By Ralf Frank

XBRL – the medium is the message[1]

ABSTRACT: This paper demonstrates how XBRL eXtensible Business Reporting Language can make a contribution to enhancing business reporting. It looks at transparency, the role which is commonly assigned to it and how it is implemented. By looking at traditional vehicles of corporate business reporting such as annual reports and examining common examples of non-transparent reporting patterns, it seeks to point out how adopting XBRL to reporting processes can result in a higher order of transparency.

Transparency (more precisely: the lack of it) is one of the most common themes in the current global debate on the financial crisis. Regulators, standard setters and the trade press are criticising financial institutions around the globe for lack of transparent business activities. Neologisms are a sign of change, and there are examples of new creations, such as “toxic securities”, which seem to disguise the fact that there must have been a time when these securities were considered non-toxic or even healthy. We, or whoever is responsible, seem to have forgotten this time, and for most of us there is a significant lack of transparency about where to look for the causes of the market failure.

Transparency is often mentioned in the context of XBRL. A Google search on 25 February 2009 produced 45,500 entries for ‘xbrl’ and ‘transparency’. Does XBRL help to increase the transparency of financial statements? In what way? This paper will argue that XBRL can in fact take transparency to a higher level, but probably not in the way that this is commonly conceived. This article will demonstrate that one good piece of advice to XBRL proponents and the financial community is to say farewell to the idea that an interactive representation of today’s primary financial statements is the future of business reporting. In essence, the potential of XBRL is completely underestimated if interactive data concepts focus on electronic versions of “paper under glass” (PDF). XBRL is an electronic *medium*, not just another way of presenting financial reports.

Let us take a look at transparency first. When we encounter a situation that qualifies as non-transparent, we are prone to ask for more information. The spontaneous reaction to a seemingly non-transparent company report is to ask the company for more data. Back when the new economy bubble burst, many investors lost significant amounts of hard cash. All of a sudden, it became clear that the public and the capital market audience did not have sufficient understanding about the intrinsic risk of high-growth businesses in new media, telecoms and life sciences. It also became clear that the business ideas of 25-year old CEOs who declared how “Granny will buy eggs, butter and milk in an internet portal, which also gives her the ability to chat with other senior citizens and exchange

[1] NB. Opinions expressed in this document are those of the author and do not represent official statements from XBRL Intl, XBRL Intl’ Best Practice Board, XBRL Germany, or any other organisation the author is member of or affiliated with.

investment ideas", or the like, lacked significantly in substance. Read equity research reports from this period and you will be shocked to see just how naïve the belief in business models was, and how few hard facts were known. But was company reporting non-transparent back then?

When criminal acts like those of Enron, Worldcom and Parmalat became visible, it was clear that the organisation of financial reporting was in drastic need of improvement. Fraud being fraud, the issue that regulators addressed was how to make company financial statements more transparent. In the US, Sarbanes Oxley was introduced. In Europe, the Market Transparency Directive was implemented, which in the context of the European Union means national adoption and the likelihood that implementation looks different from one country to the next. If you are looking for tangible signs of what the regulators striving for increased transparency were thinking of, look at the 3-page disclaimers which banks or brokers publish with their investment products today. Or think of any pamphlet you receive from your bank or broker, and the annual reports of listed companies, which are the size of the telephone directory of a major city.

Regulators and legislators, as well as the accounting profession at large, have a love of annual reports (ARs) in common. ARs, according to conventional wisdom, are the main instruments by which corporates report their results to investors and financial analysts. This belief is wrong. An AR is merely one of several communication instruments. And an AR does not drive the share price.

Earnings releases, interim reports and discussions with management are the instruments most commonly used by investment professionals to decide whether a stock is worth investing in. True, many investment professionals do read ARs, but typically only *cursorily and selectively*. And, more important, as ARs typically do not contain guidance on the future or forward-looking statements, their reception is not really time-critical. But who would deny that capital markets are effective in timing the right point for a decision to invest or divest?

ARs have grown is size. 300+ pages are no longer an exception, but rather the rule these days. In 2006, postal workers in the UK refused to deliver the ARs of a major British bank, because it contained 500 pages and weighed more than 4 kilograms (8.8 US pounds). Moreover, regulators and legislators around the globe have forced corporates to disclose more information more frequently. This is one of the main reasons that ARs have grown in size. There are other reasons as well, e.g. the communication consulting industry, which has been found guilty of seducing companies to utilize the AR as a marketing tool. Consequently, we find photos of employees, customers and suppliers, pages about philanthropic engagement and a stylish design. Here is an interesting figure: according to a survey of German listed companies from 2005, the preparation, design, production and distribution of the AR consumes up to 20% of the annual investor communication budget.

The call for more transparency is probably as old as the capital markets themselves. Transparency has been referred to as "the opiate of the people in the capital markets".[2] There can be only one answer to the typical credo of the 'More transparency!' crowd (which says that more data from corporates increases the usefulness of corporate reports). And that answer is: "more data is simply more data!" Marylin Strathern's highly instrumental paper on the topic, entitled "The Tyranny of Transparency"[3] may serve to add to this point.

[2] I owe this to a speaker, whose name I no longer remember, and who coined this phrase at the G3 launch in Amsterdam in October 2006.
[3] Strathern, Marylin, "The Tyranny of Transparency", British Educational Research Journal, Vol. 26, No. 3, 2000

Strathern shows that it is a one-sided and simplistic approach to the complexity of organisations in their environments which pleads for more transparency and that, "In a social world where people are conscious of diverse interests, (…) an appeal to a benevolent or moral visibility is all too easily shown to have a tyrannous side."[4] In the context of transparency, and the call for more visibility, Haridimous Tsoukas points out that in societal relations (of which relations between corporate management and investors are part), accountability is axiomatically related to increasing the amount of information. However, he points out that *more* information typically leads to *less* understanding. In particular, more information also means less trust. Trust, however, is a necessary ingredient for effective functioning of an expert system.[5] Transparency is often related to a paradigm that rests on the assumption of perfect information, which is based on the antiquated presumption of homo economicus[6].

Before we look at why this development is detrimental to transparency, let us be semantically and conceptually precise. It was at the Washington D.C. conference in October 2008 that Prof. Bill Lutz, Chair of the 21st Century Disclosure Project, reminded us of the fundamental difference between data and information. Data is what is reported by corporates; information is generated by individuals through an intellectual process[7]. In corporate reporting, nothing is gained by adding sets of details and data when the original set was irrelevant in the first place, and did not answer your needs as an investor. Nothing is gained by adding further sets of data when the bulk of material is so overwhelming that users cannot find the pieces in the report that are relevant for them. A slightly alternative view would suggest that increasing the amount of data is a potential means of omission and avoiding giving investors the right answers. Can you imagine sifting through 350+ page annual reports times x corporates to cover or maintain equity positions? Bad news can easily be hidden behind ostensibly investor-centric reporting.

Even without increasing the load of data, there are certain methods of corporate transparency-management that are anything but a sign of good disclosure policy. Take a look at the following example[8]:

1. A user downloads an interim report for the period Q1-3 2008 from a mid-cap capital goods manufacturer with a fairly reasonable international exposure (hence sufficiently accustomed to global financial reporting);
2. The overview section on page 2 lists several non-GAAP items such as Adjusted EBIT, Adjusted EBITDA etc. Faced with the question of what the adjustments were, the user turns to the income statement on page 24. There, an EBIT is quoted, but no EBITDA. Using a pocket calculator he tries to add up several items in the income statement to analyse adjustments to the EBIT. Several items commonly aggregated to EBIT, however, do not add up.
3. The notes contain a link which promises to take the user to the *accounting policy statement* in the IR section of the corporates' webpage. However, here he finds himself confronted with a German-only passage, which otherwise seems to be

[4] Ibid:309
[5] Tsoukas, Haridimous, Introduction: from social engineering to reflective action in organizational behaviour, in: Tsoukas, H. (Ed) (1994). New Thinking in Organizational Behaviour: from social engineering to reflective action. Oxford
[6] Nielsen, Christian & Toft Madsen, Mona, "Discourses of transparency in the Intellectual Capital reporting debate: Moving from generic reporting models to management defined information, Working paper A-2007-01, Accounting Research Group at Aarhus School of Business, University of Aarhus, 2007.
[7] The Reporting Processes Group at XBRL Intl's Best Practice Board which I have the honour to chair is currently taking a close look at the vocabulary used to describe XBRL projects. The idea is to arrive at a clear and unambiguous classification of XBRL projects in order to identify best practices, but also areas for potential XBRL practices.
[8] Source: the author

identical with the English section. Even though the PA or somebody else in the team might speak German, this is no help: because there simply is no section or paragraph on the accounting policy.

4. A phone call to the IR department is answered three hours later by the IRO, who informs the user that the requested adjustment data is in the appendix of an analyst presentation hidden in a subsection where users typically would not expect it. Under the title "Adjustment Bridge" on slide 20+, adjustment data can be found, albeit only for 2008!
5. The whole exercise took the user approx. 2.5 hours in total (not counting the time waiting for a qualified answer from the IR department). But, this concerned only items in the income statement. What about the cash flow statement and balance sheet?

This is an example of anecdotal evidence, and readers might wonder whether this opaque and - depending on your standpoint - clumsy or intentionally bad disclosure is an exception. Speaking with financial analysts, it becomes evident that independent of the size or international exposure of a corporate, the phenomenon of playing "hide-and-seek" is well-known corporate behaviour. Schilit names 7 examples of accounting gimmicks and fraud in financials statements. "Classics" include recording revenue too soon or of a questionable quality, boosting income with one-time gains, shifting current expenses to a later or an earlier period, or shifting future expenses to the current period as a special charge[9]. Understanding early warning signals for earnings surprises is one of the key activities within financial analysis. There are training materials on the market which instructs financial analysts and investors on how to differentiate external reasons (which company management cannot have possibly influenced) from those unpleasant surprises, e.g. from overstating certain aspects such as revenues or undervaluing liabilities, which the company management can influence[10].

Poor corporate disclosure policy is an issue that XBRL will not be able to solve. XBRL is an enabling technology. It will prevent neither fraud nor the intention to hide bad news in corporate financial statements. Unless (and this is the first of two assertions in this paper) we manage to implement a higher level of transparency in the capital markets.

As Nielsen & Toft Madsen argue, transparency in business reporting is primarily concerned with *understanding* the company[11]. As consumers of financial statements, the user's prime concern is understanding what the corporate reported, because he/she needs to compare the results as reported with his/her own model. For decisions on whether or not to invest in a structured product, investors need to be able to see the assumptions, the calculations and the analysis of the underlying. The main point I find expressed in the following statement:

> "[there is] the necessity of an emancipation from the normative understanding of transparency being merely a question of disclosing as much as possible, as this [creates] problems of excess complexity and lack of understanding."[12]

As a matter of conventional wisdom in capital markets, and well-documented in literature, investment professionals often complain about "not getting the right type of information or material" that they consider meaningful and relevant. However, from the author's personal experience, users crying out for data typically are not looking for

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[9] Schilit, Howard. Financial Shenanigans. How to Detect Accounting Gimmicks & Fraud in Financial Statements (2002)
[10] Mulford, Charles W. / Comiskey, Eugene E. Financial Warnings. Detecting Earnings Surprises. Avoiding Business Troubles. Implementing Corrective Strategies. (1996)
[11] Nielsen, Christian & Toft Madsen, Mona (2007:13)
[12] ibid

access to 13,000 US-GAAP line items. Over the last 7 years, I have met and worked with plenty of investment professionals in Europe, and have never met any who want more data in corporate reports or who think that higher granularity is a worthy goal. They generally do not read the annual report of a corporate from A to Z and then voluntarily consume an additional package of 80+ page G3 reports on corporate ESG performance.

When surveying investment professionals, a recurring demand is for relevance of data, not amount of data. This is what counts as good and transparent corporate behaviour. A company understanding what investment professionals require and deliberately satisfying these expectations is considered transparent! Fulfilling the expectations of investors in terms of transparency, relevance and materiality is also a sign of good corporate governance.

Often, investment professionals use specific Business Reporting Patterns (BRPs)[13]. BRPs ideally are subsets and excerpts from the primary financial statements. They come in the form of summaries, i.e. several items from income statement, balance sheet and cash flow statements are placed in a table, both GAAP and Non-GAAP items plus extra-financial items. Additional sources of BRPs are infomediaries such as Bloomberg, ThomsonReuters, FactSet etc. BRPs serve as a kind of low granularity executive summary that is sufficient to answer the main questions investors and financial analysts initially have for corporates: i.e. What are the main financial Key Performance Indicators (KPIs) for a given period? What does the reported period look like compared to the same period last year? What is the corporate's guidance for the immediate future?

Typically, BRPs are used as a first step in financial analysis, or a summary, in the way that abstracts are used in literature. They are very common, but are almost never a substitute for detailed working through parts of the primary financial statements. You can find BRPs in presentations for financial analysts and investors, on websites and/or in intermediate reports as a summary sheet. They do not replace the primary financial statements, but rather, following a top-down approach to data processing, leading you to the essential points in the primary financial statement that you want to check or delve deeper into. At best, BRPs are consumed "as reported" i.e. the source is the corporate. If not available as reported from the corporate, BRPs from infomediaries are used, in the knowledge that infomediaries typically apply data normalisation, which changes the substance of data. "As reported" is commonly considered to be *pure*.

Given that XBRL taxonomies for both US-GAAP and IFRS exist, it should not be too much of an issue to build a taxonomy for a typical overview BPR or a 30-40 item core financial BRP – if it were not for the non-GAAPs such as EPS, EBIT, EBITDA, ROCE etc! The inadequate and unregulated way in which corporates often present non-GAAP items is one of the root causes for insufficient transparency.

Non-GAAP items, as the name would suggest, are not standardised by any accounting standard setter or clear directive for application. They leave companies with an incredible amount of discretion to decide a) what they will call the non-GAAP item, b) which GAAP line items they will use when calculating the non-GAAP and c) which items to classify as one-off items or non-recurring items. There are market conventions and there is peer pressure that prevents corporates from an "anything goes" attitude. Still, there is too much discretion at work, which many corporates exploit. This is only natural as financial

[13] Note that I am not using this term in the sense that Rene van Egmont and Charlie Hoffman use the concept in their paper "XBRLS: how a simpler XBRL can make a better XBRL", 2008 at http://xbrl.squarespace.com/xbrls/

communication is tactical in the sense that corporates typically only disclose what they are legally required to or what their investors ask for.

A higher order of transparency in corporate reporting means disclosure of a complete list of GAAP items used to calculate non-GAAP data. One suggestion of the author is to work for a consensus between corporates, peers and their sectors on how to calculate industry-specific non-GAAP KPIs and disclose these in an XBRL format, including the constitutive line items. These would effectively report how management accounts for its performance, and allow consumers a management perspective – the proverbial look over the shoulder of management. This in itself is already a different quality of transparency. But in terms of perception of corporate management, it would show that games, trickery and hide-and-seek are done with, over, a thing of the past.

Don Tapscott[14] in an article recently looked at the financial industry and how transparent this industry is about its investment products. He came up with the brilliant idea that rather than blowing up prospectuses for structured products, algorithms for products should be disclosed to inform investors how investment products are being calculated, how risk assumptions are being priced, what margin and performance assumptions were factored in etc. In plain words: the formula which was calculated to determine whether there was a market and a margin for the product should be published[15]. His main point was that a financial services provider that publishes the algorithms of their investment products achieves a level of transparency (and credibility), thus a higher order of transparency, which even a 500-page, highly granular prospectus can never achieve. As part of his assumptions, Don Tapscott looks at the Human Genome project, as part of which pharmaceutical companies contributed their R&D results to a database that will provide the basis for major breakthroughs in cancer research. Why did pharmaceutical companies participate in this programme and offer their R&D results for free? It was primarily public pressure!

This paper argues that XBRL International and its community should support Tapscott's Investment Product Algorithm idea and volunteer to write and prototype the taxonomy. It serves retail investors and capital markets and gives XBRL a prominent position as thinking ahead by *providing practical solutions* that transcend the current paradigm of more data = increased transparency.

Speaking about practical solutions: what about Business Reporting Patterns? DVFA, the author's home organisation, has started to categorise and define a) Business Reporting Patterns (BRPs) for a specified number of industries in order to b) develop taxonomies including standard definitions of non-GAAPs, i.e. definitions for calculating those non-GAAPs that investment professionals require. For instance, in 2008, DVFA published "KPIs for ESG" which have become part of the WICI framework and are also available as an XBRL taxonomy. DVFA has gained significant experience on how to organise a due process for defining the right sets of financial KPIs.

The process of definition is tedious and time-consuming work that requires precision and patience. The Reporting Processes Working Group of XBRL Intl's Best Practice Board might help to define and communicate Business Reporting Patterns as a kind of neglected practice. Important representatives of investors such as CRUF Corporate Reporting User Forum, EFFAS, CFA Institute, ICGN International Corporate Governance Network, NSMF

[14] Don Tascott. " Risk Management 2.0: Overcoming the Current Financial Crisis and Restoring Stability and Prosperity with a New Perspective on Risk" (2008)
[15] Fair enough, Don Tapscott proposed XML but I assume what he unknowingly really meant was a standardised way of disclosure, which requires taxonomies that XBRL can easily deliver.

Network for Sustainable Financial Markets and others may be interested in joining the process.

Marshall McLuhan's famous phrase "The medium is the message"[16] is often quoted, but just as often misunderstood. Consider the following analogy which helps to explain that XBRL is about a shift of paradigm and not a surface technology, as well as why XBRL as a medium offers a whole new dimension:

Not too long ago, newspapers were the most widely disseminated medium in civil society to inform readers about news in the world. What would have happened if over night (which as we know was not the case) a radio receiver had been placed in each household around the globe? Until the day before, citizens would have read an article in the newspaper. With radio receivers, a new service becomes available: a female voice reading the articles to listeners who no longer have to read for themselves. The radio programme starts with reading out the front page news and ends up with reading the weather forecast.

This is not all that happened when radio receivers gained prominence, as we all know. A medium that was predestined to feature live voices and real-time news coverage offered promise, far beyond reading the news. The radio reporter was reporting live to the audience. The radio provided "your eyes and ears", and you could feel as if you were out there where the news was happening. You were able to listen to people interact in the radio. There was music and you could even phone in and listen to yourself on the radio. There was interaction and speed. Completely new formats of broadcasts were introduced. The medium of radio brought features along which changed the way in which content was made possible - the medium became the message!

Despite the fact that many in the XBRL community are working hard on identifying user demands for XBRL (or, to be precise, demands of potential users) it is also a well-known fact from market research that users often simply cannot know what dramatic changes a technology might bring along. Users are often incapable of envisaging quantum leaps in processes, ways of doing things and applications.[17] There is a common assumption that no user 15 years ago would have possibly foreseen all of the applications the Internet is offering today. The Web changed the way of thinking of users - a classic example of market supply creating demand.

That is also my perception of the opportunities of XBRL. I would like to invite ideation power to the XBRL table. But, is the idea of replacing a paper-based annual report with an interactive format that allows a user or a company to render a report from interactive data (which looks like the annual report) a sign of ideation power? Probably not. It is somewhat uninspired and backward-looking – like reading newspaper articles over the radio. Bloggers and Tapscott's Net Generation have demonstated what can be done with interactive data, which XBRL in essence is. However, until these people are grown up and have sufficiently senior positions in the investment industries, the XBRL community will have to start moving ahead with the search for better ways of deploying XBRL. This paper has named two ways of doing so.

[16] Marshall McLuhan. Understanding Media: The Extensions of Man (1964)
[17] Cf. Kjell Nordstrom and Jonas Ridderstrale. Funky Business (2001)

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