Insights into integrated reporting 2.0: walking the talk
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ACKNOWLEDGEMENTS

ACCA would like to thank the IIRC for giving us the opportunity to take part, for the second year running, in the <IR> Business Network Report Critique project. We are grateful to the reviewers on the <IR> Specialist Panel (listed in Appendix 2) for their expert input, and also to the interviewees (listed in Appendix 1) for giving their time to be interviewed for this report.
YEN-PEI CHEN

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SARAH PERRIN

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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.

Helen Brand OBE
Chief executive
ACCA
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.

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 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.

![FIGURE 1.1: The types of report reviewed](image-url)
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%).

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.

76%

of reports this year referred to the <IR> Framework (up from 59% 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).\footnote{All paragraph and section numbers in the following text refer to paragraphs or sections of the International <IR> Framework.}

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
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.
‘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.

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**APPLYING TECHNOLOGY**

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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, 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.

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5. Linking strategy and performance to the capitals

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.

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’.

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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.

4 Weblinks to all best practice examples cited in this report are provided in Appendix 4.

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.

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).
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.

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.
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.
In its Annual Report 2017, Novartis summarised its mission, vision and strategy in an admirably clear and concise way. This conveys a very strong sense to report users that innovation is at the heart of Novartis’ strategic advantage.
Work cross-functionally with colleagues responsible for strategy and risk management to align reporting with strategy.

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.
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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
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’.

‘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.’
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 new 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 island 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 610,000 more households in the North West.
  - We will install 3 million extra water meters, covering 70 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
- 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) underpin both long-term and shorter-term planning to identify how we can best deliver our 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 PPM and other performance measures, which help us to formulate our future improvement plans for our various stakeholders.

Wholesale business areas

All of the group’s ROCs, of the order of £10 billion, sit within the wholesale water and wastewater business areas, and we are allowed to earn an annual profit 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 time cost assessment model. Our cost performance against our allowed cost of debt and equity will determine how much our performance is or under-performance is penalised.

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 small 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.

Vision: to be the best UK water and wastewater company, providing great service to our customers
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.
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.
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

8. Basis of preparation
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 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.

‘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’.6 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’,

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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.

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.

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.

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.
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.
**Country Priorities**

<table>
<thead>
<tr>
<th>Macro Dimension</th>
<th>Indicator</th>
<th>Italy</th>
<th>Germany</th>
<th>Austria</th>
<th>CEE*</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Social Wellbeing</strong></td>
<td>Employment rate of people 20-64 years</td>
<td></td>
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<tr>
<td></td>
<td>Social decay (or incivilities) rate</td>
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<td></td>
<td>Work satisfaction</td>
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<tr>
<td></td>
<td>Citizens who benefit from infancy services</td>
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<tr>
<td><strong>Economic Wellbeing</strong></td>
<td>People suffering poor housing conditions</td>
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<tr>
<td></td>
<td>Severely materially deprived people</td>
<td></td>
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<tr>
<td></td>
<td>Index of subjective evaluation of economic distress</td>
<td></td>
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<tr>
<td><strong>Education and Efficient use of talent</strong></td>
<td>Country capacity to attract talent</td>
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<tr>
<td></td>
<td>Percentage of young people not in education, employment, or training (NEET)</td>
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<tr>
<td></td>
<td>Percentage of people participating in formal or non-formal education</td>
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<tr>
<td><strong>Health</strong></td>
<td>Healthy life expectancy at birth</td>
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<tr>
<td></td>
<td>Waiting lists</td>
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<tr>
<td></td>
<td>Life expectancy without activity limitations at 65 years of age</td>
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<tr>
<td><strong>Environment &amp; Landscape</strong></td>
<td>Energy from renewable sources</td>
<td></td>
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<tr>
<td></td>
<td>Public expenditure for recreation, culture and religion</td>
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<tr>
<td></td>
<td>Emissions of CO₂ per inhabitant</td>
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<tr>
<td><strong>Infrastructure &amp; Quality of services</strong></td>
<td>Quality of overall infrastructure</td>
<td></td>
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<td></td>
<td>Quality of roads</td>
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<td></td>
<td>Internet bandwidth</td>
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<tr>
<td><strong>Financial Market</strong></td>
<td>Availability of financial services</td>
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<td></td>
<td>Ease of access to loans</td>
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<td></td>
<td>Venture capital availability</td>
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<tr>
<td><strong>Business Sophistication</strong></td>
<td>Local supplier quality</td>
<td></td>
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<tr>
<td></td>
<td>Extent of marketing</td>
<td></td>
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<tr>
<td></td>
<td>Nature of competitive advantage</td>
<td></td>
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<tr>
<td><strong>Innovation</strong></td>
<td>Innovation rate of the national productive system</td>
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<tr>
<td></td>
<td>Research intensity</td>
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<tr>
<td></td>
<td>Patent propensity</td>
<td></td>
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</tbody>
</table>

* 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. The inherent uncertainty surrounding forward-looking statements is described.
If different stakeholders demand different information, focus on the topics that are most relevant to the execution of your organisation’s strategy.

**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 the materiality-assessment process.

Van Weede says: ‘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’. Aegon’s board has been discussing its materiality matrix, produced as a result of the materiality-assessment process. This proved to be, on average, one of the lower-scoring areas reviewed – although

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.
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 of 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
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’.

‘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.’
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.

<table>
<thead>
<tr>
<th>Material matter</th>
<th>Current impact on value creation</th>
<th>Timeframe of impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regulatory environment and secularity of the electricity price path, including the treatment of RECUs</td>
<td>Negative</td>
<td>Short, medium and long term</td>
</tr>
<tr>
<td>The impact of economic performance, cost, management and liquidity</td>
<td>Negative</td>
<td>Short to medium term</td>
</tr>
<tr>
<td>Funding plan and the impact of interest rate movements, together with Governance support</td>
<td>Both positive and negative</td>
<td>Short, medium and long term</td>
</tr>
<tr>
<td>Integration of customer dialogue and engagement between Eskom and its stakeholders</td>
<td>Negative</td>
<td>Short to medium term</td>
</tr>
<tr>
<td>Sustainability performance, including emissions, water use and environmental commitments, which may affect our ability to maintain and develop our grid infrastructure</td>
<td>Negative</td>
<td>Short to medium term</td>
</tr>
<tr>
<td>Energy mix and carbon intensity of our grid, including renewables and nuclear energy, coupled with concerns around water scarcity and climate change</td>
<td>May be either positive or negative</td>
<td>Medium to long term</td>
</tr>
<tr>
<td>Skills and transformation of our workforce</td>
<td>Positive</td>
<td>Medium to long term</td>
</tr>
<tr>
<td>Governance and procurement practices</td>
<td>Perceived as negative</td>
<td>Short, medium and long term</td>
</tr>
</tbody>
</table>

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

- 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.
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.

<table>
<thead>
<tr>
<th>Question</th>
<th>Answer</th>
</tr>
</thead>
<tbody>
<tr>
<td>WHAT DOES VALUE MEAN FOR ME AND MY ORGANISATION?</td>
<td></td>
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<tr>
<td>WHAT DIFFERENTIATES MY ORGANISATION FROM ITS COMPETITORS?</td>
<td></td>
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<tr>
<td>WHAT IS MY ORGANISATION’S MISSION?</td>
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<tr>
<td>WHERE DOES MY ORGANISATION WANT TO GO (ITS VISION)?</td>
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<tr>
<td>WHO ARE THE KEY STAKEHOLDERS WE RELY ON TO FULFIL OUR MISSION AND REALISE OUR VISION?</td>
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<tr>
<td>WHAT KEY RESOURCES DO WE NEED TO DO THIS?</td>
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</tr>
<tr>
<td>HOW DO WE PUT OUR MISSION AND VISION INTO ACTION?</td>
<td>HOW IS OUR STRATEGY?</td>
</tr>
<tr>
<td>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?</td>
<td>HOW WILL I KNOW WHETHER MY ORGANISATION IS FULFILLING ITS MISSION AND REALISING ITS VISION? HOW WILL OUR KEY STAKEHOLDERS KNOW?</td>
</tr>
<tr>
<td>HOW CAN I TALK TO THE BOARD ABOUT THESE QUESTIONS?</td>
<td></td>
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</tbody>
</table>
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

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

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

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

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

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

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

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.

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

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

Integrated reporting is a valuable tool for stakeholder communication.

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

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

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

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.

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

‘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’

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

‘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.’

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.

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.
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.

<table>
<thead>
<tr>
<th>FRAMEWORK PARAGRAPH REFERENCE</th>
<th>&lt;IR&gt; FRAMEWORK TEXT</th>
<th>AVERAGE RATING</th>
<th>2016 AVERAGE RATING</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>RESPONSIBILITY FOR AN INTEGRATED REPORT</strong></td>
<td>1.20 • An integrated report should include a statement from those charged with governance that includes:</td>
<td>2.51</td>
<td>2.27</td>
</tr>
<tr>
<td></td>
<td>- An acknowledgement of their responsibility to ensure the integrity of the integrated report</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- An acknowledgement that they have applied their collective mind to the preparation and presentation of the integrated report</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Their opinion or conclusion about whether the integrated report is presented in accordance with this Framework</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1.20 • or, if it does not include such a statement, it should explain:</td>
<td>1.36</td>
<td>1.20</td>
</tr>
<tr>
<td></td>
<td>- What role those charged with governance played in its preparation and presentation</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- What steps are being taken to include such a statement in future reports</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- The time frame for doing so, which should be no later than the organisation’s third integrated report that references this Framework.</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>GUIDING PRINCIPLES</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Strategic focus and future orientation</td>
<td>3.3 • An integrated report should provide insight into the organisation’s strategy...</td>
<td>3.87</td>
<td>3.78</td>
</tr>
<tr>
<td></td>
<td>3.3 • ...and how that relates to its ability to create value in the short, medium and long term...</td>
<td>3.29</td>
<td>3.24*</td>
</tr>
<tr>
<td></td>
<td>3.3 • ...and to its use of and effects on the [six] capitals.</td>
<td>3.18</td>
<td>3.24*</td>
</tr>
<tr>
<td>FRAMEWORK REFERENCE</td>
<td>&lt;IR&gt; FRAMEWORK TEXT</td>
<td>AVERAGE RATING</td>
<td>2016 AVERAGE RATING</td>
</tr>
<tr>
<td>----------------------</td>
<td>---------------------</td>
<td>----------------</td>
<td>-------------------</td>
</tr>
<tr>
<td>Connectivity of information</td>
<td>• 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.</td>
<td>3.47</td>
<td>3.44</td>
</tr>
<tr>
<td>Stakeholder relationships</td>
<td>• 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.</td>
<td>3.53</td>
<td>3.73</td>
</tr>
<tr>
<td>Materiality</td>
<td>• 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.</td>
<td>3.18</td>
<td>3.68</td>
</tr>
<tr>
<td>Conciseness</td>
<td>• An integrated report should be concise.</td>
<td>3.36</td>
<td>3.15</td>
</tr>
<tr>
<td>Reliability and completeness</td>
<td>• An integrated report should include all material matters, both positive and negative, in a balanced way and without material error.</td>
<td>3.56</td>
<td>3.44*</td>
</tr>
<tr>
<td></td>
<td>• 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.</td>
<td>3.49</td>
<td>3.44*</td>
</tr>
<tr>
<td>Consistency and comparability</td>
<td>• The information in an integrated report should be presented on a basis that is consistent over time…</td>
<td>3.87</td>
<td>2.78</td>
</tr>
<tr>
<td></td>
<td>…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.</td>
<td>3.4</td>
<td>2.32</td>
</tr>
</tbody>
</table>

**CONTENT ELEMENTS**

**Organisational overview and external environment**

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>4.4</td>
<td>• An integrated report should answer the question: What does the organisation do…</td>
</tr>
<tr>
<td>4.4</td>
<td>…and what are the circumstances under which it operates?</td>
</tr>
<tr>
<td>4.8</td>
<td>• 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?</td>
</tr>
</tbody>
</table>

**Governance**

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>4.10</td>
<td>• An integrated report should answer the question: What is the organisation’s business model?</td>
</tr>
</tbody>
</table>

**Business model**

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>4.23</td>
<td>• 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…?</td>
</tr>
<tr>
<td>4.23</td>
<td>• What are the specific … opportunities that affect the organisation’s ability to create value over the short, medium and long term…?</td>
</tr>
<tr>
<td>4.23</td>
<td>… and how is the organisation dealing with them?</td>
</tr>
</tbody>
</table>
### FRAMEWORK TEXT

<table>
<thead>
<tr>
<th>FRAMEWORK PARAGRAPH REFERENCE</th>
<th>&lt;IR&gt; FRAMEWORK TEXT</th>
<th>AVERAGE RATING</th>
<th>2016 AVERAGE RATING</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strategy and resource allocation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4.27</td>
<td>• An integrated report should answer the question: Where does the organisation want to go…?</td>
<td>3.84</td>
<td>3.76*</td>
</tr>
<tr>
<td>4.27</td>
<td>• …and how does it intend to get there?</td>
<td>3.49</td>
<td>3.76*</td>
</tr>
<tr>
<td>4.29</td>
<td>• What differentiates the organisation to give it competitive advantage and enable it to create value?</td>
<td>3.42</td>
<td>3.46</td>
</tr>
<tr>
<td>Performance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4.30</td>
<td>• An integrated report should answer the question: To what extent has the organisation achieved its strategic objectives for the period…?</td>
<td>3.49</td>
<td>3.54</td>
</tr>
<tr>
<td>4.30</td>
<td>• …and what are its outcomes in terms of effects on the capitals?</td>
<td>3.29</td>
<td>3.12</td>
</tr>
<tr>
<td>Outlook</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4.34</td>
<td>• 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?</td>
<td>3.02</td>
<td>3.29</td>
</tr>
<tr>
<td>Basis of preparation and presentation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4.40</td>
<td>• An integrated report should answer the question: How does the organisation determine what matters to include in the integrated report…?</td>
<td>2.98</td>
<td>3.24*</td>
</tr>
<tr>
<td>4.40</td>
<td>• …and how are such matters quantified or evaluated?</td>
<td>2.87</td>
<td>3.24*</td>
</tr>
<tr>
<td><strong>FUNDAMENTAL CONCEPTS</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Value creation for the organisation and for others</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2.4 – 2.9</td>
<td>• Overall, does the report explain how the organisation creates value for itself…?</td>
<td>4</td>
<td>3.71*</td>
</tr>
<tr>
<td>2.4 – 2.9</td>
<td>• …and others?</td>
<td>3.91</td>
<td>3.71*</td>
</tr>
<tr>
<td>The capitals</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2.10 – 2.19</td>
<td>• 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?</td>
<td>3.8</td>
<td>3.71</td>
</tr>
<tr>
<td>Value creation process</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2.20 – 2.29</td>
<td>• The value creation process [aligns] with the Content Elements</td>
<td>3.67</td>
<td>–</td>
</tr>
</tbody>
</table>
## <IR> Business Network participants interviewed:

<table>
<thead>
<tr>
<th>ORGANISATION</th>
<th>HEADQUARTERS</th>
<th>INDUSTRY</th>
<th>NUMBER OF INTEGRATED REPORTS PREPARED</th>
<th>NOTES</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aegon</td>
<td>Netherlands</td>
<td>Life insurance, pensions and asset management</td>
<td>6</td>
<td>Aegon first adopted &lt;IR&gt; in its 2011 report.</td>
</tr>
<tr>
<td>Eskom</td>
<td>South Africa</td>
<td>Energy</td>
<td>6</td>
<td>Eskom made its first real effort to apply the &lt;IR&gt; Framework for the year ending 31 March 2012.</td>
</tr>
<tr>
<td>United Utilities</td>
<td>UK</td>
<td>Water</td>
<td>4</td>
<td>United Utilities believes itself to be the only FTSE 100 company to have produced four integrated reports.</td>
</tr>
<tr>
<td>FMO</td>
<td>Netherlands</td>
<td>Banking</td>
<td>3</td>
<td>FMO adopted &lt;IR&gt; in 2014.</td>
</tr>
<tr>
<td>UniCredit</td>
<td>Italy</td>
<td>Banking</td>
<td>3</td>
<td>UniCredit issued its first integrated report in 2014, but has been reporting sustainability information since 2000.</td>
</tr>
<tr>
<td>Novartis</td>
<td>Switzerland</td>
<td>Healthcare</td>
<td>0</td>
<td>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.</td>
</tr>
</tbody>
</table>

### 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).

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8 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  
*Review Reporting Supplement 2016*  

**ArcelorMittal**
Annual review 2016  
http://annualreview2016.arcelormittal.com/

**BASF**
BASF Report 2016  

**Eskom**
Integrated Report 2017  

**Far East Tone**
2016 Corporate Social Responsibility Report  

**FMO**
Annual Report 2016  

**Nedbank Group**
Integrated Report 2016  

**Novartis**
Annual Report 2017  

**UniCredit**
Integrated Report 2016  

**United Utilities**
Annual Report 2017  
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.