PRIVATE SECTOR TRANSPARENCY AND POST 2015

Mandatory corporate reporting of non-financial performance: a potential indicator of the private sector's contribution to a post-2015 framework

Save the Children recently published its proposed outline for the post-2015 replacement of the Millennium Development Goals (MDGs). This proposal *Ending Poverty in our Generation* focused on human development outcomes and 'finishing the job' of the existing framework, while incorporating environmental sustainability. In addition, it looked at key gaps in the MDGs, such as inequality, and proposed ways of addressing these.

One of the gaps to be closed in the new framework is to provide a way to harness more effectively the power of the private sector. The private sector is a key driver of development – creating jobs, innovating, providing products that meet development needs and paying taxes. Business activities obviously impact children, adults and the environment in many ways, so it is important that they are clearly understood and the consequences shaped so they are as positive as possible. Through dialogue with corporations and other stakeholders, Save the Children is exploring the role of business in

developing and advancing potential post-2015 development goals. Future papers will focus on harnessing the power of business strategies to contribute to these development goals. This paper aims to stimulate debate on the accountability of the private sector and focuses more narrowly on steps to enhance the transparency of large businesses, which provide key information that companies and other stakeholders need to assess and measure business impacts on children – positive and negative. To increase accountability for these impacts, establishing a robust transparency mechanism should be considered by the United Nations High Level Panel to enable and ensure businesses disclose social, environmental and governance information.

Save the Children has proposed a set of indicative targets and potential indicators for the panel's consideration (see below) relating to the following suggested goal: 'By 2030 governance will be more open, accountable and inclusive.'

Indicative target	**Potential indicators**
Ensure all countries have transparent governance, with open budgeting, freedom of information and holistic corporate reporting.	1a. Increase in Open Budget Index score (transparency and participation in public budgeting). 1b. Existence of Freedom of Information (FOI) Act. 1c. Existence of legislation on corporate reporting that requires companies to report on their social and environmental impact, including human rights impact and tax paid. [1]

Save the Children's vision for a post-2015 framework, *Ending Poverty in our Generation*, identifies a clear set of goals to be considered in shaping a new socially inclusive, economically transformational and environmentally sustainable human development agenda that champions children's rights. Along with business strategies that are aligned with the new development goals, the responsible business practices that are enabled by corporate transparency are also essential to creating a world where children, families, communities, and businesses can thrive – and a precursor to establishing the partnerships that will help achieve these goals.

The evidence we present suggests that disclosure of non-financial performance data improves financial and reputational performance, encourages investment in responsible companies and builds a trusted relationship with consumers. This briefing explains how mandatory reporting of non-financial

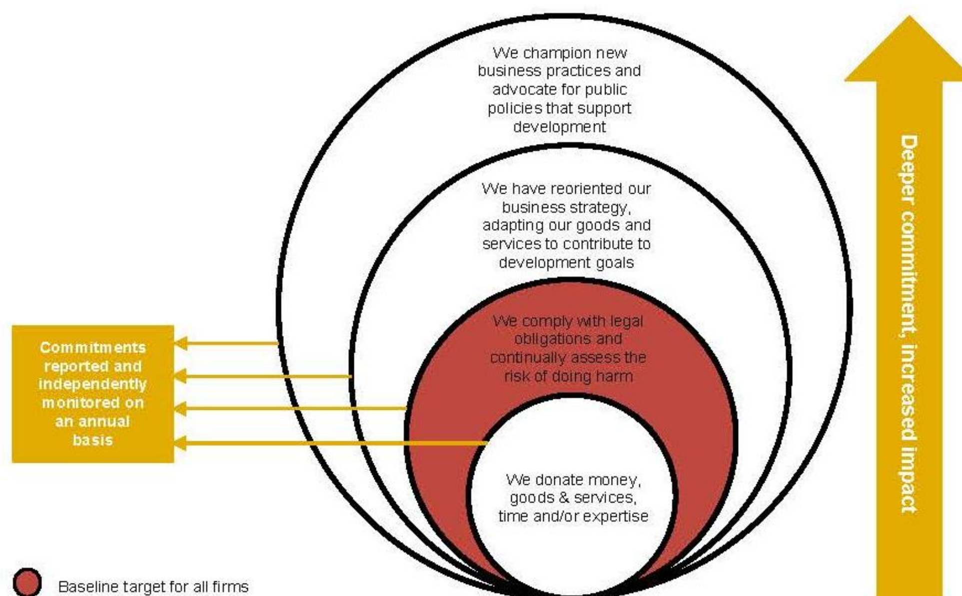
performance for all large companies[2] can help mitigate any negative social, environmental and political impacts of businesses, build trust and increase accountability.

The private sector, which comprises a huge variety of domestic and multinational businesses, has an invaluable contribution to make to the delivery of the next human development framework in a wide range of ways, including: stimulating inclusive growth and creating decent jobs; enhancing access to essential services; developing innovations to address human and sustainable development challenges; paying fair taxes; applying its expertise and resources to improve the lives of those most in need; and reducing its environmental footprint.

The potential impact of private sector investment in developing countries is increasing dramatically, and dwarfs in volume all other forms of economic engagement with developing countries. The rise in inward foreign direct investment to developing countries is clear (US$3.8bn in 1970 to US$684bn in 2011).[3] The fact that foreign direct investment accounts for approximately 10% of total investment (gross fixed capital formation) in middle and low income countries over the last decade[4] indicates the significance of domestic private sector investment in these countries – something that has often been overlooked in discussions on the role of business in development. Given this potential, and the growing impact of business on the delivery of development objectives, the engagement of the private sector in the conception and implementation of the post-2015 framework is critical to its success.

In November 2012, Save the Children published a three-point plan for business engagement in the post-2015 framework. This included:

1) Measures to ensure all firms apply a 'do no harm' approach to their core business.
2) Shaping core business strategies to contribute to development goals.
3) Advocating for change at the national and global level.



Ultimately, the most transformative impact would come from businesses aligning their financial targets with the development of products, services and value chain practices that contribute to poverty reduction, human well-being and environmental sustainability.

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Some leaders in the private sector are embracing this approach, and hopefully more will join them. However, given the relatively small number of companies at this end of the spectrum, one of the most significant contributions business leaders can make at this moment may be to ensure that all businesses fully engage in, support and realise a 'do no harm' approach. Such an approach is not a minor ask. It requires all companies to analyse and report on their direct and indirect impacts. It means analysing the potential harm that products, practices, suppliers and their day-to-day business may do. It means they must adhere to legislation, but much more than that, it includes adhering to international human rights standards, respecting international labour and safety conventions, paying taxes appropriately, and assessing and addressing environmental impact.

Corporate reporting is important for the accountability of businesses for their impacts on children. The General Comment by the UN Committee on the Rights of the Child regarding Child Rights and the Business Sector makes it clear that the potentially harmful effects on children of some companies' activities need to be considered, stating that "business enterprises can also negatively impact children's rights."[5] The Child Rights and Business Principles,[6] developed jointly by Save the Children, UNICEF and the UN Global Compact is one approach to shaping these impacts. Adapted to other global frameworks such as the work of the Global Reporting Initiative (GRI) and the Organisation for Economic Co-operation and Development (OECD), this mechanism helps a business respect and support children's rights. UNICEF has stated that "public reporting will be one way in which stakeholders can and will hold companies accountable for implementing the Principles. In most cases companies will be expected to integrate children's rights into existing sustainability reporting."[7]

Only by capturing and measuring such non-financial information can companies hope to control these impacts and build sustainable business models – through mechanisms such as the Children's Rights Business Principles[8] – and implement the concept of 'shared value'.

While some companies have already recognised these benefits, the current system for corporate reporting of environmental, social and governance (ESG) impacts is fragmented.[9] There are too many voluntary – and in some cases regulatory – mechanisms, meaning that the inconsistency in what is reported by companies is matched by an inconsistency in who is reporting. Although different mechanisms often apply to different sectors or groupings of companies, such differentiation can obstruct accurate comparisons of companies' performance, limiting the value of this information to investors and blocking the market incentive for a significant number of companies to adopt non-financial reporting. The High Level Panel could address this issue by recommending that national governments mandate who reports, giving clear guidelines on what should be reported.

The High Level Panel on the post-2015 development framework should consider recommending that national governments introduce mandatory reporting for all large companies of their non-financial performance, accompanied by a robust set of guidelines and performance indicators as baseline reporting requirements. While national governments will still develop their own guidelines, they could ensure alignment by using the Global Reporting Initiative Guidelines as their starting point.

While Save the Children sees the possibility of mandatory reporting as an important potential indicator for the private sector's contribution to development and the protection of children's

rights, this should not be regarded as the only step for companies to engage in the post-2015 framework. The private sector has made a great contribution to progress under the current MDGs, and future progress will depend on its continued, positive engagement. Mandatory reporting acts to raise the minimum requirements of companies, bringing a common approach to international and national standards. The private sector represents a vast spectrum of businesses, many of which have a highly sophisticated understanding of their contribution to environmental sustainability, economic transformation and human development. These businesses will continue to compete in extending their positive impacts through embedding the principle of shared financial and social value into their core business.

THE TRANSPARENCY AGENDA

The global financial crisis has shaken public confidence in the ability of an unregulated free market to correct itself and to work in the interests of all people. This has offered the international community the opportunity to engage in a meaningful debate about recasting global institutions, including corporations, to work for those who most need help.[10]

Members of the UN Secretary-General's High Level Panel on the post-2015 development agenda, including co-chairs President Ellen Johnson Sirleaf of Liberia and UK Prime Minister David Cameron, have recognised transparency as a prerequisite for sustainable and equitable growth and for improving democratic governance by equipping citizens and parliaments with information to hold their governments to account.[11] This runs parallel to growing international momentum within the UN, the World Bank and others behind the concepts of National Wealth and Natural Capital Accounting, whereby non-financial indicators and a nation's 'natural capital' are incorporated into national accounts to better reflect the sustainability of a country's growth.[12] The latter mechanism forces environmental costs to be recognised and reflected in pricing, encouraging behaviour change in producers and consumers. This supports the principle that what gets measured gets managed.

Likewise, many shareholders in large companies are demanding changes in corporate governance that afford them more say in how businesses are run. Expectations of companies to introduce a longer-term understanding of return on investment are growing,[13] while consumers are increasingly interested in the environmental and social impact of the products they buy. The publication of detailed information showing companies' financial and non-financial performance, disclosed using new technologies, would allow the same level of accountability of the private sector as the public sector and could lead to enhanced outcomes for overall human development goals, especially for children.

According to the 2012 Edelman Trust Barometer, which measures attitudes about the state of trust in business, government, NGOs, and media across 25 countries, the public perceives the most important roles of government in its relations with business as protecting consumers from irresponsible business practices and regulating business activities to ensure companies are behaving responsibly.[14] As a result of these shifts in public mood and policy landscape, the international community once reluctant to place global demands on the private sector, has a new opportunity to adopt focused, smart regulation, such as mandating corporate reporting of non-financial performance.

The direct social and developmental benefits for children of mandatory corporate ESG reporting are tangible, and go beyond arguments for greater accountability and transparency. Good performers could receive credit and visibility for the work they are doing to contribute to human development, environmental sustainability and the protection and support of child rights and others will increase their compliance. For example, reporting violations of the WHO International Code of Marketing of Breastmilk Substitutes that could directly harm infants could increase code compliance and save children's lives. Reporting on environmental indicators would highlight companies that are reducing pressure on scarce natural resources such as timber, food and water and therefore contributing to more equitable growth.

The disclosure of this information aligns with existing normative expectations of large businesses, allows people and communities to engage in a constructive dialogue with companies and, when necessary, enables them to hold companies to account for infringements of their rights. It also provides companies with a clear set of expectations and encourages those companies to seek mechanisms for redressing these harmful practices while maximising their positive social benefits. For instance, corporate reporting of non-financial performance can support the realisation of children's rights. The General Comment by the UN Committee on the Rights of the Child regarding Child Rights and the Business Sector states:

> As part of child rights due diligence, large business enterprises should be encouraged and, where appropriate, required to make public their efforts to address children's rights impacts. Such communication should be available, efficient, and comparable across enterprises and address measures taken by business to mitigate potential and actual adverse impacts for children caused by their activities. Business enterprises should be required to publish the actions taken to ensure that the goods and services they produce or commercialise do not involve serious violations of children's rights such as slavery or forced labour. Where reporting is mandatory, States should put in place verification and enforcement mechanisms to ensure compliance. States may support reporting by creating instruments to benchmark and recognize good performance with regard to children's rights.[15]

Publicly available datasets of comparable ESG indicators would act as an incentive for companies to adopt robust mechanisms to minimise and improve impacts on children, through the implementation of frameworks such as the Children's Rights Business Principles. In this way, transparent information could very much catalyse the responsible and innovative corporate behaviour that results in enhanced outcomes for children and broader developmental priorities.

The availability of data underpins the accountability of all actors. As Save the Children's report *Ending Poverty in a Generation* explains: "Access to information and meaningful accountability are inextricably linked, and better data, transparently available, needs to be a high global priority to support accountability."[16]

THE BUSINESS CASE FOR REPORTING

Corporate reporting of non-financial performance not only allows citizens to hold the companies that impact upon their lives to account, but is also in the interests of the private sector itself.

Companies that disclose their ESG performance can expect to directly benefit financially. Goldman Sachs has found a "positive relationship between the effectiveness with which companies address the ESG issues facing their industry and their financial performances (returns on capital) across most sectors."[17] Similarly, recent research has concluded that while reporting may highlight the weaknesses of some businesses in the short-term, the reputational benefits of disclosing and mitigating ESG impacts will be much longer-lasting. [18]

It is only through measurement and disclosure of these impacts that a company can seek to control them, to drive out inefficiencies and to enhance its practices. The publication of this data by all large companies will make environmental sustainability and human rights information a source of competition, advantaging high-performing companies and reducing the risk of contracting certain suppliers and service providers.

It is indicative that the organisations at the forefront of the campaign for the mandatory reporting of non-financial performance are large institutional investors.[19] The sort of ESG data that mandatory reporting could present would significantly enhance the ability of investors to evaluate the long-term viability of a company. In fact, such assessments would be near impossible without data on the social, political and environmental footprint of a company.[20] This assertion is backed up by the statistics, with Bloomberg's online ESG Valuation Tool for investors receiving 44 million hits from November 2010 to April 2011.[21]

Companies are operated by, and sell to, people whose motivation in the workplace or the marketplace can be affected by a business' non-financial performance, necessitating communication of ESG footprint to both sets of stakeholders.[22] The rise of consumer activism in particular means that companies cannot afford to ignore public concerns over unfair executive pay, unscrupulous tax practices, human health risks and environmental degradation. In June 2012, the Reputation Institute surveyed 47,000 consumers across 15 markets, finding that perceptions of a company's social responsibility performance accounted for 42% of a consumer's affinity for a business.[23]

The confluence of investor, consumer and employee interest in ESG performance is clearly not lost on the senior management of a large proportion of the private sector, with a 2010 McKinsey survey stating that "50 percent of executives consider sustainability—the management of environmental, social, and governance issues—'very' or 'extremely' important in a wide range of areas, including new-product development, reputation building, and overall corporate strategy." The same survey, however, demonstrates how companies need either greater incentives to act more sustainably or disincentives to stop malpractice, with only 30% of the same executives admitting that their companies "actively seek opportunities to invest in sustainability or embed it in their business practices."[24]

Conversely, the most high-performing companies are attracted to the idea of targeted government intervention, with leading businesses at a conference hosted during the 2009 Danish presidency of the European Union (EU) calling for a stronger role for governments in ensuring a 'level playing field' for those businesses that are already incorporating environmental and human rights considerations into their core business practices.[25]

The disclosure of information is also an opportunity for governments planning for economic growth. The publication of government and corporate information has a functional purpose in supporting local innovation and growth, providing information entrepreneurs with the data they need to create valuable new products and services.[26] The widespread reporting of companies' environmental, social and governance (ESG) impact would provide further information for companies to exploit for economic value, for instance by allowing suppliers to provide buyers inputs that could reduce their water usage.

Edna Molewa, Minister of Water and Environmental Affairs for South Africa, is clear that the sustainable approach that can be supported by non-financial reporting provides an economy with a competitive advantage: "Adoption of more sustainable approaches will create new green jobs, open up new investment opportunities and export markets; supports the creation of knowledge based economy and allow South Africa to set standards and demonstrate thought leadership." [27]

WHAT IS WRONG WITH THE STATUS QUO?

A large number of companies already manage and/or report on their non-financial performance through a plethora of voluntary global mechanisms and legal requirements at the national level.[28] These initiatives vary in scope from the single issue Carbon Disclosure Project to the sector-specific Extractive Industries Transparency Initiative. At the national level, some countries have legislated to enhance corporate transparency. At the regional level, the European Commission recently announced its intention to strengthen disclosure requirements for the management of non-financial risks for companies falling under the provision of the European Accounting Directive.[29] Internationally the UN Global Compact is a multi-stakeholder network that boasts over 7,000 business participants across 145 countries.

Stock exchanges, too, have taken the initiative. Notably, Johannesburg Stock Exchange has included in its listing requirements the 'King Code of Governance Principles' (known as King III) which stipulate that "as a responsible corporate citizen, the company should protect, enhance and invest in the wellbeing of the economy, society and the natural environment." Company directors are judged by the "ethical values of responsibility, accountability, fairness and transparency and based on moral duties" and required to report on both financial and non-financial performance in an annual report.[30]

While these various transparency mechanisms all serve a purpose, the 142 national standards and laws relating to ESG reporting inevitably result in incoherence, with varying definitions of 'materiality' – what is worth reporting.[31] This fragmentation means that companies have to track and determine if and how they participate in these various efforts. It also means that they may not publish information on key issues of concern to developing countries, such as: responsible management of, and investment in, a company's supply chain; taxes paid at the national level and lobbying and marketing practices.

Non-financial reporting, which originated at the 1992 UN Conference on Environment and Development, tends to focus on environmental concerns in much greater detail than on human rights. For instance, one company that has pioneered an environmental profit and loss system[32] is still linked to suppliers accused of abusing workers' rights.[33] A further example of how voluntary mechanisms do not result in publicly available data has been found by research commissioned by the

Core Coalition into ESG reporting by the FTSE100, with extractive companies failing to publish information on security issues even though 50% of those analysed were committed to the Voluntary Principles on Security and Human Rights.[34]

This inconsistency in what is reported by companies under voluntary regimes is matched by an inconsistency in who is reporting. Less than 2% of listed companies are members of the UN Global Compact,[35] and 31% of the FTSE 100 do not even publish a corporate social responsibility report.[36] Without a change in approach to reporting, it is likely that this trend will continue: Globescan's Sustainability Survey, conducted in December 2011, found that 88% of business, NGO and government leaders still see "pressure for short-term financial results as a barrier to businesses becoming more sustainable."[37]

There are simply too few companies providing ESG information in a format that lends itself to a comparison that can form the basis of a high quality investment decision. Forward-thinking stock exchanges, such as Johannesburg, have enhanced transparency, but with less than 10% of global investments being made by institutions that evaluate ESG criteria and only 25% of Bloomberg companies reporting on ESG performance, governments need to play a more active role.[38] This should be accompanied by more vigorous advocacy around the virtues of transparency on the part of business leaders. The market agrees, with a survey of global stock exchanges finding that more than 50% of respondents see the responsibility for increasing sustainability reporting as shared between the exchange and government.[39] Similarly, The Financial Times recently reported that many of the chairmen of 25 large FTSE 100 companies surveyed by Korn/Ferry felt that public anger at their tax practices ought to be directed at the policymakers with the responsibility to close permissive tax loopholes.[40] Just as governments are considering using their regulatory powers to address ongoing concerns around tax avoidance (at the 2013 G8, for example), so too should the High Level Panel consider recommending regulation in this instance.

To date, global efforts[41] supporting mandatory corporate reporting of non-financial performance have culminated in paragraph 47 of the outcome document from the Rio +20 UN Conference on Sustainable Development. This acknowledged "the importance of corporate sustainability reporting," encouraging companies to "consider integrating sustainability information into their reporting cycle."[42] These efforts have tended to advocate the 'report or explain' principle, whereby companies should either reveal their ESG performance in their annual report or explain the reasons why they don't. In order to avoid being overly-prescriptive, and to gain a critical mass of private sector support, these efforts have not specified a preferred reporting mechanism or stated what information should be reported. Save the Children recognises the wisdom of this approach, but sees issues with a system that allows a sector too much flexibility, which can result in inconsistency of reporting among companies competing in the same space. For example, the EU's action plan for European company law and corporate governance recently stated that a broad 'comply or explain' approach was unsatisfactory for reporting on corporate governance:

> the explanations provided by companies are often insufficient. They either simply state that they had departed from a recommendation without any further explanation, or provide only a general or limited explanation… such shortcomings limit the system's usefulness and viability. [43]

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By recommending the development of extensive guidance on *what* should be included in non-financial reporting, the post-2015 framework can add comprehensiveness and consistency to corporate disclosure to match the universality that mandatory reporting can ensure.

THE CASE FOR THE GLOBAL REPORTING INITIATIVE

While Save the Children recognises that national governments will develop their own guidelines, to ensure alignment in what information is reported, these guidelines could take the Global Reporting Initiative Guidelines as their starting point. The Global Reporting Initiative's G3.1 Guidelines are arguably the most sophisticated framework currently in operation (both the next generation of GRI guidelines and the International Integrated Reporting Council framework will not be published until Q2 2013).

GRI is a multi-stakeholder initiative whose guidelines have been developed in consultation with companies and other organisations. For this reason it is the most popular framework for businesses wishing to disclose their ESG data, with 77% of Global 250 companies that publish ESG information choosing to employ the GRI system.[44] Despite being user-friendly, GRI is rigorous, with the G3.1 indicators spanning impacts in terms of:

- the economy
- the environment
- society
- labour practices and decent work
- decent work
- human rights
- product responsibility.

These extend to "taxes paid by country"', a company's lobbying positions, the "total value of financial and in-kind contributions to political parties, politicians, and related institutions by country" and its approach to managing the risk of child labour in the supply chain.[45] There are also sector-specific supplements, allowing companies to adapt their ESG reporting to reflect their highest areas of risk, for example in relation to the protection of children. Notably, the Food Processing Sector Supplement recommends "reporting on policies and guidelines relating to marketing to vulnerable groups" and explicitly references the WHO International Code of Marketing of Breastmilk Substitutes.[46]

Recommending the use of the Global Reporting Initiative Guidelines as a baseline is not unprecedented. Ten governments already include a reference to the GRI in their official guidance on non-financial reporting, and some have applied it as a rule to state-owned enterprises.[47] The GRI Guidelines align with the Carbon Disclosure Project, United Nations Global Compact and the UN Guiding Principles on Business and Human Rights, with the latter recommending that governments "encourage, and where appropriate require business enterprises to communicate how they address their human rights impacts."[48] Those companies that have good practices or have improved the way they do business through mechanisms such as the Children's Rights Business Principles can communicate this information through the GRI reporting model. Companies can still use their own

reporting format and simply include a GRI index that indicates on what page of a sustainability report a particular GRI indicator has been referenced.

One of the most controversial issues in sustainability reporting is the relevance or 'materiality' of sustainability information, or the point at which a factor could affect the 'economic decision' of an investor. The GRI addresses the failure to disclose sustainability information on the basis of 'immateriality' by expanding its materiality definition to include indicators "that reflect the organization's significant economic, environmental, and social impacts or that would substantively influence the assessments and decisions of stakeholders."[49]

Raising non-financial reporting to the level of financial reporting in this way demands rigorous auditing by a professional external organisation, undoubtedly creating new responsibilities and not insignificant resource implications for a company. On the other hand, it also creates a new market for companies or entrepreneurs around the world. Financial reporting is also onerous, but is accepted as such given its importance to a company's effective functioning, something that this paper argues is equally true of non-financial reporting.

The requirement to report on ESG performance would only apply to those large companies (defined by having either more than 250 employees, or more than €50m turnover and €43m assets)[50] listed on stock exchanges or otherwise, which could reasonably be expected to find the resources necessary to do so. National governments may wish to extend the reporting requirement – for instance, a country could tie public sector contracts to the disclosure of certain information, although such steps could require adaptation of the body of international regulations on public procurement.

The inclusion in the post-2015 framework of mandatory reporting of non-financial performance for all large companies would not need to go that far. The objective of this requirement would be to raise the minimum level of ESG reporting of large companies, to bring commonality to the format in which information can be accessed and to align international and national standards. Above this minimum standard, companies will continue to compete in advancing their relative sustainability credentials, combining risk mitigation with more proactive approaches, for example through integrating the Children's Rights Business Principles into their core business.[51]

Recommendation: The High Level Panel on the post-2015 development framework should consider recommending in its report to the UN Secretary-General that all governments that are party to the post-2015 goals ensure greater transparency and accountability by all companies, with a potential indicator being a legislative requirement that all large companies report on their non-financial performance in their annual report. This legislation could be accompanied by a robust set of guidelines and performance indicators as baseline reporting requirements that could consider taking the Global Reporting Initiative Guidelines as their starting point.

The inclusion of an explicit indicator in the post-2015 framework under an overarching goal of achieving more open, accountable and inclusive governance by 2030 could be an effective way to do this.

This recommendation is an issue which can bring together both the High Level Panel and Sustainable Development Goals processes around a common interest and serve as the basis for more detailed agreements on the future development agenda.

Non-financial reporting is not a silver bullet for improving outcomes for children and the societies they live in, but it could significantly enhance the transparency of key development actors: large corporations. It could create clearer, consistent expectations of the private sector, ensure a level playing field among private sector competitors, and empower citizens, consumers and governments to make informed decisions. The role for the private sector in the post-2015 framework clearly goes beyond reporting, with more lasting sustainable development benefits likely to come from leveraging companies' core business practices in search of shared financial, social and environmental values. However, mandatory corporate reporting should be considered seriously by the High Level Panel as an important potential indicator.

Save the Children works in more than 120 countries. We save children's lives. We fight for their rights. We help them fulfil their potential

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