Advancing the HR Profession: Consistent Standards in Reporting Sustainable Human Capital Outcomes

By Laurie Bassi, David Creelman, and Andrew Lambert

As professions mature, they tend to define consistent standards and metrics, and human resources (HR) is still in the process of doing that. Consider operations and ISO standards, or finance and GAAP standards, or marketing and the "4P's." All have advanced by internal agreement, customer expectations, or external legislation on standards and metrics that are consistent. HR is still developing consistent standards and metrics for the reporting of important human capital outcomes in organizations—and we are making progress.

A well-established voluntary, global movement is underway to improve annual reports so that they go beyond narrow financial reporting and provide stakeholders—not just stockholders—with important insights and information about an organization's value-creation processes. The purpose of this movement is to promote deeper, more integrated thinking among leadership and the board. It is a means for helping people see beyond short-term financials.

Since a core element of this movement is the integration of human capital and financial information into a single report, it has important implications for all HR

professionals—even if you work in an organization that does not produce an annual report or if HR is far removed from the process, and even if your organization decides that the consistent metrics are better used to inform senior leadership and the board rather than being made publicly available.

Here we summarize the key findings that emerged from an extensive analysis we recently conducted of the early adopters of this perspective. These findings come from all sectors of the economy, including not-for-profits, government entities, privately-held companies, and publicly-traded companies. For the purposes of this article, we will call this new consistent set of human capital outcomes the "smarter annual report." It will serve as a primer for HR leaders to use to communicate with their executive team and board. Whether or not organizations choose to make any of this new, integrated method of reporting available to additional shareholders—either internal or external (for example, through the publicly available annual report)—remains, of course, a choice, not a mandate.

Who Is Behind This Movement?

The big players in driving a push to smarter annual reports are the Sustainability Accounting Standards Board (SASB) in the United States and, globally, the International Integrated Reporting Council (IIRC).

An important well-established player in sustainability reporting is the Global Reporting Initiative (GRI). Its focus is more on corporate responsibility than value creation; nonetheless it plays an important role in defining the metrics that will go into the smarter annual report.

A variety of other bodies are actively supporting improved corporate reporting. For example, The B-Team is a group of global business leaders including Sir Richard Branson and Ariana Huffington who are pushing for greater corporate responsibility with "true accounting" being a clear part of their mission. And the Vitality Institute is explicitly working on a set of recommendations on the human capital metrics that progressive, forward-looking organizations should consider incorporating into their internal assessments and annual reports.

Will Anything Come of This?

Michael Bloomberg, former New York City mayor and multi-billionaire and international philanthropist, and Mary Shapiro, a former chair of the U.S. Securities and Exchange Commission, are serving as the chair and the vice chair of the SASB. Do they have the power to drive change in the world?

IIRC and B-Team have the Prince of Wales and Richard Branson as flag wavers. Do they have the power to bring international attention to this issue?

The bottom line: Yes, change is coming. And it has important implications for the future of the HR profession. Hence, HR professionals will be well-served by seeking to understand, harness, and leverage the best insights from this movement.

Best- and Worst-Case Scenarios

Smarter human capital reporting can give the CEO a platform to communicate a more complete and comprehensible picture of how the firm is creating value, and provide a better basis to manage relations with stakeholders. This, in turn, could help lay the foundation for more patient investors who accept short-term drops in earnings when it is clear that the long-term trajectory is sound. This type of investor is sometimes called "patient capital." If stakeholders—especially stockholders—have credible, forward-looking information about the sources of value creation, the sole focus on this quarter's earnings could begin to diminish. That, in turn, would be a very positive development for strategic HR professionals and functions that truly are drivers of long-term value creation. In short, a drive to provide better evidence of value creation can spur improved practices and investment in human capital, and also in HR information and analytics.

If badly done, however, it could become just another expensive compliance exercise, throwing more metrics into a report without providing better insight into value creation. Organizations that have inadequate HR data management or poor results on human capital measures are likely to resist publicly revealing these metrics.

Customers who care about quality care about HR

It is common for manufacturers with a well-established quality program to ask their suppliers about their own quality programs. Quality standard may specifically cover HR topics; for example the ISO ISO/TS 16949 standard includes "Maintain appropriate records of education, training, skills and experience" and "The organization shall have a process to motivate employees to achieve quality objectives, to make continual improvements and to create an environment to promote innovation." The takeaway is that it is not just boards and investors who want to see evidence that the firm has good HR processes and outcomes; customers may care as well.

What Are Companies Reporting Now?

In our extensive analysis of the "smarter reporting" movement, we carefully studied 62 integrated reports from a broad range of industries around the globe. We found that nearly 80 percent of these integrated reports have a separate "people section". This section goes by a variety of names, such as "our people," "investing in employees," "winning with people." or, more prosaically, "human capital report" or "labor practices."

The length and depth varies greatly. At one extreme, Enel provided 13 pages of employee data, but many others had just a few pages, often light on data. What is actually covered also varies considerably. Different companies cover different topics and use different formats for the same topics. We see everything from absenteeism to leadership to training and talent development. These reports, while by no means perfect, can provide tangible examples that might be useful in conveying your organization's human capital and value creation story to stakeholders. The large variations in what is reported show that as a profession we are still early in grappling with the issue of consistency of definition and measurement.

We discovered that information in these reports may include:

- A discussion of HR and people strategy and goals; essentially stating what HR's goals were for the last period, how they performed against those goals and what the goals are for the upcoming period.
- Familiar HR metrics such as absenteeism, demographics and diversity, health and safety, talent retention, investment in training and hours of training, and results from employee or engagement surveys. There is usually text to explain the numbers, but often the data speaks for itself such as engagement trending upwards or injury metrics that are worse than industry benchmarks.
- Contextual information that helps investors better understand how the company operates, for example information on leaders and leadership development, organization structure (usually to explain the rationale behind a reorganization), governance processes and information on composition of the board, statements about culture and values, and information on labor relations and upcoming negotiations.
- Finally, we may find financial information such as total employee costs or ratios such as revenue per employee.

We are seeing an era of experimentation, which is helpful because it provides many examples of what your organization might do and what your organization might want to avoid doing.

HR's Challenge

Higher standards of human capital reporting—whether for internal or external stakeholders—offers great opportunities for HR to demonstrate its contribution, through playing a core role in shaping the organization's value creation narrative.

There are also threats to HR if it is underprepared—if it is a bit player in the corporate reporting process, with little knowledge of the various emerging standards, and if its HR information systems and analytics are patchy and unintegrated, with limited ability to demonstrate cause and effect between human capital investment and business results.

Based on our review of these annual reports, we've identified key areas for your organization to focus on as it addresses the issue of the consistency of human capital outcome measures.

Ensure Full HR Involvement

HR leaders should be sure they are part of the team working with the CEO, not standing on the sidelines.

What to Include and What to Exclude

The starting point is to articulate clearly and succinctly the description of the role that people and HR play in creating value.

Finding Data

You probably will not be able to achieve your ideal reporting status in the short-term, but that shouldn't become an excuse for inaction. It is important to develop aspirational goals in this regard, but also to operate in the reality of the here and now.

How to Tell a Smarter Story

Simple yet compelling visualizations, along with a well-constructed narrative, is important. In addition, a parsimonious, well-chosen set of metrics that is consistent with and supportive of the narrative needs to be provided.

What to Do with Bad News

It is bound to happen. Although smarter reporting will have the benefit of helping your organization focus on the most important human drivers of organizational performance, not every key metric will improve from one report to the next. You need to anticipate that and decide in advance how to handle setbacks along the way.

How to Generate Smarter Data

Almost certainly working through the issues noted here will point to needed enhancements of both your analytics strategy and your HR information system. The good news is that obtaining the required funding is more likely when the need is identified as a part of the holistic process described above.

What to Do Next

You need to build awareness in the organization that the movement to smarter reports is underway, and make sure key stakeholders recognize the opportunities along with the risks—including that of failing to respond proactively.

A Framework for Smarter Human Capital Reporting

Achieving smarter human capital reporting requires thinking differently. We have found that a good way to do this is to think like an external investor, rather than from the perspective of (internal) HR. Doing so tends to separate the wheat from the chaff—the essential essence of "people issues"—from all of the processes, procedures, details, cultural, political, and budgetary issues the HR function is immersed in on a day-to-day basis.

As you consider this framework, keep in mind that every organization—government, not-for-profit, privately held, and publicly traded—has investors (including your organization's employees who invest a large percentage of their waking hours at work). At the most fundamental level, here's what investors— both internal and external, current and prospective—want to know:

- Does the organization have the capability to achieve its goals?
- Will the organization be able to innovate so that it not only stays relevant, but also grows?
- What are the risks that the organization faces that threaten its future capability and ability to innovate?

And so, at the most fundamental level, this is how HR creates value. It builds capability, it helps create a culture that fosters innovation, and it helps mitigate "people risks." Every HR activity—recruiting, onboarding, training, leadership development, performance management, compensation and benefits, rewards and recognition—is in service to one or more of these goals. This perspective provides the building blocks for the narrative for telling a smarter story.

The metrics that correspond to this narrative will, of course, be more specific when applied to your organization. Universally, however, the metrics fall into one of six categories noted in the graphic below.

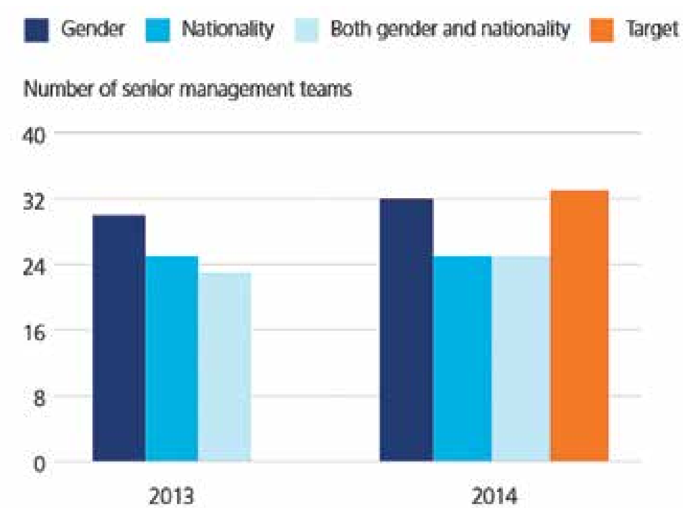
Examples of the types of metrics that you might use to provide corroboration of your value creation and risk reduction narrative include some of the following:

- **Health and safety.** Injury rates, participation rates in employee wellness programs, trends in employees' health risk measures
- **Skills.** Scores on questions about employee capabilities from customer or employee surveys, investment levels for training and development
- **Leadership.** An index of leadership quality based on employee survey questions about leadership behaviors
- **Alignment.** An index of questions that measure employees' alignment with the organization's goals and values (based on the organization's employee survey)
- **Engagement**. An engagement index (based on the organization's employee survey)
- **Talent pipeline**. Percent of key positions for which a qualified internal candidate has been identified, percent of turnover in key positions that were filled by internal candidates during the previous year

To share one example, consider the "Diverse Senior Management Teams" graphic from Novo Nordisk on a factor that is important to them: diversity. Note that they do not just show a table or pie chart; they show the trend over time, and they show their target so stakeholders know what level of diversity Novo Nordisk is aiming for. In other words, they provide the context so that the data has meaning. The graph shows that in 2014, 32 of their senior management teams were diverse in terms of gender and 24 in terms of nationality. Their target is to have all 33 teams diverse in both gender and nationality.

The framework noted above is largely consistent with specific metrics that were proposed in 2012 by a SHRM working group charged with developing an ANSI standard for voluntary public disclosure of human capital metrics to investors. (See sidebar, "Proposed ANSI Guidelines for Reporting on Human Capital," at right for a summary of

Diverse Senior Management Teams



Source: Novo Nordisk Annual Report 2014

A Framework for Smarter Human Capital Reporting

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Proposed ANSI Guidelines for Reporting on Human Capital

1. Spending on human capital

a. Total amount spent on employees (salaries, benefits, taxes)

b. Total amount spent in support of employees

c. Total amount spent in lieu of employees

d. Total amount invested in training and development

e. Total headcount and total FTE (full time equivalents) at the end of the period

2. Ability to retain talent

a. Voluntary and total turnover

b. Broken down by subset of EEO-1 job types

c. Industry standard formula of (# of terminations during the period) / (average active headcount during the period)

3. Leadership depth

a. Percentage of defined positions that have an identified successor

b. Percentage of open defined positions filled internally during the period

4. Leadership quality

a. Index of relevant questions from employee survey

b. Information on the response rate and methodology/tool

5. Employee engagement

a. Index of relevant questions from employee survey

b. Information on the response rate and methodology/tool

6. Human Capital Discussion & Analysis (HD&A)

a. Narrative to provide context and discussion of the reported metrics

b. Disclosure of any material risks or any other material information related to human capital

the metrics proposed by the taskforce.) While the proposal was never brought to ANSI for final approval, the proposed metrics remain highly relevant.

Subsequent to the work of the SHRM taskforce, SASB has been addressing many of the same issues. Its Materiality Map goes so far as to define specific measures for specific industries. For example it has concluded that the semiconductor industry should report the "percentage of employees that are (1) foreign nationals and (2) located offshore. Disclosure shall include a description of potential risks of recruiting foreign nationals and/or offshore employees, and management approach to addressing these risks."

It is evident this "investors' framework" is equally useful with both your board of directors and executive team—even if your organization decides not to disclose any of this information externally. The board needs to know everything that investors need to know, plus some. Similarly, the executive team needs to know everything that the board needs to know, plus more. So once you've done the hard work of creating a smarter reporting framework that would be of interest to investors, you've gone a long way toward creating a framework for smarter, more compelling reporting for your executive team and board.

Higher Standards

The bar is being raised, and our HR profession has the opportunity to define more consistent human capital metrics. A convergence of forces—economic, social and political—are pushing organizations to meet a set of higher standards. Social media is fueling increased transparency that, in turn, is enabling consumers to reward virtuous corporate behavior and punish bad behavior. Sustainability has evolved from a marginal issue to a business imperative. Investors, in turn, want more than backward-looking financial results. All of this is leading to smarter forward-looking value creation reporting, both internally and externally.

HR professionals are uniquely positioned to ensure their organizations benefit from these forces, rather than be blindsided by them. In so doing they will advance both the profession and themselves.

Laurie Bassi, Ph.D., is CEO of McBassi & Company, a leading analytics firm. She can be reached at lbassi@mcbassi.com.

David Creelman is CEO of Creelman Research. He does research and consulting on emerging areas of HR. He can be reached at dcreelman@creelmanresearch.com.

Andrew Lambert has been a management consultant for 35 years and headed corporate functions in two U.K. banks. He can be reached at andrewlambert@eircom.net.

References

A copy of the full report, "The Smarter Annual Report: How Companies Are Integrating Financial and Human Capital Reporting", is available at

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Two of the authors (Bassi and Creelman) co-chaired the SHRM working group.

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