# Beyond the Balance Sheet

## IFC Toolkit for Disclosure and Transparency

LE GOUVERNEMENT
DU GRAND-DUCHÉ DE LUXEMBOURG
Ministère des Finances

IFC International Finance Corporation
WORLD BANK GROUP
*Creating Markets, Creating Opportunities*

# Beyond the Balance Sheet

## IFC Toolkit for Disclosure and Transparency

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## Disclaimers

This Toolkit draws on international good practice, national regulations and codes, and the experience of various experts and practitioners on a deeply complex subject and is not intended to be comprehensive. Nor is it even a complete evaluation of the issues explored.

This publication reviews a large number of annual reports from companies in developed and emerging markets. IFC makes no comment on the performance of those companies. The excerpts from the annual reports are used solely to illustrate different parts of reports covered in this publication, and IFC in no way guarantees the accuracy of the information or the present or future performance of the companies.

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# Foreword

The UN Sustainable Development Goals have brought the global community together in a quest to end poverty, fight inequality, and tackle climate change by 2030. Reaching these goals across emerging markets requires a $4 trillion annual investment—a sum far beyond the means of governments and development partners. Capital markets in developing countries—many still in their infancy—hold great potential to channel private capital toward priority development needs.

Strong local capital markets are essential for a thriving private sector. They help people and businesses obtain long-term financing. They encourage the kind of entrepreneurial risk-taking that fosters innovation and accelerates job creation and economic growth. They can shield entire economies against potentially destabilizing fluctuations in international financial markets.

IFC plays a vital role in strengthening local capital markets, introducing innovative tools to unlock private sector funds for an array of important development goals and to set standards. We are often the first international nongovernment issuer of local-currency bonds in developing countries, helping establish the conditions that enable local markets to grow and thrive. We help developing countries draft policies and regulations that build stronger capital markets.

Equally important, well-functioning markets require trust. Investors need to know that markets are reliable and credible, and that the information disclosed—which they base their trading decisions on—is accurate, complete, and verified. Disclosure of accessible, reliable, timely, and useful information contributes to liquid and efficient markets by enabling investors to make decisions based on material information. Adhering to high standards of disclosure and transparency can mitigate some inherent risk of investing in emerging and frontier markets, including weaker public institutions and governance, heightened social and environmental risk, and smaller companies with controlling shareholders.

To promote high standards in disclosure and transparency across emerging capital markets, IFC developed this Disclosure and Transparency Toolkit. It is designed to guide companies in the preparation of comprehensive and best-in-class annual reports that are appropriate for their size and organizational complexity and adapted to the context of operation—to provide information that investors and other stakeholders can use to make informed decisions.

What is new and different about this Toolkit is that it reflects today's investors' views of what drives corporate value. These factors include the impact of environmental and social risks on a company's strategy, governance, and performance. They affect how key opportunities and risks are managed as part of the company's corporate governance.

The Toolkit is based on IFC's comprehensive new integrated approach to assessing environmental, social, and governance practices in the context of its own investments in emerging markets. In addition to applying this approach in evaluating its prospective investee companies, IFC incorporates it into its advisory work with regulators and stock exchanges for application to listings, reporting requirements, and disclosure obligations, among others.

We hope this Toolkit will help build momentum across capital markets—matching responsible companies in emerging markets with institutional investors. Stock exchanges, regulators, and development organizations are our key partners in advancing standards for increased disclosure and transparency to help build investor trust and confidence in emerging markets.

On behalf of IFC, I thank Luxembourg's Ministry of Finance for support that made this Toolkit possible.

*Ethiopis Tafara*
*IFC Vice President and General Counsel, Legal, Compliance Risk and Sustainability*

## Acknowledgments

In April 2016, the IFC Corporate Governance Group called together 50 representatives of international organizations and development finance institutions, reporting frameworks, investors, asset managers, institutes of directors and corporate governance associations, stock exchanges and regulators, subject-matter experts in the field, and members of the IFC Corporate Governance Private Sector Advisory Group.

These participants explored key changes in international corporate governance standards and codes of best practice in the wake of the recent global financial crisis and how these changes have helped draw corporate attention to sustainability issues and enhanced disclosure and transparency. This publication arises from the issues and information from these discussions and builds on previous work and research.

The project team would like to thank those who attended the April 2016 gathering. We are grateful to everyone who participated in the Practice Group meeting on Corporate Governance Codes, Standards, Disclosure, and Transparency and provided us with insights and information. All responses were instrumental in developing the rationale and key thinking points for this publication.

In January 2018, in a joint event with the UN Sustainable Stock Exchanges Initiative hosted by London Stock Exchange, the Toolkit was launched to representatives of 15 stock exchanges from around the world, investors, asset managers, and development partners, as a tool for filling in the environmental, social, and governance information gap.

This publication was developed by a team led by Ralitza Germanova, in cooperation with Charles Canfield, as part of the IFC Corporate Governance Group.

Project team: Ralitza Germanova, Jerome Lavigne-Delville, Charles Canfield, and Atiyah Curmally.

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# Executive Summary

IFC is releasing this Toolkit as part of a broader effort to enhance disclosure and transparency in countries and companies we work with, either as investors or advisers. Disclosure and transparency have become increasingly relevant for IFC as the field of corporate governance has expanded from purely board-related matters to include engagement with various external stakeholders.

The Toolkit and IFC's efforts to promote corporate disclosure and transparency more broadly are part of ***IFC 3.0***—a new strategy that focuses on creating markets and mobilizing private capital, especially in low-income countries and FCS (fragile and conflict situations).

The Toolkit builds on ***IFC's Access to Information Policy***, which seeks to provide accurate and timely information regarding IFC investment and advisory services activities to its clients, partners, and stakeholders.

### *Focus on Building Markets in Emerging Economies*

In developing countries, economic and social development is often limited by insufficient flow of private capital. In part, this is due to a heightened perception of risk in these countries, compounded by a lack of information or transparency or limited price discovery.

This Toolkit is designed to help companies in emerging economies access global capital markets, and to help global investors better price the risk of investing in these markets. It is also designed to help regulators and market authorities in developing countries improve the local market infrastructure.

### *A Comprehensive and Integrated Approach to Corporate Reporting*

The Toolkit's purpose is to guide companies in the preparation of integrated annual reports for investors. It provides guidance on the disclosure of material information—about a company's strategy, governance, and performance—that will be useful in making investment decisions.

The Toolkit often goes beyond legal requirements for disclosure and transparency, looking to the next frontier of reporting on environmental, social, and governance (ESG) issues and making sure it is integrated into the company's strategy, culture, and risk management, and that the information is subject to independent verification and assurance.

### *Incorporating International Best Practices*

The Toolkit incorporates international best practices and standards in corporate governance, environmental and social management systems, and disclosure and transparency, including the following:

- The IFC Corporate Governance Progression Matrix for Listed Companies[1] (Integrating Environmental, Social, and Corporate Governance Issues)—referred to herein as the IFC Corporate Governance Matrix, or the Matrix
- The IFC Performance Standards
- Global frameworks for sustainability management and disclosure

### *Flexible Framework*

The practice of disclosure and transparency is not a compliance exercise. Rather, it is a journey that takes into account a company's size and organizational complexity. The Toolkit's modular approach makes it applicable to a range of company sizes, organizational complexity, and operating contexts.

For example, smaller and family-owned businesses can initially focus on the following sections: Strategic Objectives, Risk Analysis and Response,

[1] Use of the Matrix is not limited to listed companies. Any organization—listed or not, and across sectors—can apply its concepts. For greater detail, see ***Appendix D*** of this Toolkit.

Structure and Functioning of the Board of Directors, and Financial Statements. Publicly listed and global companies should consider more comprehensive reports, with information covered in the sections on Sustainability Governance, Stakeholder Engagement, and Sustainability Statements.

### Toolkit Structure

At its core, the Toolkit provides a ***Disclosure Framework*** with detailed guidance, best practices, and examples in the three areas of an integrated annual report: Strategy, Corporate Governance, and Performance.

The Toolkit also provides general ***Reporting Guidance*** and considerations for preparing and presenting the information—including information quality, materiality, and specificity.

### Primary Users of the Toolkit

The Toolkit is designed to guide emerging-markets companies in the preparation of integrated annual reports that include strategic, governance, and performance information and that are commensurate with their size and organizational complexity and adapted to their context of operation. It can also be used by developed-markets companies looking to create sophisticated annual reports that integrate economic, social, and environmental factors.

### Abbreviations

| | |
|---|---|
| BBG | Broadcasting Board of Governors |
| CDP | Climate Disclosure Project |
| CDSB | Climate Disclosure Standards Board |
| CSO | civil society organization |
| DJSI | Dow Jones Sustainability Index |
| DVFA | German Association for Financial Analysis and Asset Management (Deutsche Vereinigung für Finanzanalyse und Anlagenberatung) |
| E&S | environmental and social |
| ECM | External Communications Mechanism |
| EFFAS | European Federation of Financial Analysts Societies |
| ESG | environmental, social, and governance |
| ESMS | Environmental and Social Management System |
| FASB | Financial Accounting Standards Board |
| FSB | Financial Stability Board |
| FRC | Financial Reporting Council |
| G20 | Group of 20 countries in an international forum for the governments and central bank governors |
| GAAP | Generally Accepted Accounting Principles |
| GHG | greenhouse gas |
| GRI | Global Reporting Initiative |
| IAS | International Accounting Standard, a standard under IFRS |
| IASB | International Accounting Standards Board |
| ICGN | International Corporate Governance Network |
| IFRS | International Financial Reporting Standards |
| IIRC | International Integrated Reporting Council |
| <IR> Framework | Integrated Reporting Framework of the IIRC |
| ISA | International Standards of Auditing |
| ISO | International Organization for Standardization |
| JSE | Johannesburg Stock Exchange |
| KPI | key performance indicator |
| NGO | nongovernmental organization |
| OECD | Organisation for Economic Co-operation and Development |
| PRI | Principles for Responsible Investment |
| RPT | related-party transaction |
| SASB | Sustainability Accounting Standards Board |
| SDGs | Sustainable Development Goals |
| SEC | Securities and Exchange Commission (United States) |
| TCFD | Task Force on Climate-related Financial Disclosures |

# 0. Introduction

The **business case for disclosure and transparency** is clear: Disclosure and transparency fill information gaps for customers, investors, and employees and, as a result, can have a positive effect on a company's revenues or its access to human capital or financial capital. Their use also promotes more efficient capital markets by ensuring "fair disclosure" to all investors and preventing asymmetric information. These benefits are amplified when companies take into account wider sustainability concerns, such as environmental, social, and governance issues, and disclose how they manage material environmental and social issues and stakeholder concerns.

## 0.1 Benefits of Disclosure and Transparency

A growing body of **academic research confirms the positive results of enhanced disclosure** by companies. Studies in developed markets—covering financial and nonfinancial disclosure (including corporate governance)—have found strong correlations between improved disclosure and 1) lower cost of capital, 2) better access to finance, and 3) increased company valuation.[2] Additional benefits include improved capital allocation, enhanced earnings and growth of earnings, and more liquidity in the market for the securities of the company. More recent research has found a similar correlation in emerging markets.[3]

Academic research often points to selection bias (or adverse selection) of any studies on the link between disclosure and performance, since companies that perform better tend to report more. The result is a notion that the practice of disclosure and transparency is a continuation of company performance and is the mechanism by which performance is reflected in a company's financial valuation.

Some studies have found proof of that relationship in individual companies, regardless of the level of disclosure and transparency in the rest of the market. However, there is an added benefit to individual companies when the level of transparency increases across the market. Indeed, information asymmetry can lead to adverse selection, where less informed investors either require additional return or exit the market, which results in higher cost of capital or lower levels of liquidity for individual companies. Academic research points to the positive effect of transparency on the liquidity of capital markets and the associated benefit that a firm in that market can receive in the form of cheaper cost of capital (Garay et al. 2013).

At the same time, academic research also suggests a positive, differentiating effect of disclosure and transparency in markets or for topics where the prevailing level of disclosure is low. For example, a recent study of firms in the five largest markets in Latin America shows a statistically significant and positive correlation between the level of disclosure on the one hand and Tobin's Q (ratio of book to market value) and return on capital on the other. This is especially true in areas of reporting—such as boards of directors, risk management, and responsibility to customers, suppliers, and shareholders—where disclosure is lacking in these markets (Davila and Vasquez 2015).

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[2] For studies on the United States and other developed economies, see Khurana, Pereira, and Martin (2006); Lang and Lundholm (1993); Leuz and Verrecchia (2000); and the papers summarized in Bushman and Smith (2003) and Leuz and Wysocki (2008).

[3] For studies that include emerging markets, see Durnev and Kim (2005); Klapper and Love (2004); Leuz, Lins, and Warnock (2009); Francis, Khurana, and Pereira (2005); and Aggarwal, Klapper, and Wysocki (2005).

### 0.1.1. Benefits of ESG Management and Disclosure

Academic studies also have found **a strong link between ESG reporting and financial performance:** Companies with effective management and disclosure of sustainability issues tend to have lower costs of capital, attain higher valuations, and deliver better returns to shareholders.[4] A recent Harvard Business School study differentiated between material and immaterial sustainability factors and found that firms with good performance on material sustainability issues—using the Sustainability Accounting Standards Board (SASB) framework—and low performance on immaterial issues generated an annualized alpha (performance above a market index or benchmark) of 6.01 percent (Kahn, Serafeim, and Yoon 2015). This was also found to be true in emerging markets, where a recent study found that ESG factors helped investors achieve significant outperformance (Cambridge Associates 2016).

This link was confirmed in a subsequent study of 1,333 U.S. companies representing 56 percent of U.S. market capitalization, excluding financials and utilities, for 2007–2014. The study found that disclosure of material ESG information (defined by SASB) results in stock prices that reflect more firm-specific information and thereby lower synchronicity (or correlation) with market and industry returns. This provides additional evidence of the link between stock prices and the effective integration of ESG in business operations and strategy (Grewal, Hauptmann, and Serafeim 2017).

Meaningful ESG reporting can provide insights into the **quality of a company's management**, including its ability to do the following:

- Understand key stakeholder priorities;
- Assess risks and opportunities over different time horizons;
- Create and execute strategies that achieve multiple objectives, both financial and nonfinancial;
- Manage different concerns and priorities from a diverse set of stakeholders.

ESG reporting can help publicly listed companies—or those contemplating a listing—**comply with increasing ESG stock exchange listing requirements**, especially in emerging markets (see ***0.1.3. Drivers of ESG Reporting***, below.

### 0.1.2. Benefits of Integrated ESG Disclosure

When integrated with strategic and financial reporting, ESG information can bring both internal and external benefits. The following are some of the internal benefits:[5]

- Understanding value creation over the short, medium, and long term;
- Improving internal data quality and decision making;
- Identifying gaps in ESG practices and improving risk management;
- Raising awareness and educating board directors about new or emerging material risks, and improving collaboration with the management.

For investors and external stakeholders, integrated ESG reporting helps provide context and **give a broader view of strategy and performance** and can provide confidence in the **long-term viability of the business model.** Some nonfinancial dimensions of performance, such as employee turnover or product quality, may even be thought of as pre-financial or leading indicators of long-term financial performance. (See Box 0.1.)

Integrated ESG reporting can also help external stakeholders and investors assess how a company is creating value over time and whether it is making a **positive contribution to society**, a factor that is increasingly important, given the rise of impact investing[6] and the increased perception that companies should participate in economic and social development and the realization of the United Nations Sustainable Development Goals (SDGs). It provides an account of a company's total contribution beyond economic and financial—its human capital, relationships, and destruction or preservation of natural resources as well as its effect on other dimensions of society's wellbeing.

### 0.1.3. Drivers of ESG Reporting

A recent study by HSBC, conducted with 1,000 companies and institutional investors globally, found that the main driver for ESG disclosure is investor pressure (83 percent), followed by international regulation (77 percent) (HSBC 2017).

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[4] See Dhaliwal et al. (2011); Goss and Roberts (2011); El Ghoul et al. (2010); El Ghoul et al. (2014); Khan, Serafeim, and Yoon (2015); and Deutsche Bank (2012).

[5] In a survey of 66 companies that were early adopters of the IIRC's Integrated Reporting Framework, more than 90 percent of respondents reported improvements in internal understanding of how their organizations create value—including improvements in understanding by the board (Black Sun 2014).

[6] Impact investing: investments intended to generate a measurable, beneficial social or environmental impact alongside (or in lieu of) a financial return.

**Box 0.1:** Benefits of ESG Management

Managing environmental, social, and governance factors can contribute to various corporate value drivers:

- Revenue generation:
  *Innovation*
  *New consumer needs*
  *Access to new markets*
  *Increased customer loyalty*
- Cost savings:
  *Optimizing use of natural resources (water, energy, and other inputs) in production*
  *Establishing partnerships and developing suppliers*
- Productivity and intellectual capital:
  *Attracting and retaining talent*
  *Raising workforce productivity*
- Risk mitigation:
  *Reducing exposure to environmental and social risks*
  *Impact on operational, market, financial, and other risks*
- Compliance with and anticipation of legal requirements
- Enhancement of reputation and image

Source: BM&F Bovespa (2016).

### *Investor Demand*

There is empirical evidence that **investors value ESG information**, driving rapid growth in the demand for this information.[7] According to a global survey of mainstream investment organizations, conducted by the Said Business School at the University of Oxford and Harvard Business School, "The clear majority of respondents (82%) suggest that they use ESG information because it is financially material to investment performance" (Amel-Zadeh and Serafeim 2017).

Investors want to know about ESG factors for a range of purposes, but their main objectives are risk management and credit analysis. The Said/HBS study cited above found that ESG material is perceived to provide information primarily about risk. Similarly, a CFA (Chartered Financial Analyst) Institute survey found that 73 percent of investors take ESG issues into account in their investment analysis and decisions, mainly to help manage investment risks (CFA 2017). A PRI (Principles for Responsible Investment) report on ESG factors in credit risk analysis shows that investors and credit rating agencies are ramping up efforts to consider ESG factors in credit risk analysis, mostly focused on environmental issues (PRI 2017b).

However, ESG integration into financial analysis is hindered by the low quality of ESG information. In the 2017 HSBC study, 56 percent of investors described current disclosure levels as "highly inadequate." In its recent survey, the CFA Institute found that the main factor limiting investors' ability to use nonfinancial information in investment decisions was the lack of appropriate quantitative ESG information (55 percent), followed by the lack of comparability across firms (50 percent) and the questionable data quality and lack of assurance (45 percent) (CFA 2017).

One partial explanation is the gap between company performance and disclosure. The HSBC survey found that 53 percent of companies now have an environmental strategy, yet only 43 percent actively disclose it (HSBC 2017). Another explanation is a gap between the perceptions of investors and companies. A recent PwC study on investors, corporations, and ESG reporting found that only 29 percent of *investors* view the information the companies report as high-quality, while 100 percent of the *companies* rank the same information as high-quality (PwC 2016b). Another study, by MIT Sloan School of Management, found that 75 percent of investors agree that sustainability performance is materially important for investment decisions, compared with 60 percent of managers in publicly traded companies (Unruh et al. 2016).

### *Regulatory Pressure*

Regulatory and quasi-regulatory mechanisms also put pressure on companies to disclose information that is relevant for a growing list of stakeholders, including investors, customers, and employees. For example, stock listing requirements in emerging markets, where capital markets represent the main driver for reporting, often include disclosure and transparency and increasingly require the disclosure of sustainability information. (See Box 0.2 on the next page.)

Adding to the regulatory pressure, the EU High-Level Expert Group on Sustainable Finance issued its final report on January 31, 2018, and included as one of its key recommendations to upgrade disclosure rules to make sustainability risks fully transparent, starting with climate change. The report also recommends having listing authorities promote disclosure of ESG information.

[7] A formal analysis of the growing demand for environmental, social, and related information is provided by Eccles, Krzus, and Serafeim (2011).

**Box 0.2:** Drivers of ESG Reporting

***Regulations.*** Increasingly, regulation at the national level requires disclosure of ESG information. For example:

- *India.* The securities regulator requires the 500 largest listed companies to include a business responsibility report in their annual financial report, based on the *National Voluntary Guidelines on Social, Environmental & Economic Responsibilities of Business*. The guidelines encourage disclosure of amounts spent on community programs, stakeholder engagement on specific issues, and supply-chain management.
- *South Africa.* Since 2010, companies listed on the Johannesburg Stock Exchange (JSE) are required to produce integrated financial and sustainability reports or explain their reasons for not complying.
- *Brazil.* In 2011, the Brazilian stock exchange amended its sustainability reporting requirement to allow listed companies to decide whether to produce sustainability reports or integrated reporting.
- *Peru.* In 2015, the Securities Market Regulator issued a resolution requiring public companies to produce an ESG report together with their annual report.
- *European Union.* An EU directive on disclosure of nonfinancial and diversity information (2014/95/EU) requires large companies (with more than 500 employees in the EU) to disclose nonfinancial information, including policies, main risks, and outcomes relating to environmental, social, and employee matters, respect for human rights, anticorruption and bribery issues, and diversity on the board.

***Corporate governance codes.*** An increasing number of countries have adopted corporate governance codes that often include specific provisions on the management and public reporting of sustainability (Brazil, Kenya, Malaysia, and South Africa, among others).

***Stewardship codes.*** An emerging practice among institutional investors in many countries, including the United Kingdom and the United States, is to adopt stewardship codes that set guidelines for proxy voting and engagement, and for investor expectations about governance practices.

***Stock exchanges.*** Stock exchanges in many countries either require or actively encourage sustainability reporting. For example, stock exchanges in Brazil, Malaysia, and South Africa have adopted a "comply or explain" approach, requiring sustainability or integrated reporting or an explanation for nondisclosure. The BVL (Lima Stock Exchange) has issued detailed guidance for listed companies on what ESG information to report and how to report it.

***State-owned enterprises.*** Sustainability management and reporting requirements for state-owned enterprises are now in place in more than a dozen counties, including China, Ecuador, Indonesia, and Russia.

***Supply chains.*** As large, multinational companies are under increasing pressure to report and to manage supply-chain risks, they are asking or requiring their main suppliers to also report on sustainability policies and performance.

Source: IFC.

## 0.2. Comprehensive and Integrated Approach to Corporate Reporting

As part of its effort to further disclosure and transparency, IFC promotes a comprehensive and integrated approach to corporate reporting—one that supports the analysis of modern drivers of corporate value that are not always captured in typical annual reports.

This approach presents strategic and corporate governance information together with financial results—providing investors with a better understanding of how the company is likely to perform in the future. It also calls for disclosure of the impact that environmental and social issues may have on the company's strategy, risk profile, and performance, and how key opportunities and risks are managed as part of the company's corporate governance.

### 0.2.1. Sustainability Integrated into Strategic, Governance, and Performance Reporting

Sustainability represents both opportunities and risks for companies, and it should be integrated into all major sections of an annual report, including the following:

- ***Sustainability strategy.*** In the *strategy* section of the annual report, companies should present an overview of key sustainability issues and their method for selecting those issues.

- ***Sustainability governance.*** Management and governance processes related to sustainability issues—whether considered strategic objectives or risks—should be disclosed in the *governance* section.

## Model Structure of Annual Report

### 1. Strategy

- Business Model and Environment
- Strategic Objectives
- Risk Analysis and Response
- Sustainability Opportunities and Risks
- Introducing Key Performance Indicators

### 2. Corporate Governance

- Leadership and Culture: Commitment to ESG
- Structure and Functioning of the Board of Directors
- Control Environment
- Treatment of Minority Shareholders
- Governance of Stakeholder Engagement

### 3. Financial Position and Performance

- Performance Report
- Financial Statements
- Sustainability Statements

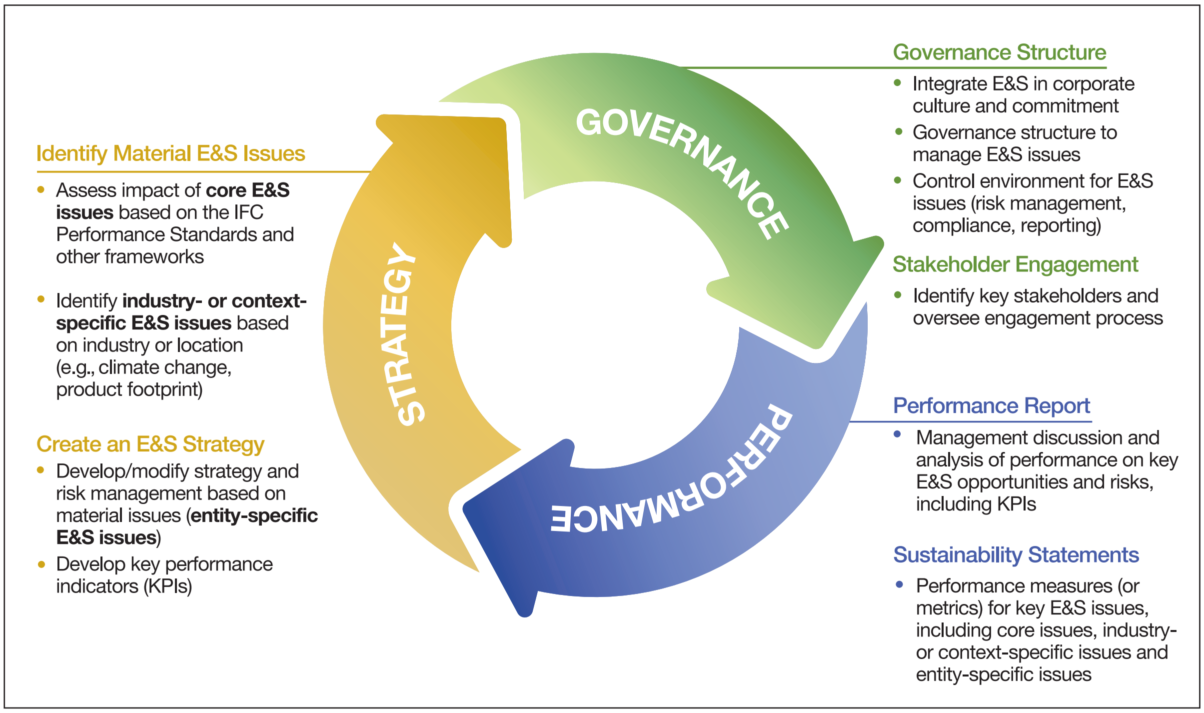
- ***Sustainability performance.*** In the *performance* section of the annual report, companies should report on their performance in managing the sustainability issues they have identified as material. This includes a discussion of performance and key performance indicators (KPIs) in the *performance report* as well as the disclosure of quantitative, comparable, and consistent sustainability metrics in the *sustainability statements*.

Figure 0.1 provides a roadmap for integration of environmental and social (E&S) issues into a company's strategy.

The integration of a company's reporting on strategy, governance, and performance reflects a long history of innovation in corporate reporting. It brings together reports that are typically separate, and combines disclosures that are mandatory in most markets (such as financial statements and elements of corporate governance) with disclosures that are voluntary in most markets (such as sustainability).

This approach is in line with a recent international trend toward integrated reporting, which expands the scope of traditional financial reports and integrates nonfinancial information about such intangible factors as environmental, social, and governance considerations. Various practical applications of the concept have been proposed, including the Integrated Reporting (<IR>) Framework by the International Integrated Reporting Council (IIRC).

**Figure 0.1:** Roadmap for Integration of Environmental and Social Issues




Source: IFC.

The Toolkit promotes a version of integrated reporting that combines the most material elements of information currently contained in separate reports—such as financial, management commentary, governance and remuneration, and sustainability—into a single coherent document.

The Toolkit builds on international best practices and promotes a set of principles for corporate disclosure and transparency that are particularly relevant for emerging markets.

### Principles of Corporate Disclosure and Transparency in Emerging Markets

- ***Connected.*** Links strategic, governance, and financial information
- ***Integrated.*** Sustainability addressed as part of the company's core management and governance functions
- ***Open.*** Promotes a culture of openness and transparency within and outside the organization, based on dialogues and feedback loops and a dynamic information management system
- ***Inclusive.*** Supports dialogue and mutual learning between the company and its stakeholders
- ***Material.*** Relevant, based on the context of operation, especially in emerging markets
- ***Credible/reliable.*** Robust management process for internal data collection and external verification, including ESG information

## 0.2.2. Incorporating ESG Good Practices and Global Standards

Disclosure guidance on ESG issues is based in large part on IFC's own Corporate Governance Matrix and Performance Standards as well as other globally recognized standards, such as the IIRC's <IR> Framework and the Global Reporting Initiative (GRI) Standards.

### Terminology Used in This Toolkit

***Sustainability*** or *corporate sustainability* refers to environmental and social factors that have an impact on the long-term performance of companies. (See ***1.4. Sustainability Opportunities and Risks***, page 26 of this Toolkit, for a more complete definition of corporate sustainability.)

***ESG*** refers to the combination of environmental and social factors with corporate governance.

### *The IFC Corporate Governance Matrix*

The Toolkit incorporates the IFC Corporate Governance Matrix, a tool to evaluate and improve the corporate governance of a company—including the governance of key environmental and social policies and procedures—to identify, reduce, and manage risk. The Matrix does not include all of the requirements of the IFC Performance Standards for Environmental and Social Sustainability, but it does include the governance attributes required to manage these risks.

The Matrix updates the IFC Corporate Governance Matrix (2007) to include key corporate governance considerations following the financial crisis and integrates environmental and social issues consistent with IFC's Policy on Environmental and Social Sustainability. It expands the definition of stakeholders to include Affected Communities, contracted workers, primary-supply-chain workers, suppliers and contractors, and local and international nongovernmental organizations (NGOs) and civil society organizations (CSOs). Use of this tool can help a company confirm its commitment to demonstrate leadership and promote good environmental, social, and corporate governance practices throughout the company.

The Matrix is based on the IFC Corporate Governance Methodology, which defines corporate governance as a set of structures and processes for the direction and control of companies, involving a set of relationships between a company's shareholders, board, and executive bodies, for the purpose of creating long-term shareholder and stakeholder value. The Matrix represents a summary of key ESG provisions along six parameters:[8]

- Commitment to Environmental, Social, and Governance (Leadership and Culture)
- Structure and Functioning of the Board of Directors
- Control Environment (Internal Control System, Internal Audit Function, Risk Governance and Compliance)
- Disclosure and Transparency
- Treatment of Minority Shareholders
- Governance of Stakeholder Engagement

The provisions are general, based on international good practice, and may be modified or supplemented to take into account any particular jurisdictional requirements or local environment.

[8] The IFC Corporate Governance Matrix is found in ***Appendix D.***

**How the IFC Corporate Governence Matrix is Used in the Toolkit**

Relevant excerpts of the Corporate Governance Matrix are replicated at the beginning of each section on corporate governance to suggest how companies can manage and disclose ESG practices with increasing levels of sophistication.

The Toolkit and model annual report do not include a section on the fourth parameter of the Matrix: Disclosure and Transparency. Instead, these practices are integrated throughout the Toolkit and its recommendations.

***IFC Performance Standards***

The Toolkit provides guidance for E&S disclosures that are consistent with IFC's Environmental and Social Performance Standards (2012),[9] which define IFC clients' responsibilities for managing their environmental and social risks. The Performance Standards were developed as a risk management framework and have become a global benchmark for project finance. (See Figure 0.2.)

***Global Frameworks for Sustainability Management and Disclosure***

The Toolkit is consistent with the major global sustainability frameworks and provides a flexible tool that can be used to integrate a variety of sustainability management and reporting best practices.

**Figure 0.2:** IFC Performance Standards


Source: IFC.

**RESOURCE:** IFC's *Environmental and Social Management System Implementation Handbook*.

Table 0.1 on the next page compares the Toolkit with global frameworks and standards that are widely used and most comprehensive, focusing on differences in objectives, audiences, and the assessment of what is material. (*Appendix E* provides a more detailed, but not exhaustive, list of major frameworks for sustainability management and disclosure.)

### 0.2.3. Progressive Levels of ESG Performance and Reporting

The IFC Corporate Governance Matrix is organized by four levels of company maturity and complexity and emphasizes the importance placed on ongoing improvements in a company's governance practices, graduating from basic to intermediate to advanced:

- **Level 1.** Basic ESG practices that the company should develop and adopt. Level 1 likely reflects newly formed or young companies or those developing an ESG agenda from the beginning.
- **Level 2.** Intermediate ESG practices, incorporating basic steps to strengthen ESG within the organization, which reflects a culture of continuous improvement.
- **Level 3.** Good international practices, including incorporating intermediate and other good ESG practices that indicate that the organization has a track record of mature and established ESG practices.
- **Level 4.** Leadership, international best practices, indicating that the organization has achieved the preceding three levels of ESG maturity and conforms to the recognized international practices.

Table 0.2 on page 9 provides a general illustration of how the progression works. (For the complete IFC Corporate Governance Matrix, see *Appendix D*.)

***Modular Use of the Toolkit***

In addition to providing reporting guidance for different levels of performance, the Toolkit can be used in modules to implement different depths of reporting, based on the company's size and organizational complexity. Figure 0.3 on page 10 describes the different elements of an integrated strategy, governance, and performance report and suggests how different modules can be used, depending on company size and sophistication.

[9] IFC Performance Standards: http://www.ifc.org/wps/wcm/connect/Topics_Ext_Content/IFC_External_Corporate_Site/Sustainability-At-IFC/Policies-Standards/Performance-Standards.

**Table 0.1** Comparing the Toolkit with the Main Disclosure Frameworks and Standards

| | IIRC | GRI | CDSB | SASB | TFCD | IFRS/IASB | IFC DT Framework |
|---|---|---|---|---|---|---|---|
| **Type of Guidance** | Framework | Standards | Framework | Standards | Guidelines | Standards | Framework |
| **Application** | Voluntary | Voluntary | Voluntary | Voluntary | Voluntary | Compulsory | Voluntary |
| **Coverage** | Global | Global | Global | U.S., can be applicable globally | Global | Global | Global, focus on emerging markets |
| **Objective** | Help organizations explain to providers of financial capital how they create value over time | Enable all organizations—regardless of size, sector, or location—to report the sustainability information that matters | Help organizations prepare and present environmental information in mainstream reports | Help public corporations disclose material sustainability information in mandatory SEC filings | Enable stakeholders to understand the financial system's exposures to climate-related risks | Provide financial information that is useful in making investment decisions | Improve capital flows to emerging markets by reducing actual and perceived risk |
| **Topics** | Value creation over time; use of or effects on all capitals: financial, manufactured, intellectual, human, social & relationship, and natural | Reporting entity's economic, environmental, and social activities and impacts | Environmental information & natural capital | Environment, social capital, human capital, business model & innovation, leadership & governance | Climate-related risks, opportunities, financial impacts, and scenario analysis | Financial accounting | Strategy, governance, and performance |
| **Target Audience** | Providers of financial capital | Multiple stakeholders | Investors | Investors | Investors | Current/potential capital providers, lenders | All stakeholders addressed; investors prioritized |
| **Materiality** | A matter is material if it could substantively affect the organization's ability to create value in the short, medium, or long term | "Material aspects" are those that reflect the organization's significant economic, environmental, and social impacts; or that substantively influence the assessments and decisions of stakeholders | Allow investors to see major trends and significant climate-change events that affect or have ability to affect financial condition and/or ability to achieve strategy | A fact is material if "there is a substantial likelihood" that a "reasonable investor" would view its omission or misstatement as "having significantly altered the total mix of information" | Public companies' legal obligation to disclose information in their financial filings—including material climate-related information | Information is material if omitting it or misstating it could influence decisions that the primary users of general-purpose financial reports make on the basis of financial information about a specific reporting entity | A combination of financial materiality and sustainability material |

**Table 0.2:** IFC Corporate Governance Matrix—How It Works

| Level 1. Basic Practices | Level 2. Intermediate Practices | Level 3. Good International Practices | Level 4. Leadership |
|---|---|---|---|
| Companies that fulfill the requirements of national legislation | Companies that take extra steps to ensure good ESG practices | Companies that provide a major contribution toward improving ESG nationally and that comply with good international standards (e.g., IFC Performance Standards) | International best practices—companies that are publicly recognized as among national and global leaders on ESG; trailblazers |
| Companies fulfill Level 1 requirements | Companies fulfill Level 1 + Level 2 requirements | Companies fulfill Level 1 + Level 2 + Level 3 requirements | Companies fulfill Level 1 + Level 2 + Level 3 + Level 4 requirements |

Source: IFC.

### Toolkit and IFC Corporate Governance Matrix Terminology

***Progression Levels:*** The Toolkit provides guidance for companies to report ESG practices that are considered **good international practices**, in line with Levels 1–3 of the Matrix. When applicable, the Toolkit also provides guidance on practices that constitute leadership, according to Level 4 of the Matrix. The following terminology is used in the Toolkit:

***Common Practices:*** Refers to the Matrix Level 1 (Basic Practices) and Level 2 (Intermediate Practices).

***Good Practices:*** Refers to the Matrix Level 3 (Good International Practices).

***Leadership Practices:*** Refers to Matrix Level 4 (Leadership Practices).

***Best Practices:*** Refers to other good practices, outside of the IFC Corporate Governance Matrix.

For example, small, family-owned companies with basic management and ownership can report at the basic level, focusing on the business model and environmental and strategic objectives, the structure and functioning of the board of directors, and financial statements. A midsize company with more complex management and ownership could also focus on risk analysis and management, report on its control environment, and produce audited financial reports. At the top end of the spectrum, publicly traded companies that are part of the global value chain can demonstrate leadership in ESG by following the more sophisticated modules of the Toolkit, including the integration of sustainability into strategy, governance, and performance reporting.

#### *Use of the Toolkit as an Information Management and Communication System*

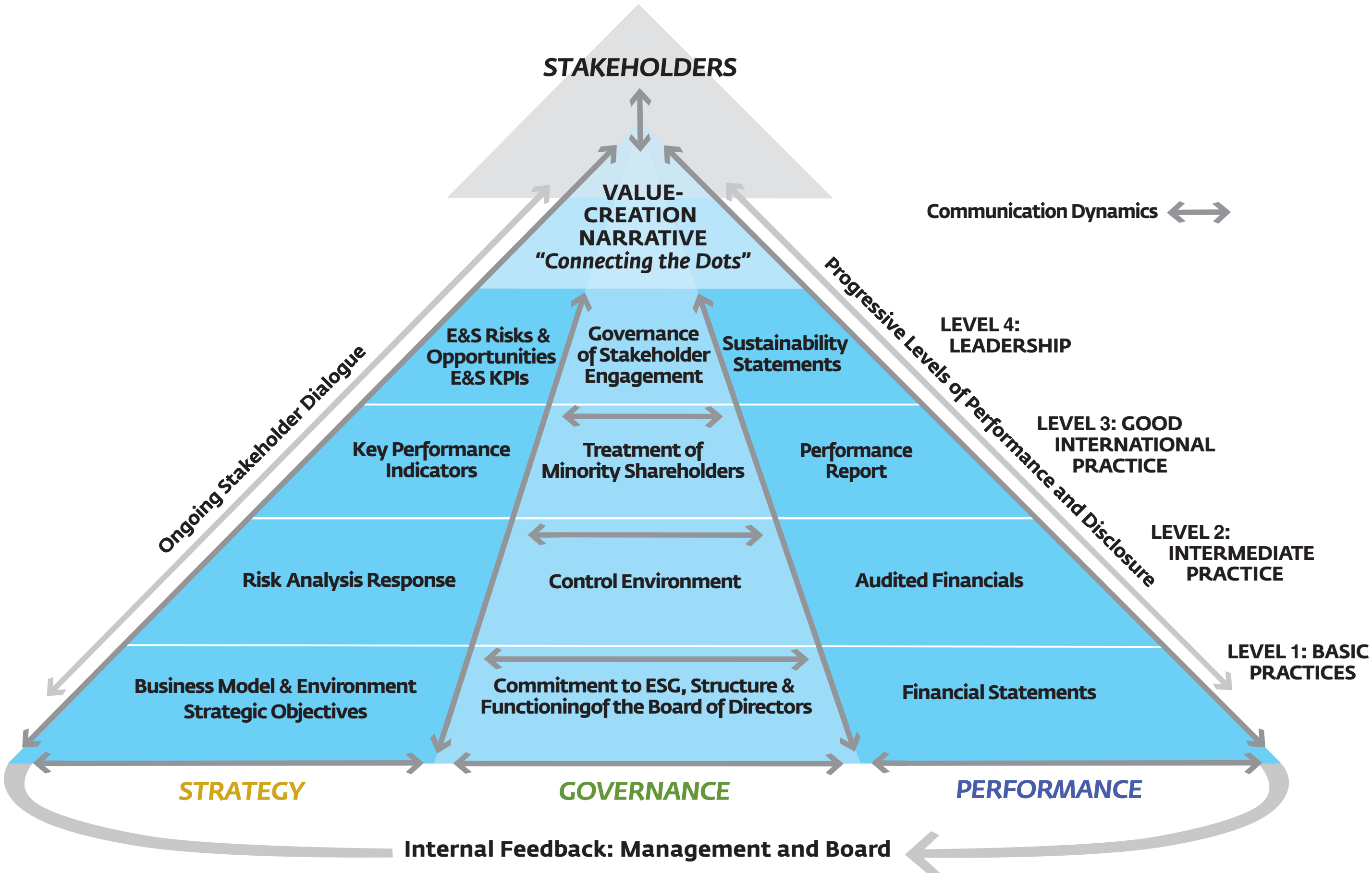
The three pillars of the Toolkit disclosure framework—strategy, governance, and performance—form an integrated pyramid structure, illustrated in Figure 0.3 on page 10. This pyramid shows how the Toolkit can be used as an internal as well as external management and communication system.

The Toolkit can function as a dynamic internal information management system emphasizing the importance of ongoing collaboration, communication, and feedback loops among different departments, functions, and people in the organization. As Figure 0.3 shows, it follows the typical internal organization of a company, in which different departments collect, analyze, and provide the information for relevant components. At the top, the executive management and the board of directors connect the dots and provide the narrative linking the company's strategy and governance to its financial and sustainability performance.

The Toolkit can also be used as an external information management system or communication tool for companies to build strong relationships and engagement with stakeholders. The pyramid reflects the most important components of an integrated ESG report and follows progressive levels of disclosure, from basic to intermediate and good practices, and culminating with ESG Leadership. The pyramid also builds on a two-way stream of information, where material stakeholder priorities inform the company's strategy, while proper disclosure creates a company culture of openness and transparency that encourages ongoing constructive and dynamic dialogue with all stakeholders and mutual learning both inside and outside the company.

Note: Modules of the pyramid correspond exactly to the different sections of the Toolkit's Disclosure Framework (Part I). Table 0.3 on page 10 provides a correspondence between the modules of the pyramid and the Toolkit.

**Figure 0.3:** Using the Toolkit as an Information Management and Communication System




Note: The progressive levels of performance and disclosure are cumulative, whereby each level also integrates practices of the preceding levels.
Source: IFC.

**Table 0.3:** Correspondence between the Modules of the Pyramid and the Toolkit

| Pyramid Sections | Toolkit Sections (page #) |
|---|---|
| **STRATEGY (page 18)** | |
| E&S Risks & Opportunities, E&S KPIs | Section 1.4 and 1.2 (pages 26 and 22) |
| Key Performance Indicators (KPIs) | Section 1.5 and 1.2 (pages 49 and 22) |
| Risk Analysis & Response | Section 1.3 (page 24) |
| Business Model & Environment; Strategic Objectives | Section 1.1 and 1.2 (pages 18 and 22) |
| **GOVERNANCE (page 55)** | |
| Governance of Stakeholder Engagement | Section 2.5 (page 92) |
| Treatment of Minority Shareholders | Section 2.4 (page 81) |
| Control Environment | Section 2.3 (page 68) |
| Commitment to ESG, Structure & Functioning of the Board of Directors | Section 2.1 and 2.2 (pages 55 and 58) |
| **PERFORMANCE (page 97)** | |
| Sustainability Statements | Section 3.3 (page 109) |
| Performance Report | Section 3.1 (page 97) |
| Audited Financials | Section 3.2 (page 102) |
| Financial Statements | Section 3.2 (page 102) |

Source: IFC.

### 0.2.4. Stakeholder Engagement—A Key to Integrating Sustainability

Companies today operate in an environment where their business is affected by numerous stakeholders, not just shareholders. Building a high degree of loyalty, cooperation, and mutual trust with key stakeholders through ongoing, constructive, and dynamic engagement and dialogue can have a significant impact on the future performance of the company.

Stakeholder engagement is a key to integrating sustainability in the company's strategy, governance, and performance.

Stakeholder engagement is a critical tool for identifying environmental and social risks and opportunities for the company and developing strategies that ensure sustainable, long-term value creation and profitability. As described in Section 1.4 and Appendix A of this Toolkit, defining the materiality of environmental and social issues is based in part on a company's outward impacts on the environment and society, including its internal and external stakeholders. IFC Performance Standard 1 on Assessment and Management of Environmental and Social Risks and Impacts provides that an effective Environmental and Social Management System (ESMS) should include stakeholder engagement, external communication and grievance mechanisms, and ongoing reporting to Affected Communities.

Governance of stakeholder engagement is also an integral part of the company's governance, as described in Section 2.5 of this Toolkit, and it is one of the six pillars of the IFC Corporate Governance Matrix. Governance of stakeholder engagement includes stakeholder mapping, stakeholder engagement policy, and grievance mechanisms for workers and Affected Communities.

Stakeholder engagement is a key outcome of an integrated corporate disclosure and transparency report, which should include matters that substantively influence the assessments and decisions of shareholders as well as stakeholders.

In this context, it is particularly important for companies to have open communication with its stakeholders and a mechanism to coordinate the interests of various stakeholders interests. Open communication is not just a one-way dissemination of information from one part of the company to another, or from the company to external actors, most notably investors; it is an ongoing stakeholder dialogue and a process of "mutual" learning, which supports an open and transparent company culture of involvement, engagement, and connectivity both inside and outside the organization. (See Figure 0.4. on page 12.)

#### *IFC Corporate Governance Matrix on Disclosure and Transparency*

The fourth dimension of the Matrix—on disclosure and transparency—provides further guidance on different levels of reporting. Table 0.4 on page 13 presents an excerpt of the Matrix on disclosure and transparency.

### 0.2.5. Toolkit Structure

The ***Disclosure Framework (Part I)*** is the core of the Toolkit. It provides detailed guidance for the three main parts of the annual report: *Strategy*, *Corporate Governance*, and *Performance*. For each of those major content areas the Toolkit provides the following:

- *Content elements*—suggests elements to be included in the report and provides guidance on how to report.
- *Integration of sustainability*—describes how sustainability information can be integrated into the main sections of the annual report, where relevant.
- *IFC Corporate Governance Matrix*—provides four levels of performance that can be described in the annual report, where relevant, supporting a flexible and progressive framework that accommodates companies of different sizes and sophistication.

#### Global versus Local Practices

The guidance in the Toolkit reflects globally accepted standards of environmental, social, and corporate governance practices. However, some standards may apply differently in different places around the world, based on local corporate culture and corporate governance practices. This includes, for example, practices involving the board structure and the definition of director independence or reporting on employees' ethnic composition in countries with tense ethnic relations.

In these situations, companies should follow the spirit of the disclosure guidance rather than its specific prescriptions. For board independence, for example, the company could discuss which areas are questionable for independence, and how it chooses to address them. For ethnic diversity, a company could report on efforts to promote inclusion of employees of all ethnic backgrounds.

- *International standards*—summarizes key frameworks and guidance for relevant content elements.
- *Examples of disclosure*—provides excerpts from annual reports from a range of companies and countries.

***Reporting Guidance (Part II)*** offers advice and considerations for preparing and presenting the information, including information quality, materiality, and specificity. It also offers guidance on integrating financial and nonfinancial information.

*Appendixes*

- Appendix A: Materiality Assessment for Sustainability Issues
- Appendix B: Questions the Board Should Ask on ESG Management and Disclosure
- Appendix C: Internal Planning for Annual Report Preparation
- Appendix D: IFC Corporate Governance Progression Matrix for Listed Companies[10] (Integrating Environmental, Social, and Corporate Governance Issues)
- Appendix E: Major Frameworks for Sustainability Management and Disclosure
- Appendix F: Annual and Sustainability Reports Used in the Toolkit

*Glossary*

***References for Further Reading***—including sources cited in the Toolkit.

**Figure 0.4:** The Process of Stakeholder Dialogue


### How do we do this?

The process involves executive management, directors, investors, and other stakeholders. Interactive dialogue embeds insights from stakeholder engagement into strategy, governance, performance, and reporting.

**1.** Customer surveys, assessments of employee engagement, focus groups, and community engagement are all ways to gain insight into what stakeholders value.

**2.** Insights from key stakeholders (e.g., customers, regulators, employees, Affected Communities) are used in strategy setting to ensure sustainable, long-term value creation and profitability.

**3.** Long-term strategic goals can be broken down into annual performance targets. To implement strategy, these goals are then assigned to units, departments, and specific individuals throughout the organization.

**4.** Progress, or performance against the strategy and objectives, is disclosed to all stakeholders in interim and annual reporting.

REPEAT

Source: IFC.

[10] Use of the Matrix is not limited to listed companies. Any organization—listed or not, and across sectors—can apply its concepts. For greater detail, see ***Appendix D*** of this Toolkit.

**Table 0.4** IFC Corporate Governance Matrix—Disclosure and Transparency

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Financial Reporting** | 1. Financial statements are audited by recognized independent external auditing firm. | 1. Financial statements prepared in accordance with International Financial Reporting Standards (IFRS) or equivalent.<br>2. Financial statements are audited in accordance with International Standards on Auditing (ISA). | 1. Audit committee oversees financial and nonfinancial reporting and audit.<br>2. Disclosure policy in place. | |
| **Risk Appetite** | | | 3. Company discloses its risk appetite. | 1. Risk appetite disclosure includes both qualitative and quantitative information. |
| **Corporate Disclosure** | 2. Compliance with all disclosure requirements and listing rules. Investors and financial analysts are treated equally regarding information disclosure.<br>3. Shareholders provided with accurate and timely information on the number of shares of all classes held by controlling shareholders and their affiliates (ownership concentration). | 3. Company discloses its code of ethics/ conduct. | 4. Significant ultimate beneficial shareholders are disclosed.<br>5. All disclosure and communications with shareholders and stakeholders made available online in a relevant and timely fashion. | 2. Tax transparency statement disclosed.<br>3. Executive compensation is disclosed.<br>4. Dividend policy is disclosed. |
| **ESG Disclosure** | 4. ESG/sustainability reporting, if any, follows minimum national requirement. | | 6. Annual report includes ESG information.<br>7. E&S/sustainability committee reviews annual report ESG information.<br>8. ESG data subject to independent review.<br>9. Information disclosed to Affected Communities is in understandable format and language.<br>10. Annual updates to locally Affected Communities. | 5. Nonfinancial disclosure in accordance with highest international standards (e.g., GRI, IIRC, SASB).<br>6. Periodic nonfinancial reporting of ESG issues that are of concern to stakeholders.<br>7. ESG data subject to an annual audit by an independent provider. |

### 0.2.6. Users of the Toolkit

***Companies*** are the primary intended users of the Toolkit, especially those with the following circumstances:

- Companies with ***separation of ownership and control***, either publicly held or privately owned but with outside investors;
- Companies based in ***emerging markets***, or foreign companies with significant operations in these markets;
- Companies looking to ***leverage superior ESG performance*** to increase their capital market valuation.

***Investors*** and banks can use the Toolkit and the resulting company reports to reduce risk and support their valuation and credit analyses.

***Regulators and stock exchanges*** can use the Toolkit to design or refine regulatory requirements related to disclosure and transparency and for comparison of local practices with global good practices.

***Others*** may find the Toolkit useful, including suppliers, customers, and the media as well as academia, data providers, and standard-setting organizations that prepare guidelines on corporate reporting.

**TOOLKIT STRUCTURE: Modular Use of the Toolkit for Small Companies**

The Toolkit's modular approach makes it relevant for a range of company sizes and operating contexts. For example, smaller and family-owned businesses can use the sections that are most appropriate for their size—Strategy and Risk, Board Structure and Functioning, and Financial Statements—and then introduce other sections, such as Treatment of Minority Shareholders and Stakeholder Engagement, at a later stage of development. (For more detail on modular use of the Toolkit, see **Figure 0.3**, page 10 of this Toolkit).

# Part I: Disclosure Framework

## Model Structure of Annual Report

### 1. Strategy

- Business Model and Environment
- Strategic Objectives
- Risk Analysis and Response
- Sustainability Opportunities and Risks
- Introducing Key Performance Indicators

### 2. Corporate Governance

- Leadership and Culture: Commitment to ESG
- Structure and Functioning of the Board of Directors
- Control Environment
- Treatment of Minority Shareholders
- Governance of Stakeholder Engagement

### 3. Financial Position and Performance

- Performance Report
- Financial Statements
- Sustainability Statements

# Part I: Disclosure Framework

Part I of the Toolkit is a *disclosure framework*, which provides guidance on the different topics that companies should address in their communication with investors and other stakeholders, including in their annual reports. Table 1.1 outlines the main content elements of a model annual report, structured around a company's strategy, governance, and performance.

**Table 1.1:** Model Structure of an Annual Report

| STRATEGY | |
|---|---|
| **STRATEGY** | **Business Model**<br>• Products and services<br>• Customers<br>• Business processes<br>• Relationships, resources, and inputs<br>**Business Environment**<br>• Markets<br>• External environment<br>• Internal drivers<br>**Strategic Objectives**<br>• Major plans and initiatives; financing needs<br>• Target setting<br>• Use of KPIs for target setting |
| **RISK** | **Risk Analysis**<br>• Risk factors<br>• Sustainability risks<br>**Risk Response and Mitigation** |
| **SUSTAINABILITY** | **Assessing Sustainability Opportunities and Risks**<br>• Opportunities identification process<br>• Risks identification process<br>**Materiality Determination of Sustainability Issues**<br>**Management of Sustainability Opportunities and Risks**<br>• Core issues<br>• Industry- and context-specific issues<br>• Contribution to economic and social development<br>• Context- and outcome-based reporting |

*(Continued on next page)*

TABLE 1.1: Model Structure of an Annual Report *(Continued from previous page)*

| CORPORATE GOVERNANCE | |
|---|---|
| **COMMITMENT TO ESG** | **Description of ESG Codes and Policies**<br>**Compliance with ESG Codes and Policies** |
| **BOARD STRUCTURE AND FUNCTIONING** | **Nomination, Appointment, and Succession**<br>• Board member tenure<br>• Rights of shareholders and other stakeholders<br>• Role of nomination committee (optional)<br>**Qualification**<br>• Background (work, education); link with board role and company strategy<br>• Sustainability expertise (aggregate and individual)<br>• Director training<br>**Independence**<br>• Executive versus non-executive versus independent directors<br>• Links between company and non-independent directors<br>• Balance of power: independence of board chair; role of independent board members<br>**Diversity**<br>• Gender<br>• Ethnicity<br>• Age<br>• Other |
| **BOARD WORK AND COMMITTEES** | **Work of Boards**<br>• Main activities and responsibilities<br>• Role of board versus management<br>**Committees**<br>• Committee mandates and work (types, roles)<br>• Composition, qualification (aggregate), and independence<br>**Board Evaluation**<br>**Governance of Sustainability** |
| **CONTROL ENVIRONMENT** | **Internal Controls and Internal Audit**<br>• Internal controls: management and oversight; scope<br>• Internal audit: main activities, challenges, and findings<br>• Audit committee: role and deliberations, including financial accounting and reporting<br>• Integrating sustainability<br>**Risk Governance**<br>• Risk appetite<br>• Risk assessment and management<br>• Risk oversight<br>• Integrating sustainability<br>**Compliance**<br>• Management system (whistleblowing, compliance program, officer in charge)<br>• Integrating sustainability<br>**External Audit**<br>• Role<br>• Qualifications<br>• Tenure<br>• Non-audit work |

*(Continued on next page)*

TABLE 1.1: Model Structure of an Annual Report *(Continued from previous page)*

| | |
|---|---|
| **CORPORATE GOVERNANCE** | |
| **TREATMENT OF MINORITY SHAREHOLDERS** | **Ownership and Control**<br>• Significant direct shareholders<br>• Indirect or "deemed" ownership<br>• Groups and control chains<br>• Controlling shareholder (identity, role, succession policy)<br>**Rights of Minority Shareholders**<br>• Board nomination and other minority shareholder rights<br>• Change of control<br>• Voting rights<br>• Protective rights<br>**Remuneration**<br>• Remuneration policy<br>• Actual remuneration<br>**Related-Party Transactions (RPTs)**<br>• Policy and management process<br>• Details on RPTs<br>**Investor Relations Function** |
| **GOVERNANCE OF STAKEHOLDER ENGAGEMENT** | **Stakeholder Identification**<br>**Stakeholder Commitment, Policy, and Strategy**<br>**External Communication and Grievance Mechanisms for Workers and Affected Communities** |
| **FINANCIAL POSITION AND PERFORMANCE** | |
| **PERFORMANCE REPORT** | **Discussion of Financial and Sustainability Performance**<br>• Financial results<br>• Financing needs<br>• Investments and initiatives<br>• Intangibles<br>• Material changes or trends<br>• Forward-looking information<br>• Sustainability performance<br>**Key Performance Indicators**<br>• Financial<br>• Operational<br>• Sustainability |
| **FINANCIAL STATEMENTS** | **Financial Statements**<br>• Statements of income<br>• Balance sheet<br>• Statement of cash flows<br>• Statement of change in stockholders' equity<br>• Notes to financial statements<br>**Statement of Audited Financial Results**<br>**Segment Report**<br>**Results per Share, Dividends, and Tax Disclosures** |
| **SUSTAINABILITY STATEMENTS AND KPIs** | **Core Issues**<br>**Industry- and Context-Specific Issues**<br>**Contribution to Economic and Social Development and SDGs**<br>**Link Back to Strategy** |

Source: IFC.

# 1. Strategy

*Strategy* can be defined as the determination of the basic long-term goals and objectives of an enterprise, and the adoption of courses of action and the allocation of resources necessary for carrying out these goals (Chandler 1962). *Strategic management* involves the formulation and implementation of the major goals and initiatives taken by a company's top management on behalf of owners, based on consideration of resources and an assessment of the internal and external environments in which the organization competes (Nag, Hambrick, and Chen 2007).

Good strategy is not just "what" you are doing, but "how" and "why" you are doing it. Just as a lever increases mechanical advantage, good strategy focuses sources of advantage on specific challenges (Rumelt 2011).

**Model Structure of Annual Report**

**1. Strategy**
- Business Model and Environment
- Strategic Objectives
- Risk Analysis and Response
- Sustainability Opportunities and Risks
- Introducing Key Performance Indicators

**2. Corporate Governance**
- Leadership and Culture: Commitment to ESG
- Structure and Functioning of the Board of Directors
- Control Environment
- Treatment of Minority Shareholders
- Governance of Stakeholder Engagement

**3. Financial Position and Performance**
- Performance Report
- Financial Statements
- Sustainability Statements

The *strategy* section of an annual report focuses attention on the company's distinct advantages, risk factors, and performance indicators. It provides the critical information that investors and other stakeholders seek in order to make informed decisions about the organization's market value and sustainability.

Critical questions include the following:

- What is the purpose of the company?
- What distinguishes this company from its competitors?
- How does the company create value?
- What are the risk factors? Are environmental and social risks taken into consideration?
- What are the key performance indicators for the business?

## 1.1. Business Model and Environment

Investors and other stakeholders need to understand what a company does, how it operates, and the context of its operations. There is a dynamic relationship between the company's business model, its environment, and its strategy. The business environment materially affects the business model, and it provides context and rationale for strategic priorities.

## 1.1.1. Business Model

The report should describe the company's main products and services, its customers, and where it fits in the value chain for the industry. It should describe the business processes that are most important to the generation, preservation, or capture of value. This can be at different stages of the value-creation process. Also, the report should describe the relationships, resources, and inputs that are key for the business to succeed. It should describe how the company is structured, the markets it operates in, and how it engages with those markets.

It is **BEST PRACTICE** for the report to present what the company does to create value—and how it does it.

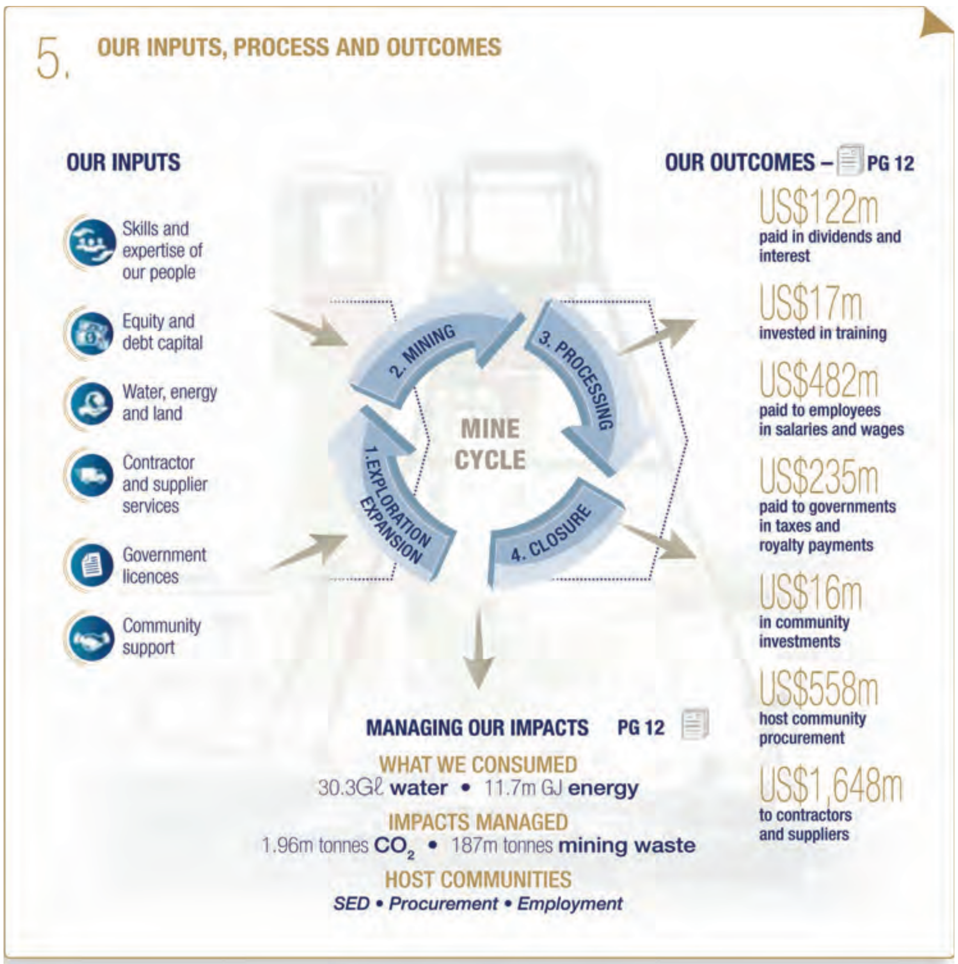
What are the business steps—inputs, process, and outcomes—that are most important for the generation and preservation of value? The examples below demonstrate how three companies focus attention on the advantages in their business process, depending on the industry, their products and services, and their challenges.

In Example 1.1, Gold Fields, a South African mining company, explains its business model—its inputs, process, and outcomes—in the context of financial and nonfinancial information.

Example 1.2 on the next page shows the concise business model for continuous innovation in the drug-development process at Chugai Pharmaceutical, a Japanese company. It focuses on key inputs, relationships, and results. Product development includes drug discovery, proof of value, and optimization of value in marketing territories. The process results in contributions to global health care.

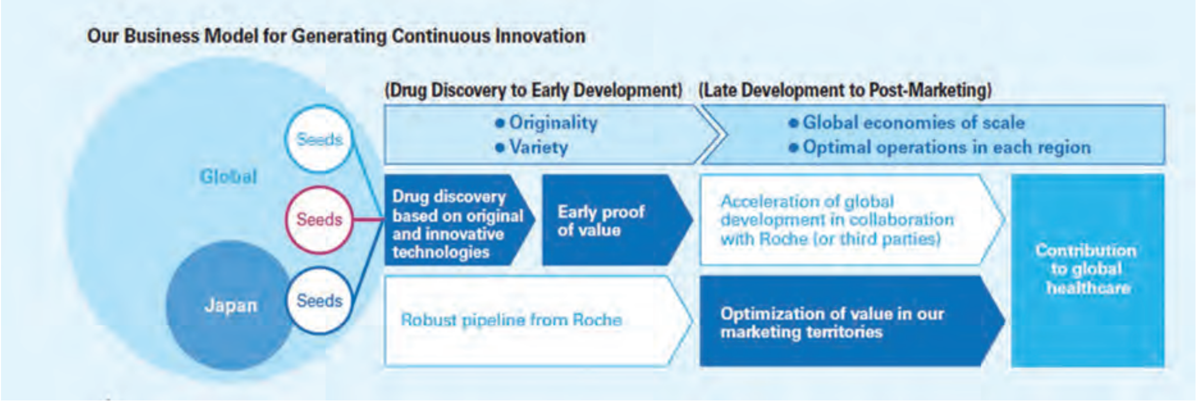
In Example 1.3 on the next page, Commercial Bank of Ceylon describes its business model in terms of value creation, based on different kinds of capital, including manufactured, social and network, intellectual, human, and natural. Strategic advantages are centrally positioned to focus attention on the bank's range of products, services, and delivery channels. Governance and Risk and Capital Management are highlighted as priorities.

**Example 1.1:** Business Environment—Gold Fields 2016 Annual Report




Source: Gold Fields.

## **Example 1.2:** Business Model—Chugai Pharmaceutical 2016 Annual Report

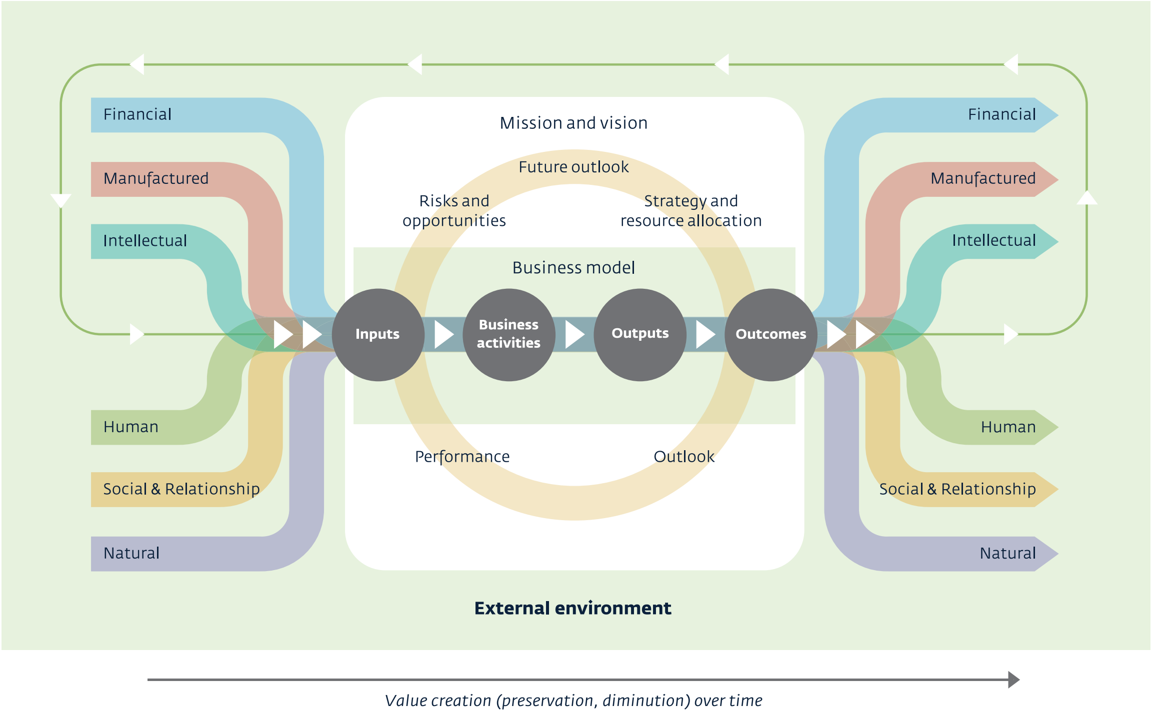



Source: Chugai Pharmaceutical Company.

## **Box 1.1:** IIRC's Value-Creation Process

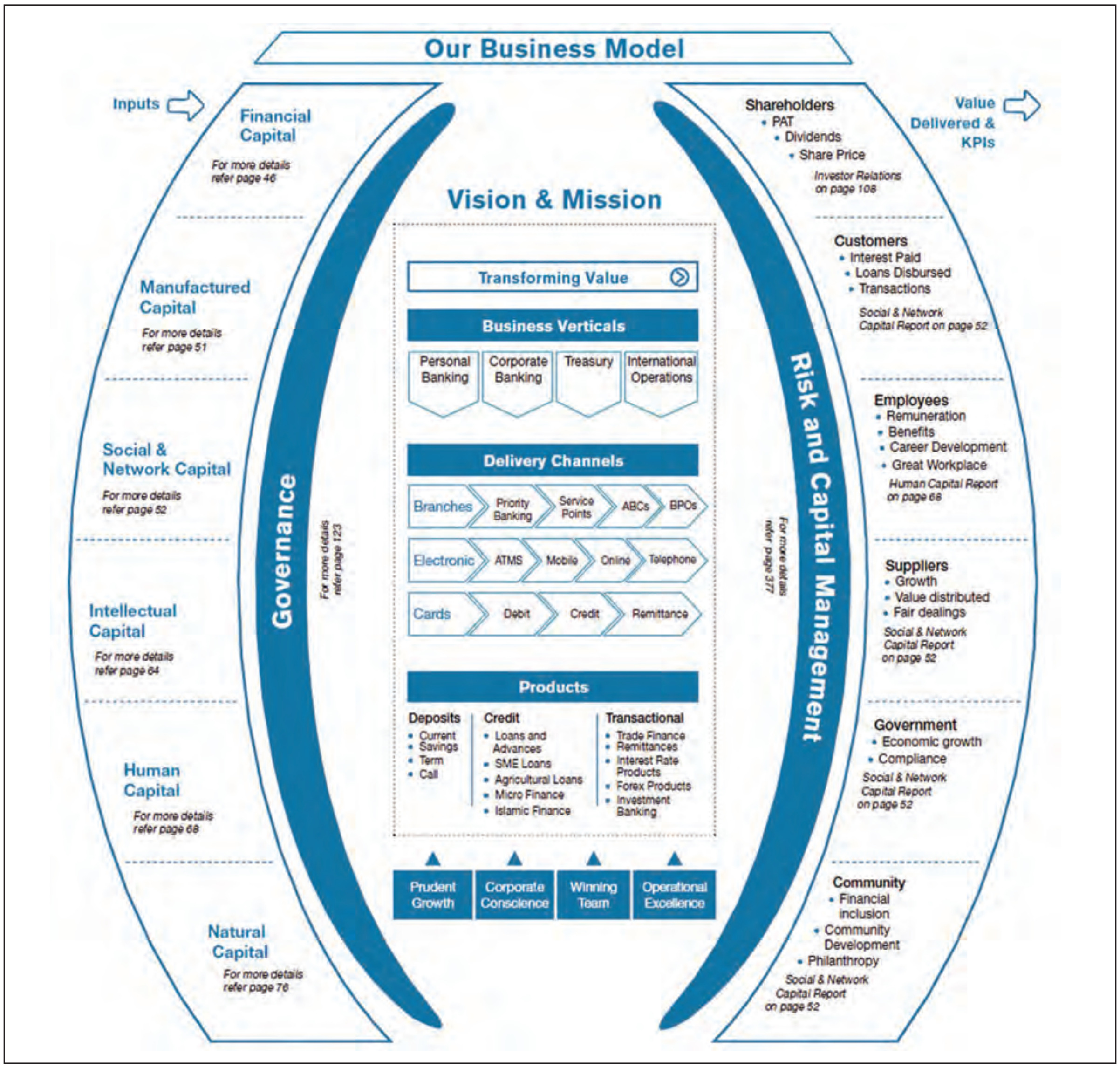
According to the IIRC's International <IR> Framework, value is created through an organization's business model, which takes inputs from the capitals and transforms them through business activities and interactions to produce outputs and outcomes that, over the short, medium, and long term, create or destroy value for the organization, its stakeholders, society, and the environment.

An organization's business model takes inputs or resources in one form or another from the capitals, identified in the capitals background paper (IIRC and EY 2013) as financial, manufactured, intellectual, human, social and relationship, and natural capital.




Source: IIRC <IR> Framework.

**Example 1.3:** Business Model—Commercial Bank of Ceylon Annual Report 2016




Source: Commercial Bank of Ceylon.

The International Integrated Reporting Council's <IR> Framework recently introduced a more holistic definition of value creation that takes into account inputs and outputs not only of financial capital but also of manufactured, intellectual, human, social and relationship, and natural capitals. (See Box 1.1 on page 20.)

### 1.1.2. Business Environment

Reporting on the business environment provides context for the company's business model and strategic objectives. It also provides a key link between strategy, risk, and performance. A careful analysis of the business environment can determine whether the company is able to create value in a sustainable manner.

Guidance for reporting on the business environment:

- *Company's markets:* Elaborate on the business model to provide clarity on key changes and trends in the markets where the company operates. Include product prices and input prices, drivers of demand and competitors' supply, and technology.
- *External environment:* Describe the macroeconomic, legal, regulatory, environmental, and social factors that can materially affect the business. Identify industry- and context-specific environmental and social issues (such as climate change, product footprint). Acknowledge the legitimate and reasonable needs and interests of stakeholders.
- *Internal drivers:* Describe company resources, structures, and processes that can affect the organization's ability to support strategy. Include internal forces driving costs, productivity, and market access. Recognize the potential effects

of major investments and projects, including the development of new products and services.

In Example 1.4, Astellas Pharma Inc., a Japanese pharmaceutical company, describes its external environment and key trends in the prescription and generic drug markets. The report provides forecasts for the global market for prescription drugs and describes the drivers of growth, including aging populations and economic development. The report also acknowledges challenges to the industry, such as stakeholder pressure to restrain health-care spending and stricter regulatory requirements for new drug approvals. Opportunities are associated with sound, long-term investments, innovative medicines, and better therapeutic solutions.

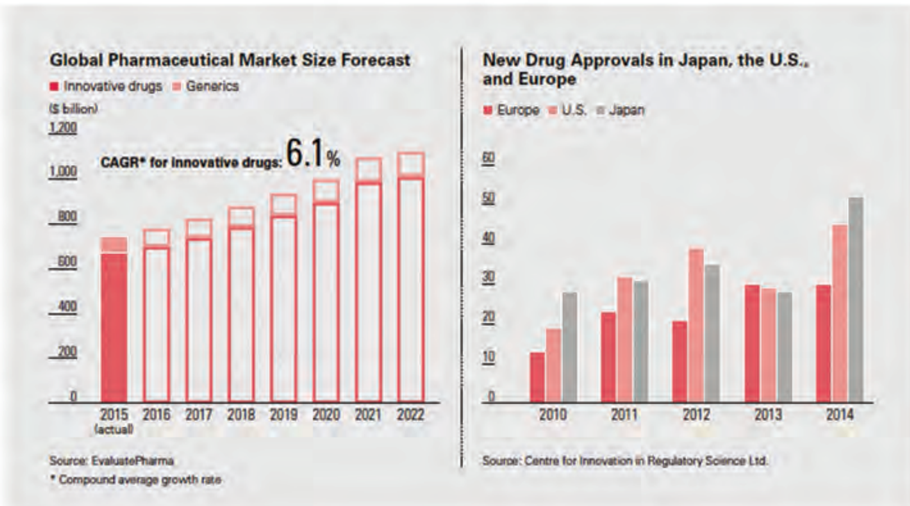
## 1.2. Strategic Objectives

The report should describe the company's major objectives, especially in the context of its business model. It should also describe how the company intends to achieve its strategic objectives in the context of its business environment, performance, and future

**Example 1.4:** Business Environment—Astellas Pharma Annual Report 2016

# Business Environment

**Market expansion driven by aging populations and economic development**




### Trends in the Prescription Drug Market

There remain many diseases with high unmet medical needs for which patients are looking for new drugs to deliver value. In step with continuing scientific and technological advances, governments are putting frameworks in place for recognizing innovation and have created regulatory systems that can accelerate review of innovative drugs. Moreover, the global market for prescription drugs is expected to continue expanding against the backdrop of aging populations and economic development.

### Growth Challenges and Opportunities

While the market expands, there are also issues that must be overcome to achieve sustained growth. Measures to restrain the rapid growth in healthcare spending are accelerating in the form of reimbursement price cuts and the promotion of generic drugs. With insurance payers becoming increasingly more involved in the decision-making process, the requirements for a new drug to gain regulatory approval and secure price reimbursement at a reasonable level are also becoming more complex and more strict. Thus, it is more essential than ever to prove a new drug's added value over existing drugs and therapies during development.

In this environment, there are higher expectations for the development of innovative medicines and better general therapeutic solutions that can raise the quality of medical care from the patient's standpoint. In recent years, the development and application of new treatment modalities and drug discovery technologies, including cell and gene therapies, have been advancing, and these advances are expected to be applied to healthcare in a variety of fields.

This evolving healthcare environment also present opportunities for Astellas to grow. Astellas will continue to deliver new value to patients by creating innovation through the execution of sound investments from a long-term perspective.

Source: Astellas Pharma Inc.

prospects. This includes plans and initiatives as well as financing and other resources needed for specific investments.

The report should indicate how the company integrates sustainability opportunities and risks into its strategic objectives. This may include sustainability objectives, which are in some cases linked to other financial or nonfinancial objectives.

Sustainability issues can constitute major opportunities. **BEST PRACTICE** suggests that they be an integral aspect of a company's strategy-setting process. (For further guidance, see ***1.4. Sustainability Opportunities and Risk***s, page 26 of this Toolkit.)

Example 1.5 presents the medium-term to long-term strategic initiatives of Santova, a logistics company in South Africa, in the context of its key differentiators.

Example 1.6 on the next page lists key strategic directions for Nedbank South Africa, including the company's strategic-focus environmental and social considerations, and it links them to its economic and social environment risks and opportunities in the short and long terms.

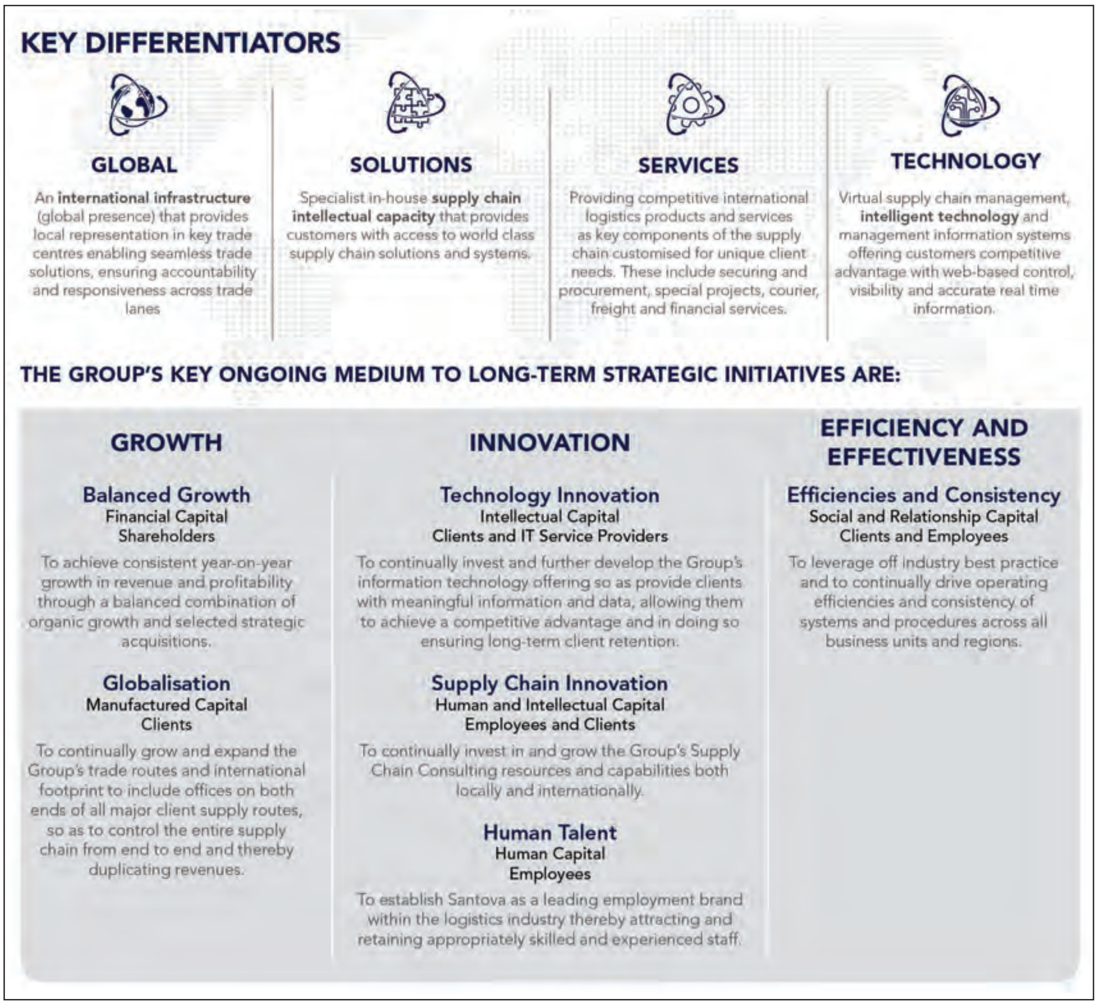
Example 1.7 on page 25 provides a one-page strategy overview that links profitability and sustainability objectives for Kumba Iron Ore Limited.

### *Target Setting*

Objectives and target setting are considered a proxy for good management. **BEST PRACTICE** suggests that companies translate strategic objectives into specific and measurable targets or goals. One approach is to use "SMART" goals, developed by management consultant George T. Doran (Doran 1981):

- ***Specific:*** Target a specific area for improvement.
- ***Measurable:*** Quantify, or at least suggest, an indicator of progress.
- ***Assignable:*** Specify who will do it.
- ***Realistic:*** State what results can realistically be achieved given available resources.
- ***Time-related:*** Specify when the result can be achieved.

**Example 1.5:** Strategic Initiatives—Santova Limited 2016 Annual Integrated Report


KEY DIFFERENTIATORS

GLOBAL
An **international infrastructure** (global presence) that provides local representation in key trade centres enabling seamless trade solutions, ensuring accountability and responsiveness across trade lanes

SOLUTIONS
Specialist in-house **supply chain intellectual capacity** that provides customers with access to world class supply chain solutions and systems.

SERVICES
Providing competitive international logistics products and services as key components of the supply chain customised for unique client needs. These include securing and procurement, special projects, courier, freight and financial services.

TECHNOLOGY
Virtual supply chain management, **intelligent technology** and management information systems offering customers competitive advantage with web-based control, visibility and accurate real time information.

THE GROUP'S KEY ONGOING MEDIUM TO LONG-TERM STRATEGIC INITIATIVES ARE:

GROWTH

Balanced Growth
Financial Capital
Shareholders
To achieve consistent year-on-year growth in revenue and profitability through a balanced combination of organic growth and selected strategic acquisitions.

Globalisation
Manufactured Capital
Clients
To continually grow and expand the Group's trade routes and international footprint to include offices on both ends of all major client supply routes, so as to control the entire supply chain from end to end and thereby duplicating revenues.

INNOVATION

Technology Innovation
Intellectual Capital
Clients and IT Service Providers
To continually invest and further develop the Group's information technology offering so as provide clients with meaningful information and data, allowing them to achieve a competitive advantage and in doing so ensuring long-term client retention.

Supply Chain Innovation
Human and Intellectual Capital
Employees and Clients
To continually invest in and grow the Group's Supply Chain Consulting resources and capabilities both locally and internationally.

Human Talent
Human Capital
Employees
To establish Santova as a leading employment brand within the logistics industry thereby attracting and retaining appropriately skilled and experienced staff.

EFFICIENCY AND EFFECTIVENESS

Efficiencies and Consistency
Social and Relationship Capital
Clients and Employees
To leverage off industry best practice and to continually drive operating efficiencies and consistency of systems and procedures across all business units and regions.

Source: Santova Limited.

**Example 1.6:** Strategic Focus—Nedbank Group 2015 Integrated Report

| MATERIAL MATTER | RISK: Short term | RISK: Medium to long term | OPPORTUNITY: Short term | OPPORTUNITY: Medium to long term |
|---|---|---|---|---|
| Tough economic conditions with limited forward visibility | ↑ | ↑ | ↓ | → |
| Banking relevance amid consumerism and increased competition | → | ↑ | → | → |
| Increased demands on governance, regulation and risk management | ↑ | ↑ | → | → |
| Growth opportunities in the rest of Africa | ↑ | → | ↓ | → |
| Transformation of society within planetary boundaries | ↑ | ↑ | ↑ | ↑ |
| Scarce skills | ↑ | ↑ | → | → |

↓ Risk/Opportunity has decreased
→ Risk/Opportunity has stayed fairly constant
↑ Risk/Opportunity has increased

Source: Nedbank Group.

### *Using KPIs in the Strategy-Setting Process*

Companies can use key performance indicators to measure the effectiveness of the company strategy and evaluate performance. KPIs can be used to set *SMART* goals and targets as part of the strategy-setting process.

Example 1.8 on page 26 shows how KPIs can be formulated as targets that relate to the company's environmental and social commitments.

For further guidance, see ***1.5. Introducing Key Performance Indicators***, page 49, ***3.1.2. Key Performance Indicators***, page 99, and ***3.3.2. Suggested Metrics for Sustainability KPIs and Statements***, page 110 of this Toolkit.

## 1.3. Risk Analysis and Response

A critical element of the strategy-setting process is the identification of internal and external risks to the company. This includes assessing the risks and determining how to respond to them.

Risk analysis and responses should be undertaken by management. However, the board should oversee risk management systems and receive regular reports on their effectiveness. This is usually the responsibility of the audit committee or another specialized committee with risk expertise and composed of a majority of independent directors. (For further guidance on the governance of risk, including through internal controls and board oversight, see ***2.3. Control Environment***, page 68 of this Toolkit.)

### 1.3.1. Risk Analysis

Risk assessment involves analyzing the likelihood and magnitude of inherent and residual risks—those that cannot be avoided—as a basis for determining how the company should manage and mitigate them.

### *Risk Factors*

The report should describe the key risk factors that have the potential to significantly affect the company and its operations. (See Example 1.9 on page 27.) The report should describe the following:

- *Risk events:* description of significant risk events and how they might be triggered;
- *Risk analysis:* likelihood and magnitude of the impact of significant risk events on operational and financial performance.

**Example 1.7:** Strategy—Kumba Iron Ore Limited 2017 Integrated Report


Source: Kumba Iron Ore Limited.

In Example 1.10 on page 27, Kumba Iron Ore Limited uses a heat map to present its risk factors, showing the likelihood and magnitude of impact, and integrating both financial and sustainability risks.

### *Incorporating Sustainability Risks*

Sustainability issues can constitute major risks for companies. Therefore, **BEST PRACTICE** suggests that they be an integral aspect of risk analysis, monitoring, and management. (See ***1.4. Sustainability Opportunities and Risks***, page 26 of this Toolkit.)

### 1.3.2. Risk Response and Mitigation

Risk response is the course of action a company chooses to take when a risk event occurs. It should be aligned with the company's risk appetite and tolerance levels. Risk responses include *accept*, *avoid*, *limit/mitigate*, and *transfer*. Specifically, the report should address the following:

- Risk mitigation for each significant risk;
- Disaster-recovery and business-continuity plans.

**Example 1.8:** KPIs for Target Setting—Integrated Annual Report 2017 of EnBW

| Goal | Key performance indicator | 2017 | Target in 2020 | |
|---|---|---|---|---|
| **Customers and society goal dimension** | | | | |
| Reputation | Reputation Index | 52.1 | 55.4 | In parallel with the restructuring of the business model, EnBW aims to continuously improve its reputation. |
| Customer proximity | EnBW/Yello Customer Satisfaction Index | 143/ 161 | > 136/ > 159 | EnBW and Yello customers are satisfied customers with a high level of customer loyalty. EnBW and Yello are organisations strongly oriented towards customers and meet the needs and wishes of their customers through tailored solutions and products. |
| Supply reliability | SAIDI (electricity) in min./year | 19 | < 25 | Maintaining supply quality for its customers is of central importance to EnBW in the further development of its grids. The high degree of supply reliability in the grid area operated by EnBW is based on comprehensive investment in grids and plants and our abundant system expertise. |
| Customers and society goal dimension › page 69 ff. | Expected trends › page 89 f. | | Report on opportunities and risks › page 91 ff. | |
| **Employees goal dimension** | | | | |
| Employee commitment | Employee Commitment Index (ECI) [2] | 60 | 65 | The commitment of our employees to EnBW is very strong and there is faith in the future viability of the company. |
| Occupational safety | LTIF[2] | 3.0 | ≤ previous year | The number of accidents at work and the resulting days of absence remains stable or is falling. |
| Employees goal dimension › page 72 ff. | Expected trends › page 90 | | Report on opportunities and risks › page 91 ff. | |
| **Environment goal dimension** | | | | |
| Expand renewable energies (RE) | Installed output of RE in GW and the share of the generation capacity accounted for by RE in % | 3.4/ 25.9 | 5.0/ > 40 | The share of the generation capacity accounted for by renewable energies has doubled compared with 2012. Onshore and offshore wind power and hydropower are at the forefront of this development. |
| Climate protection | $CO_2$ intensity in g/kWh | 556 | -15% to -20% | EnBW actively contributes to climate protection by successively reducing the $CO_2$ intensity of its own generation of electricity (excluding nuclear power) by 15 to 20% by 2020 compared to 606 g/kWh in the reference year 2015. |
| Environment goal dimension › page 77 ff. | Expected trends › page 90 | | Report on opportunities and risks › page 91 ff. | |

Source: EnBW.

In Example 1.11 on page 28, CLP Group, an electric power generation company in Hong Kong, describes its main risks, how those risks evolved during the past fiscal year, and the company's key risk mitigation efforts.

## 1.4. Sustainability Opportunities and Risks

Sustainability issues can constitute major opportunities and risks for companies and therefore should be an integral aspect of their strategy-setting process and risk management. IFC Performance Standard 1 underscores the importance of an effective **Environmental and Social Management System** (ESMS), including the following steps:

- Policy
- Identification of risks and impacts
- Management programs
- Organizational capacity and competency
- Emergency preparedness and response
- Monitoring and review
- Stakeholder engagement
- External communication and grievance mechanisms
- Ongoing reporting to Affected Communities

In this section, the Toolkit provides guidance for reporting on critical elements of an Environmental and Social Management System in the *strategy* section of the report, including the following:

- The process for assessing key sustainability opportunities and risks for the company—and how it takes into account the dynamic and evolving nature of sustainability issues;

**Example 1.9:** Risk Assessment—Astellas Pharma Inc. 2016 Annual Report

**Business Risks**

The main risks that could significantly impact the business results and financial position of the Astellas Group are outlined below.

**Inherent Uncertainties in Pharmaceutical R&D**

In general, the probability of discovering a promising compound through drug discovery research is not high. Further, it takes a large amount of investments and a great deal of time to successfully launch a new product after discovery of a new compound. However, it may be necessary to discontinue clinical development if the effectiveness of a drug is not proven as initially expected, or if safety issues arise. In addition, pharmaceuticals are subject to legal restrictions in each country, so that authorization from local regulatory authorities is a prerequisite for a product launch in each country. It is difficult to accurately foresee if and when approvals for new products can be obtained.

The Astellas Group's R&D activities are subject to these inherent risks.

**Sales-Related Risk**

The pharmaceutical industry operates in a highly competitive environment characterized by rapid technological innovation. The Astellas Group faces fierce competition from drug makers and generics manufacturers based in Japan or overseas. The launch of competitive products by rivals could impact the Astellas Group's business results significantly.

**Intellectual Property (IP) Risk**

The Astellas Group's ethical pharmaceuticals business benefits from the protection of many patents. Although the Astellas Group manages IP rights properly and is vigilant against third-party violation of such rights, the adverse impact on the Astellas Group's business results of actual IP violations may still be substantial. The Astellas Group's business results are also subject to the outcome of litigation undertaken by the Astellas Group to protect patents where infringement has occurred.

While the Astellas Group strives to ensure that its actions do not infringe the IP rights of other parties, there is a risk of litigation in the event of any inadvertent violations. Such litigation could also impact the Astellas Group's business results significantly.

**Risks Relating to Product Side Effects and Safety**

Any problems arising due to serious side effects or other safety issues that are caused by the Astellas Group's products could impact the Astellas Group's business results significantly.

**Environment-Related Risks**

The Astellas Group is careful to observe laws and regulations relating to environmental or health and safety issues and has instituted internal standards that aim to exceed most statutory requirements. Despite such precautions, the costs involved in the unlikely event of a business-related incident causing a serious breach of compliance in this area could impact the Astellas Group's business results significantly.

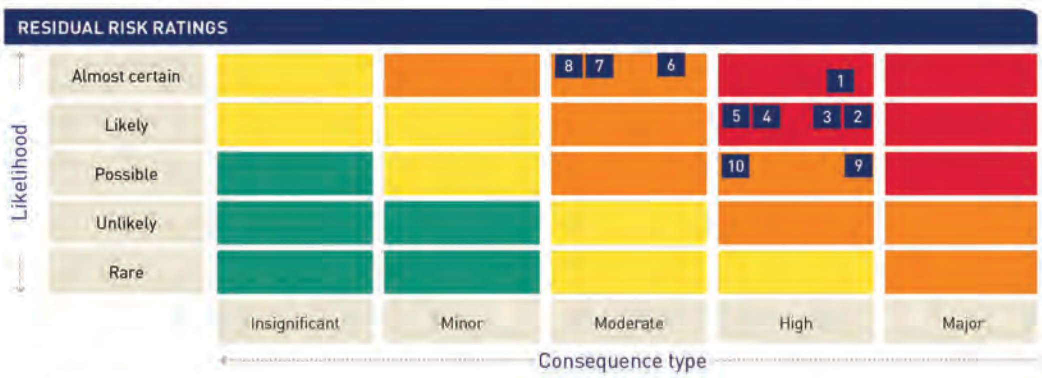
**Foreign Exchange Rate Fluctuations**

The Astellas Group's business results and financial position are subject to the impact of exchange rate fluctuations due to the Astellas Group's extensive international operations.

In addition to the risks outlined above, the Astellas Group is exposed to a wide range of business-related risks, including but not limited to (1) general commercial litigation, (2) delays or suspension of manufacturing activities due to natural disasters or other factors, and (3) partial dependence on licensing or sales agreements relating to pharmaceuticals developed by other companies.

Source: Astellas Pharma Inc.

**Example 1.10:** Residual Risk Ratings—Kumba Iron Ore Limited 2017 Integrated Report




**RISK**

1 Commodity markets and exchange rate fluctuations →
2 Safety and health ↑
3 Third-party infrastructure ↑
4 Mining legislation and regulatory compliance ↑
5 Socio-economic and current governance challenges (new risk)

**RISK**

6 Stakeholder relations and social licence to operate ↓
7 SIOC empowerment status ↓
8 Cyber risk ↑
9 Resource depletion and securing our growth (new risk)
10 Managing change (transformation of the business) (new risk)

Outlined in the heat map above is the residual rating per key/material risk for Kumba. Residual risk is the remaining risk exposure after all identified mitigation measures have been applied. The external factors beyond management's control are key contributors to the current high residual risk ratings.

Due to the improvement in risk rating, the following risk is no longer included in the top 10 risks:
– labour relations.

Source: Kumba Iron Ore Limited.

## **Example 1.11:** Risk Mitigation—CLP Group 2015 Annual Report

| Risk Description | Changes in 2015 | Key Risk Mitigations |
|---|---|---|
| **Regulatory Risk** remains the key challenge of most business units. Notably in Hong Kong, some calls to lower the level of rate of return, an increased focus on renewable energy and energy efficiency on the next SoC Agreement, for which discussions have already started between the Government and CLP Power Hong Kong. The Australian energy market continues to face regulatory uncertainty on numerous fronts from carbon, renewable energy targets, liabilities of mine rehabilitation to retail pricing re-regulation. The Chinese Government has issued power market reforms, the practical implementation of which is still very difficult to assess. | | |
| **Regulatory & political risk of Hong Kong business**<br>Medium-term risk of adverse changes to the post-2018 regulatory structure exists. The results of Hong Kong Government's public consultation on future development of the electricity market recognised the value of SoC and supported a continuation of the established regulatory framework, although there was a range of views expressed on the level of the rate of return as well as greater expectations for more renewable energy, energy efficiency and conservation and further improvements to the penalty / incentive scheme under the new regulatory regime. | *Consultation on electricity market development ended with results announced* | • Implement comprehensive stakeholder engagement plan to facilitate sensible and informed discussion on the post-2018 regulatory regime.<br>• Focus on operating performance, customer service and brand building to reinforce CLP's demonstrated performance and commitment to our customers and the wider community. |
| **Uncertain regulatory outcomes impacting EnergyAustralia's performance**<br>EnergyAustralia's performance remains under the influences of regulatory uncertainty such as carbon mitigation, renewable energy targets, spot market rule changes, technical & regulatory obligations of assets, potential changes in regulations about mine remediation, Greenhouse Gas Emissions Reduction scheme, retail pricing re-regulation etc. | *Renewable Energy Target (RET) revised down to 33TWh by 2020 (down from 41TWh previously)* | • Centralised regulation and compliance team to manage EnergyAustralia's position on proposed regulatory changes.<br>• Stakeholder and government engagement to advocate our position on regulatory changes. |

Source: CLP Group.

- The management systems in place to address key sustainability risks and opportunities;
- The key sustainability opportunities and risks for the company to monitor and manage—in the context of its business model, industry, and location of its operations and markets.

### 1.4.1. Assessment of Key Sustainability Opportunities and Risks

Sustainability opportunities and risks are specific to a company's business model, its industry, and the location of its operations and markets. What is material can differ significantly from one company to the next.

In the *strategy* section, the report should describe the company's method for assessing material sustainability opportunities and risks. The report should also address how often the assessment is performed and the roles of management and the board in overseeing the assessment.

#### *Materiality of Sustainability Issues*

Materiality was first defined as a threshold for disclosure of financial information, but the concept has evolved to reflect other, nonfinancial information—such as environmental and social information—that can be useful in understanding companies' future

**TOOLKIT RESOURCES: Further Reporting Guidance on Governance and Performance on Sustainability Issues**

*Reporting on Sustainability Governance:* The Governance section of the Toolkit provides further guidance for reporting on the governance of sustainability risks and impacts. (See ***2.1. Leadership and Culture: Commitment to ESG***, page 55; ***2.2. Structure and Functioning of the Board of Directors***, page 58; and ***2.5. Governance of Stakeholder Engagement***, page 92.)

*Reporting on Performance in Mitigating Risk and Impact:* In the *performance report* and *sustainability statements*, the Toolkit provides guidance for reporting on the management of material environmental and social issues, including mitigation efforts, and the results of such efforts. (For more information, see ***3.1. Performance Report***, page 97, and ***3.3. Sustainability Statements***, page 109 of this Toolkit.)

**Definition of Corporate Sustainability**

"**Sustainable development** is development that meets the needs of the present without compromising the ability of future generations to meet their own needs." – The Brundtland Commission

When applied to companies, *sustainability* (or *corporate sustainability*) refers to the creation of economic value, taking into account the interests of various stakeholders of the firm, including workers, customers, local Affected Communities, and the environment. It typically includes social and environmental impacts that companies may impose, and that can affect their long-term performance:

- *Social factors* include considerations that affect the wellbeing of employees, customers, and local communities and that are under the control or influence of the company. This includes fair treatment of workers, health and safety of workers and consumers, access to and affordability of basic services, economic impact on local communities, and conditions of relocation and livelihood restoration for resettled communities.
- *Environmental factors* include the effect of the company's physical activities on the environment or natural capital the company uses to operate. Effects on the environment include harmful releases, such as greenhouse gas (GHG) emissions, air pollution, and waste, as well as the use of natural resources in production (for example, water, energy, minerals) that adversely affect other users of these resources.

prospects. (See Box 1.2 on the next page for definitions of materiality.)

Sustainability issues are material when they constitute trends, opportunities, or risks that can meaningfully affect a company's operational and financial results.

Material impact can also arise from issues that have a less direct financial impact (such as damage to reputation or the license to operate, impact on non-financial capitals) but are nonetheless key for companies to create long-term value and for investors to understand future prospects of the company.

Global frameworks for financial and sustainability accounting and reporting (IFRS, GRI, SASB, IIRC) propose different but related definitions of materiality as it relates to sustainability, focusing on outward impacts of the company, inward impacts on the company, and long-term value creation.

***Focus outward.*** GRI focuses on companies' outward impacts on the environment and society and defines as material the matters that reflect the significant economic, environmental, and social impacts of the organization or that substantively influence the assessments and decisions of stakeholders.

***Focus inward.*** IFRS and SASB focus inward on the impact that environmental and social factors have on the performance of companies, and they define as material the information that a reasonable investor would consider important in making an investment or voting decision, based on the probability and magnitude of impact on a specific entity's operational or financial condition.

At some level, both inward and outward impacts are related, as outward impacts on stakeholders or the environment can translate into inward impacts on performance through reputation, regulation, license to operate, and the availability, affordability, and quality of capitals.

***Focus on long-term value creation.*** Building on this notion of a two-way interaction between a company and its surrounding environment and community, the IIRC proposes an integrated approach based on long-term value creation. It defines as material the "matters that substantively affect the organization's ability to create value over the short, medium, and long term," where value creation is defined with reference not only to financial capital but also to manufactured, intellectual, human, social and relationship, and natural capitals (IIRC 2013).

Examples 1.12 and 1.13 on page 30 and 31 show the processes two South African companies—Absa Group (formerly Barclays Africa) and Sasol—use to identify material issues. In each example, the company defines material issues as those that could substantially affect its ability to create value in the short, medium, and long term, according to the IIRC definition.

For guidance on the general use of the concept of materiality in annual reporting, see ***Materiality*** in ***Part II: Reporting Guidance***, page 123 of this Toolkit.

**Box 1.2:** Definitions of Materiality

### Materiality According to Major Accounting and Reporting Frameworks

**IFRS**: "Information is material if omitting it or misstating it could influence decisions that users make on the basis of financial information about a specific reporting entity. In other words, materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of an individual entity's financial report" (IFRS Conceptual Framework).[a]

**IIRC**: "An integrated report should disclose information about matters that substantively affect the organization's ability to create value over the short, medium and long term."

**SASB** (referencing the U.S. Supreme Court): Information is material if there is "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available" (U.S. Supreme Court, TSC Industries, Inc., versus Northway, Inc, 426 U.S. 438, 449, 1976). Materiality is determined by balancing the probability that an event will happen against the potential magnitude of the event in light of the totality of the company activity (Basic Inc. versus Levinson, 485 U.S. 224, 1988).

**GRI**: "The report should cover aspects that: reflect the organization's significant economic, environmental, or social impacts, or substantially influence the assessments and decisions of stakeholders."

[a] In September 2017, the International Accounting Standards Board (IASB) submitted for public comment proposed amendments to the IFRS definition of "material," as follows: "Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of a specific reporting entity's general purpose financial statements make on the basis of those financial statements. Materiality depends on the nature or magnitude of information, or both.".

**Example 1.12:** Materiality Determination—Absa Group (formerly Barclays Africa) 2017 Integrated Report

## Materiality

We include information in the integrated report based on the principle of materiality. Material matters are those which have influenced, or could influence, our ability to create value over the short, medium and long term as we pursue our ambition to have a positive impact on society and deliver shareholder value.

Our ability to create value is impacted by a multitude of factors ranging from the operating environment and our responses to the risks and opportunities 16 to our business model and our chosen strategy 24. Through this report we provide the context for what we have deemed our material matters and how we are managing and governing our responses. Our Balanced Scorecard provides a suitable framework for reporting back on our performance and is presented along with our risk, governance and remuneration structures which support value creation. Our material matters have remained fundamentally the same as in 2016 with the Separation being a material matter extending across all elements of our Balanced Scorecard.

| Company | Customer & Client | Colleague | Citizenship | Conduct |
|---|---|---|---|---|
| Sustainably growing revenue and delivering appropriate shareholder returns while managing the risks arising from the operating environment as well as the Separation. | Understanding customers' and clients' needs while ensuring trust and safety and providing relevant customer and client value propositions through a balanced distribution model that is engineered for the future. | Maintaining a diverse workforce of capable, committed and motivated employees with distributed leadership who are focused on, and empowered to, deliver on our strategic ambition. | Having a positive impact on society by investing in education small and medium business development and financial inclusion, while responsibly managing our environmental impact. | Driving ethical behaviour and delivering appropriate products and services compliant with the regulatory requirements and our social licence to operate. |

Source: Absa Group (formerly Barclays Africa).

**Example 1.13:** Materiality Determination—Sasol Integrated Annual Report 2017

# MATERIAL MATTERS

Our material matters are those issues that could substantially affect Sasol's ability to create value in the short, medium or long term as a result of not being able to execute on our strategy and impact our ability to stay competitive.

## We use the following process to manage our material matters:

**step 1 IDENTIFY**

By reviewing:
- Board submissions
- Quarterly submissions to the Group Executive Committee
- Our operating environment
- Risk management process and findings
- Stakeholder issues

**step 2 PRIORITISE**

By assessing:
- Materiality
- Impact of delivering on our strategy
- Risk metrics in the context of our strategy

**step 3 RESPOND**

Through:
- Assessing impact on risk tolerance and risk appetite
- Actioning activities required to manage material matters
- Evaluating scenario modelling outcomes
- Evaluating trade-offs between capitals

**step 4 REPORT**

- Plausible outcomes to the Board
- Report to stakeholders

**step 5 REVIEW AND MONITOR**

STAKEHOLDER INCLUSIVENESS

SUSTAINABILITY CONTEXT

## In 2017, we identified five material matters:

| | |
|---|---|
| **MACRO-ECONOMIC ENVIRONMENT** | The volatile macro-economic environment requires us to maintain our cash-conservation and savings initiatives, while effectively allocating capital for growth projects and improving our competitive position. |
| **DELIVERING VALUE-BASED GROWTH** | Driving continuous improvement, harnessing technology and talent, developing a diverse portfolio and embracing more digital solutions enables us to deliver superior value to our stakeholders and ensure long-term sustainability. |
| **HUMAN CAPITAL MANAGEMENT** | Promoting safety, diversity and cultural transformation as well as attracting, developing and retaining high-performing people, while engaging all employees and respecting human rights. |
| **ENVIRONMENTAL SUSTAINABILITY** | Securing our licence to operate by driving sustainable air quality, waste and land risk management, responding to the climate change and energy security challenges, promoting water stewardship and ensuring responsible product stewardship. |
| **COMMITMENT TO OUR COMMUNITIES** | Consistently delivering on our commitments to community stakeholders and optimising the impact of our social investment programmes by increasing local content and collaborating more broadly to address social and economic development challenges. |

Source: Sasol.

### Considerations in Assessing Sustainability Opportunities and Risks

The process of identifying material sustainability opportunities and risks should include the following considerations:

*Stakeholder-based.* Identification of key environmental and social risks should be based on an ongoing engagement with the company's key stakeholders, because their concerns as employees, customers, and surrounding communities will likely translate to material risks.

*Context-specific.* Key sustainability risks are specific to the context of a company's operation, including its industry, the capitals used (human, natural, financial, and manufactured), and countries of operation.

*Opportunities and risks.* Sustainability issues can represent both risks and opportunities, depending on how they are managed. For example, poor management of air emissions and waste can give rise to legal liability and stakeholder concerns/opposition, whereas proactive management can boost revenue and reputation.

*Positive and negative impacts.* The sustainability impact of companies can be both positive and negative. For example, food companies can help alleviate hunger while also creating health issues.

*Impacts of operation versus products and services.* Sustainability issues can relate to a company's operations (such as employee treatment, waste generated) as well as its products and services (such as car safety and fuel consumption).

*Impact "of" the company and impact "on" the company.* Certain sustainability issues relate to the impact companies have on their environment and surrounding communities, and their effort to mitigate those impacts (for example, GHG emissions or resettlement of indigenous people). Others are related to the impact that the environment and society have on the company. For example, climate change can affect a company's ability to operate profitably or to deliver reliable products and services, or community relations can affect a company's social license to operate. (This is related to the concept of inward versus outward impacts, discussed on page 29.)

These two aspects are often linked. According to the IIRC, the effect on external stakeholders reverts to put "pressure back on the organization through enhanced or diminished organizational reputation (e.g., an oil spill in the ocean), or the availability, affordability and quality of capitals upon which the organization relies (e.g., the availability of clean water)" (IIRC and AICPA 2013).

*Magnitude and probability.* For matters that constitute risks, uncertainty, or future prospects, the magnitude of impact and the likelihood of occurrence should be considered. As noted in Box 1.2, "materiality is determined by balancing the probability that an event will happen against the potential magnitude of the event in light of the totality of the company activity" (Basic Inc. versus Levinson, 485 U.S. 224, 1988).

Issues that have a greater likelihood of occurring or a greater likelihood of significant impact on either the reporting organization or its stakeholders should be determined to be of greater importance. (See Figure 1.1.)

### Opportunities and Risks Identification Process

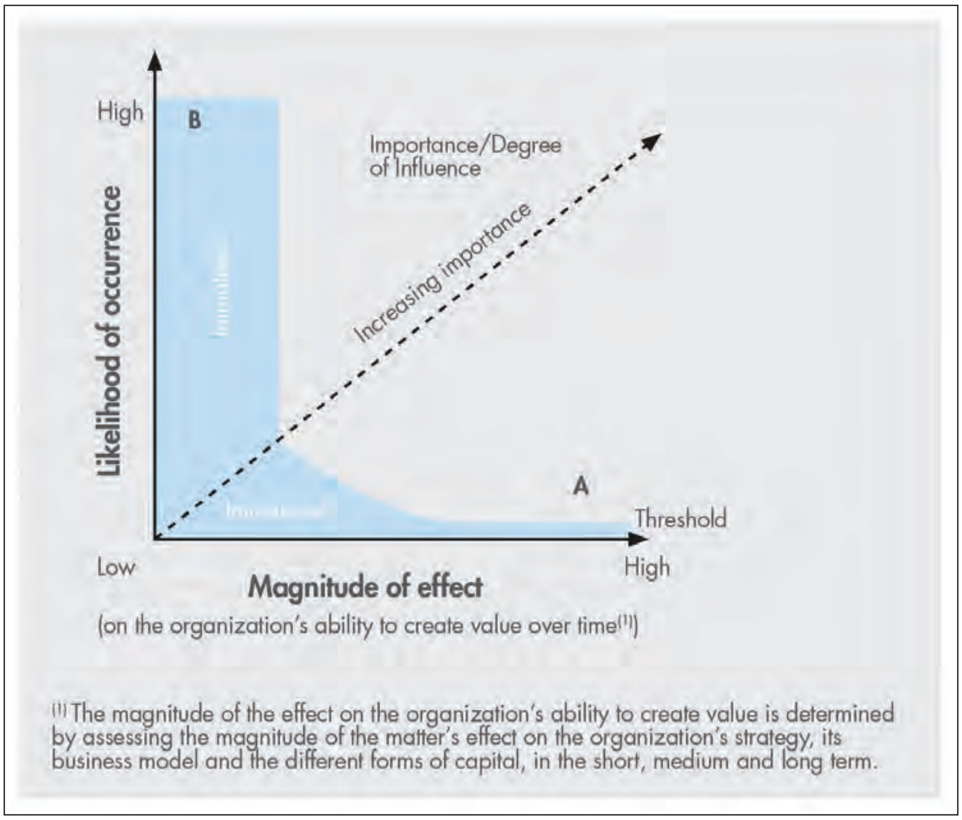
Different methods exist for prioritizing relevant issues to determine what sustainability information is material.

*Risk and opportunity assessment.* One common method for assessing key sustainability opportunities and risks is to integrate with the company's ongoing risk and opportunity assessment processes. According to the IIRC, "To be most effective, the materiality determination process is integrated into the organization's management processes and includes regular engagement with providers of financial capital and others to ensure the integrated report meets its primary purpose" (IIRC 2013). This ensures that matters determined to be material are appropriately addressed in strategy development, risk mitigation and management processes, and relevant governance structures.

*Environmental and Social Management System.* An ESMS can provide important sources of information for identifying a company's key sustainability issues. IFC Performance Standard 1 lays the foundation for a dynamic and management-driven ESMS, which includes a comprehensive identification and assessment of environmental and social risks and impacts. (For more information on ESMS, see ***1.4.2. Management of Sustainability Opportunities and Risks***, page 35 of this Toolkit.)

*Materiality matrix.* Another common method for prioritizing material issues is to create a materiality matrix that ranks the importance of sustainability issues to the company against the perception of its key stakeholders. Examples 1.14–1.17 on the following pages show the materiality matrixes for companies in the auto manufacturing, financial services, food and beverage, and resource transformation industries. Common E&S issues are found in all three matrixes, but the most material issues vary greatly among companies and industries, from product safety and fuel efficiency for Tata Motors, to customer satisfaction and information security for Deutsche Bank, nutrition and water stewardship for Nestlé, and health and safety for CEMEX.

**Figure 1.1:** Materiality: Assessing the Probability and Magnitude of Occurrence

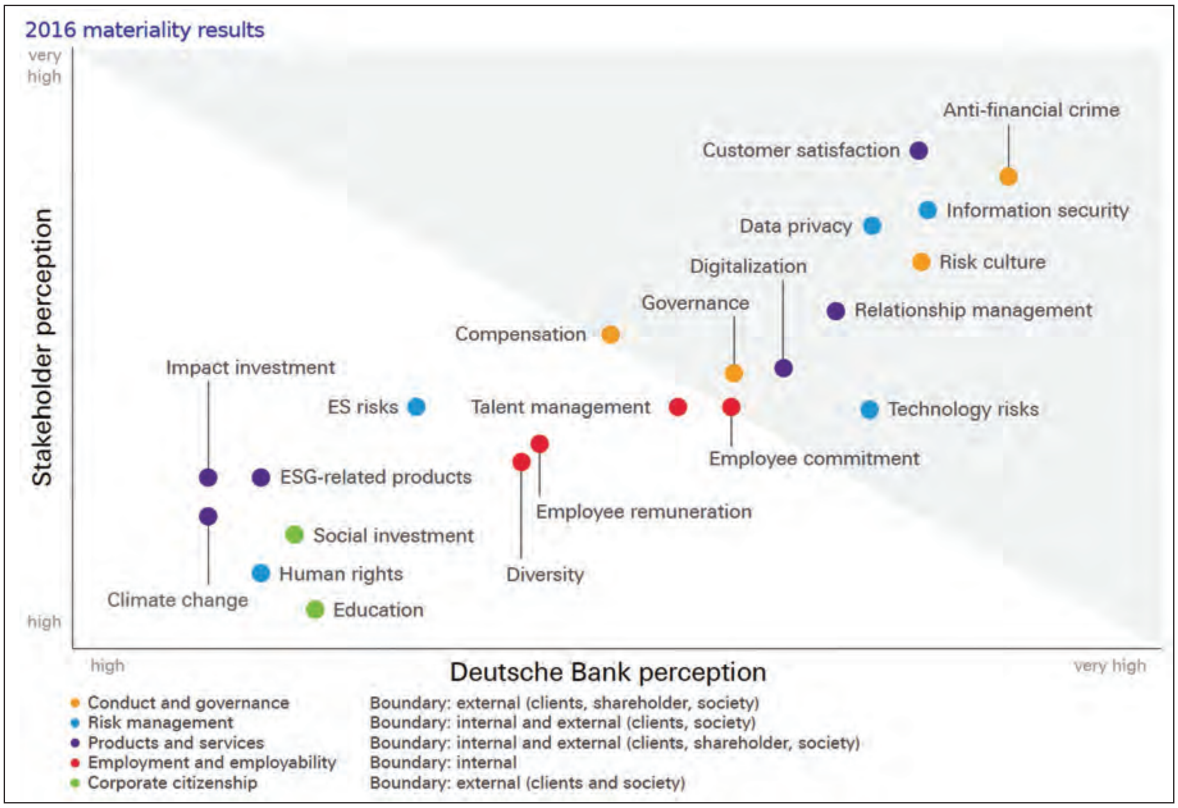



Source: IIRC.

**Example 1.14:** Materiality Matrix—Tata Motors 2015–2016 Sustainability Report

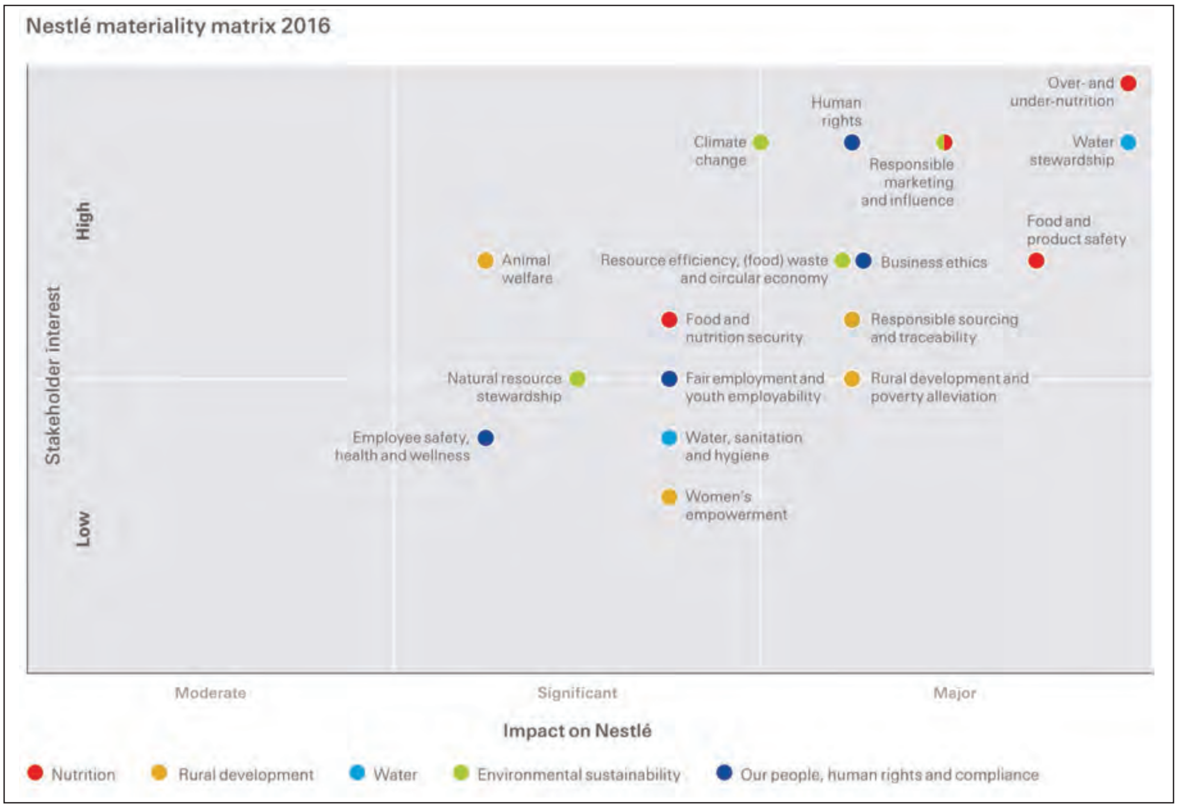

Source: Tata Motors.

**Example 1.15:** Materiality Matrix—Deutsche Bank 2016 Corporate Responsibility Report



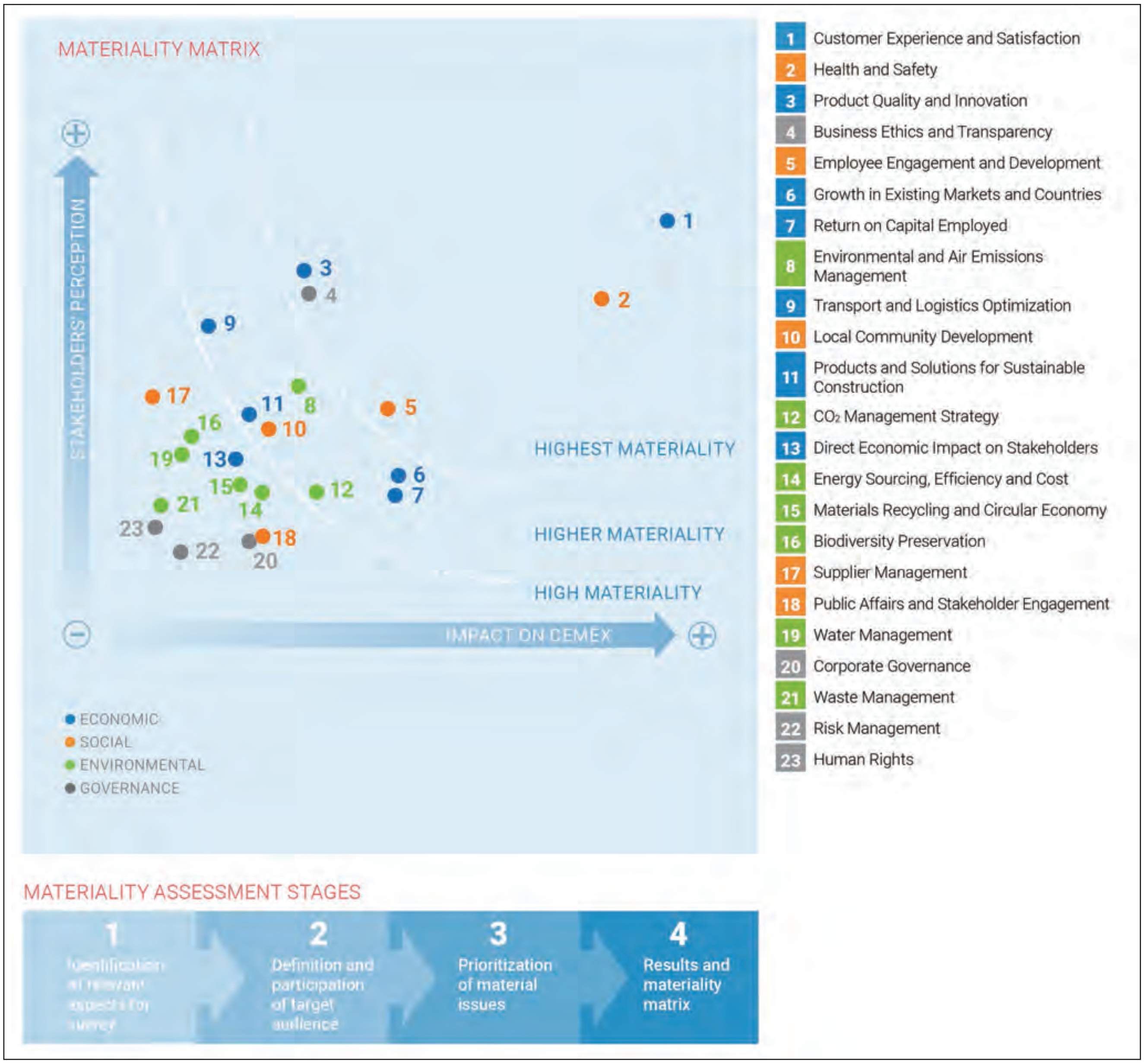

Source: Deutsche Bank.

**Example 1.16:** Materiality Matrix—Nestlé in Society 2016




Source: Nestlé.

**Example 1.17:** Materiality Matrix—CEMEX 2017 Integrated Report




Source: CEMEX.

## 1.4.2. Management of Sustainability Opportunities and Risks

The report should describe how the company integrates sustainability opportunities and risks as part of its strategic objectives, day-to-day management, and risk management. This is consistent with IFC Performance Standard 1. The company ESMS should be consistent with international standards, and the particular system applied by the company should be named and reported (for example, ISO 14000).

Companies should report on the strategy and management systems they have in place to manage and monitor the core environmental and social issues. IFC Performance Standard 1 specifies that companies should adopt a **mitigation hierarchy** to anticipate and avoid—or where avoidance is not possible, minimize—impacts and, where residual impacts remain, compensate for or offset risks and impacts to workers, Affected Communities, and the environment.

**BEST-PRACTICE RESOURCES: IFC ESMS Implementation Handbook**

*The ESMS Implementation Handbook* provides step-by-step instructions on how to develop and implement a management system in line with IFC Performance Standard 1, addressing common environmental, occupational health and safety (OHS), labor, and community risks and impacts that companies are likely to face.

Example 1.18 provides details on how Kumba Iron Ore Limited, a South African mining company, manages material issues and the year-on-year change in outlook.

### 1.4.3. Key Sustainability Issues to Manage and Monitor

The report should list the key sustainability opportunities and risks facing the company and describe how they specifically affect the company's business model, its strategy, and its risk profile.

Typically included are core sustainability issues that apply to all or most industries (such as climate-change mitigation or labor and working conditions) as well as issues that are specific to the company's industry or context of operations (such as impacts on critical habitat or indigenous people's land and natural resources). Where relevant, the report should also address the company's contribution to economic and social development.

#### *Core Environmental and Social Issues*

Core issues are those covered in the IFC Performance Standards and other generally accepted sustainability frameworks. (See ***Appendix E: Major Frameworks for Sustainability Management and Disclosure.***)

IFC Performance Standard 1 specifies that the process for identifying risks and impacts should consider "*all relevant environmental and social risks and impacts, . . . including the issues identified in Performance Standards 2 through 8, and those who are likely to be affected by such risks and impacts*."

The Standard further recommends that the process also consider "*the emissions of greenhouse gases, the relevant risks associated with a changing climate and the adaptation opportunities, and potential transboundary effects, such as pollution of air, or use or pollution of international waterways*."

Table 1.2 provides a summary of the core environmental and social issues covered by the IFC Performance Standards.

These core environmental and social issues—sometimes also referred to as cross-cutting, systemic, or universal—generally apply to all or most companies and industries.

**Example 1.18:** Management of Material Sustainability Issues—Kumba Iron Ore Limited 2017 Integrated Report

**5. SOCIO-ECONOMIC AND GOVERNANCE CHALLENGES** NEW RISK

| ROOT CAUSE | IMPACT ON VALUE | MITIGATING ACTIONS | OUTLOOK |
|---|---|---|---|
| Low levels of economic growth in South Africa exacerbate the current challenges of inequality and unemployment that are prevalent in communities where Kumba operates.<br><br>Governance and political challenges could impact on our key stakeholders on whom we depend. | – Increased reliance and growing expectations on mining companies by government and communities.<br>– Community activism and slow levels of local service delivery may cause disruptions at operations.<br>– Increased cost of living on our host communities and cost of doing business.<br>– Negative impact on investor confidence in South Africa and higher cost of doing business. | – Develop a shared vision and shared value journey with communities, youth, municipality, provincial government, NGOs, religious organisations, peer mining companies and local business.<br>– Localised preferential procurement targets have been set.<br>– Implementation of municipal capacity building initiatives. | The external socio-economic environment remains complex and challenging, with a continuing strong need to foster inclusive economic growth and good governance practices across the public and private sector.<br><br>**STRATEGIC FOCUS AREAS**<br><br>**Key enablers**<br>Provide leadership through responsible citizenship<br>Proactively engage with key stakeholders |

Source: Kumba Iron Ore Limited.

**Table 1.2:** Core Environmental and Social Issues

| CATEGORY | ISSUES |
|---|---|
| **Environmental & Social Management System** | • Environmental and social policy<br>• Emergency response plan<br>• External communication<br>• Grievance mechanism<br>• Environment and social management of supply chain[a] |
| **Environmental Issues** | **Resource Efficiency and Pollution Prevention:**<br>• GHG emissions<br>• Water use<br>• Resource efficiency<br>• Pollution prevention<br>**Biodiversity Conservation and Sustainable Management of Living Natural Resources**<br>• Ecosystem services<br>• Protected areas<br>• Endangered species<br>• Habitats and biodiversity<br>• Water sources |
| **Social Issues** | **Labor and Working Conditions:**<br>• Worker protection<br>• Opportunities and fairness<br>• Health and safety<br>• Forced and child labor[a] |
| | **Community**<br>• Community health, safety, and security<br>• Land acquisition and resettlement<br>• Infrastructure and public safety[a]<br>• Indigenous peoples<br>• Cultural heritage |

[a] Industry-specific. For further details, see ***1.5. Introducing Key Performance Indicators***, page 49 of this Toolkit.

Source: IFC.

However, they apply differently depending on the industry and context. A few of the core issues (environmental and social management in the supply chain, forced and child labor, and infrastructure) are more likely to apply in specific industries.

For example, most companies have employees or contractors, so management of labor issues and talent is generally relevant. However, depending on the nature of the industry, these issues can range from working conditions and safety in garment manufacturing to child labor in the agribusiness industry and discrimination in service industries.

Similarly, environmental impacts are common to most industries, but they occur at different points in the value chain and with different intensity. For example, manufacturing-based companies affect the environment through manufacturing and distribution, whereas knowledge-based businesses can have a considerable effect on the environment through business travel and data centers.

***The report should address how these core environmental and social issues apply specifically to the company—and describe how the company manages associated risks and opportunities, including mitigating its impact.*** Examples 1.19 and 1.20 (next page) are from two very different industries.

For a list of the most commonly reported E&S metrics, see ***Table 3.3*** on page 117 of this Toolkit.

**Example 1.19:** GHG Emissions—Apple Environmental Responsibility Report 2016

Our 2015 carbon footprint

38,400,000

metric tons of greenhouse gas emissions

| 77% | 17% | 1% | 4% | 1% |
|---|---|---|---|---|
| Manufacturing | Product Usage | Facilities | Transportation | Recycling |

Source: Apple.

***Industry-Specific and Context-Specific Sustainability Issues***

In addition to the core environmental and social issues covered in the IFC Performance Standards and other generally accepted sustainability frameworks, **BEST PRACTICES** suggest that other sustainability issues can be material for companies, based on industry and context of operation. This includes climate-change strategy, the impact of products and services, and contribution to economic and social development. (For suggested metrics for sustainability KPIs and sustainability statements based on the most commonly reported ESG metrics, see *Table 3.3*, page 117 of this Toolkit.)

**Example 1.20:** Diversity—Takeda Annual Report 2016

## Diverse perspectives lead to insightful solutions

**Our global diversity & inclusion statement (D&I):** Takeda strives to have a workforce as diverse as the patients we serve. We are committed to embracing differences, exploring possibilities and developing our employees. Our success depends on fostering an inclusive environment where all employees are welcomed, empowered and inspired to use their unique voices and talents. This is how we will find innovative approaches to serve our patients, customers and communities. This is how we will reach our highest potential together.

**Diversity has been proven to lead to more creativity and innovation. Companies with diverse leadership teams have been shown to respond more efficiently to a wide range of global challenges. For a research- and innovation-driven global company like Takeda, diversity is critical to our long-term success in delivering better health and a brighter future.**

Our ultimate goal is to offer every employee at Takeda the opportunity to thrive, develop and grow based on merit, potential and ambition regardless of gender, age, nationality, race or sexual orientation. We are committed to leveraging the unique and diverse backgrounds, experiences and insights of all our employees to better serve patients worldwide with integrity, honesty, fairness and perseverance.

We are accelerating D&I activities in Japan and many other parts of the world, and have introduced several initiatives to enhance **gender**, **work-style**, **age** and **career diversity**.

These include:

- Launching *Hanamizuki*, a network where women can learn from each other, share knowledge and information, and help each other develop professionally (Japan).
- Introducing a flexible work-style program that gives employees the choice to select the work times and places that enable them to perform at their best (Japan).
- Enhancing career diversity by encouraging faster promotion of employees who are demonstrating high performance early in their career (Japan).
- Hosting the first Takeda U.S. Diversity & Leadership Symposium week in Deerfield, IL. This symposium included employee events, workshops and keynote speakers, and featured D&I leaders within Takeda (United States).

**FY2016 Targets for Japan**

**30%** of new manager appointments will be filled by women

**10%** of newly appointed managers will be less than 8 years into their careers

Source: Takeda.

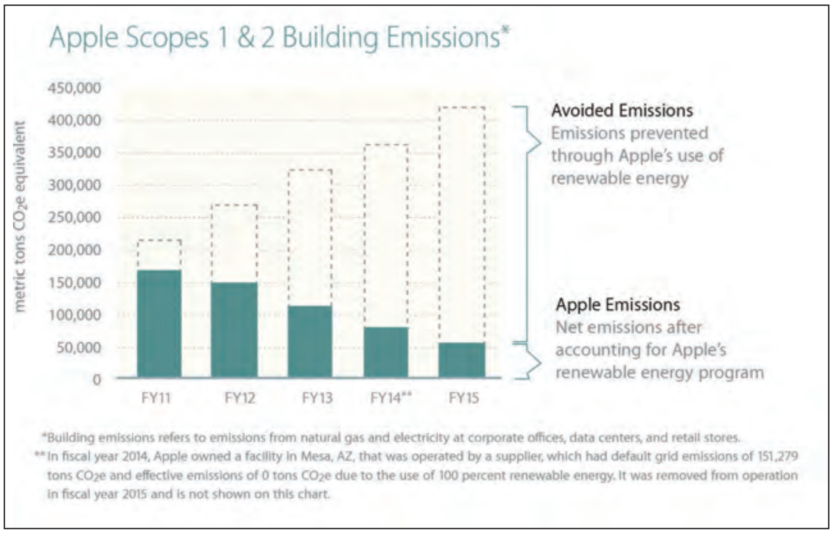
*Climate-Change Strategy.* Climate change affects companies in virtually all industries and regions, but its effects are multifaceted and highly differentiated and include opportunities as well as risks. It relates not only to a company's contribution to the release of GHG emissions into the atmosphere but also to how its capital, assets, and operations are affected by the physical effect of climate change. (See Example 1.21.)

Broadly, there are two types of climate-related risks and opportunities (Stern 2007):

- Risks (and opportunities) involved in the transition to a lower-carbon economy;
- Risks related to the physical consequences of climate change, including flooding, droughts, heat waves, landslides, erosion, reduction of lifetime of infrastructure, and effects on the supply chain, among others.

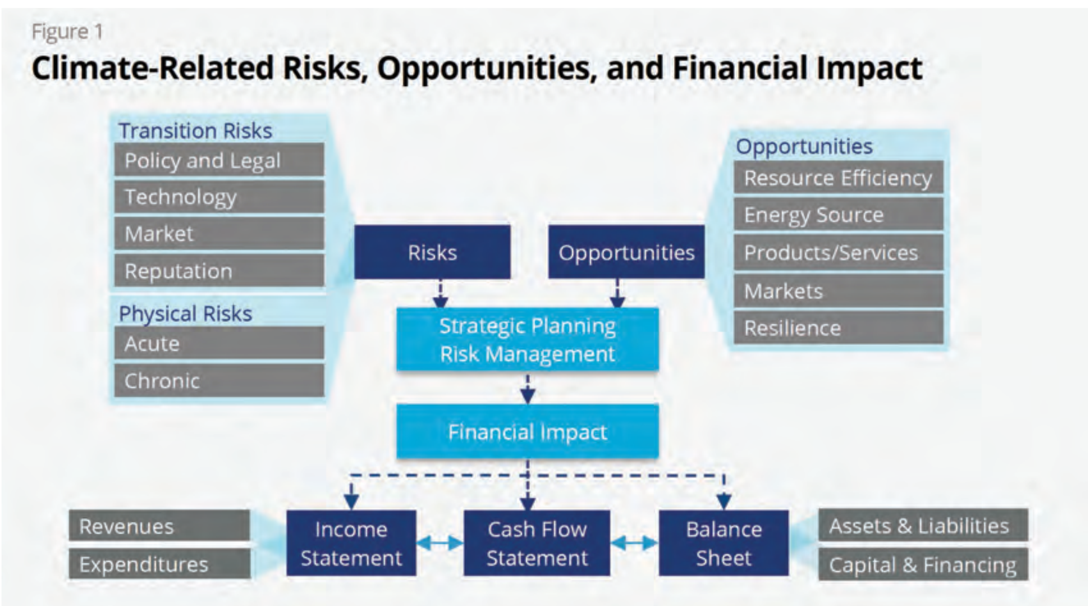
Each of these climate-related risks has several subcategories of risks. For example, the risk of transition to a lower-carbon economy comprises consumption shifts (market-segment risk) as well as policy and legal risks, such as a cap-and-trade regime for GHG emissions, carbon taxes, and tariffs imposed on companies, based on energy efficiency or GHG emissions (such as carbon taxation). (See Figure 1.2.)

**Example 1.21:** Avoided Emissions—Apple Environmental Responsibility Report 2016




Source: Apple.

**Figure 1.2:** Climate-Related Risks, Opportunities, and Financial Impact




Source: TCFD (2017).

Part I: Disclosure Framework

1. Strategy

In the strategy report, companies should address the compatibility of their business model with emerging climate regulations as well as changing consumer preferences and market expectations. For example, companies in the food industry should address climate-change vulnerabilities in the whole value chain, from crops to food processing and transportation and retail.

Companies should report on how they manage the effects of climate change on their operations and assets. This includes climate vulnerability assessments that are specific to the company's context, industry, and location. For example companies can address the elasticity of their value chain and their ability to mitigate climate risk by changing aspects of their business model, such as leasing instead of owning facilities or outsourcing transportation capabilities.

Companies should also report on how they will take advantage of climate opportunities. Guidance in this area can come from the commitments that the country made in advance of the Paris Agreement (called Intended Nationally Determined Contributions), which provide a detailed roadmap for how each country will manage its transition to a low-carbon economy and adapt to the effects of climate change.

By some estimates, the Paris Agreement opened up nearly $23 trillion in opportunities for climate-smart investments in emerging markets through 2030. An IFC study based on the national climate-change commitments and underlying policies of 21 emerging-market economies, representing 48 percent of global emissions, identifies sectors in each region where the potential for investment is greatest (IFC 2016a).

***Products and Services.*** Sustainability issues for products and services typically include consumption-related environmental and social impacts, such as product safety, energy efficiency, and pollution during use. They also include issues arising from the impact of products at the end of their useful life. Together, these issues are sometimes referred to as use-phase, life-cycle, or end-of-life impact. Examples 1.22–1.24 show Apple's reporting on product-related issues, including take-back, use-phase emissions, and chemicals in products.

Product-related sustainability issues can be ***unique to a specific industry*** because of technology, the business model, or use of resources. For example, risks and impacts concerning ***data privacy and security*** can have a major effect on companies in the technology, telecommunications, media, and retail e-commerce industries.

In certain industries, such as health care, finance, education, and insurance, the ***quality of services*** provided

**BEST-PRACTICE RESOURCES: Climate-Related Reporting**

*Climate Disclosure Standards Board Reporting Framework:* Companies making climate disclosures might consider the voluntary CDSB Reporting Framework, which is designed to elicit climate-change-related information from companies. It considers how climate-change factors affect a company's financial performance and value creation.

*The Task Force on Climate-related Financial Disclosure* (Financial Stability Board) recommends *scenario planning for climate risk*. It involves disclosing the potential effects of climate-related risks and opportunities on an organization's businesses, strategies, and financial planning under different potential future scenarios, including a 2 degree Celsius warming scenario. The Task Force suggests, over time, applying more quantitative analyses in disclosures, including the underlying assumptions of climate-related scenarios.

**Example 1.22:** Product Take-Back—Apple Environmental Responsibility Report 2016

Amount of material recovered for reuse through take-back initiatives in 2015

61,357,800 lbs

| | | | | |
|---|---|---|---|---|
| Steel 23,101,000 | Plastics 13,422,360 | Glass 11,945,680 | Aluminum 4,518,200 | Copper 2,953,360 |
| Nickel 39,672 | Lead 44,080 | Zinc 130,036 | Tin 4408 | Silver 6612 |

Source: Apple.

**Example 1.23:** Use-Phase Impact—Apple Environmental Responsibility Report 2016

Product Usage

Your energy use is our energy use.

All of the energy it takes to run your device—from the time you open the box to the day it's recycled—is added to our carbon footprint. We even include the energy it takes to charge your device, which usually comes from carbon-intensive sources such as coal or gas. So we're always developing new ways to make our products as efficient as possible. For example, the Mac operating system puts the hard drive to sleep and runs processors in an ultralow power mode when you're not hard at work. It can even save energy when the screen is static and between keystrokes when you type.

MacBook Air consumes 52 percent less energy than the original model. Mac mini consumes 40 percent less power when idle than the previous generation. Apple TV consumes 90 percent less energy than the first generation. And you can charge your iPhone 6s once a day for a year for only 53 cents.[3] In fact, since 2008 we've reduced the average total power consumed by Apple products by 64 percent, bringing down our overall carbon footprint and your electricity bill at the same time.[4]

Source: Apple.

**Example 1.24:** Chemicals in Products—Apple Environmental Responsibility Report 2016

## The worst toxins and what we've done about them.

**After we identify toxins in our products, we reduce them, remove them, or develop new materials that are safer. These efforts also remove toxins from our manufacturing and recycling processes, which protects workers and keeps pollutants out of the land, air, and water.**

**Beryllium**
Found in copper alloys used to make connectors and springs. All new products are designed without the use of beryllium.

**Mercury**
Eliminated in 2009. We use energy-efficient, mercury-free LEDs instead of mercury-based fluorescent lamps in all our displays.

**Lead**
We completely phased lead out of our display glass and solder in 2006.

**Arsenic**
Traditionally used in glass. Our display glass has been arsenic-free since 2008.

**PVC and Phthalates**
Both are still used by other companies in power cords and headphone cables. We have replaced PVC and phthalates with thermoplastic elastomers.[11]

**Brominated Flame Retardants (BFRs)**
Eliminated from thousands of parts such as enclosures, circuit boards, and connectors in 2008. We use safer metal hydroxides and phosphorus compounds in their place.

Source: Apple.

**BEST-PRACTICE RESOURCES: Human Rights Reporting**

*Human Rights Report—ABN AMRO.* In 2016, ABN AMRO was the first financial institution to publish a human rights report based on the reporting framework of the UN Guiding Principles on Business and Human Rights.

The report focuses on four categories of human rights that are most at risk of being violated by the activities of the bank and the companies it finances or invests in on behalf of clients: privacy, discrimination, labor rights, and land-related human rights.

To minimize the risk of human rights violations, ABN AMRO actively monitors clients that operate in high-risk industries and countries and, where necessary, engages with clients to bring about improvement.

can become an issue of public interest and therefore affect a company's social license to operate.

*Ethics.* Issues related to ethics usually involve corruption and bribery, political donations, taxation, and regulatory compliance. (For further guidance on reporting on a company's ethical behavior, see ***2.3. Control Environment***, page 68 of this Toolkit; and see ***Appendix E*** for a summary of the major frameworks for sustainability management and reporting.)

**BEST-PRACTICE RESOURCES: Ethics**

*2015 United Kingdom Modern Slavery Act:* Companies subject to the act must report annually the steps they have taken during the financial year to ensure that slavery and human trafficking are not taking place in their own business or in their supply chains.

### *Contribution to Sustainable Economic and Social Development*

The private sector is an important contributor to economic and social progress, especially when companies manage their environmental and social impact.

Including a company's contribution to economic and social development in the annual report can provide a balanced view of the company's overall contribution to society. It can provide context for its E&S impact and reinforce public confidence in the company and its social license to operate. Guidance for reporting in this area can be found in two related development frameworks: IFC Development Impact Framework and the UN Sustainable Development Goals.

***IFC Development Impact Framework***

The annual report can address a business's direct contribution to economic and social development by using IFC's company-level development-measurement frameworks, which include the following:

- The IFC Development Goals (see Box 1.3).
- The Development Outcome and Tracking System. DOTS measures, among other things, the economic and social return in key sectors of the economy, such as the numbers of basic services in health, education, finance, and energy as well as the number of people employed, wage payments, community outlays, and tax payments.
- The new Anticipated Impact Measurement and Monitoring framework. AIMM complements DOTS by measuring the expected or potential development impact at the outset of IFC transactions (*ex ante*) and focusing on two main dimensions: project outcomes and contribution to market creation. Project-level outcomes include the direct effects of a project (or a firm), the indirect effects on other stakeholders (including customers, suppliers, and the community), the economy overall, and the environment. (For more information on AIMM, see *Context- and Outcome-Based Reporting*, below.)

**Box 1.3:** IFC Development Goals

- Agribusiness: Increase or improve sustainable farming opportunities.
- Health and Education: Improve health and education services.
- Financial Institutions: Increase access to financial services for microfinance clients.
- Financial Institutions: Increase access to financial services for SME clients.
- Infrastructure: Increase or improve infrastructure services.
- Climate Business: Reduce greenhouse gas emissions.

***The Sustainable Development Goals***

Companies can demonstrate their contribution to sustainable development by linking company-level sustainability strategy and risk to the UN Sustainable Development Goals, a set of 17 universal goals issued by UN member states to frame their economic development and sustainability agendas between 2015 and 2030. (See Figure 1.3.)

Core environmental and social issues have a direct link with countries' efforts to meet the SDGs. For example, companies' efforts to protect biodiversity and promote sustainable management of living natural resources have a direct corollary in SDG 15, which aims to "[p]rotect, restore and promote sustainable use of terrestrial ecosystems, sustainably manage forests, combat desertification, and halt and reverse land degradation and halt biodiversity loss."

KPIs for core sustainability issues are also closely related to the SDG indicators to measure countries' progress against the Goals. For example, KPIs on

**TOOLKIT RESOURCE: ESG Metrics and SDG Indicators**

For examples of generally accepted environmental and social KPIs that have a direct correspondence with the SDGs and their indicators, see ***Table 3.3***, page 117.

**Figure 1.3:** The Sustainable Development Goals


Source: United Nations.

waste-recycling ratio is directly linked to SDG Indicator 12.5.1, which measures the national recycling rate and quantity of material recycled.

Examples 1.25 and 1.26 on the next page show how two South African companies in different sectors contribute to the economic and social development of the country. Standard Chartered, a bank, focuses on access to finance and responsible finance, and Eskom, the country's main electric utility, provides access to electricity.

Example 1.27 on page 45 shows how global pharmaceutical company Roche has been at the forefront of efforts to find a cure for cancers.

In Examples 1.28–1.30 on pages 46 and 47, Akzo Nobel, a Dutch chemical company, CEMEX, a Mexican resource transformation company, and Takeda, a Japanese pharmaceutical company, take a different approach by aligning their activities to the SDGs.

### Context- and Outcome-Based Reporting

With the rise of impact investing and the growing interest of institutional investors in the impact of their investments, companies are increasingly expected to report on their environmental and social performance in the context of the limits and carrying capacity of the resources they rely on. They are also expected to measure the environmental and social outcomes of their activities, beyond direct inputs and outputs.

#### *Context-Based Reporting*

Context-based reporting is a natural evolution from the concept of integrated reporting, where companies are expected to explain their value-creation process in terms of their use of—and impact on—multiple capitals. According to the <IR> Framework, "The overall stock of capitals is not fixed over time. There is a constant flow between and within the capitals as they are increased, decreased or transformed" (IIRC 2013). Furthering this concept, an IIRC background paper on value creation suggests that "ultimately value is to be interpreted by reference to thresholds and parameters established through stakeholder engagement and evidence about the carrying capacity and limits of resources on which stakeholders and companies rely for wellbeing and profit, as well as evidence about societal expectations" (IIRC and EY 2013).

Context-based reporting is also addressed in GRI Sustainability Reporting Guidelines, under the Principles of Sustainability Context, which states, "The underlying question of sustainability reporting is how an organization contributes, or aims to contribute in the future, to the improvement or deterioration of economic, environmental and social conditions, developments and trends at the local, regional or global level." The Guidelines further provide that the report should discuss "the performance of the organization in the context of the limits and demands placed on environmental or social resources at the sector, local, regional, or global level" (GRI 2016c).

**Example 1.25:** Contributing to Sustainable Economic Growth—Standard Chartered Sustainability Summary 2015

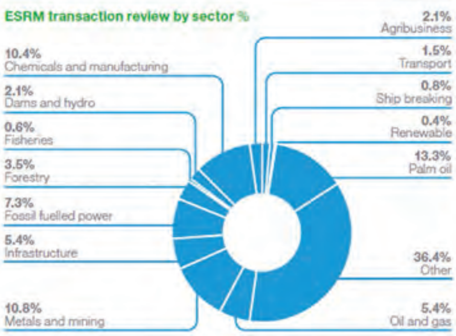
## Contributing to sustainable economic growth

**We use our core capabilities as a Bank to support sustainable economic growth. We partner with our clients to extend access to financial services and to promote responsible finance across our markets.**

Sovereign ratings advisor to
10 governments

Connected to mobile wallets* in
7 new markets, totalling 11 markets

Reviewed >480
client relationships and transactions on environmental and social risk management (ESRM)



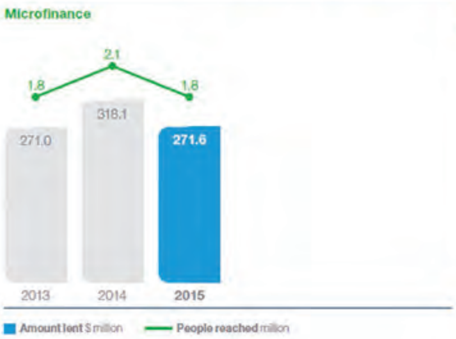

### Supporting the economy against Ebola

In response to the Ebola Virus Disease (EVD) crisis, in 2015 we partnered with CDC Group plc (CDC), the UK's development finance institution, to support and enable businesses in Sierra Leone to continue to operate.

Our agreement with CDC supported new working capital lending of up to $50 million to businesses in Sierra Leone. This enabled us to increase the number of short-term loans and overdrafts we made, thereby allowing businesses to continue to operate and expand despite slower economic growth.

Many of the companies who benefited from this agreement were able to scale up their operations to supply consumer goods such as food, building materials and hygiene products to affected areas.

CDC Chief Executive, Diana Noble, said: 'The exceptional circumstances presented by Ebola require a unique response from the international community – both in terms of humanitarian efforts and economic support. Standard Chartered is a trusted partner with an excellent network and understanding of the market in Sierra Leone. By working together in a risk-sharing deal we can support the working capital needs of businesses whose survival and growth is vital to the country's economic health'.





Source: Standard Chartered.

**Example 1.26:** Socioeconomic Contribution—Eskom Integrated Report 2016

### Maximising our socio-economic contribution

| Measure and unit | Target 2020/21 | Target 2016/17 | Target 2015/16 | Actual 2015/16 | Actual 2014/15 | Actual 2013/14 | Target met? |
|---|---|---|---|---|---|---|---|
| Corporate social investment committed, R million[1] | 953.6 | 225.3 | 98.6 | 103.6 | 115.5 | 132.9 | |
| Corporate social investment, number of beneficiaries[1] | 1 810 000 | 400 000 | 300 000 | 302 736 | 323 882 | 357 443 | |
| Total electrification connections, number[1, 2] | 1 010 000 | 160 000 | 194 374 | 158 016 | 159 853 | 201 788 | |

1. The 2020/21 targets are the cumulative figures targeted over the next five years.
2. The reporting boundary for the number of connections was changed in March 2014, to exclude farm worker connections. A total of 296 farm worker connections were also completed during the year, resulting in a total of 158 312 connections being achieved.

Source: Eskom.

**Example 1.27:** Key Achievements in Oncology—Roche Annual Report 2016

# A strong heritage

## *Progress in oncology and neuroscience*

**At the forefront of finding cures for cancer**
For more than 50 years, Roche has been at the forefront of developing medical solutions to fight cancer. In 1962, '5 FU' was synthesised, Roche's first anticancer drug inhibiting cell growth. In 1986, Roche's first biotech product Roferon-A was approved for the treatment of a previously fatal form of blood cancer.

Over the last 20 years, Roche has brought 14 new medicines to cancer patients. Long-term durable remissions and even cures are now possible in specific disease settings. For example, Herceptin has been shown to reduce the number of cases of metastatic HER2-positive breast cancer when used in the early setting,[1] and for people with an aggressive form of lymphoma, MabThera/Rituxan together with chemotherapy has been shown to cure the disease in a majority of patients.[2] However, there are more than 200 types of cancer and there is still significant progress needed to overcome the challenge of this disease.

Oncology:

Our goal is to be at the forefront of finding cures for cancer, as demonstrated by the fact that we recently launched four new cancer medicines that significantly improve patient outcomes: Tecentriq (bladder and lung cancer), Venclexta (chronic lymphocytic leukaemia), Alecensa (lung cancer) and Cotellic (skin cancer).

A major highlight in 2016 was the US launch of our first cancer immunotherapy medicine Tecentriq. Cancer immunotherapy is revolutionising the way cancer is treated, and we are proud to be among the leaders in this field. We expect important data for as many as ten investigational cancer immunotherapy molecules, either in monotherapy or combination approaches, before the end of 2017.

Gaining regulatory approval of medicines does not mean that all patients in need are able to receive these treatments immediately. Reimbursement negotiations and healthcare infrastructure can all contribute to delays numbering years before patients have access to innovative new medicines. In many cases, this can prove to be too late.

We are making many efforts to accelerate access to our medicines around the world, one example being our personalised reimbursement models. These frameworks enable more flexible pricing solutions by allowing medicines to be priced according to the benefit they deliver across different indications and combinations. This provides more flexibility when it comes to reimbursement decisions, and ensures timely access to innovative medicines for patients.

***Key achievements in oncology***

- More than 10 million cancer patients treated
- 4 new cancer medicines recently introduced
- 8 FDA breakthrough therapy designations granted for cancer medicines since 2012

Source: Roche.

### **Example 1.28:** Contribution to the Sustainable Development Goals—AkzoNobel Report 2016

**United Nations Sustainable Development Goals**

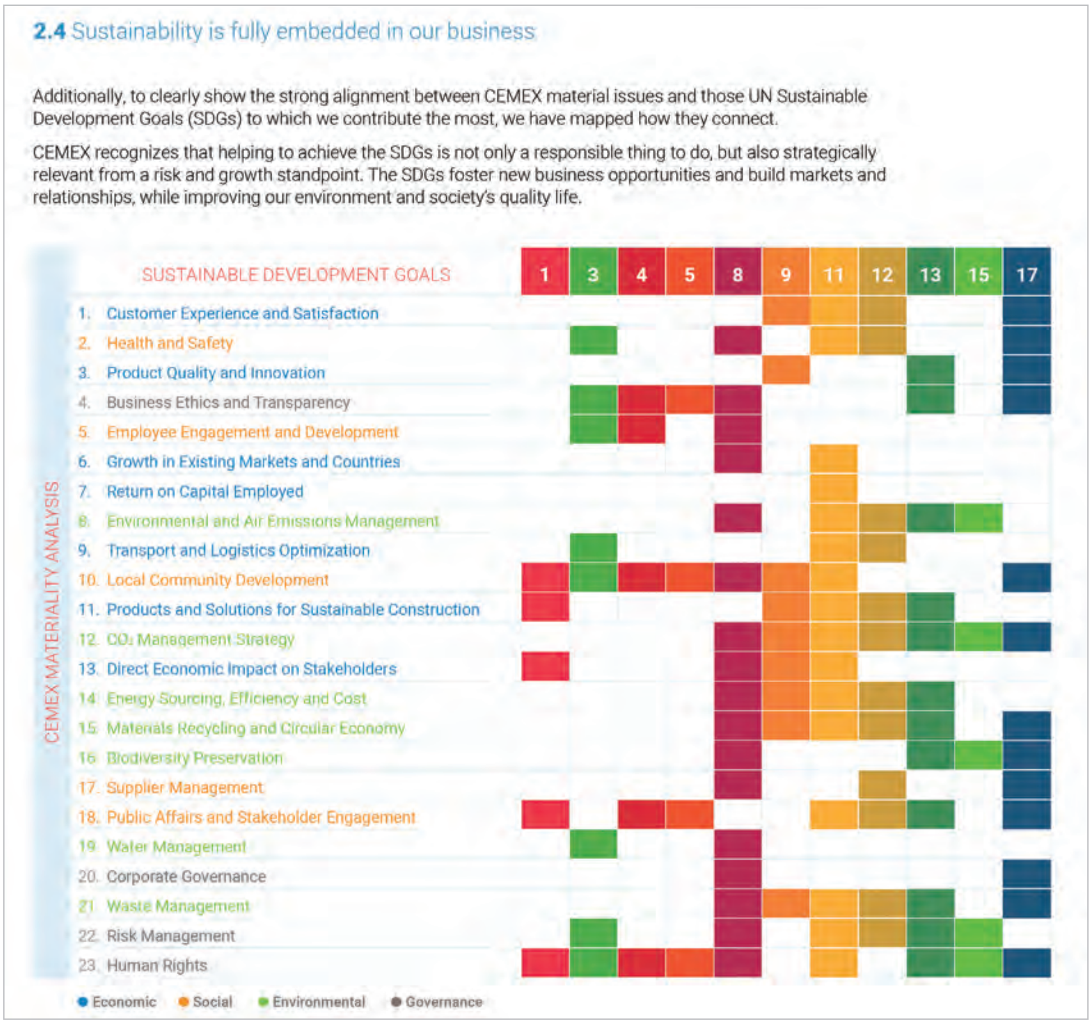
Assessment of AkzoNobel contribution

● Main ● Intermediate ● Minor

| | | Supply chain and Operations | Products | Human Cities |
|---|---|---|---|---|
| 1 | No poverty | Minor | | |
| 2 | Zero hunger | | Minor | |
| 3 | Good health and well-being | Minor | Minor | |
| 4 | Quality education | Intermediate | | Minor |
| 5 | Gender equality | Intermediate | | |
| 6 | Clean water and sanitation | Intermediate | Minor | |
| 7 | Affordable and clean energy | Main | Intermediate | |
| 8 | Decent work and economic growth | Main | | Minor |
| 9 | Industry, innovation and infrastructure | Intermediate | Main | |
| 10 | Reduced inequalities | Minor | | |
| 11 | Sustainable cities and communities | | Main | Main |
| 12 | Responsible consumption and production | Main | Main | |
| 13 | Climate action | Main | Main | |
| 14 | Life below water | Minor | Minor | |
| 15 | Life on land | Minor | Minor | |
| 16 | Peace, justice and strong institutions | Minor | | |
| 17 | Partnerships for the goals | Main | | Main |

Source: AkzoNobel.

### **Example 1.29:** Contribution to the Sustainable Development Goals—CEMEX 2017 Integrated Report




Source: CEMEX.

**Example 1.30:** Contribution to the Sustainable Development Goals—Takeda Annual Report 2016

Global Compact LEAD PARTICIPANT

**Action Mapping for SDGs**

As a UN Global Compact Lead company, we have created a Takeda Action Map for SDGs based on the SDG industry matrix, Healthcare and Life Sciences. In terms of the corporate citizenship programs, Takeda has established a mid-term strategy, "Prevention for Health in Developing and Emerging Countries" which will meet the needs of the international community.

**Good Health**

- Pharmaceutical Business (Medicines and Vaccines)
- Prevention-focused partnership programs in developing and emerging countries
  - Vaccination for Children
  - Maternal and Child Health
- Environmental Protection

**No Poverty**

- Capacity Building of Healthcare Workers for HIV/AIDS, Tuberculosis and Malaria (The Global Fund)

**Zero Hunger**

- Maternal and Newborn Health for Ethnic Minority (Save the Children Japan)

**Education**

- Diabetes e-Learning for Healthcare Professionals (Project HOPE)

**Gender**

- Community Health Workers Training for Material and Child Health (World Vision)

**Decent Work**

- Health to Female Workers In Emerging and Developing Countries (Business for Social Responsibility)

**Innovation**

- Polio Vaccine Partnership (Bill & Melinda Gates Foundation)
- Global Measles Vaccination for Children (UN Foundation)

**Equities**

- Digital Birth Registration (Plan International Japan)

**Climate Action**

- Caring for Climate (UNGC/UNEP)

**Institutions**

- The Global Health Innovative Technology Fund (The GHIT Fund)

**Other**

- Response to Natural Disasters for Resilient Society (JVOAD)
- Global Relay for Life (American Cancer Society)
- Biodiversity Conservation Initiatives (Takeda Garden for Medicinal Plant Conservation, Kyoto, Japan)

**Partnerships**

| | | | |
|---|---|---|---|
| United Nations | The Global Fund | UN Global Compact LEAD | American Cancer Society |
| Health Ministries | The GHIT Fund | Business for Social Responsibility | Plan International Japan |
| World Health Organization (WHO) | Bill & Melinda Gates Foundation | CSR Europe | Project HOPE |
| Industry Associations | UN Foundation | CSR Asia | Save the Children Japan |
| | | | World Vision |

Source: Takeda.

**BEST-PRACTICE RESOURCES: Context-Based Reporting Tools**

**Future Fit Business Benchmark**
The Benchmark identifies the extra-financial break-even point for business, expressed as a unified set of 23 social and environmental goals. Each goal is complemented by indicators designed to support effective monitoring of progress.

**MultiCapital Scorecard**
The MultiCapital Scorecard is an open-source, context-based, multicapital performance accounting framework. It uses context-based metrics to determine the thresholds or carrying capacities of the capitals, and allocations of an organization's fair share of responsibilities, to ensure sufficiency of capitals and stakeholder wellbeing.

**Reporting 3.0 Blueprints**
Reporting 3.0, a global work-ecosystem for scouting out and accelerating reporting innovations, prepared Blueprints with recommendations on the redesign for next-generation sustainable practices in the fields of 1) reporting, 2) accounting, 3) data, and 4) new business models.

***Outcome-Based Reporting***
Investors in both developed and developing markets are creating frameworks for the measurement and reporting of outcomes, including IFC's new impact measurement system.

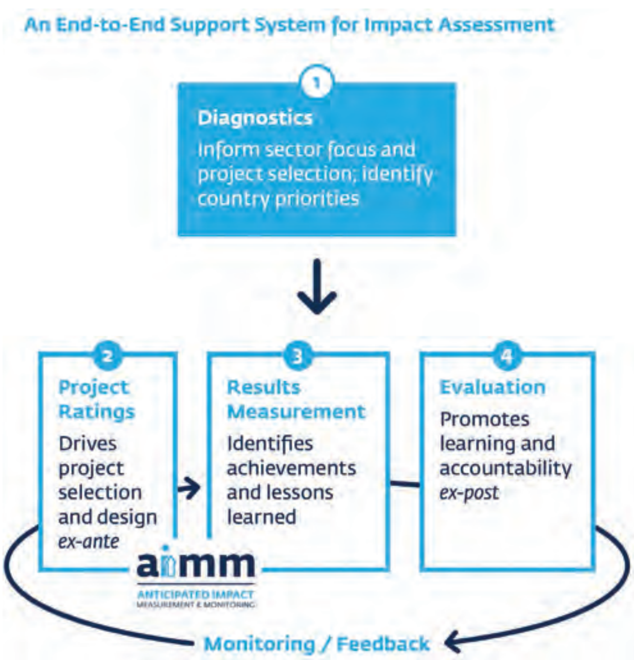
The world's development challenges are far too vast for the old ways of doing business. The need is for a new approach that unlocks the power of private sector solutions to deliver development impact. In 2017, IFC piloted a new ex ante project impact assessment tool—the Anticipated Impact Measurement and Monitoring (AIMM) system. In 2018, IFC began using the AIMM system to score all of its investment projects for developing impact.

IFC's AIMM system is designed to assess the anticipated—or ex ante—impact of IFC investment and advisory projects at two levels: what the specific project is expected to achieve (project outcomes) and how it is expected to contribute to market creation. At the project level, the AIMM framework is based on an assessment of 1) the extent of impact that the investment is anticipated to have and 2) the development gap that is addressed. (See Figure 1.4.)

In a similar trend, the World Bank is launching a Human Capital Index to rank countries on the outcomes of their investments in health, education, and social services. The index is part of a broader World Bank emphasis on human capital as a key to countries' development path toward high-income status.

**Figure 1.4:** IFC's Anticipated Impact Measurement and Monitoring Framework

The AIMM system comprises two critical pillars (project ratings and results measurement) that help connect an "end-to-end" impact-assessment system for IFC interventions. It connects 1) diagnostics to 2) ex ante project selection/scoring, which is tied to 3) results measurement during portfolio supervision and, ultimately, to 4) ex post evaluation.




Source: IFC.

**BEST-PRACTICE RESOURCES: Outcome-Based Reporting**

**Embankment Project for Inclusive Capitalism**
The project is a market-led initiative of global investors and companies seeking to create an outcome-based reporting mechanism for corporations to measure and report on value creation for a broad base of their stakeholders, including customers, employees, communities, government, and the environment. The aim is to "agree on a set of metrics that is underpinned by a methodology focused on outcomes for each significant set of stakeholders, measures the execution of a company's strategy and links it to long-term financial value for shareholders."

## 1.5. Introducing Key Performance Indicators

The Accounting Standards Board defines key performance indicators as "factors by reference to which the development, performance or position of the business of the entity can be measured effectively. They are quantified measurements that reflect the critical success factors of an entity and disclose progress towards achieving a particular objective or objectives."

The report should introduce financial and nonfinancial KPIs with links to the high-level priorities, the wider strategy, and the long-term prospects of the company. KPIs should also link to risks the company would like to mitigate and challenges to overcome.

Example 1.31 on the next page shows how Gold Fields, a South African mining company, links KPIs with a wider set of strategic objectives.

Examples 1.32 and 1.33 on pages 50 and 51 show how KPIs can be linked to the company strategy and formulated as targets that relate to the company's environmental and social commitments. (For guidance on how to use key performance indicators as part of the strategy-setting process, see ***1.2. Strategic Objectives***, page 22 of this Toolkit.)

### *Characteristics of KPIs*

KPIs should be specific enough to reflect the company strategy while enabling a credible analysis of company performance on a standalone as well as a comparative basis. Some of the key characteristics of KPIs are described below.

***Measurable.*** While qualitative goals are important, KPIs generally should be measurable, and some creativity may be needed when translating a qualitative goal into a metric.

***Comparable.*** If there are generally accepted KPIs for the industry or activity, those may be more credible for investors and other stakeholders.

***Industry-Specific.*** Industry specificity is important for setting strategic KPIs. For example, talent and innovation are important for software or pharmaceuticals; whereas acquisition of mining rights, community relations, and health and safety are important for extractive industries. Industry-specific KPIs can also be very useful for sustainability strategies. For example, companies in the animal protein market can use FCR (feed conversion ratio) to benchmark their efficiency against their peers' performance. Similarly, agricultural companies may use proxies such as productivity per hectare and water consumption per ton of produce to document their performance.

**Consistent.** Although the strategy may evolve, it is important for the KPIs to remain as consistent as possible, especially regarding the scope of the information reported, both to show trends and to maintain credibility.

**Definitions and Assumptions.** Credibility also requires that the assumptions behind the KPIs and their measurement are clear. This is especially true if they are creative, new, or have otherwise been changed. If a KPI from the financial statements is adjusted, the adjustment and its relevance must be made clear. This is also true if industry standards or other standard KPIs are adjusted.

**Incorporating Context.** Companies can improve the usefulness of KPIs for decision making by incorporating context into them. KPIs are generally formulated as absolute values. The following are some suggestions for how to add context to environmental and social KPIs:

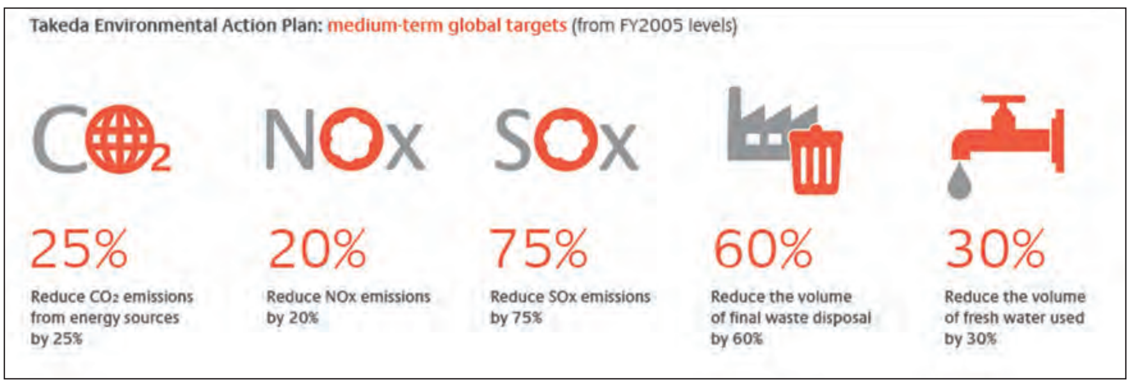
- *Efficiency:* KPIs on resources consumed (energy, materials) or released (waste/GHG emissions) can be contextualized as a ratio of financial results (revenue, profit) or operational results (number of products produced, sold).

**TIP:** Consider discussing **different time periods** relating to performance—with KPIs that apply to the different time periods. Financial KPIs are often short-term and backward-looking; nonfinancial KPIs, on the other hand, can be forward-looking, providing insight into future performance.

**Example 1.31:** Strategic Objectives and KPIs—Gold Fields 2015 Integrated Annual Report


Source: Gold Fields.

**Example 1.32:** Targets for Environmental Impact—Takeda Annual Report 2016




Source: Takeda.

**Example 1.33:** Sustainability Strategy and KPIs—Standard Chartered Sustainability Summary 2015

| Theme | Committment | Target | Timeline | Progress in 2015 | SFG |
|---|---|---|---|---|---|
| **Contributing to sustainable economic growth** | Bolster investment in power generation across Sub-Saharan Africa through Power Africa | $5 billion. Expected to add up to 7,500 megawatts of generation capacity | 2013-2018 | 3.4 gigawatts | 7, 9 |
| **Being a responsible company** | Increase women on the Board | 25% women | 2013-2017 | 23% | 5 |
| | Reduce energy use intensity | 35% in tropical locations<br>20% in temperate locations | 2008-2019 | Reduced by 22% tropical, 17% temperate locations | 7, 12 |
| | Reduce water use intensity | 71% | 2008-2019 | 44% | 6, 12 |
| | Reduce office paper use | 10 kg per full-time employee (FTE) | 2012-2020 | 17.7 kg per FTE | 13, 15 |
| **Investing in communities** | Invest in our local communities | 0.75% of prior year operating profit (PYOP) | Annual | 1.42% | 17 |
| | Raise funds to tackle avoidable blindness | $100 million | 2003-2020 | $86.3 million | 3 |
| | Empower girls through education and sport | 600,000 girls | 2006-2018 | 217,000 girls | 4, 5, 8 |
| | Educate micro and small businesses | 5,000 micro and small businesses, with 20% women-owned or led | 2013-2018 | >1,200 entrepreneurs, including 71% women | 4, 5, 8 |

Source: Standard Chartered.

- *Targets:* E&S KPIs can be presented in the context of targets (percent of completion or reduction target).
- *Peers:* Performance on E&S issues can be compared with industry peers.
- *Time:* Performance on E&S issues can be compared year-on-year and analyzed through a rate of increase.

Example 1.34 on the next page shows how Rio Tinto incorporates KPIs into its annual report.

(For more guidance on reporting on KPIs, see ***3.1. Performance Report,*** page 97 of this Toolkit. For suggested metrics for sustainability KPIs and sustainability statements, see ***3.3. Sustainability Statements,*** page 109 of this Toolkit. Also, see ***Table 3.3: Most Commonly Reported E&S Metrics***, page 117 of this Toolkit

## BEST-PRACTICE RESOURCES: Determining and Reporting KPIs

From the **Accounting Standards Board (ASB) Reporting Statement: Operating and Financial Review** (2006):

- Those KPIs judged by the directors to be effective in measuring the development, performance and position of the business of the entity shall be disclosed, together with information that will enable members to understand and evaluate each KPI.
- Comparability will be enhanced if the KPIs disclosed are accepted and widely used, either within the industry sector or more generally.

**PricewaterhouseCoopers Guide to Key Performance Indicators** (2006) provides a model for effective communication of key performance indicators, with the following criteria:

- **Link to strategy:** Enable readers to assess the strategies adopted by the company and their potential to succeed.
- **Definition and calculation:** Understand exactly what is measured. Allows comparisons between companies within an industry.
- **Purpose:** Measure progress toward achieving a specific strategic objective.
- **Source, assumptions, and limitations:** Identify the sources, assumptions, and limitations of the data.
- **Future targets:** Forward-looking orientation to assess the potential for strategies to succeed.
- **Reconciliation to GAAP:** Where the amounts measured are not “traditional” measures required by accounting standards.
- **Trend data:** How performance has improved or worsened over time. Explain what a trend in the data means.
- **Segmental:** Assess progress toward specific segmental strategic aims, in addition to groupwide measures.
- **Changes in KPIs:** KPIs may evolve over time as strategies change or more information becomes available. These changes need to be explained.
- **Benchmarking:** Comparison with peer group, with explanation of why these peers were chosen.

**Example 1.34:** KPIs—Rio Tinto 2017 Annual Report

## All injury frequency rate (AIFR)

Per 200,000 hours worked

**Relevance to strategy**
Safety is our number one priority, one of our core values and an essential component to everything we do. Our goal is zero harm, including, above all, the elimination of fatalities.

We are committed to reinforcing our strong safety culture and key to this is improving safety leadership and simplifying the tools and systems used in operational tasks.

**Performance**


Our AIFR has improved 37 per cent over the last five years. At 0.42, our AIFR decreased in 2017 versus 2016. However, we did not meet our goal of zero fatalities. In 2017, one colleague died as a result of a safety incident while working at our Rio Tinto Kennecott smelter and there was a health-related death of a colleague undertaking exploration activities. Both fatalities were at Rio Tinto managed operations.

**Definition**
AIFR is calculated based on the number of injuries per 200,000 hours worked. This includes medical treatment cases, restricted work-day and lost-day injuries for employees and contractors at Rio Tinto-managed operations.

**Associated risks**
- HSE risks, as our operations are inherently hazardous.
- Operations, projects and people risks, including management of major hazard and safety control frameworks.

**Link to executive remuneration**
AIFR and other safety metrics are included in the short-term incentive plan for executives. Refer to the Remuneration Report on page 81.

**Forward plan**
The Group will:
- Maintain critical risk management implementation.
- Strengthen collaboration with contractors and joint venture partners to improve safety performance.
- Continue to implement our major hazard standards with strong assurance processes.
- Simplify critical safety tools.

## Greenhouse gas (GHG) emissions intensity

Indexed relative to 2008 (2008 being equivalent to 100)

**Relevance to strategy**
We are committed to reducing the energy intensity of our operations and the carbon intensity of our energy, including through the development and implementation of innovative technologies. Our GHG performance is an important indicator of this commitment and our ability to manage exposure to future climate policy and legislative costs.

**Performance**


(a) Number restated from that originally published to ensure comparability over time.

There was a 2 per cent reduction in GHG emissions intensity in 2017 versus 2016. This is largely a result of improvements in emissions intensities at several of our aluminium and alumina operations.
We are on track to meet our target of 24 per cent reduction in total GHG emissions intensity between 2008 and 2020.

**Definition**
Our GHG emissions intensity measure is the change in total GHG emissions per unit of commodity production relative to a base year. Total GHG emissions are direct emissions, plus emissions from imports of electricity and steam, minus electricity and steam exports and net carbon credits purchased from or sold to recognised sources. The measure is indexed relative to 2008 (2008 being equivalent to 100).

**Associated risks**
- Strategic risks, including those related to acquistions, divestments and capital project delivery.
- Operational risks, including failure to manage portfolio energy requirements.

**Link to executive remuneration**
There is no direct connection between executive remuneration and GHG emissions intensity performance.

**Forward plan**
The Group will:
- Continue to report on progress against our GHG emissions intensity target.
- Continue to improve our understanding, management and disclosure of the resilience of our portfolio and of our physical assets to climate risks in a two degree Celsius temperature increase scenario.

Source: Rio Tinto.

# Part II: Reporting Guidance

# 2. Corporate Governance

Corporate governance can be defined as a set of structures and processes for the direction and control of companies. It involves relationships between the company's shareholders, stakeholders, board, and executive bodies for the purpose of creating long-term shareholder and stakeholder value.

Reporting on these structures and processes is critical if investors and others are to understand how companies are governed and managed, how the board and management monitor and control risks and ensure compliance with ethical conduct, how they treat minority shareholders and avoid conflicts, and how they manage relationships with a broader group of stakeholders.

**Model Structure of Annual Report**

**1. Strategy**
- Business Model and Environment
- Strategic Objectives
- Risk Analysis and Response
- Sustainability Opportunities and Risks
- Introducing Key Performance Indicators

**2. Corporate Governance**
- Leadership and Culture: Commitment to ESG
- Structure and Functioning of the Board of Directors
- Control Environment
- Treatment of Minority Shareholders
- Governance of Stakeholder Engagement

**3. Financial Position and Performance**
- Performance Report
- Financial Statements
- Sustainability Statements

## 2.1. Leadership and Culture: Commitment to ESG

The *governance* section of the report should include a description of the organization's leadership and culture as well as its commitment to sound corporate governance and the management of environmental and social issues. This includes an account of how this commitment is translated into policies and codes that address, at a minimum, the role of the board, shareholder rights, and compliance with all laws and regulations, including environmental and social regulations. It should also describe how compliance with internal policies and codes is monitored, including internal controls and audit.

Without strong corporate governance, extra-financial issues, such as environmental and social opportunities and risks, would lack a decision chain that assures accountability and sound management across the company. Therefore, it is recommended that the implementation of environmental and social management systems be placed within strong corporate governance mechanisms, including a designated corporate governance officer or corporate secretary.

## CONSULT THE MATRIX

The Matrix can be used to gauge a company's level of progress with leadership and culture and its commitment to environmental, social, and governance issues. The Toolkit recommends the disclosure of information related to Levels 1–3 of the Matrix, which corresponds to good international practices. Guidance is also provided for disclosure of leadership practices, consistent with Level 4 of the Matrix. (See Table 2.1.)

### 2.1.1. ESG Codes and Policies

The report should describe the company's policies or codes regarding corporate governance, environmental and social issues, and ethics. It should indicate whether such codes address the following:

- Rights and treatment of shareholders and other stakeholders;
- Role of the board;
- Disclosure and transparency;
- Objectives and principles of the institution;
- Compliance with E&S laws and regulations;
- Governance of stakeholder engagement;
- Integration of ESG practices in business activities and strategy;
- Code of conduct in the supply chain.

The report should describe the approval process for the code of ethics or conduct, including board approval. Intermediate practices (Matrix Level 2) suggest that a company have a designated fulltime corporate governance officer or company secretary to support its commitment to corporate governance and sustainability. In good international practices (Matrix Level 3), the report should indicate whether the company code of ethics or conduct integrates ESG practices into business activities.

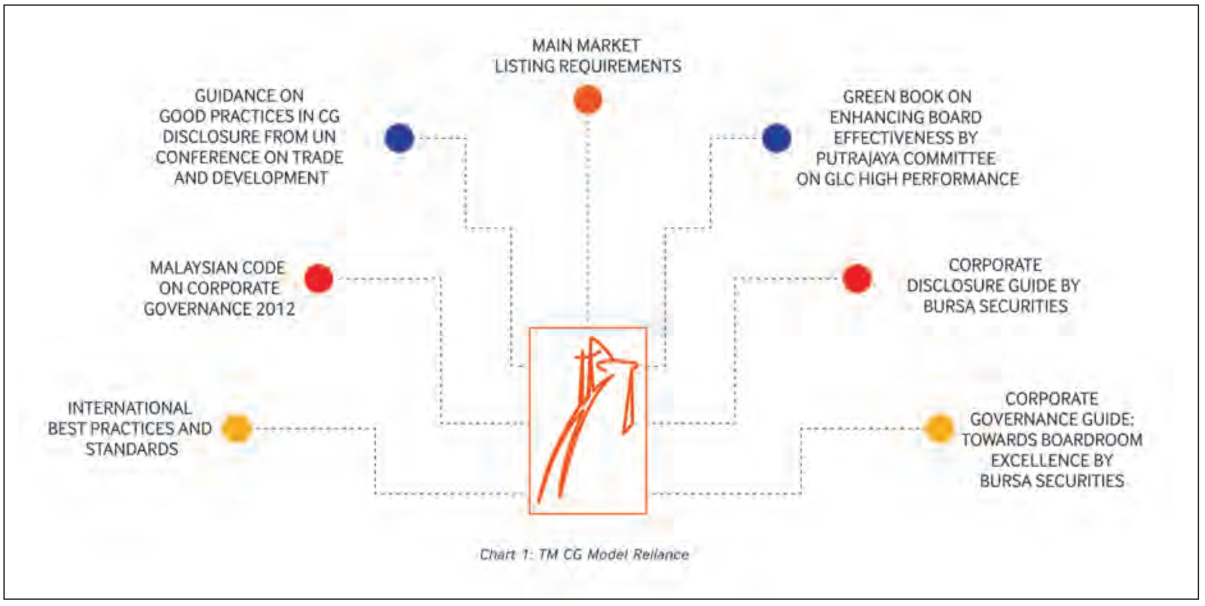
The report should also address whether the company's policies and codes conform to the voluntary provisions of the country's code of best corporate governance practices (when one exists). (See Example 2.1.)

**BEST-PRACTICE RESOURCES: Corporate Culture**

*From Companies to Markets—Global Developments in Corporate Governance*, an IFC publication on global developments in corporate governance, highlights the emerging importance of corporate culture and the role of boards in promoting it throughout the organization.

*Culture by Committee—The Pros and Cons* is a survey report from the Institute of Business Ethics on the role of board committees of U.K. companies in delivering corporate responsibility and embedding values.

**Example 2.1:** Corporate Governance Model—Telekom Malaysia Annual Report 2015




Source: Telekom Malaysia.

**Table 2.1:** IFC Corporate Governance Matrix—Commitment to Environmental, Social, and Governance (Leadership and Culture)

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Formalities** | 1. Written policies/corporate governance (CG) code addressing, at a minimum, the role of the board, rights and treatment of shareholders and other stakeholders, compliance with the law and transparency and disclosure, and stating the objectives and principles guiding the company.<br>2. Written policies that address, at a minimum, compliance with E&S law and regulations. | 1. CG code, which addresses E&S issues.<br>2. Periodic disclosure to shareholders on CG code and practices, and their conformance to the country's code of best practices. | | 1. Adequacy of ESG policies and procedures is disclosed. |
| **Code of Ethics and Culture** | 3. Code of ethics and/or conduct approved by the board. | 3. Code of ethics included in employee orientation program. | 1. Codes of ethics and/or conduct fully integrate ESG practices in business activities. | 2. Organization culture has embedded ESG awareness and a control consciousness throughout the organization. |
| **Designated Officer/ Functions** | 4. A company officer serves as a corporate secretary. | 4. Designated fulltime CG officer and/ or company/corporate secretary. | 2. Designated compliance function ensuring compliance with ESG policies and procedures, code of ethics and/or conduct.<br>3. Internal audit of implementation of ESG policies and procedures. | |
| **Recognition** | | 5. Publicly recognized as a national leader in ESG practices. | 4. Publicly recognized as a regional leader in ESG practices. | 3. Publicly recognized as a global leader in ESG practices. |

### 2.1.2. Compliance with ESG Codes and Policies

The report should describe the management and governance mechanisms that are in place to ensure that the company complies with its policies or code of ethics and/or conduct, including the following:

- Designated compliance function—including fulltime corporate governance officer or corporate secretary—to ensure compliance with ESG policies and codes;
- Internal audit;
- External verification;

Good international practices (Matrix Level 3), suggest that the report also describe the internal control processes function (compliance, internal audit) to ensure implementation of ESG policies and procedures.

Example 2.2 illustrates how Türk Telekom rates its own compliance with its corporate governance principles.

## 2.2. Structure and Functioning of the Board of Directors

The board of directors is a central function of corporate governance and of the company's organizational structure. The board is appointed by shareholders to oversee the strategy, management, and performance of the company. Its primary duty is to select and oversee the chief executive officer, to monitor management's performance, and to ensure legal and ethical conduct. The board meets regularly to conduct its general duties and to carry out more specific duties through specialized committees, including on nomination, audit, remuneration, governance, and sustainability.

**Example 2.2:** Corporate Governance Rating—Türk Telekom Annual Report 2015

Corporate Governance Rating was determined as a result of the examination made under four major topics (Shareholders, Public Disclosure and Transparency, Stakeholders, Board of Directors) weighted differently within the framework of the CMB's Corporate Governance principles. Breakdown of our corporate governance rating under major categories is as follows:

| Sub Categories | Weight (%) | Rating |
|---|---|---|
| Shareholder | 25 | 8.45 |
| Public Disclosure & Transparency | 25 | 9.66 |
| Stakeholders | 15 | 8.68 |
| Board of Directors | 35 | 8.79 |
| **Total** | **100** | **8.91** |

Source: Türk Telekom.

It is critical to have a balanced board membership that ensures both operational performance and quarterly results. Also critical is a long-term strategic vision to integrate sustainability into the value proposition of the company.

The board is also responsible for managing agency problems that typically arise in companies between management and shareholders, between majority shareholders and minority shareholders, and between the company and its stakeholders. Therefore, one key aspect of the board structure and functioning is independence, which is typically ensured by the presence of directors that are neither executives nor major shareholders of the company.

Further, to balance power and to bolster the independent leadership of the board, good international practice (Matrix Level 3) recommends that the CEO and chair roles be separate and that the board be led by an independent non-executive director.

**DEFINITION: Board Structures**

In jurisdictions where companies have a **dual board structure**, the board of directors (or the board) is referred to as the **supervisory board**, as distinct from the **executive board** or **management board.** This section addresses only the structure and functioning of the board of directors or supervisory board.

### CONSULT THE MATRIX

The report should address key aspects of board structure and functioning:

- Board qualifications and appointment, including diversity and ESG qualifications;
- Board independence and the role of independent directors in accountability, oversight of the management, and management of conflicts;
- The work of boards, including committees, evaluation, and the company secretary;
- The role of the board in overseeing environmental and social issues.

The Matrix can be used to gauge a company's level of progress with board structure and functioning. The Toolkit recommends the disclosure of information related to Levels 1–3 of the Matrix, which corresponds to good international practices. Guidance is also provided for disclosure of leadership practices, consistent with Level 4 of the Matrix. (See Table 2.2.)

**Table 2.2:** IFC Corporate Governance Matrix—Structure and Functioning of the Board of Directors

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Role, Election, and Succession** | **1.** Board approves strategy.<br>**2.** Board members are given sufficient time and information to exercise their duty. | **1.** The board is fully elected on an annual basis. | **1.** Board-established succession plan for its members and senior management. | |
| **Composition** | **3.** The board has a number of independent directors in accordance with law and regulations. | **2.** 1/5 or more of board members are independent from management and controlling shareholders.<br>**3.** Board composition is based on a skills matrix. | **2.** 1/3 or more of board members are defined as independent in accordance with international best practices.[a]<br>**3.** Board diversity, including but not limited to gender, achieved in all aspects.<br>**4.** Roles of chair and CEO are separate. Board chair is independent, or a lead independent director has been designated. | **1.** 1/2 or more of board members are defined as independent in accordance with international best practices. |
| **Committees** | | **4.** Board-established audit committee. | **5.** Majority of audit committee membership is independent.<br>**6.** Specialized committees address special technical topics or potential conflicts of interest (e.g., nominations, compensation, technology/ cybersecurity, E&S/sustainability, risk management, etc.), if applicable.<br>**7.** Committee of independent directors approves all material related- party transactions. | **2.** Audit committee membership 100% independent.<br>**3.** Special board-level CG committee established.<br>**4.** Specialized committees (governance, nominations, E&S/ sustainability, and compensation) composed of a majority of independent directors, including the chair.<br>**5.** Compensation committee ensures that executive compensation is based on performance and long-term incentives (and adjusted for all types of current and future risk), based on financial and nonfinancial performance.<br>**6.** Risk management or other specialized committee with a majority of independent directors, and a majority who have experience managing risks. |
| **Meeting Frequency** | **4.** Board meets at least quarterly and is charged with objectively overseeing management. | | **8.** Non-executive directors meet separately at least once a year. | **7.** Independent directors periodically meet separately. |

*(continued on next page)*

**Table 2.2:** IFC Corporate Governance Matrix—Structure and Functioning of the Board of Directors (*continued from previous page*)

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Evaluation and Performance** | | **5.** The board as a whole undergoes periodic evaluation.<br>**6.** Formal performance evaluation of management conducted annually. | **9.** Board, committees and individual directors undergo an annual evaluation. | **8.** Board and committee evaluations conducted/facilitated by third party. |
| **Oversight of E&S** | | **7.** Board is trained on general E&S risk issues. | **10.** Board is trained on industry E&S risk issues.<br>**11.** Strategy and risk appetite integrate E&S issues/risks.<br>**12.** At least 1 director has experience analyzing and interpreting E&S risks.<br>**13.** In sensitive industries,[b] 1 director or more has in-depth knowledge of E&S risks.<br>**14.** ESG issues are recurring board agenda items; board approves ESG strategy and E&S policies; routinely reviews E&S performance; ensures appropriate dialogue between the company and key stakeholders; and ensures effectiveness of External Communications Mechanism (ECM).<br>**15.** Board ensures that management systems are in place to identify and manage E&S risks and impacts. | **9.** Special board-level committee established to review E&S issues.<br>**10.** Board reviews independent audits on effectiveness of Environment and Social Management System (ESMS), including stakeholder engagement processes and grievance mechanism. |

[a] For example, IFC's "Indicative Independent Director Definition."

[b] Examples of "sensitive industries" include oil, gas, mining, heavy industry (steel, cement), and chemical manufacturers, and large agro-commodity production or processing.

### 2.2.1. Board Qualifications and Independence

The report should describe the criteria used to select members of the board, including the requirements for independent directors.

#### *Nomination and Appointment*

The report should describe the process of nominating and appointing directors. It should also summarize the roles of the board, the nomination committee (if any), and shareholders in nominating and appointing board members. (See Example 2.3.)

### **Example 2.3:** Board Nomination Procedure—Siam Commercial Bank Annual Report 2016

**5.9 Procedure for Nomination of Directors and Senior Executives**

The Nomination, Compensation and Corporate Governance Committee is responsible for screening and proposing to the Board qualified candidates that meet the Bank's strategies to serve as directors and members of Board committees based on each candidate's knowledge, capabilities, expertise, and the experience required for any vacancy, by using a board skill matrix as a tool, as well as, in the case of independent directors, their independence. With regard to the directors representing major shareholders, in principle, the major shareholders nominate individuals to be elected as the Bank's directors and the Board is in charge of verifying that the qualifications of such individuals nominated are not contrary to relevant laws and conform to the Bank's policies governing directors' holding of position in other companies. The Nomination, Compensation and Corporate Governance Committee selects candidates for directorship from the director pool of the Thai Institute of Directors Association (IOD) and the proposals submitted by the directors and the shareholders of the Bank. After a scrutiny of each candidate's qualifications to ensure compliance with laws and regulations, the Nomination, Compensation and Corporate Governance Committee will propose the nomination to the Board for consideration. Following the Board's endorsement of the nominated candidates, the Bank will consult with and seek endorsement from the Bank of Thailand prior to proposing the nomination to the shareholders, if applicable, for approval of the appointment.

Source: Siam Commercial Bank.

The report should explain how shareholders can nominate or appoint board members—and whether there is a difference in the process for major shareholders and small or minority shareholders. Where companies have employee representatives, creditor representatives, or government representatives on their boards, the report should identify these representatives and state how they are appointed. (See Example 2.4.)

For all board members, the report should clearly indicate when they came onto the board and when their terms will end. Board members who have been reappointed for multiple terms may not always be considered independent. In Example 2.5 on the next page, BHP Billiton, an Anglo-Australian mining company, provides justification for board members who have served for extensive periods.

Regardless of how a director is nominated, all directors have a responsibility to act in the best interests of the company.

### **Example 2.4:** Nominating Process—The Coca-Cola Company 2016 Proxy Statement

**2015 DIRECTOR NOMINEES**

Our By-Laws provide that the number of Directors shall be determined by the Board, which has set the number at 15. Upon the recommendation of the Committee on Directors and Corporate Governance, the Board has nominated each of Herbert A. Allen, Ronald W. Allen, Marc Bolland, Ana Botín, Howard G. Buffett, Richard M. Daley, Barry Diller, Helene D. Gayle, Evan G. Greenberg, Alexis M. Herman, Muhtar Kent, Robert A. Kotick, Maria Elena Lagomasino, Sam Nunn and David B. Weinberg for election as a Director. All of the nominees are independent under New York Stock Exchange ("NYSE") corporate governance rules, except Herbert A. Allen and Muhtar Kent. See "Director Independence and Related Person Transactions" beginning on page 38.

Each of the Director nominees currently serves on the Board and was elected by the shareowners at the 2015 Annual Meeting of Shareowners. If elected, each Director will hold office until the 2017 Annual Meeting of Shareowners and until his or her successor is elected and qualified. We have no reason to believe that any of the nominees will be unable or unwilling to serve if elected.

Source: The Coca-Cola Company.

**Example 2.5:** Director Tenure—BHP Billiton Annual Report 2016

**TENURE**

As at the end of the year under review, two Directors, Jac Nasser and John Schubert, had each served on the Board for more than nine years. Jac Nasser is standing for re-election at the 2016 AGMs, having undergone a formal performance assessment.

Mr Nasser was first appointed to the Board in June 2006 as an independent Non-executive Director. The Board believes his expertise and broad international experience materially enhance the skills and experience profile of the Board. In accordance with the UK Corporate Governance Code, Mr Nasser's term of appointment has been subject to a particularly rigorous review which took into account the need for progressive refreshing of the Board.

The Board does not believe Mr Nasser's tenure materially interferes with his ability to act in the best interests of the Company. The Board believes he has retained independence of character and judgement and has not formed associations with management (or others) that might compromise his ability to exercise independent judgement or act in the best interests of the Company.

Source: BHP Billiton.

### *Qualifications*

The report should concisely present the relevant work experience, education, and other board positions currently held by each board member. It should emphasize elements of the board members' backgrounds that are particularly relevant in their board roles, including for any committees they serve on.

The report should link board members' qualifications to the skills needed for the board to carry out its function, such as legal, financial, market, and risk skills. It should also link to the wider strategy and purpose of the company. This can be done for the board as a whole, and **BEST PRACTICE** suggests that it also can be done for each board member. It may be presented as a matrix of current board members' skills and experience against key functions of the board.

The report should also describe professional development and training for board members, both as part of the onboarding process and on an ongoing basis.

**BEST PRACTICE** (and the concept of the "strategic-asset board") suggests that companies have in place a longer-term board succession plan that ensures that the composition and qualifications of the board are aligned with the company's strategy and the required qualifications of directors.

**Sustainability expertise:** Good international practices (Matrix Level 3) suggest that the board have oversight of environmental and social matters as part of the regular agenda of board meetings, and that it should approve E&S policies and strategy and routinely review performance. The board should also oversee the dialogue with key stakeholders and ensure effective communication. This means that the board must have the expertise required to evaluate E&S management systems and understand ESG risks.

The report should describe the board's expertise on sustainability matters and whether board members receive training on ESG issues generally as well as for the industry sector. Intermediate practices (Matrix Level 2) suggest that the board be trained on general E&S risk issues. In industries that are more prone to E&S risks (such as oil, gas, mining, heavy industry, chemical manufacturers, and large agro-commodity production or processing), good international practices suggest that at least one board director have an in-depth knowledge of E&S risks.

Example 2.6 shows a detailed summary of the qualifications and experience of board members of Prudential, a U.S. insurance company, and how they align with the core skills for the board of directors, including expertise on ESG issues.

### *Independence*

The report should clearly define the different types of directors and levels of independence regarding board membership. It should identify the following:

- *Executive board members:* board members who have fulltime (usually C-level) positions;
- *Non-independent non-executive board members:* board members who do not work fulltime for the company but have some other significant link to it, typically through ownership or family relationships to board members, major shareholders or senior management, or company suppliers or customers;

**BEST-PRACTICE RESOURCES: Building a Strategic-Asset Board**

*The NACD (National Association of Corporate Directors) Blue Ribbon Commission on Building the Strategic-Asset Board* provides guidance on a continuous-improvement plan to maximize a board's skill sets and ensure that it is aligned with the organization's current and future needs.

**Example 2.6:** Director Qualifications—Prudential Proxy Statement 2016

**Summary of Director Qualifications and Experience**

| | Baltimore, Thomas J., Jr. | Casellas, Gilbert F. | Cullen, James G. | Grier, Mark B. | Hund-Mejean, Martina | Krapek, Karl J. | Lighte, Peter C. | Paz, George | Pianalto, Sandra | Poon, Christine A. | Scovanner, Douglas A. | Strangfeld, John R. | Todman, Michael A. |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **ACADEMIA/EDUCATION** experience is important because it brings perspective regarding organizational management and academic research relevant to our business and strategy. | | | | | | | • | | • | • | | | |
| **BUSINESS ETHICS** experience is important given the critical role that ethics plays in the success of our businesses. | | • | | • | | | | | | | | • | |
| **BUSINESS HEAD/ADMINISTRATION** experience is important since directors with administration experience typically possess strong leadership qualities and the ability to identify and develop those qualities in others. | • | • | • | • | • | • | • | • | • | • | • | • | • |
| **BUSINESS OPERATIONS** experience gives directors a practical understanding of developing, implementing and assessing our operating plan and business strategy. | • | • | • | • | • | • | • | • | • | • | • | • | • |
| **CORPORATE GOVERNANCE** experience supports our goals of strong Board and management accountability, transparency and protection of shareholder interests. | • | • | • | • | • | • | • | • | • | • | • | • | • |
| **ENVIRONMENTAL/SUSTAINABILITY/CORPORATE RESPONSIBILITY** experience strengthens the Board's oversight and assures that strategic business imperatives and long-term value creation for shareholders are achieved within a responsible, sustainable business model. | | • | | • | | • | | | | | | • | |
| **FINANCE/CAPITAL ALLOCATION** experience is important in evaluating our financial statements and capital structure. | | | | • | • | • | • | • | • | | • | • | • |
| **FINANCIAL EXPERTISE/LITERACY** is important because it assists our directors in understanding and overseeing our financial reporting and internal controls. | • | • | • | • | • | • | • | • | • | • | • | • | • |
| **FINANCIAL SERVICES INDUSTRY** experience is important in understanding and reviewing our business and strategy. | | | | • | • | | • | • | • | | • | • | |
| **GOVERNMENT/PUBLIC POLICY** experience is relevant to the Company as it operates in a heavily regulated industry that is directly affected by governmental actions. | | • | | • | | | • | • | • | | | | • |
| **INSURANCE INDUSTRY** experience is important in understanding and reviewing our business and strategy. | | | | • | | | | • | | | | • | |
| **INTERNATIONAL** experience is important in understanding and reviewing our business and strategy. | | | • | • | • | • | • | | | • | | • | • |
| **INVESTMENTS** experience is important in evaluating our financial statements and investment strategy. | • | • | | | • | | • | | | | • | • | |
| **MARKETING/SALES** experience is relevant to the Company as it seeks to identify and develop new markets for its financial products and services. | | | • | | | | | | | • | | | • |
| **REAL ESTATE** experience is important in understanding and reviewing our business and strategy. | • | | | | | • | | | | | • | | |
| **RISK MANAGEMENT** experience is critical to the Board's role in overseeing the risks facing the Company. | | • | | • | • | • | • | • | • | | • | • | • |
| **TALENT MANAGEMENT** experience is valuable in helping us attract, motivate and retain top candidates for positions at the Company. | • | • | • | • | • | • | • | • | • | • | • | • | • |
| **TECHNOLOGY/SYSTEMS** experience is relevant to the Company as it looks for ways to enhance the customer experience and internal operations. | | | | • | | • | | | | | | • | |

Source: Prudential.

- *Independent non-executive board members:* board members who are not major shareholders and do not otherwise work for the company or have relationships or business links, formal or informal, that enable significant influence on company decisions—and therefore are independent of management and controlling or major shareholders.

It is considered good practice (Matrix Level 3) for companies to have a board composed of at least one-third independent directors, and companies are encouraged to move toward having a majority of the board be independent directors. At a minimum, the board must have a level of independent directors that is in accordance with local laws, regulations, or codes.

Good international practice (Matrix Level 3) recommends that independent directors meet separately from other board members at least once a year.

Example 2.7 on the next page provides a breakdown of independent and non-independent directors for Fresnillo, a Mexican mining company.

The report should clearly present the links between the company and non-independent board members, briefly noting why an independent member is considered to be so. Sometimes more justification may be necessary

**Example 2.7:** Board Composition and Independence—Fresnillo 2015 Annual Report

**BOARD COMPOSITION AND INDEPENDENCE**

The Board is comprised of six Non-executive Directors who are considered to be independent and six Non-executive Directors who are considered to be non-independent, as shown in the diagram below.

| NON-INDEPENDENT | INDEPENDENT |
|---|---|
| Alberto Baillères (Chairman and Chairman of Nominations Committee) | Guy Wilson (Senior Independent Director and Chair of Audit Committee) |
| Alejandro Baillères | María Asunción Aramburuzabala |
| Juan Bordes | Bárbara Garza Lagüera |
| Arturo Fernández | Charles Jacobs (Chair of Remuneration Committee) |
| Rafael MacGregor (Chair of HSECR Committee) | Fernando Ruiz |
| Jaime Lomelín | Jaime Serra |

Source: Fresnillo Plc.

in situations where independence seems compromised. For example, a board member may have some link to a supplier or customer of the company, may have been a board member for nine or more years, may have a relative employed by the company, or may have done some part-time work for the company. The board may still determine that the member is independent, as long as a substantive explanation is given and it is consistent with local requirements or international best practice.

In Example 2.8, BHP Billiton explains why a board member, whose independence could be questioned because of a prior role with one of the company's auditors, is acceptable as an independent director.

### *Diversity*

Boards are increasingly expected to achieve better gender balance and draw from a wider pool of potential candidates. Beyond gender, this can include candidates of different ages, ethnicities, and other differences in background, including relevant experience or exper-

**Example 2.8:** Explanation of Director Independence—BHP Billiton Annual Report 2016

**RELATIONSHIPS AND ASSOCIATIONS**

Lindsay Maxsted was the CEO of KPMG in Australia from 2001 until 2007. The Board believes this prior relationship with KPMG does not materially interfere with Mr Maxsted's exercise of objective, unfettered or independent judgement, or his ability to act in the best interests of BHP Billiton. The Board has determined, consistent with its policy on the independence of Directors, that Mr Maxsted is independent. The Board notes in particular that:

- at the time of his appointment to the Board, more than three years had elapsed since Mr Maxsted's retirement from KPMG. The Director independence rules and guidelines that apply to the Company—which are a combination of Australian, UK and US rules and guidelines- all use three years as the benchmark 'cooling off' period for former audit firm partners;
- Mr Maxsted has no financial (e.g. pension, retainer or advisory fee) or consulting arrangements with KPMG;
- Mr Maxsted was not part of the KPMG audit practice after 1980, and while at KPMG was not in any way involved in, or able to influence, any audit activity associated with BHP Billiton. The Board believes Mr Maxsted's financial acumen and extensive experience in the corporate restructuring field to be important in the discharge of the Board's responsibilities. His membership of the Board and Chairmanship of the Risk and Audit Committee are considered by the Board to be appropriate and desirable.

Source: BHP Billiton.

**BEST-PRACTICE RESOURCES: Independent Directors**

*The International Corporate Governance Network (ICGN) Global Governance Principles:* "The board of directors should identify in the annual report the names of the directors considered by the board to be independent and who are able to exercise independent judgment free from any external influence. The board should state its reasons if it determines that a director is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination. . . ."

tise. Good international practice (Matrix Level 3) recommends that board diversity, including but not limited to gender, be achieved in all respects.

The report should explain how diversity was considered in recent board nominations and any policy of the board in this area. In Example 2.9, Natura, a Brazilian cosmetics company, illustrates the composition of its board in terms of gender, age, and number of terms served.

### 2.2.2. Board Work and Committees

The report should describe the board's work, its committee structure, and its relationships within and outside the company.

***Roles and Responsibilities***

The report should describe the main activities and responsibilities of the board, focusing on major responsibilities and decisions. It should also include a link to where committee charters are disclosed on the company's website. The report should explain how the board serves classic functions: providing guidance to and monitoring the performance of senior management for the benefit of all shareholders. It should also indicate the frequency of board meetings. The board should meet regularly, and its members should be given sufficient time and information to exercise their duties.

***The Board and the Management Team***

The report should describe the division of responsibilities between the board and senior management, including whether executives are also members of the board. If executives on the board routinely attend board meetings, the report should indicate whether the board holds "executive sessions" without the presence of management.

The report also should address the role of the board in relation to management. Specifically, it should describe the role of the board in the following areas:

- Setting strategy and vision of the company;
- Selection of the chief executive officer and senior management;

**BEST-PRACTICE RESOURCES: Board Diversity**

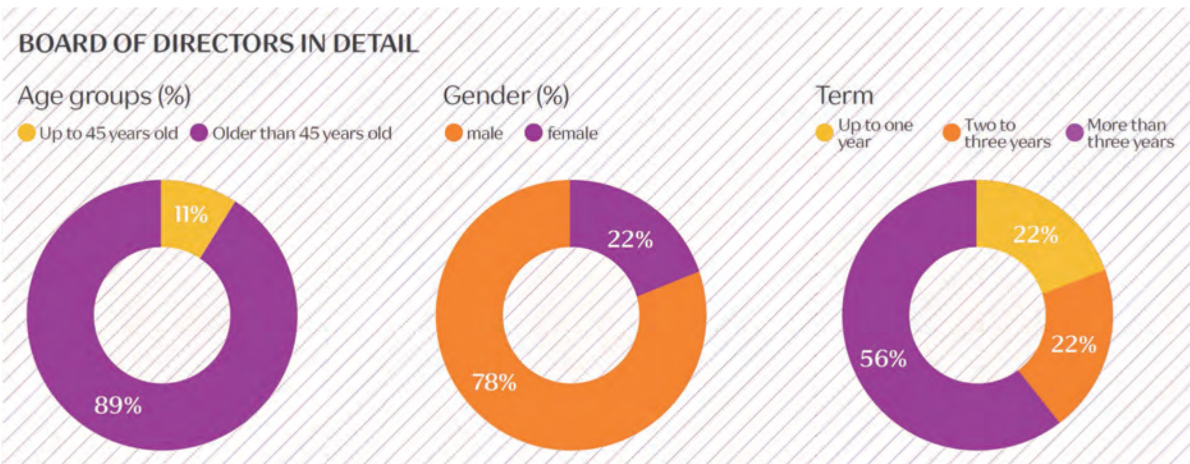
*The G20/OECD Principles* call for disclosure of the following:

- Board member qualifications, their board (and other) positions;
- Board member independence—and why it matters;
- Board selection process.

*The <IR> Framework* calls for board skills and diversity, including a range of backgrounds and gender.

*The King IV Report on Corporate Governance for South Africa, 2016,* Principle 7: The governing body should comprise the appropriate balance of knowledge, skills, experience, diversity, and independence for it to discharge its governance role and responsibilities objectively and effectively.

**Example 2.9:** Board Diversity—Natura 2016 Annual Report




Source: Natura.

- Risk management;
- Oversight of internal controls, internal and external audit, and preparation of financial statements;
- Authorization of major capital expenditures, large-value transactions, and conflicted transactions, such as related-party transactions;
- Oversight of human resources policy.

The report should indicate whether there are decisions that the board reserves only to itself.

Example 2.10 describes the roles of management and the board of Aggreko, a U.K. energy company, focusing on the main officers and directors.

### Board Committees

The board should establish specialized committees of board members to support specific board activities or areas where conflicts of interests may arise. Good international practice (Matrix Level 3) also recommends having specialized committees of the board with responsibility for addressing technical topics or potential conflicts of interest (such as nomination, compensation, technology, cybersecurity, E&S/sustainability, risk management, and so on), if applicable. Leadership practices (Matrix Level 4) suggest that a majority of members of all committees be independent directors, and that each committee have an independent chair.

The report should describe the following:

- The types of committees—audit, risk, finance, nomination, remuneration, corporate governance, sustainability, and risk management;
- Committees' roles (including communication with the board);
- Committees' composition (including independence and qualifications) and a website link to the committees' charters.

The report also should include a review of each committee's work, highlighting important areas the committee addressed as well as any changes in the focus or policy of a particular committee.

In good practice (Matrix Level 3), the audit committee should be composed of a majority of independent directors. **LEADERSHIP PRACTICES** (Matrix Level 4) suggest 100 percent independence. Leadership practices also suggest that companies have a risk committee with a majority of members experienced in managing risk. (For further guidance on the role and deliberations of the audit committee, see ***2.3.1. Internal Controls and Audit***, page 71 of this Toolkit.)

According to **LEADERSHIP PRACTICES** (Matrix Level 4), the compensation committee should ensure

**BEST-PRACTICE RESOURCES:**
**Board and Management**

*The G20/OECD Principles* call for disclosure on division of authority between management and the board and, if applicable, the rationale for combining roles of board chair and CEO.

*The <IR> Framework* calls for disclosure on how governance and decision making are linked to value creation, strategic decisions, and innovation.

**BEST-PRACTICE RESOURCES:**
**Board Committee Structure**

*The G20/OECD Principles* call for disclosure on committee structures and charters.

**Example 2.10:** Board and Management Team—Aggreko 2015 Annual Report

| How we divide up our responsibilities | |
|---|---|
| **Chairman** | Responsible for leading the Board, its effectiveness and governance. Setting the agenda to take full account of the issues and concerns of the Directors and ensuring the links between the Shareholders, Board and management are strong. |
| **Chief Executive Officer** | Responsible for the day-to-day leadership, management and control of the Group, for recommending the Group strategy to the Board and ensuring that the strategy and decisions of the Board are implemented via the Executive Committee. |
| **Chief Financial Officer** | Responsible for the day-to-day management of the financial risk of the Group and providing general support to the Chief Executive Officer including the operational performance of the business. |
| **Senior Independent Director** | Provides a sounding board for the Chairman, acts as an intermediary for the other Directors when necessary and is available to meet with Shareholders. |
| **Independent Non-executive Directors** | Constructively challenge the Directors and monitor the delivery of the Group strategy within the risk and control environment set by the Board. |
| **Company Secretary** | Supports the Chairman and Chief Executive Officer and is available to all Directors for advice and support. Informs the Board and Committees on governance matters and responsible for development of corporate governance policies. |

Source: Aggreko.

that executive compensation is based on financial and nonfinancial performance so as to provide long-term incentives.

Example 2.11 provides an activity report for the remuneration and human resources committee of Absa Group (formerly Barclays Africa), a South African bank.

### Board Evaluation

The report should describe the process of annual evaluation of the board as a whole, of board members individually, and of the board committees. It should include the following:

- A description of the process (including frequency and who conducts the evaluation);
- Key indicators that the evaluation was based on;
- Results/areas of improvement;
- Action plans based on the results;
- Actions taken after the previous period's board evaluation.

**Example 2.11:** Committee Description—Absa Group (formerly Barclays Africa) 2015

Group Remuneration and Human Resources Committee

| | |
|---|---|
| **Mohamed Husain (Chairman)**<br>Patrick Clackson<br>Yolanda Cuba<br>Alex Darko<br>Wendy Lucas-Bull<br>Trevor Munday<br>*Attendees:*<br>Maria Ramos<br>Chief: Human Resources Executive<br>Head of Reward | Reviewed:<br>• 2015/2016 remuneration structure, policy and philosophy for the Group in general and the executive team in particular;<br>• proposals from the Group Chairman on the performance of the Chief Executive Officer, and proposals from the Chief Executive Officer on the performance of the Financial Director and other Executive Committee members;<br>• proposals relating to senior hires and terminations, and provided approval where required as per the Committee mandate;<br>• updates from management's Remuneration Review Panel (RRP) on conduct-related incidents and the impact on compensation;<br>• updates on role-based pay, the definition of 'material risk taker', and certain European Banking Association and Prudential Regulatory Authority guidelines and policy statements on compensation;<br>• updates on pensions and benefits across the Group;<br>• reports on subsidiary entities pertaining to pay and benefits; and<br>• reports from an external adviser on trends in compensation practices and industry approaches.<br><br>Responded to:<br>• investor feedback on our remuneration disclosures and further enhanced our remuneration disclosure in line with best practice.<br><br>Approved:<br>• the conversion of the phantom share plan to an equity share plan which was approved at the 2015 annual general meeting;<br>• vesting outcomes for the 2012 long-term incentive awards (vesting mid-2015) and received reports on the prognosis of the 2013 awards (vesting in mid-2016);<br>• compensation for the Chief Executive Officer, Financial Director, and other Executive Committee members;<br>• the salary mandate for bargaining unit and non-bargaining unit employees; and<br>• the remuneration report for inclusion in the integrated report for 2014.<br><br>Recommended to the Board:<br>• proposed 2015 incentive pools, projected 2015 total compensation expenditure and compensation ratios; and<br>• final 2014 incentive pools.<br><br>The GRHRC is satisfied with the status of remuneration and incentives in the Group. The GRHRC spent considerable time in refining the link between pay and performance, and will continue on this journey through 2016. |

Source: Absa Group (formerly Barclays Africa).

**LEADERSHIP PRACTICES** (Matrix Level 4) suggest that evaluations of the board and its committees be conducted by an independent third party. Board evaluation should link to succession planning for the board and for senior management.

### *Governance of Sustainability*

The report should address whether the company has set up a process for oversight of environmental and social issues at the board level. If relevant, it should also describe the following:

- Board approval of sustainability strategy and policies;
- Whether ESG is on the board agenda;
- Board approach to overseeing E&S issues, including any special committee and stakeholder dialogue;
- A review of the effectiveness of E&S management processes, including a grievance mechanism.

The report should describe the structure and processes in place to ensure that ESG issues are periodically reviewed and addressed. It should include the following:

- Oversight over E&S issues at the board level;
- Corporate governance committee;
- Committee or subcommittee to review sustainability issues.

Example 2.12 describes BHP Billiton's approach to governance of sustainability, including the sustainability committees.

## 2.3. Control Environment

The control environment refers to an interconnected system of internal control and risk management structures, processes, and activities that are designed to provide reasonable assurance that the company can deliver on its strategic objectives and is operating efficiently and effectively. The control environment should ensure coverage of the entire enterprise in a holistic manner.

Internal control systems, including the internal audit, are designed to ensure the integrity and reliability of financial statements and nonfinancial reporting as well as compliance with the law and with internal standards and policies. This includes the governance of subsidiaries.

Risk management supports the company strategy by assessing and managing risks and opportunities for the business. It includes risk identification, assessments, integration, and responses and monitoring.

### CONSULT THE MATRIX

The Matrix can be used to gauge a company's level of progress with its control environment. The Toolkit recommends the disclosure of information related to Levels 1–3 of the Matrix, which corresponds to good international practices. Guidance is also provided for disclosure of leadership practices, consistent with Level 4 of the Matrix. (See Table 2.3.)

**Example 2.12:** Board Sustainability Committees—BHP Billiton Annual Report 2016

#### 1.11.1 Our sustainability approach

Our approach to sustainability is led by a sustainability framework that guides our investments in our host countries and local communities, as well as directly at our operated assets. The framework applies a risk-based approach to sustainability, and assesses sustainability risks deemed material to our business with consideration of the potential health, safety,environmental, community, reputational, legal and financial impacts. Risk severity is assessed according to the most severe associated impact, which allows us to understand the potential causes and impacts in the context of business plans.

We also have public sustainability performance targets and mandatory minimum performance requirements, as articulated in Our Requirements standards. These standards are the foundation for developing and implementing management systems at our operated assets. We seek to influence the application of our standards at our non-operated joint ventures.

Our Board oversees our sustainability approach, with the Sustainability Committee overseeing health, safety, environment and community (HSEC) matters, including climate change, human rights, HSEC-related risk control, and legal and regulatory compliance, sustainability reporting and overall HSEC performance.

**Our approach to sustainability is led by a sustainability framework that guides our investments in our host countries and local communities.**

Source: BHP Billiton.

**Table 2.3:** IFC Corporate Governance—Control Environment (Internal Control System, Internal Audit Function, Risk Governance and Compliance)

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Internal Controls** | 1. Company has established documented internal control policies and procedures. | 1. Audit committee ensures corrective actions on control deficiencies identified in Management Letters. | 1. "Three lines of defense" model of risk management, internal control and internal audit has been adopted.[a] | 1. Control environment in accordance with highest international standards, including but not limited to IIA,[b] COSO, ISO 31000, 19600, 37001, and 27001.<br>2. The organizational structure adopted by management has a positive effect on performance, productivity, and leadership effectiveness. |
| **Internal Audit** | 2. Internal audit function regularly interfaces with external auditors and is accountable to the board. | | 2. Internal audit function is independent, objective, risk-based, and has unlimited scope of activity.<br>3. Head of internal audit reports to the audit committee and administratively to management. | 3. Audit committee ensures that the internal audit function is subject to periodic quality assessment by third party. |
| **Risk Governance** | | 2. Board approves risk appetite.<br>3. Company has established risk-management framework with a chief risk officer (CRO) or equivalent with unfettered access to the board. | 4. Board routinely monitors risk management and compliance with policies and procedures.<br>5. CRO reports to board-level risk management committee or equivalent. | |
| **Compliance** | | 4. Comprehensive compliance program annually reviewed, with mechanisms to report wrongdoing and misconduct. | 6. Chief compliance officer reports to the audit committee or equivalent and administratively to management. | |
| **External Audit** | 3. Written Management Letters provided by external auditor. | | 7. Audit committee owns relationship with external auditor (EA); agrees on scope and audit fees, and undertakes a periodic quality assessment of EA, using relevant Audit Quality Indicators.<br>8. Company has established CFO function. | 4. Audit committee reviews long association of EA. |

*(continued on next page)*

**Table 2.3:** IFC Corporate Governance Matrix—Control Environment (Internal Control System, Internal Audit Function, Risk Governance and Compliance) *(continued from previous page)*

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Integrating of E&S** | | 6. Company has established industry practices in its E&S risk-management practices. | 9. ESG activities are highly integrated, effective, and efficient and support the strategic and operational business objectives, and controls support objectives.<br>10. Periodic ESG, IT, and Information Security internal audits.<br>11. Comprehensive ESMS integrated in risk-management framework, and E&S risks are part of establishing the risk appetite.<br>12. E&S/sustainability head has unfettered access to senior management and CRO. | 5. Board or sustainability committee ensures corrective actions on E&S issues.<br>6. Head of ESG reports to board E&S/sustainability committee.<br>7. ESMS is consistent with international standards (e.g., ISO 14001). |
| **Subsidiary Governance** | 4. Company can identify its subsidiaries. | 7. Company has policies and procedures to control the creation and dissolution of subsidiaries. | 13. Company has a centralized subsidiary governance function and subsidiaries are categorized based on complexity and an appropriate governance framework applied to each category. | 8. Board exercises oversight over the organizational structure and the activities of its subsidiaries. |

[a] Namely, management is the first line of defense, risk management and compliance function are the second line of defense, and internal and external audit as independent assurance providers are the third line of defense.

[b] The Institute of Internal Auditors standards and related promulgations.

There are several internationally recognized frameworks for such control systems, such as those set by the Institute of Internal Auditors, COSO, and ISO 31000.

### 2.3.1. Internal Controls and Audit

The report should address the process and structure in place for the company's internal and external controls.

**LEADERSHIP PRACTICES** (Matrix Level 4) suggest that the control environment be in accordance with the highest international standards, such as those set by the Institute of Internal Auditors, COSO, and ISO 31000, 37001, and 27001.

**BEST-PRACTICE RESOURCES: Internal Control**

*The 2013 COSO Framwork:* The Committee of Sponsoring Organizations of the Treadway Commission **Internal Control Framework** helps companies design and implement internal controls that adapt to changing business and operating environments, mitigate risks to acceptable levels, and support sound decision making and governance. The Framework consists of 17 principles in 5 areas:

- Control environment
- Risk assessment
- Control activities
- Information and communication
- Monitoring activities

Together these cover an entity's operations, reporting, and compliance and make specific provisions for issues at the entity, divisional, operating unit, and functional levels.




#### *Internal Controls*

The report should describe the roles of the board, audit committee, and senior management in the internal controls of the company. Disclosure should include the scope of internal controls, specifically whether it covers the following:

- Financial accounting and reporting controls;
- Nonfinancial accounting and reporting controls;
- Operational controls, including sustainability and stakeholder risks (worker, consumer, community health and safety);
- Compliance controls, including ethics and compliance: code of ethics, whistleblower systems, anticorruption measures.

Example 2.13 on the next page describes typical elements of a company's internal controls, including financial, operational, and compliance controls and risk management.

#### *Internal Audit*

The report should describe how the board is carrying out its responsibility to ensure the financial integrity of the company and the integrity of its operations, and it should provide insight into the work of the board and audit committee in this area.

In good international practices (Matrix Level 3), the internal audit function should be independent, objective, risk-based, and empowered with an unlimited scope of activities.

Good international practice (Matrix Level 3) also suggests that the head of the internal audit function report to the audit committee and administratively to management.

It is common practice for the internal audit function to meet regularly with the external auditors. It is also common practice to have an internal audit function (either in-house or outsourced) that regularly tests and checks the effectiveness of internal controls, to ensure the financial integrity of the company.

**LEADERSHIP PRACTICES** (Matrix Level 4) suggest that the internal audit function be subject to periodic quality assessment by a third party.

The report should include the following information:

- Whether the internal auditor reports to the audit committee, whether that is its main or only line of reporting, and the internal auditor's relationship with senior management;
- Main activities, challenges, and findings of the internal audit;
- If the company does not have a dedicated internal audit function, how this role is carried out, including by an external firm;

- Whether internal audit assesses the adequacy and effectiveness of ESG policies and practices and of the IT and information security systems;
- How the audit committee ensures corrective action on control deficiencies, especially those highlighted in the external auditor's management letter.

Example 2.14 describes the internal audit process for Nedbank, a South African bank, and how it forms part of the risk management framework—as a third line of defense.

**Example 2.13:** Internal Controls—Fresnillo 2015 Annual Report

**Internal controls**

The Board has overall responsibility for the Group's system of internal control, which includes all material controls, including financial, operational and compliance controls and related risk management, and reviewing its effectiveness. The system of internal control is designed to identify, evaluate and manage significant risks associated with the achievement of the Group's objectives. Because of the limitations inherent in any system of internal control, the Group'ssystem is designed to meet its particular needs and the risks to which it is exposed. It is designed to manage risk rather than eliminate risk altogether. Consequently it can only provide reasonable and not absolute assurance against material misstatement or loss.

The Board has delegated to the Audit Committee its responsibility for reviewing the effectiveness of Fresnillo's internal controls. The Audit Committee reviews the system of internal control on an annual basis. The day-to-day responsibility for managing risk and the maintenance of the Group's system of internal control is collectively assumed by the Executive Committee. The Executive Committee is supported in this task by the Internal Audit department. The annual Internal Audit programme, approved by the Audit Committee, ensures that internal controls over all of the operations are all reviewed at least once over a three-year timeframe. The risk categories set out in the risk matrix were used as the basis for the process of reviewing the effectiveness of the system of internal controls. The Internal Audit department obtained letters of representation from the Executive Committee and the executive management on the Group's system of internal control.

The Group has in place internal controls and risk management systems in relation to the Group's financial reporting process and the Group's process for preparing consolidated accounts. These systems include policies and procedures to ensure that adequate accounting records are maintained and transactions are recorded accurately and fairly to permit the preparation of financial statements in accordance with IFRS.

Source: Fresnillo Plc.

**Example 2.14:** Internal Audit—Nedbank Group 2014 Integrated Report

INTERNAL AUDIT

Group Internal Audit (GIA) is a centralised, independent assurance function. It was constituted in terms of the Banks Act, 94 of 1990 (as amended) and the regulations thereto, with its purpose, authority and responsibilities set out in the Banks Act and regulations and formally defined in a charter approved by the Group Audit Committee (GAC).

GIA forms part of the Enterprisewide Risk Management Framework as a third line of defence. The purpose of GIA is to provide independent, objective assurance to the board that the governance processes, management of risk and systems of internal control are adequate and effective to mitigate the most significant risks, both current and emerging, that threaten the achievement of the group's objectives, and in so doing help improve the control culture of the group. It is responsible for developing a 12-monthrolling-audit plan, using a risk-based methodology and taking into consideration specific regulatory requirements pertaining to internal audit, including any risks or control concerns identified by management and the board. This plan is approved by the GAC.

Source: Nedbank Group.

> **BEST-PRACTICE RESOURCES: Financial Reporting, Audit, and Controls**
>
> *The G20/OECD Principles* note the primacy of the board in ensuring the effectiveness of the board's financial reporting systems, internal audit, and internal controls.

### *Audit Committee*

The report should describe the role and deliberations of the audit committee. This committee typically ensures that appropriate accounting and auditing are in place to produce true and accurate financial statements. It also typically oversees the internal audit process, the external audit, and the external auditor. The committee may also oversee related-party transactions and, if there is no risk committee, risk oversight and management.

Example 2.15 introduces Aggreko's audit committee, its members, key achievements, and areas of focus. This example is also interesting for its future focus—a good practice (Matrix Level 3) that helps hold the audit committee accountable.

### *External Audit*

The report should describe the tenure, qualifications, and independence of the external auditor.

**Example 2.15:** Audit Committee—Aggreko Annual Report 2015

THE ROLE OF THE AUDIT COMMITTEE IS TO MONITOR AND REVIEW THE INTEGRITY OF THE GROUP'S FINANCIAL STATEMENTS TO DETERMINE WHETHER THE JUDGEMENTS TAKEN BY MANAGEMENT ARE APPROPRIATE. WE ALSO MONITOR THE INDEPENDENCE AND EFFECTIVENESS OF THE EXTERNAL AUDITOR AND OVERSEE THE GROUP'S SYSTEMS FOR INTERNAL CONTROL AND RISK MANAGEMENT.

**2015 Key achievements**

- Oversaw the external audit tender process, making a recommendation to the Board on the appointment of a new external auditor.
- Reviewed and ensured compliance with the new UK Corporate Governance Code requirements for going concern and viability statements.
- Reviewed the effectiveness of the risk management process.
- Monitored the changes made to the financial control environment following the reorganisation.
- Provided oversight on the Group's risk management processes, receiving presentations from the Group Financial Controller on financial controls under the new structure, the Director of Tax on the structure of the tax team, strategy and control framework and the Chief Information Officer on our cyber governance framework.

**Members in 2015**

| | Meetings attended |
|---|---|
| Robert MacLeod – Audit Committee Chairman | ✓ ✓ ✓ |
| Russell King – Senior Independent Director | ✓ ✓ ✓ |
| Diana Layfield – Non-executive Director | ✓ ✓ ✓ |
| Ian Marchant – Non-executive Director | ✓ ✓ ✓ |

**Areas of focus for 2016**

- Oversee the transition of responsibilities to the new external auditor.
- Continue risk management oversight with presentations scheduled from the Directors of Finance for Power Solutions and Rental Solutions.
- Managing the transition of responsibilities for the Chairmanship of the Committee from Robert MacLeod to Ian Marchant.

Source: Aggreko.

(See Example 2.16.) Specifically, the report should provide the following information:

- Independence and qualifications of the external auditor, why a particular auditor is engaged or reengaged, and the effect of any long association on independence;
- Non-audit work by the external auditor and its impact, if any, on the independence of the audit, plus a breakdown of audit and non-audit fees;
- Tenure and rotation of the audit firm and partner (the longer the tenure the more risk of conflict of interest);
- Periodic assessment of the quality of the external audit;
- Subsequent actions by management on issues raised in the audit report or external auditor management letter.

The report should also address the audit committee's role in agreeing to the audit plan as well as the committee's oversight and regular relations/meetings with the external auditor before, during, and after the audit.

Good international practice (Matrix Level 3) suggests that the audit committee own the relationship with the external auditor, agree on scope and audit fees, and undertake a periodic quality assessment of the external auditor, using relevant audit quality indicators.

### *Integrating Sustainability*

The report should indicate whether environmental and social issues are within the scope of the audit committee. The report should also describe the role of the audit committee in ensuring the quality of nonfinancial and sustainability information.

For the board to make informed decisions, it is **BEST PRACTICE** for business-critical nonfinancial information, including sustainability, to be of the same quality as financial statements.

**LEADERSHIP PRACTICES** (Matrix Level 4) suggest that ESG data be subject to an annual audit by an independent provider.

Example 2.17 illustrates the process and results of assurance of key sustainability data for Goldfield, a South African mining company, as part of its internal audit process and audit committee oversight.

### *Subsidiary Governance Framework*

Strong subsidiary governance can be a critical tool in an organization's risk management framework. Subsidiaries are set up for various reasons, including tax optimization, limitation of liability, or requirements to set up a locally incorporated entity, and they can represent a large share of the parent company's value. Furthermore, since they generally are more than 50 percent owned by the parent, their financial results are consolidated into the parent's financial results.

## **Example 2.16:** External Auditor—CLP Group Annual Report 2015

**EXTERNAL AUDITOR**

The Group's external auditor is PwC. PwC has written to the Audit Committee confirming that they are independent with respect to the Company and that there is no relationship between PwC and the Company which may reasonably be thought to bear on their independence. In order to maintain their independence, PwC will not be employed for non-audit work unless the non-audit work meets the criteria suggested in the Listing Rules and has been pre-approved by the Audit Committee.
In addition, there must be clear efficiencies and value-added benefits to CLP from that work being undertaken by the external auditor, with no adverse effect on the independence of their audit work, or the perception of such independence.

During the year, the external auditor (which for these purposes includes any entity under common control, ownership or management with the external auditor or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as part of the audit firm nationally or internationally) providing the following audit and permissible audit related non-audit services to the Group:

| | 2015 HK$M | 2014 HK$M |
|---|---|---|
| Audit | 39 | 37 |
| Permissible audit related and non-audit services | | |
| Accounting/tax advisory services relating to business development | 2 | 1 |
| Other services | 6 | 6 |
| Total | 47 | 44 |

Source: CLP Group.

**Example 2.17:** Assurance of Sustainability Data—Gold Fields Integrated Annual Report 2016

## Key Sustainability Performance Data

The following key sustainability performance information was selected by Gold Fields, for assurance by KPMG in 2016 which have been reported in accordance with the criteria listed in the table below.

| Parameter | Level of assurance | Management figure |
|---|---|---|
| **Selected sustainability performance information presented in compliance with Subject Matter 4 of the International Council of Mining and Metals' (ICMM) Sustainable Development Framework: Assurance Procedure (ICMM Assurance Procedure), and prepared in accordance with the Global Reporting Initiative (GRI) G4 Guidelines and Gold Fields' internally developed Guidelines (available on request):** | | |
| **Environment** | | |
| Total $CO_2$ equivalent emissions, scope 1-3 (in tonnes) | Reasonable | 1,963,759 tonnes |
| Electricity (MWh) | Reasonable | 1,400,422MWh |
| Number of environmental incidents - Level 3 and above | Reasonable | 3 incidents |
| Total water withdrawal (Mℓ) | Reasonable | 30,321Mℓ |
| Diesel (kℓ) | Reasonable | 183,497kℓ |
| Total water recycled/re-used per annum (Mℓ) | Reasonable | 44,274Mℓ |
| Water intensity (kℓ withdrawn per ounce of gold produced) | Reasonable | 30,321,160kℓ / 2,218,873 = 13.67 |
| Total energy consumed (GJ)/total tonnes mined | Reasonable | 11,696,447GJ / 185,102,637 = 0.06 |
| Total energy consumed (GJ)/ounce of gold produced | Reasonable | 11,696,447GJ / 2,218,873 = 5.27 |
| **Health** | | |
| Number of cases of Silicosis reported | Reasonable | 7 cases |
| Number of cases of Noise Induced Hearing Loss reported | Reasonable | 9 cases |
| Cardio Respiratory Tuberculosis (number of new cases reported) | Reasonable | 35 cases |
| Number of cases of Malaria tested positive per annum | Reasonable | 514 positive cases |
| Number of South African and West African employees in the HAART programme (cumulative) | Reasonable | 354 employees |
| Percentage of South African and West African workforce on the voluntary counselling and testing (VCT) programme | Reasonable | 4,670 people on VCT / 13 450 people = 34.72% |
| **Safety** | | |
| TRIFR[1] | Reasonable | 124 TRIs / 54,669,196 hours = 2.27 |
| Number of fatalities | Reasonable | One |
| **Social** | | |
| Total socio-economic development (SED) spend in US Dollars[2] | Reasonable | $16,190,509.50 |

Source: Gold Fields.

Although they are controlled by the parent company, subsidiaries are separate legal entities with separate management and governance structure. This creates an inherent conflict, especially in subsidiaries that are less than 100 percent owned, where the board of the subsidiary owes a fiduciary duty not only to the parent (controlling shareholder) but also to the subsidiary itself and all its shareholders.

In addition, unlike public companies that are subject to strict disclosure requirements, private companies can be opaque. Therefore, a robust subsidiary governance framework provides the controls and information flow that allow the parent company's board to exercise oversight over the organizational structure and activities of subsidiaries. The Matrix provides for escalating practices of a subsidiary governance framework:

- ***Basic Practices:*** The company can identify its subsidiaries.
- ***Intermediate Practices:*** The company has policies and procedures to control the creation and dissolution of subsidiaries.
- ***Good International Practices:*** The company has a centralized subsidiary governance function, and subsidiaries are categorized based on complexity with an appropriate governance framework applied to each category.
- ***Leadership:*** The board exercises oversight over the organizational structure and the activities of its subsidiaries.

Following this approach, the annual report should provide organizational charts of the legal-entity structure of the organization, both holistically and based on criteria that would help the board determine the organization's footprint, including jurisdiction, line of business, assets, revenue, regulators, branches, and representative offices.

The annual report should also include a description of the subsidiary governance framework as part of the control environment, covering the following:

- *Creation and dissolution of legal entities:* information on the internal approval process for the creation and dissolution of new legal entities, what entities have been created or dissolved over the reporting period, and why;
- *Structure and composition of subsidiary boards:* information on the organization's policy on the structure of subsidiary boards, including independent non-executive directors that serve on subsidiary boards;
- *Subsidiary categorization:* how the subsidiary governance is adapted to each subsidiary, based on a categorization of its strategic importance and complexity;
- *Subsidiary oversight at the board level:* how the board of the parent company oversees the organizational structure and activities of subsidiary entities;
- *Internal control process:* application of audit and other internal control processes of the parent to ensure compliance by the subsidiary;
- *Escalation procedures:* information on the criteria used to determine transactions that require escalation to the parent board for review or approval.

**BEST PRACTICES** suggest that, when conducting periodic assessments, the parent company can use its internal audit function to evaluate the robustness and compliance of the governance practices put in place by the subsidiary.

> **BEST-PRACTICE RESOURCES: Holding Companies**
>
> *King IV Code of Corporate Governance:* "The board of the holding company should. . .ensure that the group governance framework addresses governance matters as appropriate for the group, including. . .the extent to which governance and operational policies of the holding company have been adopted by subsidiary companies in the group."

### 2.3.2. Risk Governance

The report should describe the companywide system and governance structure for managing risks, including the role of the board in setting the company's risk appetite and overseeing the risk management process.

Common practices suggest that companies establish a risk management framework, with a chief risk officer (CRO) or equivalent that has unfettered access to the board. Good practices (Matrix Level 3) suggest that the CRO should report to the risk management committee of the board or the audit committee of the board, whichever is responsible for risk oversight. (For more on risk assessment and mitigation, see ***1.3. Risk Analysis and Response***, page 24 of this Toolkit.)

#### *Risk Appetite*

The report should include a description of the aggregate level and type of risk that the organization is prepared to accept in pursuit of its strategic objectives and business plans. Specifically, the report should address the following:

- Overall risk appetite, risk capacity, and the risk profile of the organization;
- Maximum risk tolerance for each material risk;
- How risk appetite is determined;
- Quantitative and qualitative measures used.

**BEST PRACTICE** suggests that risk appetite disclosure include both qualitative and quantitative information.

The report should indicate whether the organization's risk appetite was approved by the board. In Example 2.18, CLP Group describes its risk appetite and risk profiling criteria. Example 2.19 illustrates quantitative measures of risk appetite for UBS, a Swiss bank.

> **BEST-PRACTICE RESOURCES: Risk Appetite for Banks**
>
> *Corporate Governance Principles for Banks—Basel Committee on Banking Supervision:* The Basel Principles provide extensive guidance on risk appetite, including the role of the board in setting the risk appetite, the formulation of a risk appetite statement, and the translation of risk appetite into risk limits, structures, and management decisions.

#### *Risk Assessment and Management*

The report should describe the risk management process—how risks are identified, monitored, and controlled; how the level of risk is evaluated; and what information is used.

The report should describe the methodology for determining the response to risk events. It should address how the company evaluates the effectiveness of its risk controls to determine whether the risk level is within the organization's risk appetite, and how it decides whether additional controls are required.

**Example 2.18:** Risk Appetite and Profiling—CLP Group 2015 Annual Report

### CLP's Risk Appetite and Risk Profiling Criteria

CLP's risk appetite represents the amount of risk the Group is willing to undertake in pursuit of its strategic and business objectives. In line with CLP's Value Framework and expectations of its stakeholders, CLP will only take reasonable risks that (a) fit its strategy and capability, (b) can be understood and managed, and (c) do not expose the Group to:

- material financial loss impacting ability to execute the Group's business strategy and / or materially compromising the Group's ongoing financial viability,
- incidents affecting safety and health of our staff, contractors and the general public,
- material breach of external regulations leading to loss of critical operational / business licence and / or substantial fines,
- damage of the Group's reputation and brand name,
- business / supply interruption leading to severe impact on the community, and
- severe environmental incidents.

Based on the above, CLP has established its risk monitoring in the form of a risk assessment matrix to help rank risks and prioritise risk management efforts at the Group level. Business units are required to adopt the same risk matrix structure in order to establish their own risk profiling, determine consequence and likelihood of identified risks with reference to their own materiality and circumstances as well as establishing risk mitigation strategies.

Source: CLP Group.

**Example 2.19:** Quantitative Risk Appetite Objectives—
UBS 2016 Annual Report

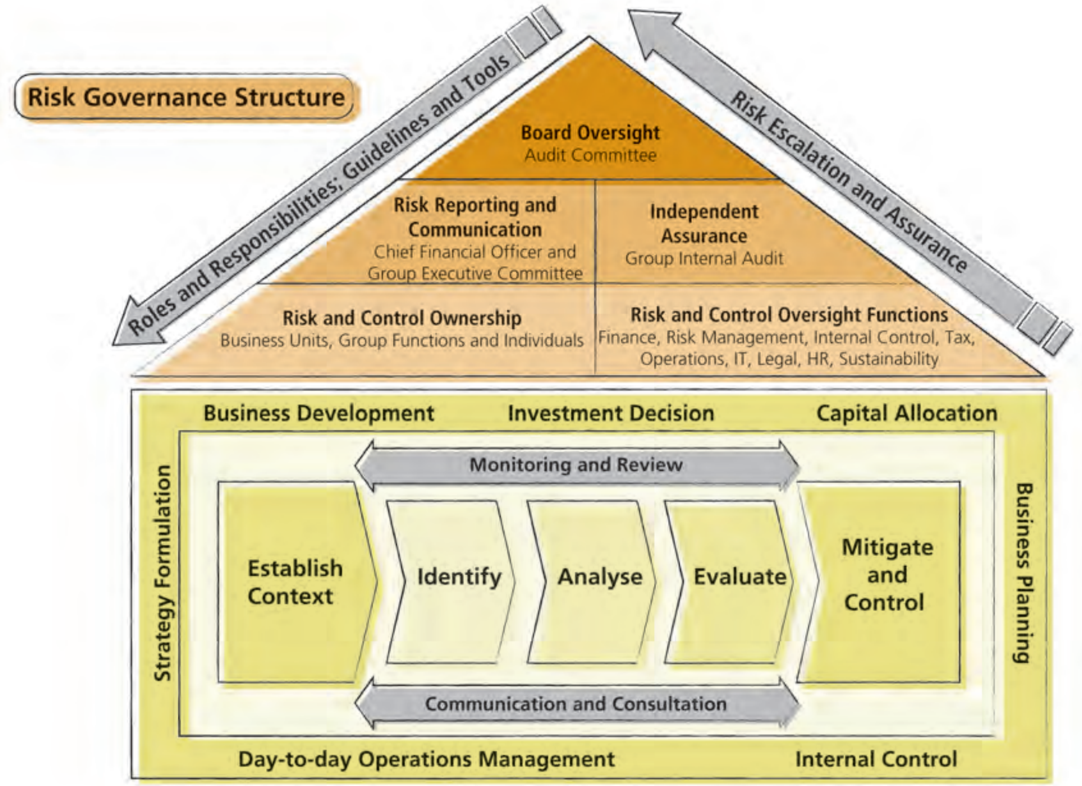
**Group-wide quantitative risk appetite objectives**

| | | |
|---|---|---|
| **Minimum capital objectives**<br><br>Capital is sufficient to maintain a post-stress fully applied CET1 capital ratio of at least 10% and a post-stress going concern capital ratio of at least 13% | **Minimum leverage ratio objectives**<br><br>Capital is sufficient to maintain a leverage ratio of at least 2.5% based on CET1 capital, and at least 4.0% based on going concern capital, even if a severe stress event were to occur | **Solvency objectives**<br><br>CET1 capital plus contingent capital is sufficient to ensure that the probability of loss for the bank's debt holders is consistent with the bank's target credit rating |
| **Earnings objectives**<br><br>Earnings in our core businesses should be positive in most years. In addition, we aim to avoid consecutive quarterly losses in our core businesses in a severe stress event | **Liquidity objectives**<br><br>Ensure that the firm has sufficient funding sources to survive a severe 12-month idiosyncratic and market-wide liquidity stress event without significantly impacting our business franchises | **Funding objectives**<br><br>Ensure that the firm has sufficient long-tern funding to maintain franchise assets at a constant level under stressed market conditions for up to one year |

Source: UBS.

The report should describe the method to determine appropriate responses for each risk identified. It should also address how management incorporates risk when planning new strategies, activities, and products. (See Examples 2.20 and 2.21.) It is important to include the accountability of specific individuals at each level of the risk system.

### **Example 2.20:** Risk Management—CPL Group 2015 Annual Report




Source: CPL Group.

### **Example 2.21:** Risk Management—Santova Limited 2016 Annual Integrated Report

**RISK MANAGEMENT PROCESS**

Santova's approach to risk is to use a Risk Management Cycle to govern its risk management process, as follows:

**Identify and understand objectives** – these include Santova's strategic, business and process objectives.

**Set the risk tolerance** – the level of residual risk that the Santova Board is prepared or willing to accept without further mitigating action being put in place.

**Identify risks** – using the various committees and role players listed in the Risk Management Framework, other relevant Santova forums, the Risk Register and the Risk Inbox process.

**Assess risks** – using the Risk Register, rate the impact and probability of risks and establish the Inherent Risk score.

**Identify current controls** – assign an owner to the risk, identify the Current Controls and rate the Perceived Control Effectiveness (management's rating of Current Controls).

**Establish residual risk** – the Risk Register will calculate a Residual Risk score by weighing up the Perceived Control Effectiveness against the Inherent Risk to establish what risk remains.

**Identify response strategy and action required** – determine the control gaps by identification of controls which should be in place in order to reduce the Residual Risk to an acceptable level and then capture the necessary activities or actions to mitigate these control gaps.

**Reporting and monitoring** – All risks with a High or Maximum Residual Risk will be reported by Management to the Audit and Risk Committee. Continuous monitoring by the variety of forums and methods listed in the Risk Management Framework above, will be undertaken to ensure that the desired Response Strategy and Action Required for Risk is implemented successfully.

Source: Santova.

### *Risk Oversight*

The report should describe the responsibility of the board for oversight and control of risk management, either through a formal risk management committee or through the audit committee.

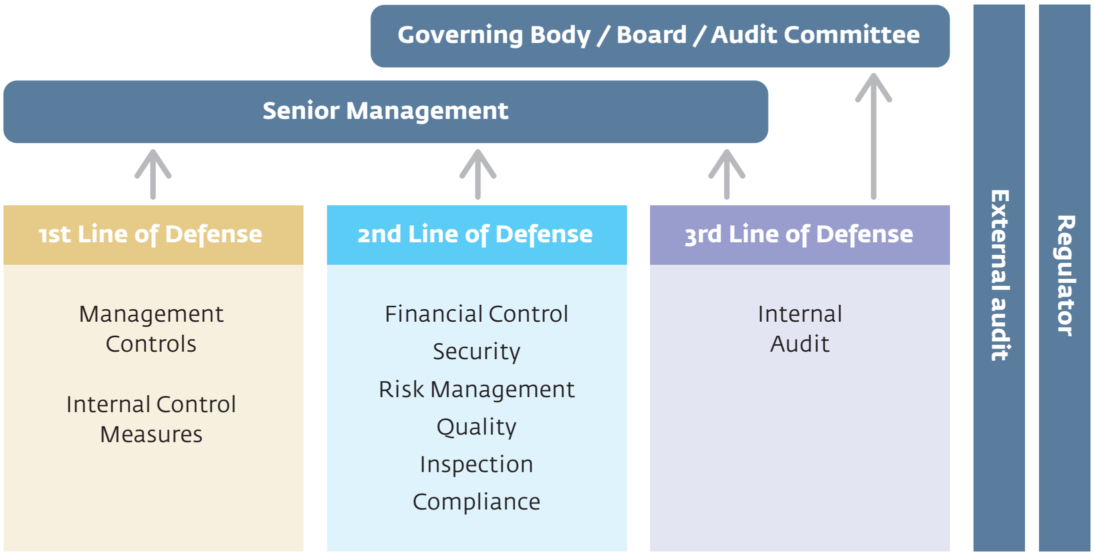
Good international practices (Matrix Level 3) suggest that companies adopt the "three lines of defense" model of risk management, in which the lines of defense in risk management are 1) management control, 2) the various risk control and compliance oversight functions established by management, and 3) independent assurance. (See Figure 2.1.) The report should indicate whether this model is adopted in company practices.

### *Integrating Sustainability*

The report should describe how environmental and social risks have been integrated into the risk management framework. This should include a description of the relationship between the head of ESG/sustainability, the board, and the risk management committee. It also should describe how environmental and social considerations are taken into account in the determination of risk appetite.

Good international practices (Matrix Level 3) recommend that a comprehensive Environmental and Social Management System be integrated into a company's risk management framework, and that E&S risks be part of the process of establishing risk appetite.

**Figure 2.1:** The Three Lines of Defense Model




Adapted from ECIIA/FERMA *Guidance on the 8th EU Company Law Directive, article 41*

Source: The Institute of Internal Auditors.

**BEST-PRACTICE RESOURCES:**
**Disclosure of Risk Management**

*The U.K. Corporate Governance Code* suggests the following practices for risk management disclosure:

- Director statement that the board has carried out a robust risk assessment of the principal risks facing the company, and that it expects that the company will be able to continue in operation and meet its liabilities;
- Description of the risks and an explanation of how the company is managing or mitigating them;
- Results of review of the effectiveness of risk management and internal control systems.

*The King IV Report on Corporate Governance for South Africa, 2016,* provides that the board should ensure that there are processes in place to enable complete, timely, relevant, accurate, and accessible risk disclosure to stakeholders.

Good practice also recommends that the head of ESG/sustainability have unfettered access to senior management and the most senior risk officer.

The report should describe how different aspects of sustainability risks are addressed, including not only operational risk but also financial risk, such as credit risk and liabilities. (For further disclosure guidance, see ***1.4.1. Assessment of Key Sustainability Opportunities and Risks***, page 28 of this Toolkit.)

**BEST-PRACTICE RESOURCES: Risk Oversight**

*The ICGN Global Governance Principles:* "The board should adopt a comprehensive approach to the oversight of risk which includes all material aspects of risk including financial, strategic, operational, environmental, and social risks (including political and legal ramifications of such risks), as well as any reputational consequences."

### 2.3.3. Compliance

The report should include a discussion of the company's compliance program or procedures, including employee training, auditing and monitoring systems, company "hotline" for reporting violations, guidance for conflicts of interest, and sanctions and disciplinary action for violations.

Good international practice (Matrix Level 3) suggests that the compliance function be led by a designated compliance officer who reports to the audit committee of the board and administratively to management.

#### *Management System*

The report should describe the management system to ensure compliance with the law, the company's charter and corporate governance policies, and its code of ethics. It should also provide information on mechanisms—such as whistleblowing policies and processes—to report wrongdoing or misconduct.Example 2.22 shows the governance structure of Li & Fung, a Chinese logistic company, with accountability and responsibilities associated with different aspects of risk governance.

**Example 2.22:** Compliance—Li & Fung Limited 2015 Annual Report

**Our Governance Structure**

Our governance structure enables risk identification and escalation whilst providing assurance to the Board. We assign clear roles and responsibilities for managing risk and implement systems to facilitate the implementation of policies and guidelines. This structure comprises three layers of roles and responsibilities to manage risk and internal control as follows:

| Role | Accountability | Responsibilities |
|---|---|---|
| Oversight | Audit Committee of the Board, Risk Management and Sustainability Committee of the Board | Oversight of corporate governance, financial reporting, risk management and internal control systems |
| Risk and control owner | Li & Fung Management and Operations Support Group | • Day-to-day execution and monitoring of internal control<br>• Strategic policies and operating guidelines formulation and execution<br>• Balance between business operation efficiency and exercising internal controls |
| Risk monitoring and communication | Corporate Compliance team | • Evaluation of risk management and internal controls to identify areas for improvement<br>• Monitoring of corporate governance disclosure, statutory and listing rules compliance<br>• Undertaking of investigations |

Source: Li & Fung Limited.

### *Integrating Sustainability*

Internal compliance is a central function in managing environmental and social issues facing companies. This includes compliance with the environmental and social aspects of internal codes of conduct or ethics, including in the supply chain.

It also includes regulatory compliance with rules and regulations associated with environmental and social issues, including pollution, corruption and bribery, and treatment of workers.

## 2.4. Treatment of Minority Shareholders

Minority shareholders are best protected if all shareholders of the same class of shares have equal voting, subscription, and transfer rights and there are efficient voting mechanisms—such as supermajority or "majority of the minority" voting practices—to protect them from concentrated ownership or conflicts of interest with controlling shareholders.

There should also be in place processes for engaging with minority shareholders. It is important that they receive adequate notice and the agenda for all shareholder meetings and are permitted and encouraged to participate and vote in shareholder meetings. All holders of securities of the same class should have access to equal information (fair disclosure). The company should have a publicly disclosed dividend policy.

Further, the company should have in place well-understood policies and practices to deal with minority shareholder interests in material transactions that may affect their rights.

### CONSULT THE MATRIX

The Matrix can be used to gauge a company's level of progress in its treatment of minority shareholders. The Toolkit recommends the disclosure of information related to Levels 1–3 of the Matrix, which corresponds to good international practices. Guidance is also provided for disclosure of leadership practices, consistent with Level 4 of the Matrix. (See Table 2.4 on the next page.)

### 2.4.1. Ownership and Control

The report should give a clear view of who owns the company, including those who own or can exert influence, directly or indirectly, over shares and thus voting, and it should provide details on controlling shareholders and their associates and affiliated entities.

#### *Significant Direct Shareholders (or Beneficial Owners)*

The annual report should list significant shareholders (or beneficial owners, typically those with more than 5 percent of shares), the percentage of shares held, and the percent of voting rights. This should also include share options.

The report should note when significant shareholders are management personnel or board members (or, for two-tier boards, supervisory board members). It is generally good practice to disclose all shareholdings of board members and of management, even when that represents less that 5 percent of shares.

If certain shareholders cannot be identified or confirmed, the report should note that as well. Example 2.23 details the ownership of the top 10 shareholders of True Group Thailand, a telecommunications company.

**Example 2.23:** Beneficial Ownership—True Group Thailand 2015 Annual Report

| Name | No. of Shares (Million Shares) | % of Total Issued Shares |
|---|---|---|
| 1. CP Group [2/] | 12,554.31 | 51.02 |
| 2. CHINA MOBILE INTERNATIONAL HOLDINGS LIMITED [3/] | 4,429.43 | 18.00 |
| 3. THAI NVDR COMPANY LIMITED [4/] | 1,597.00 | 6.49 |
| 4. UOB KAY HIAN (HONG KONG) LIMITED - Client Account [3/] | 456.14 | 1.85 |
| 5. UBS AG HONG KONG BRANCH [5/] | 206.52 | 0.84 |
| 6. HSBC (SINGAPORE) NOMINEES PTE LTD [6/] | 185.03 | 0.75 |
| 7. STATE STREET BANK EUROPE LIMITED [7/] | 155.48 | 0.63 |
| 8. MR. PAMORN POLTEP | 131.22 | 0.53 |
| 9. MR. PICHIT CHINWITTHAYAKUL | 84.00 | 0.34 |
| 10. CORE PACIFIC-YAMAICHI INTERNATIONAL (H.K.) LIMITED-CLIENT [3/] | 79.01 | 0.32 |

Source: True Group Thailand.

**Table 2.4:** IFC Corporate Governance Matrix—Treatment of Minority Shareholders

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Voting Rights** | 1. All shareholders of the same class have equal voting, subscription, and transfer rights.<br>2. Minority shareholders receive adequate notice and the agenda for all shareholders' meetings; and are permitted to participate and vote at shareholders' meetings. | 1. Effective representation of minority shareholders through cumulative voting or similar mechanisms; and economic rights such as inspection rights, exit rights, and tag-along rights.<br>2. Company has a dividend policy.<br>3. Clearly articulated and enforced policies on treatment of minority shareholders in changes of control. | 1. Effective shareholder voting mechanisms to protect minority shareholders from concentrated ownership or strong conflicts of interest with controlling shareholders (e.g., supermajority or "majority of minority" provisions).<br>2. Shareholders are consulted on executive compensation. | 1. Treatment of shareholders consistent with best international market practices.<br>2. Executive compensation subject to shareholder approval.<br>3. Each share is afforded one vote at the AGM. |
| **Protective Rights** | 3. Holders of all securities of the same type and class have access to equal information (fair disclosure). | 4. Well-understood policy and practice of full and timely disclosure to shareholders of all material related-party transactions and shareholder agreements. | 3. Well-understood policy and practices of company material transactions that could potentially affect the rights of minority shareholders.<br>4. Annual report discloses material risks to minority shareholders associated with controlling shareholders, ownership concentration, cross-holdings, and voting-power imbalances. | 4. Related-party transactions (over 2.5% of net assets or $150,000) subject to shareholder approval or stricter requirements.[a] |
| **Investor Relations** | 4. Investor relations function established. | | 5. Investor relations functions include program for engaging minority shareholders. | |

[a] Often, requisite thresholds are set by law/regulation in the listing jurisdiction; however, the OECD has recommended the referenced limits. See OECD, *Guide on Fighting Abusive Related Party Transactions in Asia* (2009) 31.

In many jurisdictions, the disclosure of ownership is strictly prescribed. Some countries also require companies to disclose the distribution of shareholdings, with bands showing the number of shareholders in a range of ownership percentage (for example, more than 5 percent, more than 50 percent, and so on). An indication of foreign versus domestic shareholders is also sometimes required. Example 2.24 shows the distribution of shareholdings for Telekom Malaysia.

### *Indirect or "Deemed" Ownership*

Disclosure on ownership and control should also include arrangements that provide indirect control or deemed ownership. An example is trusts and similar arrangements. Shares of the company held in a trust should be reported under the beneficial ownership of a founder (or a trustee or beneficiary of the trust if they can influence the voting on behalf of the trust). If control is held primarily through a trust, a foundation, or similar vehicle, the report should disclose the officers in control of these vehicles and how control is exercised.

Deemed ownership also can include the following:

- *Shareholder agreements* to vote shares in line with those of a substantial shareholder;
- *Special voting rights*;
- *Multivoting shares* and the voting rights they grant to major shareholders;
- *Control-enhancing or anti-takeover mechanisms*, such as voting caps and poison pills;
- *Special shareholder rights* (golden share) to block certain major decisions or to appoint one or more board members directly (common in state-owned enterprises).

Example 2.25 shows Telekom Malaysia's beneficiaries under nominee accounts and a spouse's shares added to a board member's shares to determine his or her "deemed interest." Box 2.1 on the next page lists generally accepted ownership disclosure requirements from around the world.

**Example 2.24:** Shareholdings Distribution—Telekom Malaysia Annual Report 2015

| Size of Shareholdings | Shareholders | | | | Shares | | | |
|---|---|---|---|---|---|---|---|---|
| | Malaysian | | Foreign | | Malaysian | | Foreign | |
| | No. | % | No. | % | No. | % | No. | % |
| Less than 100 | 1,485 | 6.54 | 22 | 0.10 | 24,817 | 0.00 | 514 | 0.00 |
| 100 – 1,000 | 5,765 | 25.41 | 104 | 0.46 | 4,399,304 | 0.11 | 74,450 | 0.00 |
| 1,001 – 10,000 | 12,497 | 55.08 | 282 | 1.24 | 38,295,186 | 1.02 | 1,169,955 | 0.03 |
| 10,001 – 100,000 | 1,605 | 7.07 | 263 | 1.16 | 37,400,034 | 1.00 | 10,324,828 | 0.28 |
| 100,001 – 187,896,740(*) | 365 | 1.61 | 299 | 1.32 | 1,223,400,067 | 32.56 | 428,764,965 | 11.41 |
| 187,896,741 and above (**) | 3 | 0.01 | 0 | 0.00 | 2,014,080,703 | 53.59 | 0 | 0.00 |
| **Total** | **21,720** | **95.72** | **970** | **4.28** | **3,317,600,111** | **88.28** | **440,334,712** | **11.72** |

Notes:
* Less than 5% of issued shares
** 5% and above of issued shares

Source: Telekom Malaysia.

**Example 2.25:** "Deemed Interest"—Telekom Malaysia Annual Report 2015

| Interest in the Company | No. of Ordinary Shares of RM0.70 each | | |
|---|---|---|---|
| | Direct | Deemed Interest | Percentage (%) |
| Tan Sri Dato' Sri Zamzamzairani Mohd Isa | 5,337 | 4,270# | * |
| Datuk Bazlan Osman | 2,134 | – | * |

Note:
\# Deemed interest in TM shares held by spouse
* Less than 0.01%

Source: Telekom Malaysia.

## **Box 2.1:** National Ownership-Disclosure Requirements

An analysis of major markets around the world reveals generally accepted requirements for ownership disclosure:

- 5 percent owners
- Beneficial owners
- Directors and executives
- Includes derivatives
- Includes trusts
- Other control devices
- Rights attached to shares

Source: IFC internal analysis of regulations in Australia, Brazil, India, Singapore, South Africa, the United Kingdom, and the United States.

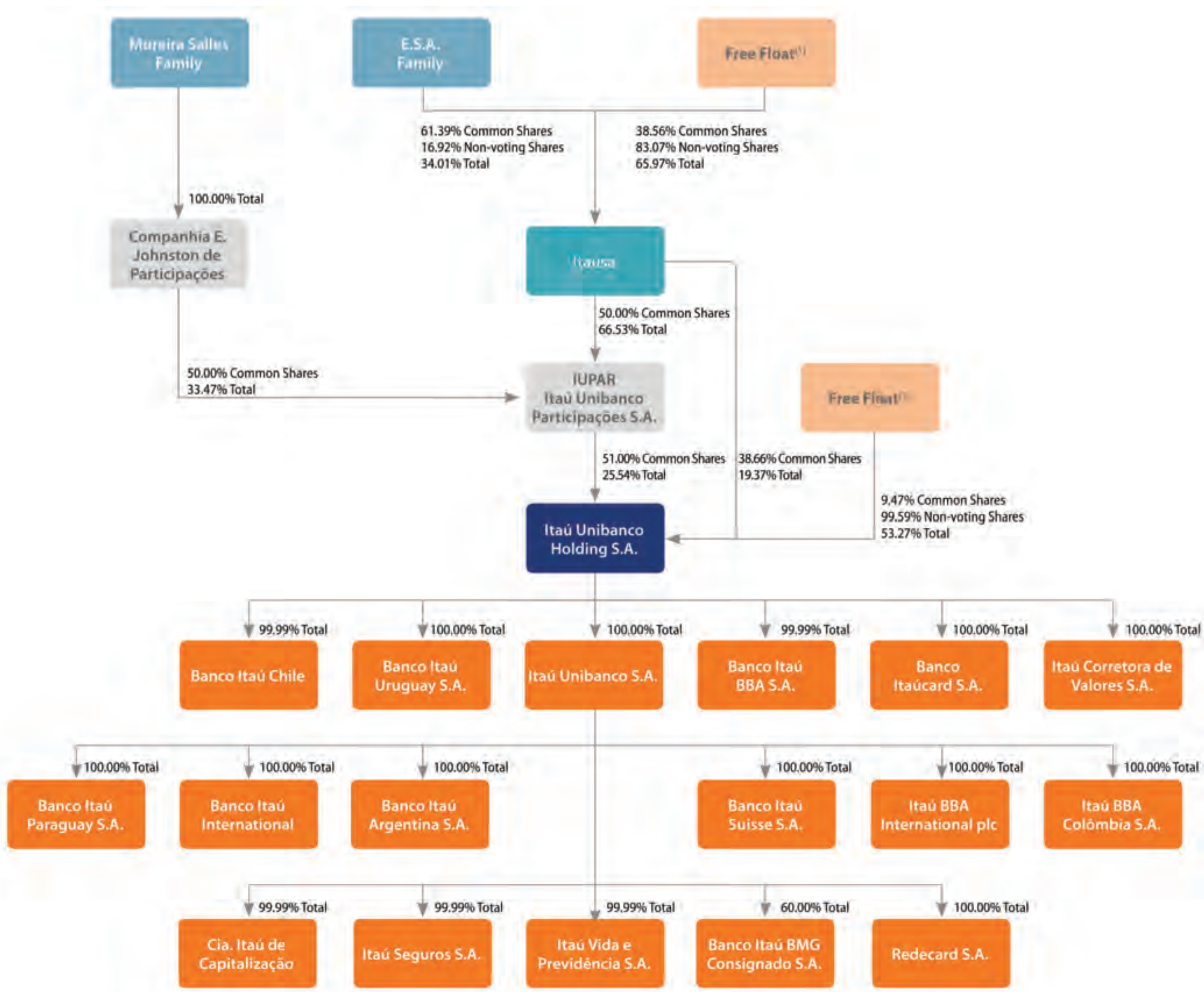
### *Groups and Control Chains*

The report should indicate whether the company is part of a group and, if so, how it fits in. It should also disclose the various intermediaries, if any, through which a controlling shareholder holds control. Example 2.26 shows how control is held in Itau Unibanco Brazil and describes the major subsidiaries of the bank.

**BEST-PRACTICE RESOURCES: Subsidiaries, Parents, Investments, and Joint Ventures**

*IFRS:* Companies are expected to disclose their parent and subsidiaries (IAS 24) as well as their investments and interests in associates and joint ventures (IAS 28, IAS 31).

## **Example 2.26:** Control Chains—Itau Unibanco Brazil 2014 Annual Reports




Source: Itau Unibanco Brazil.

### *Controlling Shareholders*

**Identity and Position.** The report should disclose the identity of controlling shareholders (individual, family, or group), how much of the company's shares they ultimately control, how control is held, and whether such shareholders are in a position to effectively dominate the company—that is, any material risks to minority shareholders associated with controlling shareholders, ownership concentration, cross holdings, and voting-power imbalances.

**Role.** The report should address the role of controlling shareholders, such as founding the company, providing capital, or other role in the management of the company.

**Succession Policy.** Disclosure of succession policies is particularly important in controlled companies. A controlling shareholder may have a specific plan or process in mind, including through inheritance or a family governance body, or through the policies of the corporate group or those applicable to state-controlled companies. The absence of succession policies in controlled companies can be a major challenge and should also be disclosed.

Example 2.27 offers a clear statement of the main shareholders, a description of the risks associated with a single dominant shareholder, and how the company protects other shareholders.

**BEST-PRACTICE RESOURCES: Ownership Disclosure**

*The G20/OECD Principles* call for disclosure on a range of ownership and control information, including the following:

- Direct and indirect holdings of major shareholders;
- Shareholdings of board members and senior executives;
- Company groups and other corporate control.

*The Financial Action Task Force Principles* (focused on money laundering and terrorism finance) encourage countries to do the following:

- Have a definition of "beneficial owner" that captures the natural person(s) who ultimately owns the shares or controls the legal person;
- Ensure that beneficial ownership and control information is adequate, accurate, current, and accessible;
- Have a legal framework that enables national authorities to participate in information exchange on beneficial ownership domestically and internationally.

**Example 2.27:** Controlling Shareholders—True Group Thailand 2015 Annual Report

The Company is backed by the Charoen Pokphand Group ("CP Group"), Asia's largest agro-conglomerate, and China Mobile, the world's largest mobile operator, with shareholding of 51% and 18% of the Group's total number of issued shares, respectively. As of 31 December 2015, True Group's total registered and paid-up capital was Baht 98,432 million. The Company's main operations are not directly and materially related to its major shareholders. It only has minor transactions in some occasions with its major shareholders.

**Risks from having majority shareholders holding more than a 50-percent stake in the Company**

As at September 5, 2014, the group of majority shareholders in True Group comprises CP Group and affiliated companies which hold combined shares of 51.3 percent of the total allocated shares. In this regard, investors may be exposed to a risk from the circumstance in which majority shareholders hold more than a 50-percent stake in True Group. This is because the group of majority shareholders may control agendas which require majority votes, such as appointments of directors. Therefore, retail shareholders may not be able to accumulate sufficient votes to check and balance agendas proposed by the majority shareholders. However, the Board of Directors focuses on operating the business guided by the principles of corporate governance. The Company has provided the opportunity for minority shareholders to propose the Annual General Meeting's agenda and nominate candidates to be selected as directors of the Board prior to the Annual General Meeting. In regard to matters related to major shareholders and transactions that may result in a conflict of interest with the Company, the Company processes the matter in accordance with procedures set forth in the "Connected Transaction Regulation" which strictly follows the legal framework.

Source: True Group Thailand.

### 2.4.2. Rights of Minority Shareholders

The report should spell out voting, board nomination, and all other rights of minority shareholders, including those related to change of control and related-party transactions. It should also disclose information on how to exercise such rights.

#### *Board Nomination and Other Minority Shareholder Rights*

The report should include information on mechanisms that allow minority shareholders to nominate members of the board. These include the following:

- *Cumulative voting*, where shareholders can cast all their votes for a single nominee for the board when the company has multiple openings;
- *Block voting*, where a large number of shareholders vote their shares in a single block;
- *Super majority*, where certain transactions require approval by a large majority of shareholders;
- *Majority of minority*, where certain transactions require approval from the majority of minority shareholders.

The report should also mention whether such rights were exercised in the past year. Example 2.28 describes the rights attached to various types of shares of Türk Telekom.

#### *Change of Control*

The report should describe the company policy on treatment of minority shareholders in the event of a change of control of the company. This includes tag-along rights, where the new controller must make an offer to purchase the shares of minority shareholders or meet other requirements—for example, that a new controller must make a tender offer concurrent with or following the change of control of the company.

Example 2.29 provides a detailed explanation of the change-of-control process for various types of shares in Türk Telekom.

**BEST-PRACTICE RESOURCES: Protection of Minority Shareholders**

*IOSCO Final Report on Protection of Minority Shareholders in Listed Issuers:* "In all jurisdictions, there are rules and regulations that protect or have the effect of protecting minority shareholders in a change of control transaction. In virtually all jurisdictions, a shareholder or third party is required to make a general offer to all shareholders to purchase its shares when that shareholder or third party acquires control of an issuer or acquires a certain percentage of the issuer's voting shares. The percentage of voting shares that triggers the mandatory offer requirement [ranges from 20% to 75%], depending on the jurisdiction.

. . . .

"In [most] jurisdictions, a substantial shareholding or control block cannot be sold to a third party at a premium without triggering any obligation to, or protection of, minority shareholders. . . . [W]hen a general offer is required to be made to all shareholders, there are minimum price requirements or rules applicable to the determination of the price."

[Note: This June 25, 2009, report is based on an analysis of regulation in Australia, Brazil, Canada, Germany, Hong Kong, Israel, Italy, Japan, Mexico, the Netherlands, Poland, Portugal, Spain, Switzerland, Thailand, Turkey, the United Kingdom, and the United States.]

**Example 2.28:** Voting and Minority Rights—Türk Telekom 2015 Annual Report

**Voting and Minority Rights**

All Shares of Türk Telekom can be transferred except for one privileged (golden) share of Group C. For the purpose of protecting the national interest in issues of national security and the economy, the following actions and resolutions cannot be taken without the affirmative vote of the holder of the C Group Privileged Share at either a meeting of the board of directors or the General Assembly. Otherwise, such transactions shall be deemed invalid.

a) Any proposed amendments to the Articles of Association;
b) The transfer of any registered Shares in the Company which would result in a change in the management control of the Company;
c) The registration of any transfer of registered shares in the Company's shareholders' ledger

Pursuant to the Articles of Association, the holder of the C Group Privileged Share appoints one member representing the Privileged Share. The C Group Privileged Share owner cannot participate incapital increases.

Source: Türk Telekom.

**Example 2.29:** Change of Control—Türk Telekom 2015 Annual Report

**Transfer of Shares**
The provisions in the Company's Articles of Association restricting transfer of shares are as follows:

Holder of Class A shares may transfer, always subject to vetoing by the Class C golden share, all or part of its shares to a third party at any time after either the expiration of the Strategic Undertaking Period, or after the date of full payment of the amount payable by the holder of Class A shares for its shares in the Company, whichever occurs later.

Holder of Class A shares may create pledge or encumbrance in favor of a financial institution over its shares which will not be subject to pledge of shares in time, as guarantee for money borrowed for the acquisition of such shares or otherwise. In the event that such pledge or encumbrance is cashed by the relevant financial institution, the same may be able to transfer the Class A shareholder's shares subject to pledge an encumbrance only upon prior written consent of the Treasure, which consent will not be unreasonably withheld.

Subject to the provisions of the following two paragraphs, holder of Class B shares may not transfer to a third party all or part of its shares during the course of the Strategic Undertaking Period without the prior consent of the holder of Class A shares, which consent will not be unreasonably withheld.

Source: Türk Telekom.

### 2.4.3. Remuneration

The report should describe the company policy on executive compensation, including components of remuneration and contractual details regarding compensation. It should also disclose actual compensation for key executives and directors and explain the shareholders' role in the approval of executive compensation.

#### *Remuneration Policy*

The report should describe the company's policy on executive compensation and, when applicable, provide details on pay-for-performance plans, including the areas of performance (financial, operational, sustainability) and whether compensation is delayed or conditional or subject to "claw back" (recovery of money already disbursed). The report should also address the role of the board (or specialized committee) and shareholders in reviewing and approving executive compensation.

Example 2.30 on the next page describes the remuneration policy for Absa Group (formerly Barclays Africa), a South African bank, and performance criteria on finance, risk, and sustainability.

The report should describe the process to establish the remuneration policy, and it should describe the role of the board (or specialized committee) and shareholders in reviewing and approving executive compensation. It should also disclose any discretion used by the remuneration or another board committee in setting actual compensation.

It is considered **BEST PRACTICE** to use KPIs to determine remuneration. They should be 1) nonfinancial as well as financial and 2) linked to strategic objectives and include next year's targets.

**BEST PRACTICE** also suggests integrating ESG considerations into criteria for determining remuneration of executives.

**BEST-PRACTICE RESOURCES: Integrating ESG Issues into Executive Pay**

*Guidance by the UN Global Compact and PRI* provides a tangible engagement tool to guide dialogue between shareholders and investee companies on ***Integrating ESG Issues Into Executive Pay*** and to help improve corporate boards' practices to the benefit of companies and their investors.

#### *Actual Remuneration*

The report should contain actual remuneration data, in tabular form, for each board member, the chief executive officer, and other key executives. The table should present the following information:

- *Salary:* Pay earned during the year includes fees paid to board members as well as salary for executives. Supplemental information should break down board member fees for chairing, attendance, and serving on particular committees.

### Example 2.30: Remuneration Policy—Absa Group (formerly Barclays Africa) 2015 Integrated Report

The Barclays Africa Long-Term Incentive Plan 2013 – 2015 is the last remaining long-term incentive arrangement and will vest in October 2016. This is a share-based plan with awards vesting after three years, subject to three specifi c performance metrics based on the 2013 to 2015 medium-term plans. The performance metrics of the scheme are:

- **Finance:** From 10% to a maximum of 60% can vest, subject to average return on risk-weighted assets of 1.99% (at threshold) to 2.99% (at maximum) on a straight-line basis.
- **Risk:** From 5% to a maximum of 30% can vest, subject to performance against the annual impairment ratio of 1.55% (at threshold) to 1.13% (at maximum) on a straight-line basis.
- **Sustainability:** Up to 10% of awards can vest, at the discretion of the GRHRC considering performance against our Balanced Scorecard.

Vesting: Based on actual 2013 – 2015 performance, 55% of the maximum vests, as detailed below:

- **Finance:** Average return on risk-weighted assets is 2.19%, therefore 20% of the maximum vests.
- **Risk:** Average impairment ratio is 1.09%, therefore 30% of the maximum vests.
- **Sustainability:** The GRHRC assessed and determined that 5% of the maximum vests.

Source: Absa Group (formerly Barclays Africa).

- *Cash bonuses:* These are additional payments linked to performance. Some jurisdictions distinguish between "short-term" (or "annual") and "long-term" (based on multiyear performance) bonuses. Supporting information should include the rationale for the bonus, such as meeting a specific target or other achievements.
- *Stock and stock-based awards:* These may be presented separately or as part of short-term or long-term performance awards. For shares, the table should describe the number, type, and market value. For options, it should describe the type and value, with an explanation of valuation presented in supporting information. As with cash bonuses, the link to performance should be explained.
- *Pension accruals:* These are the company's contribution to the recipient's defined contribution plan. For defined benefit plans, it includes any increase in the recipient's annual payments. Disclosure should also include other benefits received at retirement as well as expected retirement age and date.
- *Other monetary and in-kind benefits:* This includes company cars, housing or housing allowances, personal travel, medical benefits, and benefits that only some employees receive.

In example 2.31, Fresnillo, a Mexican mining company, details all components of remuneration for the company's main executives, including cash, short-term incentives, long-term incentives, and contribution to retirement.

*Note:* Delayed compensation (for example, share-based) is generally accounted for when granted, with a note explaining when the award vests. Conditional compensation (for instance, if certain future conditions are met) is not included in compensation totals, but it is indicated in the supporting information.

**BEST-PRACTICE RESOURCES: Remuneration Disclosure**

*The G20/OECD Principles* call for companies to disclose remuneration, preferably on an individual basis, and show the link with performance.

*IAS 24* requires disclosure of compensation for "key management personnel."

*The ICGN Global Governance Principles:* "The remuneration report should. . .describe how awards granted to individual directors and the CEO were determined and deemed appropriate in the context of the company's underlying performance in any given year. This extends to non-cash items such as director and officer insurance, fringe benefits and terms of severance packages if any."

**Example 2.31:** Actual Remuneration—Fresnillo 2015 Annual Report

| Executive directors R000 | Mike Brown | | | Mfundo Nkuhlu | | |
|---|---|---|---|---|---|---|
| | 2015 | 2014 | % | 2015 | 2014 | % |
| Cash portion of package | **6 374** | 6 056 | | **4 258** | 3 124 | |
| Other benefits | **141** | 130 | | **130** | 112 | |
| Defined-contribution Retirement Fund | **910** | 864 | | **613** | 452 | |
| **Guaranteed remuneration** | **7 425** | 7 050 | 5,3 | **5 000** | 3 687 | 35,6 |
| Cash performance incentive | **8 250** | 8 000 | | **4 750** | 4 625 | |
| Cash performance incentive (delivered in shares) | **7 250** | 7 000 | | **3 750** | 3 625 | |
| **Total STI[1]** | **15 500** | 15 000 | 3,3 | **8 500** | 8 250 | 3,0 |
| **Total remuneration[2]** | **22 925** | 22 050 | 4,0 | **13 500** | 11 937 | 13,1 |
| Value of share-based awards (face value at award) | **13 500** | 13 000 | | **8 750** | 11 750[9] | |
| **Total direct remuneration[3]** | **36 425** | 35 050 | 3,9 | **22 250** | 23 687 | (6,1) |
| Other payments[4] | | | | | | |

Source: Fresnillo Plc.

## 2.4.4. Related-Party Transactions

According to IAS 24, a related-party transaction is "a transfer of resources, services, or obligations between related parties, regardless of whether a price is charged." A related party is a person or an entity that is related to the reporting entity, such as the following:

- A board member, chief executive officer, controlling shareholder, senior executive, or their immediate family members, broadly defined to include parents, siblings, uncles, aunts, in-laws, cousins, and step-children;
- Another company linked by ownership or other investment, including joint venture;
- A company pension plan or entity linked to the company pension plan;
- A company where a board member or senior executive has joint control or significant influence.

Related-party transactions include the following:

- Sale, purchase, or supply of goods or materials;
- Sale or disposal of or purchase of property and/or assets;
- Lease of property and/or assets;
- Provision or receipt of services;
- Transfer of intangible items (for example, research and development, trademarks, license agreements);
- Provision, receipt, or guarantee of financial services (including loans and deposit services).

### *Policy and Management Process*

The report should describe the company's oversight and management systems, policies, and processes for related-party transactions. This can include the following:

- Existence of a policy on RPTs;
- How potential RPTs are identified and then vetted;
- Role of the board and committees, especially independent directors and other nonconflicted board members, including the audit committee, in approving RPTs, and of shareholders in approving material RPTs;
- How to handle a situation where a board member is conflicted;
- Whether different transactions have different approval procedures;
- Shareholder approval and third-party evaluations;
- Conflicts of interest resulting from RPTs, and how they are managed.

Example 2.32 on the following page shows how Fresnillo, a Mexican mining company, manages RPTs through monitoring of directors' interests, negotiations by the executive committee, and approval by independent directors.

**Example 2.32:** Managing RPTs—Fresnillo 2015 Annula Report

## Identifying Directors' interests

| Process | How this is managed | Responsibility |
|---|---|---|
| Monitoring of Directors' interests | If a Director is interested in a company which could potentially enter into transactions with a Fresnillo plc Group company, the Board will normally consider that interest under its arrangements for authorising conflicts of interest under s175 of Companies Act. | Directors |

## Managing a related party transaction

| | | |
|---|---|---|
| **Proposed transaction** ↓ | Ongoing monitoring of Directors' interests and related parties of the Company provides the information to determine if a related party approval is required for a proposed transaction. | |
| Contract negotiation and verification ↓ | The Executive Committee will seek to ensure that the best possible terms are achieved for a proposed transaction and that they are verified by industry benchmarking reports or independent valuation/ assessment. | Fresnillo management and Executive Committee |
| Financial scrutiny ↓ | The Audit Committee reviews the key terms of major transactions which are verified as to price and quality with external consultants or independent benchmarking where possible. | Audit Committee review |
| Independent Director approval | Under the Relationship Agreement, the independent Directors must approve any transaction with the Peñoles Group and its associates without the non-independent Directors voting. | Independent Directors |

Source: Fresnillo.

### *Details on RPTs*

For all material RPTs concluded or contemplated during the past year, the report should disclose the following information:

- Name of the related party;
- Type of related party (parent, entity with joint control of or significant influence over the company, subsidiary, associate, joint venture, key management personnel, other related parties);
- Amount of the transaction;
- General type of the transaction (sale of goods, provision of services, loan, and so forth);
- Any outstanding balances, contingencies, or bad debts or impairments involving the transaction.

For significant transactions, it might be useful to include additional details:

- Terms of the transaction (interest rate and duration for a loan, cost per hour, and hours of consulting);
- Reasonableness (market benchmarks, transaction process such as competitive tender);
- Third-party evaluation of the transaction, if any.

**BEST-PRACTICE RESOURCES: RPT Disclosure**

*The IFRS IAS 24 Related Party Disclosures* requires disclosure of the nature of the related-party relationship as well as information about those transactions and outstanding balances, including commitments, necessary for users to understand the potential effect of the relationship on the financial statements.

*The G20/OECD Principles* state that it is "essential to fully disclose all material related party transactions and the terms of such transactions to the market individually." The Principles also suggest disclosing "the policy/criteria adopted for determining material related party transactions."

*The ICGN Global Governance Principles:* "The process for reviewing and monitoring related party transactions should be disclosed. For significant transactions, a committee of independent directors should be established to vet and approve the transaction. This can be a separate committee or an existing committee comprised of independent directors, for example the audit committee. The committee should review significant related party transactions to determine whether they are in the best interests of the company and, if so, to determine what terms are fair and reasonable. The conclusion of committee deliberations on significant related party transactions should be disclosed in the company's annual report to shareholders."

**LEADERSHIP PRACTICES** (Matrix Level 4) suggest that related-party transactions over 2.5 percent of net assets or over $150,000 are subject to shareholder approval or stricter requirements.

Example 2.33 presents summary information on all RPTs of Sappi Group, a South African pulp and paper company, including counterparts and type of transaction.

The report should describe the effect of the transaction on the financial situation of the company and/or the potential conflict of interest it creates with key officers or directors in the company.

Although not sufficient by itself, summary information can be useful to help the reader understand the total amount and broad nature of RPTs. It can be used to aggregate the same type of transactions and summarize small transactions with the same related party. Example 2.34 on the next page provides summary information on RPTs for Reliance Industries, an Indian conglomerate.

**Example 2.33:** Details on RPTs—Sappi Group 2016 Annual Financial Statements

| | Sales of goods | | | Purchases of goods | | | Amounts owed by related parties | | Amounts owed to related parties | |
|---|---|---|---|---|---|---|---|---|---|---|
| (US$ million) | **2016** | 2015 | 2014 | **2016** | 2015 | 2014 | **2016** | 2015 | **2016** | 2015 |
| **Joint ventures and associates:** | | | | | | | | | | |
| – Sapin SA[1] | **–** | 0.4 | 0.6 | **–** | 24.9 | 31.2 | **–** | – | **–** | 0.8 |
| – proNARO GmbH | **–** | – | – | **125.8** | 138.3 | 162.7 | **–** | – | **1.2** | 5.9 |
| – Umkomaas Lignin Proprietary Limited | **4.8** | 6.3 | 7.2 | **0.1** | – | – | **0.5** | 0.7 | **–** | – |
| – Papierholz Austria GmbH | **–** | – | – | **82.5** | 60.1 | 115.7 | **–** | – | **4.8** | 4.3 |
| | **4.8** | 6.7 | 7.8 | **208.4** | 223.3 | 309.6 | **0.5** | 0.7 | **6.0** | 11.0 |

Source: Sappi Group.

**Example 2.34:** Summary Information on RPTs—Reliance Limited 2015 Annual Report

| Sr. No. | Nature of Transactions (Excluding Reimbursements) | Subsidiaries/ Beneficiary | Associates | Key Managerial Personnel/ Relative |
|---|---|---|---|---|
| 1. | Purchase of Fixed Assets | 2,302<br>*2,434* | 237<br>*264* | -<br>- |
| 2. | Purchase / Subscription of Investments | 38,085<br>*11,506* | -<br>- | -<br>- |
| 3. | Sale / Redemption of Investments | 422<br>*150* | -<br>- | -<br>- |
| 4. | Capital Advance Given/ (Returned) | -<br>- | -<br>*(8)* | -<br>- |
| 5. | Net Loans and Advances, Deposits given/ (Returned) | (11,913)<br>*133* | 43<br>*166* | -<br>- |
| 6. | Revenue from Operations | 24,925<br>*24,395* | 301<br>*428* | -<br>- |
| 7. | Other Income | 1,721<br>*1,536* | 17<br>*27* | -<br>- |
| 8. | Purchases / Material Consumed | 2,201<br>*1,562* | 631<br>*267* | -<br>- |
| 9. | Electric Power, Fuel and Water | -<br>- | 1,719<br>*1,579* | -<br>- |
| 10. | Hire Charges | -<br>- | 585<br>*622* | -<br>- |

Source: Reliance Industries Limited.

## 2.5. Governance of Stakeholder Engagement

The IFC Corporate Governance Matrix includes best practices in governance of engagement with stakeholders.

**CONSULT THE MATRIX**

The Matrix can be used to gauge a company's level of progress with its governance of stakeholder engagement. The Toolkit recommends the disclosure of information related to Levels 1–3 of the Matrix, which corresponds to good international practices. Guidance is also provided for disclosure of leadership practices, consistent with Level 4 of the Matrix. (See Table 2.5.)

### 2.5.1. Commitment, Policy, and Strategy

The report should describe the company's policy and strategy for stakeholder engagement, including the following:

- Stakeholder identification;
- Stakeholder analysis to identify the needs and interests of diverse stakeholders;
- Differentiated approaches for priority groups;
- Iterative disclosure and consultation;
- Grievance mechanism and reporting;
- Management-level mechanisms to raise and resolve consistent stakeholder issues.

The report should also note whether stakeholder engagement extends to suppliers and contractors through its policies or tender requirements.

**LEADERSHIP PRACTICES** (Matrix Level 4) suggest that stakeholder engagement be visible to staff, contractors, suppliers, and collaborators through a publicly disclosed code of conduct setting out expectations for stakeholder engagement and human rights. The report should mention the existence of such a code.

### 2.5.2. Stakeholder Identification

The report should describe the constituencies that have been identified as key stakeholders of the company. It should also describe the process of identification of material stakeholders. Based on the size and impact of the company, stakeholders typically include the following:

- Local communities directly affected by the company;
- Customers and regulators;
- Workers, contractors, and primary-supply-chain workers;
- Neighboring projects;
- International NGOs and CSOs.

In good international practices (Matrix Level 3), companies should adopt a formal stakeholder-mapping

**Table 2.5:** IFC Corporate Governance Matrix—Governance of Stakeholder Engagement

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Stakeholder Mapping** | 1. Ad hoc stakeholder-identification, including workers, customers, regulators, and the locally Affected Community. | 1. Key stakeholders identified also include local nongovernmental organizations (NGOs) and civil society organizations (CSOs). | 1. Formal stakeholder-mapping process and expanded definition of stakeholders includes contracted workers, primary- supply-chain workers, neighboring projects, and international NGOs and CSOs. | 1. Senior executive responsible for stakeholder relationships, including ensuring integration with strategy and target setting. |
| **Stakeholder Engagement Policy** | | 2. Established Stakeholder Engagement (SE) policy and procedures. | 2. SE policy and strategy includes procedures with stakeholder analysis, differentiated approaches for priority groups, iterative disclosure and consultation requirements, and reporting.[a] | 2. Commitment to SE visible to staff, contractors, suppliers, and collaborators via codes of conduct setting out expectations for stakeholder interactions and human rights.<br>3. SE practices incorporated into requirements for primary suppliers.<br>4. SE activities and outcomes included in board decision making and external reporting procedures. |
| **Worker Grievance Mechanism** | 2. HR policy and procedures for worker engagement. | 3. Basic grievance mechanism for workers. | 3. Management responds to grievances from workers and contracted workers on a regular basis. | 5. Issues raised through grievance mechanism for workers are analyzed and resolved with the participation of a worker representative.<br>6. The board is informed about grievance outcomes and trends on a regular basis. |
| **Affected Communities Grievance Mechanism** | 3. Informal response to stakeholder requests and concerns. | 4. External Communications Mechanism for stakeholder questions and complaints, and if there are Affected Communities, a grievance mechanism is established. | 4. External and publicly accessible communication procedure.[b]<br>5. Grievance mechanism facilitates the resolution of concerns from Affected Communities.<br>6. Designated Affected Communities engagement personnel have clearly defined responsibilities, training, and reporting lines to senior management and the board.<br>7. SE policy incorporated into requirements for contractors.<br>8. Unresolved stakeholder issues require a management action plan. | 7. Periodic analysis of grievances to identify trends and root causes is conducted by senior management.<br>8. Senior management participate actively in international industry discussions on related topics.<br>9. SE and reporting consistent with international standards (AA 1000 Standards on Stakeholder Engagement and Accountability Principles and ISO 26000). |

[a] Consult with Social Specialist to determine quality of SE policy, strategy, and procedures, if applicable.

[b] Consult with Social Specialist to determine whether communication procedure is adequate to (a) receive and register external communication from the public; (b) assess issues raised and determine response; (c) provide and document responses, if any; and (d) adjust the management program, as appropriate and if applicable.

process. They also should adopt an expanded definition of stakeholders to include contracted workers, primary-supply-chain workers, neighboring projects, and international NGOs and CSOs.

In **LEADERSHIP PRACTICES** (Matrix Level 4), a senior executive should be responsible for stakeholder relationships and should ensure integration with strategy and target setting.

The report should also explain the issues associated with each category of stakeholders. In Example 2.35, Vopak, a Dutch transportation company, describes its key stakeholders and the types of issues that affect them.

### 2.5.3. Management and Governance

The report should note whether employees or executives, or both, are responsible for stakeholder engagement, including stakeholder engagement activities and outcomes.

The report should describe the role of the board in overseeing the management of stakeholder engagement, including grievance mechanisms and company dialogue with key stakeholders. This includes ensuring that the grievance mechanisms are effective, that there is no retaliation, and that the number of grievances reflects actual incidents rather than just how comfortable workers or other stakeholders are with using these mechanisms.

**Example 2.35:** Stakeholder Identification—Vopak Annual Report 2016

**Stakeholder groups**

We reassessed the stakeholders who can impact or influence our business and those that could be impacted by our operations. This longlist of various stakeholders was then categorized into groups based on their common interest. As a result, a total of nine stakeholder groups were identified:

| Stakeholder group | Expectations | Key topics |
|---|---|---|
| Customers | Increasingly put sustainability high on their agenda and require Vopak, as an important link in their supply chain, to at least align its sustainability policy with theirs. | • Business ethics and integrity<br>• Process safety<br>• Occupational health and safety |
| Business partners | Looking for long-term relationships to realize growth based on mutual trust and value creation. | • Application of best practices<br>• Process safety<br>• Customer acceptance and continuation |
| Authorities | Issue stricter regulations and increase inspections for the industry as a whole. | • Business ethics and integrity<br>• Process safety<br>• VOC emissions, Soil and groundwater pollution and Water pollution |
| Financial and capital markets | Increasingly take a long-term appreciative view of companies that aim for sustainable profitability. | • Financial performance<br>• (Cyber) security threats<br>• Process safety |
| Neighbors and local communities | Increasingly require Vopak to engage with them to address issues such as stench and odors. | • VOC emissions, soil and groundwater pollution and water pollution<br>• Business ethics and integrity<br>• Process safety |
| NGOs | NGOs expect Vopak to be a responsible, transparent, cooperative and trustworthy partner. | • VOC emissions, Soil and groundwater pollution and Water pollution<br>• Business ethics and integrity<br>• Process safety |
| Employees | Value a company that cares, helps to develop their talents and offers training programs to develop the full potential of every individual. | • Business integrity and ethics<br>• Financial performance<br>• (Cyber) security threats |
| Senior management | Determines the overall long-term strategy on our 'License to Operate' and our expansion plans. | • Business ethics and integrity<br>• Process safety<br>• (Cyber) security threats |
| Suppliers | Suppliers of assets value long-term relationships. Suppliers of services (e.g. contractors) expect a safe and healthy workspace and fair treatment. | • Occupational health and safety<br>• Process safety<br>• Business ethics and integrity |

Source: Vopak.

**BEST-PRACTICE RESOURCES: Stakeholder Engagement**

*The AA1000 Stakeholder Engagement Standard* is a framework for assessing, designing, implementing, and communicating stakeholder engagement. The purpose of the standard is to establish the benchmark for good-quality stakeholder engagement.

*IFC Performance Standard 1* incorporates stakeholder engagement as the basis for building strong, constructive, and responsive relationships that are essential for the successful management of a project's (or company's) environmental and social impacts. It requires a more robust and extensive stakeholder-engagement process than many other management system standards to establish and maintain a constructive relationship with a variety of external stakeholders, particularly local communities directly affected by the project.

**LEADERSHIP PRACTICES** (Matrix Level 4) suggest that stakeholder engagement policies and procedures be integrated into requirements for contractors and primary suppliers.

### 2.5.4. External Communication and Grievance Mechanisms

The report should describe the mechanisms that the company has in place to respond to stakeholders' questions or complaints in a timely fashion. This includes grievance and whistleblowing mechanisms for both external and internal stakeholders.

The report should describe whistleblowing policies and mechanisms, types of complaints received, and outstanding matters. It can be useful to have KPIs for the number of complaints submitted and how many were resolved.

Good international practices (Matrix Level 3) suggest that issues raised by workers through grievance mechanisms be resolved with the participation of a worker representative. Grievances and complaints, as well as the company's responses, should be documented to ensure resolution of concerns, especially for issues related to Affected Communities, and this documentation should be updated at least annually. Unresolved stakeholder issues should require a management action plan.

In **LEADERSHIP PRACTICES** (Matrix Level 4), external communication and stakeholder engagement should be consistent with internationally accepted standards, such as AA1000 Stakeholder Engagement Standard, Accountability Principles, or ISO 26000. Communication should be in an understandable format and language.

Example 2.36 on the next page describes the management of stakeholder engagement at Tata Motors, an Indian auto company. It provides details on engagement mechanisms as well as frequency and method of engagement for key stakeholder groups.

In general, periodic analyses of grievances to identify trends and root causes should be conducted by senior management who are well versed in international industry stakeholder engagement practices and topics.

### 2.5.5. Integrating Sustainability

Regular stakeholder engagement can help ensure that sustainability targets are sufficiently ambitious and that emerging issues are properly understood and appropriately managed. This interaction with stakeholders helps companies produce reporting that is complete and credible.

**BEST PRACTICES** suggest that stakeholder interests should be factored into the setting of sustainability strategies or integrated into management strategies and management priorities and processes.

**BEST-PRACTICE RESOURCES: Grievance Mechanisms**

*The IFC Performance Standards* incorporate external and internal grievance mechanisms:

- ***External grievance mechanisms*** must be established to receive and facilitate resolution of Affected Communities' concerns and grievances about the client's environmental and social performance (Performance Standard 1).
- ***Internal grievance mechanisms*** must be provided for workers—including contracted workers—to raise workplace concerns without retribution (Performance Standard 2).

**Example 2.36:** Stakeholders and Sustainability—Tata Motors 2015–2016 Annual Report

| Stakeholder Engagement at TML | | | | |
|---|---|---|---|---|
| **Stakeholder Groups** | **Engagement Mechanisms** | **Frequency of Engagement** | **Key Concerns** | **Feedback assessment** |
| **Employees** | Sunrise and Sunset meetings; Horizontal Communications; Horizontal deployment; Weekly/Monthly reviews improvements; Displays; HR Forum; Q12 Tool; Skip Level Meets; Town Halls; Focused Group Discussions | Annual; Quarterly; Monthly; Weekly | Communicating policy decisions and seeking feedback; communicating performance; Media Reports, Labour Issues | Employee satisfaction survery; Appraisels; Internal Surveys |
| **Communities** | Meetings with local community; public hearing | Quarterly; Daily | Community development initiatives communication; capturing societal concerns | Minutes of meeting; action plans; feedback letters |
| **Suppliers/ Service Providers** | Technology Days, Supplier meets, Joint programmes, Kaizen events, Participation in NPI, Competitor data and analysis; Vendor Council; Vendor mentoring | Annual; Quarterly | Delivering quality products; time management; compliance to Tata Motor's code of conduct and other policies; | Vendor rating; Board reviews; Vendor Satisfaction Surveys |
| **Opinion Leaders** | One-to-one meetings | Need based | Following the regulations, complying with the industry standards | Minutes of meeting, action plans |
| **Media** | Regular interactions | Ongoing | Communicating company's performance and seeking feedback | Minutes of meeting, action plans |
| **Dealers and Service Station** | Dealer meets. Joint programmes, Kaizen events, Participation in QFD and NPI, Competitor data and analysis, Special training Programmes; Dealers Council; Dealer visits; Audits | Annual; Quarterly; Daily | Building capacity and technical know-how; improving and delivering better response to customers; | Dealer Satisfaction Survery |
| **Customers** | Customer meets; Key account process; Surveys; Feedback calls, Training Forums; Direct Visits | Need based | Understanding product feedback; redress complaints; suggestions on product development; | Customer Satisfaction Index; JD Power Survery |
| **Investors and Shareholders** | Investor meets; Investor calls; Road Shows, Shareholder / Investor Grievance Forum, Ethics Committee | Annual; Quarterly; Need based | Financial performance; broad future strategies; feedback and addressal of concerns | Minutes of meeting; action plans |
| **Government Authorities** | One-to-one meetings; Meeting in Industry Forums | Need based | Relationship building; appraising the government on industry constraints; discussions on way forward | Minutes of meeting; action plans |

Source: Tata Motors.

# 3. Financial Position and Performance

The performance report presents a broad range of financial, operational, and sustainability information, linking performance to the wider strategy and how the company creates value going forward.

The financial statements provide a historical record of the financial activities and the position of a business at a given point, with information on income, cash flow, assets, liabilities, and owners' equity. These are developed according to the International Financial Reporting Standards (IFRS) or other prescribed national standards.

Sustainability statements are mostly voluntary and provide a summary view of performance indicators that the company tracks as part of its management of key sustainability issues.

**Model Structure of Annual Report**

**1. Strategy**
- Business Model and Environment
- Strategic Objectives
- Risk Analysis and Response
- Sustainability Opportunities and Risks
- Introducing Key Performance Indicators

**2. Corporate Governance**
- Leadership and Culture: Commitment to ESG
- Structure and Functioning of the Board of Directors
- Control Environment
- Treatment of Minority Shareholders
- Governance of Stakeholder Engagement

**3. Financial Position and Performance**
- Performance Report
- Financial Statements
- Sustainability Statements

In good international practice (Matrix Level 3), the audit committee of the board should oversee financial and nonfinancial reporting. This includes any annual report information related to environmental, social, and governance matters and sustainability or to a separate sustainability report if there is one. Or an E&S/sustainability committee of the board can review the ESG information in the annual report.

## 3.1. Performance Report

The performance report presents an analysis of annual performance and the company's financial and non-financial year-end position, including sustainability performance. It includes a management discussion of how the company has performed and a presentation of key performance indicators. It provides an introduction and context for the financial and sustainability statements, which formally present the company's year-end position and performance.

### 3.1.1. Discussion of Financial and Sustainability Performance

The report should include a management discussion of the company's performance and establish a clear relationship between financial performance and the *drivers* of financial performance, including sustainability information.

### *Financial Results*

The performance report should include an in-depth discussion of financial results, including performance against key performance indicators and more detailed financial results that underlie the KPIs. It also should include narrative text that explains financial results relative to the company's strategy, business model, business environment, and business segments.

### *Financing Needs*

The report should contain information on financing needs, plans, and practices, including liquidity and capital-expenditure requirements for the coming year. More generally, it can be useful to present how cash flows through the organization as well as the financing implications of current plans, including increases or decreases in the use of outside financing.

**BEST-PRACTICE RESOURCES:**
**Management Reports and KPIs**

International disclosure requirements emphasize the importance of narrative reporting that represents the voice of management—for example, the Strategic Report in the United Kingdom and the Management Discussions and Analysis in the United States.

*The UK Companies Act of 2006* provides that the business review "must, to the extent necessary for an understanding of the development, performance or position of the company's business, include:

- analysis using financial key performance indicators, and
- where appropriate, analysis using other key performance indicators, including information relating to environmental matters and employee matters."

### *Investments and Initiatives*

While major activities and investments are usually introduced in the strategy section of the report, the performance report can provide more in-depth information, including the achievements (actual and hoped for) of the investment or activity—performance in past years, how it is now paying off, and how it fits into the wider strategy.

Performance reporting can also be useful for discussing challenges or risks associated with the investment or activity, and how they will be resolved. Sometimes, more detailed descriptions of certain key projects or investments follow the general discussion of performance.

### *Intangibles*

Much of the company's performance may depend on resources that are not found in the financial statements. In fact, much of the market value of today's companies is attributed to intangibles (Ocean Tomo 2015). Performance reporting should note any nonfinancial resources that have had a material impact on performance. These can include the company's brand and reputation, natural resources, human resources, research and development, market position, and intellectual capital and property, including patents, copyrights, and trademarks.

### *Material Changes or Trends*

The report should include a discussion of material changes in the financial situation or financial impact of ESG matters and KPIs—what changed, why it changed, and whether the change is due to an unusual event or a long-term trend. When discussing notable quantitative results, it can be helpful to also present the driving forces in quantitative terms.

### *Forward-Looking Information*

The report should provide forward-looking guidance on how the company will perform and how it plans to add value in the future. In Example 3.1,

**BEST-PRACTICE RESOURCES:**
**International Reporting Standards**

*The G20/OECD Principles* sstate that "investors are particularly interested in information that may shed light on the future performance of the enterprise." The Principles also note that company objectives should be disclosed together with financial information, and they encourage providing a discussion of that financial information and some measures of nonfinancial performance.

*The Financial Reporting Council (United Kingdom) Guidance on the Strategic Report* includes the following elements, among others:

- Analysis of annual performance, position at year end, KPIs, both financial and nonfinancial;
- A description of the principal risks and uncertainties facing the company, trends, and factors likely to affect the future performance.

*The ICSA Guidance Note,* in its contents for the annual report of a U.K. company, includes the following:

- Analysis of
  - -Development and performance of the company's business during the financial year,
  - -The position of the company at the end of the year;
- Trends and factors likely to affect the future development, performance, or position of the business, to the extent necessary for an understanding of the business.

**Example 3.1:** Forward-Looking Guidance—Novo Nordisk Annual Report 2016

# OUTLOOK 2017

The current expectations for 2017 are summarised in the table below:

| EXPECTATIONS ARE AS REPORTED, IF NOT OTHERWISE STATED | EXPECTATIONS 2 FEBRUARY 2017 |
|---|---|
| **Sales growth** | |
| • in local currencies | -1% to 4% |
| • as reported | Around 2 percentage points higher |
| **Operating profit growth** | |
| • in local currencies | -2% to 3% |
| • as reported | Around 2 precentage points higher |
| **Net financials** | Loss of around DKK 2.4 billion |
| **Effective tax rate** | 21% - 23% |
| **Captial expenditure** | Around DKK 10.0 billion |
| **Depreciation, amortisation and impairment losses** | Around DKK 3.0 billion |
| **Free cash flow** | DKK 29 - 33 billion |

Source: Novo Nordisk.

Novo Nordisk, a Danish pharmaceutical company, presents its 2017 outlook for financial key performance indicators.

### *Sustainability Performance*

Reporting on sustainability performance should provide a context for how well the company is meeting sustainability objectives, including managing environmental and social opportunities and risks and its relationships with key stakeholders.

The report should provide information on the results of its management of core E&S issues, including efforts to mitigate their impact. For example, if the company is involved in land acquisition and involuntary resettlement, the report should describe steps to avoid long-term hardship and impoverishment for the Affected Communities. It should also describe environmental damage and adverse socioeconomic effects in areas where communities have been displaced.

If the company has determined that it faces specific sustainability issues in environmentally or socially sensitive areas, the performance report should provide a qualitative description of the steps the company has taken to avoid or minimize those specific risks.

Performance information should be based as much as possible on quantitative measures (or KPIs), either of the company's impact or its efforts to avoid, reduce, or mitigate the impact. It should be complemented by qualitative information to explain the context, trends, and information not conveyed by numbers. When performance cannot be quantified, the report should provide a description of efforts and results.

In good international practice (Matrix Level 3), the audit committee or E&S/sustainability committee of the board should oversee financial and nonfinancial reporting and audit, including the ESG information in the annual report.

**LEADERSHIP PRACTICES** (Matrix Level 4) demand that nonfinancial disclosure be in accordance with the highest international standards, such as GRI, IIRC, and SASB standards, and that ESG information has been independently reviewed.

## 3.1.2. Key Performance Indicators

The performance report should present the company's results on its KPIs (introduced in the *strategy* section of the report) over the past three completed fiscal years. The scope of the reported information should be clear, especially if it differs from year to year. Any changes to the coverage of information should be explained.

Reporting on KPIs that are set during the strategy-setting process creates a performance report that is highly relevant and unique to the company's business model and context, its strategy, and the material risks that it faces. (See "Using KPIs in the Strategy-Setting Process" in ***1.2. Strategic Objectives***, page 22 of this Toolkit.)

### *Financial KPIs*

Financial KPIs are ratios and other measures of the performance of a company in managing its financial capital and creating a profit for investors. These cover some of the line items of financial statements, including sales, EBITDA (earnings before interest, depreciation, and amortization), free cash flows, and EPS (earnings per share), as well as other commonly used financial measures or ratios, such as P/E (price-to-earnings) ratio and TSR (total shareholder returns).

Example 3.2 shows reporting on financial KPIs by Rio Tinto, the Anglo-Australian mining company, with a detailed explanation of the method of calculation and relation to strategy.

### *Operational KPIs*

Operational KPIs measure the company's operational performance—that is, how efficiently it conducts its

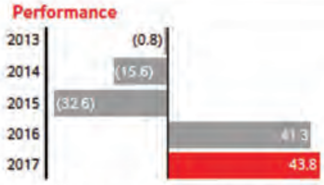
**Example 3.2:** Financial KPIs—Rio Tinto 2017 Annual Report

**Total shareholder return (five years) (TSR)[(a)]**

%

**Relevance to strategy**
The aim of our strategy is to maximise shareholder returns through the cycle. This KPI measures performance in terms of shareholder value over a period of time. We also measure relative TSR performance against the Euromoney Global Mining Index of peers and the MSCI World Index of large global companies.

**Performance**




Rio Tinto's TSR performance from 2013 to 2017 was principally impacted by movements in commodity prices and changes in the global macro environment. There was a significant recovery in the share prices of Rio Tinto plc and Rio Tinto Limited in 2017, driven by stronger pricing across most commodities and a steady improvement in the global economic outlook. The Group outperformed the Euromoney Global Mining index of peers over the five-year period by 34 percentage points but significantly underperformed the MSCI World Index over the same time frame.

**Definition**
TSR combines share price appreciation, dividends paid and reinvested, to show the total return to the shareholder.

**Associated risks**
- Market risks, such as variability in commodity prices and exchange rates.
- Stakeholder risks, including the actions of joint venture partners, third parties and governments.

**Link to executive remuneration**
Relative TSR over a five-year period, measured equally against the Euromoney Global Mining Index and the MSCI World Index, are the performance measures included in long-term incentive plans for executives.

**Forward plan**
Management will continue to focus on generating free cash flow from operations with the intention of maximising shareholder value, through an appropriate balance of cash returns to shareholders and investment in the business.

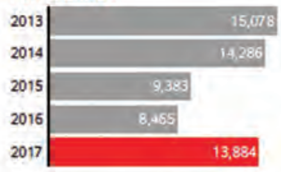
**More information**
► 94

**Net cash generated from operating activities[(b)]**

US$ millions

**Relevance to strategy**
Net cash generated from operating activities is a measure demonstrating conversion of underlying earnings to cash. It measures our ability to generate cash from our businesses to fund investment, reduce our debt and return cash to shareholders.

**Performance**




Net cash from operating activities of US$13.9 billion was 64 per cent higher year-on-year, primarily due to higher prices partly offset by an increase in taxes paid driven by higher profits.

**Definition**
Net cash generated from operating activities represents the cash generated by the Group's consolidated operations, after receipt of dividends from equity-accounted units and payment of interest, taxes, and dividends to non-controlling interests in subsidiaries.

**Associated risks**
- Market risks, such as variability in commodity prices and exchange rates.
- Operations, projects and people risks, including delivery of productivity improvements.
- Stakeholder risks, including the actions of joint venture partners, third parties and governments.

**Link to executive remuneration**
Net cash generated from operating activities is a component of the free cash flow financial performance measure included in the short-term incentive plan for executives. In the longer term, the measure influences TSR which is included in long-term incentive plans for executives. Refer to the Remuneration Report on page 80.

**Forward plan**
The Group is targeting US$5 billion in additional free cash flow from its five-year productivity programme from 2017 to 2021.

**More information**
► 114

Source: Rio Tinto.

operations and delivers its products and services. Operational KPIs can be both generic and industry-specific. For example, *capacity and utilization*, *customer satisfaction*, *employee satisfaction*, and *employee turnover* are common indicators of performance across most industries. Examples of industry-specific KPIs include the *reserve replacement ratio* for oil and gas companies, *churn rate* in telecommunications, *sales per square foot* for retail, and *assets under management* for finance.

In Example 3.3, SAB Miller, a U.K. food and beverage company, presents—in a single page—its strategy, KPIs, and recent performance, providing a clear picture of what is considered material. The specific goals give a strong indication of future prospects and challenges. This snapshot is supported by narrative discussions of the firm's regionally oriented strategy and business model.

### *Sustainability KPIs*

The report should provide a summary of performance on the environmental and social KPIs that are most relevant (or "material") to the company. The summary of KPIs in the performance report should be linked to—and provide an explanation of and context for—the sustainability statements, which provide a more comprehensive set of environmental, social, and governance metrics. (For more information on linking the summary of KPIs in the performance report to the sustainability statements, see ***3.3. Sustainability Statements***, page 109 of this Toolkit, including the tables in that section. For further disclosure guidance on KPIs, see ***1.5. Introducing Key Performance Indicators***, page 49 of this Toolkit.)

**Example 3.3:** Snapshot of KPIs: Financial and Commercial and Strategic Goals—SAB Miller 2016 Annual Report

## Measuring our progress

| What we measure | Why we measure | How we have performed | | |
|---|---|---|---|---|
| **Financial goal** | | **2016** | 2015 | 2014 |
| Total shareholder return in excess of the median of our peer group over five-year periods | To monitor the value created for our shareholders over the longer term relative to alternative investments in the drinks industry, in line with our business performance goal | **13 % pts** | 36 % pts | 98 % pts |
| Growth in adjusted earnings per share | To determine the improvement in earnings per share for our shareholders at reported exchange rates | **-6%** | -1% | 2% |
| Growth in adjusted earnings per share (constant currency) | To determine the improvement in earnings per share for our shareholders at constant exchange rates | **12%** | 5% | 9% |
| Free cash flow | To track cash generated to pay down debt, return to our shareholders and invest in acquisitions | **US$2,969m** | US$3,233m | US$2,563m |
| What we measure | Why we measure | How we have performed | | |
| **Commercial and strategic goals** | | **2016** | 2015 | 2014 |
| The proportion of our total lager volume from markets in which we have no. 1 or no. 2 national market share positions | To gain an overall picture of the relative strength of our market positions | **94%** | 94% | 95% |
| The proportion of group EBITA from developing economies | To assess the balance of our earnings exposure between regions of the world economy with highest growth potential and more developed regions | **69%** | 72% | 72% |
| Organic growth in total beverage volumes | To track the underlying growth of our business | **2%** | 1% | 2% |
| Group net producer revenue growth (organic, constant currency) | To assess the underlying rate of growth in net sales value of our brand portfolios | **5%** | 5% | 3% |
| Net producer revenue growth in premium brands (constant currency) | To monitor progress in building our portfolio of global and local premium brands | **12%** | 8% | 3% |
| EBITA growth (organic, constant currency) | To track our underlying operational profit growth | **8%** | 6% | 7% |
| EBITA margin progression (organic, constant currency) | To monitor the rate of growth in our underlying operational profitability | **60 bps** | 30 bps | 90 bps |
| Hectolitres of water used at our breweries per hl of lager produced | To gauge our progress in reducing the amount of water used in our breweries | **3.2 hl/hl** | 3.3 hl/hl | 3.5 hl/hl |
| Fossil fuel emissions from energy use at our breweries per hl of lager produced | To assess progress towards reducing fossil fuel emissions at our breweries | **8.9 kgCO$_2$e/hl** | 9.4 kgCO$_2$e/hl | 10.3 kgCO$_2$e/hl |
| Cumulative financial benefits from our cost and efficiency programme | To track the cost and efficiency savings from the programme to leverage our skills and scale | **US$547m pa** | US$221m pa | n/a[1] |

[1] Not applicable.

Source: SAB Miller.

Example 3.4 illustrates how CEMEX, a construction company in Mexico, presents sustainability KPIs in its annual reports.

## 3.2. Financial Statements

Financial statements are important for public accounting and accountability. Unlike financial KPIs, which are unique to the company's business model and context, financial statements present an account of performance that is more standardized according to generally accepted accounting practices that are comparable across companies and industries.

The preparation and presentation of financial statements is often strictly regulated at the national level and therefore should be made in accordance with national corporate or securities laws and nationally recognized general principles of accounting. Typically, countries have additional requirements for large companies listed on stock exchanges. For example, they may require listed companies to prepare financial statements according to nationally accepted accounting principles—such as GAAP in the United States and a national version of IFRS in most other countries.

The IFRS for SMEs Standard, on the other hand, is less demanding and tailored to the information needs of lenders, creditors, and other stakeholders of SMEs who are interested primarily in information about cash flows, liquidity, and solvency.

### 3.2.1. General Guidance

All financial statements and reporting should be prepared and presented in accordance with internationally recognized accounting principles, such as the International Financial Reporting Standards. Typically, financial statements are presented with comparative figures from the company's past two fiscal years.

**BEST PRACTICES** and regulation often require a statement by senior management (typically the chief financial officer or chief executive officer) accepting accountability for preparation of the financial statements and endorsing the financial statements.

Financial statements are designed to measure two key elements of a company's performance: financial position (assets, liabilities, and equity) and performance (income and cash flow). Typical annual

**Example 3.4:** Core Sustainability KPIs—Cemex Integrated Report 2016

| CHALLENGES TO ADDRESS | MAIN OBJECTIVES | CORE SUSTAINABILITY KPIs | 2016 | 2020 TARGET | ANNUAL TARGET |
|---|---|---|---|---|---|
| Economic | Provide Resilient Infrastructure and Energy-Efficient Building Solutions | Annual ready-mix sales derived from products with outstanding sustainable attributes (%) | 33.7 | | ≥ 25 |
| Environmental | Enable a Low-Carbon and Resource-Efficient Industry | Alternative fuels rate (%) | 23.3 | 35 | |
| | | Reduction in $CO_2$ emissions per ton of cementitious product from 1990 baseline (%) | 20 | 25 | |
| | | Clinker produced with continuous monitoring of major emissions: dust, $NO_x$, $SO_x$ (%) | 84 | 100 | |
| | | Annual reduction in dust emissions per ton of clinker from 2005 baseline (%) | 78 | | ≥ 50 |
| | | Annual reduction in $NO_x$ emissions per ton of clinker from 2005 baseline (%) | 26 | | ≥ 30 |
| | | Annual reduction in $SO_x$ emissions per ton of clinker from 2005 baseline (%) | 61 | | ≥ 20 |
| | | Active quarries with high biodiversity where BAPs are actively implemented (%) | 63 | 100 | |
| Social | Implement a High-Impact Social Strategy to Empower Communities | Total individuals benefited from our social initiatives (million) | 12.6 | ≥ 15 | |
| Governance | Embed Our Core Values into Every Action | Total fatalities (employees, contractors and third parties) | 20 | 0 | |
| | | Lost Time Injury Frequency Rate (LTI FR), employees (per million hours worked) | 0.6 | 0.3 | |
| | | Countries that conduct regular customer satisfaction surveys (%) | 88 | ≥ 90 | |
| | | Global procurement spend assessed under the *Supplier Sustainability Program* (%) | 17 | ≥ 55 | |
| | | Employees that perceive they are enabled to perform their job effectively (%) | 76 | 83 | |
| | | Employees that are engaged with the company (%) | 76 | 80 | |
| | | Executives and employees actively aware of our Code of Ethics (%) | 77 | ≥ 90 | |
| | | Target countries that participated in the *Global Compliance Program* covering antitrust, anti-bribery and insider trading (%) | 100 | | ≥ 90 |
| | | Ethics and compliance cases reported during the year that were investigated and closed (%) | 68 | | ≥ 90 |

Source: Cemex.

reports include the following financial statements and related information:

- Statements of income,
- Balance sheet,
- Statement of cash flows,
- Statement of change in stockholders' equity,
- Notes to financial statements.

Examples 3.5 below and 3.6 on the next page illustrate the first two of these statements for Novo Nordisk. Example 3.7 on page 105 illustrates the statement of cash flows for Sasol. And Example 3.8 on page 106 illustrates the statement of change in stockholders' equity for Liberty Holdings Limited.

**Example 3.5:** Income Statement—Novo Nordisk Annual Report 2016

# INCOME STATEMENT

AND STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER

| DKK million | Note | 2016 | 2015 | 2014 |
|---|---|---|---|---|
| **INCOME STATEMENT** | | | | |
| Net sales | 2.1, 2.2 | 111,780 | 107,927 | 88,806 |
| Cost of goods sold | 2.2 | 17,183 | 16,188 | 14,562 |
| Gross profit | | 94,597 | 91,739 | 74,244 |
| Sales and distribution costs | 2.2 | 28,377 | 28,312 | 23,223 |
| Research and development costs | 2.2, 2.3 | 14,563 | 13,608 | 13,762 |
| Administrative costs | 2.2 | 3,962 | 3,857 | 3,537 |
| Other operating income, net | 2.2, 2.5 | 737 | 3,482 | 770 |
| *– Non-recurring income from the partial divestment of NNIT A/S* | 2.5 | – | *2,376* | – |
| Operating profit | | 48,432 | 49,444 | 34,492 |
| Financial income | 4.8 | 92 | 85 | 167 |
| Financial expenses | 4.8 | 726 | 6,046 | 563 |
| Profit before income taxes | | 47,798 | 43,483 | 34,096 |
| Income taxes | 2.6 | 9,873 | 8,623 | 7,615 |
| Net profit for the year | | **37,925** | 34,860 | 26,481 |
| **EARNINGS PER SHARE** | | | | |
| Basic earnings per share (DKK) | 4.1 | 14.99 | 13.56 | 10.10 |
| Diluted earnings per share (DKK) | 4.1 | 14.96 | 13.52 | 10.07 |

| DKK million | Note | 2016 | 2015 | 2014 |
|---|---|---|---|---|
| **STATEMENT OF COMPREHENSIVE INCOME** | | | | |
| Net profit for the year | | 37,925 | 34,860 | 26,481 |
| Other comprehensive income: | | | | |
| *Items that will not be reclassified subsequently to the Income statement:* | | | | |
| Remeasurements of defined benefit plans | 3.5 | (205) | (37) | (247) |
| *Items that will be reclassified subsequently to the Income statement:* | | | | |
| Exchange rate adjustments of investments in subsidiaries | | (7) | (669) | (39) |
| Cash flow hedges, realisation of previously deferred (gains)/losses | 4.3 | 682 | 2,216 | (1,229) |
| Cash flow hedges, deferred gains/(losses) incurred during the period | 4.3 | (1,911) | (681) | (2,225) |
| Other items | | (74) | 366 | 111 |
| Tax on other comprehensive income, income/(expense) | 2.6 | 324 | (87) | 977 |
| Other comprehensive income for the year, net of tax | | **(1,191)** | 1,108 | (2,652) |
| Total comprehensive income for the year | | **36,734** | 35,968 | 23,829 |

Source: Novo Nordisk.

**Example 3.6:** Balance Sheet—Novo Nordisk Annual Report 2016

CONSOLIDATED FINANCIAL STATEMENTS | 59

# BALANCE SHEET

AT 31 DECEMBER

| DKK million | Note | 2016 | 2015 |
|---|---|---|---|
| **ASSETS** | | | |
| Intangible assets | 3.1 | 2,714 | 2,158 |
| Property, plant and equipment | 3.2 | 30,179 | 25,545 |
| Investment in associated company | 5.7 | 809 | 811 |
| Deferred income tax assets | 2.6 | 2,683 | 6,806 |
| Other financial assets | 4.7 | 1,388 | 1,339 |
| Total non-current assets | | 37,773 | 36,659 |
| Inventories | 3.3 | 14,341 | 12,758 |
| Trade receivables | 3.4, 4.7 | 20,234 | 15,485 |
| Tax receivables | | 1,552 | 3,871 |
| Other receivables and prepayments | 4.7 | 2,411 | 2,257 |
| Marketable securities | 4.2, 4.4, 4.7 | 2,009 | 3,542 |
| Derivative financial instruments | 4.2, 4.3, 4.7 | 529 | 304 |
| Cash at bank | 4.2, 4.4, 4.7 | 18,690 | 16,923 |
| Total current assets | | 59,766 | 55,140 |
| Total assets | | 97,539 | 91,799 |
| **EQUITY AND LIABILITIES** | | | |
| Share capital | 4.1 | 510 | 520 |
| Treasury shares | 4.1 | (9) | (10) |
| Retained earnings | | 46,111 | 46,816 |
| Other reserves | | (1,343) | (357) |
| Total equity | | 45,269 | 46,969 |
| Deferred income tax liabilities | 2.6 | 13 | 6 |
| Retirement benefit obligations | 3.5 | 1,451 | 1,186 |
| Provisions | 3.6 | 3,370 | 2,765 |
| Total non-current liabilities | | 4,834 | 3,957 |
| Current debt | 4.4, 4.7 | 229 | 1,073 |
| Trade payables | 4.7 | 6,011 | 4,927 |
| Tax payables | | 3,976 | 3,777 |
| Other liabilities | 3.7, 4.7 | 14,181 | 12,655 |
| Derivative financial instruments | 4.3, 4.7 | 2,578 | 1,382 |
| Provisions | 3.6 | 20,461 | 17,059 |
| Total current liabilities | | 47,436 | 40,873 |
| Total liabilities | | 52,270 | 44,830 |
| Total equity and liabilities | | 97,539 | 91,799 |

Source: Novo Nordisk.

**Example 3.7:** Statement of Cash Flows—Sasol Integrated Report 2017

## Statement of cash flows
for the year ended 30 June

| | 2017 Rm | 2016 Rm | 2015 Rm |
|---|---|---|---|
| Cash receipts from customers | **172 061** | 175 994 | 186 839 |
| Cash paid to suppliers and employees | **(127 992)** | (121 321) | (125 056) |
| **Cash generated by operating activities** | **44 069** | 54 673 | 61 783 |
| Cash flow from operations | **46 236** | 52 973 | 56 422 |
| Decrease/(increase) in working capital | **(2 167)** | 1 700 | 5 361 |
| Dividends received from equity accounted investments | **1 539** | 887 | 2 812 |
| Finance income received | **1 464** | 1 633 | 1 234 |
| Finance costs paid | **(3 612)** | (3 249) | (2 097) |
| Tax paid | **(6 352)** | (9 329) | (10 057) |
| Dividends paid | **(8 628)** | (10 680) | (12 739) |
| **Cash retained from operating activities** | **28 480** | 33 935 | 40 936 |
| Total additions to non-current assets | **(56 812)** | (70 497) | (42 645) |
| Additions to non-current assets | **(60 343)** | (73 748) | (45 106) |
| Increase in capital project-related payables | **3 531** | 3 251 | 2 461 |
| Additional investment in equity | **(444)** | (548) | (588) |
| Proceeds on disposals | **788** | 569 | 1 210 |
| Net cash disposed of on disposal of business | **–** | – | (105) |
| Purchase of investments | **(96)** | (233) | (224) |
| Proceeds from sale of investments | **28** | 171 | 264 |
| (Increase)/decrease in long-term receivables | **(141)** | (506) | 3 |
| **Cash used in investing activities** | **(56 677)** | (71 034) | (42 085) |
| Share capital issued on implementation of share options | **–** | 54 | 144 |
| Dividends paid to non-controlling shareholders in subsidiaries | **(989)** | (1 296) | (365) |
| Proceeds from long-term debt | **9 277** | 34 008 | 14 543 |
| Repayments of long-term debt | **(2 364)** | (3 120) | (1 663) |
| Proceeds from short-term debt | **4 033** | 2 901 | 2 686 |
| Repayments of short-term debt | **(1 410)** | (3 369) | (2 280) |
| **Cash generated by financing activities** | **8 547** | 29 178 | 13 065 |
| Translation effects on cash and cash equivalents | **(3 207)** | 7 069 | 3 095 |
| **(Decrease)/increase in cash and cash equivalents** | **(22 857)** | (852) | 15 011 |
| Cash and cash equivalents at beginning of year | **52 180** | 53 032 | 38 021 |
| **Cash and cash equivalents at end of year** | **29 323** | 52 180 | 53 032 |

## Commentary

**ADDITIONS TO NON-CURRENT ASSETS**

Included in additions to non-current assets of R60,3 billion is R36,8 billion relating to the construction of the Lake Charles Chemicals Project (LCCP).

**PROCEEDS FROM LONG-TERM DEBT**

Loans raised during the year amounted to R13,3 billion, mainly for the funding of our growth projects. We have sufficient liquidity in place to fund the LCCP and our business operations.

**CASH AND CASH EQUIVALENTS**

Our net cash position decreased by 44%, from R52,2 billion in June 2016 to R29,3 billion mainly due to the funding of the LCCP and the effect of a stronger closing rand/US dollar exchange rate.

Source: Sasol.

**Example 3.8:** Statement of Change in Stockholders' Equity—Liberty Holdings Integrated Report 2015

Summary consolidated statement of changes in shareholders' funds(A)

| | 2015 Rm | 2014 Rm |
|---|---|---|
| **Balance of ordinary shareholders' interests at 1 January** | **19 487** | 17 654 |
| Ordinary dividends | **(1 874)** | (1 719) |
| Total comprehensive income | **4 010** | 3 864 |
| Share buy-backs net of share subscriptions[10] | **(444)** | (355) |
| Black Economic Empowerment transaction | **520** | 153 |
| Share-based payments | **140** | 133 |
| Preference dividends | **(2)** | (2) |
| Transactions between owners[11] | **(98)** | (230) |
| Common control transaction | | (11) |
| **Ordinary shareholders' interests** | **21 739** | 19 487 |
| **Balance of non-controlling interests at 1 January** | **4 147** | 3 702 |
| Total comprehensive income | **339** | 372 |
| Unincorporated property partnerships net distributions | **(144)** | (79) |
| Non-controlling share of subsidiary dividend and capital reduction | **(44)** | (38) |
| Transactions between owners | **(44)** | 190 |
| **Non-controlling interests** | **4 254** | 4 147 |
| **Total equity** | **25 993** | 23 634 |

Source: Liberty Holdings Limited.

### 3.2.2. Statement of Audited Financial Results

The annual report should include an affirmation that the financial statements have been prepared by management and audited by an independent, qualified, and competent auditor. In good international practice (Matrix Level 3), the audit committee of the board should oversee financial and nonfinancial reporting and audit.

Larger and publicly listed companies are expected to have their financial statements audited according to international auditing standards, such as the Generally Accepted Auditing Standards or the International Auditing Standards. Example 3.9 shows a typical auditor's report from Liberty Holdings, a financial services company in South Africa.

In most jurisdictions, the law requires the financial statements of large or publicly listed companies to be audited.

**BEST PRACTICE** in auditing, which was recently codified under ISA Standard 700 (revised in 2015), requires the auditor to disclose key audit matters that arose during the audit. Example 3.10 shows key audit matters that arose during AkzoNobel's 2016 audit.

### 3.2.3. Segment Reporting

Companies should present segment information that corresponds to the company's own internal organization and management's decision making. Segment reporting in financial statements should correspond with

**BEST-PRACTICE RESOURCES: Auditing Standards**

*ISA 700 (Revised), Forming an Opinion and Reporting on Financial Statements:* This ISA (International Standard on Auditing) deals with the auditor's responsibility to form an opinion on the financial statements (that is, qualified, adverse, or disclaimer of opinion) as well as the form and content of the auditor's report issued as a result of an audit of financial statements.

**BEST-PRACTICE RESOURCES: Segment Information Reporting**

*IFRS 8* and its U.S. equivalent *FAS 131* require companies to report segment information that corresponds to the company's own internal organization and management's decision making.

**Example 3.9:** Independent Auditor's Report—Liberty Holdings Integrated Report 2015

## Appendix B – Group equity value report and independent auditor's report

**To the shareholders of Liberty Holdings Limited**

We have audited the group equity value report of Liberty Holdings Limited for the year ended 31 December 2014 on pages 204 to 209, which has been prepared in accordance with the equity value basis set out in section 2 of the group equity value report. This report should be read in conjunction with the audited annual financial statements where the policyholder liabilities are determined in terms of International Financial Reporting Standards, which are contained in the annual financial statements and supporting information.

**Directors' responsibility for the group equity value report**

The company's directors are responsible for the preparation and presentation of the group equity value report in terms of the group equity value basis set out in section 2 of the group equity value report, for determining that the basis of preparation is acceptable in the circumstances and for such internal control as the directors determine is necessary to enable the preparation of the group equity value report that is free from material misstatements, whether due to fraud or error.

**Auditor's responsibility**

Our responsibility is to express an opinion on the group equity value report. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the group equity value report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the group equity value report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the group equity value report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the group equity value report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of the group equity value principles used and the reasonableness of valuation estimates made by the directors, as well as evaluating the overall presentation of the group equity value report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

**Opinion**

In our opinion, the group equity value report has been prepared in all material respects in accordance with the basis set out in section 2 of the group equity value report.

**Basis of accounting and restriction on use**

Without qualifying our opinion, we draw attention to section 2 of the group equity value report, which describes the basis of accounting. The group equity value report is prepared to reflect the combined value of the various components of Liberty's businesses. As a result, the group equity value report may not be suitable for another purpose. Our report is intended solely for the directors of Liberty Holdings Limited and should not be used by any other parties. We agree to the publication of our report provided it is clearly understood by the recipients of the report that they enjoy such receipt for information only and that we accept no duty of care to them in respect of our report.

**PricewaterhouseCoopers Inc.**
Director: **J Goncalves**
*Registered auditor*

Johannesburg
25 February 2015

Source: Liberty Holdings Limited.

**Example 3.10:** Independent Auditor's Report—AkzoNobel Report 2016

**Key audit matter**

**Impairment testing of goodwill and other intangibles with indefinite useful lives**
**Note 8 – page 148**

At December 31, 2016, the company's goodwill and other intangibles with indefinite useful lives are valued at €3.5 billion. The key assumptions and sensitivities are disclosed in Note 8 of the Consolidated financial statements. The annual impairment test for goodwill and indefinite life intangible assets is significant to our audit because the assessment process is complex, involves significant management judgment and is based on assumptions that are affected by expected future market and economic conditions, revenue growth, margin developments, the discount rates and terminal growth rates. Based on the annual goodwill impairment test, including sensitivity tests, the Board of Management concluded that no impairment of goodwill and other intangibles with indefinite useful lives was necessary.

**How our audit addressed the matter**

Our audit procedures included, among others, an assessment of the mathematical accuracy of the calculations and a reconciliation to the 2017 five-year plan as approved by the Board of Management. We evaluated the assumptions and methodologies used in the annual impairment test prepared by the company. We have challenged management, primarily on their assumptions applied to which the outcome of the impairment test is the most sensitive, in particular, the projected revenue growth, margin developments, discount rates and terminal growth rates. We performed independent testing and analysis of the basic peer group composition, among others, and challenged management by comparing the assumptions to historic performance of the company and local economic developments, taking into account the sensitivity tests of the goodwill balances for any changes in the respective assumptions. We also focused on the adequacy of the company's disclosures in Note 8 of the Consolidated financial statement concerning those key assumptions to which the outcome of the impairment test is most sensitive.

Source: AkzoNobel.

other parts of the reports where business segments are relevant, including business model and environment and performance reporting. (See Examples 3.11 and 3.12.)

### 3.2.4. Results per Share, Dividends, and Tax Disclosures

*Results per share* is a simple but powerful financial ratio that current and prospective shareholders can use to compare alternative investments, track performance over time, and estimate price appreciation in the future. It is typically expressed as earnings per share, calculated as a company's total annual earnings (profit) that belong to common shareholders (net of tax and preferred stock dividends), divided by the number of common shares outstanding (usually the average during the year). Results per share should be developed consistently over time to enable comparability. (See Example 3.13.)

**LEADERSHIP PRACTICES** (Matrix Level 4) suggest that companies disclose their *dividend policy* as part of the annual report. A dividend policy typically sets the percentage of earnings that will be distributed to shareholders, in proportion to their holdings. Companies in growth mode often choose not to distribute dividends, whereas more stable and established companies use dividends as a feature to attract income-focused investors.

**BEST-PRACTICE RESOURCES:**
**Reporting on Tax Matters**

*King IV Report on Corporate Governance for South Africa 2016:* "Tax has become a complex matter with various dimensions. The governing body should be responsible for a tax policy that is compliant with the applicable laws, but that is also congruent with responsible corporate citizenship, and that takes account of reputational repercussions. Hence, responsible and transparent tax policy is put forward as a corporate citizenship consideration in King IV."

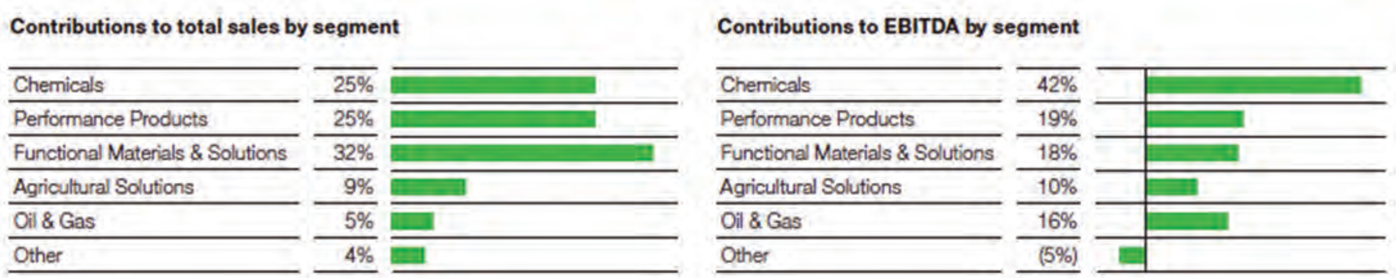
*PRI: Investors' Recommendations on Corporate Income Tax Disclosure 2017* presents recommendations by global investors under the Principles for Responsible Investment on corporate tax disclosure, including on tax policy, the company's approach to taxation, and its alignment with business and sustainability strategy, tax governance, and management of tax policy and related risks and tax-related risks and country-by-country activities.

**Example 3.11:** Segment Reporting—Liberty Holdings Integrated Report 2015

| 2015 (Rm) | Individual Arrangements | Group Arrangements | Asset Management | Other | Total | Reporting adjustments | IFRS reported |
|---|---|---|---|---|---|---|---|
| **Total revenue** | 57 694 | 18 527 | 3 436 | 2 169 | 81 826 | (7 831) | 73 995 |
| Profit before taxation | 3 427 | 499 | 842 | 1 599 | 6 367 | 223 | 6 590 |
| Taxation | (1 737) | (193) | (205) | (168) | (2 303) | | (2 303) |
| **Total earnings** | 1 690 | 306 | 637 | 1 431 | 4 064 | 223 | 4 287 |
| Other comprehensive (loss)/income | (136) | 138 | 44 | 16 | 62 | | 62 |
| **Total comprehensive income** | 1 554 | 444 | 681 | 1 447 | 4 126 | 223 | 4 349 |
| Attributable to non-controlling interests | | (106) | (10) | | (116) | (223) | (339) |
| Shareholders | 1 554 | 338 | 671 | 1 447 | 4 010 | | 4 010 |

Source: Liberty Holdings Limited.

**Example 3.12:** Segment Reporting—BASF 2017 Integrated Report




Source: BASF.

**Example 3.13:** Results per Share—Santova Limited 2016 Annual Integrated Report

| | | 2016 R'000 | 2015 R'000 |
|---|---|---|---|
| **4. EARNINGS PER SHARE** | | | |
| ***Reconciliation between basic, headline and normalised headline earnings*** | | | |
| **Profit attributable to equity holders of the parent** | | **48 713** | 38 525 |
| *Adjusted for:* | | | |
| Net loss/(profit) on disposals of plant and equipment | | **255** | (130) |
| Impairment of goodwill | | **–** | 3 892 |
| Taxation effects | | **(84)** | 19 |
| Minority interest | | **(51)** | – |
| **Headline earnings** | | **48 833** | 42 306 |
| *Adjusted for:* | | | |
| Effect of fair value gain on remeasurement of financial liability | | **(1 024)** | (5 896) |
| Effect of lease termination agreement | | **(467)** | (2 359) |
| Non-recurring transaction costs | | **929** | 394 |
| Taxation effects | | **131** | 661 |
| **Normalised headline earnings (unaudited)** | | **48 402** | 35 106 |
| **Basic earnings per share** | (cents) | **34,50** | 28,23 |
| **Headline earnings per share** | (cents) | **34,58** | 31,00 |
| **Normalised headline earnings per share (unaudited)** | (cents) | **34,28** | 25,73 |
| Weighted average number of shares | (000s) | **141 211** | 136 459 |
| Diluted weighted average number of shares | (000s) | **144 648** | 138 939 |

The difference between earnings per share and diluted earnings per share is due to the impact of share options that are yet to vest under the Group's share option scheme.

Source: Santova.

**LEADERSHIP PRACTICES** (Matrix Level 4) also suggest that companies disclose *tax transparency statements*, which typically contain a description of the company's strategy and policy regarding corporate tax and the actual amount of tax paid in different jurisdictions and segments where it operates. Example 3.14 on the next page shows how the Spanish telecommunications company, Telefonica, publicly discloses its policy and actual payment of taxes.

## 3.3. Sustainability Statements

Sustainability statements (just like financial statements) are important for public accounting and accountability. And unlike sustainability KPIs, which are unique to the company's business model and context, sustainability statements should present an account of performance that is more standardized according to more commonly used metrics that are comparable across companies and industries.

For the most part, sustainability disclosures are voluntary. However, there is a growing trend among regulators and quasi-regulators (stock exchanges, standard-setting bodies, and others) to either require or strongly encourage the disclosure of sustainability information alongside financial information.

This section of the Toolkit provides guidance on how to prepare sustainability statements, including suggested environmental and social metrics.

### 3.3.1. General Guidance

Sustainability statements consist of a tabulated presentation of metrics or performance indicators that the company tracks as part of its management of key sustainability issues. Similar to the assessment of key sustainability opportunities and risks (see ***1.4. Sustainability Opportunities and Risks,*** page 26 of this Toolkit), sustainability statements should include metrics that characterize company performance on a range of issues that the company determines to be material, for example:

- Core environmental and social issues applicable to most industries;
- Sustainability issues that are relevant to a company's specific technology, business model, or industry, and that relate to the company's products and services, ethics, and contribution to economic and social development.

In preparing sustainability statements, companies must strike a balance between using only KPIs—which should be highly individualized to reflect the strategy and serve as targets for its execution—or using a larger selection of commonly accepted metrics that can be compared with peers and across time.

Information and data in the sustainability statements should be presented with comparative figures from the company's past two fiscal years and ideally should be subject to an annual assurance process by an independent

**Example 3.14:** Tax Statement—Telefonica Integrated Report 2016

**TAXES IN 2016**

Our economic and social contribution is not only quantifiable via payment of Corporate Tax, but also through other specific contributions in the various countries where we operate, such as fees (for Public Domain Use, for Radio and Television Corporation Financing, etc.), local taxes, and Social Security payments, as well as other similar contributions in the remaining countries.

In addition to these directly borne taxes, we pay in to public coffers, as a result of our activity and on the part of other contributors, other amounts that must be considered within the total tax contribution that the Company makes, such as indirect taxes, workers' withholdings and other withholdings.

In this context and during 2016, our total tax contribution (TTC) amounted to 11,365 million euros (2,887 million euros for taxes borne and 8,478 million euros for taxes collected), accounting for 49% of the value distributed by Telefónica[1]. Brazil and Spain, the markets in we generate the most operating profit, are the jurisdictions which have most contributed to the payment of taxes.

The amount in absolute values of Telefónica's TTC for the 2016 tax year have decreased slightly in comparison to the 2015 tax year due to the evolution of the currencies in relevant Latin American countries.

Therefore, for every 100 euros of Company revenue, 21.8 euros were allocated to the payment of taxes (5.5 to the payment of taxes borne and 16.3 to the payment of taxes collected).

All the information about our tax practices is available on our website.

For every 100 euros of Company revenue, *21.8 euros* are allocated to the payment of taxes

Source: Telefonica.

provider. Example 3.15 illustrates AkzoNobel's use of a more limited set of KPIs for the sustainability statements, and Examples 3.16 and 3.17 on pages 111 and 112, illustrate a more comprehensive approach.

In good international practice (Matrix Level 3), the audit committee or E&S/sustainability committee of the board should oversee the sustainability information contained in the annual report.

**BEST-PRACTICE RESOURCES: Definition, Scope, Collection, and Assurance of Sustainability Data**

Leadership practices suggests that sustainability information and metrics be independently verified (or assured), which requires that the company clearly establish the scope, definition, and internal collection process for the data. Assurance of sustainability information is important to ensure that information is reliable—both for internal management and external reporting.

**LEADERSHIP PRACTICES** (Matrix Level 4) suggest that ESG data be subject to an annual audit by an independent provider.

### 3.3.2. Suggested Metrics for Sustainability KPIs and Statements

This section presents a large selection of ESG metrics that can be used for the identification of KPIs as well as the preparation of sustainability statements. These suggested metrics cover core sustainability issues as well as issues that are more industry- or context-specific. They are derived from commonly accepted standards of corporate sustainability performance, accounting, and reporting.

**BEST PRACTICE** suggests that companies pick the most important metrics and customize them to create KPIs that reflect the company strategy and serve as targets for its execution. Sustainability statements can include a larger selection of metrics and, like financial statements, benefit from inclusion of commonly accepted metrics that can be compared with peers and across time.

**Example 3.15:** Consolidated Sustainability Statements—AkzoNobel Report 2016

**Consolidated Sustainability statements**

| | Note | 2013 | 2014 | 2015 | 2016 | Target 2020 |
|---|---|---|---|---|---|---|
| **Economic** | | | | | | |
| Eco-premium solutions with downstream benefits (% of revenue) | 4 | 18 | 19 | 19 | 20 | 20 |
| Resource Efficiency Index (REI) (2012 baseline =100) | 5 | 98 | 96 | 113 | 112 | – |
| Customer delivery efficiency index | 6 | 92 | 93 | 94 | 96 | – |
| Critical PR[1] spend covered by supplier management framework (% of spend) | 7 | 80 | 83 | 87 | 91 | 90 (2018) |
| **Environmental** | | | | | | |
| Carbon footprint cradle-to-grave per ton of product sales (% reduction from 2012) | 8 | 2 | -4 | 3 | 6 | 25–30 |
| Renewable energy own operations (%) | 8 | 31 | 34 | 38 | 40 | 45 |
| Renewable raw materials (% of organic) | 8 | 13 | 13 | 11 | 12 | – |
| Operational eco-efficiency footprint measure (% reduction from 2009) | 9 | 24 | 24 | 23 | 28 | 40 (2017) |
| **Social** | | | | | | |
| Employee engagement score (0-5 scale) | 11 | 3.88 | 3.97 | 4.03 | 4.17 | >4.20 |
| Female executives (%) | 11 | 16 | 17 | 19 | 19 | 25 |
| Total reportable injury rate employees/supervised contractors (per million hours) | 12 | 2.3 | 1.8 | 1.6 | 1.4 | <1.0 |
| Loss of primary containment (Level 1) | 13 | – | – | – | 16 | – |
| Priority substances with management plan (%) | 14 | 62 | 82 | 100 | 33[2] | 100[2] |
| Cumulative Community Program involvement (number of projects) | 17 | 2,108 | 2,260 | 2,385 | 2,531 | – |

Note: Some 2020 projections are ambitions
1 PR = Product related (raw materials and packaging).
2 Phase 2 started in 2016.

Source: AkzoNobel.

**Example 3.16:** Employee Metrics—Standard Chartered Sustainability Summary 2015

**People**

**Countries**

| | 2015 | 2014 | 2013 |
|---|---|---|---|
| Global | 67 | 71 | 71 |

**Workforce profile**

**Headcount**

| | 2015 | 2014 | 2013 |
|---|---|---|---|
| Global total | 84,076 | 90,940 | 86,640 |
| of which businesses | 42,036 | 49,638 | 46,892 |
| of which support services | 42,040 | 41,302 | 39,748 |
| (Decline)/growth | (6,864) | 4,300 | (2,418) |
| (Decline)/growth percentage | (8.0)% | 5.0% | (2.7)% |

**Location of employees (by region)**

| | 2015 % | 2014 % | 2013 % |
|---|---|---|---|
| Greater China | 20 | 21 | 22 |
| North East Asia | 5 | 6 | 7 |
| South Asia | 27 | 25 | 24 |
| ASEAN | 25 | 25 | 25 |
| MENAP | 9 | 9 | 9 |
| Africa | 10 | 10 | 9 |
| Americas | 1 | 1 | 1 |
| Europe | 3 | 3 | 3 |

**Employee attrition**

| | 2015 % | 2014 % | 2013 % |
|---|---|---|---|
| Employee turnover rate | 21.7 | 18.5 | 19.5 |
| Employee voluntary turnover rate | 16.7 | 15.1 | 15.9 |

**Years of service**

| | 2015 % | 2014 % | 2013 % |
|---|---|---|---|
| 0-5 years | 59 | 61 | 58 |
| 5-10 years | 23 | 22 | 25 |
| > 10 years | 18 | 17 | 17 |

**Age of employees**

| | 2015 % | 2014 % | 2013 % |
|---|---|---|---|
| < 30 years | 29 | 32 | 33 |
| 30-50 years | 65 | 62 | 61 |
| > 50 years | 6 | 6 | 6 |

**Gender**

| | 2015 % | 2014 % | 2013 % |
|---|---|---|---|
| Female representation | 47 | 47 | 47 |
| Female senior management[1] | 12 | 15 | 16 |
| Female executive and non-executive director[2] | 23 | 11 | 14 |

1. Director, bands 1 and 2
2. As at 31 December 2015, the Board comprised 23 per cent women. As at 23 February 2016, the Board comprised 20 per cent women

**Gender per region (female)**

| | 2015 % | 2014 % | 2013 % |
|---|---|---|---|
| Greater China | 64 | 63 | 63 |
| North East Asia | 57 | 50 | 50 |
| South Asia | 30 | 30 | 30 |
| ASEAN | 54 | 54 | 54 |
| MENAP | 30 | 30 | 30 |
| Africa | 50 | 50 | 50 |
| Americas | 44 | 43 | 42 |
| Europe | 44 | 44 | 44 |

Source: Standard Chartered.

**Example 3.17:** Nonfinancial Summary—Westpac Group Annual Report 2016

## Five year non-financial summary[1]

Key trends across a range of non-financial areas of performance are provided in the following five year non-financial summary, with a more detailed account of sustainability performance included in our Annual Review and Sustainability Report and Sustainability Performance Report.

| | **2016** | 2015 | 2014 | 2013 | 2012 |
|---|---|---|---|---|---|
| **Customer** | | | | | |
| Total customers (millions)[2] | 13.4 | 13.1 | 12.8 | 12.2 | 11.8 |
| Digitally active customers (millions)[3] | 4.9 | 4.9 | 4.7 | 4.2 | 4.0 |
| Branches | 1,309 | 1,429 | 1,534 | 1,544 | 1,538 |
| Branches with 24/7 capability (%)[4] | 27 | 22 | 15 | - | - |
| ATMs | 3,757 | 3,850 | 3,890 | 3,814 | 3,639 |
| Smart ATMs (%)[5] | 37 | 31 | 24 | 17 | - |
| Change in consumer complaints (%) - Australia | (31) | (31) | (27) | (15) | - |
| Change in consumer complaints (%) - NZ[6] | (7) | (18) | (16) | 19 | - |
| Wealth customer penetration (%)[7] | 19.1 | 19.7 | 20.0 | 18.7 | 18.4 |
| **Employees** | | | | | |
| Total core (permanent) full-time equivalent staff | 32,190 | 32,620 | 33,586 | 33,045 | 33,418 |
| Employee voluntary attrition (%)[8] | 10.6 | 10.6 | 9.8 | 9.8 | 9.9 |
| New starter retention (%)[9] | 85.5 | 85.3 | 88.0 | 86.7 | 84.8 |
| High performer retention (%)[10] | 94.8 | 95.0 | 95.8 | 95.7 | 95.9 |
| Employee engagement index (%)[11] | 69 | - | - | - | - |
| Lost Time Injury Frequency Rate (LTIFR)[12] | 0.8 | 0.8 | 1.1 | 1.5 | 1.9 |
| Women as a percentage of the total workforce (%) | 58 | 59 | 59 | 60 | 61 |
| Women in leadership (%)[13] | 48 | 46 | 44 | 42 | 40 |
| **Environment** | | | | | |
| Total Scope 1 and 2 emissions - Aust and NZ (tonnes $CO_2$-e)[14] | 154,339 | 173,437 | 175,855 | 180,862 | 183,937 |
| Total Scope 3 emissions - Aust and NZ (tonnes $CO_2$-e)[15] | 63,016 | 67,899 | 73,871 | 85,013 | 91,855 |
| Paper consumption - Aust and NZ (tonnes)[16] | 3,304 | 4,857 | 5,334 | 5,762 | - |
| **Sustainable lending and investment** | | | | | |
| Proportion of electricity generation financing in renewables including hydro - Aust and NZ (%)[17] | 59 | 61 | 59 | 55 | 52 |
| Electricity generation portfolio emissions intensity (tonnes $CO_2$-e/MWh)[18] | 0.38 | 0.38 | 0.41 | 0.44 | - |
| Finance assessed under the Equator Principles - Group ($m)[19] | 617 | 1,065 | 851 | 268 | 1,140 |
| Responsible investment funds under management ($m)[20] | 18,723 | 15,017 | - | - | - |
| **Social impact** | | | | | |
| Community investment ($m)[21, 22] | 148 | 149 | 217 | 131 | 133 |
| Community investment as a percentage of pre-tax profits - Group (%)[22] | 1.39 | 1.30 | 2.02 | 1.33 | 1.50 |
| Community investment as a percentage of pre-tax operating profit (cash earnings basis)[22] | 1.32 | 1.33 | 1.99 | 1.28 | 1.41 |
| Financial education (participants)[23, 24] | 59,596 | 65,538 | 49,812 | 32,577 | 36,182 |
| **Supply chain** | | | | | |
| Top suppliers self-assessed - Australia (%)[25] | 100 | 100 | 100 | 98 | 94 |
| Spend with indigenous Australian suppliers - Australia ($ million)[26] | 1.6 | 1.2 | - | - | - |

Source: Westpac.

### *Suggested Metrics for Core Issues and the IFC Performance Standards*

Table 3.1 on page 113 presents model indicators that relate to the core environmental and social issues covered in the IFC Performance Standards and that are common to all or most companies and industries operating in emerging markets.

**Table 3.1:** Core Sustainability Indicators—IFC Performance Standards

| TOPIC | INDICATOR |
|---|---|
| **Performance Standard 1: Assessment and Management of Environmental and Social Risks and Impacts** | |
| Emergency Response Plan or Procedure | Emergency Response Plan or Procedure (y/n). Provide description and link. |
| Statement of intention regarding E&S | Environmental and social policy approved by senior management (y/n). Provide description and link. |
| General public knowledge and recourse | External communication mechanism accessible by general public (y/n). Provide description and link. |
| Affected Community knowledge of impacts and opportunities | Information disclosed to Affected Community (y/n). Provide description and link. |
| Affected Community feedback and recourse | Affected Community grievance mechanism (y/n). Provide description and link. |
| Systematic process to identify and manage risks/impacts and opportunities | Environmental and Social Management System (y/n). Provide description and link. |
| **Performance Standard 2: Labor and Working Conditions** | |
| Workers protection | Legal actions, employee grievances, or public controversies involving working conditions (associations, collective agreements, labor laws) (#). Describe corrective actions. |
| Opportunities and fairness for all workers | Legal actions, employee grievances, or public controversies involving discrimination or equal remuneration (#). Describe corrective actions. |
| Protection of contract workers | Legal actions, employee grievances, or public controversies involving third party or contract workers (#). Describe corrective actions. |
| Worker health and safety | Legal actions, employee grievances, or public controversies indicating poor worker health and safety practices (#). Describe corrective actions. |
| Injury and fatality | Number of work-related fatalities for direct and contract workers. |
| | Lost-time incident rate for direct and contract employees. |
| Workforce composition | Workforce composition by gender and ethnicity (#). |
| Transparent working conditions | Policy on Human Resources (y/n). Provide description and link. |
| Worker feedback and recourse | Worker grievance mechanism (y/n). Provide description and link. |
| ***Sector-Specific Risks:*** **Operations or supply chain in countries or sectors with a risk of forced or child labor (e.g., agri, textiles, construction, agribusiness).** | |
| Forced and child labor in the company | Legal actions, employee grievances, or public controversies involving forced and child labor in the company's operations (#). Describe corrective actions. |
| Forced and child labor in the primary supply chain | Legal actions, employee grievances, or public controversies involving forced and child labor in the company's primary supply chain (#). Describe corrective actions. |
| Safe worker accommodation | Legal actions, employee grievances, or public controversies involving accommodation (camps, dorms, etc.) such as health and safety (e.g., fire, water, sanitation, overcrowding) (#). Describe corrective actions. |
| Proactive management of forced and child labor and migrant workers | Labor or E&S policy, statement, or code about management of forced and child labor and migrant workers (y/n). Provide description and link. |

*(Continued on next page.)*

TABLE 3.1: Core Sustainability Indicators—IFC Performance Standards *(Continued from previous page)*

| TOPIC | INDICATOR |
|---|---|
| **Performance Standard 3: Resource Efficiency and Pollution Prevention** | |
| Impact on water used by others | Legal actions, community grievances, or public controversies involving past or ongoing impact on water used by others (#). Describe corrective actions. |
| Pollution risks | Legal actions, community grievances, or public controversies involving past or ongoing pollution risks (e.g., air or water emissions, soil or groundwater contamination, waste disposal) from the company/project (#). Describe corrective actions. |
| GHG emissions | GHG emissions: Scope 1 and 2 (t), Scope 3 if relevant, intensity (GHGs released in energy consumption for production/normalization factor [usually production or sales]). |
| Resource efficiency | Resource efficiency: resource intensity, i.e, resources (e.g., materials, energy, and water) required for the provision of a unit of a good or service; % renewables in the energy mix, % water recycled in production. |
| Pollution prevention | Pollution prevention policy and management plan (y/n). Provide description and link. |
| | Availability of an emission monitoring system (y/n). Provide description and link. |
| **Performance Standard 4: Community Health, Safety and Security** | |
| Security force impacts to a community | Statement, policy, or code on security forces and interaction with local community (y/n). Provide description and link. |
| | Legal actions, community grievances, or public controversies associated with major security incident involving the local community (#). Describe corrective actions. |
| Contribution to health impacts on a community | Legal actions, community grievances, or public controversies involving contribution to an increase of disease (HIV/Aids, malaria, etc.) in a community (#). Describe corrective actions. |
| Worker impact on a community | Statement, policy, or code on worker conduct and interaction with local community (y/n). Provide description and link. |
| ***Sector-Specific Risks:*** **Companies/projects that construct or operate buildings and structures that are accessed by the public, or that can threaten the safety of communities (bridges, dams, etc.).** | |
| Infrastructure failures that have resulted in harm to the public | If the company constructs or operates infrastructure (bridges, dams, tailing dams, or ash ponds), number of legal actions, community grievances, or public controversies indicating harm to the public. Describe corrective actions. |
| Fires or structural damage that have harmed the public | If the company constructs or operates publicly accessed buildings or structures, number of legal actions, community grievances, or public controversies indicating harm to the public. Describe corrective actions. |
| **Performance Standard 5: Land Acquisition and Involuntary Resettlement** | |
| People/communities involuntary resettled or evicted through force | Legal actions, community grievances, or public controversies involving involuntary resettlement and eviction with the use of force (#). Describe corrective actions. |
| Negative impact on peoples' livelihoods | Community grievances or public controversies where the company/project has resulted in peoples' livelihoods being negatively affected (#). Describe corrective actions. |

*(Continued on next page.)*

TABLE 3.1: Core Sustainability Indicators—IFC Performance Standards *(Continued from previous page)*

| TOPIC | INDICATOR |
|---|---|
| **Performance Standard 6: Biodiversity Conservation and Sustainable Management of Living Natural Resources** | |
| Impact on ecosystem services | Legal actions, community grievances, or public controversies involving people not having enough water or food, or suffering from the effects of larger storm events (flooding, loss of land, salinization of soil/water, etc.), because of the company/project (#). Describe corrective actions. |
| Impacts to protected areas, parks, or reserves | Company/project located in or near protected area, park, or reserve (y/n). Provide description. |
| Impact on endangered, vulnerable, or rare species | Company/project located in or near an area known to contain endangered, vulnerable, or rare species (y/n). Provide description. |
| Protection of habitat and biodiversity management | Statement, code, or policy on biodiversity management (y/n). Provide description and link. |
| Impact on water sources, rivers, lakes, or wetlands | Legal actions, community grievances, or public controversies related to large impacts on water sources, rivers, lakes, or wetlands, either through construction, permanent change in land use, or the volume of water needed for company operations (#). Describe corrective actions. |
| *Sector-Specific Risks:* **Agribusiness companies and companies that purchase agro-commodities as part of their primary business.** | |
| Agro-commodity certification | % of agro-commodity that is certified (e.g., FSC, RSPO, MSC, RTRS, BCI, GRSB, Bonsucro certification, etc.). |
| Proactive management of supply chain to protect critical habitats | Statement, policy, or code on the management of supply chain where there is the risk of significant conversion of critical habitats (y/n). Provide description and link. |
| **Performance Standard 7: Indigenous Peoples** | |
| Impact on indigenous peoples | Company/project in area that indigenous peoples may live on, migrate through, or use (y/n). Provide description. |
| Impact on indigenous peoples from land acquisition | Legal actions, community grievances, or public controversies involving harm to indigenous people (through relocation, impact on livelihoods, taking traditional knowledge, etc.) (#). Describe corrective actions. |
| Proactive engagement with indigenous people | Statement, code, or policy on indigenous people (y/n). Provide description and link. |
| **Performance Standard 8: Cultural Heritage** | |
| Impact on cultural heritage | Legal actions, community grievances, or public controversies related to company/project's impact on or use of cultural heritage (#). Describe corrective actions. |

Source: IFC.

### *Suggested Metrics for Corporate Governance*

Table 3.2 presents model indicators that relate to the good corporate governance practices (Level 3) promoted by the Matrix. The right-hand column indicates the frequency of inclusion of the metric in widely used corporate governance disclosure frameworks, standards, and information service providers.[11]

**Table 3.2:** Model Governance Indicators

| A: Commitment to ESG | | Freq. |
|---|---|---|
| CG Framework | Company has both a CG code and a code of ethics/conduct (y/n) | 38% |
| CG Officer | Is there a designated officer/body responsible for overseeing CG policies and practices? (y/n) | 11% |
| **B. Structure and Functioning of Board** | | **Freq.** |
| Board Independence | % independent directors that meet a robust definition of independence, such as the IFC Indicative Definition. | 78% |
| Board Diversity | % women (non-promoter/sponsor) on board | 78% |
| Audit Committee | Is the board-level audit committee composed of financially literate members, all of whom are non-executive directors and at least one member is independent? (y/n) | 44% |
| Role and Responsibilities | Does the board approve both the strategy and key policies? (y/n) | 22% |
| **C. Control Environment** | | **Freq.** |
| Internal Audit | Does the internal audit function have its own charter/bylaw establishing its role, responsibilities, and reporting lines? (y/n) | 1% |
| Risk Governance | Does the chief risk officer have access to the board and report to the board/risk committee? (y/n) | 1% |
| Compliance | Does the compliance function report to the audit committee? (y/n) | 1% |
| **D. Disclosure and Transparency** | | **Freq.** |
| Annual Report | Does the annual report or the sustainability report include ESG information? (y/n) | 33% |
| Risk Disclosure | Does the annual report include descriptions of risk and risk appetite? (y/n) | 11% |
| **E: Treatment of Minority Shareholders** | | **Freq.** |
| Equal Voting | Do all shareholders of the same class have: 1) equal voting; 2) subscription; and 3) transfer rights? (y/n) | 50% |
| Equal Treatment of Shareholders | Are there 100% tag-along rights for change of control transactions? (y/n). | 6% |
| Ownership Disclosure | Is ultimate beneficial ownership disclosed publicly? (y/n) | 11% |
| RPTs | Is there a related-party transaction policy that includes an escalation mechanism to shareholder approval over a certain size? (y/n) | 0% |
| Dividend Policy | Is the dividend policy publicly disclosed? (y/n) | 11% |
| Executive Compensation | Is executive compensation subject to shareholder consultation and approval? (y/n) | 43% |
| **F. Governance of Stakeholder Engagement** | | **Freq.** |
| External Communication and Grievances | Are grievance mechanisms overseen by the board? (y/n) | 0% |
| Governance of Stakeholder Engagement | Are there processes for consultation between stakeholders and the board on economic, environmental, and social topics? (y/n) | 11% |

Source: IFC.

[11] Frameworks and standards analyzed include reporting frameworks (GRI), financial analysis frameworks (DJSI), and information service providers (Asset4, BBG, MSCI, Sustainalytics).

### *Most Commonly Reported E&S Metrics*

Table 3.3 presents a summary of the most commonly reported and tracked E&S metrics, based on an analysis of 12 widely used E&S disclosure frameworks, standards, and information service providers.[12] Metrics listed are illustrative and based on either a common formulation or an amalgamation of different formulations. The right-hand column indicates the frequency of inclusion of the metric in the frameworks and standards analyzed.

**Table 3.3:** Most Commonly Reported E&S Metrics

| TOPICS | ILLUSTRATIVE METRICS | FREQ. |
|---|---|---|
| **MANAGEMENT SYSTEM** | | |
| Environmental & Social Management System | Environmental and Social Management System (y/n). Provide description and link. | 46% |
| **ENVIRONMENT** | | |
| **Resource Efficiency** | | |
| GHG emissions | GHG emissions: Scope 1 and 2 (t), Scope 3 if relevant, intensity (GHG emissions/production of sales) | 92% |
| Water use | Water used (m3), % recycled, % in water stress areas, intensity (water use/sales) | 92% |
| Energy efficiency and mix | Energy consumed (GW), % grid electricity, % renewables, intensity (energy/sales) | 85% |
| **Pollution Prevention** | | |
| Waste (water, solid, hazardous) | Waste from operations (t), % hazardous, % recycled, intensity (waste/sales) | 73% |
| Air pollutants | Air Pollutants (Tn): NOx (excl. N2O), SOx, volatile organic compounds, particulate matter | 62% |
| Pollution risks | Legal actions, community grievances, or public controversies involving past or ongoing pollution risks (e.g., air or water emissions, soil or groundwater contamination, waste disposal) from the company/project (#). Describe corrective actions. | 42% |
| Spills | Number and volume of significant spills | 25% |
| **Biodiversity Conservation** | | |
| Protection of habitat and biodiversity management | Statement, code, or policy on biodiversity management (y/n) Provide description and link. | 46% |
| Impact on endangered, vulnerable, or rare species | Company/project located in or near an area known to contain endangered, vulnerable, or rare species (y/n). Provide description and link | 23% |
| **Climate Adaptation** | | |
| Prevent or adapt to climate change | Steps to prevent and (if not preventable) adapt to the impact of climate change on the company's ability to operate profitably or the quality of its products and services | 38% 38% |

*(Continued on next page.)*

[12] Frameworks and standards analyzed include reporting frameworks (GRI, SASB), financial analysis frameworks (EFFAS/DVFA, DJSI), information service providers (Asset4, BBG, Sustainalytics), regulation and quasi-regulation (European Union, BM&F Bovespa, World Federation of Exchange, Sustainable Stock Exchange Initiative), and investor initiatives (CERES).

TABLE 3.3: Most Commonly Reported E&S Metrics *(Continued from previous page)*

| TOPICS | ILLUSTRATIVE METRICS | FREQ. |
|---|---|---|
| **LABOR AND WORKING CONDITIONS** | | |
| **Workers Treatment** | | |
| Forced and child labor in the company | Legal actions, employee grievances, or public controversies involving forced and child labor in the company's operations (#). Describe corrective actions. | 54% |
| Wages | Average hourly wage and % of employees earning minimum wage | 31% |
| Training | Hours of training per year per employee, broken down by gender | 25% |
| Temporary workers | Temporary Worker Rate | 23% |
| **Workers Relations** | | |
| Collective bargaining agreements | % of active workforce covered under collective bargaining agreements | 69% |
| Turnover | Voluntary and involuntary employee turnover rate by major employee category | 69% |
| Worker feedback and recourse | Worker grievance mechanism (y/n). Provide description and link. | 23% |
| **Diversity** | | |
| Workforce composition | Workforce composition by gender and ethnicity (#) | 69% |
| Opportunities and fairness for all workers | Legal actions, employee grievances, or public controversies involving discrimination or equal remuneration (#). Describe corrective actions. | 35% |
| Gender pay ratio | Women/men pay ratio | 23% |
| **Health & Safety** | | |
| Injury and fatality | Injury rate (TRIR) and fatality rate for direct and contract employees | 100% |
| Lost Time Incident Rate | Lost Time Incident Rate for direct and contract workers (per 200,000 hours worked or per 100 fulltime equivalent employees) | 42% |
| **COMMUNITY** | | |
| Human rights due diligence and management | Management of human rights in the value chain (codes, policies, prevention, and treatment) | 50% |
| Security force impact on a community | Statement, policy, or code on security forces and interaction with local community (y/n). Provide description and link. | 46% |
| Operations near indigenous people | Company/project in area that indigenous peoples may live on, migrate through, or use (y/n) | 31% |
| Human rights violations | Involvement in human rights violation | 25% |
| Impact on indigenous peoples | Company/project in area that indigenous peoples may live on, migrate through, or use (y/n) | 23% |

*(Continued on next page.)*

**TABLE 3.3: Most Commonly Reported E&S Metrics** *(Continued from previous page)*

| TOPICS | ILLUSTRATIVE METRICS | FREQ. |
|---|---|---|
| **PRODUCTS** | | |
| Impact consideration in product design | Integration of environmental and social consideration in products and services | 38% |
| Energy/GHG intensity of products | Energy/fuel/GHGs efficiency of products during use-phase | 38% |
| Data privacy policies | Policies and practices on collection, use, and retention of customer information | 38% |
| Packaging | Packaging weight (Tn), % from recycled or renewable materials, % recyclable or compostable | 31% |
| Recalls | Product recalls: # of recalls; total units recalled | 31% |
| Materials and chemicals of concern | Process to identify and manage emerging materials and chemicals of concern in products | 31% |
| Incidents | Product safety fines and settlements (US$) | 23% |
| **ETHICS (and GOVERNMENT RELATIONS)** | | |
| Anticorruption (management) | Management of anticorruption in the value chain (codes, policies, prevention, and treatment) | 69% |
| Political spending | Political spending, lobbying expenditures (including trade associations) (US$) | 38% |
| Anticorruption (incidents/fines) | Fines and settlements for corruption or bribery (US$), description of major fines and corrective actions | 31% |
| Competitive behavior | Amount of legal and regulatory fines and settlements associated with anticompetitive practices | 25% |
| **SOURCING** | | |
| Suppliers | % of suppliers selected and monitored according to social and environmental criteria | 85% |
| Raw materials (recycled/renewables) | % of raw materials from 1) recycled content and 2) renewable resources | 46% |
| Conflict minerals | % of tungsten, tin, tantalum, and gold smelters within the supply chain that are verified conflict-free | 38% |
| Critical materials | Critical materials: % of materials cost | 23% |

Note: Some of the metrics in this table are duplicated from the Core Sustainability Indicators—IFC Performance Standards in Table 3.1.

Source: IFC.

### *Suggested Metrics for Economic and Social Development*

Table 3.4 provides examples of commonly reported economic and social KPIs that have a direct correspondence with the UN Sustainable Development Goals and their indicators.

**Table 3.4:** Link between ESG Metrics and SDGs Indicators

| TOPIC | SUGGESTED METRICS | SDG | SDG INDICATOR |
|---|---|---|---|
| **ENVIRONMENT** | | | |
| Air Pollutants | NOx (excl. N2O), SOx, volatile organic compounds, particulate matter (Tn) | SDG 11 (Sustainable Cities) | 11.6.2: Annual mean levels of fine particulate matter (e.g., PM2.5 and PM10) in cities (population weighted) |
| Waste | Waste from operations (t), % hazardous, % recycled, intensity (waste/sales) | SDG 12 (Waste) | 12.4.2: Hazardous waste generated per capita and proportion of hazardous waste treated, by type of treatment<br>12.5.1: National recycling rate, tons of material recycled |
| Energy | Energy consumed (GW), % grid electricity, % renewables, intensity (energy/sales) | SDG 7 (Energy) | 7.2.1: Renewable energy share in the total final energy consumption<br>7.3.1: Energy intensity measured in terms of primary energy and GDP |
| Water Use | Water used (m3), % recycled, % in water stress areas, intensity (water use/sales) | SDG 6 (Water Efficiency) | 6.3: Improve water quality by reducing pollution, eliminating dumping, and minimizing release of hazardous chemicals and materials, drastically reducing the proportion of untreated wastewater and substantially increasing recycling and safe reuse globally<br>6.3.1: Proportion of wastewater safely treated<br>6.4: Substantially increase water-use efficiency across all sectors and ensure sustainable withdrawals and supply of freshwater<br>6.4.1: Change in water-use efficiency over time<br>6.4.2: Level of water stress: freshwater withdrawal as a proportion of available freshwater resources<br>6.b: Support and strengthen the participation of local communities in improving water and sanitation management<br>6.b.1: Proportion of local administrative units with established and operational policies and procedures for participation of local communities in water and sanitation management |

*(Continued on next page.)*

**TABLE 3.4: Link between ESG Metrics and SDGs Indicators** *(Continued from previous page)*

| TOPIC | SUGGESTED METRICS | SDG | SDG INDICATOR |
|---|---|---|---|
| **ENVIRONMENT** | | | |
| Raw materials | % from 1) recycled content and 2) renewable resources | SDG 12 (Resources) | 12.2: By 2030, achieve the sustainable management and efficient use of natural resources<br>12.2.1: Material footprint, material footprint per capita, and material footprint per GDP<br>12.2.2: Domestic material consumption, domestic material consumption per capita, and domestic material consumption per GDP |
| Climate Change | Steps to prevent and (if not preventable) adapt to the impact of climate change on the company's ability to operate profitably or the quality of its products and services | SDG 13 (Climate Resilience) | 13.1: Strengthen resilience and adaptive capacity to climate-related hazards and natural disasters |
| Biodiversity | Impact on ecosystem services; impact on protected areas, parks, or reserves; impact on endangered, vulnerable, or rare species; habitat protection and biodiversity management; impact on water sources, rivers, lakes, or wetlands | SDG 15 (Land) | 15.3/15.5: Take action to reduce the degradation of natural habitats, halt loss of biodiversity, and strive to achieve a land-degradation-neutral project<br>15.3.1: Proportion of land that is degraded over total land area<br>15.5.1: Red List Index |
| **EMPLOYEES** | | | |
| Treatment | Average hourly wage and % of employees earning minimum wage | SDG 8 (Decent Work and Economic Growth) | 8.5: By 2030, achieve full and productive employment and decent work for all women and men, including for young people and persons with disabilities, and equal pay for work of equal value<br>8.5.1: Average hourly earnings of female and male employees, by occupation, age, and persons with disabilities |
| | Forced or child labor in the company and its supply chain | SDG 8 | 8.7.1: Proportion and number of children aged 5–17 years engaged in child labor, by sex and age |
| Relations | % of active workforce covered under collective bargaining agreements | SDG 8 | 8.8.2: Level of national compliance with labor rights (freedom of association and collective bargaining) based on International Labour Organization (ILO) textual sources and national legislation, by sex and migrant status |

*(Continued on next page.)*

**TABLE 3.4: Link between ESG Metrics and SDGs Indicators** *(Continued from previous page)*

| TOPIC | SUGGESTED METRICS | SDG | SDG INDICATOR |
|---|---|---|---|
| **EMPLOYEES** | | | |
| Nondiscrimination | Workforce composition by gender and ethnicity (#) | SDG 8 | 8.5: By 2030, achieve full and productive employment and decent work for all women and men, including for young people and persons with disabilities, and equal pay for work of equal value<br>8.5.2: Unemployment rate, by sex, age and persons with disabilities |
| Safety | Injury rate (TRIR) and fatality rate for direct and contract employees | SDG 8 | 8.8.1: Frequency rates of fatal and nonfatal occupational injuries, by sex and migrant status |
| **ETHICS** | | | |
| Anticorruption | Management of anticorruption in the value chain (codes, policies, prevention & treatment) (y/n) | SDG 16 | 16.5: Reduce corruption and bribery in all their forms<br>16.5.2: Proportion of businesses that had at least one contact with a public official and that paid a bribe to a public official, or were asked for a bribe by those public officials during the previous 12 months |
| **GOVERNANCE** | | | |
| Board Diversity | % women (non-promoter/sponsor) on board | SDG 5 (Gender Equality)<br>SDG 10 (Reduce Inequality) | 5.1: End all forms of discrimination against all women and girls everywhere<br>10.2: By 2030, empower and promote the social, economic, and political inclusion of all, irrespective of age, sex, disability, race, ethnicity, origin, religion, or economic or other status |
| Annual Report | Does the annual report or the sustainability report include ESG information? (y/n) | SDG 12 (Sustainable Consumption and Production)<br>SDG 17 (Implementation and Partnership) | 12.6: Encourage companies, especially large and transnational companies, to adopt sustainable practices and to integrate sustainability information into their reporting cycle<br>17.5: Adopt and implement investment promotion regimes for least developed countries<br>Target 17.19: By 2030, build on existing initiatives to develop measurements of progress on sustainable development that complement gross domestic product, and support statistical capacity-building in developing countries |

Source: IFC.

# Part II: Reporting Guidance

# Part II: Reporting Guidance

This section of the Toolkit provides guidance on the preparation of the information that will be disclosed as part of the annual report. It includes guidance on the materiality of information reported as well as its quality—its reliability, completeness, conciseness, consistency, and comparability. This section also includes guidance on the scope of the information reported, the dual mandatory and voluntary nature of reporting, and special considerations for nonlisted companies.

Corporate reporting, like all business activities, should keep pace with developing economic realities and address the needs of a wide stakeholder audience. Companies are encouraged to view all reporting as contributing to better communication and an improved approach to accountability.

**NOTE: Annual reports should be provided in English when companies seek to attract foreign investors.**

## Materiality

The concept of materiality serves as a test of what should be reported by bringing into balance different objectives of corporate reporting:

- Making sure investors have sufficient information to make informed decisions;
- Ensuring the cost-benefit of disclosure for companies and society;
- Avoiding unnecessary information that can obscure a clear view of company performance.

Most countries use materiality as the test of what should be reported. National regulations typically focus on current shareholders or investors and their ability to understand the current and future performance of the company; if the information could affect the company's share price or investor decisions to buy or sell its securities, it is usually considered material.

The IASB's International Financial Reporting Standards define material information as follows: "Information is material if omitting it or misstating it could influence decisions that users make on the basis of financial information about a specific reporting entity. In other words, materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of an individual entity's financial report."

***What specifically should be disclosed?*** In some cases, regulation provides only a general requirement to disclose "material" information on a particular topic, giving companies substantial discretion to determine what is material. In other cases, the content of a report will be well defined by regulation or good practice. For instance, company discretion is more limited in the areas of governance and the board, related-party transactions, and ownership. National regulations and standards tend to give more specific guidance on what to disclose in these areas.

However, materiality determination is key in the areas of strategy and performance, risk, and sustainability. Each of those is very specific to the company, and what companies present may differ significantly— in substance and appearance. (For more information on how materiality applies to sustainability issues, see ***1.4.1. Assessment of Key Sustainability Opportunities and Risks***, page 28 of this Toolkit.)

The concept of materiality is useful in determining the amount of detail to disclose for a specific item. For example, a report may contain qualifications for each board member; however, only key qualifications—such as, in some cases, a board member's education—are likely to be material.

Materiality sometimes requires a forward-looking approach, to provide an understanding of the future prospects of the company. For material risks, a typical approach is to plot—on a "heat map"—the *likelihood* of impact versus the *magnitude* of impact. For sustainability risks and impacts, a materiality map or assessment can help companies determine what is important for the core operations of the company versus what is important for its stakeholders.

***What should* not *be disclosed?*** As a corollary to the requirement to disclose material information, regulations and best practices emphasize the need to avoid the disclosure of immaterial information that can obscure a clear view of company performance. (For further discussion of materiality assessment, see ***Appendix A*** of this Toolkit.)

## Information Quality

Good reporting requires a careful balance between competing priorities:

- A ***complete*** presentation of all material information;
- Ensuring that the report is sufficiently ***concise*** to preserve focus and readability;
- Tailoring the report to the ***company*** to give the reader a strong understanding of the company and the environment it operates in;
- Keeping the presentation ***comparable***—to the company's reporting in previous periods and to the reporting of other companies in a similar industry—to make it easy for investors and others to use.

Clearly, preparing the annual report involves tradeoffs. Attempting to be complete and comprehensive can lead to overly long reports that can easily become disjointed. On the other hand, too much emphasis on conciseness can produce some very readable reports, but they may omit key information.

Similarly, reports should be specific about the companies that issue them. A reader should understand the performance, main products, markets, risks, and future plans of this particular company—not just concerns that could be applied to any company. Regulators increasingly encourage companies to take some initiative in tailoring reports to best communicate their story with investors and others. But investors frequently express frustration that information is not comparable from one report to the next—that it is too hard to find particular items in one report and compare them to the reports of other companies. This is an especially acute concern for institutional investors analyzing and investing in large numbers of companies.

**BEST-PRACTICE RESOURCES:**
**Quality of Nonfinancial Information**

Business-critical nonfinancial information, including sustainability, should be of the same quality as financial statements.

## Scope of Disclosure

The report should cover the activities and results of the company itself and any entity in which the company holds a controlling interest (generally defined as 50 percent ownership or more). Financial reporting is typically consolidated among the reporting entity and its controlled entities. Measures of consolidated financial and operational performance include the totality of the controlled entity, regardless of the size of the minority interest, and the value of the minority interest is accounted for separately in the income statement and balance sheet.

Information on affiliated but unconsolidated entities should be included to the extent that it is necessary to explain the strategy, governance, and performance of the company and its consolidated entities. However, unconsolidated entities should not be factored into the calculation of the consolidated financial, operational, and sustainability performance.

For financial reporting purposes, minority interests in unconsolidated entities are accounted for using the equity method (profits in proportion of the minority interest) or the fair market value of the investment.

## Disclosure Requirements

Disclosure requirements are different for listed and nonlisted companies. Depending on the jurisdiction, the *reporting elements* and *suggested disclosure* can be legally mandated, voluntary, or not addressed.

### Listed Companies

For companies that issue securities to the public, it is important to be familiar with the various requirements for the annual report and other disclosure, including securities law, corporate law, stock exchange listing requirements, and corporate governance codes. Also, regulators or exchanges will often give supplemental guidance on how to prepare annual reports, including guidance on sustainability and integrated reporting.

Specific challenges can arise from mixing mandatory and voluntary information, and from mixing audited financial information (which is prepared in accordance with generally accepted accounting standards) and forward-looking information (which is not so prepared). Therefore, regulations often impose specific requirements for the disclosure of voluntary and forward-looking information in financial statements or investor reports.

### Nonlisted Companies

In some countries, such as India and the United Kingdom, larger nonlisted companies have a range of reporting requirements. Even when requirements are minimal, public reporting can still be important for private companies. Accessing new funds, engaging new stakeholders, and meeting the demands of current stakeholders as the company grows and becomes more complex will still require telling the company's story. Nonlisted companies can more easily tailor their reporting to particular investors and stakeholders.

## Who Should Be Involved in Preparing the Annual Report?

The process of preparing and filing an integrated annual report should be directed by the company management (most appropriately the corporate secretary) and overseen by the board of directors and its different committees (audit, governance, sustainability).

Ultimately, the company management (usually the top executives such as the CEO and CFO) and the board are responsible for the timely issuance and accuracy of mandatory and voluntary reports.

Preparation of the report requires the involvement of a multidisciplinary team from a number of departments in the company, including the following:

- Strategy
- Functional areas (sales, marketing, manufacturing)
- Operations
- Sustainability or environmental, health, and safety (EH&S)
- Human resources
- Risk management, internal control, and audit
- Legal and compliance
- Finance and accounting
- Investor relations
- Information technology

External auditors carry out the independent audit of financial statements and selected nonfinancial information. External auditors report to the board of directors (usually the audit committee), acting on behalf of shareholders.

## Reporting Formats

A digital copy of the annual report is often the main channel of access to the report for investors and other stakeholders. Although some companies create a Web-based version of the report, it is recommended that the annual report be made available as a PDF (portable document format), which combines many of the advantages of a printed physical copy of the report with the flexibility of a digital format.

The Financial Reporting Council (FRC) Lab Project notes that PDFs of annual reports should have the following attributes, which are valued by investors (FRC 2015):

- ***Has a clear boundary:*** Allows investors to have a clear understanding of the document, its scope and content.
- ***Is assured:*** To investors, the PDF benefits from the same level of assurance as the hard-copy annual report.
- ***Covers a defined period:*** Represents a report at a point in time that does not change, as opposed to webpages, which can be subject to update.
- ***Can be downloaded:*** Provides comfort that the investor's copy will not be subject to manipulation or removal.
- ***Is searchable:*** Gives investors more confidence that the results are relevant, as the search operates within the boundary of the single, clearly purposed document. This also allows them to quickly pinpoint areas of interest within that report.
- ***Is (relatively) timely:*** The PDF is available online prior to the hard copy arriving in the post, and it can be accessed by investors as soon as it is released.
- ***Is portable:*** The PDF can easily be stored and accessed across most devices.
- ***Is ubiquitous:*** Widespread adoption of the PDF format by companies means that investors can access and analyze files across companies and years.

The FRC recommends keeping the PDF simple—avoiding e-books and interactive PDFs, which are not valued by investors. It also recommends providing archives of the company's past annual reports as well as other supporting information—making available 5–10 years of historical records—on the company website (FRC 2015).

## Technology and Reporting

Technology plays an increasingly important role in the development of corporate reporting. Digital technologies in particular, such as artificial intelligence and blockchain, are enablers as well as drivers of this change. New technologies have already disrupted incumbent and existing business models, and all companies are increasingly using new technologies to facilitate transactions, exchange information, or connect people.

Undoubtedly, the same technologies will also significantly affect the way corporate reports are prepared and delivered to a company's stakeholders. For example, regulators are looking at the possible role of blockchain-based solutions in streamlining the reporting process—that is, the production, distribution, and consumption of financial and other corporate information.

Data analytics and artificial intelligence are further examples of how digital technologies are disrupting corporate reporting. These technologies can play a crucial role in improving a company's capacity to collect and curate information, as well as their communication of that information.

This will also allow for "continuous reporting," which instead of being implemented on an "annual" or other fixed-term basis, will be continuously updated and disseminated online. Continuous reporting will create a more engaged and responsive dialogue among the company, investors, and other stakeholders.

Companies are encouraged to innovate in their use of technology to support corporate reporting, both regulated and voluntary reporting (Kriz and Blomme 2016).

## Disseminating the Annual Report

Annual reports and related sources of information have different audiences and serve different purposes, including meeting disclosure requirements, strategic communication about the company, and engagement with smaller shareholders and stakeholders.

### Disclosure Requirements

Market authorities or stock exchanges typically impose disclosure and transparency requirements on larger, publicly listed companies, including making the annual report publicly available. For publicly listed companies, disclosure requirements are very strict, based on the need to disclose all material information fairly and equally to all shareholders, to avoid information asymmetry and insider information.

Public companies are also required to disclose material information in a timely fashion, which entails the publication of quarterly unaudited financial statements and periodic or current reports for material events that occur between the reporting cycles.

For this reason, annual reports, as well as quarterly and periodic reports, must typically be filed with the relevant market authorities and exchanges. In addition, these reports should be made available via the company's main communication channels, including the corporate website.

To make financial information easily accessible and to improve market efficiency, market authorities may also require or encourage the disclosure of financial information in electronic format, such as XBRL (a standardized, machine-readable format for tagging business and financial information).

### Strategic Communication

Beyond meeting disclosure requirements, annual reports are a great tool for promoting the company to stakeholders, including investors, employees, business partners, customers, and the community, as well as for sharing the company's vision, strategy, performance, and impact.

Companies should maximize the dissemination of their annual report and related information beyond the required filings. For example, public companies typically hold investor calls at the time of release of annual and quarterly financial reports, where the top management presents key highlights of the reports. Similarly, the information in annual reports can be used in investor roadshows to support the company's access to new capital.

Another important channel for communicating strategic, governance, and performance information is the CEO letter that introduces the annual report. Example II.1 provides an excerpt of Amazon's CEO letter to its shareholders, highlighting the company's sustainability performance. The letter introduces the company annual report and Form 10-K filed with the U.S. Securities and Exchange Commission.

Companies can also use other digital channels, such as social media, to increase the distribution of their report. Printed (and PDF) versions of the report can be supplemented by online versions (microsites). Also, while English is usually the required language for global companies accessing global capital markets, companies should make sure to have the report available in the language of the targeted audience of the report.

## Engaging with Minority Shareholders and Stakeholders

In all cases, the company should make sure the information is shared fairly and equally among all shareholders, including individual and minority shareholders. In fact, a strategic dissemination of the annual report can be a tool to actively engage with smaller and minority shareholders.

Similarly, the strategic distribution of integrated annual reports that incorporate key sustainability information can be a tool to enhance stakeholder engagement and communication with the communities affected by the company.

**Example II.1:** Amazon 2017 CEO Letter to Shareholders—Excerpt

**2017 Letter to Shareholders**
**Jeffrey P. Bezos, Founder and Chief Executive Officer, Amazon.com, Inc.**

*Sustainability*—We are committed to minimizing carbon emissions by optimizing our transportation network, improving product packaging, and enhancing energy efficiency in our operations, and we have a long-term goal to power our global infrastructure using 100% renewable energy. We recently launched Amazon Wind Farm Texas, our largest wind farm yet, which generates more than 1,000,000 megawatt hours of clean energy annually from over 100 turbines. We have plans to host solar energy systems at 50 fulfillment centers by 2020, and have launched 24 wind and solar projects across the U.S. with more than 29 additional projects to come. Together, Amazon's renewable energy projects now produce enough clean energy to power over 330,000 homes annually. In 2017 we celebrated the 10-year anniversary of Frustration-Free Packaging, the first of a suite of sustainable packaging initiatives that have eliminated more than 244,000 tons of packaging materials over the past 10 years. In addition, in 2017 alone our programs significantly reduced packaging waste, eliminating the equivalent of 305 million shipping boxes. And across the world, Amazon is contracting with our service providers to launch our first low-pollution last-mile fleet. Already today, a portion of our European delivery fleet is comprised of low-pollution electric and natural gas vans and cars, and we have over 40 electric scooters and e-cargo bikes that complete local urban deliveries.

Source: Amazon.

# Appendixes

# Appendix A: Materiality Assessment for Sustainability Issues

There is currently a debate on the definition of materiality and its application to sustainability. Different reporting formats and frameworks (IFRS, GRI, IIRC, SASB) have slightly differing definitions, as they prioritize the information needs of different stakeholders. (For definitions of materiality, see ***Box 1.2***, page 30 of this Toolkit.)

Section 1.4 of this Toolkit provides common ground among different perspectives and initiatives, and Part II offers a more general approach to materiality as it relates to the entire set of information, beyond just sustainability.

However, despite the variety of ways to approach materiality, companies can take a number of practical steps to assess materiality of sustainability topics, based on generally accepted standards and the experience of many companies.

## Step One: Identify relevant matters.

To identify relevant matters, a reporting organization must determine the specific definition of materiality it will use in its reporting. This decision may be made when the reporting organization commits to use a specific reporting framework. The definition of materiality focuses on the material information needs of the primary stakeholders for the particular report the company is issuing (IIRC 2016).

For sustainability reporting, GRI defines a material topic as a "topic that reflects a reporting organization's significant economic, environmental and social impacts; or that substantively influences the assessments and decisions of stakeholders" (GRI 2016b). Issues are usually deemed relevant for an entire sector.

For integrated reporting, issues are considered relevant based on whether the matter has an effect on the reporting organization's ability to create value over time. Relevant matters are usually linked to the reporting organization's strategy or business model—or specific inputs or outputs of the business model—and therefore are more entity-specific or at least industry-specific.

The IIRC's <IR> Framework defines material information as "matters that substantively affect the organization's ability to create value over the short, medium and long term," where value creation is defined with reference to multiple capitals: financial, manufactured, intellectual, human, social and relationship, and natural (IIRC 2013).

SASB provides guidance on disclosure of material sustainability for U.S. listed companies based on the definition of materiality adopted by the U.S. Supreme Court and interpretations by the U.S. Securities and Exchange Commission (SEC 1989; SEC 2003). According to the SEC, the following is material information (SASB 2018):

- Information necessary to an understanding of the company's financial condition and operating performance, as well as its prospects for the future;
- Known trends, events, and uncertainties that are reasonably likely to have material impacts on the company's financial condition or operating performance;
- Risk factors that may affect a company's business, operations, industry, or financial position or its future financial performance.

It is best practice for a company to disclose the definition of materiality it used to identify material issues and to structure reporting.

## Step Two: Assess the importance of relevant matters and prioritize these matters.

The following are different methods of prioritizing relevant issues to determine what is material.

***Materiality matrix.*** Assess what is important to the reporting organization compared with what is important to the organization's stakeholders—using an axis for each and plotting a matrix. In reporting, it is not necessary to produce a materiality matrix, but if this is the process the reporting organization uses for prioritization, some stakeholders may find such a matrix useful (GRI 2016b).

***Risk and opportunity assessment.*** Embed or integrate the prioritization into ongoing risk and opportunity assessment processes (IIRC 2013). Using this method of prioritizing, a company ensures that matters determined to be material are appropriately addressed in relevant governance structures, in strategy development and risk mitigation, and in management processes.

***Stakeholder engagement.*** The interests and expectations of stakeholders are an important factor in identifying relevant matters to be considered for inclusion in reporting. Some companies assess stakeholder interests specifically related to reporting, while others engage with stakeholders on an ongoing basis and use knowledge from this ongoing engagement to identify issues that are material. Because stakeholder interests and expectations change, identifying matters that are relevant to stakeholders should be done annually.

***Probability-magnitude test:*** The magnitude of the effect of an issue and the likelihood of occurrence should be considered when assessing and prioritizing relevant issues. Issues that have a greater likelihood of occurring or a greater likelihood of significant impact on either the reporting organization or its stakeholders should be determined to be of greater importance.

To help companies apply the concept of materiality to sustainability, the IIRC and the SASB have produced specific guidance on how to identify material issues in the context of integrated financial and sustainability information. (See Boxes A.1 and A.2.)

## Step Three: Respond to material issues.

Issues that are determined to be highly material need to be managed. The appropriate process depends on the specifics of the material issue, but just identifying what is material is not enough. Generally, material issues can be addressed through strategy implementation, risk management, or specific policies or strategic objectives related to the issue in question. For climate change, for instance, companies may institute specific policies and objectives related to emissions. If an issue does not warrant active management, it is probably not material (GRI 2016b).

## Step Four: Use material issues to shape disclosure.

Once a reporting organization defines its material issues, these issues should be used to shape reporting. Since material information is that which is capable of making a difference to the proper evaluation of the issue at hand, it follows that immaterial information does not make such a difference (IIRC 2016).

In other words, material information about material topics is useful to external report readers, but immaterial information is not. Reporting entities should strive to report useful information and make the case that reporting is structured using materiality to focus on what matters.

**Box A.1:** The <IR> Framework Guiding Principles on Materiality

The International <IR> Framework provides the following guidance for assessing a matter's importance.

3.24 Not all relevant matters will be considered material. To be included in an integrated report, a matter also needs to be sufficiently important in terms of its known or potential effect on value creation. This involves evaluating the magnitude of the matter's effect and, if it is uncertain whether the matter will occur, its likelihood of occurrence.

3.25 Magnitude is evaluated by considering whether the matter's effect on strategy, governance, performance or prospects is such that it has the potential to substantively influence value creation over time. This requires judgment and will depend on the nature of the matter in question. Matters may be considered material either individually or in the aggregate.

3.26 Evaluating the magnitude of a matter's effect does not imply that the effect needs to be quantified. Depending on the nature of the matter, a qualitative evaluation might be more appropriate.

3.27 In evaluating the magnitude of effect, the organization considers:

- Quantitative and qualitative factors
- Financial, operational, strategic, reputational and regulatory perspectives
- Area of the effect, be it internal or external
- Time frame.

Source: IIRC.

**Box A.2:** The SASB's Five-Factor Materiality Test

The SASB designed an evidence-based approach to help select the sustainability topics for which to develop a corresponding standard. This five-factor test can also help a company's management select material sustainability topics that should be reported.

The first factor addresses direct financial impacts and risks related to the company's performance on each topic. Each of the next three factors addresses drivers and trends that have the potential for indirect impact on the company's financial performance. The fifth factor addresses upside opportunities that can have an impact on the company's financial performance.

- DIRECT FINANCIAL IMPACTS & RISK: This factor assesses the likelihood that corporate performance on the topic will have a direct and measurable impact on near- or medium-term financial performance.
- LEGAL, REGULATORY, & POLICY DRIVERS: Existing, evolving, or emerging regulation may influence company actions and affect financial performance by forcing the internalization of certain costs and/or by creating upside opportunity associated with sustainability-related externalities.
- INDUSTRY NORMS, BEST PRACTICES, & COMPETITIVE DRIVERS: Peer actions and disclosure on industry issues may create pressure for high standards of performance related to the management and disclosure of sustainability topics in order to remain competitive and satisfy investors.
- STAKEHOLDER CONCERNS & SOCIAL TRENDS: Stakeholders may raise concerns that could influence medium- or long-term financial or operating performance or create acute short-term financial impacts through changes in customer demand, influence on new regulations, and disruptions to business viability.
- OPPORTUNITIES FOR INNOVATION: New products and business models to address the topic can drive market expansion or have the potential for a disruptive change that provides new sources of competitive advantage. Financial impacts and risks associated with these innovations may be of interest to investors.

Source: Adapted from SASB (2015).

# Appendix B: Questions the Board Should Ask on ESG Management and Disclosure

Below is a set of questions that the board of directors should ask when exercising oversight of the company's management and disclosure of environmental, social, and governance matters.

## Strategy

- Is there an integrated corporate strategy that includes goals and targets for financial and E&S performance? If not, and there are two separate strategies, how are these strategies linked internally? How is the link explained in corporate reporting?
- What are the key sustainability or E&S factors that affect the company strategy regarding risks and opportunities? Which factors affect the company's short-term financial performance? Is there a long-term value-creation process in place?
- Does the company have a documented method for assessing material E&S issues?
- Is the strategy consistent with information that the company has identified as material—including E&S information? Does the strategy include measurable targets and KPIs? Are sustainability objectives reviewed by the board?
- Is E&S information integrated into the risk management framework? Does it provide insight into emerging risks that may not be captured by traditional areas of risk management (operational, financial, and so on)?

## Governance

- Are key areas of corporate governance addressed in the report, including commitment to corporate governance, culture and leadership, board composition and functioning, compliance, risk appetite, executive compensation, controlling shareholders, and stakeholder engagement?
- How are E&S issues integrated into governance structures and processes, including risk management, control environment, compliance, board composition, disclosures?
- Is there an internal audit function and a process to ensure the accuracy of financial information? Does it include E&S information?

## Stakeholder Engagement

- Who are the company's key stakeholders? What is the process to identify them? Does the board recognize its responsibilities to stakeholders beyond shareholders?
- Is there a mechanism for stakeholder engagement and grievance redressal?
- Are the process and results of stakeholder engagement disclosed publicly? Is relevant information disclosed to Affected Communities in an understandable format and language?

## Performance

- How does the company's performance compare with its peers, including on the management of critical ESG issues?
- How does reported performance compare with the company's internal management dashboard?
- Does the reported ESG information align with material issues and priorities for the company?
- Are the links between ESG and financial performance explained?

## Disclosure and Transparency

- Who is the primary audience for reporting? What information do they need? Does company disclosure meet their information needs?
- What framework should be used (and why) to report sustainability information: GRI, IIRC, SASB? Should it be reported together with financial information?

# Appendix C: Internal Planning for Annual Report Preparation

The corporate secretary has a central role in preparing the annual report and in all aspects of the report. Other internal company departments and groups are also valuable resources for report preparation. Table C.1 offers suggestions regarding which internal entities may be critical resources for which elements of the report—and provides examples of key questions to ask in preparing the annual report. (The table follows the model annual report presented in ***Table 1.1: Model Structure of an Annual Report***, on page 15 of this Toolkit.)

### Table C.1: Internal Resources for the Annual Report, and Key Questions to Ask

| Type of Information | Who Would This Information Come From? | Questions to Think About |
|---|---|---|
| **Strategy** | | |
| Business Model | • Strategy<br>• Operations | • What does the company do, what makes it distinctive? Its customers, products or services, or business processes?<br>• Does the company have a clear business model? Can this be clearly articulated and/or presented in a diagram?<br>• What are the inputs, outputs, and outcomes of the company's activities? Its key relationships? |
| Business Environment | • Strategy<br>• Operations<br>• Sustainability | • Where does the company operate?<br>• What is the internal operating environment?<br>• What is the external environment, and what are the trends in the environment?<br>• How does the company's structure relate to its environment? |
| Strategic Objectives | • Strategy<br>• Executive Management<br>• Board of Directors<br>• Sustainability | • Where does the company want to go, and how does it intend to get there?<br>• How does the company preserve and create value?<br>• What are the short- and long-term objectives?<br>• What financial and nonfinancial KPIs are used to ensure that the company is delivering on its strategy?<br>• How does the strategy respond to the business environment? In other words, why is the strategy the right strategy?<br>• What is the governance for the strategy? How is the board involved? |
| Risk Analysis and Response | • Risk Management<br>• Executive Management<br>• Board of Directors | • What are the specific risks that may affect the company's ability to create value in the short and long term?<br>• Why does management believe these are the key risks?<br>• How are these risks assessed?<br>• How are they managed or mitigated?<br>• How does the company see these risks changing over time?<br>• How are new or emergent risks identified? |
| Sustainability Opportunities and Risks | • Sustainability<br>• Strategy<br>• Risk Management<br>• Executive Management<br>• Board of Directors | • What are the issues that affect financial performance, social/development impact, reputation, and license to operate?<br>• What are the issues that have an impact on the company's ability to create value?<br>• Is there a process for determining these issues?<br>• If so, how does this process feed into management priorities? |

*(Continued on next page.)*

TABLE C.1: Internal Resources for the Annual Report, and Key Questions to Ask *(Continued from previous page)*

| Type of Information | Who Would This Information Come From? | Questions to Think About |
|---|---|---|
| Introducing Key Performance Indicators | • Strategy<br>• Risk Management<br>• Operations | • How are KPIs chosen? Are they related to the company strategy? Are they used to evaluate performance?<br>• Do KPIs allow for performance comparisons over time and with similar companies? |
| **Corporate Governance** | | |
| Leadership and Culture | • Executive Management<br>• Board of Directors<br>• Board and Committee Chairs | • What does the company stand for?<br>• How is the company's culture defined and embedded throughout the company? What are the company's values?<br>• What are the relevant governance policies?<br>• How are these policies implemented in practice?<br>• What were the major focus areas for governance during the year? |
| Structure and Functioning of the Board of Directors | • Board of Directors<br>• Board and Committee Chairs, including Nomination | • What is the process to elect directors?<br>• What is the company's governance structure?<br>• What are the different committees of the board?<br>• Was the effectiveness of governance (or the board) reviewed during the year?<br>• How does the board oversee sustainability? |
| Control Environment | • Legal and Compliance<br>• Risk Management<br>• Internal Controls<br>• Internal Audit<br>• Audit or Risk Committee | • What is the company's risk appetite?<br>• What systems are in place to ensure compliance?<br>• What does the control environment look like?<br>• Does the company use a three-lines-of-defense model of risk management, internal controls, and internal audit?<br>• How does the board oversee this, and how is it accountable?<br>• Are there any suggestions for improvement from the external auditors? |
| Treatment of Minority Shareholders | • Finance and Accounting<br>• Legal and Compliance<br>• Remuneration Committee | • Who owns the company? How is it controlled?<br>• Is there a significant indirect ownership?<br>• Are there any controlling shareholders? Who are they and what is their role? Are there succession policies in place?<br>• What are the rights of minority shareholders, including during a change of control?<br>• What is the remuneration policy?<br>• What remuneration was awarded to the board and key executives in the current year?<br>• Does remuneration link to strategy? Does it link to performance?<br>• What is the policy on related-party transactions?<br>• Were significant transactions entered into or still in effect during the reporting period? |

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TABLE C.1: Internal Resources for the Annual Report, and Key Questions to Ask *(Continued from previous page)*

| Type of Information | Who Would This Information Come From? | Questions to Think About |
|---|---|---|
| Governance of Stakeholder Engagement | • Sustainability<br>• Board of Directors<br>• Strategy | • Who are the company's stakeholders, and what impact do the company's activities have on them?<br>• How are stakeholder concerns integrated into the strategy?<br>• What is the processes to manage stakeholder concerns, including grievance mechanisms and external communication?<br>• What is the role of the board? |
| **Financial Position and Performance** | | |
| Performance | • Executive Management<br>• Board of Directors<br>• Strategy<br>• Finance and Accounting<br>• Sustainability<br>• Risk Management | • What are the company's operational and financial results?<br>• What are some of the major trends driving operational and financial results, including investment needs, intangibles, and sustainability?<br>• What are the company's nonfinancial results, including on the management of sustainability risks and opportunities?<br>• How are different dimensions of performance (financial, operational, sustainability) linked?<br>• What are future performance targets and the outlook for future performance? |
| Financial Statements | • Accounting and Finance<br>• Legal and Compliance<br>• Audit and/or Finance Committee<br>• External Auditor | • What are the local requirements for financial reporting and auditing?<br>• What accounting standard should be followed—locally, globally?<br>• What additional financial information is required or recommended for the industry sector?<br>• How is the business segmented?<br>• What is the result of the external audit? |
| Sustainability Statements | • Executive Management<br>• Board of Directors<br>• Sustainability<br>• Strategy<br>• Finance and Accounting | • What are the cross-cutting, industry-specific, and entity-specific metrics that the company follows year on year?<br>• Is it possible to present more than one year's worth of data, for comparison?<br>• What reporting/accounting standards should be used? Can it be audited?<br>• What explanation is needed to ensure that the data are understandable and comparable? |

# Appendix D: IFC Corporate Governance Progression Matrix for Listed Companies (Integrating Environmental, Social, and Corporate Governance Issues)

The core of this Toolkit is the IFC Corporate Governance Progression Matrix for Listed Companies, but any organization—listed or not, and across sectors—can apply its concepts. This was the basis of the Toolkit, because it is the most comprehensive tool of its kind. Adapted versions of the Matrix—for financial institutions, small and medium enterprises, family-owned companies, and funds—will eventually be available on our website: www.ifc.org/corporategovernance.

## A. Commitment to Environmental, Social, and Governance (Leadership and Culture)

| | 1. Basic Practices | + | 2. Intermediate Practices | + | 3. Good International Practices | + | 4. Leadership |
|---|---|---|---|---|---|---|---|
| **Formalities** | 1. Written policies/corporate governance (CG) code addressing, at a minimum, the role of the board, rights and treatment of shareholders and other stakeholders, compliance with the law and transparency and disclosure, and stating the objectives and principles guiding the company.<br>2. Written policies that address, at a minimum, compliance with E&S law and regulations. | | 1. CG code, which addresses E&S issues.<br>2. Periodic disclosure to shareholders on CG code and practices, and their conformance to the country's code of best practices. | | | | 1. Adequacy of ESG policies and procedures is disclosed. |
| **Code of Ethics and Culture** | 3. Code of ethics and/or conduct approved by the board. | | 3. Code of ethics included in employee orientation program. | | 1. Codes of ethics and/or conduct fully integrate ESG practices in business activities. | | 2. Organization culture has embedded ESG awareness and a control consciousness throughout the organization. |
| **Designated Officer/ Functions** | 4. A company officer serves as a corporate secretary. | | 4. Designated fulltime CG officer and/ or company/corporate secretary. | | 2. Designated compliance function ensuring compliance with ESG policies and procedures, code of ethics and/or conduct.<br>3. Internal audit of implementation of ESG policies and procedures. | | |
| **Recognition** | | | 5. Publicly recognized as a national leader in ESG practices. | | 4. Publicly recognized as a regional leader in ESG practices. | | 3. Publicly recognized as a global leader in ESG practices. |

**B.** Structure and Functioning of the Board of Directors

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Role, Election, and Succession** | **1.** Board approves strategy.<br>**2.** Board members are given sufficient time and information to exercise their duty. | **1.** The board is fully elected on an annual basis. | **1.** Board-established succession plan for its members and senior management. | |
| **Composition** | **3.** The board has a number of independent directors in accordance with law and regulations. | **2.** 1/5 or more of board members are independent from management and controlling shareholders.<br>**3.** Board composition is based on a skills matrix. | **2.** 1/3 or more of board members are defined as independent in accordance with international best practices.[11]<br>**3.** Board diversity, including but not limited to gender, achieved in all aspects.<br>**4.** Roles of chair and CEO are separate. Board chair is independent, or a lead independent director has been designated. | **1.** 1/2 or more of board members are defined as independent in accordance with international best practices. |
| **Committees** | | **4.** Board-established audit committee. | **5.** Majority of audit committee membership is independent.<br>**6.** Specialized committees address special technical topics or potential conflicts of interest (e.g., nominations, compensation, technology/cybersecurity, E&S/sustainability, risk management, etc.), if applicable.<br>**7.** Committee of independent directors approves all material related-party transactions. | **2.** Audit committee membership 100% independent.<br>**3.** Special board-level CG committee established.<br>**4.** Specialized committees (governance, nominations, E&S/sustainability, and compensation) composed of a majority of independent directors, including the chair.<br>**5.** Compensation committee ensures that executive compensation is based on performance and long-term incentives (and adjusted for all types of current and future risk), based on financial and nonfinancial performance.<br>**6.** Risk management or other specialized committee with a majority of independent directors, and a majority who have experience managing risks. |
| **Meeting Frequency** | **4.** Board meets at least quarterly and is charged with objectively overseeing management. | | **8.** Non-executive directors meet separately at least once a year. | **7.** Independent directors periodically meet separately. |

[11]For example, IFC's "Indicative Independent Director Definition."

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**B.** Structure and Functioning of the Board of Directors *(continued from previous page)*

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Evaluation and Performance** | | 5. The board as a whole undergoes periodic evaluation.<br>6. Formal performance evaluation of management conducted annually. | 9. Board, committees and individual directors undergo an annual evaluation. | 8. Board and committee evaluations conducted/facilitated by third party. |
| **Oversight of E&S** | | 7. Board is trained on general E&S risk issues. | 10. Board is trained on industry E&S risk issues.<br>11. Strategy and risk appetite integrate E&S issues/risks.<br>12. At least 1 director has experience analyzing and interpreting E&S risks.<br>13. In sensitive industries,[12] 1 director or more has in-depth knowledge of E&S risks.<br>14. ESG issues are recurring board agenda items; board approves ESG strategy and E&S policies; routinely reviews E&S performance; ensures appropriate dialogue between the company and key stakeholders; and ensures effectiveness of External Communications Mechanism (ECM).<br>15. Board ensures that management systems are in place to identify and manage E&S risks and impacts. | 9. Special board-level committee established to review E&S issues.<br>10. Board reviews independent audits on effectiveness of Environment and Social Management System (ESMS), including stakeholder engagement processes and grievance mechanism. |

[12] Examples of "sensitive industries" include oil, gas, mining, heavy industry (steel, cement), and chemical manufacturers, and large agro-commodity production or processing.

## C. Control Environment (Internal Control System, Internal Audit Function, Risk Governance and Compliance)

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Internal Controls** | 1. Company has established documented internal control policies and procedures. | 1. Audit committee ensures corrective actions on control deficiencies identified in Management Letters. | 1. "Three lines of defense" model of risk management, internal control and internal audit has been adopted.[13] | 1. Control environment in accordance with highest international standards, including but not limited to IIA,[14] COSO, ISO 31000, 19600, 37001, and 27001.<br>2. The organizational structure adopted by management has a positive effect on performance, productivity, and leadership effectiveness. |
| **Internal Audit** | 2. Internal audit function regularly interfaces with external auditors and is accountable to the board. | | 2. Internal audit function is independent, objective, risk-based, and has unlimited scope of activity.<br>3. Head of internal audit reports to the audit committee and administratively to management. | 3. Audit committee ensures that the internal audit function is subject to periodic quality assessment by third party. |
| **Risk Governance** | | 2. Board approves risk appetite.<br>3. Company has established risk-management framework with a chief risk officer (CRO) or equivalent with unfettered access to the board. | 4. Board routinely monitors risk management and compliance with policies and procedures.<br>5. CRO reports to board-level risk management committee or equivalent. | |
| **Compliance** | | 4. Comprehensive compliance program annually reviewed, with mechanisms to report wrongdoing and misconduct. | 6. Chief compliance officer reports to the audit committee or equivalent and administratively to management. | |
| **External Audit** | 3. Written Management Letters provided by external auditor. | | 7. Audit committee owns relationship with external auditor (EA); agrees on scope and audit fees, and undertakes a periodic quality assessment of EA, using relevant Audit Quality Indicators.<br>8. Company has established CFO function. | 4. Audit committee reviews long association of EA. |

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[13] Namely, management is the first line of defense, risk management and compliance function are the second line of defense, and internal and external audit as independent assurance providers are the third line of defense.

[14] The Institute of Internal Auditors standards and related promulgations.

**C.** Control Environment (Internal Control System, Internal Audit Function, Risk Governance and Compliance) *(continued from previous page)*

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Integrating of E&S** | | **6.** Company has established industry practices in its E&S risk-management practices. | **9.** ESG activities are highly integrated, effective, and efficient and support the strategic and operational business objectives, and controls support objectives.<br>**10.** Periodic ESG, IT, and Information Security internal audits.<br>**11.** Comprehensive ESMS integrated in risk-management framework, and E&S risks are part of establishing the risk appetite.<br>**12.** E&S/sustainability head has unfettered access to senior management and CRO. | **5.** Board or sustainability committee ensures corrective actions on E&S issues.<br>**6.** Head of ESG reports to board E&S/sustainability committee.<br>**7.** ESMS is consistent with international standards (e.g., ISO 14001). |
| **Subsidiary Governance** | **4.** Company can identify its subsidiaries. | **7.** Company has policies and procedures to control the creation and dissolution of subsidiaries. | **13.** Company has a centralized subsidiary governance function and subsidiaries are categorized based on complexity and an appropriate governance framework applied to each category. | **8.** Board exercises oversight over the organizational structure and the activities of its subsidiaries. |

## D. Disclosure and Transparency

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Financial Reporting** | 1. Financial statements are audited by recognized independent external auditing firm. | 1. Financial statements prepared in accordance with International Financial Reporting Standards (IFRS) or equivalent.<br>2. Financial statements are audited in accordance with International Standards on Auditing (ISA). | 1. Audit committee oversees financial and nonfinancial reporting and audit.<br>2. Disclosure policy in place. | |
| **Risk Appetite** | | | 3. Company discloses its risk appetite. | 1. Risk appetite disclosure includes both qualitative and quantitative information. |
| **Corporate Disclosure** | 2. Compliance with all disclosure requirements and listing rules. Investors and financial analysts are treated equally regarding information disclosure.<br>3. Shareholders provided with accurate and timely information on the number of shares of all classes held by controlling shareholders and their affiliates (ownership concentration). | 3. Company discloses its code of ethics/ conduct. | 4. Significant ultimate beneficial shareholders are disclosed.<br>5. All disclosure and communications with shareholders and stakeholders made available online in a relevant and timely fashion. | 2. Tax transparency statement disclosed.<br>3. Executive compensation is disclosed.<br>4. Dividend policy is disclosed. |
| **ESG Disclosure** | 4. ESG/sustainability reporting, if any, follows minimum national requirement. | | 6. Annual report includes ESG information.<br>7. E&S/sustainability committee reviews annual report ESG information.<br>8. ESG data subject to independent review.<br>9. Information disclosed to Affected Communities is in understandable format and language.<br>10. Annual updates to locally Affected Communities. | 5. Nonfinancial disclosure in accordance with highest international standards (e.g., GRI, IIRC, SASB).<br>6. Periodic nonfinancial reporting of ESG issues that are of concern to stakeholders.<br>7. ESG data subject to an annual audit by an independent provider. |

## E. Treatment of Minority Shareholders

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Voting Rights** | 1. All shareholders of the same class have equal voting, subscription, and transfer rights.<br>2. Minority shareholders receive adequate notice and the agenda for all shareholders' meetings; and are permitted to participate and vote at shareholders' meetings. | 1. Effective representation of minority shareholders through cumulative voting or similar mechanisms; and economic rights such as inspection rights, exit rights, and tag-along rights.<br>2. Company has a dividend policy.<br>3. Clearly articulated and enforced policies on treatment of minority shareholders in changes of control. | 1. Effective shareholder voting mechanisms to protect minority shareholders from concentrated ownership or strong conflicts of interest with controlling shareholders (e.g., supermajority or "majority of minority" provisions).<br>2. Shareholders are consulted on executive compensation. | 1. Treatment of shareholders consistent with best international market practices.<br>2. Executive compensation subject to shareholder approval.<br>3. Each share is afforded one vote at the AGM. |
| **Protective Rights** | 3. Holders of all securities of the same type and class have access to equal information (fair disclosure). | 4. Well-understood policy and practice of full and timely disclosure to shareholders of all material related-party transactions and shareholder agreements. | 3. Well-understood policy and practices of company material transactions that could potentially affect the rights of minority shareholders.<br>4. Annual report discloses material risks to minority shareholders associated with controlling shareholders, ownership concentration, cross-holdings, and voting-power imbalances. | 4. Related-party transactions (over 2.5% of net assets or $150,000) subject to shareholder approval or stricter requirements.[15] |
| **Investor Relations** | 4. Investor relations function established. | | 5. Investor relations functions include program for engaging minority shareholders. | |

[15] Often, requisite thresholds are set by law/regulation in the listing jurisdiction; however, the OECD has recommended the referenced limits. See OECD, *Guide on Fighting Abusive Related Party Transactions in Asia* (2009) 31.

## F. Governance of Stakeholder Engagement

| | 1. Basic Practices | 2. Intermediate Practices | 3. Good International Practices | 4. Leadership |
|---|---|---|---|---|
| **Stakeholder Mapping** | 1. Ad hoc stakeholder-identification, including workers, customers, regulators, and the locally Affected Community. | 1. Key stakeholders identified also include local nongovernmental organizations (NGOs) and civil society organizations (CSOs). | 1. Formal stakeholder-mapping process and expanded definition of stakeholders includes contracted workers, primary- supply-chain workers, neighboring projects, and international NGOs and CSOs. | 1. Senior executive responsible for stakeholder relationships, including ensuring integration with strategy and target setting. |
| **Stakeholder Engagement Policy** | | 2. Established Stakeholder Engagement (SE) policy and procedures. | 2. SE policy and strategy includes procedures with stakeholder analysis, differentiated approaches for priority groups, iterative disclosure and consultation requirements, and reporting.[16] | 2. Commitment to SE visible to staff, contractors, suppliers, and collaborators via codes of conduct setting out expectations for stakeholder interactions and human rights.<br>3. SE practices incorporated into requirements for primary suppliers.<br>4. SE activities and outcomes included in board decision making and external reporting procedures. |
| **Worker Grievance Mechanism** | 2. HR policy and procedures for worker engagement. | 3. Basic grievance mechanism for workers. | 3. Management responds to grievances from workers and contracted workers on a regular basis. | 5. Issues raised through grievance mechanism for workers are analyzed and resolved with the participation of a worker representative.<br>6. The board is informed about grievance outcomes and trends on a regular basis. |
| **Affected Communities Grievance Mechanism** | 3. Informal response to stakeholder requests and concerns. | 4. External Communications Mechanism for stakeholder questions and complaints, and if there are Affected Communities, a grievance mechanism is established. | 4. External and publicly accessible communication procedure.[17]<br>5. Grievance mechanism facilitates the resolution of concerns from Affected Communities.<br>6. Designated Affected Communities engagement personnel have clearly defined responsibilities, training, and reporting lines to senior management and the board.<br>7. SE policy incorporated into requirements for contractors.<br>8. Unresolved stakeholder issues require a management action plan. | 7. Periodic analysis of grievances to identify trends and root causes is conducted by senior management.<br>8. Senior management participate actively in international industry discussions on related topics.<br>9. SE and reporting consistent with international standards (AA 1000 Standards on Stakeholder Engagement and Accountability Principles and ISO 26000). |

[16] Consult with Social Specialist to determine quality of SE policy, strategy, and procedures, if applicable.
[17] Consult with Social Specialist to determine whether communication procedure is adequate to (a) receive and register external communication from the public; (b) assess issues raised and determine response; (c) provide and document responses, if any; and (d) adjust the management program, as appropriate and if applicable.

# Appendix E: Major Frameworks for Sustainability Management and Disclosure

## BROAD-BASED SUSTAINABILITY FRAMEWORKS

| Guidelines/ Framework | Objective | Strengths | Limitations | Best Use |
|---|---|---|---|---|
| United Nations Global Compact | Companies that commit to the 10 principles of the UN Global Compact are required to annually report on their progress and sustainability performance. | Covers environmental and social issues and human rights. | Principle-based framework does not offer specific key performance indicators for measuring performance, comparability. | Creating accountability for upholding broad-based international norms.<br>Topics and flexible framework relevant for emerging markets and smaller companies. |
| ISO | Guidance to maximize contributions to sustainable development.<br>Includes external communication on improving performance related to social responsibility. | Guidance on core social responsibility topics.<br>Guidance on integrating social responsibility throughout an organization. | Reporting guidance is limited. | Reporters who want to use global best practice but want a great deal of flexibility in how they report.<br>Topics and flexible framework relevant for emerging markets; comprehensiveness limits smaller companies. |

## BROAD-BASED SUSTAINABILITY REPORTING FRAMEWORKS

| Guidelines/ Framework | Objective | Strengths | Limitations | Best Use |
|---|---|---|---|---|
| GRI Empowering Sustainable Decisions | To improve sustainability of organizations and support sustainable development.<br>Guidelines are developed using a multistakeholder approach | Specific indicators for all companies. Sector-specific indicators for some industries. | Used for standalone sustainability reports.<br>More detailed information is not always relevant for strategic management and investment. | Communicating a broad range of sustainability/ nonfinancial management practices to many different types of stakeholders.<br>Topics relevant for emerging markets; comprehensiveness limits smaller companies. |

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## BROAD-BASED SUSTAINABILITY REPORTING FRAMEWORKS

| Guidelines/ Framework | Objective | Strengths | Limitations | Best Use |
|---|---|---|---|---|
| INTEGRATED REPORTING <IR> | To increase long-term, integrated thinking within companies, and improve the allocation of financial capital.<br><br>Investor prioritized. | Can help drive internal change, embedding environmental and social considerations in core operations. | Principle-based framework does not offer specific KPIs for measuring and reporting performance. | Reporting on value-creation processes and explaining how sustainability issues are managed strategically.<br><br>Approach relevant for emerging markets; sophistication limits smaller companies. |
| European Commission | Large public-interest entities (> 500 employees) should disclose policies, risks, and outcomes relating to environmental, social, and employee matters, human rights and anticorruption, and diversity in the board of directors. | Mandatory reporting (or explain) with flexibility to choose among the most widely used reporting frameworks. | Limited to companies based or operating in the EU. | Reporters with significant operations or markets in the EU. |
| Sustainable Stock Exchanges SSE Initiative | Enhance corporate transparency—and ultimately performance—on ESG issues, and encourage sustainable investment. | Designed for both emerging and developed markets.<br><br>Although designed for public companies, guidance can be used by private counterparts. | Guidance geared primarily to stock exchanges in their efforts to issue reporting guidance to their members (indirect). | Topics and flexible framework relevant for emerging markets. |

## ISSUE-BASED SUSTAINABILITY REPORTING FRAMEWORKS

| Guidelines/ Framework | Objective | Strengths | Limitations | Best Use |
|---|---|---|---|---|
| SASB Sustainability Accounting Standards Board | To democratize the availability of decision-useful sustainability information.<br><br>Primary audience is investors. | Specific for each sector and subsector.<br><br>Fully embedded within financial reporting. | For U.S.-listed companies.<br><br>Integrating sustainability information and financial regulatory filings; not a user-friendly format. | Explaining sustainability management and performance to investors.<br><br>Focus limited to listed U.S. companies. |

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## BROAD-BASED SUSTAINABILITY REPORTING FRAMEWORKS

| Guidelines/ Framework | Objective | Strengths | Limitations | Best Use |
|---|---|---|---|---|
| UN GUIDING PRINCIPLES REPORTING FRAMEWORK | Improve transparency of human rights performance and adoption of the UN Guiding Principles on Business and Human Rights. | Focused on governance and management of salient human rights issues.<br>Can be used with other guidelines or frameworks. | Very process oriented.<br>Indicators are qualitative. | Detailed communication regarding human rights management, adoption of UN Guiding Principles on Business and Human Rights ("Ruggie Framework").<br>Topic relevant for emerging markets; sophistication limits smaller companies. |
| CDP DRIVING SUSTAINABLE ECONOMIES | CDP requests standardized climate change, water, and forest information through annual questionnaires sent on behalf of institutional investors. | Provides comparable and aggregate information on key climate-related measures of corporate performance. | Standalone disclosure, not integrated in annual reports.<br>Sophistication and comprehensiveness limits application to very large companies. | Specialized disclosure to investors.<br>Industries with significant climate change impacts and/or those with regulatory requirement to report on climate change.<br>Focused on large listed companies. |
| CDSB Climate Disclosure Standards Board | Provide information for investors on how climate change affects strategy, performance, and future prospects.<br>Intended for use with financial reporting. | Harmonizes climate-related disclosures and supplements financial statements, placing climate information in context for investors. | Format may not be user-friendly for stakeholders other than investors. | Integrated reporting.<br>Industries with significant climate-change impacts and/or those with regulatory requirement to report on climate change.<br>Focused on large listed companies. |
| TCFD TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES | Develop voluntary, consistent climate-related financial risk disclosures for use by companies in providing information to stakeholders. | Comprehensive and integrated disclosure of climate risks, including governance, strategy, risk, and performance.<br>Includes scenario planning and industry-specific metrics. | Sophistication and comprehensiveness limits application to very large companies. | Integrated reporting.<br>Industries with significant climate-change impacts and/or those with regulatory requirement to report on climate change.<br>Focused on large listed companies. |

# Appendix F: Annual and Sustainability Reports Used in the Toolkit

| Company Name | Country | Industry | Listing | Report | Year |
|---|---|---|---|---|---|
| Absa Group (formerly Barclays Africa) | South Africa | Finance | JSE | Integrated Report | 2015 |
| Absa Group (formerly Barclays Africa) | South Africa | Finance | JSE | Integrated Report | 2017 |
| Aggreko | United Kingdom | Energy | LSE | Annual Report | 2015 |
| AkzoNobel | United Kingdom | Chemicals | Euronext | Report | 2016 |
| Apple | United States | Hardware | APPL | Environmental Responsibility Report | 2016 |
| Astellas Pharma | Japan | Pharmaceuticals | TYO | Annual Report | 2016 |
| BASF | Germany | Chemical | Borse Frankfurt | Integrated Report | 2017 |
| BHP Billiton | Anglo-Australian | Mining | NYSE | Annual Report | 2016 |
| CEMEX | Mexico | Building Materials | NYSE | Integrated Report | 2016 |
| CEMEX | Mexico | Building Materials | NYSE | Integrated Report | 2017 |
| Chugai Pharmaceutical Co | Japan | Pharmaceuticals | TYO | Annual Report | 2016 |
| Commercial Bank of Ceylon | Sri Lanka | Finance | Private | Annual Report | 2016 |
| Deutsche Bank | Germany | Finance | ETR | Corporate Responsibility Report | 2016 |
| EnBW | Germany | Electric Utility | Borse Frankfurt | Integrated Annual Report | 2017 |
| Eskom | South Africa | Electric Utility | JSE | Eskom Integrated Report | 2016 |
| Exxaro | South Africa | Coal and Heavy Minerals Mining | JSE | Integrated | 2015 |
| Ford | United States | Auto | NYSE | Sustainability Report | 2014–2015 |
| Fresnillo | Mexico | Precious metals mining | LON | Annual Report | 2015 |
| Gold Fields | South Africa | Extractive | NYSE | Integrated Annual Report | 2015 |
| Gold Fields | South Africa | Extractive | NYSE | Integrated Annual Report | 2016 |
| Impahla Clothing | South Africa | Apparel | Private | Integrated Annual Report | 2013 |
| Itau Unibanco | Brazil | Finance | NYSE | Annual Report | 2014 |
| Kumba Iron Ore Limited | South Africa | Iron-Ore Mining | JSE | Integrated Report | 2017 |
| Li & Fung Limited | China | Logistics | HKG | Annual Report | 2015 |
| Liberty Holdings | South Africa | Finance | JSE | Financial Results | 2015 |
| Liberty Holdings | South Africa | Finance | JSE | Integrated Report | 2015 |
| Natura | Brazil | Cosmetics | BVMF | Annual Report | 2016 |
| Nedbank Group | South Africa | Finance | JSE | Integrated Report | 2015 |
| Nestlé | Switzerland | Food & Beverage | VTX | Nestlé in Society | 2016 |
| Novo Nordisk | Denmark | Pharmaceutical | CPH | Annual Report | 2016 |
| Prudential | United States | Finance | NYSE | Proxy Statement | 2016 |

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| Company Name | Country | Industry | Listing | Report | Year |
|---|---|---|---|---|---|
| Reliance Industries Limited | India | Conglomerate | NSE | Annual Report | 2015 |
| Rio Tinto | Australia and United Kingdom | Metals & Mining | LSE | Annual Report | 2017 |
| Roche | Switzerland | Pharmaceuticals | VTX | Annual Report | 2016 |
| Siam Commercial Bank | Thailand | Finance | BKK | Annual Report | 2016 |
| SABMiller (InBev) | Belgium | Food & Beverage | EBR | Annual Report | 2016 |
| Santova Limited | South Africa | Logistics | JSE | Annual Integrated Report | 2016 |
| Sappi Group | South Africa | Pulp & Paper | JSE | Annual Financial Statements | 2016 |
| Sasol | South Africa | Energy and Chemical | NYSE | Integrated Annual Report | 2017 |
| Standard Chartered | United Kingdom | Finance | LON | Sustainability Summary | 2015 |
| Takeda | Japan | Pharmaceuticals | TYO | Annual Report | 2016 |
| Tata Motor | India | Auto | NYSE | Sustainability Report | 2014–2015 |
| Telefonica | Spain | Telecommunications | BME | Integrated Report | 2016 |
| Telekom Malaysia | Malaysia | Telecommunications | KLSE | Annual Report | 2015 |
| The CLP Group | China | Utilities | HKG | Annual Report | 2015 |
| The CLP Group | China | Utilities | HKG | Sustainability Report | 2015 |
| The Coca-Cola Company | United States | Food & Beverage | NYSE | Proxy Statement | 2016 |
| True Group | Thailand | Telecommunications | SET | Annual Report | 2015 |
| Türk Telekom | Turkey | Telecommunications | Private | Annual Report | 2015 |
| Unilever | United Kingdom | Food & Beverage | NYSE | Annual Report | 2015 |
| Vopak | Netherlands | Marine Transportation | Euronext | Annual Report | 2016 |
| Westpac Group | Australia | Finance | ASX | Annual Report | 2016 |

# Glossary

In the following definitions, “project” and “client” refer to companies or specific projects that companies are undertaking. Following each definition is the source of its substance.

**Affected Communities.** Local communities directly affected by the project. —*2012 Performance Standard 1, paragraph 1 (IFC).*

**audit.** A review of the historical financial statements to enhance the degree of confidence in them. Examination and verification of a company’s financial and accounting records and supporting documents by a competent, qualified, professional, and independent external auditor to assure readers that the records are in accordance with applicable reporting and accounting requirements, are free from material misstatement due to fraud or error, and constitute a true and fair representation of the company’s financial condition. —*Who’s Running the Company: A Guide to Reporting on Corporate Governance (IFC).*

**audit committee.** A committee constituted by the board of directors, typically charged with oversight of company reporting and disclosure of both financial and nonfinancial information to stakeholders. Usually responsible for selecting and recommending the company’s audit firm, to be approved by the board/shareholders. Usually responsible for the control environment of the company and risk oversight, if there is no separate risk committee of the board. —*Who’s Running the Company (IFC).*

**auditor’s opinion.** A certification that accompanies financial statements, provided by independent auditors of a company’s financial statements and records. The opinion indicates whether or not, overall, the financial statements present a fair reflection of the company’s financial condition. —*Who’s Running the Company (IFC).*

**biodiversity (also biological diversity).** The Convention on Biological Diversity defines biodiversity as “the variability among living organisms from all sources including, inter alia, terrestrial, marine and other aquatic ecosystems and the ecological complexes of which they are part; this includes diversity within species, between species, and of ecosystems.” —*2012 Performance Standard 6, paragraph 1 (IFC).*

**board of directors (or board).** A body of elected or appointed members who jointly oversee the activities of a company or organization. Some countries use a two-tier system where “board” refers to the “supervisory board” and “key executives” refers to the “management board.” —*G20/OECD Principles of Corporate Governance.*

**business model.** An organization’s system of transforming inputs through its business activities into outputs and outcomes to fulfill the organization’s strategic purposes and create value over the short, medium, and long term. —*Integrated Reporting Framework (IIRC).*

**capitals.** Stocks of value that all organizations depend on for their success as inputs to their business model, and that are increased, decreased, or transformed through the organization’s business activities and outputs. The IIRC <IR> Framework categorizes capitals as financial, manufactured, intellectual, human, social and relationship, and natural. —*Integrated Reporting Framework (IIRC).*

**chief executive officer (CEO).** The highest-ranking management officer of the company, who reports to the board of directors. The CEO is tasked with short-term decisions and leadership of employees, implementation of strategy, risk management, and oversight of management. —*Who’s Running the Company (IFC).*

**child labor.** IFC’s Environmental and Social Performance Standards classify a child as a person under age 18. According to IFC Performance Standards, the client will not employ children in any manner that is economically exploitative or is likely to be hazardous, to interfere with the child’s education, or to be harmful to the child’s health or physical, mental, spiritual, moral, or social development. —*Glossary of Terms 2006; Performance Standard 2, paragraph 21; and Guidance Note 2, paragraph 61 (IFC).*

**classified board.** Structure of a board of directors in which, every year, a fraction of the directors are elected, each for a multiyear term. —*Who’s Running the Company (IFC).*

**climate-change adaptation.** Reduction in the vulnerability of human or natural systems to the effects of climate change and to risks related to climate variability by maintaining or increasing adaptive capacity and resilience. —*Definitions and Metrics for Climate-Related Activities, version 3.1, June 2017 (IFC).*

**climate-change mitigation.** Reduction in **greenhouse gas (GHG) emissions** into the atmosphere or absorption of GHGs from the atmosphere. Can include 1) a reduction in GHG emissions currently emitted, 2) lower emissions as a result the project than those of a credible business-as-usual alternative, or 3) sequestration of emissions currently in the atmosphere. —*Definitions and Metrics for Climate-Related Activities, version 3.1, June 2017 (IFC).*

**codes of conduct/ethics.** Developed and adopted by organizations to define appropriate behaviors and actions on relevant and potentially delicate subjects. An indicator of how the company will achieve its goals and go about its business. —*Who's Running the Company (IFC).*

**collective bargaining.** Discussions and negotiations between employers and representatives of workers' organizations to determine working conditions and terms of employment by joint agreement. Collective bargaining also includes the implementation and administration of any agreements that may result from collective bargaining and the resolution of other issues that arise in the employment relationship with workers represented by the workers' organizations. —*2012 Guidance Note 2, paragraph 34 (IFC).*

**committees of the board.** Committees (comprising board members only) established to assist the board in the analysis of specific subjects outside of regular board meetings. Common board committees are audit, remuneration, and nomination. —*Who's Running the Company (IFC).*

**common shares.** Equity securities representing ownership in a corporation and providing the holders with voting rights and the right to a share of the company's residual earnings through dividends and/or capital appreciation. —*Who's Running the Company (IFC).*

**compliance.** Agreeing to and abiding by rules and regulations. In general, compliance means conforming to a specification or policy (internal or external), standard, or law that is clearly defined. —*Who's Running the Company (IFC).*

**concentrated ownership.** A form of ownership in which a single shareholder (or a small group of shareholders) holds the majority of the company's voting shares. —*Who's Running the Company (IFC).*

**controlled companies.** Firms in which an individual or a number of connected individuals or a legal entity holds the majority of the voting rights. —*Who's Running the Company (IFC).*

**controlling shareholder.** Person or entity that owns enough of the company's voting capital (typically, 30 percent or more) to control the composition of the board of directors—usually a family or state shareholder. —*Who's Running the Company (IFC).*

**corporate governance.** Involves a set of relationships between an organization's management, its board, its shareholders, and other stakeholders. Governance provides the structure and processes through which the organization sets its objectives, monitors its progress against performance goals, and evaluates its results. —*G20/OECD Principles of Corporate Governance.* Corporate governance is defined as the structures and processes by which companies are directed and controlled. *IFC.*

**corruption.** Abuse of entrusted power for private gain. Corruption can be classified as grand, petty, or political, depending on the amounts of money lost and the sector where it occurs. —*Transparency International.*

**critical habitat.** An area with high biodiversity value, including 1) habitat of significant importance to critically endangered and/or endangered species; 2) habitat of significant importance to endemic and/or restricted-range species; 3) habitat supporting globally significant concentrations of migratory species and/or congregatory species; 4) highly threatened and/or unique ecosystems; and 5) areas associated with key evolutionary processes. —*2012 Performance Standard 6, paragraph 16 (IFC).*

**cultural heritage.** Refers to 1) tangible moveable or immovable objects, property, sites, structures, or groups of structures having archaeological (prehistoric), paleontological, historical, cultural, artistic, or religious value; 2) unique natural features or tangible objects that embody cultural values, such as sacred groves, rocks, lakes, and waterfalls; and 3) certain instances of intangible forms of culture that are proposed to be used for commercial purposes, such as cultural knowledge, innovations, and practices of communities embodying traditional lifestyles. *—2012 Performance Standard 8, Paragraph 3 (IFC).*

**cumulative voting.** A system that gives minority shareholders more power by allowing them to cast all of their board-director votes for a single candidate, as opposed to regular or statutory voting in which shareholders must vote for a different candidate for each available seat or distribute their votes among a number of candidates. *—Who's Running the Company (IFC).*

**disclosure.** Refers to a firm's obligation to provide material, market-influencing information in accordance with the requirements of a number of parties, including regulatory authorities and the public, or in accordance with such standards as accounting standards and self-regulatory contracts. Disclosure contributes to the firm's **transparency**, which is one of the main corporate governance principles. *—Who's Running the Company (IFC).*

**discrimination in employment.** Any distinction, exclusion, or preference with regard to recruitment, hiring, working conditions, or terms of employment—made on the basis of personal characteristics unrelated to inherent job requirements—that nullifies or impairs equality of opportunity or treatment in employment or occupation. "Inherent job requirements" refers to genuine occupational qualifications that are necessary to perform the job in question. *—2012 Guidance Note 2, Paragraph 41 (IFC).*

**ecosystem services.** Benefits that people, including businesses, derive from ecosystems: 1) *provisioning services*—products from ecosystems, such as food, fresh water, timber, fibers, medicinal plants; 2) *regulating services*—benefits from the regulation of ecosystem processes, such as surface-water purification, carbon storage and sequestration, climate regulation, protection from natural hazards; 3) *cultural services*—nonmaterial benefits from ecosystems, such as natural areas that are sacred sites and areas of importance for recreation and aesthetic enjoyment; and 4) *supporting services*—natural processes that maintain the other services, such as soil formation, nutrient cycling, primary production. *—2012 Performance Standard 6, paragraph 2 (IFC).*

**employee grievance mechanism.** A vehicle for workers (and their organizations, where they exist) to raise workplace concerns. The client will inform the workers of the **grievance mechanism** at the time of recruitment and make it easily accessible to them. The mechanism should involve an appropriate level of management and address concerns promptly, using an understandable and transparent process that provides timely feedback to those concerned, without any retribution. The mechanism should also allow for anonymous complaints to be raised and addressed. The mechanism should not impede access to other judicial or administrative remedies that might be available under the law or through existing arbitration procedures, or substitute for grievance mechanisms provided through collective agreements. *—2012 Performance Standard 2, paragraph 20 (IFC).*

**Environmental and Social Impact Assessment (ESIA).** The client should conduct a comprehensive full-scale ESIA for certain projects—particularly for greenfield investments and projects (including, but not limited to, major expansion or transformation-conversion activities) involving specifically identified physical elements, aspects, and facilities that are likely to generate potentially significant adverse environmental and social **risks** and impacts. Generally, the key process elements of an ESIA are 1) initial screening of the project and scoping of the assessment process; 2) examination of alternatives; 3) stakeholder identification (focusing on those directly affected) and gathering of environmental and social baseline data; 4) impact identification, prediction, and analysis; 5) generation of mitigation or management measures and actions; 6) significance of impacts and evaluation of residual impacts; and 7) documentation of the assessment process (the ESIA report). The breadth, depth, and type of analysis should be proportionate to the nature and scale of the proposed project's potential impacts as identified during the course of the assessment process. The ESIA must conform to the requirements of the host country's environmental assessment laws and regulations, including the relevant disclosure of information and public consultation requirements, and should be developed following principles of good international industry practice. —*2012 Guidance Note 1, paragraph 23 (IFC).*

**Environmental and Social Management System (ESMS).** A set of policies, procedures, tools, and internal capacity to identify and manage a financial institution's exposure to the environmental and social risks of its clients/investees. An effective ESMS is a dynamic and continuous process initiated and supported by management, and it involves engagement between the client and its workers, local communities directly affected by the project (**Affected Communities**), and, where appropriate, other stakeholders. Drawing on the elements of the established business management process of "plan, do, check, and act," the ESMS entails a methodological approach to managing environmental and social risks and impacts in a structured way on an ongoing basis. A good ESMS appropriate to the nature and scale of the project promotes sound and sustainable environmental and social performance and can lead to improved financial, social, and environmental outcomes. —*First for Sustainability website and Performance Standard 1, paragraph 1 (IFC).*

**environmental and social risk.** Risk of adversely affecting people or the environment through inadequate or failed internal processes, people, and systems, or through external events. Environmental and social risk is a combination of the probability of certain hazards and the severity of impacts resulting from such an occurrence. Environmental and social impacts refer to 1) any change, potential or actual, to the physical, natural, or cultural environment and 2) impacts on the surrounding community and workers, resulting from the business activity to be supported. —*IFC; and 2012 Performance Standard 1, paragraph 1, footnotes 2 and 3 (IFC).*

**External Communications Mechanism (ECM).** Procedure that includes methods to 1) receive and register external communication from the public; 2) screen and assess the issues raised and determine how to address them; 3) provide, track, and document responses, if any; and 4) adjust the management program, as appropriate. —*2012 Performance Standard 1, paragraph 34 (IFC).*

**financial statements.** A complete set of financial statements comprises a balance sheet, an income statement, a statement of changes in equity, a cash flow statement, and notes, which collectively communicate an entity's economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework. —*Who's Running the Company (IFC).*

**forced labor.** Any work or service not voluntarily performed, exacted from a person under threat of force or penalty. It includes any kind of involuntary or compulsory labor, such as indentured labor, bonded labor, or similar labor-contracting arrangements. —*2012 Performance Standard 2, paragraph 22 (IFC).*

**Free, Prior and Informed Consent (FPIC).** Despite no universally accepted definition, for purposes of IFC Performance Standards, FPIC builds on and expands the process of **Informed Consultation and Participation** and is established through good-faith negotiation between the client and the **Affected Communities** of **indigenous peoples**. FPIC does not necessarily require unanimity and may be achieved even when individuals or groups within the community explicitly disagree. —*Glossary of Terms 2006; 2012 Performance Standard 7, paragraph 12 (IFC).*

**freedom of association.** The right of workers and employers to form and join organizations of their own choosing is an integral part of a free and open society. —*International Labour Organization.*

**Generally Accepted Accounting Principles (GAAP).** Accounting rules, conventions, and standards for companies, established by reporting requirements and accounting standard setters in a particular country. Each country is likely to have a GAAP, which is unlikely to be identical to any other country's GAAP. For example, U.S. GAAP is the body of accounting policies applicable to U.S.-registered firms, and the GAAP rules are issued by the Financial Accounting Standards Board (FASB). These are not identical to IFRS standards issued by the International Accounting Standards Board and applied in Europe and many other countries. —*Who's Running the Company (IFC).*

**greenhouse gas (GHG) emissions.** Scope levels: *Scope 1*—all direct GHG emissions; *Scope 2*—indirect GHG emissions from consumption of purchased electricity, heat, or steam; and *Scope 3*—other indirect emissions, not covered in Scope 2, that occur in the value chain of the reporting company, including both upstream and downstream emissions. Scope 3 emissions could include the extraction and production of purchased materials and fuels, transport-related activities in vehicles not owned or controlled by the reporting entity, electricity-related activities (such as transmission and distribution losses), outsourced activities, and waste disposal. —*Greenhouse Gas Protocol (WRI)*.

**grievance mechanism.** A means for a company to receive and facilitate resolution of **Affected Communities'** concerns and grievances about the company's environmental and social performance. The grievance mechanism should be scaled to the risks and adverse impacts of the project and have Affected Communities as its primary user. It should seek to resolve concerns promptly, using an understandable and transparent consultative process that is culturally appropriate and readily accessible—and at no cost and without retribution to the party that originated the issue or concern. (See **employee grievance mechanism.**) —*2012 Performance Standard 1, paragraph 35 (IFC)*.

**hazardous waste.** Substances classified as hazardous wastes possess at least one of four characteristics—ignitability, corrosivity, reactivity, or toxicity—or appear on special lists. —*Glossary of Terms 2006 (IFC)*.

**independent auditor.** Professional(s) from an external audit firm charged with undertaking an audit of the **financial statements**. An **audit** may be required annually, semiannually, or quarterly. In most countries the independent auditors undertake an annual audit. They must have no personal interest in the financial statements and should have no role in the development of the financial statements. The independent auditor is required to render an unbiased judgment that the financial statements and accounting records of the firm are likely to be free from material misstatement and are a fair reflection of the financial position of the firm. —*Who's Running the Company (IFC)*.

**independent director.** A director whose only non-trivial professional, familial, personal, or financial connection to the corporation, its chairman, CEO, or any other executive officer is his or her directorship. The independent director is expected to be capable of applying objective judgment to all company decisions. —*Who's Running the Company (IFC)*.

**independent non-executive director.** A director who 1) has not been employed by the company or its related parties in the past five years; 2) is not, and is not affiliated with a company that is, an adviser or consultant to the company or its related parties; 3) is not affiliated with a significant customer or supplier of the company or its related parties; 4) has no personal service contracts with the company, its related parties, or its senior management; 5) is not affiliated with a nonprofit organization that receives significant funding from the company or its related parties; 6) is not employed as an executive of another company where any of the company's executives serve on that company's board of directors; 7) is not a member of the immediate family of an individual who is, or has been during the past five years, employed by the company or its related parties as an executive officer; 8) is not, nor in the past five years has been, affiliated with or employed by a present or former auditor of the company or of a **related party**; and 9) is not a controlling person of the company (or member of a group of individuals and/or entities that collectively exercise effective control over the company) or such person's brother, sister, parent, grandparent, child, cousin, aunt, uncle, nephew or niece, or a spouse, widow, in-law, heir, legatee, or successor of any of the foregoing (or any trust or similar arrangement of which any such persons or a combination thereof are the sole beneficiaries) or the executor, administrator, or personal representative of any person described above who is deceased or legally incompetent. For the purposes of this definition, a person is deemed to be "affiliated" with a party if such person 1) has a direct or indirect ownership interest in or 2) is employed by such party. —*IFC*.

**indigenous peoples.** Generically refers to a distinct social and cultural group possessing the following characteristics in varying degrees: 1) self-identification as members of a distinct indigenous cultural group and recognition of this identity by others; 2) collective attachment to geographically distinct habitats or ancestral territories in the project area and to the natural resources in these habitats and territories; 3) customary cultural, economic, social, or political institutions that are separate from those of the mainstream society or culture; or 4) a distinct language or dialect, often different from the official language or languages of the country or region in which they reside. *—Performance Standard 7, paragraph 5 (IFC).*

**Informed Consultation and Participation (ICP).** For projects with potentially significant adverse impacts on **Affected Communities**, ICP requires clients to involve Affected Communities (both men and women) in decision making that affects them directly, such as proposed mitigation measures, the sharing of development benefits and opportunities, and implementation issues. The client will document the process, in particular the measures taken to avoid or minimize risks to and adverse impacts on the Affected Communities, and will inform those affected about how their concerns have been considered. **—***Performance Standard 1, paragraph 31 (IFC).*

**integrated report.** A concise communication about how an organization's strategy, governance, performance, and prospects, in the context of its external environment, lead to the creation of value in the short, medium, and long term. *—Integrated Reporting Framework (IIRC).*

**internal audit.** An independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluating and improving the effectiveness of risk management, control, and governance processes. *—Who's Running the Company (IFC).*

**internal control.** A process, effected by an entity's board, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in 1) effectiveness and efficiency of operations; 2) reliability of financial reporting; and 3) compliance with applicable laws and regulations. *—IFC.*

**material/materiality.** Information is material if omitting, misstating, or obscuring it could reasonably be expected to influence decisions that the primary users of a specific reporting entity's general-purpose financial statements make on the basis of those financial statements. Materiality depends on the nature or magnitude of information, or both. Assessing whether information is material requires consideration of the entity's circumstances. *—Exposure Draft, 09.14.2017 (IFRS).*

**minority shareholder.** A person or entity with a minority stake in a company controlled by a majority shareholder. It is usually less than a 5 percent stake, but each country may determine various thresholds applicable to the term "minority shareholder." *—Who's Running the Company (IFC).*

**non-executive director.** A director who does not have executive management responsibilities within the organization. *—IFC.*

**non-voting shares.** Owners holding this share class do not commonly have voting rights at the annual general meeting, except on some matters of highest importance. Usually, non-voting shareowners have preferential rights for receiving dividends. *—Who's Running the Company (IFC).*

**one-tier board.** A board of directors composed of both executive and non-executive members. It delegates day-to-day business to the management team. Found in the United States, the United Kingdom, and Commonwealth countries. (See **two-tier board**.) *—Who's Running the Company (IFC).*

**operational risk.** Risk of loss resulting from inadequate or failed internal processes, people, and systems, or from external events. This definition includes legal risk, but excludes strategic and reputational risk. *—IFC.*

**ownership structure.** The way company shares are distributed among shareholders. *—Who's Running the Company (IFC).*

**Paris Agreement.** To address climate change, countries adopted the Paris Agreement at the Conference of the Parties (COP) 21 in Paris on December 12, 2015. In the agreement, which entered into force less than a year later, the countries agreed to work to limit global temperature rise to well below 2 degrees Celsius, and given the grave risks, to strive for 1.5 degrees Celsius. —*United Nations.*

**pollution.** The IFC Performance Standards use the term to refer to both hazardous and nonhazardous chemical pollutants in the solid, liquid, or gaseous phases, and include other components such as pests, pathogens, thermal discharge to water, **GHG emissions**, nuisance odors, noise, vibration, radiation, electromagnetic energy, and the creation of potential visual impacts, including light. —*Performance Standard 3, paragraph 1, footnote 1 (IFC).*

**related party.** A party is related to an entity if it can directly or indirectly control the other party or exercise control through other parties; it may also be where parties are subject to a common control from the same source. Related parties tend to have influence over the financial or operating policies of a firm or have the power to influence another party's actions. A related party may be a close family member (including partners, spouses, children, other relatives), a key manager in the entity (and his or her close family members), or entities such as subsidiaries of the entity, its holding company, joint ventures, and associates. —*Who's Running the Company (IFC).*

**renewable energy.** Energy sources derived from solar power, hydro, wind, certain types of geothermal, and biomass. —*Glossary of Terms 2006 (IFC).*

**renewable resources.** Natural resources that, after exploitation, can return to their previous stock levels by natural processes of growth or replenishment. Conditionally renewable resources are those for which exploitation eventually reaches a level beyond which regeneration will become impossible, such as clear-cutting of tropical forests. —*Glossary (OECD).*

**risk.** Anything that can affect the ability of an enterprise to meet its objectives. —*IFC.*

**risk analysis.** A process intended to reveal the nature of potential **risk** and determine the level of risk. —*IFC.*

**risk appetite.** The broadly based level of **risk** the entity is willing to seek or accept in pursuit of long-term objectives. —*IFC.*

**risk assessment.** The process of identifying **risks,** assessing the critical functions necessary to continue business operations, defining the controls in place to reduce exposure, and evaluating the cost of such controls. Risk assessment often involves an evaluation of the probability of a particular event. —*IFC.*

**risk governance.** The principles of good governance, applied to the identification, assessment, management, and communication of **risk.** It incorporates the principles of accountability, participation, and **transparency** in establishing policies and structures to make and implement risk-related decisions. —*IFC.*

**risk management.** Coordinated activities to direct and control **risk.** —*IFC.*

**risk management framework.** The complete set of components that provide the foundation and organizational arrangements for designing, implementing, monitoring, reviewing, and continually improving **risk management** throughout the organization. —*IFC.*

**share option.** An agreement, or privilege, which conveys the right to buy or sell a specific security or property at a specified price, by a specific date. The most common share options are calls (the right to buy a specified quantity of a security at a set strike price at a time on or before expiration) and puts (the right to sell a specified quantity of a security at a set strike price at a time on or before expiration). —*Who's Running the Company (IFC).*

**shareholder.** A person or entity that owns shares issued by companies. —*Who's Running the Company (IFC).*

**shareholders rights.** The rights resulting from ownership of shares, which may be based in legal rights or other rights contracted with the company. The basic shareholder rights include the right to information on the company, to attend the meeting of **shareholders,** to elect directors, and to appoint the external auditor, plus voting rights and cash flow rights. —*Who's Running the Company (IFC).*

**shareholders' agreement.** A written document governing the relations among **shareholders** and defining how the company will be managed and controlled. The agreement helps align the objectives of controlling shareholders to safeguard common interests and to protect the interests of **minority shareholders**. —*Who's Running the Company (IFC).*

**staggered board.** Structure of a board of directors in which every year a fraction of the directors are elected, each for a multiyear term. Also called a **classified board**. —*Who's Running the Company (IFC).*

**stakeholder engagement.** Establishing and maintaining a constructive relationship with a variety of external stakeholders over the life of the project. It is an integral part of an efficient and adaptive **Environmental and Social Management System**. An effective engagement process allows the views, interests, and concerns of different stakeholders, particularly of the local communities directly affected by the project (**Affected Communities**), to be heard, understood, and taken into account in project decisions and creation of development benefits. —*2012 Guidance Note 1, paragraph 6 (IFC).*

**supply chain.** Materials, components, goods, or products for use in ongoing operations. —*2012 Guidance Note 2, paragraph 93 (IFC).*

**supply chain workers.** People employed by suppliers that provide goods and materials to the company. There is no direct contractual or labor relationship between the client and the workers at the supplier level, and costs and benefits are paid by suppliers. —*2012 Guidance Note 2, paragraph 12 (IFC).*

**Sustainable Development Goals (SDGs) or Global Goals.** The 17 SDGs of the 2030 Agenda for Sustainable Development were adopted in September 2015 to "end poverty, protect the planet and ensure prosperity for all." The Goals came into force on January 1, 2016. —*United Nations.*

**sustainable development/sustainability.** Development that meets the needs of the present without compromising the ability of future generations to meet their own needs. —*Brundtland Commission.*

**tag-along rights.** If a majority **shareholder** sells his or her stake, **minority shareholders** have the right to participate and sell their stake under the same terms and conditions as the majority shareholder. This right protects minority shareholders and is a standard inclusion in **shareholders' agreements**. —*Who's Running the Company (IFC).*

**transparency.** The corporate governance principle of publishing and disclosing information relevant to stakeholders' interests and to **shareholders** on all price-sensitive material matters. —*Who's Running the Company (IFC).*

**value creation.** The process that results in increases, decreases, or transformations of the **capitals** caused by the organization's business activities and outputs. —*Integrated Reporting Framework (IIRC).*

**voting rights.** The right to vote at **shareholders'** meetings on issues of importance for the company. —*Who's Running the Company (IFC).*

**voting shares.** Shares that give the **shareholder** the right to vote on matters of corporate policy, including elections to the board of directors. —*Who's Running the Company (IFC).*

**working conditions.** Conditions in the workplace (including the physical environmental, health and safety precautions, and access to sanitary facilities) and treatment of workers (including disciplinary practices, reasons and process for termination of workers, and respect for the worker's personal dignity). —*Glossary of Terms 2006 (IFC).*

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