

## 8. XBRL and the Financial Reporting Supply Chain

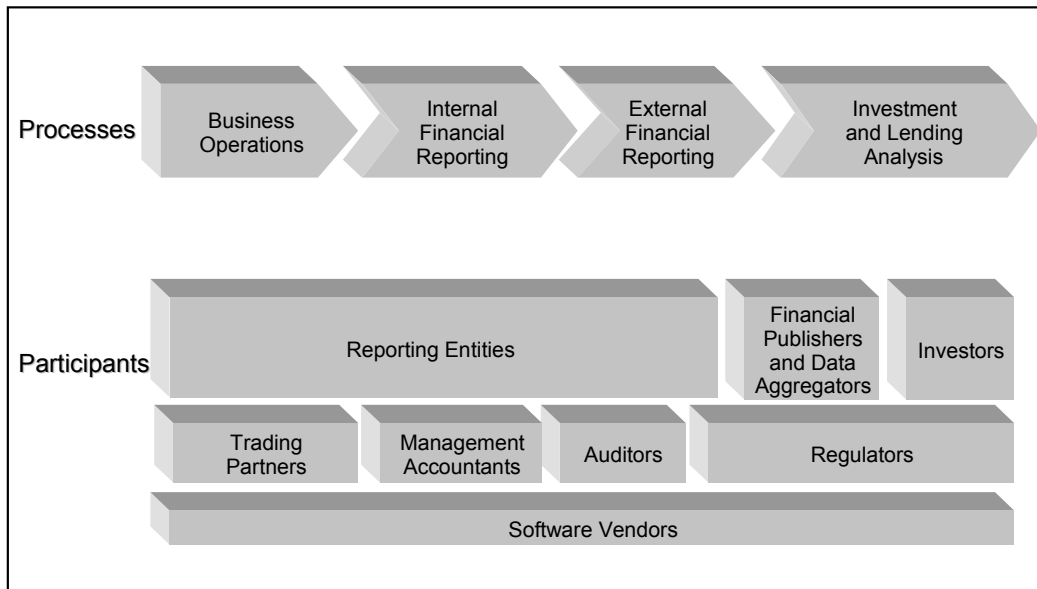
The purpose of this section is to provide a big picture perspective of the financial reporting supply chain, how XBRL might effect that piece of the supply chain, etc. The primary reason for this is so that accountants can see the bigger picture of what is going on.

Imagine that the Semantic Web exists. Imagine that most applications can import and export XBRL. Imagine a WSDL (web services definition language) service that validates XBRL instance documents and taxonomies. Imagine if XBRL could be easily and reliably be exchanged between members of the financial reporting supply chain. How might financial reporting change?

### 8.1. Overview

XBRL will have an impact on the financial reporting supply chain at its very fundamental levels. XBRL will make the supply chain work better, faster and cheaper. Some work may be moved around and reorganized, but over all, everyone will be better off.

The following is an almost obligatory slide if you are talking about the financial reporting supply chain (provided by XBRL International)<sup>6</sup>:



The above image shows the processes involved in the financial reporting supply chain:

- Business operations
- Internal financial reporting
- External financial reporting
- Investment and lending analysis

The participants in the supply chain are:

- Reporting entities

- Financial publishers and data aggregators
- Investors
- An entities trading partners who might desire financial information
- Management and financial accountants
- Internal and external auditors
- Regulators
- And software vendors which serve all the processes for all the different participants.

Think about how the participants interact. Think about how the participants exchange information and what information is exchanged. The participants and the processes of the supply chain will be elaborated on next.

## **8.2. Participants in the Supply Chain**

The participants in the financial reporting supply chain are:

- **Reporting entities** which, report information internally and externally.
- **Accountants and other consultants** such as attorneys who assist these reporting entities in preparation of these reports.
- **Data aggregators** and others which take this data, add value to it by organizing it or more likely re-keying it into standardized formats for use by others.
- **Analysts and Other Consumers** who make use of the information.
- **Standards Setters** are also part of this group, they write the standards which everyone must use, for example IFRS/IAS are written by standard setters, the IASB.

Not included in this list, but more in a support role, are software vendors who provide software to meet the needs of the participants of the supply chain.

### **8.2.1. Reporting Entities**

At first glance, it appears that all the brunt of the additional work of XBRL goes on the reporting entities, everyone else is a beneficiary of their effort.

But, this is a very short sighted view of what is actually occurring.

The following is a summary of the ways reporting entities will benefit or be impacted by XBRL:

- Financial statements are difficult to prepare accurately. Accountants spend hours and hours with a calculator and green eye shades checking all the numbers and making sure they add up, tick, tie, cross-cast, etc. Computers can do this work in minutes using XBRL, AND not make any mistakes (to the extent the humans got the taxonomy correct). XBRL will help improve the quality of financial information reported, particularly numeric information. Several entities have data on the error rates in financial information. For example the National Center for Charitable Statistics calculated a 2% error rate when they took tax return data from a PDF and keyed it into a database. Similar results exist for the US Federal Deposit Insurance Corporation (FDIC) and EDGAR-Online. XBRL will help reduce errors and improve report quality.

- Information is already being tagged, and companies are being evaluated using that information. Data aggregators re-key company data into standard formats all the time. Who would you rather have tagging your data: (a) yourself so you can control the tagging which will eventually be used for analysis or (b) someone else who really has no interest in your organization? XBRL will move this tagging from data aggregators to the reporting entities.
- In the US less than 20 percent are even analyzed; the rest fall below the radar screen as analysts spend too much time re-keying data. Small companies who know they have value but need capital will be highly motivated to tag their data using XBRL if it means their entities will get more attention.
- Financial reporting is very complicated, but XBRL will make it easier to understand and use. If you know how to read an XBRL taxonomy, then you will be well versed in financial reporting in terms of where things go, how things add up, what disclosures are actually required, it is all in the taxonomy and there for anyone to make use of. As the taxonomy was created with input from experts from around the world in IFRS reporting, it reflects a lot of financial accounting and reporting knowledge.
- Templates and reference materials are integrated into applications as web services to better understand the financial information which must be reported.
- Companies sometimes don't like comparisons of their data with other data, particularly if they may not be seen in a favorable light. If they are the top of their peer group, they have less trouble with comparisons. Companies spend a lot of time differentiating their entity from other entities in their financial reports. That should not be lost. In fact, XBRL can help that process.

The bottom line is that for reporting entities, the quality of what is reported because there will be better automated processes for verifying data, it will be easier to understand the financial reporting standards because applications will help you use the standards, because computers can read the meta-data of financial reporting. Disclosure checklists for financial reporting can be operated as wizards to help those reporting. Business rules can be used to check data quality, rather than "green eye shades" and hours behind a calculator.

### **8.2.2. Accountants and Other Consultants**

Accountants, as a group, have a hard time accepting change. That is not really a bad thing, it is far better for the world to be stable and for change to take a lot of effort rather than for change to be easy, and the world to be in chaos because it changes too much. Accountants are maintainers of the status quo, as a group. That is not bad or good, it is just the way it is.

One thing which we have to be careful about during the transition from paper-based reporting to XBRL-based electronic reporting is to not bring unnecessary baggage from paper-based reporting which actually reduces the quality, functionality and transparency of XBRL-based electronic reporting. There is a huge risk this that will occur, and it is inevitable that it will occur to some degree.

XBRL can actually work better if unnecessary paper-based reporting constraints are not imposed on it. Absolutely apply necessary constraints, but not the unnecessary ones. The trick is to understand the difference.

- Accountants are intermediaries between the reporting entities and the standards setters; they should provide feedback to standards setters to help the standards setters prescribe reasonable standards which can be adhered to.
- Financial reporting standards are complex. XBRL will help make them easier to understand as they will make them more clear. Throughout the process of creating the IFRS-GP taxonomy it was interesting to see the accountants interact and realize that there were far fewer different ways of seeing things than people thought. As the accountants learned from the better accountants, the differences which people thought existed, did not really exist at all. A bit of education made the differences go away.
- Part of the reason for different view of what IFRS is saying have to do with the fact that IFRS/IAS is vague in many cases. In these cases, the standards should be better written. More on this in the standards setting section, see below.

For accountants, XBRL means better tools to help them do their job in increasingly complex industries. XBRL allows accounting meta-data to be read by computers. Accountants and software developers will collaborate to make incredibly useful tools to accountants above and beyond their wildest expectations. This can occur because of the XBRL taxonomies which contain the meta-data in a format which computers can use it.

### **8.2.3. Data Aggregators**

Data aggregators appear to have the most to lose as a result of XBRL being adopted as a global standard. The reality is that information is already being tagged by data aggregators like EDGAR Online and Compustat. They do the best job they can, as fast as they can, as time is money and all they are doing is re-keying data, lots of data.

But if you are a reporting entity, rather than accept the tagging imposed by say Compustat, wouldn't you like to provide the data already tagged, as YOU want it tagged to Compustat?

Companies have gone through great lengths to differentiate themselves from other companies partially through their financial statements. But, the data aggregators remove much of that meaning in order to tag data at "the least common denominator.

XBRL will move the least common denominator to a higher level, and it will use a global standard set of meta-data, rather than Compustat specific meta-data.

But data aggregators are going to need to change their business models a bit, focusing more on adding value to data rather than re-keying data. There are lots of ways value can be added, and there is going to be a lot more data as a result of XBRL.

### **8.2.4. Analysts and Other Consumers**

A major beneficiary of XBRL will be those who consume data. Analysts, regulators, the commercial loan department which has to analyze and keep track of organizations they have loaned money to in order to determine if their loan is moving toward becoming a write-off.

Regulators have been early adaptors of XBRL as they have power over those they regulate. There is clear value from XBRL to a regulator:

- Standard way of expressing meta data, rather than having to invent their own way, build their own tools; they can simply use or leverage off-the-shelf software.
- Flexible meta-data, they can change their reporting requirements easier.
- Off the shelf tools for analyzing data, for example the in the US the FDIC has 2000 business rules to enforce, and they had to write proprietary methods of enforcing those rules. With XBRL, they can use off-the-shelf methods such as the formulas linkbase, a global standard.
- Distributing the data to others is also easy, in XBRL. Many times regulators make data available to the public, or exchange data with other regulators around the world.

Will there be a day when financial data which is typically reported quarterly, will be reported monthly because it is just easier to report now, with tools such as XBRL? Perhaps.

### **8.2.5. Standards Setters**

XBRL is emerging at the same time the world is moving from a hundred different local sets of accounting standards to IFRS/IAS. While the US is not moving to IFRS currently, and may not in the short term if ever, it is far better to have two standards for financial reporting than 102.

Another thing which became quite evident when trying to express IFRS/IAS in XBRL is the inconsistencies in IFRS/IAS, vagueness in certain areas, missing pieces to IFRS/IAS.

One story to make the point. IAS states that an entity must report "Finance Costs" under IFRS/IAS. However, IFRS/IAS fails to provide details of what is included in Finance Costs. Without the list, reporting entities and their accountants have to make judgment calls on what is included and what is not. It may, on the face of it, simply be better to provide the list.

The exercise of creating the IFRS-GP taxonomy became even more interesting as a result of participating in the creation of the XBRL 2.1 conformance suite and the FRTA conformance suite. What IFRS/IAS needs is a good "conformance suite", basically the IASB building a financial statement using IFRS/IAS so they can see the inconsistencies that exist. There is resistance to specifying rules as IFRS/IAS desires to be more principles based, and creating examples can be seen as tending toward being more rules based.

The goal though is to create clear accounting and financial reporting standards so that the participants in the supply chain all derive the same meaning from the same information. IFRS/IAS is a "specification". Based on the information gleaned and experiences through creating the IFRS-GP taxonomy, someone with good specification writing skills, by tuning the IFRS/IAS standards to make them less vague and more consistent would be a very good thing.

### **8.2.6. Regulators**

Regulators will drive, are driving, the first wave of XBRL adoption. The reason for this is that the regulators will certainly benefit from reduced costs of analysis and reduced costs of leveraging a mechanism such as XBRL rather than creating their own proprietary formant for exchanging information with those they regulate. But also because they can demand that those they regulate report using XBRL. Regulators generally control all aspects of the supply chain.

In the US the FDIC (Federal Deposit Insurance Corporation) is using XBRL and has 7000 national banks reporting call reports (balance sheets and income statement information) using XBRL quarterly. In Europe, CEBS (Commission of European Bank Supervisors) is expressing its COREP (COMmon REPeorting) of liquidity information using XBRL.

So regulators will drive the first use of and exposure to XBRL. If entities report to multiple regulators and all regulators use XBRL, there is no marginal burden, really, for adding a new regulator and having to report in XBRL.

It is more efficient and effective if there were one common reporting format every business had to use for all external reporting, as opposed to a business have to comply with a number of different formats.

### **8.3. Summary**

XBRL will likely cause a change at fundamental levels in the financial reporting supply chain. What would not be appropriate is any disruption in the supply chain. It is too important, stability is necessary.

Any change needs to be incorporated slowly but deliberately, in the authors view.

There are a lot of possibilities, many of which no one has even thought of. The next 25 years should prove interesting for financial reporting.