

# Insights into integrated reporting 2.0: walking the talk



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## About this report

This report examines the reporting practices of organisations in the International Integrated Reporting Council's <IR> Business Network. It highlights the progress made towards integrated reporting over the past year, discusses the challenges that preparers face, and gives practical recommendations to guide more organisations on the path to integrated reporting.

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## **ACKNOWLEDGEMENTS**

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# Foreword



**As a long-term supporter of, and advocate for, integrated reporting, I'm delighted that ACCA has again partnered with the IIRC this year to produce this latest assessment of integrated reports from around the world.**

Through analysing 45 reports produced during 2017, we've been able to develop invaluable practical guidance for integrated reporters – whether seasoned practitioners or those starting out on their integrated reporting journey.

Pleasingly, we're seeing demonstrable advances being made by reporters in term of adherence to the International <IR> Framework; many reports provide useful examples of best practice.

As ever, we need to keep in mind that integrated reporting is not an end in itself but a means of developing better and more coherent leadership and governance – the all-important holy grail of integrated thinking. So the challenge for reporters now is ensuring that this message is heard loud and clear across the organisation – from the board to all those charged with delivering strategy and creating long-term value. This active advocacy will help ensure that integrated reporting lives up to its promise of being a transformational exercise, not simply a compliance one.

Within this latest Insights report, there are many compelling examples of the business and culture benefits that integrated reporting can deliver. I hope they inspire many more organisations to seize the huge opportunity integrated reporting brings.

A handwritten signature in black ink, appearing to read 'Helen Brand'.

**Helen Brand OBE**  
**Chief executive**  
ACCA



# Executive summary

## Integrated reporting (<IR>) and its focus on long-term value creation is a concept increasingly embraced around the world.

Issued by the International Integrated Reporting Council (IIRC), the International <IR> Framework (<IR> Framework) embraces an approach to integrated management – often referred to as integrated thinking – as well as an approach to reporting that considers wider drivers of organisational performance in a forward-looking way.

For the last two years, ACCA has worked with the IIRC to review a sample of the corporate reports produced by participants in the <IR> Business Network, a forum for organisations committed to adopting the <IR> Framework. Findings from the review conducted in 2016 were summarised in last year's report, *Insights into Integrated Reporting: Challenges and Best Practice Responses*. In continuing this series, we want to provide practical insights to help not only those organisations already preparing integrated reports, but also those just starting to adopt integrated reporting.

The 2017 review findings, which we present in this report, show that the <IR> Business Network participants have made striking progress over the past year. It was notable that significantly more organisations have made explicit reference to the <IR> Framework this year, thus underlining their commitment to integrated reporting. Just as encouraging is the increasing use of consistent performance measures from year to year, emerging bases for

comparison between organisations, and the reducing length of reports. Innovative approaches are being tested for measuring the value that organisations create for their stakeholders, demonstrating their commitment the UN Sustainable Development Goals, and using technology to make reports more concise and user-friendly. Innovations may also be emerging from audit firms: this year significantly more integrated reports were externally assured.

However, new challenges have also come to light, particularly in the following areas:

- the linking of strategy and performance through to key resources and value creation over the short, medium and long term
- the description of the board's role in enabling value creation
- discussions about the organisation's outlook, and
- the application of materiality.

ACCA's survey and interviews with <IR> Business Network participants show that solving these challenges would require report preparers to think beyond reporting practice, about organisational management. How are functions structured within the organisation? How are decisions made? What kind of oversight does the board exercise? How does management engage with internal and

external stakeholders? How transparent do organisations believe they can be in these conversations? Although the <IR> Framework focuses on reporting practice, it is clear that, for many organisations, the parallel journey of implementing integrated thinking is just as important and arduous as integrated reporting, if not more so.

Therefore, in our recommendations, we also encourage preparers to tackle wider questions about governance, strategic planning and corporate culture. These include:

- on the topic of strategic focus, defining a consistent mission statement hand-in-hand with the strategy function and the board
- in relation to outlook, challenging the board about how to approach information considered commercially sensitive, and
- regarding materiality, considering whether the materiality assessment process could be aligned with the strategic planning cycle.

For many, this will require opening new channels for dialogue with the board, and new ways of collaborating with other teams. The benefits make this effort worthwhile – as the organisations quoted in this report can testify.

# 1. Introduction

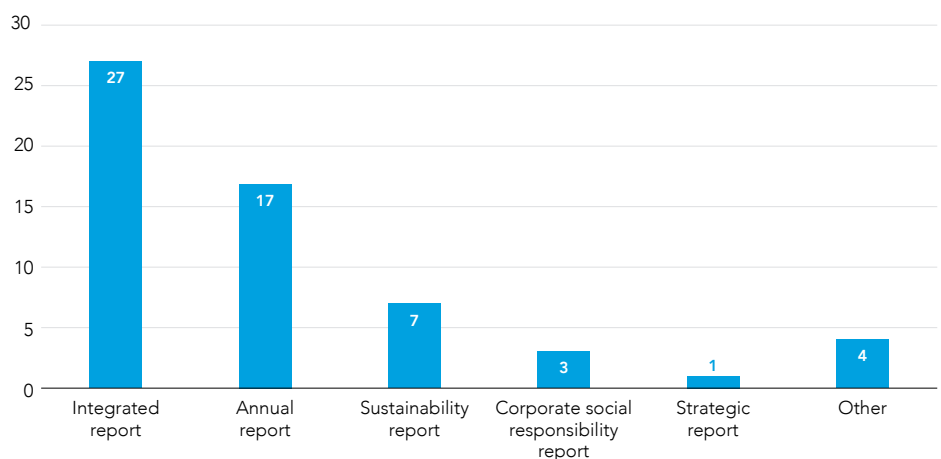
**The <IR> Business Network provides a forum where participants can share their experiences with a view to improving the quality of their reporting and, at the same time, helping to prove the business case for integrated reporting adoption.**

ACCA is honoured to work alongside the IIRC to co-convene the <IR> Specialist Panel (the list of <IR> Specialist Panel participants is provided in Appendix 2) and to review corporate reports produced by <IR> Business Network participants.

This report highlights the results of the reviews conducted during the summer of 2017, which looked at 45 reports for accounting periods up to 31 March 2017. These reports were provided by the companies under review, and constituted any documents they perceived to be part of their integrated reporting package – potentially including annual reports, supplements, and/or standalone sustainability reports (Figure 1.1). Participants received confidential feedback on their reports, including an indication of the areas where their reporting had particularly strong alignment with the <IR> Framework, and any gaps where adoption of principles could be improved or content added and integrated.

This report focuses on the main areas where this year's review project found most room for improvement. In order to gain a deeper understanding of some of the challenges involved in applying the <IR> Framework and how organisations are responding, we conducted interviews with representatives from six network participants in December 2017 and

**FIGURE 1.1:** The types of report reviewed



January 2018. Their views are shared throughout the following sections. We also include findings from a short online survey among network participants conducted in December 2017, reflecting the views of 20 respondents from 11 countries (see Appendix 5).

All the organisations interviewed for this report produce what they consider to be integrated reports, except for Novartis, which has not yet taken an official decision to publish an integrated report and sees itself as a 'combined reporter' – using its annual report as its primary report for both financial and non-financial

information (eg on environmental, social and innovation issues). Nevertheless, the direction of travel is towards the publication of an official integrated report at some point. We therefore see Novartis' experiences as relevant for our study.

This report also identifies examples of good practice and offer some practical suggestions to help organisations in their implementation of integrated reporting. We hope the insights will be of help both to entities just beginning their exploration of integrated reporting, and to those already producing integrated reports but looking to improve what they do.



## 2. Benefits of <IR>

**Although this report focuses on integrated reporting practice, it is important to highlight that many <IR> Business Network participants have experienced wider business benefits through adopting, or progressing towards the adoption of, integrated reporting.**

Interestingly, the most widely reported benefits are internal: 95% of respondents to the survey say they have a better understanding of how their organisation creates value as a result of embarking on their integrated reporting journey; 70% have seen more connections between different departments, leading to a broadening of perspectives.

Even so, there is also strong evidence of the external benefits, most notably through stakeholder engagement. Exactly half of those surveyed have seen positive impacts in their engagement with providers of capital, including investors, and 65% have seen positive impacts in their engagement with other stakeholders. Giuseppe Zammarchi, who is responsible for group sustainability and foundations at pan-European bank UniCredit, thinks his bank has seen these improvements as a result of integrated reporting. In January 2018, Moody's

Investors Service upgraded the outlook on UniCredit's long-term deposit and senior unsecured ratings from 'stable' to 'positive'. Zammarchi thinks integrated reporting can take some credit for this 'because it creates a clear link between targets... [It shows] how much we value transparency and that supports the credibility of the company'.

Marc van Weede, global head of strategy and sustainability at insurance company Aegon, thinks the <IR> Framework helps this life insurance, pension and asset management company to communicate more effectively with its wider stakeholder group. Aegon began experimenting with integrated reporting when recovering from the global financial crisis of 2008. Van Weede says that in 2010 and 2011 there was 'a refocusing of the business and rethinking – starting from first principles – about what purpose we have as a business, how our business impacts

our customers and also our employees and the communities we are active in'. The <IR> Framework was being developed at this time. 'It seemed to fit very well with this more stakeholder-driven approach', van Weede says.

It seems that done well, integrated reporting can transform organisations from the inside out. Russ Houlden, CFO of British water company United Utilities believes the major change that integrated reporting can bring to organisations is around integrated thinking. 'That fundamentally changes the way we operate the business', he says. 'In terms of the reporting, it gives all our stakeholders a little bit more of a broad understanding so they can then engage with us on their specific topics. It gives them a broader feeling of the sort of responsible company we are and the way that we try to give the best service to customers by operating in a more integrated way'.





### 3. What progress have integrated reporters made this year?

#### EXPLICIT COMMITMENT TO INTEGRATED REPORTING

Striking progress has been made by the <IR> Business Network participants in adopting the <IR> Framework: 58% of the reports reviewed stated that they were integrated reports (up from 51% last year). Similarly, the percentage of reports that referred to the <IR> Framework also increased – rising to 76% (up from 59%).

# 76%

of reports this year referred to the <IR> Framework (up from 59% last year).

A comparison of the review scores showed no significant difference in 'compliance' with the <IR> Framework between reports that explicitly state they are integrated reports and those that do not. Indeed, the lack of a reference to an integrated report on the front cover does not necessarily mean that the report is not an integrated report. For example, United Utilities publishes an 'annual report' (as on its cover) but this is also an integrated report prepared and presented in accordance with the <IR> Framework. Local regulations and market expectations are likely to have an influence here. The correlation between an explicit reference to integrated reporting and adherence with the <IR> Framework may be an area worthy of further investigation, perhaps with a wider sample of reports.

#### DATA QUALITY AND OTHER IMPROVEMENTS

Significant improvements have been made in only a year, particularly in relation to the quality of the data. In particular, reports were found to be more consistent: this was one of the lowest-rated areas in last year's review project, but became one of the strongest this year. Improving consistency was one of the 'quick wins' that we identified in last year's report, so this result is highly encouraging.

Organisations are applying performance measures in a more consistent way from year to year, and are providing better bases for comparison with other organisations. From our discussions this year and last year with report preparers, it appears that comparability remains hard to achieve, particularly on the level of detailed metrics, but the increased references to internationally recognised benchmarks, stock market indices and industry-wide performance measures is a welcome step in the right direction.

49%

of reports reviewed contain 100 pages or fewer, excluding the financial statements (compared with 20% last year).

A key principle in the <IR> Framework is that reports should be reliable and complete. Part of this means that all material matters – both positive and negative – should be presented in a balanced way. It is pleasing to see improvements in this area, as it strengthens the credibility of integrated reports. However, more can still be done to eliminate bias in the selection and presentation of the information. This could require some careful thinking about not only the visual prominence of information on the page, but also the order in which information is presented in the report.

There are also signs of a focus on conciseness. The length of reports has reduced significantly: just under half (49%) of reports reviewed contain 100 pages or fewer, excluding the financial statements (compared with 20% last year). This could be a sign that more effective application of materiality has allowed organisations to filter out information that is not material to value creation from their main reports. Many organisations that are more experienced in integrated reporting, in particular, seem to be moving supplementary information, which is relevant for only some stakeholders, out of the main report, into reporting supplements or onto the company website.

#### NEW CHALLENGES

As well as such improvements, the reviewers also identified some new challenges, mostly on the theme of linking distinct content and tying them together to produce a consistent narrative. The areas that were rated lowest overall include the following (refer to Appendix 2 for a full summary of review outcomes).

- Governance responsibility for the integrated report – a statement from those charged with governance acknowledging their responsibility for the integrity of the integrated report.
- Governance – explaining how the organisation’s governance structure supports its ability to create value in the short, medium and long term.
- Strategic focus and future orientation – linking strategy to the way organisations use and manage their resources (called ‘capitals’ in the <IR> Framework); and linking strategy to how they create value over time.
- Outlook – looking at what challenges and uncertainties could affect the execution of the organisation’s strategy and future performance.

- Basis of preparation – describing the materiality determination process that organisations have applied.
- Materiality – focusing on matters that substantively affect the organisation’s ability to create value in the short, medium and long term.
- Risks and opportunities – specifically, describing the *opportunities* that affect the organisation’s ability to create value over time, and explaining how the organisation is dealing with them.
- Performance – specifically, the organisation’s effects (both positive and negative) on the capitals.

This report will focus primarily on the challenges of linking strategy and performance through to the capitals, strategic focus, outlook and materiality. Throughout, we emphasise the importance of the board, both in exercising oversight over the reporting process, and in defining and driving strategy. The Outlook section touches upon the challenges of describing opportunities.

First, we set the scene by looking at some general challenges in integrated reporting adoption and some areas of current discussion.



## 4. Adoption challenges and talking points

### INTERPRETING THE CAPITALS

United Utilities was already preparing its first integrated report when the finalised <IR> Framework was published in December 2013. Adoption was a natural development for the business, which was already 'driving hard down a direction that we call systems thinking', CFO Russ Houlden explains. The company's 2017 annual report describes 'systems thinking' as 'thinking of our entire network of assets as one big system, and managing it as such'. Houlden says: 'Systems thinking has a lot in common with integrated thinking, which is at the heart of integrated reporting. The December 2013 <IR> Framework therefore seemed quite helpful. We had changed the way we were working and we wanted to communicate that. This seemed a natural vehicle through which to communicate'.

The main issue Houlden found when applying the <IR> Framework concerned its terminology, particularly the term 'capitals'. 'They were expressed in a language that our readers of the annual report don't think of', he explains. For example, they might think about different types of 'resources' rather than 'capitals'. United Utilities' 2017 annual report identifies its key resources as being natural resources, people, assets and financing. Houlden confirmed with the IIRC that the specific terminology was not relevant. 'What's relevant is that you consider things from a number of different angles and once that was clear,

it was clear to me that the report we were already working on was an integrated report', he says. 'So the main barrier was trying to understand whether the <IR> Framework should be taken literally, or whether there was quite a wide degree of discretion about how you express yourself – and it was the latter'. The <IR> Framework does acknowledge that 'not all capitals are equally relevant or applicable to all organisations' (para. 2.16).<sup>1</sup>

Aegon's Marc van Weede also found the 'capitals' terminology challenging and 'not always very intuitive'. He found that part of the challenge of integrated reporting adoption lay in making the capitals relevant to the business. 'Human capital is easy, but natural capital is one that we find difficult to apply directly', van Weede says. 'We are an office-based organisation, so we don't have a big, direct impact on the environment. We do have a very large investment portfolio of companies that potentially do have an impact on the environment, but it's not easy to link that in a simple way to the concept of environmental capital'. This is because, for Aegon, the term 'capitals' is understood to refer to resources owned or controlled by the company, and because the environmental impact of the investee companies are not within Aegon's control, it's conceptually difficult to apply the capitals model. The <IR> Framework leaves the question of control over the capitals open, although it does clarify that the boundary of an integrated report

includes 'risks, opportunities and outcomes attributable to or associated with other entities/stakeholders *beyond the financial reporting entity* that have a significant effect on the ability of the financial reporting entity to create value' (para 3.30).

### QUALITY OF DATA

For Dutch development bank FMO, adopting integrated reporting was attractive because its non-financial results are just as important as its financial results. The bank supports job creation and responsible business practices in developing countries through its private sector investment activities. 'The <IR> principles made this [dual approach looking at financial and non-financial performance] more structured and we found a common language to better explain our story', says Job Bakker, senior planning and control officer in finance at FMO. 'We also liked the idea of integrated thinking as it would help us to improve our strategy development by taking into account these different capitals'. The main barrier to adoption, however, was a 'technical, external' one, he says – 'getting the right data, getting it of good quality, having the right indicators, especially in non-financial areas. That is a big challenge'.

### BOARD INVOLVEMENT

The discussions with integrated reporters have found varying levels of board involvement in the integrated reporting process. Eskom's board plays more of an

<sup>1</sup> All paragraph and section numbers in the following text refer to paragraphs or sections of the International <IR> Framework.



of the reports reviewed had gained some form of assurance on their report in addition to the statutory audit (up from 46% last year).

oversight than an active participation role, while experts are involved in drafting the report. The integrated reporting team writes the report based on input from the business. The report is approved by the Audit & Risk Committee and the Sustainability & Ethics Committee (both board sub-committees), before being approved by the board.

United Utilities' board also provides oversight, but also a degree of 'challenge', Houlden says. 'They see the various drafts [of the annual report] and say, should this be in? Should this be out? Why have you decided that's out?'

UniCredit's sustainability strategy is discussed within the Group Environmental and Social Council (GESC), which is made up of executive directors, representing the first line of reports to the CEO. The board, which with the exception of the CEO is composed only of independent non-executive directors, then reviews and approves the sustainability strategy, the outcomes of the materiality assessment, and the integrated report. Although the board as a whole is not closely involved in the reporting process, some board members exercise more active oversight through their participation on the Corporate Governance, Nomination and Sustainability Committee, which reviews the integrated report before it is brought to the board. 'Last year we had a few discussions with them on the implementation of the European Non-Financial Reporting Directive', says Giuseppe Zammarchi. 'We took the

chance to involve the committee in discussing the perimeter of companies in the group on which we report, and also in discussing what we were going to include in the next edition of the report'.

At healthcare company Novartis, Carrie Scott, head of corporate brand and reputation management, says the company takes its reporting very seriously, producing an annual report with corporate responsibility (CR) information plus an expanded CR Report, directed at environmental, social and governance (ESG) analysts and CR experts. 'The annual report is the responsibility of the board of directors', says Scott. 'So we work directly with the chairman on the annual report, and the corporate responsibility report is reviewed by the board committee that oversees corporate responsibility'. As Scott explains, the annual report is guided by a steering committee made up of the chairman of the board, the general counsel, the CFO and the chief communications officer, as well as herself and the chief accountant. This committee handles all non-financial disclosures, while a separate disclosure committee handles financial disclosures.

#### ASSURANCE

This year, we found striking evidence that more organisations are seeking assurance on integrated reporting content: 60% of the reports reviewed had gained some form of assurance on their report in addition to the statutory audit (up from 46% last year). In the online survey of <IR> Business Network participants, 80% said

they already have external assurance on at least some aspects of their integrated report. Another 10% said they aimed to have this at some point, but 10% have no plans to seek external assurance and think that internal forms of assurance are more important than external assurance. However, the subject matter and scope of assurance differ greatly, ranging from limited assurance on specific metrics to a broader review of the overall report's compliance with the <IR> Framework.

The assurance on Eskom's integrated report starts with its internal audit team, which goes through the entire report and 'verifies the numbers and ensures the narrative makes sense', says Karen Koch, <IR> specialist within group finance at Eskom. The external auditors provide mandatory assurance on the shareholder compact KPIs – the KPIs set by the South African government's Department of Public Enterprises (DPE), Eskom's owner – in accordance with ISAE 3000 *Assurance engagements other than audits or reviews of historical financial information*. The external auditors also consider whether the integrated report's content contradicts anything in the financial statements. Koch sees value in external assurance in order to improve the credibility of the reported numbers. She notes that although internal audit assurance should be deemed independent, the internal auditors are still seen as part of the company. Therefore having assurance from the external auditors is important to promote public trust, especially for a state-owned company such as Eskom.



of the reports reviewed referred users to a microsite or section of the corporate website for supplementary information.

'In future Eskom might also consider gaining some assurance under the AA1000 AccountAbility Principles Standard, which looks at elements such as stakeholder engagement. That's something we could consider in future because it provides assurance on the process followed, rather than just the numbers themselves', says Martin Buys, general manager for financial and management reporting at Eskom.

FMO gains limited assurance from its external auditors on the 'sustainability information' contained in its 2016 annual report (comprising the non-financial information included in five chapters of the report). 'It gives more credibility to your story', Bakker says. However, the 'step up' to gaining 'reasonable assurance' is quite a big one because of the challenge of collecting and calculating sufficiently reliable non-financial data. FMO gathers data on its direct client impact, and calculates its estimated indirect impact using models. 'One of our strategic ambitions is to double the number of jobs supported through our investments', Bakker says. 'Take the example where we finance an infrastructure project: the construction phase will support a number of direct jobs for the time being, but it also has a huge indirect economic impact on an area in the long run'. Although it's possible to measure the number of jobs supported through the construction, it is challenging to create accurate models to estimate the indirect impact. What's more, the quality of data collected from companies in developing countries varies. 'To achieve reasonable assurance would

require substantial efforts from our clients and us, so on balance we decided for now to focus on other priorities', Bakker says. 'Our current focus is to move our reporting to online reporting to our report more accessible'.

United Utilities seeks Big Four auditor assurance on its integrated report only to the extent required by UK company law, ie in relation to the financial statements. 'Company law also requires the auditors to look at the front, but not to audit the front', Houlden says. 'In addition we have some external assurance on regulatory measures and some internal assurance on bonusable measures. We think it would be a bad idea for the IIRC to require formal assurance of integrated reports. The cost of that additional assurance would probably more than double our audit fee and so that would be negative value to my shareholders, because they would effectively be paying it'.

#### APPLYING TECHNOLOGY

One area of experimentation among integrated reporters is the extent to which they use new technology to enhance their integrated reporting. Of the reports reviewed, 51% (23 out of 45) referred users to a microsite or section of the corporate website for supplementary information. Although downloadable PDF documents are the most common feature of such sites, for some organisations this is an opportunity to include interactive content.


United Utilities, for example, makes its integrated report available both in PDF

form and in an online format. 'The online format is a bit different from the paper format', Houlden says. 'We have lots of cross-references to videos, audios and other relevant reports, such as the corporate responsibility report, our regulatory reporting and so on'.

Better use of technology is the next step in FMO's integrated reporting journey. 'We are now working to move from offline to online first', Bakker says. 'We want to have improved accessibility. At the moment we have a PDF, which works, but we feel we can much better serve the needs of different types of readers by providing online reports where they can select for themselves the different levels of detail'. This will be introduced for the 2017 annual report, although readers will still be able to download a PDF. The introduction of the European Single Electronic Format,<sup>2</sup> requiring companies listed on regulated markets in the EU to publish annual financial reports in a structured electronic format with XBRL tagging from 1 January 2020, could push more European companies to experiment with digital reporting over the coming years.

In South Africa, Eskom developed an app for tablets in 2016, which included formats such as video. However, this was not continued in 2017. Koch notes that it was quite labour intensive to develop, especially to source and add additional content, and the rewards are dependent on effectively promoting it to stakeholders. 'It will however be reconsidered in future, as technology is definitely the way to go', she says.

<sup>2</sup> ESMA, 'European Single Electronic Format' [website information] <<https://www.esma.europa.eu/policy-activities/corporate-disclosure/european-single-electronic-format>>, accessed 20 February 2018.



## 5. Linking strategy and performance to the capitals

### OBSERVATIONS FROM THE REPORT REVIEWS

The <IR> Framework describes capitals alternately as ‘the resources and relationships used and affected by an organisation’ (Executive Summary) and ‘stocks of value that are increased, decreased or transformed’ (para 2.11) through the organisation’s activities. It identifies six kinds of capital: financial, human, social and relationship, manufactured, natural and intellectual.

Through integrated reporting, the IIRC aims to encourage management and boards to exercise stewardship over these different drivers of value, safeguarding the non-financial as well as financial resources. The <IR> Framework also emphasises the fact that the capitals are interdependent – using up one form of capital may increase another. For example, upgrading a company’s digital capacity could increase the company’s manufactured and intellectual capital (in the form of new servers, software and ways to share knowledge) in return for a reduction in financial capital (the financial investment) and human capital (through the replacement of some manual roles with automated processes). Depending on whether the digital transformation is successful or not, there may also be an impact on social and relationship capital (customer goodwill gained or lost). Therefore, in setting their organisations’ strategies and directing their operations, boards need to balance the trade-offs between different capitals carefully.

The <IR> Framework states that an integrated report should describe how an organisation’s strategy relates to its use of and effects on the capitals (Section

3A). It also says that organisations should, as part of reporting on their performance, describe their ‘outcomes in terms of effects on the capitals’ (para. 4.30). These should cover both positive and negative effects. The <IR> Framework further suggests that reporting could take the form of ‘KPIs that combine financial measures with other components (eg the ratio of greenhouse gas emissions to sales) or narrative’ (para. 4.32).

This year’s review found that most reports do talk about a wide range of capitals. Over four-fifths (80%) report on five or more capitals. Nonetheless, the linkage between the discussion on capitals and the organisation’s strategy and performance is weak. For example, commentary on the capitals is usually given with little reference to the organisation’s overall strategy, and outputs and outcomes in terms of capitals are presented discretely – with a separate section for each relevant capital. In other words, many organisations struggle to tell a really integrated story about how these different resources combine and interact to deliver the organisation’s strategy.

### WHAT CHALLENGES DO COMPANIES IDENTIFY?

#### Clarifying and presenting the business model

Summarising how an organisation uses the various capitals to implement its strategy can be challenging. ‘We spend a lot of time thinking about the business model diagram’, Russ Houlden of United Utilities says. ‘The way we have drawn it has evolved. We have had three versions [over the last three years]. Trying to get everything onto one page is the biggest challenge but it’s good because it forces us to cut through complexity’.

Despite the challenges of applying the <IR> Framework’s concept of capitals, Job Bakker sees benefits from clarifying or formalising the organisation’s business model. FMO encourages innovation, but this can make it hard to check that there is a ‘common denominator’ running through all the various initiatives under way. ‘Making your business model more explicit helps to have more structured decision making’, Bakker says.

#### Quantifying value creation outcomes

Houlden does not see any specific barriers to narrative reporting on how strategy affects the capitals. Even so, he does see challenges in quantifying environmental and social impacts. ‘Environmental accounting and sustainability accounting today are at an equivalent stage of development as accounting was at the time of the Merchant of Venice’, he says. ‘The Merchant of Venice invented double-entry bookkeeping and it then took 500 years for us to get to international accounting standards’. These new forms of accounting therefore also need time to develop. ‘There are lots of people involved in this space with lots of different ideas’, Houlden says. ‘There are no accounting standards and people will struggle for the next few years to produce anything meaningful that everybody can apply’.

As an example, FMO’s Job Bakker notes that many organisations report on the number of employees, but he believes this only partly covers the concept of human capital. ‘Having concrete indicators for all the capitals that are relevant to our industry is the holy grail’, he says. However, in the absence of those concrete indicators, Bakker ‘would for now rather have a more qualitative

The past year has seen encouraging developments, with a myriad mostly business-driven initiatives aiming to find a way to quantify value creation outcomes meaningfully.

discussion of the capitals than come up with indicators that do not reflect the actual value creation process'. He adds: 'One of the reasons we adopted integrated reporting was because of integrated thinking. A huge part of the added value of integrated thinking is the concept of how you as a company create value through your business model'.

Aegon's Marc van Weede agrees that introducing quantitative analysis is difficult. 'You are often dealing with impacts that are not easily quantifiable', he says. 'Say one of our impacts on society is that we help people with financial security. So far we have a fairly basic indicator of that: how much we pay out in claims and benefits. But how much do those payouts really contribute to people's financial security and how much freedom does that give them to undertake other activities or lead a life without suffering poverty? More development and more thinking are needed on this whole area of impact measurement. Coming up with indicators that are not too theoretical, but have practical value, is one of the remaining challenges'.

Novartis has been working on financial, environmental and social impact valuation with the support of external experts and industry peers for the past two years. 'We are trying to measure in quantitative terms – putting a dollar value on it – the impact both positive and negative of not only the financial activities of the company, but the environmental and social activity', says Charlie Hough, Vice President and global head of corporate responsibility strategy and stakeholder engagement at Novartis. 'What's the positive and negative incremental value of our mission and our impact on society? Not just from a profit and loss standpoint,

but the impact of the taxes we pay, the wages we pay – and trying to quantify the total effect of the company'.

Novartis first attempted to measure the full financial, environmental and social impact of its activities in two countries – China and Kenya. Its latest annual report, for the year ended December 2017, contains figures for the company's global financial and environmental impact. 'Social impact is still a challenge for us', Hough says. 'We are still developing different methodologies because valuing the social impact of some of our medicines – given the diversity of our medicines – is not easy to do. We are still working with experts and experimenting'.

Carrie Scott adds that Novartis is also benefiting from knowledge-sharing with its counterparts from industry peer Novo Nordisk, which was featured in ACCA's 2016 *Insights into Integrated Reporting* report: 'We have a good relationship with the reporting team there, and we are exchanging information with them on reporting trends and challenges. We are very much in the same mindset. Inside Novartis, we're also working with investor relations, corporate strategy and finance colleagues to determine non-financial KPIs for reporting'.

The past year has seen encouraging developments, with a myriad mostly business-driven initiatives aiming to find a way to quantify value creation outcomes meaningfully. Novartis' 2017 Corporate Responsibility Performance Report references (page 14) one such initiative – the Embankment Project,<sup>3</sup> launched jointly by the Coalition of Inclusive Capitalism and EY in June 2017 to test a framework for measuring and reporting on the value that businesses create for their stakeholders.

### Embedding the capitals into decision making

At UniCredit, all the capitals except for manufactured capital are strategically relevant to the business. Giuseppe Zammarchi explains: 'The human capital is the engine for everything. It's always on the radar screen of top management... Intellectual capital is again very important – we rely a lot on ideas and innovation in order to be aligned with changes in society and customer behaviours. Natural capital is affected through the use of energy, for example to run data centres. The interaction between all these things creates some opportunities for the bank'. For example, offering head office staff the opportunity to work from home one day a week reduces the carbon emissions produced by people commuting to work, and also boosts financial capital as office space is required for only 90% of the total workforce at any time.

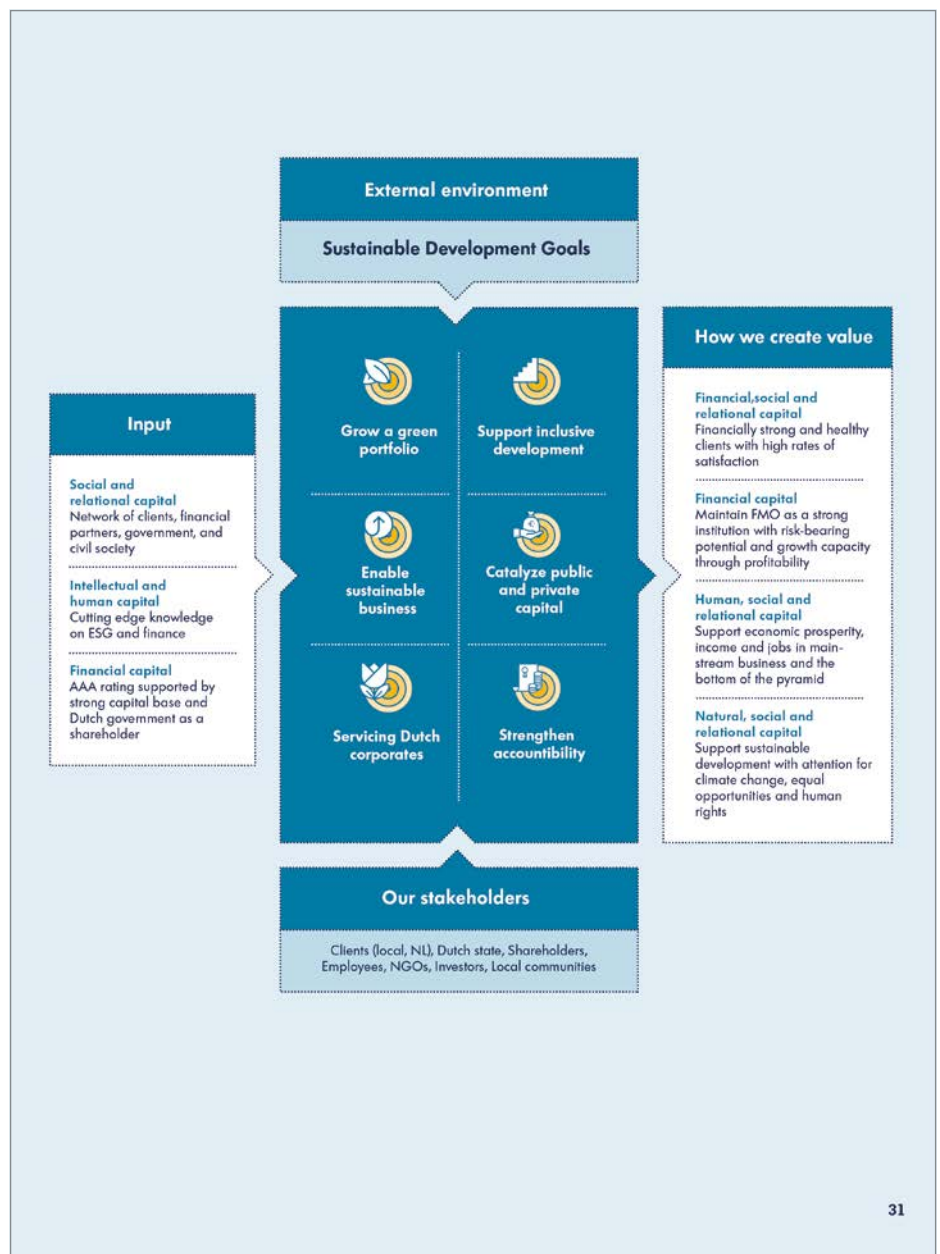
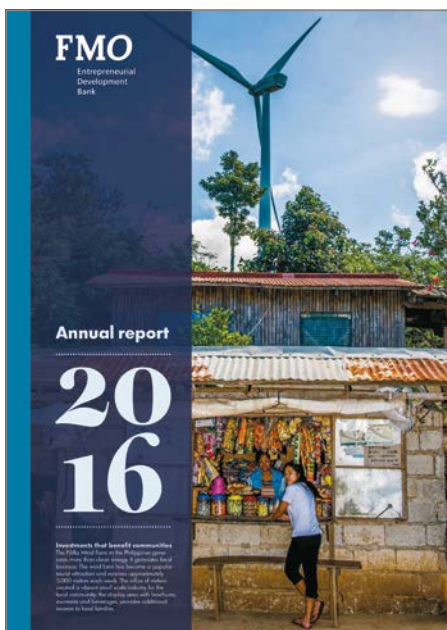
Zammarchi suggests that multi-capitals thinking is more embedded in some teams than in others. 'There are some [areas of the bank] where the impact of capitals can be found and described, but [it] probably was not the first thought of the management when they developed those initiatives', Zammarchi says. Nonetheless, over time, integrated reporting could encourage this thinking. 'The fact that we have interactions with so many colleagues who are providing data for the report, reviewing the data... that has created much more knowledge about what we are doing, how we do it and why we are doing it this way', Zammarchi says. 'So talking about capitals is growing and... hopefully will become the only way we talk at a certain point. That will require more time'.

3 Inclusive Capitalism, 'Embankment Project for Inclusive Capitalism' [website] <<https://www.inc-cap.com/embankment-project/>>, accessed 20 February 2018.

FMO's Annual Report 2016 contains a clear and simple business model, which integrates capitals and stakeholder needs with the strategic objectives of the organisation.

**PRACTICAL APPROACHES**

FMO's Annual Report 2016 (page 31)<sup>4</sup> contains a clear and simple business model, which integrates capitals and stakeholder needs with the strategic objectives of the organisation. It also sets FMO's value-creation outcomes squarely against the context of the United Nations' Sustainable Development Goals,<sup>5</sup> adopted by governments around the world from September 2015.



<sup>4</sup> Weblinks to all best practice examples cited in this report are provided in Appendix 4.

<sup>5</sup> United Nations (n.d.), 'Sustainable Development Goal' [website] ,<<http://www.un.org/sustainabledevelopment/sustainable-development-goals/>>, accessed 20 February 2018.



UniCredit's 2016 Integrated Report includes a section on each of its relevant capitals, clearly identifying the firm's stocks of capital, headline results, community impacts and priorities for the coming year.

UniCredit's 2016 Integrated Report includes a section on each of its relevant capitals, clearly identifying the firm's stocks of capital (contributors of value), headline results, community impacts and priorities for the coming year.

The connectivity between different capitals is illustrated through case studies, such as, on pages 48 and 49, the case study on its 'Open' programme – a major turnaround initiative in Italy involving a review of the bank's distribution and service model, designed to enhance customer experience and nurture innovation. The case study is an effective and innovative way of demonstrating connectivity, both between different capitals and between the past and the present (through the presentation of results in comparison with 2015).



## Connectivity - case studies

*Value is created from the connections made between a wide range of factors. An understanding of how the company's capitals, material topics for stakeholders, strategic pillars and business model are interconnected and interact is key to properly assessing our value creation process over time.<sup>1</sup>*

### Transform our operating model in Italy

Digitization has increased the commoditization of banking and finance products, especially in the individual clients segment. Customers expectations of their banks are rapidly changing, creating the possibility that customers will access some of their products and services from different providers. This is a threat to traditional commercial banks, but it is partially offset by the opportunity to gain market share.

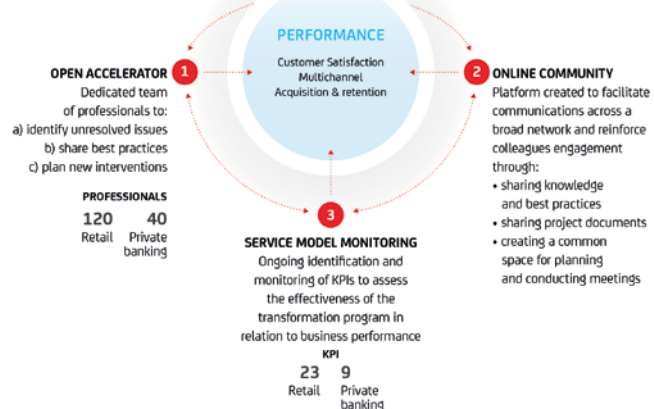
We consider the changing behaviors of our clients an incentive to further transform our network and the way we serve them. Our objective is to make sure we are slightly ahead of the curve, responding to new trends and improving the quality of what we do on an ongoing basis. In 2013, UniCredit launched a major turnaround program in Italy, where the Group has

more than 7 million retail customers and 12 percent market share.<sup>2</sup> This program, *Open*, encompassed a significant review of our distribution and service model. Its purpose was to enhance customer experiences and nurture the kind of innovation that not only creates value for our customers but also optimizes our cost to serve.

Thanks to this program, we have significantly transformed our network by rebalancing the combination of digital and physical interactions we have with our customers.

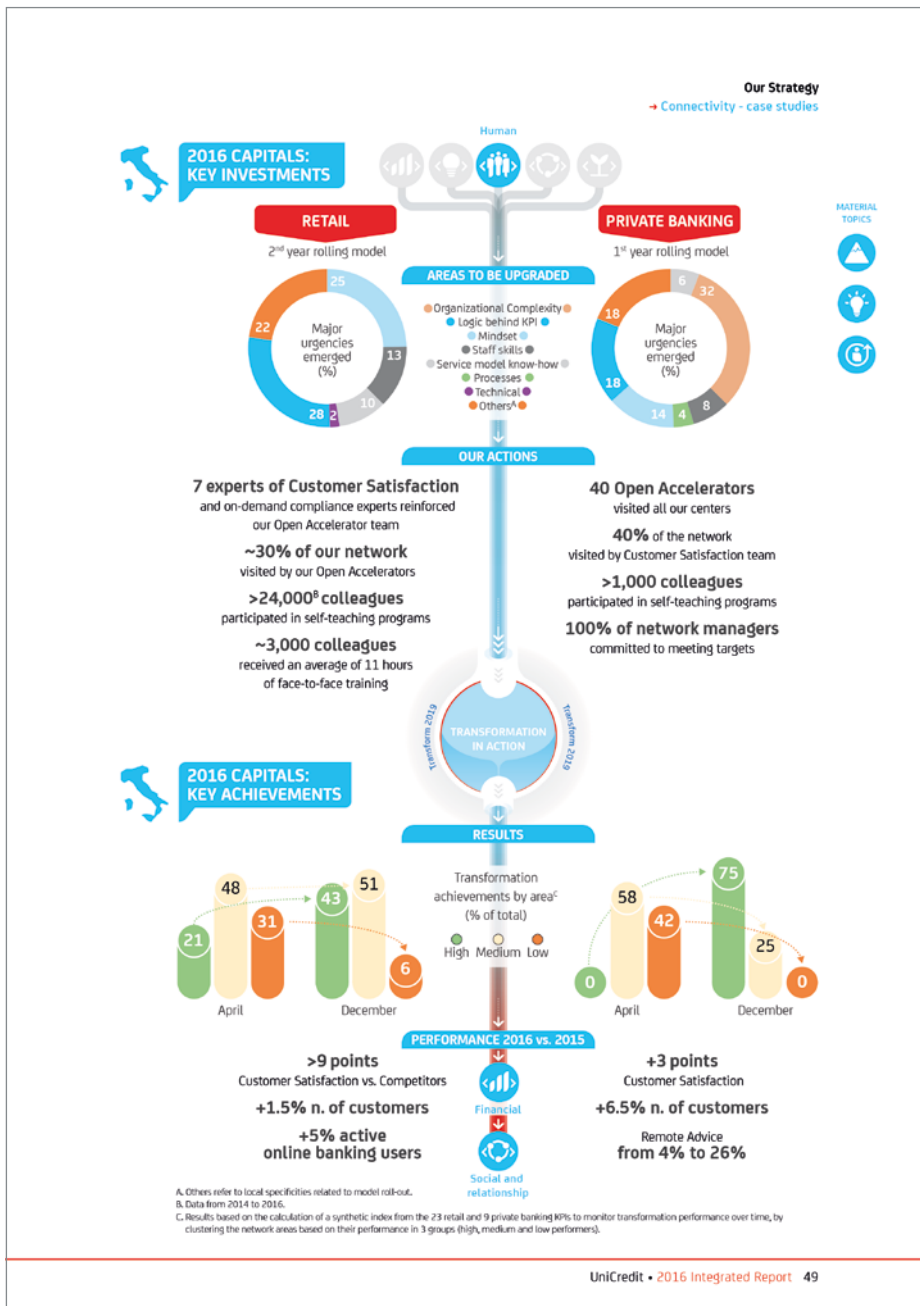
To speed up the pace of change within our organization, we leverage the existing knowledge in our intellectual capital. In addition, we make significant investments in enhancing the skills of our people, who represent our human capital. The *Open in Action* project, which has been running for the past few years, was designed to facilitate the transformation of both the retail and the private banking segments. The project utilizes an integrated, three-pronged approach that consists of dedicated professionals team, an online community and a service model monitoring the program's progress. Together, this approach amplifies the impact of the changes we make, and assures the achievement of our performance targets. The release of the strategic plan, *Transform 2019*, served to confirm and reinforce this approach to transforming our operating model.

#### TRANSFORMATION IN ACTION: OUR APPROACH



1. Refer to <http://integratedreporting.org/resource/international-framework/> for more information about Connectivity concept.  
2. Households loans and deposits, August 2016.

Only discuss the capitals that are relevant to how your organisation creates value.



**GOOD PRACTICE IDEAS**

- Only discuss the capitals that are relevant to how your organisation creates value, which is what the <IR> Framework asks for. Focus on a small number of key resources, explain why they are important to your organisation’s success and demonstrate how the board exercises stewardship over them.
- Dedicate some time to working with the board and executive management to formalise the organisation’s business model: make it as concise as possible.
- Encourage the executive management team to consider the effects on key capitals when they make strategic and operational decisions.
- Define what value means for your organisation. This may not be quantifiable in the first instance, but don’t let this hold you back: the definition will help you and the report’s users to understand how value is enhanced or reduced.

## 6. Tying strategy to value creation over the short, medium and long term



### OBSERVATIONS FROM THE REPORT REVIEWS

The reports reviewed this year indicate that organisations are relatively good at explaining both how the entity creates value for itself and how it creates value for others. They are good at setting out their strategy and the context around it. They are generally good at explaining what the organisation does and the circumstances under which it operates. They are less effective, however, at tying strategy to the organisation's ability to create value over the short, medium and long term.

### WHAT CHALLENGES DO COMPANIES IDENTIFY?

#### Short-term management focus

Eskom has a corporate plan that feeds into the strategy section of the integrated report to a great extent. This plan covers five years, but Koch admits that 'the current year is probably where 90% of the focus lies, which is not ideal in a business with a lifecycle of several decades'. She explains: 'People are hesitant to look into the future, and the further into the future it gets, the more difficult it becomes. When we talk about the longer term it's probably five-plus years, instead of 20 to 30 years'.

Last year UniCredit presented a three-year plan, called Transform 2019, setting out specific targets for the years up to and including 2019. 'But our management has always been very clear in saying to journalists and market participants that our strategy doesn't stop in 2019, so what we are doing now is to make sure we also have long-term value creation well beyond 2019', Giuseppe Zammarchi says. UniCredit was the first bank to give a full disclosure of the impact on the bank's capital ratios of new regulation coming into force in 2019. 'This is a clear example

of how thinking in terms of value creation, and thinking long term, can be applied to communication with the markets and your stakeholders', Zammarchi says.

#### Separation of strategy and reporting teams

In theory, clear reporting on how the organisation plans to create value over time could help to reinforce integrated thinking and influence future strategy development. However, this requires traditionally distinct functions to work closely together. In Eskom, the strategy development and reporting teams are separate, and as a result, the influence of the integrated reporting team on strategy development is quite limited.

At FMO, Bakker says that integrated reporting and integrated thinking have become embedded in the organisation, and this has been helped by structural factors. As senior planning and control officer, 'I am partly working on integrated reporting but am also in the strategy department', Bakker explains. 'So I spend a lot of my time on strategy development, with a number of other people. Together we are combining integrated reporting and integrated thinking'.

#### Commercial sensitivity

Commercial sensitivity can be a challenge in trying to tie strategy to the ability to create value over the short, medium and long term. 'Inevitably you will have some commercially sensitive things but you are just a bit careful about how you talk about them', United Utilities' Russ Houlden says. 'In our case it might be what's going to happen in the next price review and the price review after that, or what's going to happen in politics'. Every organisation will have its own sensitive issues, depending on its sector and activities, Houlden believes. 'Generally these are things that

investors would be interested in, but they are also things that competitors or regulators would be interested in and may be able to use against you. So you are trying to get across the important points, without risking negative consequences'.

#### Articulating value creation and strategic aims

United Utilities' 2017 annual report (page 13) identifies eight key features that make it attractive to investors, and two areas of competitive advantage (systems thinking and prudent financial risk management). 'Investors found this articulation of our competitive advantage helpful', says Houlden.

Articulating strategic aims can help to keep the business on track, Houlden suggests. He refers to United Utilities' statement that its strategy is to create sustainable value by giving customers the best service, at the lowest sustainable cost, in a responsible manner. This provides internal discipline when new initiatives or actions are being considered. 'It's a sort of beacon', Houlden says. 'You leave the beacon there and you know where you are going because that's the direction you have told people you are going in. If you don't have the beacon, it's very easy for pet projects to take you off course'.

#### The need to gain feedback and learn from experience

It can take time to develop a real understanding of how an individual organisation creates value, and then how to convey that in an integrated report. Aegon's reporting in this respect has evolved over the years. 'The biggest change is that we now put more emphasis on things like how the business creates value, who it creates value for, in what way', Marc van Weede says. 'I don't think we had those elements very strongly

BASF's Report 2016 defines what 'value added' means for its organisation, and then shows how different stakeholder groups benefit from the value added.

in the early reports. That certainly has evolved over time – partly in response to feedback from stakeholders, partly due to the evolution of our thinking'.

**PRACTICAL APPROACHES**

BASF's Report 2016 (page 3) defines what 'value added' means for its organisation, and then shows how different stakeholder groups benefit from the value added. This is shown right at the start of the report, before the contents page – thus demonstrating a strong focus on value creation. Later on in the report (pages 26 and 27), short and long-term goals (covering economic, employees, product stewardship, energy, etc.) are shared, together with short-term and long-term opportunities and risks, giving a clear insight into management's evaluation of the future environment for BASF.



**BASF Group 2016 at a glance**

**Economic data**

	2016	2015	Change in %
Sales	57,550	70,449	(18.3)
Income from operations before depreciation and amortization (EBITDA) and special items	10,327	10,506	(1.7)
EBITDA	10,526	10,649	(1.2)
Amortization and depreciation <sup>1</sup>	4,251	4,401	(3.4)
Income from operations (EBIT)	6,275	6,248	0.4
Special items	(34)	(491)	93.1
EBIT before special items	6,309	6,739	(6.4)
Financial result	(880)	(700)	(25.7)
Income before taxes and minority interests	5,395	5,548	(2.8)
Net income	4,056	3,967	1.7
EBIT after cost of capital	1,136	194	485.6
Earnings per share	4.42	4.34	1.8
Adjusted earnings per share	4.83	5.00	(3.4)
Dividend per share	3.00	2.90	3.4
Research and development expenses	1,863	1,953	(4.6)
Personnel expenses	10,165	9,962	1.8
Number of employees	113,830	112,435	1.2
Assets	76,496	70,836	8.0
Investments <sup>2</sup>	7,258	6,013	20.7
Equity ratio	42.6	44.5	–
Return on assets	8.2	8.7	–
Return on equity after tax	13.3	14.4	–
Net debt	14,401	12,935	11.3
Cash provided by operating activities	7,717	9,446	(18.3)
Free cash flow	3,572	3,634	(1.7)

<sup>1</sup> Amortization of intangible assets, depreciation of property, plant and equipment, impairments and write-ups  
<sup>2</sup> Additions to intangible assets and property, plant and equipment (including acquisitions)

**Value added 2016<sup>3</sup>**

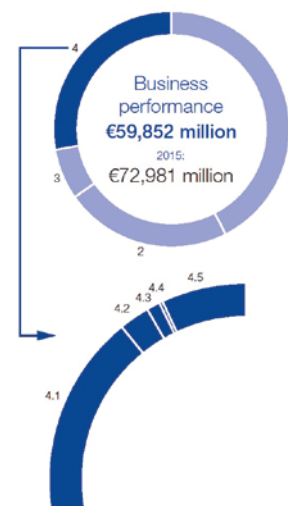
**Creation of value added (million €)**

	2016	2015
Business performance	59,852	72,961
1 Cost of raw materials and merchandise	(25,450)	(37,323)
2 Services purchased, energy costs and other expenses	(13,658)	(14,787)
3 Amortization and depreciation	(4,251)	(4,401)
4 Value added	16,493	16,470

**Use of value added**

	2016	2015
4.1 Employees	61.6%	60.6%
4.2 Government	8.6%	9.4%
4.3 Creditors	4.0%	3.9%
4.4 Minority interests	1.2%	1.9%
4.5 Shareholders (dividend and retention)	24.6%	24.2%

<sup>3</sup> Value added results from the company's performance minus goods and services purchased, depreciation and amortization. Business performance includes sales revenues, other operating income, interest income and net income from shareholdings. Value added shows the BASF Group's contribution to both private and public income as well as its distribution among all stakeholders.



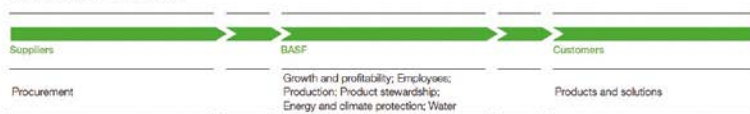
Short and long-term goals are shared, together with short-term and long-term opportunities and risks, giving a clear insight into management's evaluation of the future environment for BASF.

## Goals

We carry out our corporate purpose, "We create chemistry for a sustainable future," by pursuing ambitious goals along our entire value chain. In this way, we aim to achieve profitable

growth and take on social and environmental responsibility. We are focusing on issues through which we as a company can make a significant contribution.

### Goal areas along the value chain



### Procurement

	2020 Goal	Status at end of 2016	More on
Assessment of sustainability performance of relevant suppliers <sup>1</sup> according to our risk-based approach; development of action plans where improvement is necessary	70%	32%	Page 92

<sup>1</sup> We define relevant suppliers as those showing an elevated sustainability risk potential as identified by risk matrices and with respect to corresponding country risks. Our suppliers are evaluated based on risk due to the size and scale of our supplier portfolio.

### Growth and profitability

As determined in 2015, our aim for the years ahead is, on average, to grow sales slightly faster and EBITDA considerably faster than global chemical production (excluding pharmaceuticals; 2016: 3.4%), and to earn a significant premium on our cost of capital. Moreover, we strive for a high level of free cash flow each year, either raising or at least maintaining the dividend at the prior-year level. The goals for sales and EBITDA are based on the 2015 figures, excluding contributions from the business disposed of in the asset swap with Gazprom in September 2015.

	2016	Change since 2015
Sales	€57.6 billion	(4.6%) <sup>2</sup>
EBITDA	€10.5 billion	5.3% <sup>2</sup>
Dividends per share paid out	€2.90	€0.10
Premium on cost of capital	€1.1 billion	
Free cash flow	€3.6 billion	

<sup>2</sup> Baseline 2015, excluding business transferred to Gazprom

For more on our Results of Operations, see pages 50 to 54

### Employees

	2021 Goal	Status at end of 2016	More on
Proportion of women in leadership positions with disciplinary responsibility	22–24%	19.8%	Page 43
<b>Long-term goals</b>			
International representation among senior executives <sup>1</sup>	Increase in proportion of non-German senior executives (baseline 2003: 30%)	36.4%	Page 43
Senior executives with international experience	Proportion of senior executives with international experience over 80%	84.6%	Page 43
Employee development	Systematic, global employee development as shared responsibility of employees and leaders based on relevant processes and tools	The project has been implemented for around 78,150 employees worldwide.	Page 42

<sup>1</sup> The term "senior executives" refers to leadership levels 1 to 4, whereby level 1 denotes the Board of Executive Directors. In addition, individual employees can attain senior executive status by virtue of special expertise.

### Production

	2020 Goal	Status at end of 2016	More on
Reduction of worldwide lost time injury rate per one million working hours	<0.5	1.4	Page 98
Reduction of worldwide process safety incidents per one million working hours	<0.5	2.0	Page 98
Health Performance Index	Annual goal	<1.0	Page 98

### Product stewardship

	2020 Goal	Status at end of 2016	More on
Total assessment of products that are sold in quantities of more than one metric ton per year worldwide	>90%	75.6%	Page 103

### Energy and climate protection

	2020 Goal	Status at end of 2016	More on
Coverage of our primary energy demand by introducing certified energy management systems (ISO 50001) at all relevant sites <sup>1</sup>	90%	42.3%	Page 104
Reduction of greenhouse gas emissions per metric ton of sales product (including CR & Gas, baseline 2003)	90%	107.7%	Page 104

<sup>1</sup> The selection of relevant sites is determined by the amount of primary energy used/retail energy prices.

### Water

	2020 Goal	Status at end of 2016	More on
Introduction of sustainable water management at all production sites in water stress areas and at relevant sites (including CR & Gas)	100%	42.5%	Page 107

### Products and solutions

	2020 Goal	Status at end of 2016	More on
Increase the proportion of sales generated by products that make a particular contribution to sustainable development ("Accelerators") <sup>1</sup>	25%	27.2%	Page 30

In its *Annual Report 2017*, Novartis summarised its mission, vision and strategy in an admirably clear and concise way.

In its *Annual Report 2017* (page 17), Novartis summarised its mission, vision and strategy in an admirably clear and concise way, and these underscore the annual report throughout – from the introduction to the report (page 2), which quotes the mission, through to variable CEO and executive committee remuneration, which is based on long-term value creation targets (including innovation and growth targets, page 120). This conveys a very strong sense to report users that innovation is at the heart of Novartis’ strategic advantage.



**STRATEGIC OVERVIEW**  
Our strategy

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## Our strategy

**Science and innovation remain at the heart of our strategy, while our mission and vision are anchored in the important role we play in society. Together, our mission, vision and strategy help guide us through a world that is experiencing rapid advances in technology to deliver better health outcomes for patients and society.**

In an increasingly fragmented research landscape, we are working to break down barriers to collaboration both inside and outside our company to improve our access to the best early-stage science.

### Drive a digital transformation

We are finding new ways to harness the power of digital technology in all aspects of our business – including R&D, sales and operations – to improve effectiveness and efficiency. A particular focus is advanced analytics. Artificial intelligence and other technologies can help us extract insights from vast pools of data from clinical trials, from our daily interactions with physicians, and from other sources.

### Growing areas of healthcare

We will prioritize further steps to reinforce our presence in growing areas of healthcare with unmet needs. We aim to strengthen our position in specific therapeutic areas in innovative medicines (including oncology, cardiology, ophthalmology, and immunology and dermatology), as well as in biosimilars and some specialty generics. Geographically, we see scope to reinforce our presence in some key markets, such as the US and Japan, and in emerging markets that are long-term growth opportunities, such as China.

**Our mission** is to discover new ways to improve and extend people’s lives

**Our vision** is to be a trusted leader in changing the practice of medicine

**Our strategy** is to use science-based innovation to deliver better patient outcomes in growing areas of healthcare

Our mission sums up our company’s reason for being. Our vision is an aspiration to strive for, even as society’s expectations about healthcare are changing. Our strategy describes where we will channel our energy and how we expect to continue creating value for our company, shareholders and society.

We have been consistent in our commitment to science-based innovation. We believe future trends in our industry and society will only increase the importance of innovation leadership.

As we implement our strategy, we have identified key priorities in the areas of innovation, digital technology and scale.

### Further strengthen innovation

Novartis has long been an innovation leader, and we are taking steps designed to ensure we remain one. We continue to maintain our investment in research and development (R&D) at a level that is among the highest in the industry. And we are ruthlessly prioritizing our R&D spending to focus resources on the projects most likely to deliver true innovations with the potential to change the practice of medicine.

We believe future trends in our industry and society will only increase the importance of innovation leadership

Looking ahead, we think success will be driven by our scientific expertise, how well we leverage new technologies to improve productivity, and our ongoing ability to deliver value to our customers and patients.

**Photo** Ioanna Meli, 86, finds plenty to laugh about at her home on Ikaria, a Greek island identified as one of the places in the world where people live the longest. Mrs. Meli has been married to her husband, Yannis, for 70 years. Experts believe family and social activity are two keys to longevity in places like Ikaria, along with low levels of meat eating and smoking, and frequent moderate physical activity.

NOVARTIS

Work cross-functionally with colleagues responsible for strategy and risk management to align reporting with strategy.

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## Executive Committee compensation at a glance (pages 127 to 142)

### 2017 Executive Committee compensation system

Reflecting a strong focus on pay for performance and alignment with shareholder interest, variable pay represents a significant proportion of the package. Outcomes from variable pay elements can vary significantly (from 0% to 200% of the target level), depending on the level of performance achieved.

	Fixed pay and benefits		Variable pay – performance-related		
	Annual base salary	Pension and other benefits	Annual Incentive	Long-term share awards	
				LTPP <sup>1</sup>	LTRPP <sup>2</sup>
<b>Purpose</b>	Reflects responsibilities, experience and skill sets	Tailored to local market practices / regulations	Rewards for performance against key short-term targets and Values and Behaviors	Rewards long-term shareholder value creation and innovation in line with our strategy	
<b>Form of payment</b>	Cash	Country / individual specific	50% cash 50% equity <sup>3</sup> deferred for three years	Equity	
<b>Performance measures</b>	-	-	Performance matrix based on: • Individual balanced scorecard, including financial targets and individual objectives • Values and Behaviors	• Novartis Cash Value Added • Innovation milestones	• Relative TSR vs. global sector peers

<sup>1</sup> LTPP – Long-Term Performance Plan  
<sup>2</sup> LTRPP – Long-Term Relative Performance Plan  
<sup>3</sup> Executive Committee members may elect to receive more of their Annual Incentive in equity instead of cash.

The CEO's Annual Incentive at target is 150% of base salary, his target LTPP is 200% of base salary and his target LTRPP is 125% of base salary. Based on Novartis' compensation guidelines, the other members of the Executive Committee have Annual Incentive targets that range from 90% to 120% of base salary, and have Long-Term Incentives (LTPP and LTRPP) in total that range from 170% to 270% of base salary.

### 2017 CEO pay for performance – outcomes

#### 2017 ANNUAL INCENTIVE – NOVARTIS PERFORMANCE

<b>Deliver financial results</b>	• Group net sales, net income and free cash flow as a % of sales above target
<b>Ensure world-class commercial execution</b>	• Innovative Medicines delivered strong performance: Cosentyx well ahead of target, Entresto in line with expectations, Oncology sales slightly below target • Sandoz sales below target due to pricing pressure in the US
<b>Transform Alcon into an agile medical device company</b>	• Alcon returned to growth with sales and core operating income results ahead of target, and all seven key approvals in innovation projects achieved
<b>Strengthen R&amp;D</b>	• Pipeline milestone targets either achieved or surpassed, including 16 major approvals, 16 major submissions and six FDA breakthrough therapy designations
<b>Improve access to healthcare</b>	• Novartis access to healthcare programs expanded, with agreements now signed in six countries, delivering a portfolio of 15 products for USD 1 per treatment, per month
<b>Create a stronger company for the future</b>	• NTO, NBS and GDD delivered or over-delivered on productivity targets • Compliance, reputation and culture further improved
<b>Overall performance outcome</b>	• Overall performance of the CEO was determined to be above expectations, based on achievements versus the targets set by the Board, and demonstration of the Novartis Values and Behaviors <b>Overall outcome of 125% of target</b>

#### 2015–2017 LONG-TERM INCENTIVES

<b>Long-Term Performance Plan (LTPP)</b>	• Novartis Cash Value Added outcome of 113% of target (75% weighting) • Key innovation milestones outcome of 115% of target (25% weighting) <b>Overall outcome of 114% of target</b>
<b>Long-Term Relative Performance Plan (LTRPP)</b>	• Annual Total Shareholder Return (TSR) in USD was 20.4%. Absolute TSR growth in USD was 0.1% over the last three years. Relative performance in USD over the three-year performance cycle compared to peers was rank No. 12 out of 13 companies <b>Overall outcome of 0% of target</b>

### GOOD PRACTICE IDEAS

- Find effective ways of engaging with the board, the executive team and key external stakeholders to add value to the reporting process.
- Work cross-functionally with colleagues responsible for strategy and risk management to align reporting with strategy: an integrated strategy and reporting steering committee may help.
- Engage with key internal and external stakeholders to define a purpose or mission statement that is clear and concise. This mission statement can form the basis of both strategic planning and integrated reporting.
- Consider including a value-added statement up front in your report, to clearly explain what your organisation defines as value.



## 7. Outlook

### **OBSERVATIONS FROM THE REPORT REVIEWS**

The <IR> Framework identifies 'outlook' as one of the core content elements in an integrated report. An integrated report should answer the question: 'What challenges and uncertainties is the organisation likely to encounter in pursuing its strategy, and what are the potential implications for its business model and future performance?' (para.4.34).

Outlook is related to another forward-looking content element in the <IR> Framework: risks and opportunities. The <IR> Framework states that an integrated report should answer the question: 'What are the specific risks and opportunities that affect the organisation's ability to create value over the short, medium and long term, and how is the organisation dealing with them?' (para. 4.23). Interestingly, although the <IR> Framework refers to risks and opportunities in equal measure, the reports reviewed scored much more highly on risk than on opportunities.

It seems that some concerns about disclosing commercially sensitive information – and, in some jurisdictions, the risk of legal liabilities arising from making forward-looking statements – could be making organisations hesitant about discussing the future.

Nonetheless, many reports cover a reasonable timeframe. For example, 53% of reports reviewed this year consider the long term (defined as four years ahead or more). The issue therefore is more about content than time span. Many organisations are willing to discuss their expectations about the external environment in the next few years or even 10 years ahead, but very few discuss what that would actually mean for the organisation, for example, its future opportunities.

### **WHAT CHALLENGES DO COMPANIES IDENTIFY?**

#### **Management concerns**

In the online survey of <IR> Business Network participants, 80% of respondents did not think that concerns about director liability affected the statements made by directors and board members in their integrated reports. This is encouraging.

Nevertheless, management may have other related concerns. The team at Eskom finds that some people in the business are hesitant about talking about the future – possibly because by commenting on some future potential action under their control, they might be seen as committing to that action. Koch doesn't see this as a legitimate fear, however. 'That's why we have the forward-

looking information disclaimer', she says. This makes it clear that reported information is based on current knowledge and circumstances and, if things change, so might the organisation's actions. On the other hand, some individuals may be concerned about being held accountable for something they can't control.

Her colleague Martin Buys sees the fact that some people in the business have not made the mental shift to seeing reporting as a future-focused activity as part of the challenge. 'Everybody is used to reporting on the past', he says. 'Integrated reporting forces you to be more forward-looking, and I don't think everybody has made that shift yet'. Encouraging forward-looking thinking certainly requires support from top leadership.

UniCredit's Giuseppe Zammarchi acknowledges that 'making sure you don't give out too much always worries every company management'. Even so, from his previous experience in investor relations, he says that: 'giving details and transparency is always a plus, provided you never give out any proprietary trademark or intimate secrets on how you deal with new opportunities'. Explaining how and why indicators are important



**‘It’s right that your annual report should tell your shareholders how you are creating competitive advantage. But it’s not right that you tell your competitors how to beat you.’**

and why management discusses them on a monthly basis sends two important messages: first, the commitment of management to hit these targets; and second, the need for staff in charge of specific indicators to ‘pay more attention and be more engaged in doing a good job, because they know it’s going to be on the CEO’s desk’. An integrated report that is transparent about future objectives also gives external parties (such as, in UniCredit’s case, rating agencies) more confidence in the organisation, because it shows ‘how much we value transparency’, Zammarchi says. ‘That supports the credibility and viability of the company’.

### **Sectoral factors**

For some organisations, the environments in which they operate may be particularly unstable or uncertain, creating even greater challenges when reporting on their outlook. As a development bank, FMO invests in private businesses in developing countries, economies that are often volatile. ‘One of our challenges is to capture the context in which we operate,’ Bakker says. ‘There’s quite a level of uncertainty. There will always be countries that are not going to perform the way you expect them to, but you don’t know which ones. Sometimes you can predict [some event], but the timing and impact is difficult to predict. This context presents a dilemma on how to include targets.

‘On the one hand, we want to be transparent and communicate our targets for next year. On the other hand, we don’t want to say there’s quite a chance we will overshoot or not meet our targets’.

United Utilities is a strong reporter of outlook. Operating in a regulated sector may be an advantage here, because the company has to think about business plans five years into the future. ‘In general terms we give a lot of forward-looking information because we have a five-year plan essentially agreed with our economic regulator for prices’, says Houlden. ‘So it’s not a problem for us to look forward five years’. Under the UK’s regulatory system, before the start of each five-year period, companies submit their business plans to regulator Ofwat (the Water Services Regulation Authority), which then agrees the prices each company can charge its customers across the period. This makes it possible for the company to give clarity about its dividend policy for the next five years – ‘it’s not quite a commitment – but it’s as close as you can get without...being a formal commitment’, Houlden says. The annual report also makes forward-looking statements for up to 25 years in relation to the company’s Water Resource Management Plan, which sets out the investment needed to ensure that the company has sufficient water to continue supplying its customers.

### **Fear of crystallising risks**

Reporting on United Utilities’ future risks is not necessarily straightforward. ‘It can get trickier in the risk section because you are not talking about what your plan is; you are talking about things that could mess up your plan’, Houlden explains. ‘There are some things where, by writing it down, you can make the risk more likely to happen’, he says. ‘That’s where we have to be quite careful. For example, if a risk was that the regulator would set a lower cost of capital, just writing it down might encourage them to set a lower cost of capital. So we prefer not to be too explicit in such areas. Similarly, discussing potential government interventions in detail is not something we would tend to do unless there is already a public debate in progress. That’s not to say we don’t talk about them – we do’. But the company is careful about how it raises issues if discussing them could ‘magnify a risk in people’s minds or magnify it in reality’.

There is a ‘subtlety’ required when deciding what to say, Houlden comments. ‘Our systems thinking is creating competitive advantage so we talk about it because it’s right that your annual report should tell your shareholders how you are creating competitive advantage. But it’s not right that you tell your competitors how to beat you. You might give some examples, you might have some concepts, but you don’t tell them exactly how to copy you’.

In its *Annual Report* for 2017, United Utilities reports its key planning milestones through to 2040, as part of its business model discussion, giving measurable targets.

**PRACTICAL APPROACHES**

In its *Annual Report* for 2017 (pages 26 and 29), United Utilities reports its key planning milestones through to 2040, as part of its business model discussion, giving measurable targets. A consistent vision informs its 25-year, 5-year and 1-year plans.



**Our business model**

**Planning – key milestones**

- 2017** — Our non-household retail JV, Water Plus, was operational and ready for the market opening to competition
- 2020** — Over 90 per cent of meters will be automatically read  
 We will reduce, by more than 40 per cent, the number of properties flooded internally by sewage
- 2020+** — We will continue to improve bathing waters to at least 'sufficient' or 'good' status
- 2025** — We will extend our integrated water supply network into West Cumbria
- 2027** — We will improve all inland rivers to be at least 'good' status
- 2030** — We will work with others to achieve 'Blue Flag' beaches along our coastline
- 2040** — We will serve 600,000 more households in the North West  
 We will install 3 million extra water meters, covering 76 per cent of households



**Planning cycles**

We have structured our business in line with Ofwat's four distinct price control areas:

- › Wholesale water;
- › Wholesale wastewater;
- › Household retail; and
- › Non-household retail.

The non-household retail area is now subsumed within our joint venture with Severn Trent, Water Plus. While we can influence it, we cannot control it. It is not part of our consolidated group, therefore it does not form part of our group's business model.

The three business areas within our business model (wholesale water, wholesale wastewater, and household retail) undertake both long-term and shorter term planning to identify how they can best deliver their outcomes. We adopt an integrated approach, which considers a whole range of stakeholders including customers, investors, the environment, our employees and local communities. These plans take into account the internal and external factors described on pages 18 to 24. Underpinning our approach to planning, we undertake a cycle of continuous assessment using KPIs, and other performance measures, which helps us formulate our future improvement plans for our various stakeholders.

**Wholesale business areas**

All of the group's RCV, of just over £10 billion, sits within the wholesale water and wholesale wastewater business areas, and we are allowed to earn an annual return on this asset base on the basis of an industry-allowed cost of debt and equity set by Ofwat. Allowed costs for both of these wholesale price controls are determined by Ofwat using its totex cost assessment models. Our cost performance against our allowed cost of debt and totex will determine how much outperformance or underperformance we generate.

**Retail business areas**

Allowed costs within the household retail price control are determined using a water industry average cost to serve approach, rewarding companies who are able to achieve costs below the industry average. The opening of full competition in the non-household retail price control from 1 April 2017 provides a strong incentive for water companies to deliver efficiencies and service improvements in that area.

### Household retail

Continue to improve the customer experience by being more proactive with customers, anticipating problems before they materialise and improving our communication channels so that we are easier to do business with.

Reduce further the number of customer complaints and resolve them whenever we can, avoiding the need for complaints to be referred to the Consumer Council for Water.

Reduce the debt burden on the company and its customers by engaging with those who are struggling to pay, helping them return to sustained payment behaviour. We are extending our options for assistance to hard-pressed customers, including the social tariff, and we remain committed to contributing to the United Utilities Trust Fund, which has proven effective in helping customers in difficulty return to regular payment.

Reduce the cost to serve our customers through systems and process improvements. This is particularly important under the new price control methodology which uses an industry average retail cost to serve to determine part of customer bills.

### Planning 1 year

Each financial year, we develop a business plan which is approved by the board. This sets our annual targets which are designed to help deliver further improvements and move us towards achievement of our five-year goals.

Our business plan covers a broad range of measures across the three strategic themes: **The best service to customers**, **at the lowest sustainable cost**, **in a responsible manner**.

#### Performance monitoring

Senior management has quarterly business review meetings with the executive directors to monitor and assess our performance against these measures, helping to ensure that we are on track to deliver our targets.

#### Performance measurement

At the end of every financial year, our performance is assessed against these measures and this determines employees' annual bonuses right through the organisation. As well as annual targets, our directors are assessed against three-year performance, covering total shareholder return, sustainable dividends and customer service, through long-term incentive plans.

Details of the 2016/17 annual bonus and vested long-term incentive plans for our executive directors are shown on pages 99 to 101 respectively within the remuneration report.

 Read more about [KPIs](#) on pages 31 to 33

The diagram below shows how our strategic themes flow through each planning cycle and help us work towards our vision.





In its 2016 *Corporate Social Responsibility Report* (page 19), Taiwan-based telecoms company Far East Tone addresses not only the negative impacts, but also opportunities related to each of its risk factors. These then inform the detailed response strategies that are also set out on the same page.

Overview of Operational Development Strategy   Operating Environment and Materiality   4G Business Strategy and Value   Sustainable Governance   19			
▶ 2.1 External Environment Analysis   2.2 Stakeholder Engagement   2.3 Materiality Analysis			
2.1.3 Critical Corporate Sustainability Risks			
Risk factors	Impacts	Opportunities	Response Measures
<p><b>Technology Development and Digital Convergence</b></p>	<ul style="list-style-type: none"> <li>Changes in consumer behavior and communication patterns impact traditional telecom service revenues.</li> <li>Industrial restructuring and technology integration change the industry's ecological chain, and cross-industry competitors enter the telecoms business. Please refer to Section 2.1.2 (Market Competition) for details.</li> <li>Technology replacement and shortened product cycles lead to a substantial increase in R&amp;D and investment costs which are sunk costs and therefore not easy to recover.</li> <li>In the Internet era, hacking and information security loopholes have already become a challenging issue for the ICT industry.</li> </ul>	<ul style="list-style-type: none"> <li>Changes in consumer behavior and communication patterns can create innovative markets and application opportunities. Coupled with innovative technologies, products and services, we can meet or even create customer demand.</li> <li>We have been learning from mobile consumers for a long time, and data and experiences accumulated over this time have nurtured a thorough understanding of consumer behavior.</li> <li>Cross-industry collaboration and alliances provide us with the opportunity to expand the size of the market and explore new customers and consumer groups.</li> </ul>	<ul style="list-style-type: none"> <li>Enhance Internet-attack protection mechanisms and information security education for all employees.</li> <li>Identify and target key development areas, defend the company's leadership position, and carry out more rigorous R&amp;D and cost controls.</li> <li>Aggressively promote cross-industry technological development, strategy alliances, and accumulate innovative development experiences with core technologies, such as the cloud and Big Data.</li> <li>Drive transformation of the company to enhance flexibility and foster a innovative culture.</li> <li>Utilize Big Data accumulated from consumers' to analyze the concept of a all-mobile life. This will provide the basis for product design, communications and marketing as we seek to deliver user-centric products and services.</li> <li>Master synergies within the Group and integrate telecommunication, physical retail, e-commerce, finance, and other fields to create future development niches that create business innovation.</li> </ul>
<p><b>Policy and Economic Trends</b></p>	<ul style="list-style-type: none"> <li>Regulatory changes from the relevant authorities regarding bidding for spectrums, licensing, rate-plan policies, and reinvestment standards directly affect operating costs.</li> <li>Maturity of the telecom services market has led to saturation in the number of subscribers and slower growth.</li> </ul>	<ul style="list-style-type: none"> <li>Telecom regulations are likely to be eased in the future. Changes such as the lifting of investment limits and ability for entry of new competitors into a previously regulated industry could bring new opportunities for cross-industry collaboration.</li> <li>Changes in economic and social trends can create new economic models or consumer groups.</li> </ul>	<ul style="list-style-type: none"> <li>Closely track progress of new drafts, actively participate in policy seminars held by relevant authorities, and strengthen dialogue and communication through a public policy opinion platform.</li> <li>Change our competitive strategy to focus more on product and service quality as we aim to enhance customer stickiness and strengthen customer retention rate.</li> <li>Drive multi-user market expansion. This includes offering services to enterprise customers, providing roaming for tourists, and developing internet marketing push notifications.</li> </ul>
<p><b>Climate Change and Energy Scarcity</b></p>	<ul style="list-style-type: none"> <li>Extreme climate conditions exacerbate the impact of natural disasters and result in disruption of operations and services.</li> <li>Maintenance of the network, data centers, and base station operations requires abundant supplies of electricity. Therefore, energy use and greenhouse gas emissions could increase potential operating costs.</li> <li>Climate change-related regulations may impact the company's operations.</li> </ul>	<ul style="list-style-type: none"> <li>Effective energy and greenhouse gas management can demonstrate and enhance FET's brand image with a focus on sustainability.</li> <li>Development of energy-saving technologies helps to reduce operating costs, and can provide energy-management opportunities that create revenues.</li> </ul>	<p>[Internal Energy Savings]</p> <ul style="list-style-type: none"> <li>Accurately estimate demand for electricity, with electricity usage to become an integral KPI for energy monitoring and management purposes.</li> <li>Boost efficiency of power equipment usage, make use of energy-saving equipment, and accelerate development of resource saving initiatives.</li> <li>Take green materials and technology into account when exploring business opportunities and participating in projects.</li> <li>Advocate employee recognition of the importance of environmental protection, and raise awareness of their responsibilities through training, explicitly, and communication.</li> </ul> <p>[External Initiatives]</p> <ul style="list-style-type: none"> <li>Continue to promote e-billing and encourage consumers to save energy wherever possible.</li> <li>Actively expand mobile office and smart traffic to seize smart energy-saving opportunities.</li> </ul>
<p><b>Talent Recruitment and Cultivation</b></p>	<ul style="list-style-type: none"> <li>Taiwanese society is aging. Lower birth rates and more retirees mean that there is a widening talent and technology gap, which can lead to higher training costs. The overall quality of employees could be negatively affected if suitable talent cannot be successfully hired or retained.</li> <li>Specialization of talent must grow in accordance with industry and technological demands, otherwise the company's competitiveness will be negatively impacted.</li> </ul>	<ul style="list-style-type: none"> <li>The talent gap can be an opportunity for reorganization and self-examination, as it offers us an opportunity to rethink innovative retention measures and foster innovative internal strategies.</li> <li>As a new generation of employees joins the company it can create more possibilities for the company to harness their ideas and enthusiasm.</li> </ul>	<ul style="list-style-type: none"> <li>Systematically and strategically change human resource policies, emphasize focus on R&amp;D and innovation, and encourage employees to become more entrepreneurial.</li> <li>Strengthen the employee training system, work to cultivate leadership, and tap in to the talent pool to assist employees in career planning.</li> <li>Optimize employee remuneration, benefits, and incentives; create a humane working environment; and enhance employees' sense of identity.</li> <li>Check and continuously improve processes to help reduce manpower operation demand.</li> <li>Talent cultivation and cooperation between industry and academia.</li> </ul>

Whenever possible, set out clear timescales when discussing the organisation's future outlook, plans and targets: what do 'short term', 'medium term' and 'long term' mean for your organisation?

ArcelorMittal's *Annual review 2016* (page 30) contains a disclaimer in the Basis for Preparation section, with hyperlinks to more detailed regulatory risks disclosures (underscored below). The text reads:

**'Forward-looking statements**

*This review may contain forward-looking statements that represent the expectations, beliefs, plans and objectives of ArcelorMittal's management regarding its financial and operational performance in 2016 and beyond, and assumptions or judgements based on such performance. Future performance expectations are forward-looking and accordingly involve estimates, assumptions, judgements and uncertainties. A number of factors may cause actual results or outcomes to differ materially from the expectations of our management. These risk factors are set out in the risk section, with further details in the Form 20-F, filed each fiscal year with the US Securities and Exchange Commission.'*

Such a statement can help to manage users' expectations and assuage some of the legal liability concerns that the board, and/or the legal team, may have about making forward-looking statements. Aegon also includes a much more detailed version in its *2016 Review* (page 97).

**GOOD PRACTICE IDEAS**

- Consider including a disclaimer paragraph in your report, to help manage user expectations.
- Whenever possible, set out clear timescales when discussing the organisation's future outlook, plans and targets: what do 'short term', 'medium term' and 'long term' mean for your organisation?
- Challenge the board and/or the legal team about information they consider commercially or legally sensitive: in what way could such disclosure be detrimental to the organisation, and what might be the benefits of disclosure? Could there be a way of discussing these matters so as to minimise potential negative effects?
- Talk to executive management and the board about risks and opportunities on more distant future horizons, to encourage them to drive more forward-looking thinking within the organisation.



## 8. Basis of preparation

### OBSERVATIONS FROM THE REPORT REVIEWS

The 'content elements' section of the <IR> Framework contains guidance on the 'basis of preparation and presentation' when producing an integrated report. This clarifies that an integrated report should answer the question: 'How does the organisation determine what matters to include in the integrated report and how are such matters quantified or evaluated?' (para.4.40).

As part of this, the <IR> Framework recommends that an integrated report should, among other things, include a summary of the organisation's materiality determination process. This summary may give:

- a brief description of the process used to identify relevant matters, evaluate their importance and narrow them down to material matters, and
- identification of the role of those charged with governance and key personnel in the identification and prioritisation of material matters.

The <IR> Framework adds that organisations could also include a link directing readers to where they can find a more detailed description of the materiality determination process (para. 4.42).

Interestingly, this year has seen a trend, among some more 'mature' adopters of integrated reporting, to trim down the summary of the materiality determination process, or to remove it from the main report altogether. Some refer readers to their corporate website or to a separate report or supplement for details of their materiality determination process. This new development highlights how interactions between the integrated report and other reports are changing reporting practice.

Clarity over the materiality process has become particularly important in today's environment, where growing public interest in corporate behaviour has led some organisations to reconsider the audience for their corporate reporting. Today, most organisations do not, in fact, indicate for whom they are preparing their integrated reports. Fewer than half (44%, 20 out of 45) of the reports reviewed identify their intended audience. Among those that do, providers of financial capital and shareholders are mentioned, as are mainstream investors and responsible investors with an interest in ESG (environmental, social and governance) issues. Surprisingly, most also refer to 'all stakeholders' when describing their

audience: 37% (17 out of 45 reports) specifically identify potential users as including customers, suppliers, employees, regulators, local communities and governments. In total, 34 different audience groups were identified by the 20 organisations that did refer to their audience. These organisations, therefore, do envisage that their integrated reporting packages will be used by multiple audiences.

One challenge in defining and applying a consistent materiality process is that many companies are reporting under a number of different reporting frameworks and standards, often with different definitions of what is material and so should be reported. For example, in addition to the <IR> Framework, organisations could well be complying with any combination of the following: national company law, national corporate governance requirements, listing rules, the Global Reporting Initiative (GRI) G4 guidelines, the GRI Sustainability Reporting Standards, the UN Global Compact, the UN Sustainable Development Goals (SDGs), Sustainability Accounting Standards Board, AA1000 (AccountAbility Principles), UN Guiding Principles on Human Rights, the EU Non-Financial

**20%**

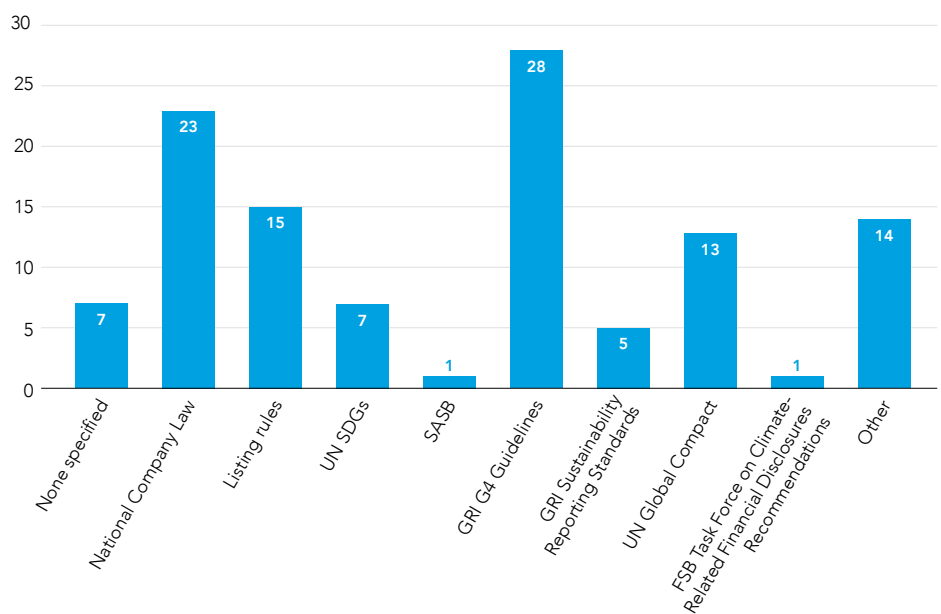
of the survey respondents said that national regulations and listing requirements were constraining their organisation’s plans to implement the <IR> Framework.

Reporting Directive – and others (Figure 8.1). In the online survey of <IR> Business Network participants, 20% said that national regulations and listing requirements were constraining their organisation’s plans to implement the <IR> Framework in some way. In order to help organisations satisfy all the many reporting requirements they face, while also producing reasonably concise reports, ACCA is calling for more convergence between different frameworks and regulations.

On the outcomes of materiality processes, some organisations are managing to report more concisely, as mentioned previously – 49% this year produced reports of 100 or fewer pages, excluding the financial statements. However, some of the integrated reporting packages still contained over 250 pages. Balancing completeness and conciseness is still a challenge for some organisations. ‘The things we struggle with most are materiality and conciseness’, says Koch. ‘How much do you disclose about material matters while still trying to keep your report concise? That’s an ongoing challenge’. One obstacle here is that Eskom’s shareholder compact (agreed with its owner, the government’s Department of Public Enterprises) identifies over 40 measures that must be reported. ‘We would love to be able to distil the reported measures down to the top five or 10, in order to improve conciseness’, Koch says. ‘It’s part of the journey’.

One factor driving high page counts is the fact that many organisations produce multiple reports. For example, 8 of the 45

**FIGURE 8.1:** Other regulatory frameworks with which reports claim compliance



integrated reporting packages reviewed for this study comprised two different reports (such as an annual report and a sustainability report), and three packages included three reports. This may be because each of these different reports is intended for a different audience.

If an organisation prepares different reports for different audiences, should the same materiality process apply? Opinions are split on this point. The answer could depend on whether materiality determination relates purely to organisation’s reporting process, or whether it is used as part of the organisation’s wider strategic planning cycle.

**WHAT CHALLENGES DO COMPANIES IDENTIFY?**

**Establishing the audience**

The <IR> Framework identifies the primary audience of the integrated report as providers of financial capital: ‘the primary purpose of an integrated report is to explain to providers of financial capital how an organisation creates value over time’ (para 1.7). However, it also acknowledges that ‘an integrated report benefits all stakeholders interested in an organisation’s ability to create value over time, including employees, customers, suppliers, business partners, local communities, legislators, regulators and policy-makers’ (para. 1.8). It is clear that, in practice, many organisations assume a

It is clear that, in practice, many organisations assume a wider audience for their integrated reporting, and may try to take account of their needs as well.

wider audience for their integrated reporting, and may try to take account of their needs as well.

‘The primary audience is investors, both equity and debt’, says Russ Houlden from United Utilities. ‘We have lots of other audiences, probably more than most companies, just because of the huge positive impact that we have on the environment and on society. Therefore we have a huge number of stakeholders. When we write the report, we have to have an eye on how they will read it. But what you can’t do is write the report for a thousand different stakeholders, because then it becomes incoherent and extremely long. So you view it mainly through your principal audience’s eyes when you decide what to put in, what to leave out and what to cross-refer to’.

The outcome of applying this materiality filter is a three-paragraph statement on page one of United Utilities’ 2017 annual report. This states that the report aims to meet the information needs of investors and contains information considered material to their decisions on, for example, ‘whether to buy, sell or hold our shares or bonds, whether to engage with management on issues and how to vote their shares’. However, it then acknowledges that the report will be read by a wide variety of other stakeholders including ‘customers, suppliers, analysts, regulators, non-governmental organisations, politicians and devolved authorities’. If a topic is thought to be material to ‘a large number’ of them, it is either included in the report or a reference made to other reports and information.

‘We are very clear’, says Houlden. ‘Those paragraphs essentially describe how we judge materiality and that is consistent with the <IR> Framework’.

Eskom’s integrated report states that it is aimed at providers of financial capital, but provides information of interest to all stakeholders. The report identifies many stakeholders, including government departments, regulators, key customers, lenders and investors, employees and organised labour, suppliers, industry, civil society, analysts, academics and media. The report writers try to consider all these stakeholders when determining and writing content, but they can’t address everyone’s needs because the report would be much too long. Nevertheless, the integrated reporting team at Eskom tries to address reader needs by making the report as accessible as they can. ‘We try to write in language that is understandable to most people’, Koch says. ‘We also use the report to educate people on issues that are critical to the business, like how we manage the electricity system, because perception and understanding of the business feeds into our tariff determinations. If people don’t understand how the business works, they don’t understand why we need the revenue that we do’, explains Buys.

Other organisations, such as Aegon, directly address a wider stakeholder group. Marc Van Weede says: ‘We are mindful that the [IIRC] guidelines say [the integrated report] should be primarily a document aimed at investors. I think there are retail investors who will read it and who appreciate this document. I think it

also serves a great purpose for the other stakeholder groups. It’s a much more accessible document for employees, business partners and other groups. But I think frankly that the institutional investors still rely more on our other disclosures – they will be digging [into] the quarterly press releases and the very extensive financials we disclose [such as the Form 20-F]. The institutional investors don’t spend a whole load of time on our integrated report’.

#### **Different materiality assessments for different audiences?**

The Corporate Reporting Dialogue, the grouping that brings together the IIRC, the GRI, the International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB) among others, defines material information as ‘any information which is reasonably capable of making a difference to the conclusions reasonable stakeholders may draw when reviewing the related information’.<sup>6</sup> From this broad consensus, a debate is growing around whether different materiality assessments should be carried out for different reports and different audiences, as the survey suggested. The majority (65%) of online survey respondents believe that materiality assessments should reflect the needs of specific audiences, but some preparers disagreed, for equally compelling reasons.

This is the view of Neil Smith, former senior associate in strategy and sustainability at Aegon. ‘Materiality is what affects the company, not what affects how you report to someone’,

<sup>6</sup> Corporate Reporting Dialogue, Statement of Common Principles of Materiality, 2016, p.2, <<http://corporatereportingdialogue.com/wp-content/uploads/2016/03/Statement-of-Common-Principles-of-Materiality1.pdf>>, accessed 22 February 2018.



For some organisations, therefore, a single materiality assessment embedded into the strategic planning process is the logical outcome of integrated thinking.

he says. 'We are aligning things more stringently with our strategy process because we see value in doing that'. Van Weede agrees: 'We are bringing things closer together, both in the internal processes we run and in the reporting'.

For some organisations, therefore, a single materiality assessment embedded into the strategic planning process is the logical outcome of integrated thinking. Looking through the lens of the organisation's strategy also provides crucial focus when sifting through what could be an overwhelming range of specific stakeholder information needs. Bruno Gasparroni, senior associate in the group sustainability team at UniCredit, points out that stakeholder needs could seem contradictory at the level of individual reporting topics, but taken at a strategic level a consistent message should emerge: 'I think if you know why you're doing what you're doing, it [materiality] really becomes a way of working, which starts with dialogue with stakeholders and then develops into a strategy.'

#### **Giving enough explanation of process**

Neil Smith at Aegon thinks it 'hugely important' to explain the materiality determination process, because of the many different approaches organisations use. Aegon previously ran an exercise looking at other organisations' approaches to materiality. 'What came out was this real feeling that everyone does it in a different way', Smith says. The numbers of material issues identified vary widely. Periods between stakeholder surveys differ. Readers of reports therefore need to have an organisation's particular approach explained to them, so they can fully understand how the material issues

were established and then compare them with the conclusions of other entities.

Karen Koch agrees it is important to explain the materiality process adopted. However, one does run the risk of boring readers due to repetition. 'Are you writing for someone who read last year's report and already understands the process?' she asks. 'Should you repeat it, or do you leave it out? It's finding that balance, because some people will have read your previous reports while some might never have read any – so you can't leave it out completely'. Eskom tries to summarise its process, but tries not to repeat standard content every year.

#### **Assessing the relative importance of stakeholder groups**

Aegon explains its materiality assessment process clearly in its 2016 annual review, with more detail provided in the accompanying reporting supplement. This involves an annual survey of stakeholders and senior management. The views of some stakeholder groups are more heavily weighted than others. For example, customers and employees are more heavily weighted than academics and independent experts. Marc Van Weede explains why. 'In alignment with our strategy, where we are in transition from being a product manufacturer to a customer company, we felt we should over-weight the customer', he says. 'The second biggest voice is that of employees, which makes sense because in our strategy...as the profile of the company changes, the capabilities we need in our employees are changing. We need more employees with scarce skills – in technology, digital marketing and change management. So building a company that is attractive for employees as

a place to develop their skills is important'. The weightings could potentially change over time, in line with strategic priorities.

#### **Managing the materiality assessment process**

UniCredit explains its materiality assessment process in some detail in its 2016 integrated report, and its diagrammatic presentation of material matters – showing their relevance to specific stakeholder groups – is given as a good practice example later in this section. However, conducting the assessment is not easy. 'It requires lots of interactions with different parts of the bank', says Giuseppe Zammarchi. 'Some stages in the dialogue we have with stakeholders are managed by the business, some are managed by central structures in the holding company. So it requires a lot of working together.'

The process for gathering stakeholder feedback has evolved over time. Initially, when UniCredit was only reporting GRI data, the focus was purely on what was important for stakeholders. 'Then with the IIRC's vision, we introduced something regarding value creation and future trends', says Bruno Gasparroni. 'A few years ago we did a survey with opinion leaders to map these trends and last year we integrated that in our materiality matrix'. Internal sentiment on the key trends was also tested, clarifying the bank's positioning on these key issues. The stakeholder engagement process has also evolved 'to take account of the huge development of social media', says Zammarchi. 'In the last three years we have enhanced our capabilities to listen to stakeholders on social media and also to interact with them'. Questions are

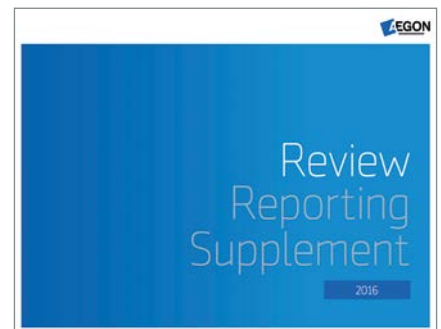
**Aegon’s Review Reporting Supplement 2016 identifies the organisation’s key stakeholders, and even applies a weighting to each stakeholder group.**

tailored for different stakeholder groups. For example, customers might be asked questions to determine what they think creates value for them as individuals. Zammarchi says: ‘When I talk to opinion leaders, the question might be more direct – what do you think the bank should do to create value? It’s a bit of a different angle’. Such opinion leaders could include journalists, academics, consultants, politicians and members of the government.

UniCredit has found that material topics can and do change over time. ‘There are things which might be material one year and the next year they are not even on the radar screen of our stakeholders’, Zammarchi says. The reverse is also true. A few years ago, financial stability was not high on stakeholders’ agenda. ‘After the financial crisis this has become more relevant’, Zammarchi says. ‘For the last two years the bank has been working hard on restructuring our operations [to make sure] we had enough capital, enough financial stability, to make sure we had a long-term survival.’ Structured stakeholder feedback, as well as regular dialogue, has helped to assure the market that UniCredit is well equipped to manage its risks.

**PRACTICAL APPROACHES**

Aegon’s Review Reporting Supplement 2016 (page 16) identifies the organisation’s key stakeholders, and even applies a weighting to each stakeholder group. This helps to inform its materiality process.



16 Stakeholder engagement Aegon's Review Reporting Supplement 2016

**Stakeholder engagement weighting and process**  
 Each year we reach out to our stakeholders to hear their views and opinions by way of an online survey and telephone interviews. This process is then the basis for identifying our material topics and in turn determines our materiality matrix.

The survey and telephone interviews are performed by an independent consultancy firm Steward Redqueen – this is to ensure impartiality.

Steward Redqueen helps in determining the selection of material issues and the list of stakeholders. They also design the questionnaire, execute the survey (including phone interviews) and present the results to us – which are then discussed by our Management Board.

Every stakeholder is important to us, but we do identify key stakeholders that are key to the success of our company and strategy. These stakeholders are given a stronger weighting when determining our material topics.

Stakeholder group	Weighting (in %)
Customers	25
Employees	20
Shareholders	20
Peers & industry associations	10
Financial & sustainability analysts	10
Government & regulators	5
NGOs	5
Academics & independent experts	5

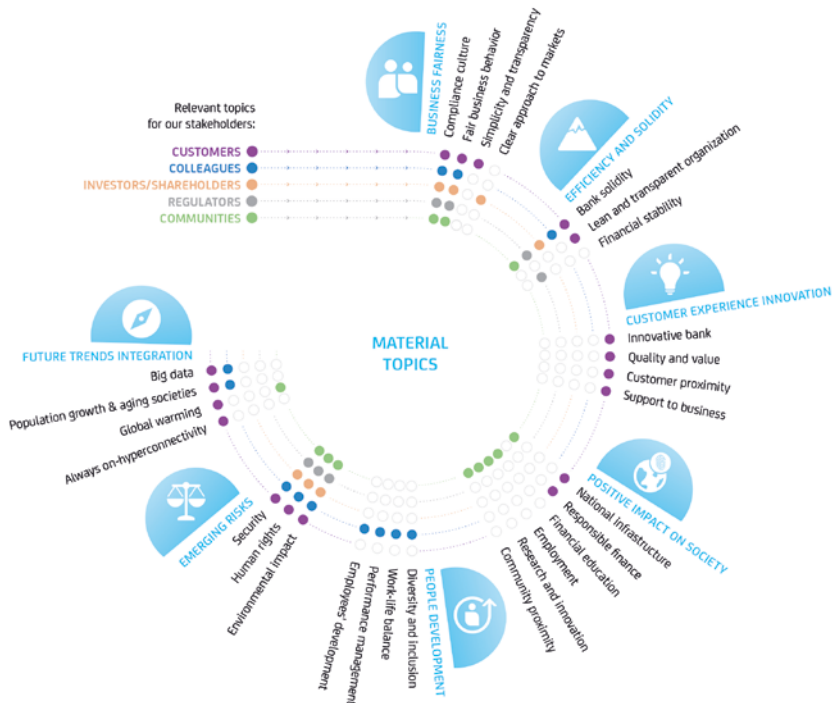
UniCredit's 2016 *Integrated Report* provides an excellent example of how stakeholder engagement takes place regularly in the ordinary course of business.

UniCredit's 2016 *Integrated Report* (pages 28 and 70) provides an excellent example of how stakeholder engagement takes place regularly in the ordinary course of business. Regular stakeholder engagement has allowed UniCredit to demonstrate an impressively granular understanding of different stakeholder needs, by stakeholder group as well as by country/region.



## Stakeholder Engagement

Continuous interaction with stakeholders at every level of our organization is an essential component of the Group's decision-making processes, which are aimed at the long-term creation of value. Expanding the knowledge base of our stakeholders is a vital undertaking that calls for specific skills and processes, and we continuously invest in the development of these assets.



see page 5.40 for further info

**Our Strategy**

→ Social and relationship Capital

**Country Priorities**



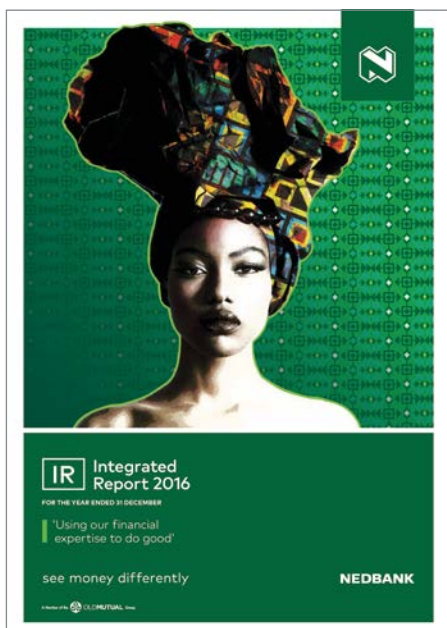
Macro Dimension	Indicator	Italy	Germany	Austria	CEE <sup>A</sup>
<b>Social Wellbeing</b>	Employment rate of people 20-64 years	Medium	Low	Low	Low
	Social decay (or incivilities) rate	High	Medium	Medium	Medium
	Work satisfaction	Medium	Low	Low	Low
	Citizens who benefit from infancy services	High	Low	Medium	High
<b>Economic Wellbeing</b>	People suffering poor housing conditions	High	Medium	High	Medium
	Severely materially deprived people	High	Low	Low	Medium
	Index of subjective evaluation of economic distress	High	Medium	Medium	High
<b>Education and Efficient use of talent</b>	Country capacity to attract talent	Medium	Low	Medium	Medium
	Percentage of young people not in education, employment, or training (NEET)	High	Low	Low	High
	Percentage of people participating in formal or non-formal education	Medium	Medium	Low	Medium
<b>Health</b>	Healthy life expectancy at birth	Low	Medium	Medium	Medium
	Waiting lists	High	Low	Low	Medium
	Life expectancy without activity limitations at 65 years of age	High	High	Medium	Medium
<b>Environment &amp; Landscape</b>	Energy from renewable sources	Low	Medium	Low	Low
	Public expenditure for recreation, culture and religion	High	High	Medium	Low
	Emissions of CO <sub>2</sub> per inhabitant	Low	Medium	Low	Low
<b>Infrastructure &amp; Quality of services</b>	Quality of overall infrastructure	Medium	Medium	Medium	Low
	Quality of roads	Low	Medium	Low	Low
	Internet bandwidth	Medium	Medium	High	Medium
<b>Financial Market</b>	Availability of financial services	Medium	Medium	Medium	Low
	Ease of access to loans	High	Low	Medium	Medium
	Venture capital availability	High	Low	High	Low
<b>Business Sophistication</b>	Local supplier quality	Low	Low	Medium	Low
	Extent of marketing	Medium	Low	Low	Low
	Nature of competitive advantage	Low	Low	Low	Medium
<b>Innovation</b>	Innovation rate of the national productive system	Medium	Medium	Low	Medium
	Research intensity	Medium	Low	Low	Medium
	Patent propensity	High	Medium	Low	Medium

A. CEE includes: Bulgaria, Croatia, Hungary, Romania.

South African company Nedbank Group begins its 2016 *Integrated Report* with an admirably clear two-page summary about its basis for preparation.

South African company Nedbank Group<sup>7</sup> begins its 2016 *Integrated Report* with an admirably clear two-page summary about its basis for preparation. It identifies (on page 2) its reporting boundary, as well as its target readers: 'This is our primary report to stakeholders and is intended to address the information requirements of long-term investors (our equity and preference shareholders, bondholders and prospective investors). We also present information relevant to the way we create value for other key stakeholders, including our staff, clients, regulators and communities'. Page 2 also contains an explanation of what the concepts of value and materiality mean for Nedbank.

The inherent uncertainty surrounding forward-looking statements is described



About our Integrated Report

Nedbank Group is committed to the principles of Integrated Reporting. Our thinking and our approach to long-term value creation are aligned with these principles, which allow us to tell a clear and comprehensive story about how we deliver on our purpose to use our financial expertise to do good for individuals, families, businesses and society.

Scope and boundary of reporting

**REPORTING PERIOD**  
The Nedbank Group Integrated Report is produced and published annually. The 2016 report covers the period 1 January to 31 December 2016 and builds on the 2015 report. Any material events after this date and up to the board approval date on 17 March 2017 have also been included. The report also contains Nedbank Group's outlook, targets and objectives for the short (2017) and medium to long term (2018 to 2020 and beyond). Our integrated thinking is reflected in our targets and key performance indicators that cover financial and non-financial performance as well as strategy, risks and how we deliver value to stakeholders.

**OPERATING BUSINESSES**  
The report covers the primary activities of the group, our business clusters, key support areas and subsidiaries in our African and international operations. Detailed information on investments in which the group holds only a minority stake is not included.

**FINANCIAL AND NON-FINANCIAL REPORTING**  
The report extends beyond financial reporting and includes non-financial performance, opportunities, risks and outcomes attributable to or associated with our key stakeholders, which have a significant influence on our ability to create value.

**TARGETED READERS**  
This is our primary report to stakeholders and is intended to address the information requirements of long-term investors (our equity and preference shareholders, bondholders and prospective investors). We also present information relevant to the way we create value for other key stakeholders, including our staff, clients, regulators and communities.

**BENCHMARKING**  
We benchmark our performance against our peers based on publicly available information. While consistent benchmarks are not always readily available, we have included these where relevant so that readers can gauge Nedbank Group's relative performance.

KEY CONCEPTS

DEFINING VALUE

Value creation is the consequence of how we apply and leverage our capitals in delivering financial performance (outcomes) and value (outcomes and outputs) for all stakeholders while making tradeoffs. Our value creation process is embedded in our purpose (page 12), described as part of our business model on pages 20 and 21 and integrated into the way we think and make decisions. Through 'case in point' illustrations we provide examples of how value is created through strategy and delivered to our stakeholders.

MATERIALITY AND MATERIAL MATTERS

We apply the principle of materiality in assessing which information is to be included in our Integrated Report. This report focuses particularly on those issues, opportunities and challenges that impact materially on Nedbank Group and its ability to be a sustainable business that consistently delivers value to shareholders, prospective investors and our key stakeholders. Our material matters, as described on pages 34 to 39, influence our group's strategy and inform the content in this report.

THE CAPITALS

Our relevance as a bank today and in the future, and our ability to create long-term value is interrelated and fundamentally dependent on the forms of capital available to us (inputs), how we use them (value-adding activities), our impact on them and the value we deliver (outputs and outcomes), as shown on pages 20 and 21. Our capitals and an explanation of what they represent to us, are provided below:

Financial

Our shareholders' equity and funding from investors and clients that are used to support our business and operational activities, including credit extension (advances).

Human

Our people, investing in their development and our collective knowledge, skills and experience to enable innovative and competitive solutions for our clients.

Manufactured

Our business structure and operational processes, including our physical and digital infrastructure, our products, as well as our information technology that provides the framework and mechanics of how we do business and make money.

Intellectual

Our brand and franchise value, research and development, innovation capacity, reputation and strategic partnerships.

Social and relationships

Our citizenship and strong stakeholder relationships, including the communities we operate in, as we recognise that banks play an important role in building a strong and thriving society.

Natural

Our positive and negative impact on natural resources through our operations and business activity.

7 Nedbank is not yet a formal participant of the <IR> Business Network.

If different stakeholders demand different information, focus on the topics that are most relevant to the execution of your organisation's strategy.

on page 3. This is then signed off by the board of directors, in an unequivocal acknowledgement of their responsibility for the integrity of the integrated report.

NAVIGATION ICONS

**STAKEHOLDERS**

- Staff
- Clients
- Shareholders
- Regulators
- Communities

**STRATEGIC FOCUS AREAS**

- Delivering innovative market-leading client experiences
- Growing our transactional banking franchise faster than the market
- Being operationally excellent in all we do
- Managing scarce resources to optimise economic outcomes
- Providing our clients with access to the best financial services network in Africa

**MATERIAL MATTERS**

- Volatile and uncertain socioeconomic environment characterised by slower growth and rising inequality
- Disruptive technologies, disintermediation and increased competition
- Increased demands on governance, regulation and risk management
- Managing growth opportunities vs risks in rest of Africa
- Transformation of society within environmental constraints
- Scarce- and evolving-skills requirements
- Changing relationships between business, government, labour and civil society

**ASSURANCE INDICATORS**

- LA External limited assurance  
Extracted from the 2016 Nedbank Group Limited Audited Annual Financial Statements
- FS Management and board oversight
- IN External sources, eg independent surveys
- OV Independent oversight by regulatory bodies

**Reporting frameworks and combined assurance**

Our Integrated Reporting process, as well as the contents of this report, is guided by the principles and requirements of the International Integrated Reporting Framework (IIRC) and the King Code of Governance Principles for SA (King III), and is in accordance with the 'core' level of the Global Reporting Initiative (GRI) G4. As an SA bank and a company listed on JSE Ltd (the JSE), we align to the JSE Listings Requirements, the SA Companies Act, 71 of 2008 (as amended), and the Banks Act, 94 of 1990.

We employ a combined assurance model to assess and assure various aspects of the business operations, including elements of external reporting.

These assurances are provided by management and the board, internal audit and independent external service providers, including KPMG Inc and Deloitte & Touche, our external auditors and providers of limited assurance on selected sustainability information, and SizweNtsalubaGobodo Inc, providers of limited assurance on our application of the Financial Sector Code (FSC) and the group's broad-based black economic empowerment (BBBEE) status.

For further information on the scope of the services provided by our external assurance providers refer to the Nedbank Group Annual Financial Statements, the Nedbank Ltd Annual Report, the Nedbank Ltd and subsidiaries BBBEE certificate, and the Independent Assurance Providers' Limited Assurance Report on Selected Sustainability Information, which are available on our group website at [nedbankgroup.co.za](http://nedbankgroup.co.za).

**Forward-looking statements**

This announcement contains certain forward-looking statements with respect to the financial condition and results of operations of Nedbank Group and its group companies that, by their nature, involve risk and uncertainty because they relate to events and depend on circumstances that may or may not occur in the future. Factors that could cause actual results to differ materially from those in the forward-looking statements include global, national and regional economic conditions; levels of securities markets; interest rates; exchange rates; credit or other risks of lending and investment activities; as well as competitive and regulatory factors. Consequently, all forward-looking statements have not been reviewed or reported on by the group's auditors.

**Responsibility of the board**

This report was approved by the board of directors of Nedbank Group on 17 March 2017.

**STATEMENT OF THE BOARD OF DIRECTORS OF NEDBANK GROUP**

The board acknowledges its responsibility to ensure the integrity of this Integrated Report, which in the board's opinion addresses all material issues and presents fairly the integrated performance of Nedbank Group.

As signed off by the board:

Vassi Naidoo  
Mike Brown  
David Adomakoh  
Tom Boardman  
Brian Dames  
Ian Gladman  
Bruce Hemphill  
Erral Kruger  
Rob Leith  
Mpho Makwana  
Mantsika Matookane  
Nomavuso Mnxasane  
Raisibe Morathi  
Joel Netshitenzhe  
Mfundo Nkuhlu  
Stanley Subramoney  
Malcolm Wyman

Nedbank Group – Integrated Report 2016  
About our Integrated Report

3

**GOOD PRACTICE IDEAS**

- Define the primary audience(s) of each corporate report: this helps to focus reporting on the information that is most relevant for that audience.
- In cases where different stakeholders demand different information, focus on the topics that are most important to the execution of your organisation's strategy.
- Show your stakeholders how you have identified, evaluated and prioritised the material matters included in your report: this increases the credibility of the report and helps users to make informed decisions when making comparisons with other organisations.
- If your organisation publishes multiple reports, consider whether they emphasise different topics or information, and why. If different materiality decisions have been taken because the reports served different purposes or addressed different audiences, could this be briefly explained at the front of each report?
- Consider the most appropriate location for the materiality summary. If it is published separately from the report to which it relates, direct users to it through cross-referencing and think about whether any conclusions may helpfully be included within the main report.



## 9. Materiality through the lens of value creation

### OBSERVATIONS FROM THE REPORT REVIEWS

The <IR> Framework contains a guiding principle on the concept of materiality. This states that an integrated report should disclose information about matters that substantively affect the organisation's ability to create value over the short, medium and long term (section 3D).

The <IR> Framework explains that the materiality determination process for the purpose of preparing and presenting an integrated report involves:

- identifying relevant matters based on their ability to affect value creation,
- evaluating the importance of relevant matters in terms of their known or potential effect on value creation,
- prioritising the matters based on their relative importance, and
- determining the information to disclose about material matters.

In essence, material matters are determined by reference to their known or potential effect on value creation. This year's review considered whether the organisations considered matters' ability to affect value creation as part of the materiality determination process. This proved to be, on average, one of the lower-scoring areas reviewed – although

60% scored a 4 or 5. In other words, it seems that while a value-creation focus is well embedded in many organisations, others clearly define materiality differently. One such different approach is that advocated by the GRI, which determines materiality on the basis of the impact on an organisation's stakeholders, rather than on the creation of value by the organisation itself.

In this context, it was notable that of the reports that specifically claimed compliance to other frameworks and standards, nearly three-quarters (73%) were applying GRI guidelines or standards. It would seem that a sizeable proportion of GRI-compliant reports were also judged to have applied a value-creation focus to materiality determination in some way.

### WHAT CHALLENGES DO COMPANIES IDENTIFY?

#### Dealing with externalities

Making an explicit link between the materiality assessment and value creation is not straightforward, particularly when some of the material matters identified are not within the organisation's control. Aegon's board has been discussing its materiality matrix, produced as a result of its materiality-assessment process. The materiality matrix in the 2016 review indicates, through colour coding, the level of control or influence Aegon has

over each material matter (see page 44 in this report). 'There is perhaps a distinction to be made between things that happen to us and are somewhat inevitable – low interest rates, ageing populations – versus elements that are more in our control, that we have more influence on, such as trust and reputation', van Weede says.

There are also challenges in taking the highly material, but external, matters and translating them into more concrete issues that the organisation can do something about. Van Weede gives this example: 'If we believe interest rates will stay down for a long time, does that have consequences for the value of our portfolios and should we be thinking of additional measures to hedge the risk of low interest rates? Or should we divest [of] certain businesses that don't make sense in this environment, at least for a long time? There is a link with value creation, but it's an area where we are still looking for how we can best articulate that'.

#### Obtaining sufficient board involvement

Board involvement in the materiality assessment process varies. In many organisations, the board's role appears limited to oversight and giving final approval. The insights that this process can provide for strategy-setting, however, suggest that there are benefits to greater board involvement.

Applying the value creation lens to materiality can be a useful tool for helping managers to think ahead about the risks and opportunities that could affect their organisations.

Aegon's two boards (supervisory and management) are very much involved, and a carefully designed process facilitates this. They both complete the stakeholder questionnaire. In addition, each member of the management board was individually interviewed, as were a number of additional people who have a lot of direct interaction with stakeholders, such as the heads of investor relations and of banking relationships, and representatives from the works council. 'People tend to be a little more outspoken in a one-on-one discussion', van Weede explains. 'We used the feedback from the one-on-one interviews to come up with a lot of key strategic issues and we used that as another input for fleshing out materiality – the key areas where we want to develop positions or develop responses in the course of 2018'. The management and supervisory boards both discussed the questionnaire and interview findings as part of this process.

#### Linking materiality determination through to strategic planning

Aegon has brought forward timing of the materiality assessment, so as to enable the outcomes to inform its other internal processes. Previously, it conducted its materiality assessment towards the end of the year, and reflected the outcomes in that year's report, but there was too little time to formulate strategic or operational responses to the issues identified. 'This year we changed the cycle,' van Weede

says. 'We do the materiality assessment at...the end of the prior year. We then use that as an input for our strategy cycle that kicks off in January. Then we have a whole year in which we go through our strategy planning and action planning and responses. So by the end of 2018, we will...have a much better story about how we responded to those issues'.

The outcome of the materiality assessment now provides 'a core input' into Aegon's strategic risk assessments, which are becoming a standard part of the strategy-review process at both group and business unit level. Van Weede sees this as a 'more integrated approach'. Conducting these strategic risk assessments in the right way should help with risk reporting, he adds.

FMO follows a similar process, with regular stakeholder engagement informing its planning, but for the development bank the materiality assessment follows from the stakeholder dialogues that took place during the year, which were already analysed each quarter. Bakker says: 'What we report at the end of the year [in the materiality disclosures] is the added sum of what we already discussed and processed internally in strategy development.'

There seems to be consensus that strategy and operations should be informed by regular stakeholder

engagement – as part of that, there needs to be an effective system for gathering and analysing stakeholder feedback in a way that can lead to concrete actions and plans. However, where the process called 'materiality assessment' sits within this cycle differs from one organisation to another. Sometimes, this might be more a difference in terminology than a difference in practice.

#### Using a value creation lens to identify risks and opportunities

Applying the value creation lens to materiality can be a useful tool for helping managers to think ahead about the risks and opportunities that could affect their organisations. Aegon is not alone in joining up the materiality process and the risk assessment process. Eskom's Koch also believes there's a natural link between material matters and risks – applying the <IR> Framework's approach to materiality has led to a longer term focus in risk identification. 'In the past we found the risk assessment was more short-term focused, although integrated reporting has helped Eskom to look further ahead,' Buys says. 'In our business the plant life is around 50 years, so you need to look at the longer term horizon', he says.

Giuseppe Zammarchi at UniCredit believes the materiality assessment process based on stakeholder feedback helps to identify both risks and



**‘Having a good dialogue with stakeholders can help us detect more opportunities than if we just sit at our desks and do what we do.’**

opportunities by getting ‘a sense of what they perceive to be under the radar screen’. The materiality assessment can help to clarify risks, but there should be relatively few surprises: ‘If the bank is doing its job well, the detection of risks should already be there and management should already have been alerted about the risk before it gets material for some stakeholders’. On the other hand, the process can be helpful for identifying opportunities. ‘Opportunities are sometimes floating outside our view’, Zammarchi says. ‘Having a good dialogue with stakeholders can help us detect more opportunities than if we just sit at our desks and do what we do’.

This proactive approach to managing opportunities, as well as risks, could be helpful to many managers and integrated report preparers. Our review of integrated reporting packages suggests that while reporting on risks is relatively robust, reporting on opportunities is done less well. There are clear market benefits to be gained by demonstrating a strong understanding of future opportunities to investors and other stakeholders.

#### **Impact of multiple frameworks**

Does the adoption of other non-financial reporting standards or frameworks (such as the GRI G4 Guidelines) make it more difficult to apply the value creation lens?

There are differing views in Eskom. ‘I don’t believe GRI is something we should try and work into the integrated report, because the GRI requirements are very specific’, Koch says. Although some aspects, such as disclosures relating to governance and stakeholder engagement are closely aligned, other GRI requirements are much more detailed. Koch therefore believes that GRI reporting should be contained in a standalone sustainability report. ‘If we brought it into the integrated report, we would lose what integrated reporting is about’, she says. ‘Conciseness would be lost, and probably materiality too’. Koch believes that the audiences for GRI reporting and the integrated report are different, which is another argument for separating the two. She also feels there should be a different materiality consideration, so that the content of each report meets the needs of its intended audience.

Aegon applies both the <IR> Framework and GRI guidelines in its annual report, although it isn’t easy. One of the previous challenges in satisfying both, Marc van Weede says, was that GRI is rules-based, whereas the IIRC is principles-based. Aegon’s next integrated report (to be published in March 2018), will therefore focus on the GRI indicators most relevant to the business: ‘the ones we can have an impact on, the outputs and the relevant KPIs’, van Weede says. ‘So we find we are scoping right back with the GRI indicators that we will report against, but they will be far more meaningful’.

UniCredit’s Giuseppe Zammarchi agrees that it is possible to apply the value creation lens in combination with other frameworks, but cautions that the methodology needs to be clearly explained: ‘We try to reconcile the value creation standpoint with the stakeholder standpoint. If we want to be compliant with GRI standards, we need to satisfy a number of requirements and indicators, which I wouldn’t say are in conflict with the IIRC, but you have to use different methods. You have to make both approaches clear. It is slightly more time-consuming to make sure you have both angles covered’.

Eskom’s 2017 integrated report clearly explains its materiality determination process, which explicitly applies the <IR> Framework’s value creation lens to materiality.

**PRACTICAL APPROACHES**

Eskom’s 2017 integrated report clearly explains its materiality determination process, which explicitly applies the <IR> Framework’s value creation lens to materiality. The report states (page 27): ‘The first step in the materiality determination process is to identify relevant matters based on their ability to affect our value creation process.’ Buys describes the <IR> Framework’s approach as logical and says that it works well for Eskom.

The outcome of Eskom’s process is a list of material matters, which it presents in a table with an indication of each one’s current impact on value creation (negative and/or positive) and the timeframe of the impact.



**Material stakeholder matters**  
Material matters are those that are both of importance to stakeholders and could have a substantial impact on our business, with the potential to significantly affect the achievement of our strategic objectives and consequently, our ability to create value.

**Materiality determination process**  
The first step in the materiality determination process is to identify relevant matters based on their ability to affect our value creation process. We perform the process annually. Our starting point is those matters reported in the prior year, which we then update based on a review of changes during the current year.

As part of that review, we consider topics discussed at Board level, the outcome of the risk management process, as well as issues raised through various stakeholder platforms – lenders and investors, key customers, customer surveys, matters raised in Parliament and by the media, and more generally via the Stakeholder Relations Department.

We then evaluate the impact of the matters identified on the execution of our strategy, future performance and value creation by considering the effect of the matter, taking account of both the likelihood of the matter occurring, as well as the magnitude of its impact.

Matters are then prioritised based on their relative importance. Although we consider all matters raised by stakeholders, only those deemed to be material matters are covered in detail in our report. Other concerns are addressed through various other platforms.

The process is overseen by Exco and ratified by the Board.

**Current year material matters**  
The majority of the material matters described in our 2016 integrated report remain relevant, even though the level of importance to stakeholders or the impact on our value creation may have changed. Some new issues have been raised, or increased in importance.

The following have been identified as material matters in this report:

Material matter	Current impact on value creation	Timeframe of impact
Regulatory environment and uncertainty of the electricity price path, including the treatment of RCAs	Negative	Short, medium and long term
The impact of stagnant or declining sales on Eskom, combined with the impact of increased electricity prices on the economy	Negative	Short to medium term
Financial performance, cost management and liquidity	Positive	Short to medium term
Funding plan and the impact of credit ratings downgrades, together with Government support	Both positive and negative	Short, medium and long term
Arrear customer debt – mainly municipalities and residential customers – and the impact of disconnections on customers	Negative	Short to medium term
Surplus capacity, which is due to improved plant performance, new capacity being brought online by the new build programme and connecting IPPs, coupled with stagnant sales, which may require the decommissioning of older power stations	Both positive and negative	Medium to long term
Environmental performance, including emissions, water use and environmental contraventions, which may affect our capacity and compromise our licence to operate	Negative	Short to medium term
Energy mix and carbon footprint of our fleet, including renewables and nuclear energy, coupled with concerns around water scarcity and climate change	May be either positive or negative	Medium to long term
Skills and transformation of our workforce	Positive	Medium to long term
Governance and procurement practices	Perceived as negative	Short, medium and long term

Our strategic risks, which are largely aligned to the material matters, are set out on page 29 with their associated risk rating and treatment strategy

Eskom Holdings SOC Ltd 27

Our business and strategy

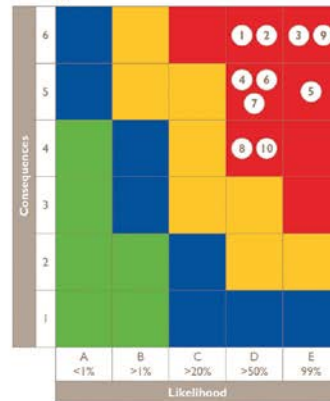
Strategic risks and opportunities are assigned a rating based on their potential consequences and likelihood, an indication of their impact on value creation, the timeframe of the impact and the treatment strategy.

Strategic risks and opportunities are assigned a rating based on their potential consequences and likelihood, an indication of their impact on value creation, the timeframe of the impact and the treatment strategy.

### Risks and opportunities, assurance and controls

The diagram below sets out the risk ratings of the strategic risks identified on the Eskom Risk Matrix.

#### Strategic risks at 31 March 2017



#### Identifying and prioritising opportunities

Globally, the electricity landscape is changing rapidly. Eskom is not immune to this change and we are facing threats on multiple fronts: within the South African electricity market, and within the broader global energy context. With a wave of change in customer, supplier and competitor behaviour, we are facing a constrained electricity sales path.

Potential sources of revenue growth range from those that are close to our current capabilities to those that are entirely new. By exploiting both regulated and unregulated opportunities, we have an opportunity to deliver significant revenue impact.

We will do this by unlocking opportunities, focusing on local demand stimulation, cross-border sales and unregulated opportunities. A clear distinction exists between the business of today and the Eskom of tomorrow, necessitating a focused and structured approach, which will ensure the right level of focus and drive for each identified opportunity.

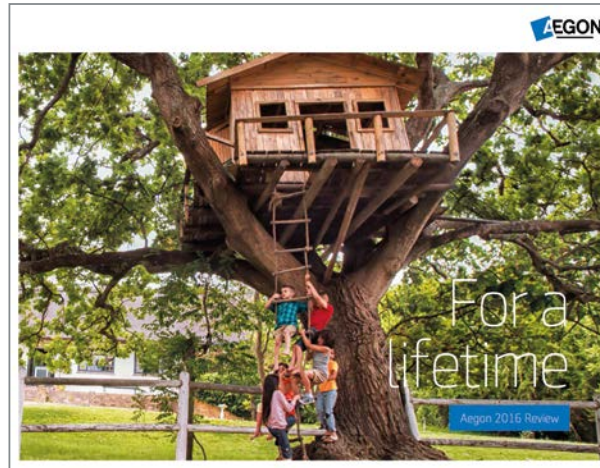
We apply a structured stage-gate process to identify, develop and prioritise opportunities through to commercial application. Opportunities are sourced from within Eskom and externally. These ideas are then assessed and filtered through an opportunity funnel.

Only ideas with the highest potential and chance of success continue to development, to ensure that scarce resources are optimally allocated



Noteworthy emerging opportunities include:

- Investigating opportunities associated with storage options in both diversifying the business and retaining customers in the medium term. Storage technologies have matured enough to enable large-scale implementation within reasonable risk parameters. We are identifying areas where battery storage can be deployed, with a view to applying these technologies at scale across the grid in the next three years
- Leveraging clean fossil fuel and transmission-based opportunities in the region through our integrated Africa strategy
- Exploring water usage and potential partnerships as a revenue-generating business



Aegon's 2016 Review (pages 22 and 23) defines material issues as 'those that will have a long-term impact on our profitability, operations and reputation'. The materiality matrix then shows the extent to which Aegon has the ability to control or influence outcomes. Each of the top material issues is covered in a detailed discussion, showing the actions that Aegon is taking.

# Introduction to our operating environment

Economic conditions, geopolitics and social factors can have an effect on our profitability, operations and reputation. We cannot always control what happens in our operating environment but we can be prepared. This starts with identifying the biggest issues affecting our business. We call these our material issues.

We are a global company with many stakeholders. We have the potential to have an impact on the people, the countries and the economies in which we operate. We make every effort to ensure this is a positive impact.

### Materiality assessment

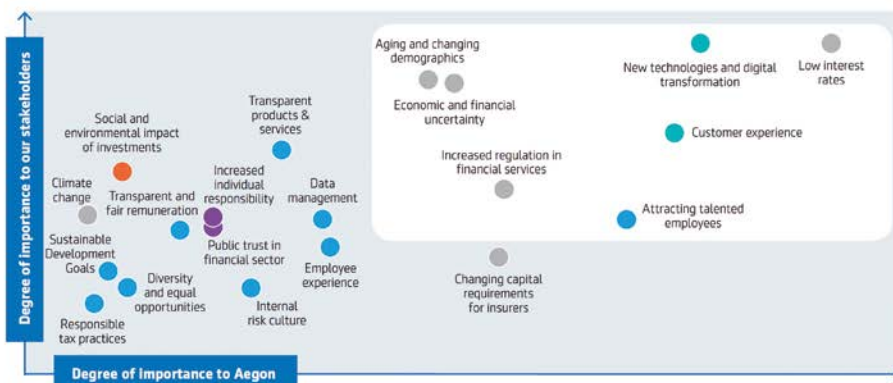
Material issues are important to our business. They inform our strategy and also determine our approach to reporting. We define material issues as those that will have a significant long-term impact on our profitability, our operations or our reputation.

To determine the issues that are most material to us, each year we ask independent consultants Steward Redqueen to survey our stakeholders and our senior management. This includes the trends and issues that we believe can, or will, have an impact on our business<sup>1</sup> – everything from climate change and responsible tax, to low interest rates and digital transformation. We then ask the respondents to identify these issues and rank them in order of importance. The results are plotted on our materiality matrix (which you can see below). The issues that are most relevant to both our stakeholders and our senior

management are then identified as our material issues. A summary of the materiality matrix results is then shared with both our Management Board and Supervisory Board for their review and discussion.

### Stakeholders

Our stakeholders are a broad group that include customers, employees, investors, financial analysts, sustainability analysts, peers, government, regulators, independent experts, academics and NGOs. They are asked to participate in the materiality survey on



### Ability to control or influence

- **Direct control**  
Issue is entirely within the company's control.
- **Shared control**  
Control of the issue is shared with, or exercised through, another company, organization or third-party.
- **Strong influence**  
Company has ability to influence the issue within its own businesses and value chain.
- **Some influence**  
Company has ability to influence, but only within its own businesses (not its wider value chain).
- **No influence**  
Company has little or no meaningful control or influence over the issue.

Please note, the focus of our materiality assessment was on non-financial issues. Due to the nature of our business and the maturity of our financial reporting, we have not included financial terms as part of this assessment. Financial impacts/externalities are also part of changing capital requirements, low interest rates and economic and financial uncertainty.

Source: Steward Redqueen

Think about what you want out of the materiality process: could it feed into your organisation's wider planning and risk management processes?



### GOOD PRACTICE IDEAS

- Review the board meeting minutes and hold regular discussions with board members, including the chair and the CEO, to understand what the board considers to be the key drivers of success.
- Explore, with members of the board and senior management, what value means for them and the organisation. This, and the key drivers of success, should form the basis of the materiality process.
- When evaluating and prioritising the material matters, consider the likelihood and magnitude of their potential impact on your organisation's ability to create value.
- Consider and explain the extent to which your organisation can influence the outcomes of material issues: this helps to manage stakeholder expectations, and demonstrates accountability.
- Think about what you want out of the materiality process: could it feed into your organisation's wider planning and risk management processes? If so, time the materiality assessment appropriately.
- Use the materiality process to proactively identify not just risks, but opportunities.



## 10. Conclusion

**Many participating organisations in the IIRC’s <IR> Business Network now have considerable experience, gained over several years, of preparing integrated reports. This year’s review has found many encouraging year-on-year improvements.**

It is also notable that integrated thinking is seen as an important aspect of integrated reporting. For some organisations, such as United Utilities, integrated thinking was developing internally before the adoption of integrated reporting. In the online survey of <IR> Business Network participants, 45% said that integrated thinking actually came before integrated reporting.


The level of current experimentation with integrated reporting is also striking among network members, whether related to establishing material matters, finessing business models or finding new ways of explaining or quantifying value creation. Such experimentation is set to continue. Looking ahead, UniCredit is interested to see how the mandatory requirements of the EU Non-Financial Reporting Directive will influence reporting practice and focus the board’s attention on non-financial reporting. Aegon notes that the Dutch national requirements for annual report content (eg relating to value creation) are moving closer to integrated reporting, which could lead to closer integration between its formal

annual report and its separate annual review, which it views as its integrated report. Many organisations will also be finding ways of reporting effectively on their commitments to the UN Sustainable Development Goals (SDGs). In the online survey of <IR> Business Network participants, 35% said they planned to use the <IR> Framework as an aid to reporting on their SDG commitments.

Regardless of national regulations or international initiatives, there are many challenges involved in reporting on company performance. Approaching these challenges in a strategic way by using the <IR> Framework can bring benefits to both reporting organisations and their stakeholders. The practical examples, shared experiences and tips included in this report are intended to inspire further experimentation and improvement in integrated reporting. Finally, remember the ultimate goal: to tell a coherent and convincing story to key stakeholders about how your organisation plans to create value over the short, medium and long term – and to put that plan into action.

**45%**

**of the survey respondents said integrated thinking actually came before integrated reporting.**



## 10 questions to get you on the way to good integrated reporting (and thinking)

To benefit fully from integrated reporting and thinking, we recommend reporting colleagues to consider the following questions. Use them to start a wider conversation about your organisation's culture, objectives and processes.

- 1 WHAT DOES VALUE MEAN FOR ME AND MY ORGANISATION?
- 2 WHAT DIFFERENTIATES MY ORGANISATION FROM ITS COMPETITORS?
- 3 WHAT IS MY ORGANISATION'S MISSION?
- 4 WHERE DOES MY ORGANISATION WANT TO GO (ITS VISION)?
- 5 WHO ARE THE KEY STAKEHOLDERS WE RELY ON TO FULFIL OUR MISSION AND REALISE OUR VISION?
- 6 WHAT KEY RESOURCES DO WE NEED TO DO THIS?
- 7 HOW DO WE PUT OUR MISSION AND VISION INTO ACTION? WHAT IS OUR STRATEGY?
- 8 WHAT CHANGES CAN I SEE COMING IN 1, 5, 10 AND 20 YEARS' TIME, WHICH COULD AFFECT OUR STRATEGY? WHAT DO WE NEED TO DO DIFFERENTLY TO RESPOND TO THOSE CHANGES?
- 9 HOW WILL I KNOW WHETHER MY ORGANISATION IS FULFILLING ITS MISSION AND REALISING ITS VISION? HOW WILL OUR KEY STAKEHOLDERS KNOW?
- 10 HOW CAN I TALK TO THE BOARD ABOUT THESE QUESTIONS?

# Appendix 1: Participants

ACCA would like to thank the individuals who gave their time to be interviewed for this report.

## Russ Houlden

CFO, United Utilities Group PLC

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*‘Integrated reporting encourages companies to communicate clearly the joined up thinking they use to deliver value for customers, shareholders and other stakeholders’.*

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Russ Houlden has a first class honours degree from Warwick Business School and has completed executive programmes at INSEAD, Stanford and London Business School. He is a Fellow of the Chartered Institute of Management Accountants, a Chartered Global Management Accountant, a Fellow of the Association of Corporate Treasurers and has won awards for Best North West PLC Finance Director in 2013 and 2014, ‘Excellence in Reporting’ in the Building Public Trust Awards 2015 and ‘Communicating Integrated Thinking’ in the Finance For The Future Awards 2016.

From 1980 to 1991 he progressed through a variety of financial roles in ICI and Spicer & Oppenheim (now part of Deloitte) covering audit, management consultancy, financial accounting, cost accounting, management accounting, controlling, corporate reporting, treasury management and corporate finance. From 1991 to 2002 he was Finance Director of ICI Japan (based in Tokyo), ICI Polyurethanes (based in Brussels) and BT Networks & Information Services and BT Wholesale (based in London). Since 2002 he has been Finance Director of Lovells (a leading international law firm, now Hogan Lovells), Chief Financial Officer of Telecom New Zealand (listed on the NZX, ASX and NYSE) and Chief Financial Officer of United Utilities (listed on the FTSE).

Apart from his executive roles he is the Audit Committee Chairman and a Supervisory Board member of Orange Polska SA (listed on the WSX) and Chairman of the Financial Reporting Committee and a Main Committee member of the 100 Group, which represents the FTSE100 to government, regulators, standard setters and other stakeholders. He has previously served as a member of the Advisory Board of Warwick Business School and as a member of the Ecosystem Markets Task Force for the UK government.

## Job Bakker

Senior Planning & Control Officer, Finance, FMO NV

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*‘Integrated reporting and integrated thinking enable FMO to increase its impact’.*

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Job Bakker is senior strategy controller with FMO NV, the Dutch development bank that invests in frontier markets, supporting jobs and income generation, and improving people’s lives in those parts of the world where this makes the biggest difference. For the past five years, Job has coordinated integrated reporting and integrated thinking within FMO. FMO received an award from Responsible Investor for its 2016 integrated annual report.

## Marc van Weede

Global Head of Strategy & Sustainability, Aegon

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*‘Integrated reporting has been a catalyst for our thinking about value creation for all stakeholder groups’.*

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Marc holds the position of Global Head of Strategy & Sustainability. He focuses on corporate strategy, customer strategy, responsible business, retirement and healthy ageing research, change management, innovation and venturing.

Marc has previously served in different roles as head of Aegon’s Group Business Development department, as President of the company’s life joint venture in China, as head of Aegon’s Public Policy and Regulatory Office and as head of Sustainability.

He is a board member of Aegon-Industrial Fund Management Company, Aegon’s asset management joint venture in China, and of Aegon Spain.



## Neil Smith

Former Senior Associate, Strategy and Sustainability team, Aegon

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*‘Reporting can teach you a lot about who you are as a company. If you get it right, it can be a big driver of change’.*

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Neil has been working in sustainability for the past 10 years, and has chaired the International Integrated Reporting Council’s Insurance Network, and the Financial Institutions Network. A regular speaker at global conferences on sustainability and integrated reporting, Neil has also lectured on sustainable development at Utrecht University.

Until recently, Neil was responsible for many of Aegon’s sustainability activities, including integrated reporting and the company’s approach to the Sustainable Development Goals, working across the US, Europe and Asia – producing seven integrated reports and winning an award along the way. Neil has now started his own consultancy, Koan – helping companies make sense of reporting.

Neil can be contacted at [neil.smith@wearekoan.com](mailto:neil.smith@wearekoan.com)

## Karen Koch

<IR> specialist within group finance, Eskom Holdings SOC Ltd

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*‘Integrated reporting is a valuable tool for stakeholder communication’.*

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Karen qualified as a chartered accountant, and worked in assurance with PwC for almost a decade. Thereafter, she joined Eskom as an IFRS adviser. Her duties have since included financial reporting, enterprise performance management and, most recently, integrated reporting. She is the editor-in-chief of Eskom’s integrated report, and is responsible for the end-to-end integrated reporting process, from concept to publication.

## Martin Buys

General manager for financial and management reporting, Eskom Holdings SOC Ltd

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*‘Integrated reporting should not be a once-a-year event but should be integrated into decision-making and risk management.’*

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Martin qualified as a chartered accountant and joined Eskom in 1987. During his career in Eskom he worked in several areas of the business, including finance, sales and pricing, as well as budgeting and planning. His current responsibilities include managing the preparation of the annual financial statements in terms of IFRS and the integrated report. He is also responsible for the development of the financial plan and budget, as well as monthly management reporting.

## Carrie Scott

Head of corporate brand and reputation management, Novartis

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*‘More meaningful information about both financial and non-financial performance helps build trust in an organisation and its ability to create value for the long term’.*

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Carrie Scott leads corporate brand and reputation management at Novartis AG. She is responsible for defining and managing the corporate brand and telling the Novartis corporate story in a consistent and compelling way. Her team manages the corporate brand strategy and visual identity, tracks the company’s reputation with key stakeholders, and creates the corporate narrative and reputation strategy. Carrie’s team also manages corporate responsibility (CR) communications and non-financial reporting, and is responsible for both the Novartis Annual Report and CR Report.

Carrie joined Novartis in 2007 in media relations and executive communications. Before joining Novartis, Carrie worked for Fleishman-Hillard. She joined the international communications agency in 1994, and worked for the consultancy in Belgium, Germany and the US.

Carrie graduated from the University of Illinois, Urbana-Champaign, Illinois, US. She lives in Basel, Switzerland.

## Charlie Hough

**Vice President & Global Head of Corporate Responsibility Strategy & Stakeholder Engagement, Novartis**

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*‘Providing quantitative data on financial, environmental and social impacts allows us to better measure and communicate the value we create for our stakeholders beyond financial value’*

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Charlie has worked with Novartis for 18 years, primarily in line management roles leading the OTC pharmaceutical business in Asia and North America, followed by being appointed Chief Marketing Officer for the OTC business. At the end of 2011, Charlie took on the role of Vice President and Head of Corporate Responsibility Strategy & Stakeholder Engagement, with the objective of leveraging his operational experience to develop and manage an integrated Novartis access to healthcare strategy and work with the Novartis divisions on implementation.

Prior to Novartis, Charlie worked with Monsanto, Bain & Co., Information Resources, Inc., Brown Brothers Harriman and Manufacturers Hanover Trust in strategy, business development and financial analysis roles. Charlie received a Master of Management degree from Northwestern University's Kellogg Graduate School of Management and a Bachelor of Arts degree from Yale University.

## Giuseppe Zammarchi

**Head of Group Sustainability and Foundations, UniCredit**

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*‘The integrated report is the result of a process based on integrated thinking that requires a deeper understanding of all the building blocks of the business’ value creation process.’*

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Giuseppe graduates in Business Administration in April 1998 at Università Commerciale L. Bocconi in Milan. After beginning his career in January 1997 in auditing and consulting within the financial services division of Arthur Andersen, Giuseppe joins UniCredit in March 2000.

He spent 9 years in the Investor Relations department of UniCredit, being in charge of relations with sell-side and buy-side equity analysts as well as with portfolio managers of the main shareholders of the stock. He is actively involved in the support to the top management in the various roadshows to present group's strategy and results in the period where UniCredit is in the international expansion phase.

He then moves to the Executive Communications department, being responsible for the team of people in charge of ghost writing for the top management of the company.

In 2014 he changed his position, joining the staff of the Group Chief Risk Officer, with direct responsibility for the coordination of the internal communication activities of Group Risk Management competence line and leading the Risk Culture strengthening program of the group.

In 2017 he joined Group Sustainability and Foundations department, becoming in November responsible for the unit which is in charge of preparing the consolidated Integrated Report (constituting a Non-Financial Information disclosure pursuant to Legislative Decree 254/2016, in application of EU Directive 2014/95) and overseeing the group's sustainability strategy and approach of the Group, including the two Foundations (UniCredit Foundation and UniCredit and Universities Foscolo Foundation).

## Bruno Gasparroni

**Senior Associate in the Group Sustainability and Foundations Unit, UniCredit**

Bruno Gasparroni works in Group Sustainability & Foundations in UniCredit since 2015. The unit supports the Company management in setting out a sustainability strategy, in embedding a sustainability approach into company activities, and also in defining the sustainability communication strategy including the responsibility for Integrated Reporting.

With more than 10 years' experience in Strategic Marketing and in Corporate Social Responsibility, Bruno has worked in different positions within the Group starting from Italian Commercial Network in 2005. In 2008 he joined the Small Business Marketing department in UniCredit Retail Division and in 2011 he started to work for Marketing Department in the Corporate Division.

# Appendix 2

## Average ratings from the 2017 <IR> Business Network Report Critique project

For each of the 45 corporate reports reviewed, <IR> Specialist Panel reviewers rated the quality of reporting against each aspect of the <IR> Framework. Ratings were on a scale of 1 to 5, where 1 = does not satisfy the <IR> Framework guidance at all, and 5 = fully satisfies the guidance.

The <IR> Specialist Panel includes Mark O’Sullivan of PwC, Grant Patterson of Grant Thornton, Dr Marvin Wee of Australian National University, Dr Gaia Melloni of the University of East Anglia, Beat Schweizer and Suzanne Erdt of Petranix, Jonathan Hanks of Incite, and expert reviewers and moderators from the IIRC and from ACCA.

Some organisations in the sample have not yet reported externally using the <IR> Framework’s principles but may be somewhat aligned to them based on their current practices and regulatory requirements. The individual reviews are used to inform companies on progress to date and opportunities for improvement.

The table below provides the average ratings given across the sample of 45 reports for each guiding principle, content element and fundamental concept of the <IR> Framework. The results from last year are shown in a separate column. In order to provide insights into specific areas of strengths and challenges, some guiding principles, content elements and fundamental concepts have been disaggregated in this year’s review: where this is the case, the related 2016 average rating is indicated with an asterix (\*).

It should be noted that the ratings given are subjective in nature, and although the reviews have been subject to moderation by ACCA and the IIRC, judgements vary from one reviewer to another.

The reports reviewed relate to accounting periods ended up to and including 31 March 2017.

FRAMEWORK PARAGRAPH REFERENCE	<IR> FRAMEWORK TEXT	AVERAGE RATING	2016 AVERAGE RATING
<b>RESPONSIBILITY FOR AN INTEGRATED REPORT</b>			
1.20	<ul style="list-style-type: none"> <li>An integrated report should include a statement from those charged with governance that includes:               <ul style="list-style-type: none"> <li>An acknowledgement of their responsibility to ensure the integrity of the integrated report</li> <li>An acknowledgement that they have applied their collective mind to the preparation and presentation of the integrated report</li> <li>Their opinion or conclusion about whether the integrated report is presented in accordance with this Framework</li> </ul> </li> </ul>	2.51	2.27
1.20	<ul style="list-style-type: none"> <li>or, if it does not include such a statement, it should explain:               <ul style="list-style-type: none"> <li>What role those charged with governance played in its preparation and presentation</li> <li>What steps are being taken to include such a statement in future reports</li> <li>The time frame for doing so, which should be no later than the organisation’s third integrated report that references this Framework.</li> </ul> </li> </ul>	1.36	1.20
<b>GUIDING PRINCIPLES</b>			
<b>Strategic focus and future orientation</b>			
3.3	<ul style="list-style-type: none"> <li>An integrated report should provide insight into the organisation’s strategy...</li> </ul>	3.87	3.78
3.3	<ul style="list-style-type: none"> <li>...and how that relates to its ability to create value in the short, medium and long term...</li> </ul>	3.29	3.24*
3.3	<ul style="list-style-type: none"> <li>...and to its use of and effects on the [six] capitals.</li> </ul>	3.18	3.24*

FRAMEWORK PARAGRAPH REFERENCE	<IR> FRAMEWORK TEXT	AVERAGE RATING	2016 AVERAGE RATING
<b>Connectivity of information</b>			
3.6	<ul style="list-style-type: none"> <li>An integrated report should show a holistic picture of the combination, interrelatedness and dependencies between factors that affect the organisation's ability to create value over time.</li> </ul>	3.47	3.44
<b>Stakeholder relationships</b>			
3.10	<ul style="list-style-type: none"> <li>An integrated report should provide insight into the nature and quality of the organisation's relationships with its key stakeholders, including how and to what extent the organisation understands, takes into account and responds to their legitimate needs and interests.</li> </ul>	3.53	3.73
<b>Materiality</b>			
3.17	<ul style="list-style-type: none"> <li>An integrated report should disclose information about matters that substantively affect the organisation's ability to create value over the short, medium and long term.</li> </ul>	3.18	3.68
<b>Conciseness</b>			
3.36	<ul style="list-style-type: none"> <li>An integrated report should be concise.</li> </ul>	3.36	3.15
<b>Reliability and completeness</b>			
3.39	<ul style="list-style-type: none"> <li>An integrated report should include all material matters, both positive and negative, in a balanced way and without material error.</li> </ul>	3.56	3.44*
3.44	<ul style="list-style-type: none"> <li>A balanced integrated report has no bias in the selection or presentation of information. Information in the report is not slanted, weighted, emphasized, de-emphasized, combined, offset or otherwise manipulated to change the probability that it will be received either favourably or unfavourably.</li> </ul>	3.49	3.44*
<b>Consistency and comparability</b>			
3.54	<ul style="list-style-type: none"> <li>The information in an integrated report should be presented on a basis that is consistent over time...</li> </ul>	3.87	2.78
3.54	<ul style="list-style-type: none"> <li>...and in a way that enables comparison with other organisations, to the extent it is material to the organisation's own ability to create value over time.</li> </ul>	3.4	2.32
<b>CONTENT ELEMENTS</b>			
<b>Organisational overview and external environment</b>			
4.4	<ul style="list-style-type: none"> <li>An integrated report should answer the question: What does the organisation do...</li> </ul>	4.36	4.32*
4.4	<ul style="list-style-type: none"> <li>...and what are the circumstances under which it operates?</li> </ul>	4	4.32*
<b>Governance</b>			
4.8	<ul style="list-style-type: none"> <li>An integrated report should answer the question: How does the organisation's governance structure support its ability to create value in the short, medium and long term?</li> </ul>	3.18	3.39
<b>Business model</b>			
4.10	<ul style="list-style-type: none"> <li>An integrated report should answer the question: What is the organisation's business model?</li> </ul>	3.55	3.54
<b>Risks and opportunities</b>			
4.23	<ul style="list-style-type: none"> <li>An integrated report should answer the question: What are the specific risks ... that affect the organisation's ability to create value over the short, medium and long term...?</li> </ul>	3.64	3.44*
4.23	<ul style="list-style-type: none"> <li>What are the specific ... opportunities that affect the organisation's ability to create value over the short, medium and long term...?</li> </ul>	3.27	3.44*
4.23	<ul style="list-style-type: none"> <li>... and how is the organisation dealing with them?</li> </ul>	3.62	3.46

FRAMEWORK PARAGRAPH REFERENCE	<IR> FRAMEWORK TEXT	AVERAGE RATING	2016 AVERAGE RATING
<b>Strategy and resource allocation</b>			
4.27	<ul style="list-style-type: none"> <li>An integrated report should answer the question: Where does the organisation want to go...?</li> </ul>	3.84	3.76*
4.27	<ul style="list-style-type: none"> <li>...and how does it intend to get there?</li> </ul>	3.49	3.76*
4.29	<ul style="list-style-type: none"> <li>What differentiates the organisation to give it competitive advantage and enable it to create value?</li> </ul>	3.42	3.46
<b>Performance</b>			
4.30	<ul style="list-style-type: none"> <li>An integrated report should answer the question: To what extent has the organisation achieved its strategic objectives for the period...?</li> </ul>	3.49	3.54
4.30	<ul style="list-style-type: none"> <li>...and what are its outcomes in terms of effects on the capitals?</li> </ul>	3.29	3.12
<b>Outlook</b>			
4.34	<ul style="list-style-type: none"> <li>An integrated report should answer the question: What challenges and uncertainties is the organisation likely to encounter in pursuing its strategy, and what are the potential implications for its business model and future performance?</li> </ul>	3.02	3.29
<b>Basis of preparation and presentation</b>			
4.40	<ul style="list-style-type: none"> <li>An integrated report should answer the question: How does the organisation determine what matters to include in the integrated report...?</li> </ul>	2.98	3.24*
4.40	<ul style="list-style-type: none"> <li>...and how are such matters quantified or evaluated?</li> </ul>	2.87	3.24*
<b>FUNDAMENTAL CONCEPTS</b>			
<b>Value creation for the organisation and for others</b>			
2.4 – 2.9	<ul style="list-style-type: none"> <li>Overall, does the report explain how the organisation creates value for itself...?</li> </ul>	4	3.71*
2.4 – 2.9	<ul style="list-style-type: none"> <li>...and others?</li> </ul>	3.91	3.71*
<b>The capitals</b>			
2.10 – 2.19	<ul style="list-style-type: none"> <li>Overall, does the report provide information on the capitals (i.e. Financial, Manufactured, Intellectual, Human, Social and Relationship, Natural) that the organisation uses or affects and which underpin its ability to create value?</li> </ul>	3.8	3.71
<b>Value creation process</b>			
2.20 – 2.29	<ul style="list-style-type: none"> <li>The value creation process [aligns] with the Content Elements</li> </ul>	3.67	–

# Appendix 3

## <IR> Business Network participants interviewed:

ORGANISATION	HEADQUARTERS	INDUSTRY	NUMBER OF INTEGRATED REPORTS PREPARED <sup>8</sup>	NOTES
Aegon	Netherlands	Life insurance, pensions and asset management	6	Aegon first adopted <IR> in its 2011 report.
Eskom	South Africa	Energy	6	Eskom made its first real effort to apply the <IR> Framework for the year ending 31 March 2012.
United Utilities	UK	Water	4	United Utilities believes itself to be the only FTSE 100 company to have produced four integrated reports.
FMO	Netherlands	Banking	3	FMO adopted <IR> in 2014.
UniCredit	Italy	Banking	3	UniCredit issued its first integrated report in 2014, but has been reporting sustainability information since 2000.
Novartis	Switzerland	Healthcare	0	Novartis considers itself to be a 'combined reporter' i.e. financial and non-financial metrics are included in its annual report in a combined way.

### YEAR ENDS

**31 December 2016:** Aegon, FMO, UniCredit

**31 March 2017:** Eskom, United Utilities

**31 December 2017:** Novartis (reviewers looked at report for year ended 31 December 2016, but the extract in this report is taken from year end December 2017 report).

<sup>8</sup> Up to and including reporting periods ended 31 March 2017 (31 December 2017 for Novartis).

# Appendix 4

## Links to company accounts from which examples have been taken:



### Aegon

2016 Review

<https://www.aegon.com/siteassets/investors--media/reports--sec-filings/aegon-annual-review-2016.pdf>



Review Reporting Supplement 2016

<https://www.aegon.com/siteassets/investors--media/reports--sec-filings/2016-review-reporting-supplement.pdf>



### ArcelorMittal

Annual review 2016

<http://annualreview2016.arcelormittal.com/>



### BASF

BASF Report 2016

[https://www.basf.com/documents/corp/en/about-us/publications/reports/2017/BASF\\_Report\\_2016.pdf](https://www.basf.com/documents/corp/en/about-us/publications/reports/2017/BASF_Report_2016.pdf)



### Eskom

Integrated Report 2017

[http://www.eskom.co.za/IR2017/Documents/Eskom\\_integrated\\_report\\_2017.pdf](http://www.eskom.co.za/IR2017/Documents/Eskom_integrated_report_2017.pdf)



### Far East Tone

2016 Corporate Social Responsibility Report

[https://www.fetnet.net/cs/Satellite?blobcol=urldownload&blobheader=application%2Fpdf&blobkey=id&blobtable=co\\_SocietyReport&blobwhere=3000009983574&ssbinary=true](https://www.fetnet.net/cs/Satellite?blobcol=urldownload&blobheader=application%2Fpdf&blobkey=id&blobtable=co_SocietyReport&blobwhere=3000009983574&ssbinary=true)



### FMO

Annual Report 2016

<http://annualreport.fmo.nl/en/library/download/urn:uuid:638188d0-5def-49f4-bf5a-7db9c94ddb52/2016+annual+report.pdf>



### Nedbank Group

Integrated Report 2016

<https://www.nedbank.co.za/content/dam/nedbank/site-assets/AboutUs/Information%20Hub/Integrated%20Report/2016/Nedbank%20Integrated%20report%20Final.pdf>



### Novartis

Annual Report 2017

<https://www.novartis.com/sites/www.novartis.com/files/novartis-annual-report-2017-en.pdf>



### UniCredit

Integrated Report 2016

[https://www.unicreditgroup.eu/content/dam/unicreditgroup-eu/documents/en/sustainability/sustainability-reports/2016/2016-Integrated-Report\\_interactive\\_13042017.pdf](https://www.unicreditgroup.eu/content/dam/unicreditgroup-eu/documents/en/sustainability/sustainability-reports/2016/2016-Integrated-Report_interactive_13042017.pdf)



### United Utilities

Annual Report 2017

<http://unitedutilities.annualreport2017.com/media/83269/united-utilities-ar2017-web-ready.pdf>

# Appendix 5

## Countries represented in online survey of <IR> Business Network participants:

Australia  
Canada  
Germany  
Italy (2)  
Mauritius  
Netherlands (5)  
New Zealand  
Russia  
Turkey (2)  
UK (4)  
US

Note: numbers of respondents are shown in brackets where more than one.





