively manages all aspects of integration and synergies,” he explains. “We typically track that on a monthly basis and we then report to the board on synergy tracking every quarter.”

**SUCCESSFUL PARTNERSHIPS**

Wang has played a critical part in Fosun Group’s M&A-led growth strategy and has successfully compiled a balanced and diverse portfolio, from growing health care businesses in India to soccer clubs in the UK, famous resorts in France and Israeli cosmetics firms. Much of his role involves assessing the merits of his CFO counterparts at the target company to see whether their outlook and skill set will fit well with Fosun’s culture.

“I’m not a traditional CFO myself – I used to work for local government and a large accountancy firm,” he explains. “So I’m looking to work with different types of CFO. And we have so many different companies, we try to move away from simply stocking them with CFOs with the same skill sets. They might have business backgrounds rather than purely accounting or finance backgrounds, for instance.”

From Wang’s perspective, the most important thing to look at is the ability, and specifically the entrepreneurship, of the management team of the target. “That’s critical,” he says. “On every project, before we decide to buy or sell, our board members will meet the management team. I like to spend time talking to the CFO and CIO, and you have to rely on your sense of those people sometimes.”

Despite all the pressure of completing a deal and overseeing its successful integration, there are some personal benefits that may accrue for the CFO. Okerstrom certainly feels that working extensively on M&A has made him a better leader.

“Apart from the due diligence process and taking a critical look at other businesses, exposing yourself to different approaches and management styles broadens your horizons,” he reflects. “It sets what you’re doing within a broader context and allows you to get an assessment of your business from almost a higher plane, because you’re doing it with the benefit of the knowledge of what else is happening in the industry. Ultimately, I think it makes you a better CFO.”

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**Lessons learned**

**Reeza Isaacs:** “I am very conscious of staying objective and avoiding getting ‘deal fever.’ It’s easy to get excited at various points in the process, but your role is to be the voice of reason. I would also say question, question, question and stay level-headed. Everyone around you could be losing their heads, so you’ve got to stay calm.”

**Robin Wang:** “If you really want to influence your company, you have to be a finance expert first. But then you have to come up with solutions – make a positive contribution, rather than simply pointing out the flaws of a deal.”

**Mark Okerstrom:** “The crucial thing for the CFO is having a good handle on what’s important to you and having the ability to say no. We’ve said no to a lot of things and I have very few regrets about deals we passed on. As a result, we have very few regrets about the deals we have done.”
Fast-forwarding finance

EY’s Peter Wöllmert discusses the findings from the organization’s global survey of finance leaders, and explains how innovative technologies and modernized operating models can deliver a new age of responsive reporting.

In today’s fast-moving world of corporate reporting, speed of reaction is everything. Not only is the volume of data increasing, but also the velocity. Reporting teams are expected to deliver – to tight deadlines – data-driven, forward-looking insight, of the highest quality and accuracy.

For many organizations, agility and speed of reporting response are a challenge. Fragmented technology makes it hard to collect and analyze large data sets, while cumbersome reporting processes result in slow reaction times.

The impact of fast-changing technology is emphasized in EY’s research, How can reporting catch up with an accelerating world?, which collected the views of 1,000 CFOs or financial controllers of large organizations. When we asked respondents to describe the major external challenges to corporate reporting, they identified “changes to technology” as the number one issue faced.

Thirty percent of respondents suggested that technological change was a concern, compared with 25% who identified market developments, 23% who mentioned regulatory issues and 23% who highlighted the need to satisfy national and international guidance and standards.

Reporting teams are no longer just seen as the stewards of reporting data – they are expected to analyze detailed information and extract insight from large, fast-changing and wide-ranging data sets. At the same time, finance staff must protect and secure that data, as the regulatory and reputational cost of a breach is a significant risk.

Finance leaders face an increasingly complex environment, and they need to prepare themselves for what the future holds. All firms are struggling with increasing automation, the advent of smart, connected devices and the need to use new technologies and harmonize systems. CFOs must get better prepared for Industry 4.0 and the disruption this involves.

When we look at the specific challenges that organizations face, we find teams struggling with IT systems that do not talk to each other, a lack of automation and a proliferation of technologies. Partly, this is due to increased reporting requirements, as firms introduce manual work-arounds to deal with the latest regulatory demands.

Upgrading IT and financial data analytics tools is the standout priority in corporate reporting, according to our survey. This was identified as a factor by 41% of respondents, outweighing the need to drive further efficiencies (33%) and the requirement to meet increasing demands for smarter and faster information (31%).

The importance placed on systems and data tools is reflected in investment intentions, with 84% of organizations worldwide expected to increase expenditure in reporting technologies over the next two years. Agile technologies will be a focus area. The cloud, in particular, allows organizations to respond more quickly and smartly to technology requirements and changing business needs. But...
there are also intelligent data capturing, artificial intelligence and blockchain to consider.

As traditional reporting back-office tasks are automated, the need for large numbers of full-time employees in these roles will disappear. Robots will be increasingly used in the next generation of reporting back offices, allowing reporting professionals to focus on other tasks, such as providing predictive analytics and managing stakeholder relationships.

Reporting leaders have to find people with the skills capable of mastering the new technologies that are driving reporting innovation. But, as our survey shows, technology- and data-related skills are at a premium. IT infrastructure skills is the most in-demand requirement (36%), followed by financial data analytics (33%) and business analysis (27%).

To address this issue, leaders must take a strategic look at the talent they need to drive reporting agility and extract value from technology. This means striking a balance between bringing in fresh blood from outside and developing existing team members.

Finance leaders also have a wider opportunity to examine how reporting is delivered. CFOs have been transforming the finance function’s operating model for many years through arrangements such as shared services and outsourcing for transactional processes. Today, however, organizations are looking to increase the functional scope of these arrangements by including corporate reporting.

Over the next two years, for example, 55% of finance leaders around the world intend to make a significant or very significant increase in outsourcing to support reporting. Group CFOs are particularly bullish and expect to see more outsourcing (67%), managed services (63%), shared service centers based onshore or nearshore (61%), and centralized centers of excellence (58%).

Operating model transformation provides an opportunity to eliminate redundant processes, streamline critical tasks, achieve global consistency and automate more activities. It should create a more agile and flexible reporting function.

It is clear that corporate reporting will look very different in the future. It will be smarter, highly automated, more streamlined and increasingly forward-looking. By focusing on innovative technologies and a more flexible and nimble operating model, CFOs can design and deliver the responsive reporting capability required for a world that will continue to accelerate.
Richard Howitt, the new CEO of the International Integrated Reporting Council (IIRC), may be based in a bright, airy London office, but he is expecting to travel – a lot. His predecessor, Paul Druckman, spent up to 60% of his time traveling and Howitt anticipates that his schedule will be equally busy. In fact, he will have visited several European countries, as well as Brazil, India, Malaysia, Singapore and the US, by the end of his first six months.

“I want to send a strong message that this is a global movement and that the IIRC is relentlessly international in its approach,” Howitt explains.

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“I want to send a strong message that this is a global movement and that the IIRC is relentlessly international in its approach,” Howitt explains.

“I’m used to working with different countries, languages and legal systems, so I’m going to bring all that knowledge and commitment to the way I work here at the IIRC.”

The “movement” Howitt is referring to is integrated reporting (IR), a forward-looking approach to corporate reporting whereby companies focus on how they are creating real value for their stakeholders over the short, medium and long term instead of treating reporting as a short-term compliance exercise – which is how many businesses view corporate reporting today.
With IR, organizations explain how they interact with six “capitals”, i.e., financial, manufactured, intellectual, human, social and relationship, and natural (see panel, p4). So, as well as reporting on financial information, such as return on equity and earnings per share, they may also disclose information on a wide range of other areas that are relevant to their business, such as customer satisfaction, investment in equipment, technology patents, employee engagement, female representation in senior positions, partnerships with external organizations and carbon dioxide (CO₂) emissions.

At the heart of the concept is the belief that reporting in an integrated way will counteract the short-termism among businesses, investors and the capital markets that provoked the damaging financial crisis of 2008-09.

CHANGING REPORTING FOR THE BETTER

“The roots of the financial crisis lay in a lack of integrated thinking, a failure to think in the long term,” Howitt argues. “Those who got into trouble thought they could reap all the benefits and simply pass the risk on to someone else. They didn’t analyze how that risk might come back to haunt them and they didn’t think outside the narrow confines of their short-term, quarterly financial business model.”

In the immediate aftermath of the crisis, he continues, “we were trapped in narrow short-termism that blotted out the necessary debates about the long term,” as politicians and regulators enacted a flood of new regulations designed to increase transparency quickly.

Over the past few years, the debate has started to center on the long term again — something the IIRC has helped to promote through its involvement with initiatives that promote long-term investment strategies, such as Focusing Capital on the Long Term and the Coalition for Inclusive Capitalism.

A POLITICAL PEDIGREE

The IIRC itself is a coalition of businesses, investors, nongovernment organizations, accountancy bodies, regulators and standard setters. Howitt officially began working for the organization in November 2016, but his involvement with it stretches back to 2010, the year the IIRC was founded. At the time, he was the Labour Member of the European Parliament (MEP) for the East of England, having been first elected in 1994, and the European Parliament’s rapporteur on corporate social responsibility (the person tasked with reporting back to the main Parliament on what was being done in that area). He had also connected with individuals trying to effect change in corporate reporting through his work as an ambassador for HRH The Prince of Wales’s Accounting for Sustainability Project, which was launched in 2004 to help embed sustainability within organizations.

“I already knew Paul Druckman, who became the IIRC’s first Chief Executive,” Howitt recalls. “He was the Chair of the Sustainability Committee of the Federation of European Accountants and we had traveled on the Eurostar together many times and discussed the case for integrated reporting.”

At Druckman’s request, Howitt agreed to become a voluntary ambassador for the IIRC. He attended meetings with the companies that piloted the first integrated reports and represented the IIRC at several international meetings. In 2013, he was at the London launch of the International Integrated Reporting Framework — part of an event that took place in 13 time zones within a 24-hour period.

In his day job as an MEP, Howitt also played a lead role in shaping the 2014 EU Non-Financial Reporting Directive, which came into force on 1 January 2017 and requires large companies to report on the social, environmental and human rights impact of their activities.

“If I die today, they can put the directive on my gravestone because I’m so proud of it,” says Howitt with a broad smile. “I proposed it, I helped negotiate it and I talked a lot with Paul about it. I believe it is a very important stepping stone toward integrated reporting. It’s aimed at large companies alone, many of which welcome it, and it’s not about burden. It’s about taking existing frameworks and applying them more efficiently.”

As a close confidante of Druckman and a supporter of the IIRC, Howitt admits that he was
RICHARD HOWITT: CV IN BRIEF

- Graduates from the University of Oxford in the UK with a degree in politics, philosophy and economics in 1982.
- After university, works as a coordinator for the Harlow Council for Voluntary Service for four years and for the Waltham Forest Disability Resource Centre for eight years.
- From 1983 until 1995, serves as a Labour councillor on Harlow District Council in Essex, acting as leader of the council for three years.
- Is elected as an MEP in 1994, first serving the Essex South constituency and then the East of England. He serves as rapporteur on corporate reporting-related issues, including social responsibility, and is an architect of the 2014 EU Non-Financial Reporting Directive.
- As lead MEP on corporate responsibility, represents the EU on many missions worldwide, traveling extensively in Asia, Africa and the Americas. Also represents European interests in numerous international initiatives, including the UN Business and Human Rights Forum on Responsible Business Conduct.
- Alongside his work as an MEP, acts as a voluntary IIRC Ambassador, promoting integrated reporting within the policy and business communities.
- In September 2016, announces his resignation from the European Parliament to become Chief Executive of the IIRC.
At the heart of the IR framework is the concept of the six capitals that a business uses to create value over time. Reporting on these capitals provides greater context for performance data and may help businesses make decisions for the long term.

The capitals are:

- **Financial capital** – the pool of funds that is:
  - available to an organization for use in the production of goods or the provision of services
  - obtained through financing, such as debt, equity or grants, or generated through operations or investments

- **Manufactured capital** – manufactured physical objects (as distinct from natural ones) that are available to an organization for use in the production of goods or the provision of services

- **Intellectual capital** – organizational, knowledge-based intangibles, including:
  - intellectual property, such as patents, copyrights, software, rights and licenses
  - “organizational capital”, such as tacit knowledge, systems, procedures and protocols

- **Human capital** – people’s competencies, capabilities and experience, and their motivations to innovate

- **Social and relationship capital** – the institutions and the relationships within and between communities, groups of stakeholders and other networks, and the ability to share information to enhance individual and collective well-being

- **Natural capital** – all renewable and nonrenewable environmental resources and processes that provide goods or services that support the past, current or future prosperity of an organization

And financial market actors know who I am and hear the energy, drive and enthusiasm from me directly,” he says.

While Howitt does not believe there is a single main barrier to the global adoption of IR, he does point out that there are “conflicting pressures in the world of business. We have to get enough space and visibility to make sure people really address the issue,” he says. “So, we have to demonstrate the growing body of evidence, which now exists, that this is financially beneficial to businesses in the long term. There is a strong business case for this. We need that case to be read, understood and
believed by key opinion-formers in business and in capital markets. We also want more regulatory endorsement.”

Another issue is potential confusion within the market as a result of similar initiatives, such as the EU’s Non-Financial Reporting Directive and the Task Force on Climate-related Financial Disclosures set up by the Financial Stability Board (FSB), which announced its recommendations in December 2016. These call for organizations to make disclosures around the climate-related risks and opportunities their businesses face, as well as their processes for identifying, assessing and managing such risks.

The IIRC was consulted on the recommendations and Howitt describes the FSB Task Force as critically important – “not because it’s about a different methodology, but because it’s getting the world to talk, at the highest level, under a G20 framework, about material risk to the financial markets. Many of us, as individual citizens, are worried about climate change for ourselves, our children and our grandchildren, and many of us want the world to be more sustainable.”

“Half of the benefit of integrated reporting is integrated thinking.”

LASTING LEGACY

Howitt’s passion for IR is clearly deep-seated and genuine. It is also consistent with his personal values, which have held firm since his pre-politics days when he worked in the charity sector, first with a community organization and later with the Waltham Forest Disability Resource Centre in east London. “If you change your role, you don’t change your beliefs,” he says. “I will always care about how disabled people are treated.”

It was during his time with the disability charity that he began to work with organizations in other countries, an experience that led to his career in international politics. “It instilled in me the benefits of international cooperation, exchange, learning and working across boundaries,” he says. “The way we are going to create a better world is by cooperation and working together, whether that’s in Europe or internationally.”

Howitt says his ultimate goal is to leave the IIRC “knowing that integrated reporting is the global norm,” and there’s no reason to doubt his commitment to his objective. “I’ve never taken up a cause or an idea without believing in it,” he says. “This is not a game of politics. What we are doing here is deeply serious.”
Vibrant Vietnam

Vietnam has one of the world’s fastest-growing economies and is working hard to encourage foreign investment. The next stage, as Tim Cooper discovers, is to make progress on vocational skills, corporate governance and IFRS adoption.

It is now 30 years since political and economic reforms started opening Vietnam’s economy to the rest of the world, a process that accelerated when it joined the World Trade Organization in 2007. During that time, Vietnam’s economy has gradually shifted focus from agriculture to industry and services, and international exports continue to grow.

As a result, Vietnam has experienced some of the fastest economic growth in the world in recent years, and this is set to continue. It posted 6.7% growth in 2015 and is forecast to sustain 6.1% until 2025, according to BMI Research.

Meanwhile, privatization of state-owned enterprises has opened new doors for foreign investors. Between 1988 and 1990, there were only around 200 foreign direct investment (FDI) projects in Vietnam, with a total value of US$1.6b. In 2015, total FDI was worth US$11.8b (according to figures from the World Bank) and investors came from more than 100 countries.

The Government that came to power at the beginning of 2016 has also worked hard to attract more investment through initiatives such as reducing enterprise tax and removing investment restrictions. One of its first initiatives was to remove many of the barriers around sublicensing to enterprises, and this was well received by the business community.

There are still some industry-specific restrictions on the amount foreign investors can hold in local companies, including in finance, retail, publishing and health care. Others, such as pharmaceuticals and manufacturing, are more open. But 100% foreign-owned companies are free to set up in Vietnam and many multinationals now have offices there.

RAPID DEVELOPMENT

According to a report by market research company Euromonitor International, Vietnam’s rapid development in recent years has been due to rising industrial output, robust exports, growing domestic demand and strong foreign investment.

The agricultural, manufacturing and services sectors are all major contributors to the economy.
Vietnam is well placed to compete with other emerging economies in the region.

Dr. Thai Lai Pham, Siemens Vietnam

opened an office there in 1993. Since then, it has increased staff numbers from 10 to 300. Dr. Thai Lai Pham, President and CEO, Siemens Vietnam, says the company has developed a significant presence in many sectors, including power-plant supply, electrical infrastructure, health care imaging devices and industrial automation. This has helped it grow in Vietnam by an average of 25% over the last four years.

Dr. Lai says Siemens regards Vietnam as strategically important, as it is one of only nine “second wave” global emerging economies that the company has identified – the first wave being Brazil, Russia, India and China. “Demand is very strong in areas we cover, such as energy, automation, transportation and health care,” he says. “Vietnam is well placed to compete with other emerging economies in the region, and infrastructure will be key to growth.”

DEPENDENT ON TRADE

However, several challenges remain. Euromonitor says Vietnam’s dependence on trade and foreign investment leaves it vulnerable to global economic uncertainty. Subdued demand in its major trading partners and interest rate rises in the US could lead to capital outflows.

Moreover, the Vietnamese economy was expected to be one of the biggest beneficiaries of the Trans-Pacific Partnership Agreement (TPPA) signed in February 2016. Since then, US President Donald Trump has created uncertainty around the trade deal by withdrawing the US from it. However, even if TPPA now fails, Vietnam could make separate arrangements with other countries and with the US.

Vietnam’s high dependence on imports from Asia-Pacific, especially China, also leaves it

Viewpoint

Work in progress

Tran Dinh Cuong, Country Managing Partner, Ernst & Young Vietnam Ltd

Vietnam has made significant progress toward international standards of best practice in corporate governance, as recommended by organizations such as the International Finance Corporation and the Asian Development Bank.

In the public sector, governance principles and rules are promoted widely and have recently been enforced by government decrees. This is enhancing transparency in capital investment and in corporate performance assessment.

The Government is also now working on a legal framework to ensure the successful implementation of public-private partnerships to help mobilize capital into infrastructure projects.

In the private sector, the revised enterprise law has also created a foundation for transparency and internal control frameworks.

Risk management is a big issue, as several enterprises have failed recently. But standards have improved in the past few years, led by the Vietnamese State Securities Commission (SSC), the body that oversees stock market operations. It has raised awareness and developed risk management regulations and guidance for stock market participants. There have also been a series of enforcement decrees in this area.

Implementation and execution of the SSC standards are not yet consistent, but they are nonetheless making Vietnam a much healthier market for investment.

Most Vietnamese Accounting Standards (VAS) have reached a level of compatibility with IFRS already, especially in certain industries, such as manufacturing. However, in others, such as finance and insurance, there is a noticeable gap and some integration work is still necessary on concepts such as fair value, impairment and financial instruments.

IFRS integration is slow because of a lack of accounting talent with exposure to IFRS in Vietnam. The Government is leading a bid to boost training in enterprises to address this. Also, several international professional associations and professional organizations such as EY will help provide the necessary training.

If Vietnam continues to reinforce regulations that ensure fair competition and transparency, its attractiveness to investors will keep growing.
Vulnerable. Furthermore, the Euromonitor report says that Vietnam's labor productivity has been lower than that of its regional peers and that it has a shortage of vocational skills.

Dr. Lai agrees that the country has insufficient higher education and vocational education providers. He is more positive about the workforce, though. For Siemens, Vietnam is an attractive manufacturing location, with a young workforce and reasonable labor costs. Its people receive a good basic education and literacy levels are good, he adds. “Vietnam has great potential because its people are very open-minded, creative and positive-thinking,” he says. “They are ready to learn and want to achieve something. It has a great future.”

SLOW IFRS ADOPTION
Globally, 149 countries, including many developing nations, have so far allowed or required the application of IFRS for all or most domestic entities. But Vietnam is still relying on Vietnamese Accounting Standards (VAS), which differ from IFRS in several ways. IFRS adoption is going ahead via a stepped program and Vietnamese standard setters now aim to have 30 key entities adopt IFRS initially. Others will then follow, with all listed companies adopting between 10 and 20 IFRS standards by 2020. The target is to achieve full adoption by 2025.

The Government acted to help smooth the transition in 2015 by changing the accounting laws to reduce the gap between VAS and IFRS. Dr. Duc Phan, Accounting Lecturer at RMIT University in Melbourne, Australia, explains that the biggest change is that the new law introduces the concept of fair value and allows the Ministry of Finance to decide which items can be re-evaluated under fair value. Previously, assets and liabilities were defined according to historical costs.

The challenge, says Dr. Duc, is that measuring fair value is outside the experience of most Vietnamese accounting professionals. “As they start to apply fair value, Vietnamese businesses are therefore advised to engage with relevant specialists, including foreign investors, banks, IFRS consultants and shareholders,” she adds. “This will also help them plan carefully for a smooth conversion to full IFRS.”

She continues: “Vietnam has been so slow to adopt due to the nature of its society and economy. In developing countries like this, international accounting firms, multinational enterprises and academics will play a key role in disseminating international accounting techniques. Nonetheless, IFRS adoption is inevitable due to demands from the World Bank, the International Finance Corporation and foreign investors, among others.”

In the meantime, the slow pace of adoption continues to be an obstacle to foreign investment in Vietnam. But at least the transition is well under way, as evidenced by a series of IFRS workshops held in October 2016 at the Ho Chi Minh and Hanoi stock exchanges, says Dr. Duc.

Siemens’ Dr. Lai adds that bureaucracy is burdensome and regulation can be unclear and unpredictable. “That can cost us time and money and can make us less competitive compared to providers in other countries,” he says.

“Also, many local companies are only beginning to develop their corporate governance structures. There is still a big deficit between the governance they have now and what they need to attract foreign investment. They realize they need to do something, but it is still too slow. The Government needs to help it speed up.”

He concludes: “To achieve anything in Vietnam, you need a long-term perspective. You might be disappointed if you expect returns in two years. We often plan our projects over 10.”
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By Sally Percy (Bloomsbury, February 2017)
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