Introducing the Integrated Profit & Loss Account to ABN AMRO

Executive summary of three pilot projects
Colophon

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True Price, 2016

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Can Integrated Profit and Loss help ABN AMRO measure, manage and report impact?

ABN AMRO and impact to society
ABN AMRO works to be a better bank contributing to a better world. It is firmly grounded in society and aims to create value for its shareholders as well as its clients and society at large.

Measure and manage impact
For any bank it is challenging to understand and manage its many and complex impacts on society.

Pilot project
True Price has developed the Integrated Profit & Loss (IP&L) account that is well suited to measure impact on society. This pilot tests its potential use to ABN AMRO.

Pilots consists of three parts

1. Mortgage provision
   - Main item on balance sheet
   - Strong social benefits of home ownership

2. Cocoa trade finance
   - Test case for corporate banking
   - Cocoa has material human rights issues

3. ABN AMRO as a whole
   - Qualitative analysis shows “hotspots” of positive and negative impacts of the bank
What happens when ABN AMRO sells a mortgage to a client?

When ABN AMRO sells a mortgage, this sets into motion a chain of effects. Some of these effects end up changing financial stocks, whereas others affect other types of ‘capital’, such as natural or social capital. Some of these effects have an impact on the bank itself and others impact its customers or even third parties such as construction companies.

What can be a good way to organize and measure the size of all these effects?
The IP&L quantifies and values each impact

Quantification & valuation
In an IP&L all these effects are quantified and then valued in monetary terms – that is, we attribute a financial value to non-financial effects, such as community sense and well-being.

In this way, we can aggregate and compare the different positive and negative impacts within one type of ‘capital.’

To illustrate how it works, below the most material impacts on social capital are shown below. Similar to a conventional P&L, the IP&L measures the value created in one year, here 2014.

<table>
<thead>
<tr>
<th>Positive impact</th>
<th>Negative impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Captures all wellbeing effects of owning a house compared to renting, e.g. saving rather than paying rent, financial security</td>
<td>Remaining debt following foreclosure (€60,000/house)</td>
</tr>
<tr>
<td>Homeownership increases feelings of autonomy and security.</td>
<td></td>
</tr>
<tr>
<td>Increased life satisfaction due to home-ownership</td>
<td>Total negative impact</td>
</tr>
<tr>
<td>Increased educational achievements of children</td>
<td></td>
</tr>
<tr>
<td>Civic involvement of homeowners</td>
<td>Physical/psychological health (under repayment distress)</td>
</tr>
<tr>
<td>Feeling of autonomy of mortgage-takers</td>
<td></td>
</tr>
</tbody>
</table>

Results of pilot analysis
The IP&L can identify value drivers, risks & opportunities

Identify risks and opportunities

The IP&L makes impact actionable. By quantifying all impacts, the key value drivers can be identified. By valuing the material impacts on stakeholders, key risks and opportunities can be identified. It enables the bank to find actions that increase benefits or decrease costs.

In addition, the IP&L uncovers KPI’s in the bank’s influence to steer on. For example, all social benefits scale with the number of mortgages issued, while the negative impact on physical and mental health of repayment distress can be mitigated by ABN AMRO’s early warning system Zorgeloos Wonen that helps clients even before their monthly payments become a problem.

Results of pilot analysis

Improvement 1: increase availability of mortgages

Improvement 2: early warning system for payment problems (“Zorgeloos Wonen”)
The IP&L divides impacts among six ‘capitals’

Six capitals of the IIRC

Providing mortgages has impact on various capitals. In total, the IP&L recognizes six capitals as defined by the International Integrated Reporting Council.

For each capital, the IP&L includes the material effects on each stakeholder: the bank itself, its employees, its suppliers, its customers, third parties and on society as a whole.

<table>
<thead>
<tr>
<th>Capital</th>
<th>Description</th>
<th>Examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial</td>
<td>Broad money: currency and bank money</td>
<td>Profit, taxes, salaries ABN AMRO, Consumers fiscal benefits, Missed government taxes</td>
</tr>
<tr>
<td>Manufactured</td>
<td>All tangible assets</td>
<td>House value increase Increase in housing stock, ABN AMRO specific skills (e.g. as a result from training), patents, licenses</td>
</tr>
<tr>
<td>Intellectual</td>
<td>All intangible assets</td>
<td>ABN AMRO specific skills (e.g. as a result from training), patents, licenses</td>
</tr>
<tr>
<td>Natural</td>
<td>Everything concerning the environment</td>
<td>Life cycle energy use, Life Cycle CO₂ emissions, pollution</td>
</tr>
<tr>
<td>Social</td>
<td>Everything concerning communities and people</td>
<td>Contribution to life satisfaction, neighbourhood cohesion</td>
</tr>
<tr>
<td>Human</td>
<td>Everything that concerns workers (at the bank or at any other company impacted)</td>
<td>Employee general skills from training, health and safety for workers</td>
</tr>
</tbody>
</table>
The resulting IP&L shows significant value creation

The IP&L of mortgage provision

The IP&L is the result of quantifying and valuing all material impacts on society over the six capitals.

It shows that ABN AMRO’s mortgage provision contributes significantly to financial, manufactured and social capital creation. The main negative impacts are on financial capital (mainly by contributing to subsidies) and on natural capital.

We have taken a conservative approach to calculate these in that we have calculated natural in an absolute way (showing all impact of house ownership and use), but social capital only compared to the alternative of renting – it seems unreasonable to take the simple fact that people are not homeless into account.

ABN AMRO Mortgages 2014

Results of pilot analysis

Incl. ABN AMRO profit, salaries and taxes as well as contribution to the increased spending power of consumers. ABN market share in mortgages is assumed to be 24%

Mainly increased housing value: corrected for inflation and increased rents (the alternative) housing prices rose 1% in 2014

Negative natural capital impact can for instance be reduced with specific loans for better energy efficiency

Financial capital

Profits, taxes, salaries
ABN AMRO
Consumers fiscal benefits
Missed government taxes

Manufactured capital

House value increase

Intellectual capital

ABN AMRO - specific skills

Natural capital

Lifecycle energy use
Lifecycle CO₂ emissions

Social capital

Contribution to life satisfaction
Increased lifetime earnings of children

Human capital

Employee general skills from training

Legend

Graph shows total IP&L for ABN AMRO’s mortgage provision and shows the impact attributed to the bank. The analysis has been exploratory and based chiefly on external data and thus its results are subject to material uncertainty. All impacts, positive and negative, are distributed over all players in the value chain, including consumers based on added value and (final) demand.
Along similar lines one can arrive at an IP&L for the cocoa trade finance services

Annual value creation
ABN AMRO is responsible for around €10 million in financial capital creation through its financial services to cocoa trade clients. This financial capital does not account only for the bank but also for other stakeholders such as the farmers.

Cocoa financed by ABN AMRO has natural and human capital costs of €1 billion. After attribution, it is found that ABN AMRO is responsible for almost €3 million of these human and natural capital costs. The human capital costs are mainly due to underpayment and human rights issues at farm level. To a lesser extent, positive intellectual, social and human capital is created. Social capital creation is mainly due to that part of certification premiums that is used to enforce local communities.

Graph shows total IP&L for ABN AMRO’s cocoa service line. Note that the analysis has been exploratory and based chiefly on external data and such its results are subject to material uncertainty.

Assumption is that added value = net interest income + service fees, where we assume net interest income to be 60% x OOE x 3% (interest spread) and service fees to be 40% times the net interest income.
Main takeaways

The largest negative impacts at farm level are on human capital.

Income (underpayment of workers and underearning of farmers) and child labour are the largest human capital costs. The five main human capital costs correspond largely to the most severe human rights impacts mentioned in ABN AMRO’s cocoa research paper, except for social security.

Land use is the single largest natural capital cost.
Attribution of impact based on value added over the cocoa chain

Attribution to ABN AMRO
Banks that finance originators, exporters/traders and importers/processors are contributing to the total financial value created in the cocoa chain by 0.5%. As consumers are held accountable for 50% of all impacts (see attribution methodology), the banks are responsible for 0.25% (=0.5%*50%) of all costs and benefits created throughout the supply chain.

If ABN AMRO’s market share is 3.4%, this means that ABN AMRO is responsible for 0.01% of all the costs and benefits linked to an average chocolate bar in the supermarket.

Legend
Graph shows the cumulative financial value added throughout the cocoa chain (per kg cocoa beans), subdivided into direct actors (e.g. farmers, exporters), financers (of which ABN AMRO) and others (e.g. suppliers of equipment, energy).

Note that the analysis has been exploratory and based chiefly on external data and such its results are subject to material uncertainty.
The IP&L of cocoa trade finance can be used to identify improvement levers

Main takeaways
Stimulation of certified cocoa to traders, so that the share of certified cocoa increases from 29% to 100% has a significant potential natural, social and human capital improvement. At farm level, negative externalities decrease by 16%.

Micro-financing can reduce underpayment and underearning at farm level. The installation of such services would decrease human capital costs. At farm level, negative externalities for targeted farmers would decrease by 43%.

Legend
Graphs show change in negative natural, positive social and negative human capital for all cocoa financed by ABN when 100% certified is demanded and underpayment/earning at the farm level is reduced by 30% by providing micro-financing services to 22,222 farmers (24% of all farmers that produce cocoa financed by ABN).
The IP&L can even be constructed for the bank as a whole

IP&L “hotspot” analysis

This pilot has qualitatively identified hotspots of impact for the entire bank. ABN AMRO’s main contributions to society are on financial and social capital creation:

- Financial capital creation consists mainly of own profits, salaries and taxes as well as enabling clients to make profits and accumulate wealth.
- Social capital creation is mainly due to services to consumers: providing a stable payment and savings system, the advantages of home-ownership, etc.

Other large positive impacts are on manufactured capital (accumulation of assets) and human capital (own workforce and that of clients). The main negative impacts are on natural and financial capital (the latter mainly due to impact on to (tax) subsidies).

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About True Price

True Price
True Price is a social enterprise with a mission to contribute to an economy that creates value for all. We do that by providing leading companies and institutions with the tools they need to measure, value and improve their impact.

Tools, methods and clients
Our tools consist of protocols, strategies, training, reports, data and software to measure and steer on impact. We develop state of the art innovative methods for impact measurement and valuation and aim to make them open source. Our customers are leading multinationals, NGOs, governments and United Nations organizations.

The true price
We developed the concept of the true price. Our work is based on a unique method – the first in the world to monetize both environmental and social impacts, at product-, company- and investment level. A true price is a measure of the sustainability of products and services, as it accounts for all negative environmental and social externalities across its value chain.

The IP&L
With the development of the integrated profit and loss (IP&L), we have now taken the concept of externalities one step further. On a company level, the IP&L does not only give insight in the negative externalities associated with production, but it also shows the positive external effects, leading to a complete picture of how your company contributes to societal value creation.
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