

# External Reporting Day 2

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# Track Recap

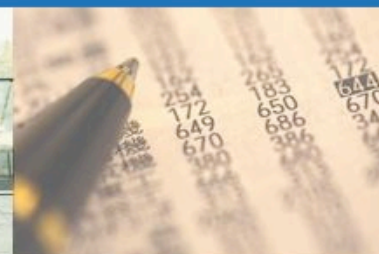
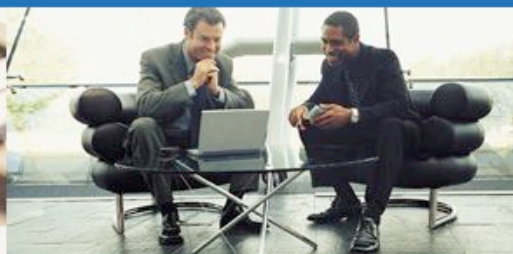
- We are exploring the impact of interactive data on the professionals involved in external reporting. We are looking forward with a view to the opportunities, challenges and new insights that XBRL offers up.
- Yesterday, focus was on the analyst on the buy and sell side and we heard about the experiences of another, vertical, standard RIXML.
- Today we are hearing from and debating with the other actors on the external reporting stage.

# Today

- The Infomediary: Reuters' Haksu Kim, world-leading authority on comparative financial analysis
- The Auditors: PwC's Eric Cohen and GT's Dan Roberts are stalwarts of XBRL and deeply involved in forming the audit framework for XBRL
- The Ratings agency: S&P's Sue Harding will provide insight into the impact that XBRL will have on the increasingly important world of corporate ratings
- The Exchanges: Sadly we are missing Luca Filippa from Borsa Italiana, but we are joined by Koji Yoshida, from the Compliance department at Tokyo Stock Exchange, supported by Chie Mitsui from JiJi Press

# Today

- The Preparer: Matthew Birnley from United Technologies, one of the best known voluntary filers in the United States will describe the highs and lows of XBRL for the Controller.
- The Investor Relations Pro: Michelle Savage, now one of the team at XBRL US but still one of the best known and well regarded figures in IR will be talking about the impacts and opportunities for that industry
- The pundit: John Turner will outline the future of Expectations Management in an XBRL world
- The Panel: Join us for a lively debate about how all of our professions will gear up for interactive data



# Expectations Management in an XBRL world

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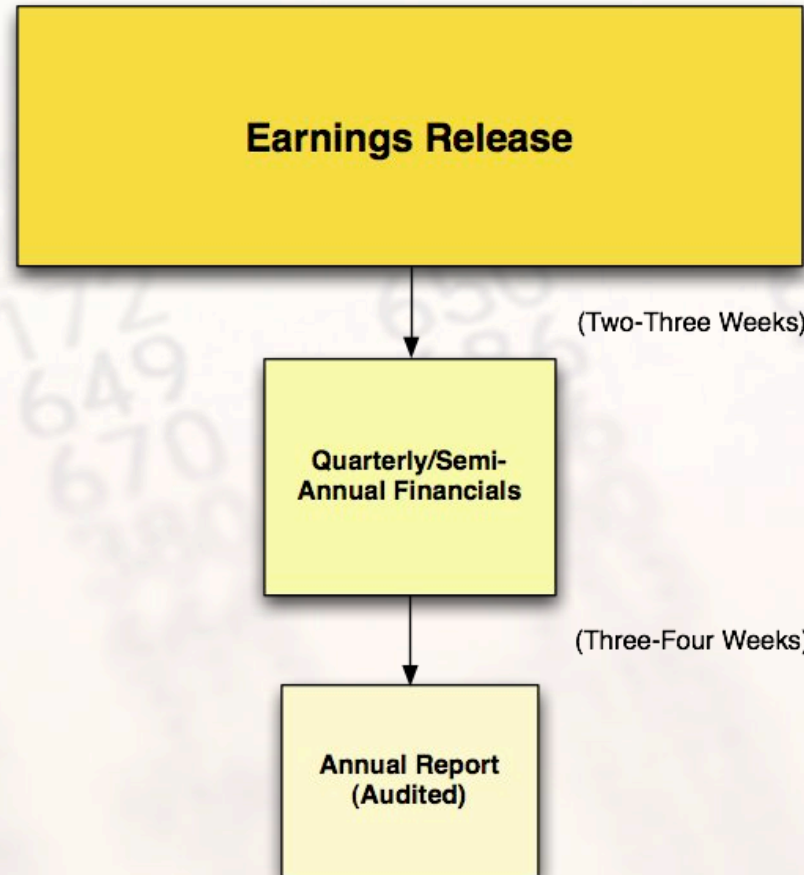
# Expectations Management

- Setting the Stage
- Current Issues and Debate
- The Blindside
- Impacts for Financial Analysts
- Impacts for Controllers

# Purpose of Disclosure

- Fundamental aspect of capital allocation
- Disclosure informs investors, lenders and their advisers (analysts) about the financial health and to a much lesser extent, financial prospects of a company.
- Financial disclosure is basically the most valuable information on the planet
- Hence: highly regulated
- Hence: Compliance is the everyday focus of many IR and finance executives

# Disclosure Impact



Market Impact





# The Earnings Expectation Game

- “Did you meet your earnings?”
- “MBE” is the game: Meeting or Beating Expectations of Analyst’s Estimates
- Estimates, in turn, for around half the market, are informed by earnings guidance
- EPS - growth and volatility is the ONLY thing that matters. It is the ONLY number that is consistently forecast. It is the ONLY number that many investors pay ANY attention to.
- Beat the number, consistently, and gain a share premium
- The market has reverted to the lowest common denominator
- Unsurprisingly, companies game the system

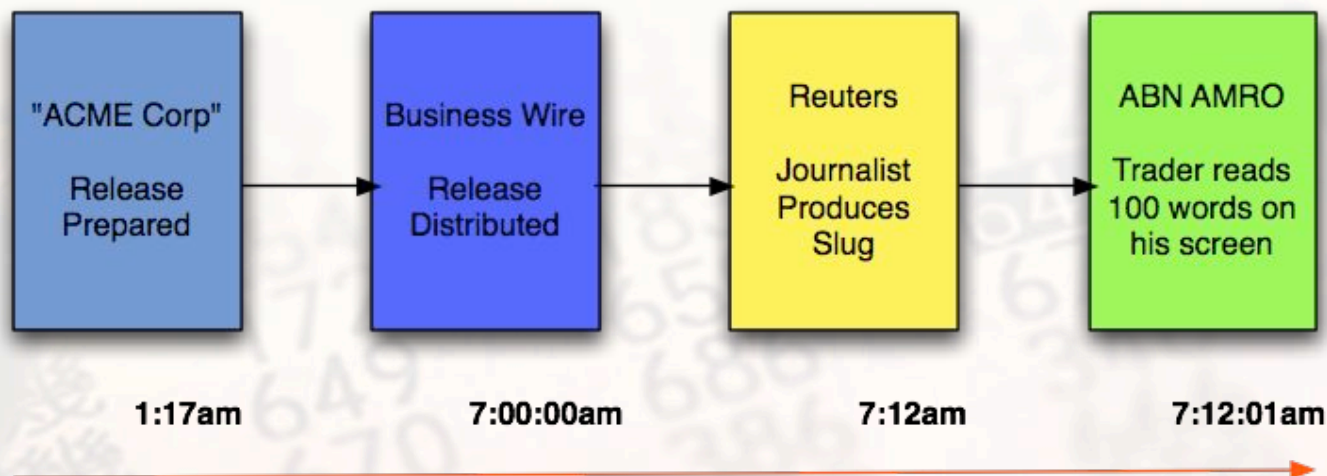
# The EPS game

- Earnings smoothing is the art and science, of managing net earnings, usually by recognizing or derecognizing various reserve accounts.
- Perfectly legal, within certain reasonably well understood constraints. Consumes plenty of Audit Partner time.
- Extends into lobbying of accounting standards setters.
- Not as obvious as it was a little while ago.
- Easier for companies with large, complex reserves.

# Why this focus?

- EPS is obviously vitally important
- Everyone knows it's not consistent
- It is recast by every sophisticated analyst and infomediary
- BUT in its raw form, it is the first thing that the professional investment community sees.
- You can't trade on information you don't have.
- And the only thing you KNOW you have, at first, is EPS.

# This is today...



- “ACME is continuing its profitable ways, reporting net income of US\$67 million, or **US\$0.02** a share, on US\$3.29 billion in revenue in quarterly financial results released Tuesday.”

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# “Apples to Apples”: CFA Institute for Financial Integrity

- Reform earnings guidance practices: *All groups should reconsider the benefits and consequences of providing and relying upon focused, quarterly earnings guidance and each group’s involvement in the “earnings guidance game.”*
- Develop long-term incentives across the board: Compensation for corporate executives and asset managers should be structured to achieve long-term strategic and value-creation goals. Demonstrate leadership in shifting the focus to long-term value creation.
- Improve communications and transparency: More meaningful, and potentially more frequent, communications about company strategy and long-term value drivers can lessen the financial community’s dependence on earnings guidance.
- Promote broad education of all market participants about the benefits of long-term thinking and the costs of short-term investing.

# Business Round Table, July 2006

- “The obsession with short-term results by investors, asset management firms, and corporate managers collectively leads to the unintended consequences of destroying long-term value”

# “Big 6” Audit Firms

- Move to continuous disclosure
- Move to long term value measures
- Move to non-financial measures
- Move to XBRL(!)

## But....

- The majority of analysts like earnings guidance
- The majority of the financial community is used to the current processes
- The vast majority of the analyst industry have not heard of this XBRL stuff

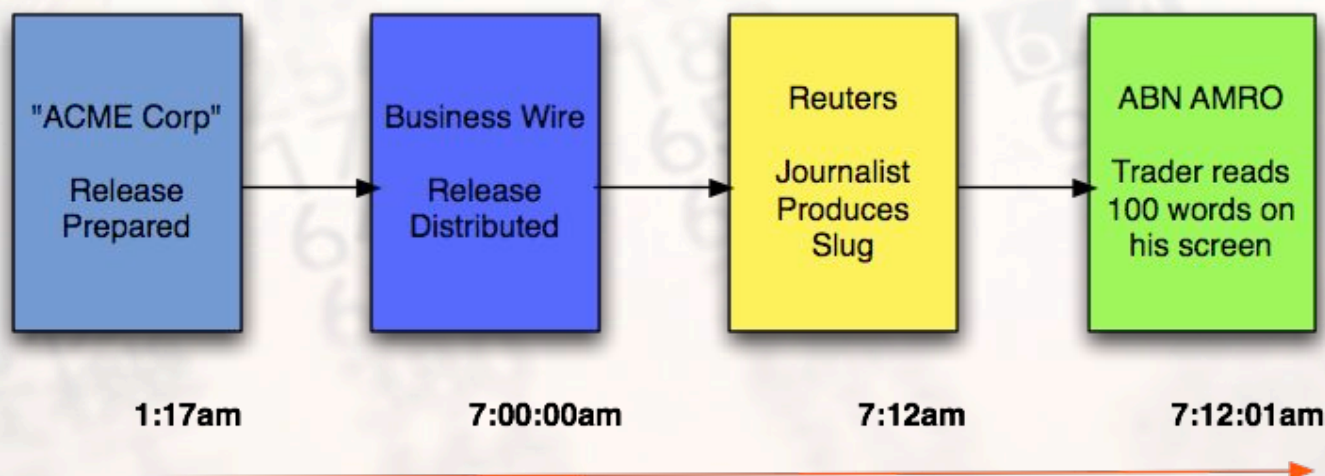
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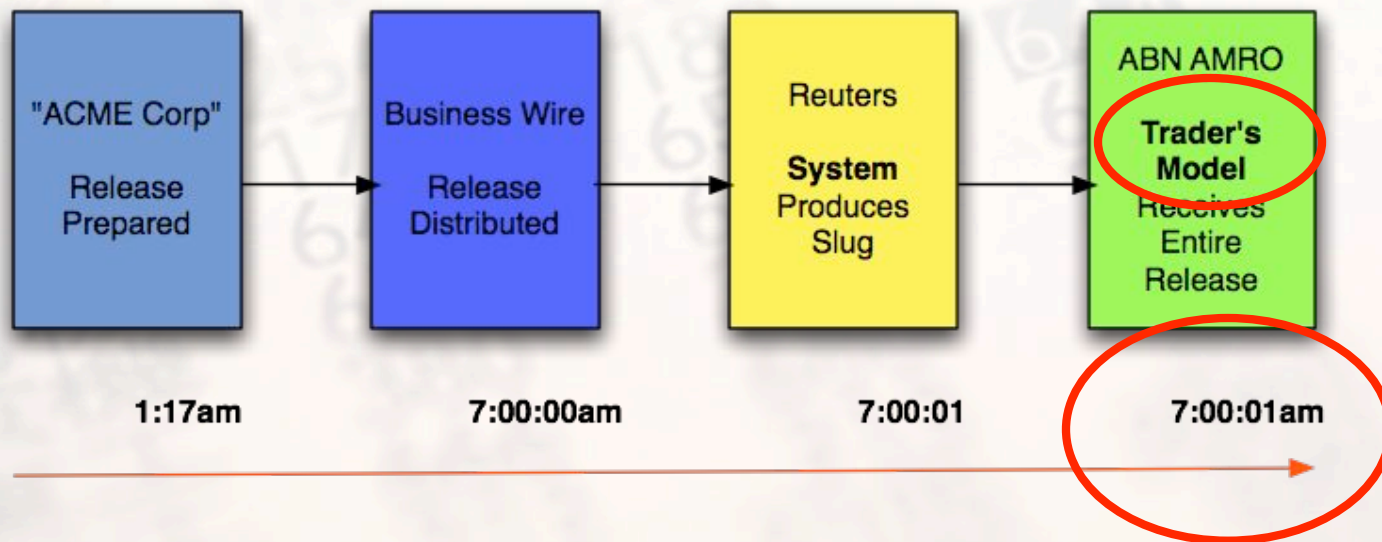


# You can only analyse what you have...

- What happens if you move from this:



**To obtaining the entire tagged release...  
with the entire earnings release in it.**



# Issues

- Substantial Impact on Infomediary Process
- Substantial Impact on Analyst Firm Tooling
- Substantial Concern from Preparers
- Downright fear from Attorney's

What is the main issue?

# Yup: Program Trading

# Expectations Management

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# Work smarter to extract better value

- Models will need to integrate with XBRL taxonomies
- This can be in a central database, a server based XBRL platform or a client-based tool
- Analysts will need to have smarter models
- Analysts will benefit from portfolio models (ie: evaluation of fundamentals across a broader set of equity and debt securities: this helps the little guy)
- Analysts will have to perform (they are remunerated against results these days)

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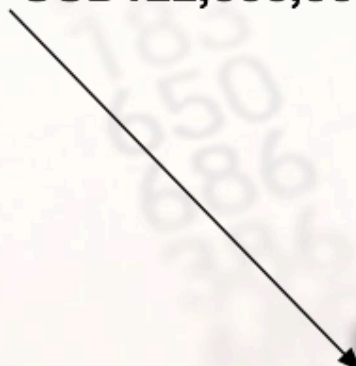
# What changes?

- Analysts will look deeper. This is good and bad.
- Analysts will be looking at errors and restatements via exceptions reports - far fewer will slip through
- Analysts will be looking at the comparable data more closely, and at the differences, more closely.
- Models will drive valuation and those models will be far deeper than they are today.
- What does that mean?

# Some suggestions

- Link concepts to assumptions

**Pension Liabilities USD122,000,000**



**17. Pension Note**

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## Be more analyst friendly

- Where there is information in your financials that you \*know\* the analyst needs: tag it.
- Make sure you are consistent. Don't change a tag unless you need to.
- Make absolutely sure that you ONLY use extensions when you HAVE to
- Make sure that your extensions are part of your messaging strategies



# Learn about the model

- Understand what the users of your financials are doing with them
- Understand what the key factors in the models are
- Understand what builds trust and what hurts trust
- Gaming will continue - calculation/presentation and formula materials will be omitted and included and the great game will continue

# Develop non-financial metrics

- Publish them.
- Work with industry to conform them.
- Ensure that these link to well established long term financial measures

# And...

- Don't forget about EPS!

**Thanks**  
**Questions?**

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