



Understanding transformation

BUILDING THE BUSINESS CASE FOR INTEGRATED REPORTING



INTEGRATED REPORTING <IR>

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Foreword

PROFESSOR MERVYN KING, CHAIRMAN OF THE IIRC

There is increasing momentum towards Integrated Reporting worldwide. At the International Integrated Reporting Council (IIRC), we define Integrated Reporting as the language evidencing sustainable business. It is the means by which companies communicate how value is created and will be enhanced over the short, medium and long term. It involves a set of processes and activities, one result of which is communication, most visibly through a concise, annual “integrated report”, about the way in which an organization’s strategy, governance, performance and prospects lead to the creation and enhancement of value. How each organization attempts to achieve this will vary.

Integrated Reporting reflects and supports ‘integrated thinking’, defined as the ability of those within the organization, especially management, to understand the interconnections between the full range of functions, operations, resources and relationships which have a material effect on the organization’s ability to create value over time. The journey towards Integrated Reporting therefore also entails a mindset change about how the company makes its money.

Those organizations willing to take the lead in reporting are participating in the IIRC’s Pilot Programme, through which we aim to develop an International Integrated Reporting Framework. Some are experiencing exciting changes during this transition period and it is these changes, together with the benefits, that we want to capture in this document.

We are grateful to Black Sun for initiating and conducting the research to help us track these changes which provide clear evidence of the business benefits of Integrated Reporting.

Executive summary

At Black Sun, we are working closely with the IIRC to support their development of the International Integrated Reporting Framework. We have worked in association with the IIRC to develop this report, ‘Understanding transformation: Building the business case for Integrated Reporting’, which is the first of two that aim to understand the processes companies go through as they move towards Integrated Reporting.

In the last two years, there has been increasing momentum towards better reporting, which has been reflected by the amount published on the topic. Our research builds on this wider body of literature which addresses questions such as what best practice in Integrated Reporting looks like¹, why change in this direction is necessary² and what more is needed to get there³. We focus on organisations that are already shifting towards better integration, although they are at different stages and progressing at different speeds. Our findings aim to build the business case for Integrated Reporting by providing evidence of the changes and benefits that the journey towards integration is bringing now and is expected to bring in future. They also reinforce the point that Integrated Reporting will not happen without integrated thinking.

WHAT IS INTEGRATED REPORTING?

Integrated Reporting provides an opportunity for companies to present a holistic and complete picture of the business in a clear, concise, connected and comparable manner. It is a means of presenting the material information about the organisation’s strategy, governance and performance on commercial, social and environmental issues. Through effectively connecting these often siloed areas, businesses are able to provide not only an update on past performance but also a long-term perspective of future value generation. Integrated Reporting is, therefore, good reporting.

“Integrated Reporting builds on the practice of financial reporting, and environmental, social and governance reporting. It equips companies to manage their operations, brand and reputation strategically and to manage better any risks that may compromise the long-term sustainability of the business.”

Professor Mervyn King, Chairman, IIRC and Chairman for the King Committee on Corporate Governance

“It’s not about speed; it’s about the right direction...”

(Public sector organisation)

1 See UBS (20 June 2012). “UBS Investment Research Q-Series: What is ‘Integrated Reporting’?”

2 See CIMA, PwC and Tomorrow’s Company (April 2011). “Tomorrow’s Corporate Reporting: A critical system at risk”

3 See Deloitte (February 2012). “Integrated Reporting: Navigating your way to a truly Integrated Report”

OUR FINDINGS

The respondents to our research survey and subsequent interviews were generally extremely positive about the impact that their journey towards Integrated Reporting is having on their organisations. As expected, companies are facing challenges but they are also finding ways to overcome them. Inevitably challenges will remain but we expect them to decrease as reporting develops.

There is a broad recognition that achieving full integration will take time but those taking steps towards it are already seeing important business benefits from their involvement.

The research found that Integrated Reporting is beginning to drive positive changes within organisations including:



Connecting departments – one of the most mentioned benefits of Integrated Reporting is the opportunity it provides to connect teams from across an organisation, breaking down silos and leading to more integrated thinking.

[Detail on page 04](#)



Improved internal processes leading to a better understanding of the business – changes to systems driven by Integrated Reporting requirements are providing greater visibility across business activities and helping to improve understanding of how organisations create value in the broadest sense.

[Detail on page 08](#)



Increased focus and awareness of senior management – a shift to Integrated Reporting is increasing the interest and engagement of senior management in issues around the long-term sustainability of the business, which is helping them to gain a more holistic understanding of their organisations.

[Detail on page 12](#)



Better articulation of the strategy and business model – better understanding of organisational activities is enabling companies to establish a holistic business model and helping to streamline communications.

[Detail on page 15](#)



Creating value for stakeholders – organisations are starting to identify ways to measure the value to stakeholders of managing and reporting on sustainability issues.

[Detail on page 18](#)

Much of the change to achieve Integrated Reporting needs to be driven by companies themselves and the development by the IIRC of the International Integrated Reporting Framework is enabling companies to shape the process based on their own experiences. As a market-led initiative, business is driving the innovation that is taking place and shaping the development and thinking on presenting solutions on how Integrated Reporting should be managed and delivered. However, there are important roles for others as well.

In particular:

- More external pressure would be welcomed by those pushing this agenda within companies, particularly from investors
- Benchmarks and other references would help those without senior-level engagement to build the case for Integrated Reporting
- There is a demand for providers of assurance and auditing to offer a more integrated service to companies

CONNECTING DEPARTMENTS



“It’s another way of
pushing and driving
change internally...”

(Member-owned credit union)

One of the most widely discussed benefits of Integrated Reporting has been improved cooperation between different departments within organisations. Such teams may include finance, sustainable development, investor relations, corporate governance and legal. This reflects the findings reported in the IIRC’s 2012 Yearbook, which highlighted the way in which “working across departments to connect information in order to develop Integrated Reporting can help break down ‘silos’ and lead to stronger cross-functional communications”⁴.

The theme of connectivity is one which arises repeatedly in recent research on Integrated Reporting. For example, a KPMG report argued that “Successful Integrated Reporting is not just about reporting, but about coordinating different disciplines within the business and focusing on the organization’s core strategy”⁵. Connecting different teams across the business is an important step to achieving the integrated thinking necessary to underpin Integrated Reporting. It not only helps to reduce the repetitions and contradictions that are a feature of many traditional annual reports, but can also identify efficiencies between departments together with opportunities to make better use of information.

Our research found that those on the journey to Integrated Reporting expect significant benefits in terms of connecting departments. In this way, Integrated Reporting will enable companies to:

- Create internal linkages between teams that previously worked in silos
- Embed the concept of long-term business sustainability deep within the organisation by bringing it into the core functions of the business

- Drive better integrated thinking internally, helping businesses to make clearer links between financial and non-financial key performance indicators (KPIs) by aligning environmental, social and governance (ESG) issues in the business

This was echoed by those who are further along the journey towards Integrated Reporting.

Evidence of changes underway:

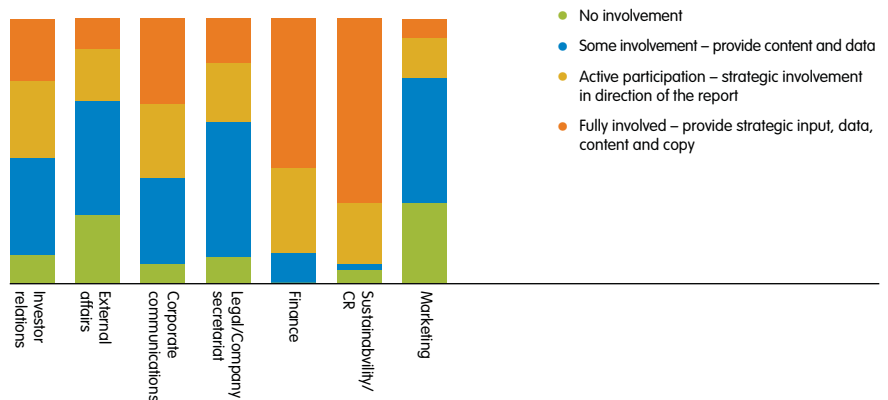
1. BREAKING DOWN SILOS AND BUILDING RELATIONSHIPS BETWEEN TEAMS

Participants in our research were extremely positive about the opportunities for relationship building that the Integrated Reporting journey is bringing with it. A significant 93% agreed that moving to an Integrated Reporting framework leads to the development of improved cross-functional working processes, breaking down silos between teams.

Responsibility for driving cooperation between teams varies between organisations. For some it is the sustainability team which is working to break down silos between financial reporting lines. For others, it is the finance team which is driving the sustainability department to address issues in financial terms and to consider the economic benefits of their priorities. In addition, many organisations reported that senior management are driving collaboration from the top down. Together these two teams are the ones most likely to be fully involved in Integrated Reporting, although respondents identified a number of other teams whose involvement ranges from strategic input to content provision.

Our research found that organisations which invest time in engaging a range of teams from across the business in the reporting process are achieving changes in corporate culture more quickly.

What is the level of involvement of these teams in contributing to your Integrated Report?



4 Integrated Reporting – The Pilot Programme 2012 Yearbook: Capturing the experiences of global businesses and investors, p.5

5 KPMG (May 2012), “Integrated Reporting: Performance insight through Better Business Reporting”, Issue 2

“Sustainable development used to be considered a separate part of the business; now things are changing...”

(Private company)

2. BETTER RECOGNITION OF THE VALUE OF ESG ISSUES

A majority of respondents stated that sustainability is currently somewhat understood within their organisations. Almost all of those who said it is totally understood have been reporting for more than six years. The research also asked how far sustainability is integrated, with 73% of respondents saying that it was somewhat integrated. The 18% of respondents who said that sustainability was totally integrated came from organisations that had been reporting for at least four years. This provides evidence for a correlation between reporting and integration.

Many respondents said that a range of teams were becoming more open to environmental, social and governance issues and starting to recognise their value. This is because the organisations in our research are working towards understanding their material sustainability issues better and linking them to financial drivers. The process is two way, with sustainability teams learning to use business language better to build cases for change and improvement. Consequently they are ensuring that sustainability issues are perceived by others as more aligned with operations and overall strategy.

This was echoed in our findings as several respondents said that achieving recognition that sustainable development is linked to business strategy is one of the most important internal changes they are already experiencing through the process of Integrated Reporting.

The shift in strategic thought is leading to better alignment of financial and

non-financial information, which is helping to demonstrate the value of the business and make reporting feel more relevant to organisations. This explains why 95% of respondents agreed that reporting on KPIs is encouraging a greater internal focus on delivering against them.

3. IMPROVED INTERNAL SUPPORT REPRESENTING SHIFTS IN ATTITUDES

Our research found that many organisations are achieving important shifts in corporate culture and attitudes towards Integrated Reporting. Initially, changing attitudes to reporting and disclosure internally can present some barriers for most organisations. Overall, 67.5% of respondents identified conflicting priorities between teams or individuals as some sort of barrier to progress with Integrated Reporting.

According to those respondents making progress in gaining internal support, the education and engagement process must be ongoing to achieve recognition of the value of Integrated Reporting. One company pointed to the fact that the economic climate is now driving the need for a more comprehensive account of their business and that this has helped to change attitudes in their legal department.

Organisations are using workshops to engage colleagues, rather than relying solely on broadcasting messages through internal communications. There is definitely scope for organisations to do more in this area as 27% admit to having done nothing yet to engage colleagues.



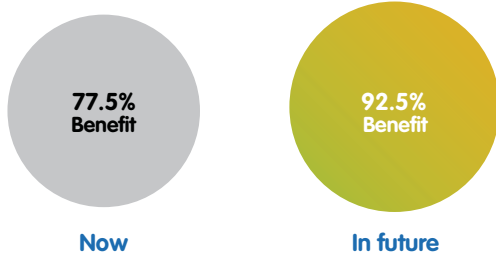
Case study

ASSOCIATION OF CHARTERED CERTIFIED ACCOUNTANTS (ACCA)

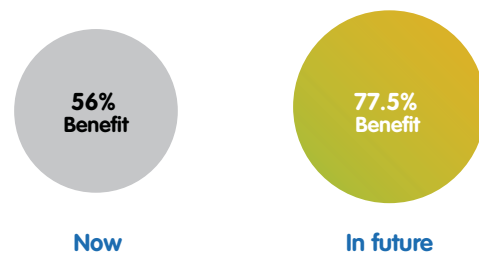
“For ACCA, the process of preparing our Integrated Report required us to adopt a fresh approach to our planning and internal communications. We ran workshops with senior staff to ascertain which areas of the organisation were key contributors to ACCA’s strategy and operations and where information relevant to these key areas would come from. We also put into place a broader stakeholder engagement process with ACCA employees, students and members (professional accountants) to find out what they wanted to know about the performance and direction of the organisation. This helped to highlight what was important to these stakeholders and to articulate a process for shaping the direction of the report.”

How is your organisation benefiting now or expecting to benefit in future as a result of developing an Integrated Reporting process and report?

Better cooperation between different teams



Sharing best practice processes across the whole business



Conclusion

Companies are at different stages in terms of connecting departments, with those who have achieved senior management buy-in furthest along. While overcoming different attitudes can be one of the most challenging parts of the Integrated Reporting journey, the benefits of joining up teams are significant and broad, demonstrating the value of perseverance. The development and deepening of cross-departmental working has not only developed working practices but has no doubt deepened the understanding of ESG issues and the value that it adds to the business.

TOP TIPS:

- Make the business case first and tailor it for different internal stakeholders
- For organisations where ESG issues feel less relevant to the business model, consider the broader role of the organisation in terms of its public interest remit and the sustainability of the business
- Ensure that representatives from all the key teams are involved in the development of the Integrated Report to bring them all along the journey together
- Focus on collaboration between finance and sustainability teams; both need to be involved from the start – work towards common indicators
- Encourage innovative thinking – use a training programme to develop internal understanding, getting different teams involved in thought leadership
- Education and engagement need to be ongoing to achieve internal support
- Don't worry about getting all colleagues to understand the intricacies and standards; focus instead on developing integrated thinking and how people can create shared value more broadly
- Use every opportunity to engage people directly, even in small issues – soft aspects really help drive the more strategic conversations
- Education is a slow process – aim to reach a point of mutual understanding with other teams by being willing to learn as much as to share and taking steps only as quickly as the business can handle



IMPROVED INTERNAL PROCESSES

LEADING TO A BETTER UNDERSTANDING
OF THE BUSINESS

“Current reporting needs to change and the new reporting framework is more sensible and presents a more holistic and relevant view of the business...”

(Listed and public sector company)

A majority of those involved in the IIRC's Pilot Programme are using the Integrated Reporting process to develop more robust systems for data collection and performance management. This is supporting the development of strategies with a greater focus on value creation in its broadest sense, rather than just revenue generation. A 2011 Deloitte report⁶ identified the rigorous preparation of metrics and the insights these bring as being among the main value drivers for companies of Integrated Reporting. Furthermore, "a properly designed set of performance measures reported on as part of regular financial management gives the incentive and ability to improve performance"⁷.

For many reporters, improvements to systems can feel like the most tangible outcome of the journey towards Integrated Reporting. Indeed, it is essential but it is not the ultimate goal. It would be highly counterproductive to reduce the whole corporate reporting system to data processes. Any organisation which does this is unlikely to focus on what is most material to the business. Data and the processes which surround it need to be considered in relation to the short- and long-term business strategy.

As Integrated Reporting develops and stakeholders increasingly start to depend on non-financial information for their investment decisions, it is likely that assurance will also become an increasingly important part of data collection processes – one possible antidote to 'greenwashing'. However, there are still significant uncertainties about how best this should work and a need for assurance and audit providers to improve their own understanding of their role in Integrated Reporting.

Our research found that the business case for Integrated Reporting, in terms of improving internal processes, can be divided up as follows:

- Use non-financial data to gain a clearer picture of the business internally
- Develop more robust systems for performance management
- Reduce the amount that is published and make the story more accessible to stakeholders
- Streamline performance reporting and find efficiencies within the business so that data sets can be used in a range of different ways
- Reduce duplication of information and ensure consistency of messaging

Overall, 48% of respondents are moving towards Integrated Reporting in order to improve their internal processes, while 33% hope it will help to develop an understanding of ESG issues internally.

Changes already underway:

1. GREATER UNDERSTANDING OF THE ORGANISATION'S MATERIAL ISSUES

Organisations are already seeing the effects through the increase in efficiencies in their internal processes. For example, one company said that the journey to Integrated Reporting is leading to a greater focus on what is material to the business, providing better structure on what is relevant and, importantly, what is not. This has meant that less time is wasted on non-material issues and provides an opportunity to move away from a compliance-driven reporting process.

Improvements to internal processes are providing greater visibility of organisations' activities and impacts. For example, one respondent said that it has helped to collect negative information about their ESG performance because it has meant that they are better able to track the wider impact of their activities. This same organisation recommended the use of a third party to assist in this and to provide objectivity. Another company said that there was now increased awareness of the broader impacts of its operations on society.

Case study

VANCITY

"We decided to start with the sustainability report and add financial information to that, rather than the other way around. To do this, we looked at the strategy, targets and commitments. What came out of that led to tangible financial numbers. By approaching the integrated report in this way, we believe it will be more accessible to lay readers who do not have detailed technical or financial knowledge. The focus of the report has been instead on how money is made and value created."



⁶ Deloitte (2011). "Integrated Reporting: A better view?"

⁷ Ibid. p.4

2. BETTER QUALITY DATA COLLECTION

Overall, 93% of respondents agreed that moving to an Integrated Reporting framework leads to better quality data collection. In particular, non-financial information is becoming more rigorous, comparable and robust, especially as more finance teams become involved in its collection. This is improving coordination between departments and speeding up the process of gathering and verifying non-financial information to financial reporting timelines. Putting these processes in place requires upfront resource and effort, together with a holistic view to decide which data is most appropriate and what it is possible to collect. One company is achieving this by making reporting part of a regular routine so that the review of processes and data capturing is ongoing.

How companies go about integrating financial and non-financial information will vary between organisations. In general, our research found that those who started by embedding non-financial issues into existing financial systems benefited from the rigour of these processes. However, other organisations are finding it easier to add financial numbers to their ESG reporting. Combining the different types of information is a first step on the journey towards integration.

3. BETTER INTERNAL UNDERSTANDING OF HOW THE ORGANISATION CREATES VALUE

Better data is leading to greater internal awareness of the bigger picture in terms of what an organisation does, how it earns money and how it is positioning itself in the market. Overall, 72% of respondents agreed or significantly agreed that developing an Integrated Reporting process is leading or will lead in future to a better internal understanding of the whole business. Linked to this, 64% of respondents agreed that it would also lead to an increased awareness across the business of non-financial reporting value drivers.



Case study

CLP HOLDINGS

“In the past, we focused on economic factors for the Annual Report. Since deciding to do Integrated Reporting, we have started to collect more information and to change the way we collect it, particularly how the sustainability reporting process can be more ‘integrated’ with that of the annual reporting process. The assurance process has helped to increase awareness of how we need to continue to manage our non-financial data well into the future and how it may evolve over time. Integrated Reporting has also spurred us to think more about how to communicate the connections between our business strategy, processes and performance, as well as how to reflect our overall strategic objectives in a more holistic fashion.”

Although there are challenges in prioritising KPIs and managing the intangibility of some non-financial information, organisations that are addressing these are seeing the benefits in terms of being better able to manage their risks and to spot business opportunities. For example, one organisation has found that their sustainability efforts are driving innovation within the business operations.

The availability of information has for some companies developed a broader understanding of ESG issues and provided a more holistic idea of value creation.

For sustainability teams, this has generated more interest in non-financial activity and an understanding of value creation beyond the financials. A significant development identified by interviewees was the shift in language being adopted by sustainability professionals. The deepening of the alignment to the mainstream business has meant a shift to what may be considered to be traditional business terminology through an articulation of business and commercial benefits of their activities.

4. ASSURANCE AS AN OPPORTUNITY

Our research found that 83% of respondents see assurance as providing an opportunity to their organisation. In addition, 79% of respondents planned to assure their integrated reports in full in future. Participants considered that the credibility that the assurance process provides demonstrates a robustness and rigour in the management of non-financial activity and helps to drive further internal change. It also adds value in demonstrating transparency. For several interviewees, the Board is taking the lead in championing the significance of the non-financial assurance process. This is helping to ensure that stakeholders, including shareholders, have confidence in the progress and performance of the business.

However, questions remain as to what is appropriate and what assurance should cover, with many respondents saying they were ‘undecided’. Some identified difficulties in aligning annual report auditing and the assurance of environmental, social and governance information. This is an area that respondents felt the wider assurance and audit providers need to help address.

How is your organisation benefiting now or expecting to benefit in future as a result of developing an Integrated Reporting process and report?

Better internal understanding of the whole business

Increased awareness across the business of non-financial reporting value drivers



Conclusion

Integrated Reporting is providing a driver for prioritising improvements to internal processes. Identifying relevant material issues and KPIs has been the first priority, followed by collecting the data itself and improving the systems for doing so. Those organisations further along the Integrated Reporting journey are embedding the information they collect into management systems and exploring the best ways of achieving rigour in the data through assurance and audit processes.

“There is behaviour change across the business and it is motivating colleagues to think in a more integrated way”

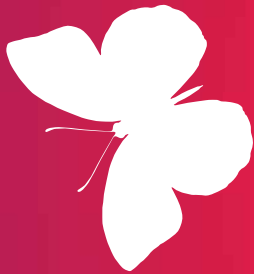
(Public sector organisation)

TOP TIPS:

- Make sure you have a clear sense of the journey for your organisation; know where you are going and what you want to achieve
- Understand what change you want reporting to make for the organisation
- Develop a roadmap, step by step – set milestones towards your goals
- Use gaps in information to identify areas for improvement
- Give yourself time to deliver the report; it won't happen overnight

INCREASED FOCUS

OF THE BOARD AND SENIOR
MANAGEMENT



“The CEO is personally committed to sustainable development and has been involved in various sustainability issues around the world, with both operator and Board level knowledge; as a result, he is driving the development of the business at a strategic level...”

(Private company)

Our research is not the first research to find that senior management engagement is crucial to the success of an Integrated Report. A 2011 report declared that “the success of any Integrated Reporting initiative is predicated on support at the executive and board level”⁸. In part this is because if the Integrated Report is to reflect information that is material to the business, then this must align with the way issues are prioritised and discussed by the Board and directors. This is a reminder that the report is not a standalone exercise but that the process behind it needs to be central to performance management and strategic decision-making. It should represent a shift from measurement and disclosure to management and action. In other words, if organisations are reporting that sustainability information is important to their success, they need to ensure that the Board is discussing it.

However, as well as being integral to its success, the journey towards Integrated Reporting also provides opportunities for the Board and senior management to gain a more holistic understanding of their organisations. KPMG’s May 2012 report⁹ found positive feedback from management teams adopting Integrated Reporting in terms of improving the focus on material issues, a wider understanding of risks and opportunities and an ability to communicate the strategy more effectively. This echoes findings that as Board-level committees become more engaged with sustainability issues through the Integrated Reporting process, they become more knowledgeable about them. Knowledge is an important step towards better management of the business.

Our research found that 31% of respondents strongly agreed that Integrated Reporting led to a stronger Board focus on critical business issues, whilst 36% felt that it led to

“We have the luxury of having a Board that really wants to drive thinking and development”

(Member-owned credit union)

a greater Board focus on KPIs. There seems to be clear evidence of such changes already underway among organisations adopting Integrated Reporting.

1. GREATER FOCUS ON SUSTAINABILITY ISSUES

Our research found that 93% of respondents agree or strongly agree that moving towards an Integrated Reporting framework leads to a greater focus by management on sustainability issues. Linked to this, 95% agreed that the attention on reporting a greater range of KPIs in the Integrated Report is leading to an increased focus among the Board on exactly what the KPIs should be for the business. This is mainly because the additional KPIs help to highlight areas of poor performance that financial metrics alone might not reveal and identify where there is scope to make a difference.

These results were reflected among interviewees who are finding that Board members are increasingly engaged in non-financial issues and are helping to drive a more integrated strategy. The changes are occurring despite a lower number of respondents (55%) saying that the reporting of KPIs is influencing the remuneration policies of directors. The key is to identify true believers who can influence other senior managers across the business. One respondent highlighted the fact that the Board does not meet that often so it is vital to get sustainability issues on their agenda in order to get their attention. Similarly for the Audit Committee, the more they see, the more buy-in there is and the greater their

understanding of non-financial issues. As a result, they are promoting integrated thinking and actively strengthening the connections across teams.

2. MORE INFORMED DECISION MAKING

Overall, 88% of organisations surveyed agreed that Integrated Reporting leads to improvements in business decision making. Some organisations are developing their own mechanisms to drive this change. For example, one has developed a non-financial dashboard for its Executive Committee, with some of the KPIs linked directly to remuneration packages. This is helping to develop more integrated thinking among senior management. In another case, Integrated Reporting is driving the inclusion of more sustainability issues on their meeting agendas. In this way, the requirement to disclose better ESG information is raising the Board’s awareness of what the business is doing. For organisations where senior-level engagement is proving more challenging, visibility of what other organisations are doing is proving useful in changing attitudes internally.

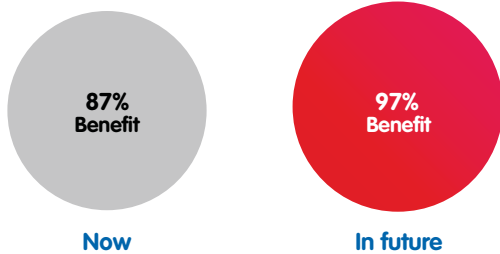
There is also a clear positive correlation between those organisations who have adopted workshops as a training tool and the level of understanding among Board and senior management. Given the complexity of the subject involved, the two-way engagement provided by a workshop seems to be the most effective way to involve senior management.

⁸ Deloitte (2011). “Integrated Reporting: A better view?” p.9

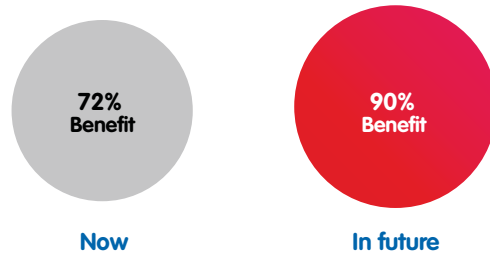
⁹ KPMG (May 2012), “Integrated Reporting: Performance insight through Better Business Reporting”, Issue 2

How is your organisation benefiting now or expecting to benefit in future as a result of developing an Integrated Reporting process and report?

Overall benefit to the Board



Collaborative thinking about goals and targets by the Board, executives and strategy departments



Conclusion

Senior level buy-in is essential in order to make progress. Those companies leading the way to Integrated Reporting have the support of the Board and have worked to ensure that senior management understand the value of a new integrated approach. This therefore needs to be a priority for those beginning the Integrated Reporting journey. The value of improving understanding of ESG issues can ultimately ensure that better, more effective long-term decisions can be made.

TOP TIPS:

- Identify a senior champion who can drive integration and does not view it just as an additional cost but as a way of building value for the company
- Use workshops to engage Board members and senior management
- Reinforce cases where integrated thinking and Integrated Reporting have had positive results in order to build the internal business case



Case study

MUNICH AIRPORT

“Our Sustainability Board was a vital mechanism for Integrated Reporting. Previously it had been the Steering Committee for Sustainability so people knew each other and had an understanding of the issues. We are working with the Sustainability Board to build a picture of the business by linking sustainability issues more closely to financial measurements in terms of cost reductions, risk and profitability. This picture will also enable us to carry out a programme of internal education on the material importance of sustainable development activities to the core licence to operate and the economic growth of the business.”

BETTER ARTICULATION

OF THE STRATEGY AND
BUSINESS MODEL



“Integrated Reporting is a natural flow from having your business integrated...”

(Private company)

As understanding of the way the business creates value improves internally, organisations are better able to articulate the strategy and business model holistically. The IIRC's 2012 Yearbook found that "there is growing recognition that a wide range of factors create value in the short, medium and long term"¹⁰. Marshalling these factors into a coherent picture is a key challenge for integrated reporters and relies on a clear understanding of material issues. Too many reports sacrifice quality for quantity, disclosing on the basis of compliance rather than materiality, an issue that Integrated Reporting aims to overcome. Deloitte's 2012 advice was to be "ruthless in excluding that which does not clearly aid understanding the fundamentals of the company, what it is trying to achieve and what its prospects are"¹¹.

Articulating the strategy is an important step in enabling organisations to communicate effectively and consistently with both internal and external stakeholders. There is a wide consensus that the content of the report should flow from the business model, strategy and operating context and not provide a separate account of sustainability activities as if they are disconnected from operations. Although it is not always clear how best to achieve this, the direction of travel appears to be positive, with an increasing number of organisations integrating ESG issues into strategy¹².

Not only does a clearly articulated strategy and business model help organisations to communicate, but there is also evidence that links corporate transparency to lower risk¹³. In addition, our research identified the following components of a business case for this aspect of Integrated Reporting:

- Develop a clearer picture of the business model, aligning ESG issues with group strategy
 - Reflect integrated thinking, using both financial and non-financial information to tell the business story
 - Use the business model and integrated strategy to communicate more clearly, demonstrating how the organisation creates value
 - Respond to demands for transparency
- Our research found that 95% of respondents agreed that moving towards an Integrated Reporting framework leads to a clearer view of the business model, while 98% agreed that it would lead to a better understanding of how the organisation will create and develop value over time. These developments in turn are improving the wider articulation of corporate strategy. Overall, 62% of respondents see Integrated Reporting as a mechanism for aligning ESG issues with the group strategy.

1. IMPROVED COMMUNICATIONS

Organisations are using the integrated report as a central articulation of the strategy for use both internally and externally. Overall, 74% agreed that it will lead to more consistency in external communications across the business. One organisation specifically mentioned that Integrated Reporting is helping them to identify the key issues that they want to define for communication purposes. Another said that it is enabling them to work towards a 'single source of truth' for employees so that they can understand the business and proactively promote it.

2. LINKING NON-FINANCIAL AND FINANCIAL KPIs

Participants in our research are demonstrating integrated thinking through their reports by linking non-financial and financial KPIs to demonstrate a holistic strategy. However, this is also one area highlighted as challenging by our respondents because there is no agreed model on how best to achieve this. Each organisation must choose how much of which information to use, where to put it and how to link it to existing published information. As more organisations spend time trying to achieve linkages and deepen the connection between financial and non-financial KPIs, we are confident that best practice approaches will start to emerge. Progress here is one of the key aims of the Pilot Programme.

A general move towards Integrated Reporting is also enabling organisations to discuss forward-looking information with more confidence. For example, one organisation is adopting Integrated Reporting to help them leverage information for long-term investors.

3. GREATER TRANSPARENCY

Our research found that organisations are becoming more confident in disclosing relevant information. For some, a commitment to transparency represents a new approach that requires changes in internal thinking. However, as a broad framework is developed, this is expected to support greater transparency and help to answer queries and questions within the business about what it is appropriate to disclose. Related to this, we expect those on the Integrated Reporting journey to move away from boilerplate information driven by compliance to more meaningful disclosures that give stakeholders a clearer picture of the business. Some have already taken significant steps in their commitment to transparency.

¹⁰ IIRC (2012). "Integrated Reporting – The Pilot Programme 2012 Yearbook: Capturing the experiences of global businesses and investors" p.4

¹¹ Deloitte (February 2012). "Integrated Reporting: Navigating your way to a truly Integrated Report" p.63

¹² Ibid

¹³ Ligteringen, Ernst (2012). "Sustainability reporting for 'the future we want'" in Making investment grade: the future of corporate reporting ed Cornis van der Lugt and Daniel Malan p.21

How is your organisation benefiting now or expecting to benefit in future as a result of developing an Integrated Reporting process and report?

Improved organisational clarity that comes from articulating a holistic view of the business and strategy



Consistency in communications about the business



Conclusion

A clearer articulation of an organisation’s business model and strategy is an iterative process. The process of clarifying the story reflects and reinforces any existing integrated thinking, which then helps to drive integration further. More advanced reporters are successfully blending financial and non-financial information into a coherent picture of operations to demonstrate how the organisation creates value. This is providing the basis for consistent transparent corporate communications.

“The integrated report is a tool to communicate more efficiently, providing a coherent story and better external articulation”

(Public sector organisation)

TOP TIPS:

- Use the report as a tool to advance discussions on strategy and the business model internally
- Focus on how to create value – this helps to shape thinking internally
- Think about what sustainability really means for the business
- Don’t ignore the governance of the business as this is really important for driving activity internally as it enables everything to be more strategic
- Use the language of business; talk in terms of economic benefits
- Use both a financial and non-financial risk system and aim to get as much certainty as possible on understanding non-financial risk



CREATING VALUE FOR STAKEHOLDERS

“More and more stakeholders in the
business are interested...”

(Listed company)

For many companies, the needs of external stakeholders are another driver in the shift to a reporting process that is more integrated. Such stakeholders include customers, investors, employees, regulators, governments and local communities. UBS's June 2012 research found that good quality reports are ones that "make it easy for the user to make insightful connections between key pieces of information in the context of the investment decision-making process"¹⁴. UBS also found greater interest from investors in mid- and long-term issues although there is still not as much pressure from these stakeholders as might perhaps be expected. This is despite findings that "there is a gap between the information currently being reported by companies and the information investors need to assess business prospects and value"¹⁵.

The importance of providing stakeholders with adequate information is a fundamental one. There is still some way to go though, with many of those yet to embrace Integrated Reporting continuing to take an unstructured approach to stakeholder engagement. Participants in our research hold a strong commitment to stakeholder engagement. This has helped to build the following business case for Integrated Reporting which enables organisations to:

- Meet demands for ESG information from stakeholders
- Understand better what stakeholders want from company reporting
- Differentiate the organisation from competitors
- Demonstrate stewardship and thought leadership

Evidence of changes underway:

1. PROVIDING BETTER ESG INFORMATION FOR STAKEHOLDERS

Organisations said that the shift to Integrated Reporting is enabling them to provide better quality and more relevant ESG information to stakeholders requesting it. Of the research participants, 61% said that analysts were asking ESG questions, with some additionally highlighting increased questioning from investors on corporate governance as a driver behind their reporting journey. For example, one organisation is finding that stakeholders want to know more about the future profile of the business and so it has become proactive in discussing this.

The adoption of Integrated Reporting is enabling organisations to react better to these requests for information. Changes to internal processes are helping companies to answer questions posed by stakeholders with greater confidence in the information and with a better balance between quality and quantity. However, some respondents said that their stakeholders are not yet using the opportunities provided by a more integrated structure, with some types of investors not asking about ESG information yet. In such instances, Integrated Reporting enables companies to be more proactive, rather than simply responding to audience demands. This is an opportunity for organisations to take on a more educational role about their place in broader society.

2. CREATING VALUE THROUGH A FOCUS ON ESG ISSUES

Our research found evidence that integrating ESG issues better can create significant value for organisations. Such benefits may be reputational, enabling companies to distinguish themselves in the marketplace

through transparency. A third of respondents to our survey saw Integrated Reporting and related integrated strategies as a means of differentiating their organisations from competitors. Benefits may also be more tangible. For example, one organisation identified an increase in ESG investors from 4.5% to 20%, demonstrating significant value creation in addressing ESG issues. The subsequent need for a model to measure the change created is driving the requirement for Integrated Reporting.

3. CLEARER UNDERSTANDING OF STAKEHOLDER REQUIREMENTS

A majority believed that they had a comprehensive understanding and extensive engagement programmes with employees (71%), regulators (66%), institutional investors (68%) and other internal stakeholders such as the Board (60%). Some gaps remain for other types of stakeholder. By mapping stakeholders more effectively, organisations on the Integrated Reporting journey are better able to meet their requirements in terms of the content and delivery of information. For example, one respondent said that the organisation now had a greater ability to streamline information for analysts. Another found that embedding better engagement with external stakeholders into reporting processes helped to identify issues that had not come up before. This then led to a rethinking of performance and contributed to developing the strategy.

The mechanisms under development as part of Integrated Reporting should enable key stakeholders to feed back into organisations, providing opportunities for them to influence change. This is an important benefit of Integrated Reporting to external stakeholders and the more they recognise this, the greater the momentum towards better reporting will become. Overall, 81% of our research respondents claimed that stakeholders have shaped the nature of the organisation's reporting so far.

¹⁴ UBS (20 June 2012). "UBS Investment Research Q-Series: What is 'Integrated Reporting'?", p.3

¹⁵ KPMG (May 2012). "Integrated Reporting: Performance insight through Better Business Reporting", Issue 2, p.4

Leading organisations are already using stakeholders effectively to guide questions of materiality in the integrated report. This is helping them to overcome the challenge of targeting their report at a range of stakeholders. One company is focusing on addressing the balance between print and online versions of the report in a way that meets the needs of a wider audience.

4. SHAPING THE AGENDA

Organisations on the Integrated Reporting journey are contributing to setting the standards for best practice. This is giving them a headstart in understanding the most effective way to develop an integrated report. It is also enabling participating organisations to demonstrate thought

leadership, which was the most popular motivation for adopting Integrated Reporting according to our survey. For example, one aspired to be a state-owned company leader in Integrated Reporting best practice, while another wanted to sponsor its adoption in their home market.

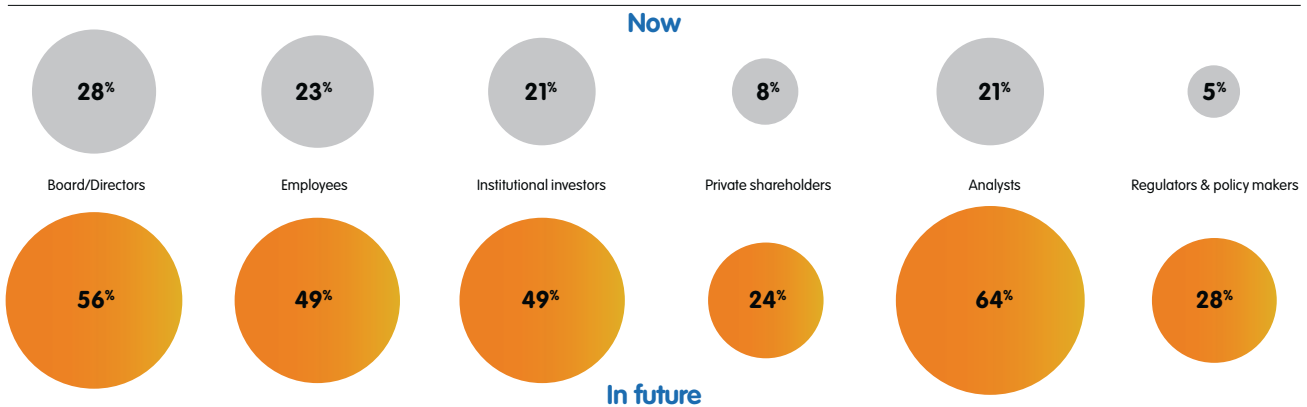
Future outlook

Our research found that many organisations believe that the Integrated Reporting journey is providing significant benefit already to a range of stakeholders including analysts (21%), institutional investors (21%), private shareholders (8%) and employees (23%). Almost all stakeholders are expected to

benefit from better integration in future, with many anticipating that these benefits will be significant. In particular, 64% of respondents believe analysts will benefit significantly as Integrated Reporting develops and 49% that institutional investors will do so. For many organisations adopting this approach,

investors are the main audience of their integrated report so these responses show optimism that efforts now will reap important rewards in the years to come. Also expected to gain in future are employees. Overall, 95% of respondents expect employees to benefit to some extent.

Significant benefit to each audience from presenting the organisation in an integrated way through integrated reporting



Conclusion

The views of stakeholders can help organisations build the business case for Integrated Reporting, particularly where there are opportunities to differentiate a company from its competitors. Those reporters furthest along the Integrated Reporting journey are effectively integrating stakeholder engagement into the reporting process. As stakeholders start to see the benefits of their involvement in reporting, we expect to see increasing pressure on organisations to adopt a more integrated approach.

TOP TIPS:

- Find out what others are doing and the lessons they are learning
- Look at the content of the report from the perspective of audience needs and interests
- View the report as an evolution in response to stakeholders – ensure it is not just what you want to say but respond to what they want to know
- Aim to meet the top-level needs of as many stakeholders as possible but use alternative means to communicate the details, such as digital technology
- Differentiate stakeholders and enable them to access different information in ways that suit them – this will help them understand the business better



SUMMARY OF CONCLUSIONS



The respondents to our research were generally extremely positive about the impact that their journey towards Integrated Reporting is having on their organisations. As expected, companies are facing challenges but these are being overcome and are expected to decrease as reporting develops.

There is a broad recognition that achieving full integration will take time but business network participants in the Pilot Programme are already seeing important benefits from their involvement.

For each of the areas outlined above, we have identified some of the steps in the Integrated Reporting journey, together with a suggested set of tactics. These may not be relevant for all organisations and we will explore their usefulness further during the next phases of our research.



What the journey can look like

1 CONNECTING DEPARTMENTS

Companies are at different stages in terms of connecting departments, with those who have achieved senior management buy-in furthest along. While overcoming different attitudes can be one of the most challenging parts of the Integrated Reporting journey, the benefits of joining up teams are significant and broad, demonstrating the value of perseverance.

Representatives from key teams across the business identified and involved in Integrated Reporting process



2 IMPROVED INTERNAL PROCESSES

Integrated Reporting is providing a driver for prioritising improvements to internal processes. Identifying relevant KPIs has been the first priority, followed by collecting the data itself and improving the systems for doing so. Those organisations further down the Integrated Reporting journey are embedding the information they collect into management systems and exploring the best ways of achieving rigour in the data through assurance and audit processes.

Relevant and material KPIs identified for the business, including non-financial information



3 FOCUS OF THE BOARD AND SENIOR MANAGEMENT

Senior level buy-in is essential in order to make progress. Those companies leading the way to Integrated Reporting have the support of the Board and have worked to ensure that senior management understand the value of a new integrated approach. This therefore needs to be a priority for those beginning the Integrated Reporting journey.

True believers identified at senior level and acting as champion of integrated approach



4 ARTICULATION OF THE STRATEGY AND BUSINESS MODEL

A clearer articulation of an organisation's business model and strategy is an iterative process. The process of clarifying the story reflects and reinforces any existing integrated thinking, which then helps to drive integration further. More advanced reporters are successfully blending financial and non-financial information into a coherent picture of operations to demonstrate how the organisation creates value. This is providing the basis for consistent corporate communications.

Material issues identified and agreed for the business



5 CREATING VALUE FOR STAKEHOLDERS

The views of stakeholders can help organisations build the business case for Integrated Reporting, particularly where there are opportunities to differentiate a company from its competitors. Those reporters furthest along the Integrated Reporting journey are effectively integrating stakeholder engagement into the reporting process. As stakeholders start to see the benefits of their involvement in reporting, we expect to see increasing pressure on organisations to adopt a more integrated approach.

Stakeholders identified, mapped and prioritised



Senior management buy-in and support achieved



Process established for ongoing education and engagement of key teams, helping to drive innovation



Integrated thinking demonstrated across teams, together with an agreed approach to performance management



Systems in place for regularly collecting non-financial information



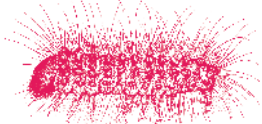
Non-financial information embedded into performance management systems



All KPI information subject to rigorous verification



Board and senior management engaged in sustainability issues



Value of integration accepted and fully understood by senior management



Sustainability information fully integrated into Board decision-making process



Financial and non-financial information successfully blended into a clear articulation of strategy and the business model



Clear corporate communications with agreed and consistent messaging



Employees across the business able to tell a coherent business story



Process and guidelines in place for engaging stakeholders



Stakeholders engaged to provide a clear picture of their requirements and to understand them better



Stakeholder views effectively integrated into the reporting process





ACHIEVING CHANGE

Much of the change to achieve Integrated Reporting needs to be driven by companies themselves and the development of the IIRC framework is enabling companies to shape the process based on their own experiences. However, there are important roles for others as well. In particular:

- More external pressure would be welcomed by those pushing this agenda within companies, particularly from investors
- Benchmarks and other references would help those without senior-level engagement to build the case for Integrated Reporting
- There is a demand for providers of assurance and auditing to offer a more integrated service to companies. We identified assurance as an area where there is generally a lack of clarity on the scope and role of assurance, together with how it should fit with financial auditing



About this report

This report 'Understanding transformation: Building the business case for Integrated Reporting' is the first of two that aim to understand the processes that companies go through as they move towards Integrated Reporting. The organisations participating in the research are at different stages but all are involved in the IIRC's Pilot Programme, which aims to help develop an International Integrated Reporting Framework. At Black Sun, we are working closely with the IIRC to support their development of this framework.

The Pilot Programme involves more than 75 private and public organisations and 25 institutional investors. Drawn from all over the world, participants are trialling the principles, content and practicalities of the Framework for two years to provide feedback and build business momentum towards its implementation. By tracking their experiences over the two year duration of the pilot, we aim to capture the changes and benefits of adopting Integrated Reporting. This will help to build the business case for a wider shift towards Integrated Reporting and help to generate support among key stakeholders, including internal audiences, boards, investors and regulators.

This report has been produced for organisations currently adopting or considering adopting an Integrated Reporting approach. It aims to provide evidence of the business case for those looking to achieve cultural change within their organisations. We expect to demonstrate that the changes to company behaviour will be of significant benefit, to an extent not anticipated when the shift towards Integrated Reporting began. In turn, the experience of organisations in transition will feed into the IIRC's draft framework and help to inform its development.

Methodology

Black Sun conducted the research in association with the IIRC. We emailed all Pilot Programme business network participants with a detailed baseline survey which we administered online. In total, 44 individuals from 43 companies completed the questionnaire, which comprised 44 questions. The research took place between June and August 2012.

Black Sun interviewed 19 of these organisations by telephone to provide greater understanding of their responses and to explore the changes and benefits further. These 19 volunteered further participation and provided an opportunity to collect detailed examples of what organisations are doing. The information from these interviews provides the bulk of material for this report.

The participants in the research included:

- 21 listed companies
- 11 private companies
- 6 public sector organisations
- 7 other organisations, including a development bank and a member-owned credit union

The research is based on the opinions of those that are managing and delivering Integrated Reporting programmes for their organisations. Of these, 48% were report owners, 25% contributors, 7% editors and the remaining respondents were involved in the report production in other ways. As all the participants are already working towards Integrated Reporting, their responses are likely to be more positive about it as an approach than those of a random selection of organisations would be. However, the purpose of the Pilot Programme is to share experiences and so the respondents have shared their challenges, as well as the benefits they are experiencing.

One of the purposes of integrated reporting is to respond better to the needs of key stakeholders, including the main target audience: investors. Over the course of this study, we will be investigating whether investor relations teams become more involved in the preparation of the report, as our research indicated that their level of involvement was relatively low among the majority of respondents. As Integrated Reporting becomes more mainstream, we aim to determine whether investor relations teams take on a greater role in developing and driving the document.

This report provides a baseline for follow-up research that will track the progress these organisations are making. We will conduct interim research in Spring 2013 which will primarily engage those that participated in the first survey and interviews. It will also engage with new members of the IIRC's Pilot Programme to maintain an awareness of general trends. A second report will be based on research undertaken in Autumn 2013 with all business network participants on the Pilot Programme. This will seek further evidence of trends in corporate behaviour, business benefits and integrated thinking as a result of adopting Integrated Reporting processes. The final publication aims to provide clear evidence of the business benefit for those embarking on the Integrated Reporting journey.

Respondents came from the following departments or teams



● Sustainability/CR	48%
● Finance	18%
● Board/Directors	5%
● Legal/Company secretariat	2%
● Corporate Communications	9%
● Other, such as strategy, advisory role or part of the wider report project team	18%

Participating companies

We would like to thank all those organisations who participated in this study:

AEGON NV	Gold Fields
Assicurazioni Generali SpA	Grant Thornton UK LLP
Association of Chartered Certified Accountants	HSBC Holdings plc
Bankmecu	Indra
BBVA Group	Industria de Diseño Textil
BNDES	KPMG International
Chartered Institute of Building	Marks and Spencer Group plc
Chartered Institute of Management Accountants	National Australia Bank Limited
Cliffs Natural Resources	Natura Cosméticos
CLP Holdings Ltd	NHS London
Deloitte Accountants BV	PricewaterhouseCoopers NV
Diesel and Motor Engineering PLC	Rabobank Group
Edelman	State Atomic Energy Corporation ROSATOM
ENAGAS S.A.	SAP
EnBW AG	Sainsbury's
Enel SpA	Solvay
Eni SpA	Stockland
Ernst & Young Nederland LLP	Takeda Pharmaceutical Company Ltd
Ernst & Young ShinNihon LLC	Telefónica S.A.
Eskom Holdings SOC Limited	Transnet Soc Ltd
Flughafen München GmbH	Vancity

Geographical spread



Africa	7.0%
Asia	9.3%
Australasia	7.0%
Europe	65.0%
North America	7.0%
South America	4.7%

Companies by sector grouping



Accounting	14.0%
Chemical and pharmaceutical	4.7%
Consumer goods and retail	11.6%
Energy and utilities	16.2%
Financial services	18.5%
IT - hardware and software	4.7%
Member body, networks and public sector	11.6%
Transportation	4.7%
Professional services	4.7%
Mining and engineering	7.0%
Telecommunications	2.3%

About Black Sun

Black Sun is one of Europe's leading strategic corporate communications consultancies. Founded in 1991, it brings together corporate reporting, sustainability and digital communications to create powerful integrated solutions for clients.

Black Sun works with companies – from small businesses to large global organisations – to produce effective communications that build greater trust and confidence with stakeholders. Its dedicated strategic research team identifies trends and best practice to provide clients with up-to-date analysis, advice and guidance.

If you would like to understand more about the work of Black Sun Plc or this research, please contact:

Laura MacSweeney at
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www.blacksunplc.com

About the International Integrated Reporting Council (IIRC)

The International Integrated Reporting Council (IIRC) is an international cross-section of leaders from the corporate, investment, accounting, securities, regulatory, academic, civil society and standard-setting sectors.

The IIRC's mission is to create the globally accepted Integrated Reporting ("<IR>") Framework that elicits from organizations material information about their strategy, governance, performance and prospects in a clear, concise and comparable format. The Framework will underpin and accelerate the evolution of corporate reporting, reflecting developments in financial, governance, management commentary and sustainability reporting. The IIRC will seek to secure the adoption of <IR> by report preparers and gain the recognition of standard setters and investors.

If you would like to understand more about the IIRC Pilot Programme, please contact:

Kate Jefferies at
kate.jefferies@theiirc.org

www.theiirc.org

Visit our new database of emerging Integrated Reporting

Black Sun has recently launched a new online database of emerging examples of Integrated Reporting in conjunction with the IIRC. The database currently houses over 100 extracts from over 35 companies across six regions globally and demonstrates how companies are embracing the concept and principles of Integrated Reporting.

To find out more visit <http://examples.theiirc.org>





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INTEGRATED REPORTING <IR>

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