Taking Shape...
The Future of Corporate Responsibility Communications
Business in the Community defines corporate responsibility as the management of a company’s impact on society and the environment through its operations, products or services and through its interaction with key stakeholders such as employees, customers, investors, communities and suppliers.

We consider it good business practice for companies to adopt the following basic principles in discharging this responsibility:
- to treat employees fairly, equitably and with respect;
- to operate ethically and with integrity;
- to observe basic human rights;
- to protect the environment for future generations; and
- to be a responsible neighbour in their communities.

We help our clients communicate through a range of specialist services including brand identity, corporate reporting, corporate responsibility, digital media, internal communication and marketing communications.

We’re unusual because we think consistency is as important as creativity. Because our clients need to know that we can be consistently creative. That we cherish the small jobs as much as the big ones. That we reliably deliver quality, value and that bit of magic. That we always go the extra mile.

We’ve been growing steadily since the day we opened in 1986, we’re independent and profitable – and we like it that way.
Foreword

This report is part of an ongoing collaboration between Business in the Community (BITC) and Radley Yeldar (RY). The objective of our collaboration is to help companies understand developments in corporate responsibility (CR), and to get more value from their investments in CR communications.


We propose two other follow-up activities:
- a survey to test the predictions; and
- a follow-up seminar.

If you would like to find out more or to get involved, please contact:

Katherine Sharp
Senior Corporate Responsibility Reporting Manager
Business in the Community
E katherine.sharp@bitc.org.uk
T +44 (0) 20 7566 8700

Tom Rotherham
Head of Corporate Responsibility
Radley Yeldar
E t.rotherham@ry.com
T +44 (0) 20 7033 0700
What’s inside?

Three initiatives
The first part of this paper provides a short overview of each of the three key initiatives. More detail is given on each initiative in the appendix.

Three trends
The second part of the paper explains three major trends that lie behind these initiatives: materiality; stakeholder engagement; and the integration of financial and non-financial performance.

Nine predictions
The final part outlines BITC and RY’s predictions for how these three trends may influence corporate responsibility communications at a practical level in the years to come. These predictions will help companies by challenging presumptions about the role of CR communications in their business.

Throughout this paper we have added statements made by CR practitioners who participated in the BITC-RY Seminar on CR reporting, held in London on 15 November 2006. The seminar was attended by over 90 people.
What’s changing?

2006 was a year of significant change in the world of corporate responsibility (CR). Three initiatives stand out in particular:

1. On 27 April 2006, as outgoing UN Secretary General Kofi Annan rang the bell at the New York Stock Exchange (NYSE), some of the world’s largest institutional investors and fund managers, representing over £4 trillion in assets under management, began to sign the United Nations Principles for Responsible Investment (UN-PRI).

2. On 4 October 2006, in Amsterdam, almost 1,000 people from around the world joined ex-US Vice-President Al Gore and current European Commission Vice-President Margot Wallström in welcoming the third edition of the Sustainability Reporting Guidelines (G3) produced by the Global Reporting Initiative (GRI).

3. On 8 November 2006, in London, the eight-year saga that started out as a fundamental review of UK company law, finally ended in Royal Assent for the Companies Act 2006. Among other things, this included requirements for an enhanced Business Review for quoted companies and, for the first time, a clearly codified list of directors’ duties.

In evolutionary terms, 2006 may be seen as the year that CR grew legs and was at last able to walk over to the mainstream.

Companies that want to be up to date with good practice in corporate responsibility communications need to be aware of these three initiatives.

Understanding the trends that lie behind them can also help companies to anticipate the future of corporate responsibility communications.

This paper will help you do both.

“CR is not an overhead - it’s part of the value proposition.”
Three initiatives shaping the future

One of the characteristics of corporate responsibility (CR) that most frustrates people is the rate at which it seems to evolve. Not only does its focus seem to expand and contract, but even the terms we use to describe it change.

The concept of CR evolves because our understanding of business’ impact on society is changing, and because our conception of the role of business in society is also changing. Occasionally, however, events can permanently alter the common understanding of CR: they cement core concepts and approaches.

These three initiatives are those kinds of events. By understanding these initiatives we can better understand the confusion and rapid changes that occur around us.

1. The United Nations Principles for Responsible Investment (UN-PRI)

The investment community has joined government as one of the prime levers of influence on corporate behaviour. To date, the attention mostly has been on a niche group of investors and asset managers in the Socially Responsible Investment (SRI) industry.

The UN-PRI symbolises a shift in the investment community away from treating CR as a niche investment product towards incorporating environmental, social and governance issues into mainstream financial analysis.

The UN-PRI process was initiated by UN Secretary General Kofi Annan in December 2004, with the support of 12 institutional investors representing roughly £1 trillion of assets. The initiative was implemented by the UN Environment Programme’s Financial Services Initiative (UNEP-FI) and the UN Global Compact, with the support of 70 experts from financial services, academia and civil society.

The UN-PRI defines principles for responsible investment, not criteria or performance requirements. By becoming a signatory, investors and fund managers make a public statement that they believe CR can have a material impact on financial performance. More importantly, they also commit to integrating CR management and performance into their investment decisions or advice. The UN-PRI also calls on companies to provide more disclosure, including more widespread use of the Global Reporting Initiative (GRI).

Since the principles were published in April 2006, 140 institutional investors and fund managers from 21 countries with a total of over £4 trillion under management have signed the UN-PRI. This sum is equal to the total combined value of the London and Tokyo stock exchanges.
2. The GRI’s Third Generation Sustainability Reporting Guidelines (G3)

The Global Reporting Initiative (GRI) develops and disseminates globally applicable “Sustainability Reporting Guidelines” for voluntary use by all types of organisations. Initiated in 1997 by CERES, a US-based NGO, and the United Nations Environment Programme (UNEP), GRI’s objective is to help organisations give a balanced overview of their economic, environmental and social impacts.

The first guidelines were released in 1999, and a second edition was published in 2002, prior to the World Summit on Sustainable Development. The third edition, referred to as G3, was released in October 2006.

The G3 edition was designed to make several specific improvements, including to:
- increase the relevance and quality of information included in the report;
- improve the comparability of data over time and between organisations;
- make qualitative indicators clearer and more results-oriented; and
- make reports more user-friendly to different audiences needing different types of information.

As a result of the changes, the total number of indicators has decreased from 97 to 79. In addition, organisations are encouraged to report against only those indicators that are of material importance to the company or its stakeholders. As a result, there is a much greater emphasis on stakeholder engagement.

Finally, GRI provides a framework for progression through three “application levels”. The application levels enable companies to communicate their compliance with the G3 in a step-wise approach over time.

3. The Companies Act 2006

The Companies Act 2006 (CA 2006) is the first major reform of UK company law since 1985. The CA 2006 received Royal Assent on 8 November 2006. Both of the elements outlined below will take effect from 1 October 2007.

One of the most controversial elements in the CA 2006 is the codification of directors’ duties. While directors’ duties had previously been contained in common law and equitable principles, the CA 2006 enshrines the general duties of directors in clear statutory requirements.

The Act defines a director’s duty to promote the success of the company in a way that is consistent with the concept of enlightened shareholder value. In this regard, the duty, although primarily concerned with the interests of members as a whole, is not limited to those interests alone. Directors are also required to give due regard to, among other things, the impact of their decisions on employees, communities and the environment.

A second key element of the CA 2006 is the enhanced Business Review, which revives, for quoted companies, most of the requirements that were included in the now-defunct mandatory Operating and Financial Review (OFR) provisions. Quoted companies must now report information on environmental matters, the company’s employees and social and community issues that are material to the company’s business, together with information on the company’s policies in these areas and the effectiveness of those policies.

The CA 2006 does not presume that CR management or performance is equally important to all companies. So boards can still decide not to disclose CR-related information if they conclude that it is irrelevant to an understanding of their company’s business. But the key change is that boards must now give the issue due consideration, based on appropriate information. They must then report on the issues they have deemed relevant, and indicate which issues are not.

Where CR management or performance is material to an understanding of the company’s business, companies are expected to report performance using key performance indicators (KPIs). Companies that produce stand-alone CR reports, but do not include CR-related KPIs in their Annual Report and Accounts risk, sending conflicting messages.

“The UK Companies Act explicitly states for the first time directors’ responsibilities towards employees, community and the environment.”
Three trends facing all companies

One of the inescapable facts about CR is that, at the practical level, it means different things to different companies. Even at the policy level, where regulations may impact one sector but not another, it is not always easy to provide general advice or guidance.

The task that we have set ourselves in this section is to identify trends in CR that are common to all companies, and that will have an impact on all companies’ CR communication programmes.

We believe that there are three such trends:

1. Materiality;
2. Stakeholder engagement; and

We also believe that companies communicating on CR – be it within an Annual Report and Accounts, through a CR report, online or across existing channels – will get more value from their investment if they consider carefully the implications of these three trends.

1. Materiality
Materiality has long been a core concept of financial accounting and reporting standards. What the three initiatives outlined in this paper suggest is that the concept of materiality is now being interpreted and applied in the context of CR management and communication. This will permanently change what we mean by CR.¹

The US Financial Standards Accounting Board (FASB) defines materiality as:

“The magnitude of an omission or misstatement of information that, in the light of surrounding circumstances, makes it probable that the judgement of a reasonable person relying on the information would have been changed or influenced by the omission or misstatement.”²

The FASB defines materiality in the context of one audience: the investor. Because the UN-PRI was developed for, and ultimately approved by, institutional investors, it also uses the term materiality as the investor. Because the UN-PRI was developed for, and ultimately approved by, institutional investors, it also uses the term materiality in this way. The main message of the UN-PRI is that investors should take CR seriously because it may impact on financial performance.

The other two initiatives, however, have broader constituencies: the GRI is a multi-stakeholder initiative; and the CA 2006 was drafted by government in the public’s interests. As a result, a different picture of materiality emerges from these initiatives.

“Don’t separate CR information in slide presentations of results. Companies can help investors see what’s relevant by putting information on people and products in with the rest.”

Whereas the UN-PRI highlights the potential impact of CR on financial performance, GRI defines materiality in terms of the significance of environmental, social or economic impacts, or the impact of the information on stakeholders’ relationship with the company.

The scope of materiality is defined in G3 as:

“The information in a report should cover topics and indicators that reflect the organisation’s significant economic, environmental and social impacts, or that would substantively influence the assessments and decisions of stakeholders.”

The presumption behind this approach is that all stakeholders are interested in non-financial issues and some may have an impact on its financial success.

What does this mean for CR communications?
Companies that undertake a comprehensive materiality assessment will identify:

a) which issues are important to the company;
b) which stakeholders are important to the company; and
c) which issues matter to those stakeholders.

The next question is then: is a CR report the right way to communicate this information to them?

Be they investors, employees, governments, communities, suppliers, customers or NGOs - people make decisions about their relationship with a company based on more than just utilitarian criteria (i.e. is the product fit for purpose? Will they pay me a reasonable salary? Will it be delivered on time?).

The GRI promotes a stakeholder-focused approach - after all, people's opinions matter. But it is not clear about the need to prioritise between the interests of different stakeholder groups, and does not suggest a process for doing this.

The CA 2006 states that it is a directors’ duty to promote the success of the company for the benefit of its members (i.e. shareholders) as a whole. But here, success is not defined solely in relation to the shareholders. Directors must also pay due regard to impacts on, for example, the environment, communities, employees and suppliers.

So what is the right approach to materiality?
There is actually no difference in the way these three initiatives use the basic concept of materiality. They all recognise that responsible business practice can impact on a company’s financial performance. Their main differences are simply due to:

a) the initiative's constituency, and
b) the time horizon of the relationship between the company and this constituency.

Most of the differences in how the concept of materiality is applied can be explained by a difference in one or both of these criteria. For instance, the UN-PRI’s constituency is investors who are seeking a maximum return on their investments (e.g. a pension fund investing pension holders’ money so that they have enough income to retire on).

In this respect, the UN-PRI signatories are no different from day traders: make as much money as possible within the defined investment horizon. This is also why the UN-PRI signatories should not be confused with niche SRI investors, who explicitly adopt ethical criteria to market investment services to a sub-set of ethical investors.

What differentiates the UN-PRI signatories from the rest of the mainstream investment community is the time horizon of their relationship with the companies in which they invest. The longer the time horizon of the investment, the more likely CR issues are to be material to financial performance. Climate change is perhaps the clearest example of this.

So it should not be surprising that the majority of asset owners signed up to the UN-PRI are pension funds and insurance companies with long-term investment horizons. There are no short-term investors lining up to join the club. But, at the same time, particularly as they invest in or buy out large publicly listed companies, it should come as no surprise if private equity players or long-only hedge funds do so in the future.

What does this mean for CR communications?
Companies that factor CR issues into their materiality assessments will better understand and be more effective at communicating how they deliver financial and non-financial value to all stakeholders.

3 The principle of materiality is one of four principles that the G3 recommends companies use to define the content of a CR report. For more information see http://www.globalreporting.org/ReportingFramework/G3Online/DefiningReportContent/
The G3 guidelines, on the other hand, are written by a multi-stakeholder group of experts with the objective of providing any interested party with a balanced picture of the economic, environmental and social performance of an organisation. The interests of this constituency naturally extend beyond financial returns.

So, while the UN-PRI concludes that CR is material because of the investment horizon of institutional investors, the G3 concludes that CR is material simply because its constituency (i.e. society) has an inherent interest in companies' environmental and social performance.

The CA 2006 is a legal framework designed by a government whose role is to act on behalf of society as a whole. But while the House of Commons and House of Lords must consider the broader public interest, directors' duties are written in the context of a free-market economy, and the Business Review is written primarily to inform shareholders. As a result, while the scope of materiality in the CA 2006 is broader than that in the UN-PRI, it is narrower than in the GRI.

It is not surprising, then, to note that the directors' duty to promote the success of the company expressly refers to the long-term consequences of directors' decisions. In addition, directors must consider the interests of other stakeholders, including their employees, suppliers, customers, communities and the environment. Finally, directors are required to consider “the desirability of the company maintaining a reputation for high standards of business conduct”.

**Enlightened shareholder value**

Although the term is not used in the CA 2006 itself, this directors' duty is based on the concept of enlightened shareholder value. From the company's perspective, this is consistent with the idea that CR should be seen in the context of enlightened self-interest: i.e. because it makes business sense.

“Enlightened shareholder value”

A materiality process must include stakeholder engagement.”

“The CR manager’s role is to work with the audit committee or board to tease out and develop thinking on reputational risk.”

“The CR report acts as a resource rather than the be all and end all.”
2. Stakeholder engagement

Another trend that is highlighted by 2006’s three initiatives is the growing importance of stakeholder engagement. Because stakeholder engagement is required to define a company’s material issues, and is fundamental to a comprehensive understanding of non-financial value creation, good stakeholder engagement will increasingly be seen as an indicator of good management.

A starting point for understanding the importance of stakeholder engagement is the codified directors’ duty to promote the success of the company. One of the implications of the CA 2006 is the emphasis on directors needing to consider various factors when making decisions. Some of the information that directors may need relates to stakeholders’ expectations and priorities: information that can be obtained only by talking with the stakeholders themselves.

What does this mean for CR communications?

The single best message for a company to communicate across all stakeholder groups is: “We recognise our interdependencies, and we recognise that there is a shared interest in identifying where our interests overlap.”

For example, one of the specific factors to which a director is to have regard is “the desirability of the company maintaining a reputation for high standards of business conduct”. If companies do not understand how their key stakeholders develop opinions on the company’s reputation, it will be difficult for companies to fulfil this requirement. And the only way to get this information is through engagement. Of course, engagement can be achieved in many ways, and does not always mean fireside chats.

Many of the factors to which directors might have regard relate to the interests of other stakeholder groups, such as communities, employees, suppliers, customers and the environment. It would seem a logical conclusion that companies will need to have some engagement with these stakeholders in order to identify, prioritise between, and address their interests.

It is important to remember that one of the core concepts behind the directors’ duty to promote the success of the company is enlightened shareholder value. This is equally applicable to stakeholder engagement, which should be seen as part of a company’s strategy to identify the full range of issues and activities on which it can pursue enlightened self-interest by delivering both financial and non-financial value.

For instance, some people have described stakeholder engagement as part of a company’s “future proofing” strategy. Certainly, it makes sense for companies to focus on those stakeholders with the most direct impact on their future success – or with the most influence. The more organised and structured a stakeholder group is, the more influence and credibility they will tend to have.

As CR performance becomes more important, and as companies recognise the impact that stakeholders can have on their business success, it may well be that effective stakeholder engagement will eventually be seen as an indicator of good overall management. This is, after all, where we are with environmental management; occupational health and safety management; human rights management; ...

Of course, there are many ways to engage with stakeholders, some more onerous than others. At the most basic level, one of the ways that companies can integrate stakeholders’ interests in their business planning is through multi-stakeholder initiatives, like the GRI’s G3.

G3 was developed by an international, multi-stakeholder group of CR experts. In some ways, then, companies that use the G3 guidelines are importing a generic proxy stakeholder engagement process.

But what the G3 guidelines stop short of stating explicitly is that companies have to prioritise between stakeholders as much as they do between CR issues. Just as no company can address at the same time all of its possible economic, environmental and social impacts, neither can a company address all stakeholders’ concerns – many of which may be conflicting. In order to prioritise effectively, a company must focus on both the important issues and the important stakeholders.

Companies that have a clearer idea of how CR issues influence business risk and opportunity will take a proactive approach to stakeholder engagement. For instance, M&S undertook stakeholder engagement to inform its strategic planning process and to define indicators to monitor performance against their CR strategy. The result of this process was a list of material indicators that included roughly 50% of the GRI indicators and 50% of their own “M&S-specific” indicators.

“You can look at GRI as ‘off the peg’ stakeholder expectations.”
3. Integrating financial and non-financial performance

As outlined in the report, Tomorrow’s Value: from risk reduction to value creation, many companies are changing the way they think about CR and moving away from an exclusively risk-based approach. The leading companies are looking at the environmental and social challenges in the context of value creation: can challenges be addressed and profits increased with new products and services, or using new business models?

There is also a move to understand value creation over a wider spectrum of metrics than traditionally measured by financial accounting. This is consistent with the increased focus in Annual Report and Accounts on non-financial accounting and narrative reporting.

Indeed, perhaps the most important linkage between the UK Government (CA 2006), institutional investors (UN-PRI) and stakeholders in general (G3) is the recognition that there is a connection between responsible business practice, non-financial issues and financial performance - and that stakeholders are a bridge that can make this connection tangible.

At a theoretical level, it is easy to understand why there is a link between financial and non-financial performance by considering four inter-connected elements:

- all economic activity has environmental and social impacts.
- Negative impacts can lead to environmental degradation and social unrest;
- environmental degradation and social unrest are not conducive to overall economic growth, and slower economic growth will impact all companies;
- a company’s ability to access natural resources, human resources, financial resources and the marketplace is influenced by both availability and by stakeholder perceptions;
- stakeholders’ perceptions are influenced by their understanding of how a company is contributing positively or negatively to environmental degradation, social unrest and overall economic growth.

Understanding the theoretical basis for the link is one thing. It is, of course, much harder to quantify the link between financial and non-financial; between tangible and intangible; and between short- and long-term performance.

A number of initiatives - most notably the Enhanced Analytics Initiative (EAI) - are researching the materiality of non-financial performance, but none have yet come up with a unified model for understanding the inter-relationships. However, this involves a level of complexity and detail that may well preclude the formulation of useful generic models.

The first challenge is to recognise the link between CR issues and other non-financial issues. It is possible that companies’ experience managing intangibles in the context of brand development and valuation may be useful here.

The basket of financial issues is relatively easy to describe, and includes things like exposure to currency risk; cash flow; debt to equity ratios; return on capital employed and depreciation. But there is no sharp line between CR and non-financial issues.

For example, at what point do the following issues stop being non-financial and start being “CR”: customer satisfaction; fair operating practices in the supply chain; employee engagement; and environmental performance improvements?

Further, what is the line that divides consumer satisfaction, employee loyalty and brand equity from environmental, social or economic performance? It is not clear that CR issues should be treated separately from other non-financial issues.

Given the number of different definitions of CR, and the inherent ambiguity in “non-financial”, it is perhaps not surprising that we are dealing with grey zones here. But recognizing the relationship between CR and non-financial risk and value creation is important to the future evolution of the field of CR and to the way that companies will extract value from good CR management.

If companies adopt an integrated approach to value creation, then there is less need to maintain clear lines between non-financial and financial; between non-financial and CR; and between tangible and intangible. They are all important in different ways and they are all connected.

One concrete example of this is the rise of ethical branding. A brand is the encapsulation of a product’s or company’s value proposition – which fundamentally includes financial and non-financial elements, such as ethics. Companies are now building environmental and social issues into their brands – adding to their brand equity, a non-financial metric for which a number of measurement tools exist.

“The CR report allows space for dialogue and experimentation. The legal nature of the Annual Report and Accounts puts liabilities around it and gives less space for this. So there is tension between integration and innovation.”
Nine predictions to challenge your presumptions

The previous section outlined three trends that we believe will shape the future of CR communications in the UK. In this section, we extrapolate from these trends a series of specific predictions on how CR communications may actually evolve in the next few years.

Although they are based on both our own analysis and discussions with a number of leading CR experts, these remain, of course, untested predictions. However, we plan to undertake a survey in order to test them. The results of this survey feed into our next joint seminar on CR communications.

Prediction 1
Boards will increasingly recognise that the CR reporting process is a valuable internal management tool.

Prediction 2
Boards will pay more attention to the accuracy of CR-related information.

Prediction 3
Companies will improve internal communication on CR.

Prediction 4
Companies will make better use of existing communication channels to deliver tailored messages to specific stakeholders.

Prediction 5
Boards will increasingly use the Annual Report and Accounts as a tool to demonstrate accountability to important stakeholders not just investors.

Prediction 6
Companies will increasingly report material issues in their Business Review but will keep a separate CR section.

Prediction 7
The role of the CR manager will increasingly be driven by an internal “pull” rather than an external “push”.

Prediction 8
Companies will take a systematic approach to integrating stakeholders’ interests into their decision-making processes.

Prediction 9
Companies that engage in dialogue through partnerships will be better able to identify opportunities for value creation.
Prediction 1
Boards will increasingly recognise that the CR reporting process is a valuable internal management tool.

Many CR managers have raised doubts about the effectiveness of a stand-alone CR report as a communication tool. But at the same time, they have recognised that a robust CR reporting process can be an effective management tool. The process of producing an annual CR report can act as a vehicle on which to build impact assessment, prioritisation; target setting; monitoring and evaluation; continuous improvement; awareness-raising; ...

As CR becomes more closely linked with core business strategy, the board will come to value the CR reporting process more as a management tool than as a communications tool. This will not lead to less CR reporting, because the annual or biennial CR report will remain an effective target or milestone.

Prediction 2
Boards will pay more attention to the accuracy of CR-related information.

With the codification of directors’ duties and the integration of CR into core business strategies, internal awareness of the importance of environmental and social issues will increase. This will increase the demand for CR-related information at board-level. And, as more core business decisions become dependent on CR-performance data, more attention will be paid to its accuracy.

This will in turn lead to companies using more robust data management systems and software, as well as more independent verification and other forms of assurance. Over time, the material CR issues will be managed, monitored and evaluated as effectively as financial issues not just because it is possible, but because it matters to the business.
Prediction 3
Companies will improve internal communication on CR.

Many companies now recognise that there are two benefits to internal communication on CR: first, good CR performance can improve employee engagement and motivation; and second, CR management requires employees to understand their role in delivering CR objectives and performance that are important to the company’s success. Internal communication can help both to build awareness and to change behaviour.

Many companies have traditionally focused on communicating responsible business practice to external stakeholders and, as a result, they may have to learn new ways of communicating on CR. In particular, employees with day-to-day experience in a company may be more skeptical of an external-facing “corporate” CR message. Also, employees will expect more two-way dialogue rather than one-way reporting.

Prediction 4
Companies will make better use of existing communication channels to deliver tailored messages to specific stakeholders.

Companies will use the annual CR reporting process as a management tool, and as a source of CR-related data and case studies. But with stakeholder segmentation, prioritisation and engagement, companies will better understand the specific interests that each audience has. They will also recognise that many of their existing communication channels can be used to communicate with these stakeholders.

As a result, while companies will continue to produce CR reports (printed or online), they will increasingly develop communications strategies that integrate the CR stories and information contained in the report into more of their communication channels. This approach will more effectively communicate that CR is integrated into everything that the company does.
Prediction 5

Boards will increasingly use the Annual Report and Accounts as a tool to demonstrate accountability to important stakeholders not just investors.

Annual Report and Accounts are legal requirements designed to ensure that shareholders have the information they need to assess the effectiveness of management. Although the Annual Report and Accounts is one of the most important communication tools, investors are not the only stakeholders concerned with management effectiveness.

The enhanced Business Review requires companies to give information that target a broader audience with a wider range of information. As Annual Report and Accounts move increasingly online, and as companies get better data management tools, it will be easier to structure the information to better address different audiences in a more cost effective manner.

Prediction 6

Companies will increasingly report material issues in their Business Review but will keep a separate CR section.

Companies that undertake materiality assessments understand that there are a range of risks and opportunities related to CR. Some of these are relevant to the business now; others are not, but may be so in the future. Companies that discuss material CR issues in their Business Reviews alongside other risks and opportunities will not flag this as “CR content”. This will mean that the role of the CR section in Annual Report and Accounts will change, or it will disappear.

Since material issues will be addressed in the Business Review, the CR section will be used to discuss those issues that, while not material now, should still be monitored by enlightened companies. The CR section in Annual Report and Accounts will evolve into a staging zone for issues that may become material in the future and will indicate other sources of information on CR.
Prediction 7
The role of the CR manager will increasingly be driven by an internal “pull” rather than an external “push”.

Many companies began to report on their CR performance in order to address vocal external critics. This led to externally-focused CR strategies and an externally-facing role for CR managers. As companies adopt a broader approach to non-financial value creation, and as CR priorities become more directly linked to business risks and objectives, CR managers will become more inwardly focused and business-driven rather than stakeholder-driven.

The CR manager will become a source of non-financial management expertise and business-critical information. Instead of “negotiating” performance improvements with different business units, the CR manager will become an implementation function acting on the board’s guidance and with the active encouragement of business units.

Prediction 8
Companies will take a systematic approach to integrating stakeholders’ interests into their decision-making processes.

The concept of “stakeholder” is becoming depoliticised and companies are now taking a constructive approach towards understanding and managing the networks of people that they influence, and that influence them. Companies that want to better understand non-financial value creation are also engaging with stakeholders as they once did only with customers – to understand where common interests can create mutual benefit.

At the same time, a range of different stakeholder engagement approaches is helping companies connect with diverse interest groups in more constructive ways. As companies get better at stakeholder engagement, they will recognise that the strategic value exceeds the operational risks, and they will integrate stakeholder engagement into strategic planning, priority setting, and new product development.
Prediction 9
Companies that engage in dialogue through partnerships will be better able to identify opportunities for value creation.

A company’s business consists of a complex set of relationships with employees, suppliers, customers, investors and governments. This network gives companies an incredible reach into communities globally, and makes them unique agents for delivering change.

As they expand these networks to include other partners, such as NGOs and community groups, companies will be better placed to identify business opportunities that also create social and environmental value.

This will help contribute not only to their own long-term success, but also to a more positive appreciation of the role of business in society.

Prediction 10 (your turn)
Some of the people reading this report will disagree with our predictions and will send us their own prediction on the future of CR communications.

This paper is part of an ongoing collaboration between Radley Yeldar and Business in the Community. Next steps will include a survey to test these predictions and a seminar to review the findings.

If you would like to be involved in this initiative, just send us your prediction on the future of CR communications and we’ll add you to our mailing list.

Send your predictions to:
predictions@ry.com
predictions@bitc.org.uk
A need to reconsider

Many CR issues have a fundamental business case. For example, no matter what your customers think of the reduction in CO$_2$ emissions, energy efficiency will save money and that is good; attracting the best and brightest employees and having suppliers that share your values will also save you money and that is good.

The UN-PRI, G3 and CA 2006 suggest that we are at the beginning of a new, more mature phase of CR. One where environmental and social impacts are recognised as part of the non-financial issues that impact on the value-creation process.

The only way to build business models that deliver financial and non-financial value is to engage in a dialogue with stakeholders to identify where your joint interests lie.

Nobody expects companies to be altruistic. Stakeholders recognise that companies are driven by self-interest. But society increasingly expects companies to be enlightened in their pursuit of long-term self-interest.

The success of a company is increasingly measured over a broader spectrum of criteria and relationships. This means that the incentives for improving non-financial performance, including CR performance, is increasing. It also means that the value of communicating CR performance is also increasing.

The leading companies already recognise that identifying and measuring responsible business practice is more valuable as a management tool than the CR report is as a communications tool. Moreover, most CR reports still focus only on the impacts of the company, not the impacts on the company. This is inconsistent with the current conception of CR.

Stakeholders want to understand the company’s response to issues of global sustainability – this requires telling a story that links the financial and non-financial performance to business strategy.

A stand-alone CR report does not on its own communicate a particularly integrated message. Audiences, such as investors and staff, are used to being communicated to more regularly and through a number of different channels. Companies should use existing channels to communicate targeted messages. If an audience is new, then new channels may have to be created.

2006 was a year that will have a permanent impact on our understanding and application of CR. It should also have a permanent impact on how companies communicate CR.
All the detail

This section contains a short overview of the Companies Act 2006; the UN Principles for Responsible Investment and the GRI-G3 Guidelines.

The Companies Act 2006
The CA 2006 is the first major reform of UK company law since 1985. In general, the reforms are designed to address four key objectives:
- Enhancing shareholder engagement and a long-term investment culture;
- Ensuring better regulation and a “Think Small First” approach;
- Making it easier to set up and run a company; and
- Providing flexibility for the future.

Directors’ Duties and Enlightened Shareholder Value
One of the most debated elements prior to the enactment of the CA 2006 concerned the general duties of directors. While it has long been accepted that directors should consider the wider interests of the company as a whole in assessing what is in the best interests of the company and its shareholders, the new legislation will move those duties from common law and equitable principles into statutory form. For the first time in the UK, the general directors’ duties have been codified.

The CA 2006 outlines seven specific directors’ duties, which are:
1. Duty to act within powers (section 171).
2. Duty to promote the success of the company (section 172).
3. Duty to exercise independent judgement (section 173).
4. Duty to exercise reasonable care, skill and diligence (section 174).
5. Duty to avoid conflicts of interest (section 175).
6. Duty not to accept benefits from third-parties (section 176).
7. Duty to declare interest in proposed transaction or arrangement (section 177).

Perhaps the most controversial of these has been section 172, which has been described as the corporate responsibility provision.

The Companies Act 2006 – Directors’ Duties
S.172 Duty to promote the success of the company
(1) A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to:
(a) the likely consequences of any decision in the long term,
(b) the interests of the company’s employees,
(c) the need to foster the company’s business relationships with suppliers, customers and others,
(d) the impact of the company’s operations on the community and the environment,
(e) the desirability of the company maintaining a reputation for high standards of business conduct, and
(f) the need to act fairly as between members of the company.

On 11 October 2005, the Minister for Energy, Malcolm Wicks, explained “enlightened shareholder value” in the context of directors’ duties:

“Under this approach the basic goal for directors should be the success of the company for the benefit of its shareholders. However, we believe, as the review did, that business prosperity and responsible business behaviour are two sides of the same coin. The duty will therefore go on to say that, in seeking to promote the success of the company, directors must have regard to factors such as the interests of the company’s employees and the impact of the company’s operations on the community and the environment.

The alternative approach (…) would enable or require company boards to override the interests of shareholders where they considered that this would satisfy broader ethical or social considerations. (…) I believe that there are two important reasons why [this alternative] would not be the best way forward (…) : directors would lack clarity about what they were meant to be doing, and it would in practice be more difficult for anyone to hold directors to account.”

5 www.publications.parliament.uk/pa/cm200506/cmhansrd/cm051011/halltext/51011h04.htm
The Department for Trade and Industry (DTI) has published explanatory notes to the CA 2006. As the DTI explains in these notes, the list of factors included in section 172 is not exhaustive, and the decision as to what will best promote the success of the company is up to the directors’ good faith judgment. This ensures that, subject to good faith, business decisions are for the directors, and not subject to decisions of the courts.

However, the DTI also noted that the directors would have to exercise reasonable care, skill and diligence in having regard to the factors. This will mean that it “will not be sufficient to pay lip service to the factors and, in many cases, the directors will need to take action to comply with this aspect of the duty”.

As the Association of Chartered Certified Accountants stated in June 2006, “[this] clause will impose on companies an element of ‘process’, in that there will be an increased level of formality attaching to the decision-making process.”

The Enhanced Business Review

On 28 November 2005, Chancellor Gordon Brown abolished the mandatory Operating and Financial Review (OFR). The OFR provisions had recently been integrated into the Companies Act 1985, and the Accounting Standards Board (ASB) had published a reporting standard (RS1). Following the repeal of the mandatory OFR, RS1 was converted into a voluntary Reporting Statement.

Despite the abolition of the mandatory OFR, bodies such as the Association of British Insurers (ABI) and the ASB still regard the Reporting Statement as a description of best practice for narrative reporting.

Under its obligation to implement the EU Accounts Modernisation Directive, the government had already enacted legislation on a Business Review to be included in the company’s Directors’ Report.

These provisions will be extended by the CA 2006 to include a new statutory purpose of the Business Review, namely to inform members and to help them assess how the directors have performed their duty under section 172 to promote the success of the company.

The CA 2006 also extends the requirements for quoted companies in a number of areas, including (where the directors consider it necessary for an understanding of the company’s business) trends and factors likely to affect the future of the company, and also in relation to a range of CR-related information (see text box).

Similarly, the Business Review provisions require the directors to exercise their judgment in relation to the reporting of KPIs to assist members in their understanding of the business of the company.

The Companies Act 2006 – Business Review

S.417 Contents of directors’ report

(1) Unless the company is subject to the small companies’ regime, the directors’ report must contain a business review.

(2) The purpose of the business review is to inform members of the company and help them assess how the directors have performed their duty under section 172 (duty to promote the success of the company).

(3) The business review must contain—

(a) a fair review of the company’s business, and

(b) a description of the principal risks and uncertainties facing the company.

(4) The review required is a balanced and comprehensive analysis of—

(a) the development and performance of the company’s business during the financial year, and

(b) the position of the company’s business at the end of that year, consistent with the size and complexity of the business.

(5) In the case of a quoted company the business review must, to the extent necessary for an understanding of the development, performance or position of the company’s business, include—

(a) the main trends and factors likely to affect the future development, performance and position of the company’s business; and

(b) information about—

(i) environmental matters (including the impact of the company’s business on the environment),

(ii) the company’s employees, and

(iii) social and community issues, including information about any policies of the company in relation to those matters and the effectiveness of those policies; and

(c) subject to subsection (11), information about persons with whom the company has contractual or other arrangements which are essential to the business of the company.

If the review does not contain information of each kind mentioned in paragraphs (b)(i), (ii) and (iii) and (c), it must state which of those kinds of information it does not contain.
(6) The review must, to the extent necessary for an understanding of the development, performance or position of the company's business, include—

(a) analysis using financial key performance indicators, and

(b) where appropriate, analysis using other key performance indicators, including information relating to environmental matters and employee matters.

“Key performance indicators” means factors by reference to which the development, performance or position of the company’s business can be measured effectively.

(7) Where a company qualifies as medium-sized in relation to a financial year (see sections 465 to 467), the directors’ report for the year need not comply with the requirements of subsection (6) so far as they relate to non-financial information.

(8) The review must, where appropriate, include references to, and additional explanations of, amounts included in the company’s annual accounts.

(9) In relation to a group directors’ report this section has effect as if the references to the company were references to the undertakings included in the consolidation.

(10) Nothing in this section requires the disclosure of information about impending developments or matters in the course of negotiation if the disclosure would, in the opinion of the directors, be seriously prejudicial to the interests of the company.

(11) Nothing in subsection (5)(c) requires the disclosure of information about a person if the disclosure would, in the opinion of the directors, be seriously prejudicial to that person and contrary to the public interest.

United Nations Principles for Responsible Investment

On 26 April 2005, Kofi Annan, UN Secretary General, launched the United Nations Principles for Responsible Investment (UN-PRI). At that time, over £1 trillion of assets signed up to the UN-PRI, including asset owners like CalPERS, the Norwegian Government Pension Fund, Universities Superannuation Scheme (USS) and the BT Pension Scheme.

The following week in Paris, at the European launch, institutional investors representing a further £1 trillion of assets became signatories, bringing the total to 39 asset owners valued at over £2 trillion.

Today, one year later, over 140 institutional investors and asset managers have signed up representing total assets under management of over £4 trillion. This is equivalent to the combined total valuation of the London and Tokyo Stock Exchanges.

Although the UN-PRI is not asset class-specific, its signatories recognise that they are likely to be phased in over time, starting with application to equities and property portfolios.

Working groups have now been established to look more closely at Responsible Investment in Emerging Market Equities, and Responsible Property Investment.

The Six Principles (UN-PRI)

Where consistent with our fiduciary responsibilities, we commit to the following:

1. We will incorporate ESG issues into investment analysis and decision-making processes.

2. We will be active owners and incorporate ESG issues into our ownership policies and practices.

3. We will seek appropriate disclosure on ESG issues by the entities in which we invest.

4. We will promote acceptance and implementation of the Principles within the investment industry.

5. We will work together to enhance our effectiveness in implementing the Principles.

6. We will each report on our activities and progress towards implementing the Principles.
The UN-PRI at a glance

- Investors with over £4 trillion under management have signed up to the UN-PRI.
- The UN-PRI is not about ethics; it is about increasing investment returns by better understanding the impact of non-financials on different asset classes.
- The two asset classes to which the UN-PRI most obviously applies is equities and property.
- The UN-PRI does not set “responsible investment” criteria; it is designed to expand the amount of research, and number of asset management mandates, that explicitly incorporate environmental, social and governance (ESG) issues.
- If it is implemented as intended, asset owners will require their asset managers to consider ESG issues in their investment analysis and decision-making.
- The Principles explicitly mention the value of standardised reporting, and mention the GRI
- The UN-PRI symbolises the shift in the investment community away from treating ESG issues as a niche product (SRI) towards incorporating ESG issues into mainstream financial analysis.
- ESG issues will remain only one, relatively minor, element guiding investment decisions. Evidence of the impact of the UN-PRI will not show up in investments or divestments; it will appear in the increase in investment and research mandates incorporating ESG issues.

More information, including a list of signatories, can be found at: http://www.unpri.org

The Global Reporting Initiative's G3 Guidelines on Sustainability Reporting

This summary is based on information available from the Global Reporting Initiative (GRI) and the United Nations Environment Programme (UNEP).

The Global Reporting Initiative (GRI) develops and disseminates globally applicable Sustainability Reporting Guidelines for voluntary use by all types of organisations. They address environmental, social and economic issues.

The GRI was initiated in 1997 by a US-based NGO called the Coalition of Environmentally Responsible Economies (CERES) in partnership with the United Nations Environment Programme (UNEP). In 1992 GRI was incorporated as an independent non-profit organisation in Amsterdam.

The GRI's key objectives are to:
- help present a balanced picture of an organisation' economic, environmental and social impacts;
- promote comparability between organisations; and
- facilitate stakeholder engagement.

The first guidelines were released in 1999; the second edition was published just prior to the 2002 World Summit on Sustainable Development (WSSD). The third edition, referred to as G3, was released in October 2006.

Key drivers for the development of G3

The decision to produce the G3 Guidelines was taken on the basis of a structured feedback process undertaken by GRI. The findings of this feedback process included the need to address the following elements:

**Relevance:** a need to clarify that a reporting organisation only needs to report on relevant indicators, not all of them. It was suggested that G3 also provide guidance on issue identification, prioritisation and selection of relevant indicators for reporting purposes.

**Reliability:** The Guidelines, including reporting principles, disclosure items, and indicators, should be refined so they represent more suitable criterion for assurance purposes.

**Investors:** Recognising their emergence as one of the main users of sustainability information, investors and other financial players were surveyed to find out what could be done to make sustainability reporting of greater utility to them.

**Number of indicators:** The G2 Guidelines contain 97 indicators. There was not a clear mandate to significantly increase the number of indicators. The objective was to improve clarity, consistency, and focus so that indicators reflect key priorities for reporting.
Performance-focus: The indicators were to be refined so that they elicit information that can be used to show change over time (i.e. “performance”), while still enabling organisations to put these results in context and explain the overarching management approach.

Comparable: Indicators should be refined so that data resulting can be more easily bench-marked to track performance by one organisation over time, or across multiple organisations.

Qualitative indicators need help: Recognising that the G2 qualitative indicators only requested descriptions and did not focus on outcomes or results, the challenge for G3 was to make qualitative indicators more comparable and results-oriented.

A how-to guide: Protocols were to be created for all indicators, containing definitions of terms that appear in the indicator wording, a compilation methodology, and other useful references.

Key findings from the structured feedback process

Different groups have different needs: The main stakeholder groups interested in reporting (i.e., businesses, investors, academics, civil society, labour, accounting, and others) had become increasingly clear about what they wanted out of sustainability reporting.

Reporting Organisations: Sustainability reporting must result in demonstrable advantages such as better management of sustainability issues, risk reduction, reputation enhancement or protection, stakeholder relations, investor relations, or internal performance benchmarking and communications. Although there is still widespread recognition that reporting fulfils external communication needs organisations are more and more looking to identify a set of key performance indicators that can fortify their effective management of sustainability issues.

Civil society: As the main issuer of the so-called “licence to operate”, organisations must still show transparency, accountability, and responsiveness to important sustainability issues for the communities in which they operate, to their employees, or to others that have a stake in their organisations. This may result in different information priorities and formats than those needed for KPI’s or internal management performance tracking.

Investors: Investors are interested in the financial health of the company. Consequently, investors information needs may not match what a company has identified as KPI’s for its own internal management, and may or may not reflect the information needs and issues identified as important for civil society stakeholders.

Principal changes made to G3

Format
Whereas G2 included accompanying resources, the G3 Guidelines focus only on reporting expectations. This ensures clearer, concise, and more targeted Guidelines, as well as a more sophisticated Reporting Framework that encompasses Protocols and Sector Supplements.

Structure
The overall structure of the G3 document has been adjusted to better match the flow of a typical reporting process. There are three parts to the G3 Guidelines:

Part 1) Principles and guidance:
- what issues to report on;
- how to ensure the quality of reported information; and
- how to set the report boundary.

Part 2) Standard disclosures; and
- organisational profile containing strategy and analysis of sustainability, including risks and opportunities;
- followed by disclosures on the management of key issues; and
- finally, results-oriented performance indicators.

Part 3) Guidance on how to apply the Guidelines.
- guidance on issues such as frequency and medium of reporting, and the reporting as a living process.

Reporting principles
G3 makes it clearer that the reporting principles are the basis of all reporting guidance and processes and updates the principles. The principles have been grouped in two categories:
1) those that help define report content, and
2) those that help ensure quality of reported information.

<table>
<thead>
<tr>
<th>Defining report content</th>
<th>Ensuring quality of reported information</th>
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<tbody>
<tr>
<td>Materiality</td>
<td>Balance</td>
</tr>
<tr>
<td>Stakeholder inclusiveness</td>
<td>Comparability</td>
</tr>
<tr>
<td>Sustainability context</td>
<td>Accuracy</td>
</tr>
<tr>
<td>Completeness</td>
<td>Timeliness</td>
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<tr>
<td></td>
<td>Clarity</td>
</tr>
<tr>
<td></td>
<td>Reliability</td>
</tr>
</tbody>
</table>
Each principle is presented with a short definition, a longer explanation on how its usefulness when applied, and a series of self-tests that help the practitioner apply the principle.

Accompanying these two sets of principles is a new section on how to set the report boundary, with new and practical guidance on how an organisation can determine which entities’ performance should be represented by the report, based on its level of significance, and level of control/influence.

**Standard Disclosures**
The Standard Disclosures section of the G3 Guidelines contains three basic parts:
1. Disclosure Items;
2. Disclosures on Management Approach; and
3. Performance Indicators.

**Disclosure items**
Disclosure items aim to elicit the overall context setting information about the reporting organisation, including size, scale, sector, approach to sustainability, stakeholder engagement, and parameters for the report. In G2, these were called “Reporting Elements”.

**Disclosures on Management Approach**
A Disclosure on Management Approach is found at the start of each of the six indicator sets (economic, environment, human rights, labour, society and product responsibility).

The DMA intends to capture much of the important narrative or qualitative information, such as policy and management oriented information, and to set the context for sustainability performance information which follows in subsequent performance indicators. In G2, the management disclosures were mixed in with the Reporting Elements and Indicators.

**Performance indicators**
The primary goals for refining indicators were to enhance their clarity, comparability, and reliability, and ensure that they focus on effectively communicating performance. There was also an effort to harmonise with definitions and terms used in existing international standards and other tools.

Although there were some new additions, consolidations and deletions, the overall number of indicators shrunk, including both for core and additional indicators.

<table>
<thead>
<tr>
<th>Total number of indicators</th>
<th>G2</th>
<th>G3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Type of indicator</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Core</td>
<td>50</td>
<td>47</td>
</tr>
<tr>
<td>Additional</td>
<td>47</td>
<td>32</td>
</tr>
<tr>
<td>Total</td>
<td>97</td>
<td>79</td>
</tr>
</tbody>
</table>

The indicators are still grouped in six categories:

**Economic (new indicators)** - retained concept of economic value added/wealth distribution, but expanded the section's coverage of indirect economic impacts. Specifically included new indicators to highlight involvement in local markets as well as indicators related to new issues such as climate change and pensions coverage.

**Environment** - mostly clarifications, refinements, and ensuring feasibility of measurement. Biodiversity indicators were streamlined to reduce overlap and inconsistencies.

**Labour Practices and decent work (new)** - new topics added on gender, pay ratios, and skills development. Focus on making the descriptive process indicators into comparable qualitative or quantitative disclosures.

**Human rights** - significant change in the section due to consolidations and refocusing on occurrence of incidents in order to get to comparable disclosures;

**Product responsibility** - focused on a move towards comparability and also did a limited amount of consolidation.

**Society** - focused on a move towards comparability and also did a limited amount of consolidation. One indicator added on corruption.

**Indicator protocols**
A one-page protocol was developed for each indicator, containing definitions of terms used, a set of compilation methodologies or expectations, and a list of useful resources for the practitioner.

**‘In Accordance’ status and application levels**
A more flexible, and complex, system was established by which organisations can declare the extent to which they have applied the Guidelines. This provides a mechanism by which advanced organisations can distinguish themselves, and it may also help to tempt organisations onto the first rung of the ladder.

Organisations may self-declare themselves to one of three application levels (A, B and C), each with specific criteria. If an organisation has sought external assurance on the report, it can add a “+” to the relevant application level.

Organisations must self-declare an application level if they are to be recognised as a GRI-user. This would enable them to list their report on the GRI website. In addition, organisations may voluntarily ask a third-party to verify the declaration, or may ask the GRI itself to do so. GRI-verified reports can use the GRI Level Check logo.
Harmonisation with CR tools
The Guidelines are still based on the major international conventions for human rights, labour and the environment, so consistency will remain. The main targets for harmonisation have been identified as global norms (i.e. OECD Guidelines for Multinational Enterprises, Global Compact), financial sector tools (i.e. rating agency questionnaires), and assurance standards.

The results of harmonisation can be seen in two forms:

a) changes to the Guidelines; and
b) linkages between the Guidelines and other initiatives.

Transition to G3 (2006)
GRI will for two full reporting cycles continue to recognise reports prepared using the 2002 Guidelines.

Future revisions
Human rights and community indicators are two priority areas that the Technical Advisory Committee (TAC) will incorporate into their work plan in 2007. Users’ experience with some elements, such as the Disclosures on Management Approach, will also lead to refinements over time.

More information on GRI and G3 is available at: www.globalreporting.org

G3 Application levels

<table>
<thead>
<tr>
<th>Report application level</th>
<th>C</th>
<th>C+</th>
<th>B</th>
<th>B+</th>
<th>A</th>
<th>A+</th>
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<tbody>
<tr>
<td>Standard Disclosures</td>
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<td>G3 Management Approach Disclosures</td>
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<tr>
<td>G3 Performance Indicators and Sector Supplement Performance Indicators</td>
<td>OUTPUT</td>
<td>Report on a minimum of 10 Performance Indicators, including at least one from each of: social, economic and environmental</td>
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<td></td>
<td>Report on all criteria listed for Level C+: 1.2 3.9, 3.13 4.5 - 4.13, 4.16 - 4.17</td>
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<td>Management Approach Disclosures for each Indicator Category</td>
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<td>Report on a minimum of 20 Performance Indicators, at least one from each of: economic, environment, human rights, labour, society, product responsibility.</td>
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<td>Report on each core G3 and Sector Supplement* indicator with due regard to the materiality principle by either: a) reporting on the indicator or b) explaining the reason for its omission.</td>
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</tbody>
</table>

Source: www.globalreporting.org

*Sector Supplement in final version
Business in the Community is a unique movement in the UK of over 750 member companies committed to improving their impact on society in the community, environment, marketplace and workplace.

Registered Details 137 Shepherdess Walk, London N1 7RQ.

Registered Charity No: 297716
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Product Code: 01IND000346