What is integrated strategic planning, budgeting and forecasting?

- What is integrated strategic planning, budgeting and forecasting?
- How does it fit into the reporting cycle?
- How can this guide help you?
- Benefits and challenges
- Getting started

How to embed sustainability into strategic and financial planning processes

- Overview
- Tools and guidance
- Budgeting
- Forecasting
- Practical examples

How to ensure effective oversight and accountability

- Overview
- Tools and guidance
- Strategic management
- Aligning business goals
- Organizational structure and oversight
- Reporting frameworks
- Decision making
- Power and process
- Risk management frameworks
- Practical examples

How to set an approach to monitoring

- Overview
- Tools and guidance
- Employee performance
- Organizational performance
- Practical examples

How to integrate sustainability into your technology and data strategy

- Overview
- Tools and guidance
- Data requirements
- Risks and challenges of implementing a big data approach
- System and functionality requirements
- Current systems gap analysis
- Common pitfalls
- Practical examples

How to assess current maturity and what to do next

- Maturity map
- Top tips
- Case study index
- References
THE PROJECT TEAM

We would like to thank all of the project team members who contributed to the A4S Strategic Planning, Budgeting and Forecasting Guide.

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INTRODUCTION FROM THE A4S CFO LEADERSHIP NETWORK

Successful organizations seek to thrive over the long term in a world that is volatile, uncertain and complex. Eight out of the top ten risks highlighted by the World Economic Forum in 2018 are related to environmental or social issues. Risks that a decade ago weren’t seen as a noteworthy threat to business, such as extreme weather events, water crises and failure of climate change mitigation and adaptation are now starting to bite. Developing a strategic response to these issues, mitigating the risks and seizing opportunities arising from an effective response, should be at the front and centre for every organization. All CFOs should ensure these issues are addressed in an integrated manner within their strategic planning, and followed through with aligned budgeting and forecasting. Integration and alignment are key to the creation of a resilient future.

The finance team plays a crucial role here. They ensure strategies are costed, financial resources are allocated, and performance is monitored. Finance teams can also prove that the strategy itself drives sustainable long term value. This is underpinned by the availability and robustness of relevant data. High quality data that is important to the strategy must be used in the formulation of the plan, not simply as a statistic in reporting.

STARTING THE CONVERSATION

If you work in finance, this guide has been designed to help you. The practical tools and insights are pragmatic and useful, so consider its content and share its ideas with your colleagues. The guide will enable you to have a conversation about what you can do in your own organization to deliver sustainable long term value.

All members of the A4S CFO Leadership Network have pledged to build sustainable business models. We pilot, refine and embed relevant integrated thinking and ideas into these models and commit to positive action. As we do this we have the opportunity to keep our financial plans, budgets and forecasts aligned to the strategies that ensure our businesses are resilient and well positioned to thrive. We hope you will want to join us.

SCOTT LONGHURST
MANAGING DIRECTOR, FINANCE
AND NON-REGULATED BUSINESS,
ANGLIAN WATER GROUP

“All CFOs should ensure these issues are addressed in an integrated manner within their strategic planning, and followed through with aligned budgeting and forecasting.”
Scarcity of resources and the impact of climate change are just two of the current sustainability related trends of growing economic concern. Demand for energy is increasing dramatically, and climate change impacts arising from extreme weather, rising sea levels and policy changes are already being felt. Other significant trends such as the ageing population, greater inequality and rapid urbanization are also starting to have an impact.

Business is not only exposed to the risks and potential turbulence from these trends, but is also well positioned to capitalize on the many opportunities which arise. To be successful, businesses will have to take a long term strategic view of sustainability and build it into the key value creation enablers that drive returns on capital, support growth and mitigate risk.

This transformational change is only possible if sustainability factors are incorporated into strategic planning and into the allocation of capital that drives innovation, invests in new ventures and builds resilience. Each organization’s path to capturing value from sustainability will be unique, but the guidance and case studies within this A4S Essential Guide can serve as a useful starting point from which to build.
WHAT IS INTEGRATED STRATEGIC PLANNING, BUDGETING AND FORECASTING?

Organizations today must navigate an increasingly complex, interconnected, and constantly evolving world. Sustainability factors affecting society, the environment, and the wider economy are posing greater risks and opportunities to businesses than ever before. As a result, an increasing number of organizations see sustainability as an integral part of overall corporate strategy and long term value creation.

To be sustainable, an organization must achieve long term financial performance, whilst operating within environmental constraints and generating positive value for society. Strategic planning, budgeting and forecasting are core processes in managing an organization’s financial and operational performance, and play a critical role in influencing and shaping the implementation of corporate strategy. Despite the importance of these processes, many organizations still have a long way to go to integrate sustainability into their activities.

COST OF INACTION

Failure to incorporate sustainability into an organization’s strategy, and subsequently into the budgeting and forecasting processes, can result in missed opportunities to improve decision making and risk management, enhance innovation and stakeholder engagement, and align business performance with long term value drivers.

Sustainability is now a corner stone of successful businesses where finance teams are providing increasing leadership within their organizations to ensure decision making fully encompasses economic, social and environmental impacts.

Gregor Alexander, Finance Director, SSE

THE ROLE OF FINANCE

The core skills of those in finance teams can be extremely valuable in integrating sustainability into business as usual processes. In particular, the following can be applied equally to non monetary data as to the monetary data that finance teams are accustomed to working with:

- Experience of data and information analysis
- Preparation and communication of management information
- Management of information systems
- Identification of opportunities for growth
- Assessment and mitigation of risks

The use of these skills are essential when performing integrated analysis, and are vital to smooth integration of sustainability into strategic planning, budgeting and forecasting.
The diagram below sets out the overall process flow from strategic planning to management reporting. For further details on the left hand side section see the forthcoming A4S Essential Guide to Integrated Management Reporting.

HOW DOES IT FIT INTO THE REPORTING CYCLE?

- Produce consistent and accurate integrated performance reports which develop insight and enhance decision making.
- Ensure the control environment is sufficiently robust to provide complete and accurate reporting under the framework.
- Extend the current reporting framework to support integrated strategic and operational decision making.
- Create an integrated strategy and set strategic objectives.
- Produce an integrated budget and forecast with sensitivity testing where appropriate.
This guide aims to support organizations in enhancing the integration of social, economic, and environmental considerations into their strategic planning, budgeting and forecasting processes. It is intended for a finance audience, including Chief Financial Officers, Finance Directors, Financial Controllers, Heads of Financial Planning and Analysis, and other finance professionals.

The guide introduces current practices and the key challenges faced by organizations when factoring sustainability into planning, budgeting, and forecasting processes. It seeks to address the questions we have outlined below and to define the characteristics of good practice.

In order to inform this guide, we have asked ourselves the following questions:

### Process
- Is there a structured way of thinking about how to integrate sustainability issues within our organization’s strategic planning, budgeting and forecasting processes?
- How do we improve the finance team’s awareness of sustainability and the value that it adds to the business?
- How can we ensure that we are allocating the right resources to adopting an integrated approach, given existing pressures on the finance team?
- How can we ensure that sustainability is integrated into our budgeting and forecasting processes consistently and effectively across the organization?

### Governance
- How do we gain buy in and support for integrated planning, budgeting and forecasting from the whole leadership team?
- How do we create a cross enterprise culture that is aligned with, and supportive of, integrated planning, budgeting and forecasting activities?
- How should each business unit and functional team become involved in supporting the integration of sustainability within planning, budgeting and forecasting processes?
- Are our planning, budgeting and forecasting processes linked to reporting, performance appraisal, and incentive mechanisms that drive the right sustainability behaviours across the organization?
- How do we improve how the finance team collaborates with sustainability specialists on strategic planning, budgeting and forecasting activities?
- How do we overcome short term financial pressures that prevent us from developing integrated planning, budgeting and forecasting processes?

### Performance Management
- How do we ensure we have timely access to reliable data to feed into our strategic planning process?
- How do we prioritize the key performance metrics to be reflected in integrated strategic plans, budgets and forecasts, given the abundance of available data?
- How should we approach enhancements to our current finance system to support integrated planning, budgeting and forecasting more effectively?
- How can we go about improving the quality of data underpinning integrated planning, budgeting and forecasting processes?

### Technology and Data
- How do we ensure we have timely access to reliable data to feed into our strategic planning process?
- How do we prioritize the key performance metrics to be reflected in integrated strategic plans, budgets and forecasts, given the abundance of available data?
- How should we approach enhancements to our current finance system to support integrated planning, budgeting and forecasting more effectively?
- How can we go about improving the quality of data underpinning integrated planning, budgeting and forecasting processes?

The case studies in this guide have been collated from both the A4S CFO Leadership Network, and other companies, to demonstrate how organizations are starting to answer these questions.
Members of the A4S CFO Leadership Network have experienced first hand how integrating sustainability into strategic planning, budgeting, and forecasting makes clear business sense. Business benefits include:

- Identifying sustainability opportunities and risks, and enabling integrated strategies and responses
- Driving investment to protect and enhance long term viability and success
- Aligning performance management with long term value drivers
- Reducing cost through operational efficiency
- Providing significant brand benefits
- Encouraging balanced organizational culture, and building better employee and customer engagement

The practical examples found throughout the guide highlight these business benefits.

For many organizations, integrating sustainability within strategic planning, budgeting, and forecasting processes represents uncharted waters. It can be challenging to link sustainability drivers to business strategy, and to embed an integrated response into finance and operations. To be effective, long term strategic objectives must be translated into near term budgeting and forecasting processes. Members of our Network have experienced the following challenges:

- “Our business runs on a three year planning timeframe, so the rest of the business wouldn’t see the value in looking further ahead.”
- “Responsibility for sustainability is still unclear.”
- “Running the financial process is difficult enough, how do we include information we don’t have data for?”
- “We don’t have the system capability or the time to complete this manually.”
- “We are all rewarded on financial metrics so this is what we focus on.”

Examples of how they have been overcome have been included in this guide:

76% of CEOs define business success by more than financial profit

73% of CFOs believe there is a strong link between sustainability performance and financial performance

“Our initial thinking was that we would enhance our understanding and management of important risks and opportunities, and we were right.”

Christian Armitage, Group Financial Reporting Manager, Yorkshire Water
BENEFITS AND CHALLENGES OF AN INTEGRATED APPROACH

HOW TO RESPOND TO THESE CHALLENGES

To respond to these challenges, firstly consider the following:

- Understand the opportunities and risks that your organization is exposed to as a result of environmental and social trends.
- Set the tone at the top and incorporate identified opportunities and risks into organizational strategy and strategic objectives.
- Determine measurement approach, define indicators and set appropriate targets against which to report.
- Identify who in the business can influence the achievement of the objectives and make them accountable.

In order to implement successfully the considerations above, we recommend focusing on the following areas of finance function activity to build capability:

**PROCESS**

- Adopt a more integrated approach to strategic, financial and operational plans.

**GOVERNANCE**

- Integrate sustainability into the relevant governance structures and associated processes across the organization. Ensure cross functional involvement and ownership of the objectives are agreed.

**PERFORMANCE MANAGEMENT**

- Identify sustainability success factors, and make these integral to performance management of both the organization and of your employees.

**TECHNOLOGY AND DATA**

- Define and build the required technology, systems and data capability to support the collation of more robust sustainability information.

This guide focuses on each of these areas in turn.
TOP TIPS FOR GETTING STARTED

1. Consider how and whether sustainability factors are reflected in the organization’s vision and mission statement.
2. Engage with internal and external stakeholders to understand the sustainability landscape faced by the organization.
3. Assess the extent to which the leadership team is supportive of building integrated planning, budgeting, and forecasting processes.
4. Identify the key sustainability change agents within the organization, and understand their roles, responsibilities, and performance objectives.
5. Extend recruitment into the finance team to include those with key skills to enable integrated planning, budgeting and forecasting.
6. Assess current short term and long term incentive plans to see how they are driving employee behaviour.
7. Define data requirements to support integration, and assess quality needs based on materiality.
8. Understand technology and system requirements and agree where improvements are needed.

Introduction
- What is integrated strategic planning, budgeting and forecasting?
- How does it fit into the reporting cycle?
- How can this guide help you?
- Benefits and challenges
- Top tips for getting started

Process

Governance

Performance management

Technology and Data

Maturity and reference
STRATEGIC PLANNING

1. Assess the organization’s mission, vision, strategic context and environment
2. Set strategic goals, incorporating sustainability considerations
3. Determine critical success factors, barriers, risks and enablers for achievement of goals
4. Define and agree high level activities and initiatives

BUDGETING

1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors
2. Convert the strategic plan and high level initiatives into annual activities and milestones, allocating accountable owners
3. Set and agree performance commitments and budgets for each business unit and function
4. Deliver detailed ‘top down and bottom up’ annual operational and financial plans

FORECASTING

1. Assess performance
2. Provide a realistic outlook based on the current business environment
3. Provide the latest view of expected underlying performance
4. Allow timely management decisions and corrective actions

PROCESS

Strategic planning, budgeting and forecasting are established business processes, although each organization will have a slightly different approach in place. We have set out a typical strategic planning, budgeting and forecasting process. Over the following pages, suggested integration activities are set against these steps so that individual organizations can tailor the guidance to meet their individual needs and the standard strategic planning, budgeting and forecasting steps that they follow.
### PROCESS: KEY CHALLENGES

**Organizations said...**

<table>
<thead>
<tr>
<th>Statement</th>
<th>We need...</th>
</tr>
</thead>
<tbody>
<tr>
<td>“The strategic planning, budgeting and forecasting processes vary across organizations, which makes it difficult to create a standard approach for integration.”</td>
<td>Tips for integration which can be adapted depending on how the organization manages the process.</td>
</tr>
<tr>
<td>“There is little awareness across finance teams on sustainability matters, and the value it adds to the business.”</td>
<td>Knowledge sharing across the organization, and increased collaboration between the finance and sustainability teams.</td>
</tr>
<tr>
<td>“Our business runs on a three year planning timeframe, the rest of the business wouldn’t see the value in looking further ahead.”</td>
<td>Tips and tools to understand the sustainability landscape and potential impacts faced by the organization, to build the business case for longer term planning.</td>
</tr>
<tr>
<td>“The finance team believe we have an important role to play in integrating sustainability, but progress to date is limited.”</td>
<td>Increased clarity on the role of finance and the difference we can make.</td>
</tr>
</tbody>
</table>
The need to plan strategically is generally understood by senior finance professionals. This strategic planning should be proactive in integrating sustainability and incorporate long term factors in order to maximize opportunities and increase resilience in the ever changing operating environment.

We outline a four step process, with supporting tools, to guide finance teams towards integrating sustainability into the strategic planning process.

### PROCESS: STRATEGIC PLANNING

1. **Assess the organization’s mission, vision, strategic context and environment**
2. **Set strategic goals, incorporating sustainability considerations**
3. **Consider critical success factors, barriers, risks and enablers for achievement of goals**
4. **Define and agree high level activities and initiatives**

### BUDGETING

1. **Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors**
2. **Convert the strategic plan and high level initiatives into annual activities and milestones, allocating accountable owners**
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### FORECASTING

1. **Assess performance**
2. **Provide a realistic outlook based on the current business environment**
3. **Provide the latest view of expected underlying performance**
4. **Allow timely management decisions and corrective actions**
**PROCESS: STRATEGIC PLANNING**

1. Assess the organization’s mission, vision, strategic context and environment

**ACTIVITIES/INITIATIVES TO SUPPORT INTEGRATION**

- Work closely with your corporate strategy team to ensure a comprehensive integration of sustainability into corporate strategy.
- Set the context for strategic analysis by starting with the corporate mission, vision and values.
- Identify the external sustainability drivers and risks that are relevant to the organization’s existing strategy, taking into account exposure along the value chain, including suppliers, own operations and customers.
- Consider if strategy needs to be revisited to address these risks, and/or to take advantage of opportunities arising.
- Assess and agree the correct timeframe for the assessment, as risks arising from macro sustainability trends often manifest themselves over a longer time horizon with uncertain timing.
- Use analytical frameworks to provide a structured approach to assessing the organization’s strategic context and environment, e.g. horizon scanning, PESTEL, BA CLIAT or sSWOT.

**PRACTICAL EXAMPLE**

To understand fully the opportunities and risks that the business was likely to face over the next 25 years, we applied the PESTEL framework to our vision and strategy. We worked with external sustainability experts to develop evidence based forecasts of Yorkshire and the UK in 25 years time and the key stages of change in between. From this work, we aligned objectives and targets with our business plans, and set scorecards for milestone years towards longer term outcomes to 2040.

"Taking a long term view and structuring our decision making around the five capitals (financial, manufactured, natural, social and human) has led to a fundamental change in our strategy."

Liz Barber, Group Director of Finance and Regulation, Kelda Group (Yorkshire Water)
1. Assess the organization’s mission, vision, strategic context and environment

APPROACHES TO IDENTIFYING RISKS ARISING FROM MACRO SUSTAINABILITY TRENDS – HORIZON SCANNING

We have found that horizon scanning is the most useful approach to inform the identification of material risks arising from macro sustainability trends.

<table>
<thead>
<tr>
<th>What is it?</th>
<th>Horizon scanning is a technique for analysing the future and considering how emerging trends and developments might affect the success of organizations through a systematic examination of potential threats and opportunities.</th>
</tr>
</thead>
<tbody>
<tr>
<td>When is it used?</td>
<td>It is an important precursor to proactive risk management and business continuity. Businesses should consider an appropriate timeframe based on the nature of business activity and the timeframe over which relevant macro sustainability trends are forecast.</td>
</tr>
<tr>
<td>Time horizon</td>
<td>The technique explores new and unexpected issues, as well as persistent issues and trends, and can help challenge past assumptions. A solid ‘scan of the horizon’ can provide the background for risk management and for developing strategies to anticipate future developments. Organizations can thereby gain lead time and a competitive edge. Horizon scanning can also be a way to assess trends to feed into the scenario development process.</td>
</tr>
<tr>
<td>Challenges</td>
<td>Organizations should take care not to take too short term a focus as they may miss issues where adaptation or mitigation measures are needed now to prepare for future risks.</td>
</tr>
</tbody>
</table>

WAYS OF UNDERTAKING HORIZON SCANNING

We have found that to be effective a range of horizon scanning techniques should be used.

Desk based research
A number of universities, NGOs and consultancies publish assessments of the macro sustainability trends that may be material to your sector. Lists of sustainability issues that may be relevant provided by sustainability reporting organizations, such as the Global Reporting Initiative (GRI), the Sustainability Accounting Standards Board (SASB), or the World Economic Forum (WEF) can be a useful place to start.

Surveys
Surveys can be used to supplement this research and can provide you with a broader reach, particularly where stakeholders are in different countries / regions. We have found this approach helpful to obtain input from our supply chain, customer base, partner organizations or internal stakeholders who are difficult to reach via interviews or workshops.

Interviews and workshops
Personal interviews or workshops can help you to understand matters from research or surveys in more detail. Workshops often consist of a small group of experts and cross functional representatives, who share their perspectives and knowledge to help identify which risks are likely to be most material and how they may impact your business.

Questions to ask
Example questions to help stimulate discussion:

- What are the macro sustainability trends that are impacting our business now? How are these likely to change over time? Are there any new risks we should consider in the future?
- How are these trends likely to impact our value chain e.g. suppliers, customers? Which other external stakeholders may be impacted?
- In what ways do these risks impact the achievement of our strategy and objectives?
- Can we turn these risks into opportunities?
- What sources of information will enable a better understanding of these risks? How can we improve our visibility of these risks and what additional internal / external data do we require?
- What is the direction of government policy and regulation? How does this vary in each of our markets?
### PROCESS: STRATEGIC PLANNING

**1. Assess the organization's mission, vision, strategic context and environment**

**APPROACHES TO IDENTIFYING RISKS ARISING FROM MACRO SUSTAINABILITY TRENDS – PESTEL, BACLIAT AND sSWOT**

<table>
<thead>
<tr>
<th>Process</th>
<th>PESTEL</th>
<th>BACLIAT vulnerability assessment</th>
<th>sSWOT (specific sustainability SWOT)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>What is it?</strong></td>
<td>Framework for external factors which may affect activities and performance e.g.:</td>
<td>BACLIAT stands for The Business Areas Climate Impacts Assessment Tool</td>
<td>The sSWOT provides a new twist on the familiar framework which helps drive action and collaboration on sustainability challenges that create material business risks and opportunities. The sSWOT is designed to help identify connections between sustainability challenges and other trends that are creating big changes in future markets.</td>
</tr>
</tbody>
</table>
| • **Political:** Increased competitiveness of emerging markets, governmental priorities/attitude to environmental and social protection | • Workshop based tool to help organizations quickly consider potential impacts of future climate change risks that include: – Past events – Events that will continue to happen as the climate changes – Potential impacts that have not yet been experienced | **Questions to ask when conducting an sSWOT:**
| • **Economic:** Move towards a circular or sharing economy, supply chain traceability | • Framework for considering impacts in the following business areas: markets, process, logistics, people, premises and finance | 1. What (or who) do you want to inform? A specific person, decision or output? |
| • **Social:** Population growth, expanding middle class, urbanization | • As a standalone tool, or as a step in a risk based framework such as the UKCIP Adaptation Wizard (a risk based adaptation resource) | 2. What do you and others see changing? What are the challenges and trends? |
| • **Technological:** Digitalization, energy efficiency and renewable energy, social media | • When there is a wide range of participants from different business | 3. Where are environmental challenges creating broad threats to future business value? |
| • **Environmental:** Climate change, resource depletion, water scarcity | • Provides insights into how climate risks are spread across different business functions | 4. Where is there a potential gap in the market where we and others can create new solutions for environmental challenges? |
| • **Legal:** Green taxation, carbon trading, mandatory disclosure requirements | • Can draw on a range of knowledge and experience, raise awareness and generate buy in to the adaptation process | 5. What are unexpected ways we can apply our strengths to environmental challenges? Are there partners that can be leveraged? |
| **When is it useful?** | • To help identify current external factors e.g. climate change as well as those that may change in the future e.g. increase in frequency of extreme weather events | • Increased awareness of the range of threats and emerging issues that climate change could bring to your business | 6. Who else has similar weaknesses or faces similar risks from environmental challenges? Can we assess the risks together? |
| • The PESTEL analysis can be further expanded to STEEPLED to also consider Demographic and Ethical factors impacting the business | • Provides insights into how climate risks are spread across different business functions | 7. Which insights will influence and resonate with your CEO, CFO, directors, or other decision makers, or what keeps them up at night? |
| **Benefits** | • As a standalone tool, or as a step in a risk based framework such as the UKCIP Adaptation Wizard (a risk based adaptation resource) | • It may be difficult to predict fully, future changes in the business environment as it rapidly evolves | 8. What can we do (together with partners) in the near term, mid term, and long term? |
| • Provides a holistic understanding of the wider business environment | • Can encourage strategic thinking beyond a short term time horizon | • If too much information is gathered, it may be challenging to identify material risks that are directly relevant to the business | **Challenges** |
| • Can encourage strategic thinking beyond a short term time horizon | • Provides insights into how climate risks are spread across different business functions | • Representatives from across the business are required | **Challenges** |
| **Challenges** | • May it be difficult to predict fully, future changes in the business environment as it rapidly evolves | • Negotiations on the trade offs between different business interests are likely | **Challenges** |
HOW TO BUILD A COMMON UNDERSTANDING OF SUSTAINABILITY WITHIN FINANCE TEAMS

Enabling the effective integration of sustainability within strategic planning, budgeting and forecasting requires finance teams to work closely with their sustainability and operations teams to ensure shared understanding of which sustainability issues and opportunities are material to the business, and how to integrate relevant data and other considerations relating to these issues and opportunities into strategic planning, budgeting and forecasting decisions.

A common understanding of sustainability factors can be enhanced through the following strategies:

- **Bridging the gap**
  - Leverage the complementary capabilities of both the finance and sustainability teams in actively managing business performance.
  - This can accelerate the integration of sustainability within strategic planning, budgeting and forecasting processes.

- **Engaging and communicating**
  - Ensure finance teams communicate and engage with operating teams and sustainability specialists throughout strategic planning, budgeting and forecasting activities.
  - Take advantage of formal (e.g. strategic planning meetings, budget validation discussions, quarterly business reviews) and informal (e.g. corporate training events) channels to interact and establish a mutually beneficial dialogue on the sustainability risks and opportunities for the organization.

- **Integrating sustainability into management information**
  - Integrate the key performance measures and metrics used for monitoring sustainability factors in financial reports, scorecards and dashboards where material.
  - Integrating sustainability performance measures within the organization's management information platform can help emphasize the importance of these issues to organizational performance and facilitate decision making.

- **Aligning with standardized processes**
  - Follow a structured and standardized process across the business to identify and assess sustainability factors in the strategic planning phase.
  - This can increase finance teams’ knowledge and experience in sustainability and can help to determine better how to integrate within financial processes.
PROCESS: STRATEGIC PLANNING

2. Set strategic goals, incorporating sustainability considerations

ACTIVITIES/INITIATIVES TO SUPPORT INTEGRATION

- Disaggregate the organization’s long term strategic priorities into a series of desired outcomes which reflect what success looks like in pursuing the organization’s strategic vision. Ideally, desired outcomes should be mutually exclusive and collectively exhaustive in representing the organization’s strategic priorities.

- Perform initial analysis to understand the potential impact of the desired outcomes on sales and cost.

- Set long term objectives that address the desired outcomes on sales and cost.

- Use non monetary targets alongside monetary ones, and provide insightful qualitative commentaries for completeness. Ensure that these are measurable, comparable and achievable in the long term.

- Define the key performance measures to monitor the objectives, and ensure that information on sustainability is appropriately included within the measures.

PRACTICAL EXAMPLE

Over the next 25 years, our ability to maintain the balance between water supply and demand will be challenged by macro sustainability trends such as population growth, climate change, growing environmental need and deteriorating raw water quality. Most of the risks to our ability to deliver arise from uncertainty about timing and the magnitude of the impacts from growth and climate change. To address these issues, Anglian Water is leading the Water Resources East project (WRE) which brings together multiple partners from a wide range of industries to manage these challenges, building on the region’s unique opportunities for sustainable future growth and pioneering a new approach to managing water resources. Performing scenario analyses using Robust Decision Making (RDM) and Multi Criteria Strategy Optimization to identify optimized, balanced, and robust water plans to define our strategic goals.

See full case study for further information

Over 300 scenarios were developed. Their performance was tracked using a number of different measures including total capital and operating costs, and environmental performance.
2. Set strategic goals, incorporating sustainability considerations

Setting targets and objectives allows the organization to translate desired outcomes into actionable long term performance measures. While the planning period should reflect the organization’s business model and industry characteristics (typically ranging from three years to 25 years), longer planning periods should be considered in order to provide a more complete view of the impacts of long term external factors, including sustainability factors, on the organization’s value drivers. This will help to identify long term risks and opportunities that require near term action, e.g. for large capex projects or significant supply chain changes.

**KEY STEPS FOR SETTING LONG TERM TARGETS AND OBJECTIVES**

- Critique the mission and vision for holistic value creation, protection and resilience
- Analyse the strategic environment, assess the opportunities and threats to success, and engage with stakeholders
- Assess resources and capabilities, and identify the internal strengths and weaknesses
- Incorporate these outputs into strategy generation and evaluation processes
- Distil strategy into long term targets and objectives
- Conduct scenario planning and analysis with dynamic assumptions

**WHEN SETTING STRATEGIC TARGETS AND OBJECTIVES, CONSIDER WHETHER THEY:**

- reflect and indicate performance against desired long term outcomes, beyond the ordinary strategic cycle
- are relevant to the organization’s mission, vision, business operations and activities
- lead not only to financial benefits for the organization, but also to broader benefits for society and the environment, thereby minimizing or eliminating the impact of negative externalities and creating positive ones
- are measurable and quantifiable
- are appropriate given the time period
- consider the transition risks and physical risks from climate change
- account for other external factors and constraints (e.g. laws, regulations, environmental standards, resource scarcity, customer and social pressures, etc.)
- are achievable given the organization’s capabilities and resources
- are linked to the organization’s performance management framework (e.g. performance appraisals, incentive compensation policies, etc.)
2. Set strategic goals, incorporating sustainability considerations

**SCENARIO ANALYSIS**

It is notoriously difficult to discern trends and determine what the future may bring. Our knowledge about business and operating markets is based on past experience and, in isolation, is increasingly inadequate to navigate the future successfully. Scenario analysis is a structured way for organizations to think about the future, as a foresight methodology used to drive better decision making. It can be used to test the resilience of a strategy in an uncertain future, and to plan how an organization wishes to position itself in terms of responsiveness, flexibility and competitive advantage in the longer term.

Scenarios are possible views of the world described in narrative form to provide context for decision making. For example, the International Energy Agency’s 2°C Scenario lays out an energy system deployment pathway and an emissions trajectory consistent with at least a 50% chance of limiting the average global temperature increase to 2°C. In setting scenarios, it is useful to have a range of scenarios that consider the possible, plausible, probable and preferable.

<table>
<thead>
<tr>
<th>What is it?</th>
<th>When should I use it?</th>
<th>Benefits</th>
<th>Challenges</th>
<th>How used in practice</th>
</tr>
</thead>
</table>
| • A tool to model a range of future scenarios against which to test potential solutions or decisions | • In setting strategic goals, to inform how the business may need to evolve to meet the need of these future scenarios  
• To develop appraisals of the cost and benefit of different responses  
• To assess whether the impacts of future scenarios are going to be negative or positive  
• To prioritize effort in further analysis or specific research | • Can take advantage of external perspectives and data sources  
• Collaborative approach, requiring input from experts and key stakeholders can give useful insights on potential sales and cost impact of a given scenario  
• Using the Delphi survey method (a collaborative approach to gathering opinions) to supplement scenario modelling, can lead to a consensus forecast on future trends, as the experts surveyed converge their opinions on a single position | • Development of future scenarios is based on assumptions  
• A wide range of stakeholder views need to be incorporated to form a balanced overview  
• Conceiving realistic scenarios requires a profound understanding of not only the macro trend, its risks and the underlying processes and factors, but also of other events that may be triggered by the trend | • The approach can be simplistic (e.g. through the development of optimistic, realistic and pessimistic scenarios) right through to highly complex computerized modelling tools and techniques using, for example, Monte Carlo Simulation |
PROCESS: STRATEGIC PLANNING

2. Set strategic goals, incorporating sustainability considerations

SCENARIO ANALYSIS

Scenario analysis is becoming increasingly important in particular in relation to climate change as part of testing the resilience of current and potential future strategy, as well as providing stakeholders with an understanding of climate related opportunities and risks.

TRANITION PATHWAY INITIATIVE

The Transition Pathway Initiative is an asset owner led initiative, supported by asset managers and owners, with over £2 trillion assets under management. The initiative assesses how companies are preparing for the transition to a low carbon economy. It:

- evaluates and tracks the quality of companies’ management of their greenhouse gas emissions, and of opportunities and risks related to the low carbon transition;
- evaluates how companies’ future carbon performance would compare to the international targets and national pledges made as part of the Paris Agreement);
- publishes the results of this analysis through an online tool.

The pension funds invested in the Transition Pathway Initiative have committed to using the results in a number of different ways including: informing their investment decision making; engagement with companies; dialogues with fund managers and engagement with policy makers.

TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES

The Financial Stability Board established this industry led task force to help identify the information needed by investors, lenders, and insurance underwriters to assess and price climate related risks and opportunities appropriately. The Task Force developed four widely adoptable recommendations on climate related financial disclosures that are applicable to organizations across sectors and jurisdictions, and recommends that these disclosures are included in organizations’ main financial filings.

The Task Force structured its recommendations around four thematic areas that represent core elements of how organizations operate:

- Governance
- Strategy
- Risk management
- Metrics and targets

Scenario analysis

One of the Task Force’s key recommended actions is related to the disclosure of potential impacts of climate related opportunities and risks on an organization’s business, strategies, and financial planning under different potential future states (scenarios), including a 2°C scenario. Over time, the Task Force expects to see more quantitative analyses in disclosures, including the underlying assumptions associated with the climate related scenarios used.

*The agreement sets out a global action plan to put the world on track to avoid dangerous climate change by limiting global warming to well below 2°C increase relative to pre-industrial levels. The use of a 2°C scenario is thus a useful way of evaluating the resilience of strategy under a 2°C scenario. It also helps investors allocate funds towards accelerating the transition to a low carbon economy and thus protects their investments and beneficiaries from the projected negative financial outcomes as the degree of warming increases.*
PROCESS: STRATEGIC PLANNING

3. Consider critical success factors, barriers, risks and enablers for achievement of goals

ACTIVITIES/INITIATIVES TO SUPPORT INTEGRATION

- Consider how sustainability trends can impact the factors that are critical to achieve strategic goals.
- Analyse these critical success factors, considering where there are barriers to the success of corporate strategy, and test the resilience of the planned strategy against sustainability risks where they have the potential to become barriers if they manifest.
- Incorporate sustainability factors relevant to the strategic goals into your corporate risk matrix, and identify where internal barriers may also prevent effective mitigation of sustainability risks.
- Determine appropriate mitigation strategies, incorporating enablers to minimize barriers to success.

PRACTICAL EXAMPLE

The Crown Estate is a specialist real estate business, with all our net surplus going to the Treasury for the benefit of the nation. Our vision at the Crown Estate is to become a truly modern, commercial business. We identified the critical success factors necessary to achieve this vision and in doing so, considered the material issues (including sustainability factors) that create risk for the organization and potential barriers to us achieving it. Using this analysis, we have implemented enablers that help us to overcome each of these material issues.

See full case study for further information
Sustainability factors have been considered in setting corporate strategy. However, they should also form part of the process for determining barriers and risks to the achievement of critical success factors. For example, where the strategy involves setting up operations in a new region, factors such as flooding risk, indigenous rights over land or water extraction need to be identified and addressed.

Identifying risks and barriers in this way ensures that the necessary enablers are implemented in such a way that considers not just internal barriers, but external risk factors too.

Consider each critical success factor in turn and assess:

1. Whether the critical success factor could impact/be impacted by social and environmental factors
2. The likelihood and potential magnitude of that impact
3. To what risks or barriers to success this exposes the organization
4. How barriers can be overcome and risks mitigated

The factors that are necessary for the business to achieve its mission, gain competitive advantage and/or deliver its strategy.

Testing the resilience of the planned strategy against sustainability risks using critical success factor analysis:

**Critical success factors**

- Ability to source critical resources
- Ability to respond to consumers’ needs
- Coping with rapid change
- Attraction of capital
- Product safety
- Engaging with strategic partners
- Product development and speed to market

**Sustainability lens**

- Ethics
- Biodiversity
- Food scarcity
- Rising poverty
- Energy security
- Social inequality
- Responsible production
- Health, safety and wellbeing
- Responsible consumption
- Gender inequality
- Finite resources
- Climate change
- Human rights
- Reputation
- Regulation
- Pollution

**Barriers and risks**

- Inhibitive structures, culture, systems, silos and/or incentives
- Employee dissatisfaction

* Risks can become barriers if they manifest. Internal barriers may also prevent effective mitigation of sustainability risks.

Ways to remove barriers and create conditions that empower people to deliver on the critical success factors, strategy and/or necessary change.
PROCESS: STRATEGIC PLANNING

4. Define and agree high level activities and initiatives

ACTIVITIES/INITIATIVES TO SUPPORT INTEGRATION

- Disaggregate the organization’s long term strategic goals, establishing a structured, consistent and standardized procedure to identify all strategic initiatives and encourage focus on sustainability issues. Adjust the assessment timeframe accordingly based on the nature of the goals.

- Enable filtering and cross business unit validation of all strategic initiatives based on established criteria that include sustainability factors.

- Set up working groups with specialists from the relevant areas of the business at an early stage to assess the impact and dependencies of the initiatives, and to ensure that the level of governance is appropriate.

PRACTICAL EXAMPLE

Scottish and Southern Electricity Networks, part of the SSE Group, provide power to homes and businesses across 59 Scottish islands through submarine electricity cables. To ensure a reliable supply of power, the cables are proactively replaced before they reach the end of their operational life. Changes to Scotland’s National Marine Plan meant that existing engineering practises within the marine environment were challenged and the cost of the works could increase dramatically. Working with an external partner to develop a tool to model the relative social, environmental and economic impacts of different engineering solutions, and with a variety of stakeholders to estimate the magnitude of the impact, we have developed an evidence and risk based assessment which has been accepted by our regulators.

See full case study for further information
4. Define and agree high level activities and initiatives

**WHO TO INVOLVE**

**Leadership:** Strategic initiatives should be approved by the Board, a delegated committee, or designed within strategic parameters set by the Board. Board level competency around sustainability is essential.

**Project team:** A cross functional team (with representatives from across the business, and potentially from supplier organizations) can broaden skillsets and increase innovation. This should include sustainability specialists.

**Investment Committee:** Consider involving the Board Investment Committee and report to them.

**Specialists:** Depending on the type, scope and complexity of the initiative, it may be appropriate to include external specialists in the project team, particularly at the design phase.

**Stakeholders:** Including stakeholders external to your organization can help increase support for the initiatives and offer additional perspectives, particularly on socio economic and environmental factors.

**WHAT TO CONSIDER**

**Suitability:** Clear criteria should be set to assess suitability of proposed initiatives. These should include a strategic alignment metric and a cost benefit analysis that includes social and environmental costs and benefits where appropriate.

**Timeframe:** The length of the initiatives should be appropriate in the context of the long term strategic goals, but also short enough to maintain momentum.

**Integration:** Ensure the initiatives are designed and performance managed in an integrated way.

**Portfolio coverage:** Ensure that the portfolio of initiatives collectively covers each key aspect of the long term strategic goals. Consider how gaps can be filled and whether overlaps will aid achievement or create inefficiency.

**Critical success factors:** Identify the factors that are necessary for successful delivery of the initiatives and achievement of the long term strategic goals, and whether there are any significant barriers to these. Ensure social and environmental, short term and long term issues are considered.

**Opportunities and risks:** Examine the external environment for opportunities and risks. Initiatives can be designed to mitigate risks, or to capitalize on opportunities to create competitive advantage. Factors external to the initiative can change significantly over its life. Consider how social, economic, political and environmental landscapes and stakeholders’ perceptions might change, and how this may affect success.

**Mitigations and enablers:** Establish whether risk can be mitigated or managed to an acceptably low level, and enablers identified to overcome perceived barriers. For sustainability risks, this can often involve working with the value chain to identify innovative solutions.
Once the strategic goals and supporting high level activities have been agreed, capital needs to be allocated effectively by aligning budgets to the desired strategic outcomes.

We outline a four step process, with supporting tools, to guide finance teams towards integrating sustainability into the budgeting process.

### PROCESS: BUDGETING

- **STRATEGIC PLANNING**
  1. Assess the organization’s mission, vision, strategic context and environment
  2. Set strategic goals, incorporating sustainability considerations
  3. Determine critical success factors, barriers, risks and enablers for achievement of goals
  4. Define and agree high level activities and initiatives

- **BUDGETING**
  1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors
  2. Convert the strategic plan and high level initiatives into annual activities and milestones, allocating accountable owners
  3. Set and agree performance commitments and budgets for each business unit and function
  4. Deliver detailed ‘top down and bottom up’ annual operational and financial plans

- **FORECASTING**
  1. Assess performance
  2. Provide a realistic outlook based on the current business environment
  3. Provide the latest view of expected underlying performance
  4. Allow timely management decisions and corrective actions
1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors

**ACTIVITIES/INITIATIVES TO SUPPORT INTEGRATION**

- Provide clear guidelines for the budgeting process that address sustainability considerations and their link to business growth and implementation of business plans.
- Use the budget process as an opportunity to integrate sustainability into other activities.
- Ensure that budget guidelines set out steps to consider the sustainability implications of activities as part of the budgeting process.
- Ensure that the guidelines incorporate all key financial, social and environmental assumptions.
- Formalize a standard approach on integrating cost savings and incremental revenues arising from sustainability initiatives directly into budgets.

**PRACTICAL EXAMPLE**

At Microsoft, we have implemented a carbon fee model that puts an incremental fee on the carbon emissions associated with our company’s operations. The price on carbon is determined by the total cost of the carbon fee fund investment strategy, which is set to meet the organizational carbon reduction policy objectives. The fees that we collect through the carbon fee model go into a central fund used to subsidize investments that enable Microsoft to reduce emissions and be net carbon neutral.

See full case study for further information

**PRACTICAL EXAMPLE**

A wide range of initiatives have been embedded into the Crossrail budgeting structure which put long term benefits at the centre of how the whole project is designed and delivered. This means that the budget priorities, rather than focusing on the construction cost, include minimizing whole of life costs of the project as well as negative social and environmental impact, and provide wider economic benefit across the country. The budgeting approach includes ring fencing £1m for safety training that sets new standards for the industry and geographical supply chain ring fencing.

See full case study for further information
1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors

**EMERGING APPROACHES TO BUDGETING FOR SUSTAINABILITY FACTORS**

Budgets are historically a purely financial domain, with a focus on factors that have a direct, short term financial impact. However, there is merit in considering non monetary factors which have a significant impact on the budgeting process. These impacts may be financial, environmental and/or social in nature, and budgeting methods to account for these vary from simple to sophisticated. Companies operate in a budget constrained environment, so integrated budgeting is about how to maximize and prioritize the resources you do have, to best effect.

Determining the right approach will depend on a number of factors such as overriding strategic goals and the required pace and nature of change. The key attributes of each approach will help with this decision. The diagram opposite summarizes potential ways to prepare an integrated budget. Each method is discussed in more detail on the following pages.

**BUDGETS AS DISTINCT FROM TARGETS**

Many organizations set sustainability related targets, some of which are set to be attainable, some of which are aspirational. They may be over the short, medium or long term. What turns a target into a budget could be considered just a matter of terminology, but it can be argued that a budget is more restrictive, more emotive, and requires a greater level of commitment. A budget is similar to a quota in that it is finite, there is a set limit or quantity that can be used e.g. a financial budget, carbon budget, or fishing quota. A budget is generally shorter term e.g. an annual budget, though it is not only about short term delivery but also investment in longer term sustainable performance. A target is typically something to aim for, rather than necessarily something that must be met.

A) Ring fencing

The simplest approach available, which involves setting aside monetary budgets for the cost associated with sustainability related initiatives (see the next page for further guidance).

Key attributes:
- Simple
- Widely understood
- Easily monitored
- Only considers monetary factors
- Enables sustainable outcomes to be prioritized

B) Allocation

Requires splitting budget out across different budget owners or operating units to meet relative needs. Allocation may, for example, be based on size of operation, or opportunity for improvement (see page 33 for further guidance).

Key attributes:
- Relatively straightforward
- Widely understood
- Can facilitate matching of positive and negative cost impacts in relation to a specific budget line, asset or business unit
- Can encourage financial efficiency, where cost savings from one project can ‘unlock’ budget for another

C) Capitals budgeting

Covers several different approaches which can be used to set budgets in non monetary terms either separately or combined with monetary budgets and the associated interdependencies. For example, a water budget may be set (see page 36 for further guidance).

Key attributes:
- Adaptable to level of simplicity/sophistication needed
- Different approaches to choose from, depending on needs
- Can account for interdependencies between monetary and non monetary capitals
- Can be focused on particular functions, e.g. procurement

D) Shadow pricing

Involves assigning a tangible value to an intangible item for which there is no current market value. Most commonly used as a way of reducing greenhouse gases by setting a carbon price (see page 39 for further guidance).

Key attributes:
- Adaptable to level of simplicity/sophistication needed
- Can drive cultural change
- Efficient way to achieve objectives
- Supports transparency, accountability and risk management
- The choice of shadow price can be highly subjective
PROCESS: BUDGETING

1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors

A) RING FENCING

Where an organization has set strategic goals that have societal and/or environmental impacts, then often a financial budget will need to be ring fenced to allow for the cost associated with meeting those goals.

Examples of human capital factors that may merit a ring fenced financial budget

- **Human health/wellbeing**
  - Health and safety team, training and equipment
  - Wellbeing initiative(s)

- **Job creation/skills development**
  - Apprenticeships
  - Staff development and training

- **Working conditions/practices**
  - Subsidized staff canteen
  - Team building away days

This approach can also apply to environmental and social factors.

**PRACTICAL EXAMPLE**

At Asda, we set monetary budgets in line with strategic sustainability objectives.

See full case study for further information

**PRACTICAL EXAMPLE**

At Bupa, we ring fenced funding for low carbon and renewable energy projects through establishment of our £50m Energy Saver Fund.

See full case study for further information

**PRACTICAL EXAMPLE**

At SSE, we developed a community investment fund package for the communities around our onshore wind farms. The methodology for determining the size of this fund is standardized and fully transparent. For the last three years we have published an overview of the sustainable impacts of these funds including a focus on economic, environmental and social projects.

See full case study for further information
1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors

A) RING FENCING

Many organizations have policies or targets to source locally. However, often this is aspirational rather than aligning processes and procedures to meet them. One way to make these targets more achievable is to use a ring fenced budget approach. The illustrative example below for a fictitious organization based in Bremen, Germany shows a potential framework for a local sourcing budget:

- A maximum of 20% of procurement spend can come from outside Bremen and Lower Saxony.
- A minimum of 80% in Bremen and Lower Saxony of which at least 30% is in Bremen and adjacent districts.

These non local budgets should be finite, or at least require senior management sign off to extend them in the same way as all other budgets. Once a local sourcing budget has been set, the case study below demonstrates how local suppliers can be engaged.

Setting budgets in this way can drive behaviour to:
- build community relationships and engage with local suppliers to help grow the local economy and create socio economic benefit in the area; and
- help build skills and capabilities to increase the value of the local human capital pool and ensure local businesses continue to grow and bring sustainable, long term, local benefits.

PRACTICAL EXAMPLE

At SSE, we set up an Open4Business portal in the Highlands and Islands to create a strong local supply chain.

See full case study for further information

Setting budgets in this way can drive behaviour to:
- build community relationships and engage with local suppliers to help grow the local economy and create socio economic benefit in the area; and
- help build skills and capabilities to increase the value of the local human capital pool and ensure local businesses continue to grow and bring sustainable, long term, local benefits.
1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors

**B) ALLOCATION**

In setting strategic goals, and determining a path towards achieving them, organizations will need to consider the costs associated with those goals in the short, medium and long term, and allocate budgets accordingly.

There are different approaches to allocating budget to the different budget owners, or operating units, depending on the specific circumstances. Budgets may be allocated top down, on application, or resolved through a more iterative approach. Depending on the allocation approach, it may assist organizations in matching negative and positive cost impacts which offset each other.

<table>
<thead>
<tr>
<th>Allocation by</th>
<th>Examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asset</td>
<td>• Budget can be allocated on a totex basis, i.e. capex plus opex. This effectively permits increased capex spend (perhaps to include energy, carbon or water saving measures) to be later offset by a reduced opex requirement.</td>
</tr>
<tr>
<td>Opportunity or exposure</td>
<td>• Allocating budget to each site to manage their risk of flooding. Some sites will be higher risk than others, and budget can be allocated based on this risk exposure, as well as size and criticality of each site.</td>
</tr>
<tr>
<td></td>
<td>• An organization has significant cost saving opportunities from energy saving technologies. Sites can be allocated budget to install measures such as LED or motion sensor lighting, and allocation can depend on the relative energy saving opportunity particular to each site.</td>
</tr>
<tr>
<td>Outcome</td>
<td>• The desired outcome is a reduction in greenhouse gas emissions. Budget can be allocated based on the marginal cost per tonne of greenhouse gases saved of the most cost effective option. These savings are then used to invest in the next most cost effective option, and so on, enabling investment options to be prioritized in the most cost effective way, ensuring efficient use of finite budgets and allowing the &quot;freeing up&quot; of cash for subsequent implementation of more expensive options at a later date (see the next page for interdependencies and cost curves).</td>
</tr>
<tr>
<td></td>
<td>• The desired outcome is for a more sustainable product. The redesign of the product means that less wood is required as a raw material in the product manufacture, and the money saved from the reduction in quantity of raw material can be used to increase the proportion of sustainable timber procured.</td>
</tr>
</tbody>
</table>
PROCESS: BUDGETING

1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors

B) ALLOCATION

Interdependencies and cost curves

Interdependencies between budgets need to be understood and opportunities for cost neutrality identified. One recognized way of doing this is to use a cost curve, with a Marginal Abatement Cost Curve being a common way of unlocking financial budget for greenhouse gas emission reduction initiatives. By plotting the marginal cost associated with a number of carbon reduction options against the carbon reductions each method can be expected to achieve, the options can be ranked in order of implementation priority. This allows carbon to be saved in the most cost effective way, freeing up cash for implementation of more expensive options at a later date.

PRACTICAL EXAMPLE

At City, University of London, we used a marginal abatement model to budget for emissions reduction options.

See full case study for further information

ILLUSTRATIVE MARGINAL ABATEMENT COST CURVE
PROCESS: BUDGETING

1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors

B) ALLOCATION

There are some potential wider applications of this approach.

Job creation and employability

- Marginal cost per £ of socio economic value created (£)
- Apprenticeships
- Partnerships with social enterprises
- Sponsoring vocational qualifications
- Socio economic value p.a.
- Work placements
- Community IT skills programmes

Water

- Marginal reduction cost per '000 litres of water saved (£)
- Sensor taps
- Rainwater harvesting
- Waterless urinals
- Install water meters
- Efficient flush toilets
- Water savings ('000 litres p.a.)

Wellbeing

- Marginal cost per £ of human capital value created (£)
- Health checks for managers
- Staff wellbeing programme
- Human capital value p.a.

Cost savings arising from increased productivity, lower absenteeism and decreased staff turnover.

See the A4S Essential Guide to Social and Human Capital Accounting for tools, guidance and links to job creation and employability measurement methodologies.
PROCESS: BUDGETING

1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors

C) CAPITALS BUDGETING

Capitals budgeting is a collective term for setting budgets for natural, human and social capitals in non-monetary terms. These can be set either separately or combined with monetary budgets, for example an energy budget of €X with a carbon budget of Y tonnes. There are a variety of different approaches, of varying uses and complexities which lend themselves to a range of different situations and purposes.

The simplest approach is to set a budget for the amount of a "capital" which can be used in the period. The examples below show how this can be applied to natural capital.

EXAMPLES OF ENVIRONMENTAL FACTORS FOR WHICH A BUDGET COULD BE SET

<table>
<thead>
<tr>
<th>Factor</th>
<th>Budgets Examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>Carbon</td>
<td>• Maximum GHGs to be emitted&lt;br&gt;• Maximum embodied carbon (i.e. GHGs emitted in the extraction, manufacture and transport of raw materials, together with end of life emissions)</td>
</tr>
<tr>
<td>Waste and pollution</td>
<td>• Maximum waste to be produced/sent to landfill&lt;br&gt;• Maximum number of pollution incidents/amount of pollutants released</td>
</tr>
<tr>
<td>Water use</td>
<td>• Maximum water to be used&lt;br&gt;• Maximum water to be abstracted</td>
</tr>
<tr>
<td>Biodiversity</td>
<td>• Maximum green belt disturbed, e.g. for construction&lt;br&gt;• Maximum use of pesticides, e.g. in agriculture</td>
</tr>
<tr>
<td>Resource use</td>
<td>• Maximum quota of non-certified materials, e.g. wood, fish, palm oil&lt;br&gt;• Maximum use of non-recycled materials</td>
</tr>
</tbody>
</table>

PRACTICAL EXAMPLE

At Anglian Water, we set an embodied carbon budget for 2030. The budget restricts embodied carbon in new assets built to 30% of 2010 embodied carbon levels.

See full case study for further information

PRACTICAL EXAMPLE

At Sainsbury’s, we set zero carbon, waste and water budgets for new stores.

See full case study for further information
PROCESS: BUDGETING

1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors

C) CAPITALS BUDGETING

Setting a carbon budget
Carbon budgets are an important tool for realizing emissions reductions either operationally and/or, through capex. They set the overall level of ambition for reductions, and the areas of the business where effort should be focused. The analysis used to develop carbon budgets can inform the types of operating policies that may be appropriate to unlock emissions reduction potential. Once set, carbon budgets provide a mechanism for monitoring emissions reduction performance, and for shaping any response should targets be missed. Monitoring of progress against carbon budgets should form part of strategic integrated management reporting.

A number of key decisions need to be made about the budgets e.g.:

• The baseline year, the timescale of each budgetary period and the long term target
• How changes in the structure of the organization over time should be accounted for (ordinarily with an adjustment to the baseline)
• Whether to use a location based or market based methodology for scope 2 emissions
• Which scope 3 emissions to include

Organizational emissions reduction targets have historically often been set without due consideration of the necessary scientifically backed reductions needed to keep climate change within “tolerable” limits, the technical feasibility of available emission reduction technologies, and/or the level of financial investment needed to achieve reduction targets. Consequently, targets are frequently of inconsequential impact (too small), failing to drive real innovation to unlock potential savings; or lack the commercial rigour needed to support the business case for investment required to achieve them. The approach presented here incorporates these factors with a view to determining an ambitious, but demonstrably achievable, carbon and financial budget programme.

For most organizations, meeting a budget such as this could be expected to include significant energy efficiency improvements in buildings and industrial processes, fuel efficiency improvements in road vehicles, and a significant shift towards renewables in electricity, heating and cooling. Some of the required emissions reduction can be achieved at negative cost and would therefore save money, unlocking financial budget for implementation of more expensive reduction options. Carbon budgets have a role to play in Shadow Pricing and Marginal Abatement Cost Curves.
1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors

AN APPROACH TO SETTING A CORPORATE CARBON BUDGET

- Assess feasible emissions reduction scenarios
  - Perform analysis of technical feasibility, costs and realistically achievable emissions reduction
  - Perform financial analysis over potential scenarios, e.g. emissions reduction scenarios:
    1. Current ambition
    2. Extended ambition
    3. Stretch ambition

- Set a long term target
  - Determine a ‘top down’ reduction target cognisant of scientifically backed required progress (e.g. under a 2°C scenario)
  - Agree a baseline year against which to measure emissions reduction potential and a timescale for the target

- Consider the need for interim budgets, splitting the long term target over strategic cycles (e.g. five year blocks) and/or matching to key interim national budgets

- Reference emissions projections
  - Review national carbon budgets and projected reductions for key regions of operation e.g. the UK’s 80% reduction by 2050 (against 1990 levels)
  - Review published scenarios reflecting alternative assumptions on fossil fuel prices and population growth
  - Consider known or anticipated policy changes for key regions of operation

- Required reductions versus reference projections
  - Required reductions versus feasible reductions

- Proposed budgets
  - Use the outcomes of the required, reference and feasible reduction target analysis to determine an ambitious, but realistic, carbon and financial budget programme for each strategic cycle that will permit achievement of the long term target. Allocate across the organization.

For guidance on setting science based targets see the Science Based Targets Initiative
PROCESS: BUDGETING

1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors

D) SHADOW PRICING

Shadow pricing provides a framework for an organization notionally to ‘cost’ an item into their business operations where it does not have a current, defined market price, or where current prices are deemed too low to factor in future risks or societal impacts. This is increasingly being used by organizations for carbon emissions, however it can also be used for other resources such as water.

Putting an internal cost on carbon provides a useful risk mitigation to the future regulation of carbon.

A shadow carbon price can be used in different ways, for example:

- Simply incorporating into project or investment budgets (monetizing the carbon impact) and thus creating the business case to invest in lower carbon options
- Using the shadow price to drive an internal carbon market

The same concept can also be used for other items such as water, waste or pollutants, where a shadow cost can be developed to represent potential higher future cost per unit or potential changes in compliance thresholds.

PRACTICAL EXAMPLE

At Danone, we incorporated carbon pricing into our capital investment appraisal process. See full case study for further information

PRACTICAL EXAMPLE

At Coca-Cola Hellenic Bottling Company, we introduced a science backed carbon reduction target, driven by an internal carbon price. See full case study for further information

PRACTICAL EXAMPLE

At Royal DSM, we have set a shadow carbon price in the valuations of large investment projects. We set the carbon price at €50/t CO₂e so it is high enough to materially affect investment decisions to drive down greenhouse gas emissions. See full case study for further information
PROCESS: BUDGETING

1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors

USING SHADOW PRICING TO DRIVE AN INTERNAL CARBON MARKET

An internal carbon market provides a mechanism for reducing emissions across the organization, whilst also pooling budget to invest further in lower carbon opportunities. A potential approach to this could be:

1. Consider the organization’s total carbon inventory, and the relative intensity of this across the business, and determine the level of reduction aspiration in the short, medium and long term.

2. Set a shadow price on emissions to be charged to each business unit profit and loss account, relative to their respective emissions, and taking into account any planned, major capex projects.

3. Engage with the Board/management of each business unit to communicate the approach, allocate accountability and autonomy, and agree the process for charges and bids for efficiency improvements, where appropriate.

4. Centrally pool the amounts charged to each business unit and reallocate based on priority efficiency improvements, either pre determined at a strategic level and/or in response to successful efficiency bids submitted by the business units.

5. Revisit the carbon price annually, raising incrementally and transparently over time.

Determining a carbon price

There are several recognized ways to price carbon:

- **Traded cost of carbon**
  The traded cost of carbon is the current value of traded emission rights within a recognized carbon market.

- **Non traded cost of carbon**
  A non traded value of carbon may be explicitly estimated by a national government or regulator (with reference to national carbon targets) to guide abatement activity for sectors not captured within a recognized carbon market.

- **Social cost of carbon**
  The social cost of carbon reflects the socio economic cost of emissions, incorporating impacts such as spread of disease, decreased food production, coastal destruction etc.

- **Marginal abatement cost**
  The marginal abatement cost reflects the cost of reducing emissions.

- **Bespoke carbon price**
  Set at a level that will drive change in line with the organization’s specific circumstances and ambition.

POTENTIAL WAYS TO COLLECT FUNDS

- Charge a fee based on relative, previous or current emission levels
- Charge a fee based on the organization wide reduction target, allocated across business units by emission levels or productivity output
- Apply a fee to emissions exceeding a predetermined level

POTENTIAL WAYS TO REDISTRIBUTE FUNDS

- Prioritize investment based on the effectiveness of projects submitted by business units (i.e. by carbon reduction and financial pay back)
- Prioritize investment based on scalability, investing in business units where behavioural reductions are greatest

It is good practice to increase the carbon price incrementally every year to drive further reductions.
PROCESS: BUDGETING

2. Convert the strategic plan and high level initiatives into annual activities and milestones, allocating accountable owners

ACTIVITIES/INITIATIVES TO SUPPORT INTEGRATION

- Disaggregate the long term targets set in strategic planning into medium and short term milestones.
- Set specific, time bound activities that are aligned to the budgeting cycle timeframe, are measurable and are clearly linked to the corporate strategy. These activities should be mapped to where financial, social and/or environmental budgets will be required. Agree who will be accountable for measurement and monitoring of the activities.
- Ensure key risks and opportunities identified by assessing the strategic context and environment are reflected in the short and medium term activities and budgets.

PRACTICAL EXAMPLE

In order to achieve a common thread from a long and short term perspective, we incorporated the strategic aims of our 25 year plan, which have a high profile position of sustainability, into our five year plan commitments. The commitments were used to develop an Outcome Delivery Incentive ("ODI") framework, which attributes financial reward or penalty to financial and other performance outcomes. ODIs are then divided into annual performance targets for internal planning and driving delivery. Each function then prepares detailed budgets and delivery plans based on their targets.

See full case study for further information
PROCESS: BUDGETING

2. Convert the strategic plan and high level initiatives into annual activities and milestones, allocating accountable owners

DEVELOP AND CASCADE THE ANNUAL TARGETS ACROSS THE BUSINESS

Develop annual targets across business units and functions by disaggregating long term targets into short term measures (annual, quarterly, monthly, etc.) and developing operating plans that incorporate sustainability actions.

LONG TERM STRATEGIC OBJECTIVES
(E.G. 25 YEAR PLAN)

Objectives incorporating aspirations for example around: growth, profitability, product development, transition to a low carbon economy, preservation of natural capital, and investment in social and human capital.

1. Enablers
   - Identify significant enablers required to achieve long term objectives.
   - Identify and assess risks which may impact achievement of long term targets.

2. Pace of change
   - Determine necessary pace of change, including key step changes across a long term time frame (e.g. 25 years).
   - Perform sensitivity analysis, accounting for potential manifestation of major risks. Consider whether specialist input is required to establish time frame e.g. for climate change impacts and/or resource scarcity risks.

3. Targets
   - Map out targets in medium term increments (e.g. five years) and short term increments (e.g. every year for first five years).

4. Investment
   - Determine investment needed in short term to meet short term targets.
   - Forecast likely investment for medium and long term targets, for enhanced viability.

5. Budgets
   - Consider savings likely to be generated by sustainability projects, for example, through reduced energy and waste costs and a more secure supply chain.
   - Define integrated budgeting approach (e.g. ring fencing, allocation, capitals budgeting and/or shadow pricing) and set the short term budgets necessary for required progress towards long term strategic goals and targets.
PROCESS: BUDGETING

3. Set and agree performance commitments and budgets for each business unit and function

ACTIVITIES/INITIATIVES TO SUPPORT INTEGRATION

- Ensure that each business unit and function sets and agrees specific integrated objectives and targets, in line with their financial and operational capability and capacity.
- Link the established commitments to the annual and long term integrated targets that are set in the strategic planning phase.
- Ensure that budget targets are based on performance measures that allow the organization to gauge success or progress towards achieving the organization’s long term objectives, and that the underlying data used to calculate performance measures is reliable.
- Consider the extent to which flexibility is required within performance commitments and budgets, such that funds can be reallocated during the course of the budget cycle should operating circumstances change.

PRACTICAL EXAMPLE

In a desire to create a more flexible approach, we have taken a radical step and moved away from a traditional annual budgeting cycle. Under the new model we have a flexible quarterly spending plan supported by a five quarter rolling forecast, which facilitates quick and responsive reallocation of non fixed resources to where they add most value at a point in time. For us, the concept of adding value is broad and not just financially based. Performance commitments are set in terms of goals, with devolved responsibility to business unit level. The role of our finance people in this is very important.

See full case study for further information
### PROCESS: BUDGETING

#### 3. Set and agree performance commitments and budgets for each business unit and function

**KEY STEPS TO AGREE PERFORMANCE COMMITMENTS**

Setting and agreeing performance commitments with business units and functions enables ownership, validation, and buy in to the organization’s short term and long term goals and objectives.

<table>
<thead>
<tr>
<th>Step</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Review historical performance</td>
</tr>
<tr>
<td>2.</td>
<td>Identify existing and expected resources and capabilities to meet desired performance</td>
</tr>
<tr>
<td>3.</td>
<td>Understand opportunities and risks relevant to achieving desired performance</td>
</tr>
<tr>
<td>4.</td>
<td>Discuss, validate, and agree performance commitments with business units and functions</td>
</tr>
<tr>
<td>5.</td>
<td>Obtain approval of agreed performance commitments by CEO and Board</td>
</tr>
</tbody>
</table>

**CONSIDER:**
- Agreed performance commitments on sustainability targets in previous years
- Extent to which sustainability targets were met in previous years
- Impact of sustainability factors on wider performance
- In house expertise and skills relevant to sustainability issues faced by the organization
- Recruitment of those with skills in integrated planning, budgeting and forecasting into the finance team
- Sustainability enabling technologies
- Ongoing sustainability initiatives and investments
- Potential for new opportunities, such as new products, services or partnerships that bring socio economic or environmental benefit
- Impact of social, environmental, and economic risks on the organization’s resources and capabilities
- Input from sustainability specialists
- Input from business unit and functional leaders
- Input from finance business partners
- Whether performance commitments are aligned with the organization’s strategic priorities and desired outcomes
PROCESS: BUDGETING

4. Deliver detailed ‘top down and bottom up’ annual operational and financial plans

ACTIVITIES/INITIATIVES TO SUPPORT INTEGRATION

- Ensure that budgets are developed ‘top down and bottom up’ with cross unit validation and the direct involvement of the finance teams and the relevant sustainability specialists where applicable.
- Incorporate incremental project costs and benefits into the business as usual budget and ensure that there is a clear link to the business case and the identified impact tied to the overall strategy.
- Use all available results to track progress against budgeted annual targets, and the contribution of sustainability factors in driving growth and mitigating risks.

PRACTICAL EXAMPLE

To allocate our financial resources, our annual planning and budgeting cycle is prepared using a ‘top down and bottom up’ approach. Our five year plan commitments are converted through our Outcome Delivery Incentive (“ODI”) framework into annual performance targets for internal planning and driving delivery. Each function then prepares detailed budgets and delivery plans based on their targets. An ODI Board, made up of executive and senior managers, then approves the ODI delivery strategies and the delivery tracking methods proposed.

See full case study for further information
4. Deliver detailed ‘top down and bottom up’ annual operational and financial plans

This diagram shows the different steps that can be followed in parallel in a ‘top down and bottom up’ approach. Sustainability considerations should be integrated throughout – some examples have been included within the diagram.

**DRIVING SUSTAINABLE OUTCOMES**

This two way process helps to bring together the different perspectives of those in the business:

- **Top down**: ensuring strategic objectives from management are filtered down into the organization’s operations
- **Bottom up**: incorporating behavioural factors and innovation that can only be identified by those in operational roles

When combined, these perspectives should give the organization a much clearer view on what activities are viable within each sustainability initiative, and the likely cost of these activities.

**Top down**

1. Agree integrated strategy and associated aims, projects and initiatives
2. Determine corporate level budgeting mechanisms to achieve these e.g. capitals budgeting, shadow pricing, ring fencing
3. Analyse business segments based on relevant factors such as size, operations, past performance, growth potential, geography, exposure, opportunities etc., depending on agreed aims, mechanisms and initiatives
4. Prepare budgeting guidelines based on initiatives, mechanisms and analysis
5. Prepare provisional top down budget allocations

**Bottom up**

1. Review budgeting guidelines and agree budget owner(s), paying special attention to how to incorporate sustainability considerations
2. Assess relevance of strategic projects and initiatives to business segment, and determine where sustainability factors will have the biggest impact
3. Identify opportunities and potential innovations at business segment level, e.g. carbon reductions, renewable energy, wellbeing programmes
4. Hold functional and segment level finance meetings to ‘test’ whether sustainability is sufficiently incorporated, and agree on innovation and budget considerations
5. Prepare and submit business case support for innovative responses and provisional budget requirements

**Aggregation and agreement**

- Compare and analyse top down and bottom up outputs, and assess against desirable outcomes as per the strategy
- Convene cross functional panel, including relevant sustainability specialists for innovative submissions
- Perform cross business segment validation
- Final sign off process
The forecasting process also needs to incorporate sustainability, ensuring relevant factors within the current and future environment are taken into consideration.

**PROCESS: FORECASTING**

The forecasting process also needs to incorporate sustainability, ensuring relevant factors within the current and future environment are taken into consideration.

<table>
<thead>
<tr>
<th>STRATEGIC PLANNING</th>
<th>BUDGETING</th>
<th>FORECASTING</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Assess the organization’s mission, vision, strategic context and environment</td>
<td>1. Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors</td>
<td>1. Assess performance</td>
</tr>
<tr>
<td>2. Set strategic goals, incorporating sustainability considerations</td>
<td>2. Convert the strategic plan and high level initiatives into annual activities and milestones, allocating accountable owners</td>
<td>2. Provide a realistic outlook based on the current business environment</td>
</tr>
<tr>
<td>3. Determine critical success factors, barriers, risks and enablers for achievement of goals</td>
<td>3. Set and agree performance commitments and budgets for each business unit and function</td>
<td>3. Provide the latest view of expected underlying performance</td>
</tr>
<tr>
<td>4. Define and agree high level activities and initiatives</td>
<td>4. Deliver detailed ‘top down and bottom up’ annual operational and financial plans</td>
<td>4. Allow timely management decisions and corrective actions</td>
</tr>
</tbody>
</table>
1. Assess performance

ACTIVITIES/INITIATIVES TO SUPPORT INTEGRATION

- Produce and review reports (e.g., month to date, year to date, etc.) containing information on the organization’s actual performance against monetary and non-monetary budgets and targets set for the previous period.
- Assess the key performance measures set previously and evaluate the level of performance attributed to sustainability considerations. Calculate variances in actual performance relative to the previous budget and/or the latest forecast.
- Determine the reasons for any significant variances from budget and identify the implications for the new forecast. If required, engage with sustainability specialists and business unit team members to understand significant variances relating to sustainability factors.
- Consider the value of performing long-term forward projection to facilitate analysis of where sustainability factors could have implications for future delivery.

PRACTICAL EXAMPLE

Reducing operational emissions (from pumping and treating water and wastewater) is essential to Yorkshire Water, as a lower carbon footprint goes hand in hand with efficiency, innovation, and cost reduction. Integrating carbon forecasting into operational and financial forecasts has allowed us to support major investments in renewables and energy efficiency, ensure regulatory and legal compliance, and enhance colleague engagement and our external brand.

See full case study for further information.
1. Assess performance

Understanding the performance to date and the reasons for fluctuations from budget is vital for effective monitoring of the business. When success is measurable in terms of both monetary and non-monetary factors, then interactions between different measures need to be considered and understood. The diagram below presents some factors to consider when assessing performance against budget in preparation for reforecasting.

- Analyse monetary and non-monetary indicators alongside each other
- Performance against budgets is monitored as part of integrated management reporting
- Investigate significant unexplained variances
- Evaluate level of success attributable to sustainability initiatives
- Consider implications for the new forecast
- Sense check anticipated interactions between monetary and non-monetary budgets and assess performance accordingly
- Consider progress of initiatives versus business plan and determine impact on performance versus budget
- Consider impact of unplanned internal and external factors
PROCESS: FORECASTING

2. Provide a realistic outlook based on the current business environment

ACTIVITIES/INITIATIVES TO SUPPORT INTEGRATION

- Use external research reports and analysis to understand potential market issues that will affect the organization’s value drivers over the forecast period, utilizing statistical techniques, spreadsheet tools, and professional judgment to determine the expected impact. For example, look at the latest scientific information on the future impact of climate change and consider how this will affect operations, supply chain, natural capital and markets.

- Use scenario and sensitivity analyses to assess the variability in business performance given hypothetical changes in material external issues, determining how a hypothetical ‘best case’ scenario and ‘worst case’ scenario would impact future business performance and develop risk mitigation plans accordingly.

PRACTICAL EXAMPLE

In integrating carbon forecasting into operational and financial forecasts, Yorkshire Water has followed a four step process. To provide a realistic outlook, previous years’ data is used to determine the underlying performance, then a forecast is prepared taking into account known changes that are projected to occur and updates to emissions factors that are determined nationally.

See full case study for further information
2. Provide a realistic outlook based on the current business environment

In developing a realistic outlook:

- understand the internal and external variables that have had an impact on the organization’s value drivers; and
- determine how the value creation model contributes to the development of a meaningful view of the organization’s expected performance.

The following diagram shows how an organization’s value drivers can be analysed and considered in developing a view of forecasted performance.
3. Provide the latest view of expected underlying performance

**ACTIVITIES/INITIATIVES TO SUPPORT INTEGRATION**

- Where possible, adapt the forecasting process to include rolling forecasts for all sustainability factors that underpin the organization’s goals and targets.
- Incorporate incremental revenues, costs and capital expenditures from budgeted projects (including sustainability initiatives) into the forecast.
- Provide the latest view of the expected underlying performance, including performance on sustainability outcomes, based on the outlook and the targets set during the budgeting process.

**PRACTICAL EXAMPLE**

City, University of London, is working to improve the organization’s energy efficiency and use of resources by integrating sustainability into strategy and operational procedures. We developed a carbon management plan which prioritized the different initiatives to reduce emissions cost effectively. We then prepared a forecast which incorporated the predicted implementation cost of the key schemes and savings, both financially and in terms of tonnes of carbon, based on the budgeted capital expenditure.

*See full case study for further information*

**THE FOLLOWING STEPS CAN BE APPLIED TO BOTH MONETARY AND NON MONETARY BUDGETS**

- Update understanding of external context and operating environment
- Revisit strategic objectives and ambition, and reconfirm/revise* as necessary
- Review progress against current period targets
- Consider impact of current performance on long term targets
- Consider if additional investment, behavioural change programme and/or additional enablers required
- Cross correlate these factors with operational forecasts to develop financial and non monetary forecasts

*Strategic objectives would ordinarily only be revised at this stage in exceptional circumstances*
PROCESS: FORECASTING

4. Allow timely management decisions and corrective actions

ACTIVITIES/INITIATIVES TO SUPPORT INTEGRATION

- Communicate the financial and operational results, highlighting elements related to sustainability factors that underpin the organization’s long term strategic goals, and seek cross functional communication and validation.
- Allow management to make timely decisions and interventions to the planned actions of any sustainability initiatives in the same way as for all other objectives, based on a comprehensive view of current conditions, short term performance and target gaps/lags.
- Revisit the budget on an iterative basis, where necessary.

PRACTICAL EXAMPLE

A significant sustainability initiative of Siemens is our Environmental Portfolio within which products, systems, solutions and services must meet specific environmental criteria. The Environmental Portfolio, representing almost 50 per cent of 2016 revenue, is anchored in the company’s strategic planning, budgeting and forecasting process. Prior to inclusion in the Environmental Portfolio, potential new elements have to undergo a multilevel evaluation and validation process. The process is monitored by two key KPIs: revenue and customers’ CO2 emissions reductions. These KPIs allow management to make timely decisions and interventions on the progress of the initiative.

See full case study for further information
## PROCESS: PRACTICAL EXAMPLES

### STRATEGIC PLANNING
- **Yorkshire Water**: Identifying long term risks and opportunities
- **Anglian Water**: Water resource scenario planning
- **Anglian Water**: Introducing sustainability factors into strategic planning, budgeting and forecasting
- **BHP**: Climate change scenario planning
- **The Crown Estate**: A strategic approach to success and future proofing our business
- **SSE**: Assessing total impact to benefit strategic planning decisions

### BUDGETING
- **Crossrail**: Developing a budgeting structure which puts long term benefits at the centre
- **Microsoft**: Implementing an organization wide carbon fee model
- **Asda**: Setting monetary budgets in line with strategic sustainability objectives
- **Bupa**: Ring fencing funding for low carbon and renewable energy projects
- **SSE**: Standardized and transparent community fund
- **SSE**: Local supplier portal
- **City, University of London**: Using a marginal abatement model to budget for emissions reduction options

### FORECASTING
- **Yorkshire Water**: Integrating carbon forecasting into operational and financial forecasts
- **City, University of London**: Forecasting carbon emissions savings
- **Siemens**: Anchoring our Environmental Portfolio into strategic planning, budgeting and forecasting processes
- **Sainsbury’s**: Delivering financial and sustainability benefits hand in hand
- **Danone**: Combining financial and carbon savings
- **Coca-Cola Hellenic**: Introducing science backed carbon reduction targets and water usage efficiency
- **Royal DSM**: Setting a shadow carbon price
- **South West Water**: Integrating sustainability throughout strategic planning, budgeting and forecasting processes
- **Danone**: Moving away from a traditional annual budgeting cycle
- **SSE**: Assessing total impact to benefit strategic planning decisions
- **City, University of London**: Forecasting carbon emissions savings
- **Siemens**: Anchoring our Environmental Portfolio into strategic planning, budgeting and forecasting processes
Yorkshire Water: Identifying long term risks and opportunities

WHY DID YOU UNDERTAKE THIS EXERCISE?

We wanted to understand fully the risks and opportunities the business was likely to face over the next 25 years, the necessary strategic responses and how they aligned to our vision and six Strategic Business Objectives. The approach taken can be illustrated through the three step process.

Step 1: What approach did you take in identifying key risks and opportunities?

We formed an internal cross business steering group (sponsored at Board level) to determine the key sustainability risks and opportunities using the PESTEL framework.

PESTEL in practice – identifying long term risks and opportunities

<table>
<thead>
<tr>
<th>Why did you use PESTEL?</th>
<th>It is a useful structure to explore fully our ‘risk universe’ over varying timescales. It ensures the Executive Team have visibility of risks from different perspectives and stakeholder views, and hence covers a whole range of issues and risk origins.</th>
</tr>
</thead>
<tbody>
<tr>
<td>What were the challenges with using PESTEL as the approach?</td>
<td>Those involved have to be prepared to put in the time and effort to go through the structure in a disciplined manner. Often, debate covers more than one PESTEL area at the same time – it is not always easy to allocate risks to just one area so this can sometimes disrupt the flow of the workshop and make note taking difficult!</td>
</tr>
<tr>
<td>What were the benefits of using PESTEL?</td>
<td>The structured approach ensures all areas are covered, generates debate, allows the process to move on naturally through each area, and provides a starter for open discussion. It is an easy format to use in a workshop style with an Executive Team, quick, straightforward and generates information to explore in more detail.</td>
</tr>
<tr>
<td>What was the outcome of the exercise and what is next?</td>
<td>We produced a view of all the risks and opportunities likely to impact our strategic business objectives over longer time horizons including those from external sources (rather than internally driven). This then allowed us to explore likely scenarios and develop appropriate annual and five yearly goals. The output is a sustainability plan to respond to these risks and opportunities (all logged within our risk register) which is wholly integrated into our corporate strategy.</td>
</tr>
</tbody>
</table>

Assess the organization’s mission, vision, strategic context and environment.
PROCESSES: STRATEGIC PLANNING
PRACTICAL EXAMPLES

Yorkshire Water: Identifying long term risks and opportunities

WHY DID YOU CHOOSE A 25 YEAR TIMESCALE?

A 25 year timescale was chosen because it allows the short term business planning to be set in the context of a long term direction (not constrained by, for example, the current regulatory framework or customer base). We wanted to understand, for example, what our customers might expect from us in 10 years’ time, what skills there might be in the talent pool in Yorkshire, and how raw material costs might affect our business in the future.

Step 2: How did you further understand how these risks and opportunities are likely to impact your business?

We aligned the risks and opportunities to our strategic risk register and considered appropriate mitigation. The approach identified that further information was needed regarding the uncertainty associated with some of the risks and opportunities that the business would face over the next 25 years. We worked with external sustainability experts to develop evidence based forecasts of what the world (specifically Yorkshire and the UK) could look like in 25 years and the key stages of change between then and now.

Risks and opportunities that are more shorter term and known are included within our risk register and are assessed, both qualitatively and quantitatively, within a scoring matrix. This establishes whether the risk or opportunity is material (against risk appetite determined by our Executive Team) and the level of control. Our Internal Audit function provides assurance over the effectiveness of the controls.

Step 3: How did this approach inform your business decisions?

Forecasting key risks and opportunities provided an insight to the changing nature of the water sector over the next 25 years. On the back of this work, objectives and targets that are aligned with our business plans, and scorecards were set for milestone years towards longer term outcomes to 2040.

Our objectives and targets are a mix of short to medium term through to the aspirational, where the way in which they will be achieved is yet unknown. An example of an aspirational objective is our ambition for ‘global safe water’ which has led to a partnership with WaterAid in Ethiopia.
Yorkshire Water: Identifying long term risks and opportunities

WHAT CHALLENGES DID YOU FACE?

The key challenge was to ensure that the sustainability strategy didn’t exist as a separate piece of work but was integrated into the company strategy. This required Board level buy-in to the concept, the work, objectives and targets that the company was signing up to, especially where these were outside of our regulatory contract.

WHAT IS NEXT FOR YOUR ORGANIZATION?

We periodically update our long term analysis to ensure our evolving strategy is always based on latest available evidence. In our latest assessment we found the same trends shaping our business, but with some critical changes to the expected rate of change, for example with even quicker developments in technology than previously forecast.

Ensuring the long term focus remains embedded at the heart of our strategy and business model is an ongoing process. As a part of mitigating long term risk, we manage a programme of activity to help us prepare for the identified opportunities and threats. We discuss regularly with our Board and Executive Team our strategy and progress against this programme of mitigation activity, and we openly report on our strategy, business model and risk management through our integrated Annual Report and Financial Statements.
WHY DID YOU UNDERTAKE THIS PROJECT?

We provide water and recycled water services to approximately six million people in the East of England. Over the next 25 years, our ability to maintain the balance between supply and demand will be challenged by macro sustainability trends such as population growth, climate change, growing environmental need and deteriorating raw water quality.

To maintain current levels of service we need to develop new reliable, affordable and sustainable systems of supply as well as reduce demand. To select the schemes that deliver this, we need to make trade-offs between various factors including social and environmental costs and environmental performance. Most of the risks arise from uncertainty about timing and the magnitude of the impacts from growth and climate change.

We want to understand the supply and demand scenarios that are considered most appropriate and cost effective for water resource planning. We also want to understand the trade-offs between customers' willingness to pay and reduced levels of service, and whether we should consider other criteria than cost effectiveness. This helps us to define our strategic goals.

WHAT APPROACH DID YOU TAKE IN IDENTIFYING SCENARIOS FOR WATER RESOURCE PLANNING?

The WRE is evaluating new scenario based approaches to long term water resource planning which is based on application of Robust Decision Making (RDM) and multicriteria Strategy Optimization.

Strategy Optimization uses an automated search algorithm to test different strategies against multiple performance criteria and finds those plans that perform best across all modelled future scenarios, and in respect of all performance criteria. In an RDM analysis, the performance of a small number of different options or strategies is tested using a wide variety of plausible future scenarios. The uncertainties which make the plan vulnerable are identified. Using statistical cluster analysis, the options or strategies are updated and then tested again.

WHAT CHALLENGES DID YOU FACE?

While RDM allows for rigorous testing of a small number of strategies or plans and can be used to explore the order in which the selected schemes are delivered, it does not suggest which combination of schemes should be included in the plans in the first place. We therefore used Strategy Optimization followed by RDM.
Anglian Water: Water resource scenario planning

WHAT WERE THE BENEFITS OF THE APPROACHES USED?

By using 1) Strategy Optimization followed by 2) RDM it is possible to identify optimized, balanced and robust water plans. By presenting optimized plans as performance measure trade off curves (step 1: Strategy Optimization), stakeholders and decision makers can debate and select an appropriate balance of system performance criteria. Trade off curves allow the identification of which portfolios of new supply and demand management schemes can reach the set objectives. Once one or a few preferred plans are chosen, they can be further refined through iterative testing with a wider selection of future scenarios leading to flexible and adaptive plans (step 2: RDM). This stakeholder led approach allows for more effective, robust and transparent decision making and is an improvement on the current least cost planning methods.

HOW DID THE APPROACHES INFORM YOUR BUSINESS ACTIVITIES?

Over 300 scenarios were developed. In each scenario, the performance of each option or strategy was tracked using a number of different measures, including total capital and operating costs, and environmental performance. To explore the robustness of a strategy based on combinations of all different options planned for Asset Management Programme 6 (2015-20), a vulnerability analysis was performed. This involved finding future conditions in which the strategy performs relatively poorly. The analysis identified two such scenarios that accounted for 96% of the simulated futures in which the strategy was vulnerable to failure. Iterative amendments can then be made to improve performance, allowing a more robust strategy to be developed.

WHAT WILL SUCCESS LOOK LIKE?

The plans will allow us to perform robustly in most plausible future scenarios. Success for the WRE is a flexible and adaptive plan for delivering a reliable, affordable and sustainable system of supply, which also needs to be resilient to the effects of population growth and climate change.

WHAT HAS HAPPENED SINCE THE PROJECT?

The project has been extended into Asset Management Plan 6 and used to inform our next Water Resources Management Plan and Business Plan. The project has also been enlarged to the WRE involving more water companies, and more water users, in the East.
Anglian Water: Introducing sustainability factors into strategic planning, budgeting and forecasting

**WHAT**
- Leveraged our integrated 25 year strategic plan to set six strategic business priorities which reflect our overall commercial aims and associated sustainability ambitions. These six priorities form the key sections of our strategic plan based on our Strategic Direction Statement, Water Resources Management Plan and the Risk Registers used in day to day operations.
- Concluded on ten outcomes that clearly included particular sustainability considerations, all of which were agreed with customers.
- Aligned our business goals and cultural values to these outcomes, resulting in greater customer brand engagement and more effective delivery.
- Developed appropriate metrics to allow us to monitor whether the desired outcomes were being achieved, which were then incorporated into our budget and forecasting processes.
- Focused on delivering outcome measures that reflect our broader performance and help us meet customer and regulatory expectations.

**WHY**
- Has resulted in improved customer outcomes whilst retaining focus on efficiency and cost savings.
- An integrated plan allows us to monitor our performance in a more holistic way, highlighting areas where action is needed, or equally where we can reduce investment yet still achieve the same financial and non financial outcome.
- Increased business resilience as we can better respond to threats, such as water stress from climate change, by targeting outcomes that drive the right benefits for the business, its customers and shareholders.
Anglian Water: Introducing sustainability factors into strategic planning, budgeting and forecasting

HOW
- As sustainability factors are part of our strategic plan, the focus on outcome based measures meant that social and environmental performance had to be reflected in our budgets, targets and forecasts.
- We modified each element of the plan, with budgeted costs linked to delivery of outcomes, and performed a risk review to identify areas where we could reprioritize investment to deliver improved performance across all outcomes.
- Our Strategic Priorities Board reviewed options and decided which to progress, where additional expenditure was required, and where funding would come from to keep the overall plan in balance.
- Having financial or reputational ‘rewards’ or ‘penalties’ for non financial metrics focused the attention of the business on non financial goals.
- Aspirational long term goals helped to change mindsets and deliver change quickly.
- The finance team collaborated with the wider business in the development process facilitating high level buy in from the whole organization.
BHP: Climate change scenario planning

**WHAT**

At BHP, our 20 year plan is prepared based on input from our businesses’ long term plans, and is then tested under both long term scenarios and ‘shock’ events. While we optimize the 20 year plan based on the central case, we use long term scenarios and shock events to test the resilience of the portfolio across a range of possible futures. Designed to interpret external factors, including technical, economic, political, environmental, social and governance trends facing the global resources industry, the scenarios offer a means by which to explore potential portfolio discontinuities and opportunities, as well as to test the robustness of decisions.

The difference between how we expect the portfolio to perform in the central case, and how we forecast it could perform in a scenario, helps us to understand the opportunities and risks and what we might do differently if the world were to move towards a particular scenario. Analysis undertaken in 2015 showed that the portfolio is resilient due to long term demand, high quality resources, low production costs and rapid payback periods of growth projects. Under a 2°C scenario, we believe there is a likelihood of upside for uranium, high quality metallurgical coal and iron ore.

Depending on the speed of transition and the energy choices made, we believe we will have opportunities to mitigate the impacts on the value of our portfolio through selectively investing in the commodities that will benefit from structural market changes.

See full Climate Change Portfolio Analysis Report 2015 for further information.
**BHP: Climate change scenario planning**

**WHY**

We believe the world is facing two critical challenges. As the global population steadily grows, the continued development of emerging economies depends on access to affordable energy. At the same time, limiting climate change requires the global average temperature increase to remain below 2°C relative to pre-industrial levels. Successfully addressing these challenges will result in substantial changes to the global economy. Companies in all sectors will have new market opportunities and face new competitors. All will need to find new ways of working.

The opportunities and risks associated with climate change cannot be expected to be spread evenly between businesses. More disclosure will inform investors, policy makers and regulators and support the companies that manage change most effectively. With the publishing of this scenario analysis, we are providing more information than ever before about how we are addressing climate change, and how climate risk might affect the portfolio.

**HOW**

Our approach to scenario planning starts with our annual corporate planning process and the construction of a ‘central case’, a forecast built through an in-depth, bottom-up analysis using rigorous processes and benchmarked with external views. The current central case assumes: the US economy continues to recover and strengthen; progressive development of China and India; integration of emerging economies into a multi-polar economic environment; and action on climate change centred on national policies. In the central case, our estimates show the world heading towards 3°C warming relative to pre-industrial levels.

The four scenarios used, shown overleaf, do not constitute preferred outcomes for BHP, but represent a range of possible long term future states. While these are possible futures, there are inherent limitations with scenario planning and it is difficult to predict which, if any, of the scenarios might eventuate. They are designed to be divergent, but also plausible, spanning unique potential future business environments. The scenarios use a consistent set of assumptions which are applied across the range of commodities. Every scenario includes an assumption that climate change occurs, what varies between them is the extent of the global response.
PROCESS: STRATEGIC PLANNING
PRACTICAL EXAMPLES

BHP: Climate change scenario planning

Tracking of signposts (trends) and triggers (events) across scenarios is integral to the planning process. These signposts and triggers provide an indication of which scenarios are becoming more or less dominant through time, offering us a powerful decision making tool that would enable us to act early. For example, a potential trigger event would be a breakthrough in low cost carbon capture and storage (CCS) for power generation.

While we test the resilience of the BHP portfolio across all four scenarios, we have a specific focus on providing further insight into the impacts of a transition to a 2°C world. The analysis includes a price on carbon, which represents the marginal inducement cost of the emissions reductions required to meet government targets. In the central case, we have a long term carbon price forecast of US$24/tCO₂ by 2030. In Global Accord, we expect the global average carbon price to reach US$50/tCO₂ by 2030. This reflects key global economies such as China, the United States and the European Union going beyond their current climate commitments and significantly increasing demand for long term emissions reductions. The higher ambitions are matched by stronger policy support to help deliver emissions reduction potential.

Along with scenario analysis, we test the portfolio against shock events. These are unlikely and extreme events, which are typically short term, but may have associated longer term impacts. We developed a shock event based on Global Accord that describes a much more rapid shift to a 2°C world where emissions align with the levels indicated by the IPCC by 2030, driven by very aggressive policy measures and technology developments. In this scenario, the carbon price rises up to US$80/tCO₂ by 2030, driven by very ambitious government targets.
The Crown Estate: A strategic approach to success and future proofing our business

Everything we do is informed by our purpose: creating brilliant places through conscious commercialism. To help us achieve our purpose we consider the material issues which are central to our business, we address them through our business model which, in turn, informs our corporate strategy.

We measure our progress against our KPIs, which is delivered through a well organized business underpinned by strong governance and leadership.

Consider critical success factors, barriers, risks and enablers for achievement of goals.

<table>
<thead>
<tr>
<th>PURPOSE</th>
<th>CRITICAL SUCCESS FACTORS</th>
<th>MATERIAL ISSUES</th>
</tr>
</thead>
<tbody>
<tr>
<td>Our purpose informs everything we do at The Crown Estate...</td>
<td>and we’ll reach it by following our four part corporate strategy which is focused on four objectives...</td>
<td>which is informed by the material issues that affect us...</td>
</tr>
<tr>
<td>Our purpose, creating brilliant places through conscious commercialism, sits at the heart of everything we do. It is what drives us to take a long term view, to see the bigger picture, identify opportunities for growth, and create environments that are relevant, attractive and profitable.</td>
<td>1. Actively manage our assets to drive sustainable outperformance against our commercial targets 2. Nurture a high performance culture and reputation as a great place to work 3. Build ever stronger relationships through high levels of customer and partner satisfaction, loyalty and recommendation 4. Be a leading responsible and resilient business which thinks long term</td>
<td>• Reputation and trust  • Government policy, constitutional change and political uncertainty  • Strategic counterparty alignment  • Impact of technology on the business  • Availability of skills and talent  • Health of the economy  • London’s place in the world  • Customer aspirations  • Climate change  • Natural resources</td>
</tr>
</tbody>
</table>

We have implemented four enablers in response to each of these issues – four ways to create conditions that empower our people to embed sustainability within the business to help us to:

• Actively manage our assets to drive sustainable outperformance against our commercial targets
• Nurture a high performance culture and reputation as a great place to work
• Be a leading responsible and resilient business which thinks long term

<table>
<thead>
<tr>
<th>ENABLERS</th>
<th>ENABLERS</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Recruiting for talent, but also seeking to develop our employees through learning and development plans 2. Offering competitive reward packages aligned to performance 3. Focusing on succession planning, inclusion and diversity and coaching 4. Facilitating the wellbeing of our staff through initiatives such as health and wellbeing information events, access to health screenings, health insurance</td>
<td>1. Actively pursuing mitigation measures across our portfolio 2. Developing science based targets 3. Developing climate change adaption plans across the portfolio 4. Helping to achieve a low carbon economy through work on derisking the offshore wind consenting process and attracting inward investment</td>
</tr>
</tbody>
</table>
Scottish and Southern Electricity Networks (SSEN), part of SSE Plc’s electricity networks business, is making sure we account for social, environmental and economic factors when planning future capex projects.

Between 2015 and 2023 SSEN plans to replace approximately 100km (22%) of its network of submarine electricity cables. Based on current projections this could cost up to £300m or six times the expected budget as a result of changes in the National Marine planning process. This cost will ultimately be paid for by electricity customers in the north of Scotland and thus their views on the process were fundamental as this would substantially effect the strategic planning and forecasting of how and when the works are carried out. The current model for quantifying the benefits and costs is the next evolution of the impact assessment process that SHE Transmission developed to support its capital expenditure programme.

The table opposite shows the key impacts that are quantified in the submarine electricity cables cost benefit analysis methodology.

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**Table 1: Key impacts quantified in the submarine electricity cables cost benefit analysis methodology**

<table>
<thead>
<tr>
<th>Category</th>
<th>Key Impact</th>
<th>Details of Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Health and safety impacts</td>
<td>Benefit</td>
<td>Decreased health and safety risk to marine vessel operators from cable snaggings</td>
</tr>
<tr>
<td></td>
<td>Net benefit/cost</td>
<td>Change in health and safety risk to cable laying vessel operators</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Note: this is based on trade-offs between (i) lower fault rates leading to less time at sea; and (ii) longer installation, repair, and decommissioning time requiring longer time at sea.</td>
</tr>
<tr>
<td>Social-economic impacts</td>
<td>Benefit</td>
<td>Decreased damage costs to marine vessel operators from cable snaggings</td>
</tr>
<tr>
<td></td>
<td>Benefit</td>
<td>Decreased risk of energy outages for island communities due to lower fault rates</td>
</tr>
<tr>
<td></td>
<td>Cost</td>
<td>Increased distribution costs leading to lower renewable generation on islands and lower Gross Value Added (GVA)</td>
</tr>
<tr>
<td></td>
<td>Cost</td>
<td>Increased cost of fuel poverty eradication programme due to higher fuel bills</td>
</tr>
<tr>
<td></td>
<td>Cost</td>
<td>Increased cost to fishing operators due to loss of access to fishing grounds during cable installation</td>
</tr>
<tr>
<td>Environmental impacts</td>
<td>Benefit</td>
<td>Decreased risk of energy outages for renewable generation due to lower fault rates</td>
</tr>
<tr>
<td>Wider economic and</td>
<td>Cost</td>
<td>Increased distribution costs leading to lower renewable generation on islands and higher greenhouse gas emissions</td>
</tr>
<tr>
<td>Engineering</td>
<td>Net benefit/cost</td>
<td>Changes in greenhouse gas emissions from use of backup diesel generators. Note: this is based on trade-off between (i) lower fault rates resulting in a reduction in diesel usage, and (ii) longer repair time resulting in an increase in diesel usage.</td>
</tr>
<tr>
<td></td>
<td>Cost</td>
<td>Increased installation costs associated with protection</td>
</tr>
<tr>
<td></td>
<td>Net benefit/cost</td>
<td>Impacts due to change in repair costs. Note: this is based on trade-off between (i) lower fault rates resulting in fewer repairs; and (ii) longer repair time because cables are protected.</td>
</tr>
<tr>
<td></td>
<td>Cost</td>
<td>Increased cost of decommissioning associated with protection</td>
</tr>
<tr>
<td></td>
<td>Benefit</td>
<td>Decreased risk of outage changes due to lower fault rates</td>
</tr>
<tr>
<td></td>
<td>NEW</td>
<td>Increased cost of maintenance surveys associated with protection</td>
</tr>
<tr>
<td></td>
<td>Cost</td>
<td>Increased cost of maintenance surveys associated with protection</td>
</tr>
<tr>
<td></td>
<td>Net benefit/cost</td>
<td>Change in use costs of using backup diesel generators. Note: this is based on trade-off between (i) lower fault rates resulting in a reduction in diesel usage, and (ii) longer repair time resulting in an increase in diesel usage.</td>
</tr>
</tbody>
</table>

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Link to the initial project which led to the development of this methodology, the Beauly-Denny transmission project which was driven by the finance team.
PROCESS: STRATEGIC PLANNING
PRACTICAL EXAMPLES

SSE: Assessing total impact to benefit strategic planning decisions

THE TOTAL IMPACT ANALYSIS

In a project overseen by our Finance Director, SSE wanted to understand better the impacts that capital investment projects have on society and to measure them using a consistent metric. In looking at the Beauly-Denny transmission line this assessment focused on a number of sustainability impacts that were assessed to be most material to the project, including:

- Total economic footprint of the construction expenditure
- Cultural heritage
- Traffic management
- Carbon footprint
- Building waste
- Visual amenity

With support from sustainability consultants, SHE Transmission developed a Sustainable Commercial Model (SCM) framework, bringing together over a dozen methodologies, to quantify and monetize the above environmental, social and economic impacts i.e., the total impact of the Beauly-Denny transmission line. The impact can be identified, measured and financially quantified in a globally recognized currency: ‘£’, where previously expected impacts were assessed using qualitative data. Using this consistent monetary value enables all stakeholders of transmission projects, and the wider community, to review the impacts and value created in a transparent and accountable format against an established baseline value. In particular it provides visibility around the relative positive and negative impacts of different options and decisions, helping us to maximize the total value created.

FINANCE FUNCTION LEADERSHIP

The finance function was instrumental in the development of the SCM. SSE’s Finance Director chaired the working groups and set the direction, while the Group Sustainability Accountant provided the knowledge and coordinated activities. We found that the critical success factors are to have the knowledge, the right culture and an engaged, supportive finance team.

The finance function:

1. Embedded a significant level of rigour into the analysis, with an audit trail of information, which provides evidence that a robust process was followed. This ensured that key decisions and assumptions were documented and substantiated, creating transparency of results for both internal and external parties.
2. Facilitated the linkage of finance with the wider sustainability community, both internally and externally. This led to greater collaboration.
3. Illustrated to senior management, both within the finance function and in other areas, that a financially sound project can also have the best sustainability outcomes. The Finance Director of the transmission division of the business is now an advocate for the commercial potential for using this approach on new line developments.
PROCESS: BUDGETING PRACTICAL EXAMPLES

Crossrail: Developing a budgeting structure which puts long term benefits at the centre

WHAT

Crossrail Limited is the company that has been set up to build the new railway that will become known as the Elizabeth Line when it opens through central London in 2018. The budgeting guidelines are designed to minimize the whole of life costs of the project (rather than just the construction cost), and to incorporate a whole range of sustainability initiatives into the project to deliver both short and long term benefits. A total funding package of £14.8 billion is available for the project, with anticipated benefits including those shown in the infographic.

ECONOMIC

- 96% of the contracts awarded by Crossrail will be awarded to companies within the UK
- £42bn estimated to be generated for the UK economy
- 55,000 jobs will be supported by Crossrail across the UK
- 62% of suppliers based outside of London

ENVIRONMENT

- 7.9 million tonnes of waste avoided during construction
- 98% of excavated material beneficially reused
- 11% CO₂ saving during construction against baseline estimates
- 84% construction machinery in central section fitted with emissions controls, reducing air pollutants
- Items operating 15 million miles annually across 20 sites

SOCIAL

- 4,544 jobs created by local or previously unemployed people
- 9,794 drivers attended HGV driver training courses
- Over 15,000 people trained at T Level
- 1,109 young people undertook work experience
- 573 apprentices gained on the project

Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors.
Crossrail: Developing a budgeting structure which puts long term benefits at the centre

WHY

We are investing public money in a world class railway so we have a broad obligation to spend it in the right way. Sustainability for Crossrail is therefore built on the ethos of contributing to a strong, stable economy that will help provide prosperity and opportunities for all. As Europe’s largest infrastructure project, Crossrail presents an excellent opportunity to lead in delivering a sustainable railway, fit for the future. Sustainability has been at the heart of the project from day one, and decision makers for the project want it to have a long lasting impact on how people travel through the capital and South East, and leave a lasting learning legacy for future projects and the wider industry.

HOW

Finance teams have been at the heart of the whole project. Finance Leadership team representatives are linked into all of the governance functions, including a sustainability committee. The committee is chaired by the CEO and attended by all Executive and top level management and is focused on delivering environmental, social and economic benefits.

Budgeting and allocation of funds has been based on the net long term benefit, whole of life costs approach. The budgeting guidelines incorporated this ethos, for example:

• A supply chain budget was structured so that economic benefit focused on regions outside London and on SMEs. Over 1,700 businesses have secured work on Crossrail with 62% from outside London and 58% from SMEs.

• We decided to use titanium rails for the Elizabeth Line, which are more expensive in the short term than conventional rails, but require less maintenance as the trains that run on these rails are lighter. This increases the life of the rails, reduces the maintenance and replacement costs, as well as the energy required to run the railway. A traditional construction cost based budgeting approach would have ruled out titanium rails on the grounds of purchase cost.

• A £1m budget was ring fenced for a lorry driver training course that set new safety standards for the industry. This was in response to the increase in heavy goods vehicles from the project, and the fact that 50% of cyclist accidents in London are due to collisions with heavy goods vehicles.

This long term benefit approach has required extensive financial modelling, taking account of environmental and social considerations, led by the finance team. Consequently, the finance team has had a decisive influence over budget allocation, investment and change decisions. The finance teams have a role in ensuring money flows down the supply chain, in helping project management teams make smarter decisions, and in supporting function heads with both monetary and non monetary analysis.

“Demonstrating long term sustainability has been at the forefront of Crossrail priorities since the earliest days of the project. As a finance team, we have worked hard to demonstrate and monitor the wider benefits of the project both internally, and to the wider stakeholder audience. Reporting on costs alone is simply not a justifiable position for a project of this scale and importance.”

Matthew Duncan, Finance Director, Crossrail
Microsoft: Implementing an organization wide carbon fee model

WHAT
The carbon fee model that we implemented at Microsoft is a financial model that puts an incremental fee on the carbon emissions associated with our company’s operations. There are three primary components to our carbon fee model:
1. Organizational carbon reduction policy
2. Price on carbon
3. Carbon fee fund investment strategy

The price on carbon is determined by the total cost of the carbon fee fund investment strategy, which is set to meet the organizational carbon reduction policy objectives.

A carbon fee internalizes the external cost of carbon pollution into the financial structure of an organization. The associated fee is charged to those groups responsible for the resource consumption. There is no “grandfathering” (that is, a pre-specified level of “free” emissions) as you might get with a cap and trade scheme.

By doing so, the fee helps educate the business groups on carbon emissions and elevates efficiency and innovation within our business.

The three primary components of our carbon free model

By using a model in which groups are charged a fee based on their actual total usage (rather than putting a cap on usage or applying the fee to usage exceeding a pre-determined level), we keep the model simple to administer and make the cost of emissions overt.

The fees that we collect through the carbon fee model go into a central fund used to subsidize investments that enable Microsoft to reduce emissions and be net carbon neutral.
Microsoft: Implementing an organization wide carbon fee model

WHY

The three primary benefits supporting the decision to implement an internal carbon fee were the opportunity to drive efficiency, demonstrate responsibility and show leadership.

1. Efficiency
A carbon fee can help drive behaviour change to increase efficiency and reduce an organization’s costs and carbon footprint. Quantifying carbon provides a standard measure, or a “level playing field”, across otherwise disparate groups to drive operational excellence.

2. Responsibility
The carbon fee model drives responsible business decisions that help mitigate potential risks associated with an organization’s environmental footprint. For Microsoft, the fee helps us address risks related to the rising costs of energy.

3. Leadership
While we believe we have a responsibility to minimize our company’s impact on the environment, we also have an opportunity to contribute to the greater good. A carbon fee model helps provide leadership in mitigating climate change, and (with the subsequent investment of the carbon fee funds) demonstrates how environmental considerations can be integrated into financial frameworks to evolve how carbon markets function. The model can ultimately support the development of a low carbon economy, jobs, education, healthcare, and address other societal challenges.

Benefits of the carbon free model to drive culture change

- Reduced energy use and employee air travel
- Reduced carbon footprint
- Reduced costs
- Alignment with code of ethics
- Risk mitigation
- Regulatory compliance
- Innovation
- Citizenship projects

“...A carbon fee model is an excellent way to provide both the financial framework and the formal discipline to drive efficiency projects. By applying a financial cost to the carbon impact of operational practices, it provides justification to prioritize efficiency – and therefore cost reductions – across the organization.”

Lee Mills, Senior Finance Manager, Microsoft Corporation
Microsoft: Implementing an organization wide carbon fee model

Step 1: Calculate your carbon impact
- A foundational building block of a carbon emissions inventory is the development and ongoing maintenance of an inventory management plan (IMP), the purpose of which is to institutionalize a process for collecting, calculating, and maintaining carbon data.
- Technology plays a vital role in improving visibility into emission levels. Access to up to date data makes it easier to integrate environmental footprint management into the business. It also provides greater transparency to the executives and business leaders responsible for making business decisions.

Step 2: Establish a carbon reduction policy and develop an investment strategy
- The success of your model will depend on gaining the cooperation and buy in of key stakeholders. You will need to have the right people engaged to form a carbon reduction policy with visibility across the organization. At a minimum, the model will need the approval and participation of the finance officer of the organization.
- A carbon reduction policy outlines what commitment the organization is making to reduce carbon (such as pledging carbon neutrality). Carbon reduction targets help ensure that the design and administration of your carbon fee align with organizational goals.
- By defining your carbon fee emissions boundary in alignment with existing organizational boundaries or groups, you will help simplify administration of the fee and minimize resistance from internal audiences.
- Your carbon fee fund investment strategy will form the basis for your environmental initiatives portfolio. Your strategy will guide selection decisions by prioritizing criteria that will have an impact on the cost of your investments and therefore on your internal carbon price.

Step 3: Determine your internal carbon price
- In simple terms, you can calculate your carbon price by dividing the total cost of your environmental initiatives portfolio by the emissions within your carbon fee emissions boundary. Alternatively, you could base the price on existing or future traded values, or an estimate of the social cost of carbon.
- By allocating the carbon fee to the groups that consume the resources (and are therefore responsible for the emissions), you can help drive education, awareness, and accountability.
Step 4: Gain approval and establish governance and feedback loops

- The key to gaining the approval of leadership is to have the support of key stakeholders from the parts of the organization where the carbon fee will have the most impact.
- A cross-organizational committee chartered with governance across the organization can help ensure that you maximize impact over time.

Step 5: Administer the fee, communicate results, and evolve to increase impact

- When you allocate the fee, you will need to determine the appropriate cycle to charge the organizational divisions for the projected emissions. For maximum transparency, include the carbon fee charge as an extra line item on each group and include the projected amount in the budget targeting process.
- Having a monthly or quarterly status update to true up actual emissions and costs with the projections being used as the basis for the carbon fee charges provides an opportunity to make calibrations where necessary.
- By communicating your progress with the carbon fee and investments internally, you can make sure your stakeholders know that the money they are putting in is having an impact.
- Reporting on your emissions performance externally introduces additional scrutiny to keep you committed.
- You now have an opportunity to refine and evolve your approach for maximum value for your organization.
**PROCESS: BUDGETING PRACTICAL EXAMPLES**

**Asda: Setting monetary budgets in line with strategic sustainability objectives**

**Strategic business planning is aligned to core sustainability objectives**

**WHAT**

Continuous improvement programmes are integrated with sustainability targets to enable Asda to reduce its cost base, which can then be invested into lowering prices.

To achieve optimal benefit, financial plans are intrinsically linked sustainability objectives. This link runs through the strategic planning, budgeting and forecasting phases, which allows:

- A meaningful plan to be set with top level support
- Tangible, quantifiable and measurable budgets aligned to these plans
- Execution of the plans and tracking of benefit realisation
- Learnings embedded back into the next cycle of the process

**WHY**

The core purpose of Asda is to save the customer money everyday. Our approach to sustainability is based on the belief that protecting the environment, helping communities thrive and saving people money go hand in hand.

Asda is part of the Walmart family, the largest retailer in the world, and therefore has a corporate social responsibility to reduce our environmental impact. We have clear aims targeted around our operations, the goods and services we sell, and the suppliers that make them. These areas are:

- To be supplied by 100% renewable energy.
- To create zero waste.
- To sell products that sustain people and the environment.

Our success is about customer trust and with the level of transparency we now have across the retail world, the customer doesn’t just want low prices, great service and quality products, they also care about how foods are sourced, how we manage our waste and ultimately our contribution to the sustainability agenda.
PROCESS: BUDGETING PRACTICAL EXAMPLES

Asda: Setting monetary budgets in line with strategic sustainability objectives

Budgeting and forecasting processes embed these aligned objectives

**HOW**

**Strategic planning process**
- Long term financial modelling is aligned to Asda’s strategic targets, including sustainability targets.
- A key building block is LCOM (Lowest Cost Operating Model) which aims to encourage the business owners to work more effectively/efficiently.
- Vision and measurable targets communicated to the business.

**Budgeting process**
- LCOM projects are identified by business owners and financial and sustainability benefits agreed and measured with business partners.
- Business cases incorporate the financial and non-financial benefits and are assessed against payback targets and strategic objectives.
- Initiatives are approved through a clear governance process, sponsored and supported by senior management.
- These benefits are then embedded into cost line plans for each area, and broader functional objectives, ensuring clear accountability.

**Forecasting process**
- This is underpinned by governance process to ensure consistency and control.
- Monthly steering groups track and monitor performance.

Aligning sustainability and financial objectives ensures that the business considers the balance of short and long term value and delivers sustainable benefits.
## PROCESS: BUDGETING PRACTICAL EXAMPLES

### Asda: Setting monetary budgets in line with strategic sustainability objectives

#### Practical Example: Energy usage

<table>
<thead>
<tr>
<th>Strategic</th>
<th>Asda’s sustainability target is to reduce its energy usage by 20% in 10 years to 2020 to reduce our environmental footprint.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Industry forecasts indicated energy prices were set to rise, causing a significant longer term financial headwind.</td>
</tr>
<tr>
<td>Budgeting</td>
<td>With headwinds from increasing cost growth, the budgeting process identified efficiencies to offset through our LCOM programme.</td>
</tr>
<tr>
<td></td>
<td>Investigations revealed that over 75% of emissions are driven by electricity usage, with a significant proportion controllable internally.</td>
</tr>
<tr>
<td></td>
<td>Initiatives were identified within our stores and supply chain and commitments built into their budgets:</td>
</tr>
<tr>
<td></td>
<td>• <strong>Stores</strong>: targets to ensure store managers are responsibly managing usage.</td>
</tr>
<tr>
<td></td>
<td>• <strong>Maintenance</strong>: improve efficiency by reducing leakage from refrigeration.</td>
</tr>
<tr>
<td></td>
<td>• <strong>Capital projects</strong>: install LED lighting, solar panels and optimizing systems to control usage remotely across stores.</td>
</tr>
<tr>
<td>Forecasting</td>
<td>With targets embedded into plans, these projects are tracked to ensure that they delivered both financial benefits and sustainability objectives:</td>
</tr>
<tr>
<td></td>
<td>• <strong>Stores</strong>: energy usage in our existing stores have reduced by over 33% since 2005.</td>
</tr>
<tr>
<td></td>
<td>• <strong>Maintenance</strong>: reduced our leakage rate from 20% in 2007 to below 8% by 2015.</td>
</tr>
<tr>
<td></td>
<td>• <strong>Capital Projects</strong>: substantial investment to trial and develop renewable energy at optimal returns.</td>
</tr>
<tr>
<td></td>
<td>• Sustainability objectives are tracked alongside financial results.</td>
</tr>
<tr>
<td></td>
<td>• Resulting Energy P&amp;L impact reducing over the past five years despite inflation in energy prices.</td>
</tr>
<tr>
<td></td>
<td>• Improving the business economics has allowed further investment into price and other areas of the business.</td>
</tr>
</tbody>
</table>

“*If we buy more sustainably, operate more sustainably, sell more sustainably – we can grow our business more sustainably. Integrated planning, budgeting and forecasting drives optimal opportunity.*”

Jessica Leng, Senior Director, Property Finance

“We’ve already made great strides in terms of our own environmental performance that have directly helped us to lower our operating costs and, in turn, provide lower prices for our customers.”

Chris Brown, Senior Director, Sustainability
PROCESS: BUDGETING PRACTICAL EXAMPLES

Bupa: Ring fencing funding for low carbon and renewable energy projects

In 2010 Bupa committed to reducing carbon emissions by 20% by 2015 on a 2009 baseline, making this the company’s only externally published target. Progress was initially slow, so recognizing this, we held a companywide workshop in November 2013 to discuss energy saving options. It was here that the CEO at the time helped turn the concept of a central funding mechanism for direct, on site carbon reduction projects into a reality, leading to the announcement of the Bupa Energy Saver Fund (ESF) the following month. To meet our goal and to accelerate projects that could reduce energy use, we established the Energy Saver Fund to invest £50m in low carbon and renewable energy projects in 2014 and 2015 across many of our properties globally.

The ESF was identified internally by the finance and sustainability community and the structure was established centrally. To apply for funding, the business unit Finance Directors and Property/Sustainability Leads had to submit a briefing note to the CFO, Financial Controller and Director of Sustainability covering the following:

**ESF FUNDING ASSESSMENT CRITERIA**

- Total amount requested from the ESF
- Overview of the expected energy and cost savings
- Description of the capability and capacity available to ensure efficient investment and successful implementation of projects

Funding requests were assessed centrally based on certain approval criteria, such as:

1. The investment opportunity has a high environmental impact and commercial return.
2. The investment programme is commercially viable; it will deliver at least a 5% IRR and has a five year financial payback overall.
3. Investment requests are subject to local review and investment appraisal as all other projects.
4. All submissions are approved by Central Finance and Central Sustainability.

The outcomes achieved include:

- Becoming the largest private operator of rooftop solar in Australia
- Using 99% renewable energy in Spain and 100% in London
- Building environmental management systems in more than 320 office and care homes
- 23% reduction in carbon emissions
- Saving £5m a year on energy bills

These were achieved whilst tripling customers, growing revenue by 40% and increasing the workforce by 30,000 people.

“Long term growth can’t be separated from economic, social, health and environmental issues. As well as being the right thing to do for the planet and health, the Bupa Energy Saver Fund also makes business sense: we can cut costs and enhance efficiency, mitigate risk, open up new competitive and revenue opportunities, drive innovation and develop our employees. It really is a win all round.”

Evelyn Bourke, CEO, Bupa
PROCESS: BUDGETING PRACTICAL EXAMPLES

### SSE: Standardized and transparent community fund

**WHAT**

For over ten years we have established funds to enable communities to develop sustainably by funding charitable and community initiatives. Communities can access funds which we make available near each of our renewable energy developments.

In Great Britain, since 2002, we have supported over 1,000 community projects with grants totalling over £13 million. We set up local and regional community funds for each new onshore wind farm we build. For our local funds, panels made up of community members review applications and decide which projects to support, and we work closely with the panel and applicants to ensure opportunities are maximized for the benefit of the community.

In January 2012, we launched what we believe to be the most generous community investment fund package of any of the major developers operating in Scotland. To make sure everyone is treated equally, this package is offered, without exception, for every future onshore wind farm we are developing in Scotland.

**WHY**

SSE has been building and operating wind farms in Scotland since 2002. Combined with our hydroelectric schemes, many of which have been in operation for over 50 years, our wind farms make us the largest generator of renewable energy across Great Britain and Ireland.

When the majority of our hydroelectric stations were built in the middle of the last century, we never even considered the idea of setting aside funds for local groups to invest in projects that would benefit their communities. At the time, ‘community benefit’ was only considered in terms of the electrification of the Highlands and of the resulting prosperity the project brought to the area through the creation of jobs, local business opportunities and improvements to local roads and other infrastructure.

But times change, and today we recognize that the development of new renewable energy projects should also bring more direct financial benefits to the communities that host them. We believe that the local community is best placed to decide what they should invest their fund in. We want them to have control over how the money is spent because they know what is important to their communities – not us!

**HOW**

Every onshore wind farm is different, so the size of the fund will vary from site to site, but the basis of the calculation remains exactly the same, so an onshore wind farm that is twice as big as another will have exactly double the amount of community investment compared with the smaller onshore wind farm.

We measure the size of our onshore wind farms in terms of the ‘installed capacity’. This is the maximum theoretical output of the wind farm, measured in ‘megawatts’ (MW).

The value of the community investment funds we set aside for onshore wind farms in Scotland is currently £5,000 per MW every year for up to 25 years.

**An example of how we calculate the value of a community fund**

Taking a 50MW wind farm, the community investment fund would be calculated as shown below:

- Installed capacity = 50MW
- Community investment fund = £5,000 per MW
- Annual value of community investment fund (50 x £5,000) = £250,000
- 50% ring fenced for local community = £125,000 per annum
- 50% set aside for the regional community = £125,000 per annum
- Total lifetime value of the community investment fund (£250,000 x 25 years) = £6,250,000

Develop guidelines for opex and capex budgeting processes that include short and long term sustainability factors.
PROCESS: BUDGETING PRACTICAL EXAMPLES

SSE: Local supplier portal

Once a local sourcing budget has been set, the case study below demonstrates how local suppliers can be engaged.

WHAT
To contribute to the economic wellbeing of the Highlands and Islands community, SSE has developed the SSE Open4Business Highlands and Islands web portal. This site facilitates trade and engagement between SSE and local suppliers and service providers. It provides a platform for SSE to promote opportunities originating in the region, and allows local suppliers to have visibility of SSE opportunities, register as a supplier and respond to notices free of charge. Users of the site can then also advertise their own opportunities such as sub contracting work for SSE projects. They can also use the portal to advertise their own opportunities to the local supplier base.

The site connects to other networks and supply chain initiatives in the Highlands and Islands which SSE supports such as through Energy North, Highland Council’s Highland Opportunities, Highlands and Island Enterprise, Chamber of Commerce and Scottish Council for Development and Industry.

WHY
SSE has a long history of working in partnership with, and in, communities in the Highlands and Islands. We want to continue that tradition and be:

• the most ‘Open for Business’ company in the Highlands and Islands;
• best at engaging and collaborating with the local and SME communities in the Highlands and Islands;
• a valuable contributor to the Highlands and Islands economy and communities; and
• working in partnership with our public sector allies and our extended supply chain to maximize community benefits and local SME opportunities.

SSE recognizes that it has a significant role to play in contributing to the economic wellbeing and sustainable development of the communities it operates within. SSE is therefore committed to demonstrating exemplary levels of engagement with local suppliers. Quite simply, SSE wants to become the best in the Highlands and Islands at engaging with the local and SME communities and be the most ‘Open for Business’ company in the region.

HOW THE PORTAL WORKS
The SSE Open4Business Highlands and Islands web portal allows buyers to find qualifying suppliers for a shortlist prior to entering into their standard tendering process, which happens outside the portal. If you are a potential supplier, SSE Open4Business Highlands and Islands enables you to respond to an opportunity by answering a simple questionnaire created by the buyer and in some cases providing a Supplier Statement. Answers to the questionnaire are scored automatically by the SSE Open4Business Highlands and Islands portal using a scoring plan defined by the buyer.

After the response deadline for the opportunity, the buyer carries out a shortlisting process on SSE Open4Business Highlands and Islands using the automatically calculated scores and other information from each supplier's response. If you are successful in reaching the shortlist, the buyer will invite you to participate in their tendering process, which will usually involve submitting further details and documents outside SSE Open4Business Highlands and Islands.

THE BENEFITS
Facilitating economic development in the Highlands and Islands:

• Improved communications within the supplier / buyer communities
• Local and SME suppliers provided with visibility of business opportunities
• Registered local suppliers can be alerted when relevant local opportunities arise
• Leveraging the wider SSE supply chain to provide opportunities with SSE supply partners and with their supply chain partners
• Maximizing local opportunities
• Local businesses and SMEs can register for free – no charges to advertise or respond to opportunities
**City, University of London: Using a marginal abatement model to budget for emissions reduction options**

City, University of London, is systematically working to improve the organization’s energy efficiency and use of resources by integrating principles of sustainability into corporate strategies and operational procedures, and by raising the awareness of environmental issues amongst our staff, students and the wider community.

We were selected to take part in the Higher Education Carbon Management programme, which was designed to assist universities like City, University of London in saving money on energy and putting it to good use in other areas, whilst making a positive contribution to the environment by lowering their CO₂ emissions.

As part of this programme, we have developed a carbon management plan to reduce emissions systematically through energy efficiency, low carbon technologies (such as Combined Heat and Power and renewable energy systems), low energy buildings, more sustainable travel arrangements and improved management systems. These measures form part of a coherent strategy to reduce emissions over time, from an established baseline to an agreed target level.

Within the carbon management plan, we considered the marginal abatement costs of the key carbon reduction options available to us, and used these to inform our carbon and financial budgets. The table and graphs below show the marginal abatement costs (MAC) for the top ten emissions reduction projects. The costs for each project have been plotted against the CO₂ saving. The marginal abatement cost of each project or cost/tonne of CO₂ is shown by the position of each project above or below the zero cost line. This gives a clear view of which projects should be implemented at different abatement costs.

The analysis was a key informant for the carbon management plan, with most of the projects planned for feasibility studies, full evaluation or implementation over a five year period, alongside some behavioural initiatives and water saving measures. The analysis also led to a budget of £78,000 per annum being put in place for energy conservation projects. This is mainly to allow low cost/fast payback projects to proceed in the first instance.

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### Marginal abatement project cost

<table>
<thead>
<tr>
<th>Project name</th>
<th>Capital cost (£)</th>
<th>Annual benefit (£)</th>
<th>Annual average CO₂ savings for project (tonnes per year)</th>
<th>Project life (years)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cass energy audit improvements</td>
<td>20,000</td>
<td>85,000</td>
<td>200</td>
<td>15</td>
</tr>
<tr>
<td>Lighting controls</td>
<td>25,856</td>
<td>31,204</td>
<td>170</td>
<td>10</td>
</tr>
<tr>
<td>Business management systems (BMS)</td>
<td>100,000</td>
<td>66,682</td>
<td>419</td>
<td>12</td>
</tr>
<tr>
<td>Voltage reduction</td>
<td>60,000</td>
<td>59,102</td>
<td>374</td>
<td>25</td>
</tr>
<tr>
<td>College window draft proofing</td>
<td>46,565</td>
<td>11,166</td>
<td>55</td>
<td>15</td>
</tr>
<tr>
<td>Economisers</td>
<td>47,593</td>
<td>22,858</td>
<td>232</td>
<td>25</td>
</tr>
<tr>
<td>Barrier Controls</td>
<td>20,000</td>
<td>5,833</td>
<td>38</td>
<td>25</td>
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<tr>
<td>Heating, ventilation and air</td>
<td>1,016,813</td>
<td>121,706</td>
<td>447</td>
<td>25</td>
</tr>
<tr>
<td>conditioning (HVAC)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Main site cavity wall insulation</td>
<td>400,000</td>
<td>98,082</td>
<td>713</td>
<td>30</td>
</tr>
<tr>
<td>Combined cooling, heat and power</td>
<td>4,970,000</td>
<td>480,000</td>
<td>1,080</td>
<td>25</td>
</tr>
</tbody>
</table>

### Marginal abatement cost curve

- CCHP
- Main site Cavity Wall insulation
- Voltage Reduction
- HVAC Improvements
- Burner Controls
- BMS Upgrade
- Lighting Controls Upgrade
- Economisers
- College Window Draught Proofing
- Cass Energy Audit Proposals
- Reduction target
Anglian Water: Setting an embodied carbon budget for 2030

**WHAT**
As part of our “Love Every Drop” campaign, we set a “Drop CO₂” budget for 2030. The budget restricts embodied carbon in new assets, and is driving us to reduce embodied carbon levels by 70% on our 2010 baseline.

**WHY**
Our region is one of the driest in the UK, which means it is particularly vulnerable to the impacts of climate change.

We want to lead the way in raising awareness about the value of water and are campaigning to change fundamentally how we all engage with it and use this precious resource.

But each drop of water – abstracted, cleaned and pumped to homes before being cleaned again, and pumped back into the environment – comes with plenty of carbon dioxide attached, and because CO₂ is contributing to climate change, we’re stepping up our work to cut it out across the business, in every single way we can.

**HOW**
We challenged our design engineers and capital delivery partners across the supply chain to deliver more sustainable assets, reducing carbon and the use of finite raw materials and cost. The success of this approach means that in five years embodied carbon emissions have reduced by 54% against our 2010 baseline.

Governance over the carbon budget forms part of our overall financial and project governance process, ensuring there is an appropriate mechanism to facilitate delivery of both our financial and our carbon budgets and targets.

Through the period 2015–2020, we will have invested over £2 billion in maintaining and improving our infrastructure. This investment will result in a forecast 360 ktCO₂e of capital carbon in the materials we use to build and replace assets. With a continued focus on energy management, innovation in design and optimizing renewable generation assets, we have again set a challenging objective of mitigating against future potential increases in operational carbon emissions and reducing capital carbon in assets we design and build. The budget is now set at a level to reduce capital carbon emissions by 60% by 2020 from a 2010 baseline.

“Because I love water I want to wake the world up to the importance of the link between carbon and water to make a fundamental difference to climate change.”
Peter Simpson, Managing Director, Anglian Water
**PROCESS: BUDGETING PRACTICAL EXAMPLES**

**Sainsbury’s: Delivering financial and sustainability benefits hand in hand**

Sainsbury’s have ambitious goals in our 20x20 Sustainability Plan to accelerate progress towards our aim to become the UK’s greenest grocer. So, for us, stepping up our sustainability investments in retail stores makes strategic sense.

The Triple Zero challenge: We had demonstrated the technical feasibility of cutting carbon consumption by 30% by 2020 through a series of sustainable technology projects. Post investment review showed that these projects were achieving better than expected financial results and accelerated cash payback periods by one year. Bolstered by confidence in the financial business case, our executive leadership set our property team a genuine challenge: to showcase Sainsbury’s sustainability innovation at scale in two of our largest new stores, Weymouth and Leicester. The aim was for these to be the most sustainable stores yet – “off the grid” for energy, water neutral and, like all Sainsbury’s stores, disposing of zero waste to landfill.

**Sustainable, but financially viable:** The project team knew that the Triple Zero stores would be approved only if they could be shown to be commercially viable and repeatable. These eco investments were not subject to any special conditions – they were evaluated against the same financial hurdles, using the same measures and models (including cash payback, NPV, NPV / gross investment, ROCE and IRR) as any other investment opportunity within Sainsbury’s. They were also funded from existing capital funds, financed via existing cash inflows and debt facilities. So a robust business case was needed.

**Finance as a key player:** A dedicated finance team was assigned to support the project team in:
- identifying and navigating the government incentives such as the renewable heat incentive (RHI) and feed in tariffs (FIT), both of which were factored into the project economics;
- determining the cost savings associated with the carbon, water and waste reductions;
- conducting financial appraisals, using standard financial appraisal techniques;
- arranging capital allocations; and
- conducting post implementation reviews.

Sainsbury’s also sought input from experts at Imperial College London, who provided technological insight on the pre evaluation assessment of the proposed sustainable technologies.

**Achieving results:** The Triple Zero stores in Weymouth and Leicester opened in 2013. In addition to a range of proven sustainable technologies (including rainwater harvesting, photovoltaic solar panels, CO2 refrigeration, efficient LED lighting and a bee hotel), the stores featured solutions new to Sainsbury’s, such as electricity and heating from gas fired combined heat and power (CHP) generators, a biogas offset scheme and partnerships with community water saving projects to offset water use. These have enabled Sainsbury’s to eliminate the stores’ operational carbon footprint (without offsetting) and achieve water neutrality within our communities. The stores continue to achieve good financial returns on investment (22% ROCE) with costs in line with expectation.
PROCESS: BUDGETING PRACTICAL EXAMPLES

Danone: Combining financial and carbon savings

Danone’s beverage company in China, Danone Waters China (DWC), is enjoying a high and growing demand for a successful isotonic beverage called Mizone. As a result we have invested in a new facility in west China to locate production closer to the consumer, satisfy demand and grow market share.

Recognizing carbon savings from the outset: We recognized early on that the commercial advantages of the chosen location also offered significant opportunities to reduce the project’s carbon footprint. For example, a west China production facility with good access to transport routes would reduce delivery distances to market by an average of 300km compared with DWC’s existing central China facilities. Shorter transport distances would mean lower fuel costs, reduced carbon emissions and also allow us to reduce the plastic packaging in our bottles.

Carbon savings led to improved NPV and payback: Danone used traditional appraisal techniques – NPV, payback and IRR – to assess the financial feasibility of the investment. The project was approved using standard, corporate wide targets and thresholds. To assess the carbon savings for the proposed plant, we consulted one of our 140 trained and certified employees known as Carbon Masters. Carbon Masters advise Danone’s business units on environmental topics and how to influence business decisions to improve our carbon footprint. Carbon savings were calculated and translated into monetary terms at €20 per tonne carbon saved. The resulting financial savings were incorporated into the project’s discounted cash flow model. Both the project’s NPV and payback period improved when the carbon savings were taken into account. So including the monetized carbon saving in the financial evaluation bolstered what might have otherwise been a marginal investment decision.
The company is a leading bottler of The Coca-Cola Company brands. Water is the main resource of a beverage business, and energy is a major input. While cost savings are a key consideration, the company believes the greatest benefit from monetizing our broader impact will come from the mid to long term strategic impact of being more efficient in natural resource and energy use, while maintaining our licence to operate and stakeholder trust.

Our commitments
Minimizing our environmental impact across the whole value chain is a core target for us. Our areas of focus are water stewardship, energy and climate change, packaging and recycling, and sustainable agriculture. Our emission reduction goals are aligned with the latest climate models to ensure that our activities help to realize the decarbonization pathway to limit average global temperature increases to 2°C. We have committed ourselves to reducing direct carbon emission intensity by 50 percent by 2020, and to reduce total value chain emissions by 25 percent per litre of produced drink against our 2010 baseline. And that’s only the beginning; we have also developed internal challenges by setting internal carbon prices high enough to affect investment decisions to drive down greenhouse gas emissions materially. In 2016 our operational carbon emissions (from production and transport) decreased by 7.5 percent vs. 2015.

Our approach
To change the capital expenditure evaluation process, a new methodology was developed to incorporate environmental and social impacts with factors such as water and carbon being monetized. Better informed decision making is now possible by requiring people to think about and prioritize investment, leading to reduced environmental impacts and improved social outcomes. Our project was to embed sustainability factors into our capital expenditure appraisal process. First we assembled a cross functional team of internal and external experts, then we studied the A4S Essential Guide to Capex. The company began to require all 28 countries we operate in to incorporate environmental and social impacts in business plans with water and carbon being monetized. The finance function brought together all of the different departments to build a simple model that the whole field could apply, and the finance function set up and led cross functional teams of experts to create the methodology.

This meant that our people thought about and prioritized investment. The key challenge was that carbon reduction can easily become very technical and we tried to bring this across to a finance and business audience. The benefits of the process were that it allowed us to make more sensible and informed decisions and better support the efforts in that area, and the ‘before’ and ‘after’ figures bear this out. Under the old system, the 2016 water savings capital expenditure projects would have had a financial payback of 5.3 years. Under the new system, a financial payback of 0.5 years was expected. As finance, we control capital expenditure and we really worked on the process so that investment in sustainability can be processed very quickly and efficiently. A collaboration approval was also key. It was important to combine the sustainability assessment with the traditional finance assessment and then, together, that allows us to get a holistic view on our overall capital expenditure strategy in the sustainability area.

Key lessons learned: to keep processes practical, grow step by step, don’t become theoretical, link well across the business and continually improve these processes further.

“For the first time we were able to monetize these impacts in the carbon and water area and it allowed us to make more sensible and informed decisions.”

Gerhard Seidl, Group Supply Chain Finance Director, Coca-Cola Hellenic Bottling Company
**Royal DSM: Setting a shadow carbon price**

**WHAT**
We include the financial impact of GHG emissions (scope 1 and 2) through internal carbon pricing in the valuations of large investment projects.

**WHY**
The internal carbon price serves as a useful model for redirecting and scaling up investments towards low carbon technologies, driving operational efficiencies, especially in markets with a carbon price or in regions where a carbon price is expected to emerge. It can help to spot energy and cost saving opportunities at an early stage and better anticipate and understand future implications of the general trend of increased carbon pricing around the world. At the same time this enhances environmental awareness inside DSM.

We are members of the Carbon Pricing Leadership Coalition where we work to advocate for carbon pricing, set an internal carbon price and report on our progress as part of our Annual Report.

**HOW**
For each large investment proposal at DSM, two business cases have to be presented – one with and one without an internal carbon price of €50/t CO2e. We set the carbon price at €50/t CO2e so it is high enough to affect investment decisions to drive down greenhouse gas emissions.

For example, by embedding the internal carbon price in the template request for quote (RFQ) for industrial gases, we make our sites more aware of the financial impact of industrial gas supply. The carbon price for two cases in Switzerland and the Netherlands had an impact of 2-4% and 17% on the total cost of ownership, respectively. In Switzerland, this confirmed that our chosen supplier was the correct business decision. In the Netherlands, the difference between the best solutions was not significant enough to influence the decision making although it showed a significant improvement over the existing situation. Business managers agreed that the inclusion of the carbon price had an added value for the RFQ process.

*"The longer we take to move to a low fossil carbon economy, the higher the costs for future generations and for those already at risk today. Effective and inclusive carbon pricing can facilitate and speed up this transition. At DSM, we apply an internal price of €50 per tonne CO2e. I am pleased to see that a rapidly growing movement of organizations, including thousands of companies, also sees climate action as both an inevitable opportunity and a moral responsibility.”*

Feike Sijbesma, Chief Executive Officer, Royal DSM
PROCESS: BUDGETING PRACTICAL EXAMPLES

South West Water: Integrating sustainability throughout strategic planning, budgeting and forecasting processes

BACKGROUND

For South West Water, sustainability is a common thread through long term strategic planning, to five year business planning and annual budgeting.

We have made sustainability commitments at Board level, as well as publicly, through our published 25 year vision. These commitments ensure that sustainability remains a key priority through planning and delivery.

Key actions within this have been:

- Integrating sustainability into our 25 year vision
- Including key sustainability outcomes linked to specific KPIs as part of our five year business plan
- Linking delivery of sustainability objectives into the governance and drive of overall business performance
- Reporting performance against committed performance levels
- Publishing the 25 year vision, commitments and performance on our website, to be transparent with stakeholders

25 YEAR VISION

In December 2012 we published our 25 year vision, “Waterfuture – What’s in the pipeline 2015 – 2040”. It outlined our long term objectives and was informed by extensive research carried out to determine our customers’ and stakeholders’ priorities for the future of water and wastewater services in our region.

Our approach to customer engagement covered two key areas:

- Understanding customers’ priorities
- Presenting options and allowing customers to choose

Understanding customer priorities

Our customer research and engagement work for the 25 year vision included customer and stakeholder focus groups to understand priorities around our region, willingness to pay surveys with over 1,200 household and 600 non household customers, and the launch of a dedicated website with our first in the industry online investment ‘e-tool’.
PROCESS: BUDGETING PRACTICAL EXAMPLES

South West Water: Integrating sustainability throughout strategic planning, budgeting, forecasting processes

The feedback we received helped us develop our 25 year ‘WaterFuture’ vision which outlined the key customer priorities for services during 2015 – 2040. This identified our key long term aims to deliver:

- reliable supplies of safe, clean drinking water that not only meet the highest water quality standards but also looks and tastes great;
- responsive, innovative and cost effective services that meet our customers’ needs;
- sustainable actions and initiatives that protect the environment; and
- resilient business decisions and investments that deliver the most value for our customers whilst keeping our costs and bills as low as possible.

A range of potential impacts on the average household customer bill for 2019/20 were presented. This gave a range of average bill values depending on the timing of initiatives and investments.

Our final phase of research and engagement was to confirm that the refined proposals from our customer consultation delivered an economic level of service whilst being affordable and acceptable.

The challenge was to find the business plan which balanced the needs of all customers and stakeholders.

Initial results from the first stage of the survey (600 customers) showed that 63% of our customers found our plans to be either acceptable or very acceptable. The main reason why the plan was not acceptable to some customers was the overarching concern about the level of the bill rather than a lack of support for the proposals.

In response to this feedback, the South West Water Board challenged itself to deliver further efficiency savings over and above those already planned. These extra efficiencies reduced our proposed average bill by a further £31.

When we updated our plans to reflect these changes we achieved our highest ever customer acceptance of our plan with 84% finding it to be acceptable.
South West Water: Integrating sustainability throughout strategic planning, budgeting, forecasting processes

The five year business plan to 2020 continued the sustainability thread but developed more specific and detailed sustainability commitments to develop five year priorities following extensive consultation with customers and stakeholders. This was our largest ever consultation and throughout this process our activities have been robustly challenged and refined with the input of the independent WaterFuture Customer Panel and our Board of Directors.

BUDGETING AND FORECASTING

The sustainability priorities identified by customers and stakeholders are embedded into performance expectations for the five year business plan through the published Outcome Delivery Incentives (ODI) framework. For internal planning and driving delivery these are further divided into annual performance targets. Annual performance targets are set (in the form of ODI targets), as well as capital investment and cost efficiency targets.

Detailed budgets and delivery plans are prepared by each function based on their targets, and presented to the executive team. An ODI board, made up of members of the executive and senior management team, approves ODI delivery strategies as well as tracking delivery against target. This ensures all ODI performance is driven through the same framework, and links delivery of sustainability objectives into the governance and drive of overall business performance. Performance against ODI targets is reported monthly through internal management reporting and Board reporting.

The research and engagement helped us to develop eight “outcomes” which form the basis of the five year plan to 2020:

- Clean, safe and reliable drinking water
- Reliable wastewater service
- Responsive to customers
- Protecting the environment
- Available and sufficient water resources
- Benefiting the community
- Resilience in extreme conditions
- Fair charging

Each outcome is published in South West Water’s 2015 – 2020 business plan together with specific KPIs that fall under each outcome. The published plan includes the current performance level, the 2020 target and plans in place to achieve the target.

These published KPIs (categorized as reputational only, reward/penalty, or penalty only) form the ODI framework which attributes financial reward and penalty to performance outcomes.

"Through identifying long term sustainable outcomes with stakeholders, it was much easier to align short term targets and incorporate these into budgeting and forecasting processes."

Susan Davy, Chief Financial Officer, Pennon Group (South West Water)
Danone: Moving away from a traditional annual budgeting cycle

The Danone Executive Board sees sustainability as a strategic priority and provides tone, guidance and direction from the top. Our approach is to integrate sustainable business practices across our 160 plants, on five continents, in over 120 countries, while applying financial skill tests to the way environmental data is measured and managed.

With this backdrop, Danone has taken a radical step and moved away from a traditional annual budgeting cycle in a desire to create a more flexible approach. Under the new model we have a flexible quarterly spending plan, supported by a five quarter rolling forecast which facilitates quick and responsive reallocation of non fixed resources to where they add most value at a point in time.

The role of our finance people in this is very important. For us, the concept of adding value is broad, and not just financially based. Our strategy is for us to grow in a sustainable way, serving the health of each person, of each community and of our planet. Resources are allocated accordingly. Under the new approach, business units have the freedom to manage their own resources while remaining accountable. Rather than managing by budgets, management is through clear priorities and boundaries, and a focus on customer outcomes.

Performance commitments are set in terms of goals, with devolved responsibility to business unit level. Business units are responsible for reviewing the medium term outlook (goals, strategies, action plans and value drivers) annually, and the short term outlook (actual and forecast performance indicators) every quarter. Operational resources are managed by setting goals based on KPIs.

The approach is adaptable to changing product and strategic cycles and the evolving risk environment. With carbon reduction established as a guiding principle, carbon reduction has been elevated to coequal status with business targets. We are also working hard to optimize water usage, which is key to operations. Executives’ vision for the future includes a monthly “sustainability closing”, much like a financial closing, for greater transparency and stronger competitive advantage. For this, reliable information systems are required, which support the measurement of wider value and the resources available to enhance that value.

See case study on the Danone sustainable ERP system for further information
### Yorkshire Water: Integrating carbon forecasting into operational and financial forecasts

#### BUSINESS NEED
At Yorkshire Water, we understand that one of our core business risks derives from operational emissions (primarily the energy consumed to pump and treat water and waste water). Reducing carbon emissions is essential to the organization, as a lower carbon footprint goes hand in hand with efficiency, innovation and cost reduction. Integrating carbon forecasting into operational and financial forecasts has allowed us to support major investments in renewables and energy efficiency, support regulatory and legal compliance, and enhance colleague engagement and our external brand.

#### PROCESS

<table>
<thead>
<tr>
<th>Assess performance</th>
<th>Provide a realistic outlook based on the current business environment</th>
<th>Provide the latest view of expected underlying performance</th>
<th>Allow timely management decisions and corrective actions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Carbon emissions data is already monitored for management reasons, and performance evaluation is integrated into business as usual activities.</td>
<td>To facilitate carbon emissions calculations, a Carbon Accounting Workbook is used. Previous years' and latest consumption data is used to determine the underlying performance, taking into account known changes that are projected to occur, and updates to emissions factors that are determined nationally.</td>
<td>As part of the annual business planning process, a target for tonnes of carbon emissions (tCO₂e) for the upcoming year is set, considering changes to our business activity that will influence our performance. Any financial impact is also reflected in our financial forecast.</td>
<td>Carbon emissions are monitored regularly through a scorecard. If performance is behind forecast, management focus is escalated to electricity consumption and renewable energy self generation in order to deliver on the established targets.</td>
</tr>
</tbody>
</table>

#### LEVERS OF INTEGRATION

- **The Carbon Accounting Workbook**, a practical spreadsheet tool, helped us to integrate sustainability within our forecasting process.
- We formalized our approach by developing written processes for all data to ensure a consistent and repeatable procedure is in place.
- The introduction of Confidence Grades enabled understanding and reporting of the maturity of each element of data, with calculations being verified externally for accuracy and completeness.
**City, University of London: Forecasting carbon emissions savings**

**WHAT**

Within the carbon management plan, we prepared a forecast of carbon emissions savings based on the budgeted capital expenditure, which included carbon reduction projects. The table below shows the predicted implementation cost of the key schemes identified here, and also gives an indication of the likely savings both financially and in terms of tonnes of carbon. If these predicted savings materialize from implementing the measures, then the initial capital investment would pay for itself within the five year time frame.

**WHY**

City, University of London is Islington’s third largest carbon dioxide emitter. Cutting CO₂ emissions as part of the fight against climate change should be a key priority for universities, it’s all about getting your own house in order and leading by example. The Higher Education Carbon Management programme has been designed to assist universities like City, University of London in saving money on energy and putting it to good use in other areas, whilst making a positive contribution to the environment by lowering their CO₂ emissions.

City, University of London was selected in 2007, amidst strong competition, to take part in this ambitious programme. As one of the most proactive Higher Education Institution’s in the UK in responding to the risks that climate change presents, City, University of London has joined the 48 universities across the UK who have to date partnered with the Carbon Trust on this programme in order to realize carbon and cost savings.

**HOW**

Firstly, an organizational carbon risk assessment exercise was carried out to categorize risk, identify the key drivers, the areas, and the nature of their impact. The outputs of this, alongside the current and expected cost of energy and carbon (£12 per tonne under the UK Carbon Reduction Commitment Energy Efficiency Scheme) were analysed. With a view to mitigation of these costs, a series of initiatives were identified alongside lifecycle financial savings. Key areas of action were identified including: purchasing, technology, energy efficiency, estates masterplan, green travel plan, working with local partners and awareness campaigns. An emissions baseline was measured and set, incorporating scope 1, scope 2 and business travel emissions. Options for reduction were identified and prioritized using a Marginal Abatement Cost Curve (MACC) approach, and these prioritized options were fed into the forecasting model to determine likely cost and carbon savings, as shown in the table above.

<table>
<thead>
<tr>
<th>Total Estimated Capital Expenditure</th>
<th>Year 1</th>
<th>Year 2</th>
<th>Year 3</th>
<th>Year 4</th>
<th>Year 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Annual Cost Savings</td>
<td>£147,157</td>
<td>£242,480</td>
<td>£272,146</td>
<td>£959,727</td>
<td>£959,727</td>
</tr>
<tr>
<td>Total Annual Carbon Reduction (tonnes CO₂)</td>
<td>574</td>
<td>1,204</td>
<td>1,361</td>
<td>3,695</td>
<td>3,695</td>
</tr>
</tbody>
</table>

See case study on using a marginal abatement model for further information.
Siemens: Anchoring our Environmental Portfolio into strategic planning, budgeting and forecasting processes

Siemens has considered climate change a megatrend for over a decade. In 2008, as part of our core strategy, we identified products, systems, solutions and services that could be independently identified as benefiting the environment and having a positive impact on CO₂ emissions. The Environmental Portfolio is part of Siemens’ response to global challenges such as climate change, scarcity of natural resources and environmental pollution. It is therefore a key element of our sustainability focus on “Decarbonization”.

Siemens’ Environmental Portfolio – our decarbonization driver

With its Environmental Portfolio, we tackle major challenges, such as climate change, environmental pollution and resource scarcity. The Environmental Portfolio comprises products, systems, solutions and services that meet one of our criteria, namely energy efficiency or the use of renewable energies. Offerings from the Environmental Portfolio help to alleviate negative impact on the environment and to reduce emissions of carbon dioxide and other greenhouse gases contributing to global warming.

Our Environmental Portfolio in facts and figures

- **36 billion €**: In fiscal year 2016, the Environmental Portfolio generated revenue of 36 billion euro.
- **46% of total revenue**: In fiscal year 2016, the Environmental Portfolio represented 46% of Siemens’ total revenue.
- **521 million tons CO₂**: Siemens’ environmental portfolio helps our customers reduce their CO₂ emissions by 521 million tons in fiscal year 2016. This amount is equivalent to more than 60% of Germany’s annual CO₂ emissions.

What characterizes a product in the Environmental Portfolio?

Renewable energy systems and components qualify for our Environmental Portfolio as well as products and systems, that are far more energy efficient in the use phase at our customers than comparable solutions, i.e. yield an increase in energy efficiency of at least 20% or a greenhouse gas reduction of at least 100,000 metric tons of CO₂ equivalents in the reporting year.
Siemens: Anchoring our Environmental Portfolio into strategic planning, budgeting and forecasting processes

The Environmental Portfolio consists of products, systems, solutions and services that meet one of our selection criteria, namely energy efficiency and renewable energy. Within this selection, products need to reach criteria such as an improvement in energy efficiency of 20% or more, or a reduction of at least 100,000 tonnes of carbon dioxide equivalent in the customer use phase during the reporting period.

With our Environmental Portfolio we intend, among other things, to help our customers reduce their carbon dioxide footprint, cut their energy costs and improve their profitability through an increase in their productivity. In addition to its environmental benefits, our Environmental Portfolio enables us to compete successfully in attractive markets and generate profitable growth underlining Siemens’ strategic focus on technologies for energy efficiency and climate and environmental protection. For fiscal 2016, more than three quarters of the revenue from our Environmental Portfolio was generated from products and solutions for energy efficiency.

Representing almost half of Siemens’ global revenues these products and solutions enable us to compete successfully in attractive markets and generate profitable growth. In 2016 the Environmental Portfolio generated €36.3m in revenue and accumulated annual emission reductions for customers of 521 million tonnes of carbon dioxide. By forecasting and monitoring two key performance indicators – revenue and customer emission reductions – management can make timely decisions and interventions on the progress of the portfolio based on short term performance of both financial and non financial impacts.

The entire Siemens business portfolio is reviewed on an annual basis to ensure the appropriate qualification of existing and new Environmental Portfolio elements. For additionally qualified elements, we report their prior year revenue and prior year contribution to the accumulated annual customer reduction of carbon dioxide emissions on a comparable basis.

Three different methods for CO₂ abatement forecasting can be applied

1. Direct before- and-after comparison of the emissions
   - For example, in the case of modernizing power plants, or optimizing the energy consumption of buildings through energy performance contracting

2. Direct comparison with a reference technology
   - For example, the reduction of emissions when using low loss, high-voltage DC (HVDC) power transmission is determined by comparing HVDC with conventional AC power transmission. This approach is also valid for e.g. wind power

3. Comparison with the installed base
   - This method is used e.g. for combined cycle power plants (CCPP) and trains. Here, global average emission factors for electricity generation (CCPP) or utilization of electricity (trains) are applied
GOVERNANCE

Governance sets the boundaries within which people operate. Presented below is a structural approach to governance, which can be used to facilitate integration of sustainability into strategic planning, budgeting and forecasting processes. Good governance is particularly important to achieve an integrated approach. This is due to the cross cutting nature of sustainability factors which require collaboration between different parts of the business to respond effectively. In this section guidance and case studies will be provided against each of the six key governance areas.

1. Mission, vision and strategy to enhance long term stakeholder value
2. Business goals that will enhance long term stakeholder value
3. Set structure for accountable strategic planning, budgeting and monitoring
4. Transparent integrated management reporting
5. Define decision authority, delegations and processes
6. Managing risk and uncertainty

What did organizations say were their key governance challenges?
How will this guide help?
## GOVERNANCE: KEY CHALLENGES

### Organizations said...

| Integration becomes very challenging when there is a lack of leadership buy in, as it leads to a lack of acceptance from the rest of the organization, and a singular focus on shareholder value. |
| Leadership to demonstrate commitment and drive the required change in the organizational culture. |

| Environmental and social factors are often not seen as being as important as other financial measures, and therefore the team’s focus is on short term goals and KPIs to increase shareholder wealth. |
| Linkage of current financial performance to longer term performance of the organization. Performance and benefits of non monetary KPIs to be tracked and communicated with internal and external stakeholders. |

| We notice that there is a lack of appetite for regular reporting of sustainability performance considerations across business units and functions, in part because of the absence of clear criteria for providing comparable and standardized performance information and systems in place for efficient collation of data. |
| Agreement of the key sustainability metrics, and the required level of data accuracy for them to be considered reliable for the end users to inform their decision making. |

| There is no wide scale adoption, or a central view of all sustainability matters, and consequently social and environmental factors are perceived as a separate issue or are integrated at different levels across the teams. |
| Leadership to demonstrate commitment and drive the required change in the organizational culture. Agreement of the key sustainability metrics, and the required level of data accuracy for them to be considered reliable, for the end users to inform their decision making. |

| Among different teams in our business units and functions there is a lack of understanding, alignment and agreement when it comes to considering the proper integration of sustainability within core financial processes, probably due to the diverse nature of sustainability. |
| Agreement of common definitions/terms to make it clear what we mean by sustainability to increase understanding, adoption and alignment. Clear demonstration of the link between social, environmental and financial value. Increased understanding of how different members of the finance team can support delivery of our sustainability performance. |
GOVERNANCE: STRATEGIC MANAGEMENT

1. Mission, vision and strategy to enhance long term stakeholder value

The Board provides the "tone at the top" through incorporating sustainability factors into the organizational mission, vision and strategy. They influence the culture by defining how the organization will respond to these factors, and through their ongoing strategic management approach.

WHY DOES LEADERSHIP BUY IN MATTER?

Leadership buy in:
• provides Board and senior management advocacy around relevance of sustainability to the business;
• demonstrates to the entire business the importance and benefits of considering social and environmental factors within strategic planning, budgeting and forecasting;
• ensures Board oversight of the organization’s integrated strategy;
• facilitates integration of sustainability considerations into all Board committees (e.g. audit, nominating, remuneration, etc.);
• plays a key role in overcoming resistance to change and scepticism over the benefits of integrating sustainability within financial processes;
• enhances integration of sustainability with the organization’s processes and procedures; and
• sets the tone on the sustainability agenda for the rest of the business.

PRACTICAL EXAMPLE

Almost twenty years ago we began to refocus our operations onto a much more sustainable and responsible footing in response to sustainability megatrends that we felt presented a significant opportunity – and threat if we didn’t respond. We have moved away from fossil fuel based petro chemical businesses and turned to health, nutrition and materials sciences.

See full case study for further information
## GOVERNANCE: STRATEGIC MANAGEMENT

### 1. Mission, vision and strategy to enhance long term stakeholder value

**BUILDING SUSTAINABILITY INTO THE LEADERSHIP AGENDA**

The theme of sustainable value creation should be integrated within business performance reviews and strategic discussions to build engagement and support from the Board and senior leadership team. The following highlights a selection of matters relevant to sustainability that might be considered in a typical Board meeting agenda:

<table>
<thead>
<tr>
<th>TOPIC</th>
<th>TYPICAL SPEAKER</th>
<th>POTENTIAL MATTERS FOR PAPERS AND DISCUSSION</th>
<th>HOW SUSTAINABILITY FITS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strategic initiatives</td>
<td>CEO/CFO/Corporate Strategy Director</td>
<td>• Review of strategic initiatives across the business and their contribution toward achieving strategic outcomes</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Analysis of returns from strategic initiatives</td>
<td>• Contribution of sustainability initiatives to strategic outcomes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• New initiatives in the pipeline and their projected benefits and costs</td>
<td>• Sustainability impacts of initiatives and business</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>• Outcomes from sustainability initiatives</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>• Communicate the benefits relating to sustainability initiatives along with all other initiatives</td>
</tr>
<tr>
<td>Business performance</td>
<td>CEO/CFO</td>
<td>• Update on long term outcomes set out in the organization's strategic plan</td>
<td>• Presentation of external impact assessment results, including opportunities identified as well as risks for consideration and management</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Update on year to date performance and comparison to budgeted key performance metrics</td>
<td>• Short term performance presented against long term performance budgets and forecast</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Forecast of key performance metrics for the remainder of the year</td>
<td>• Presentation on wider business performance e.g. staff wellbeing and skillsets, value chain and societal impacts</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Success stories from across the organization</td>
<td></td>
</tr>
<tr>
<td>Governance and compliance</td>
<td>Internal Audit Director</td>
<td>• Review of key business practices and code of conduct</td>
<td>• Ensure sustainability considerations are included within policies, practices and code of conduct and report against them</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Compliance with applicable laws and regulations</td>
<td>• Present performance against applicable laws and regulations e.g. workplace health and safety or environmental permit breaches</td>
</tr>
<tr>
<td>New business</td>
<td>CEO/CFO/Relevant Functional Heads</td>
<td>• Entry into new markets</td>
<td>• Incorporate findings from external assessments into this discussion, along with sustainability mega trend impacts</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Roll out of new products or services</td>
<td>• Analyse sustainability risk and growth opportunity e.g. impact of new acquisition on sustainability targets</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Potential non organic growth opportunities (acquisitions, joint ventures, strategic alliances, etc.) and their impact on the organization’s goals and desired outcomes</td>
<td></td>
</tr>
</tbody>
</table>
## GOVERNANCE: STRATEGIC MANAGEMENT

### 1. Mission, vision and strategy to enhance long term stakeholder value

**SPEAKING THE SAME LANGUAGE**

Common terminology across the organization helps to build understanding and alignment, particularly in instances where cross functional collaboration (such as strategic planning, budgeting and forecasting activities) is required. Use of the same terminology allows finance teams to understand the key sustainability terms that are relevant for strategic planning, budgeting, monitoring and measurement of value.

Common sustainability concepts that should be used consistently across the organization include the following:

<table>
<thead>
<tr>
<th>Natural Capital</th>
<th>Social Capital</th>
<th>Human Capital</th>
<th>Sustainability Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>All renewable and non renewable environmental resources that provide goods or services that support the prosperity of an organization and society including air, water, land, minerals and forests.</td>
<td>The networks, relationships and connections between people, communities and institutions that organizations rely on, and contribute to through their activities.</td>
<td>People’s competencies, capabilities, experience and level of motivation that support organizations to achieve their strategic goals.</td>
<td>Any environmental or social change, positive or negative, caused by an organization through its activities.</td>
</tr>
<tr>
<td>Societal Value</td>
<td>Life Cycle Assessment (LCA)</td>
<td>Shadow Price</td>
<td>Sustainable Shareholder Value</td>
</tr>
<tr>
<td>External direct and indirect non market consequences of natural, social and economic/financial capital impacts (sometimes known as stakeholder value).</td>
<td>A technique to assess environmental impacts associated with all stages of a product’s life from cradle to grave.</td>
<td>A theoretical value or notional price, relating to an activity or impact not currently reflected in market prices.</td>
<td>The internal direct and/or indirect financial consequences of environmental or social issues in monetary terms (sometimes known as company value).</td>
</tr>
<tr>
<td>Environmental Impact Measurement</td>
<td>Environmental Management Accounting</td>
<td>Dependency</td>
<td>Footprint (or Inventory)</td>
</tr>
<tr>
<td>Measuring impacts at all stages of a product’s life across the value chain using such approaches as Life Cycle Assessment and Inventory.</td>
<td>Involves combining financial costs and savings as well as quantitative information relating to the environment to enhance and inform decision making.</td>
<td>Identification and management of factors, of which the organization directly or indirectly depends, for example, agriculture is dependent on the natural process of pollination.</td>
<td>The sum total of a business’ direct and indirect impacts e.g. carbon footprint.</td>
</tr>
</tbody>
</table>
GOVERNANCE: ALIGNING BUSINESS GOALS

2. Business goals that will enhance long term stakeholder value

KEY GOVERNANCE FACTORS TO CONSIDER

Strong governance ensures goals are realistic and aligned with strategy. The ethical overlay provides a driver to consider wider stakeholders in goal setting.

Some key governance factors to consider in relation to setting, developing and delivering business goals are:

- **Determine decision authority and accountability** for the goals. Define when a sustainability specialist needs to be involved in decision making and their authority in those decisions.

- **Provide clear definitions and communication** of the goals so employees can understand the goals and be empowered to deliver on them. Communication of sustainable business goals can also enhance employee engagement, attraction and retention.

- **Test the goals using strategic risk analysis and scenario analysis** to ensure goals are realistic to achieve in the current and likely future operating environment e.g. in a more carbon constrained environment.

- **Ensure clear alignment** to mission, vision and strategy; consistent messaging and use of language. Ensure procedures are in place to prevent short termism where detrimental to long term sustainable business goals.

- **Ensure the goals are measureable and that processes are in place to ensure an effective control environment**, akin to financial KPIs, for performance management against the goals.

- **Use a timeframe** that is relevant to the exposures in the longer term life of the organization, and distil these into the strategic cycle timeframe.

See page 20 for further guidance on setting strategic goals

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PRACTICAL EXAMPLE

At Unilever, we have a simple but clear purpose – to make sustainable living commonplace. We believe profitable growth should also be responsible growth, and that approach lies at the heart of the development of our strategic goals. We developed our goals through a process of actively engaging with our stakeholders. The detail on how we intend to deliver our goals is captured in the Unilever Sustainable Living Plan. It guides our approach to how we do business and how we meet the growing consumer demand for brands that act responsibly in a world of finite resources.

See full case study for further information
GOVERNANCE: ORGANIZATIONAL STRUCTURE AND OVERSIGHT

3. Setting a structure for accountable strategic planning, budgeting and monitoring

RESPONSIBILITY AND ACCOUNTABILITY

Setting oversight responsibility and accountability is key to ensuring successful implementation of strategy and adherence to budgets:

- Establish Board and sub Board level ownership with performance remuneration structures supported by integrated KPIs.
- Incorporate responsibility for sustainability factors into roles and responsibilities within the organization. These should be embedded within ‘business as usual’ processes and practices throughout the structural and functional segments of the business.
- Ensure finance teams appropriately cost strategies, allocate financial resources, effectively monitor performance, and demonstrate that the strategy itself drives sustainable long term value.

PRACTICAL EXAMPLE

To set accountability for delivery against our sustainability targets and budgets, we have made explicit links from our Key Performance Indicators (KPIs) to the variable pay of our management board and employees. We use a selection of KPIs from our 2015 vision strategy that are well established within the business, and incorporate them into our performance management processes.

See full case study for further information

“The clear alignment of our KPIs, with our strategy and the strong governance we have around them, means that we can use them for performance management purposes.”

Geraldine Matchett, CFO, Royal DSM
GOVERNANCE: ORGANIZATIONAL STRUCTURE AND OVERSIGHT

3. Setting a structure for accountable strategic planning, budgeting and monitoring

THE ROLE OF THE BOARD OF DIRECTORS

The board are ultimately accountable for the organization, for appropriate allocation of budgets to achieve strategic objectives and for monitoring performance against those objectives. The following diagrams outline where the role of the Board and the different functions of finance and beyond are impacted by an integrated approach.

<table>
<thead>
<tr>
<th>BOARD LEVEL</th>
<th>Board of Directors</th>
<th>CEO</th>
</tr>
</thead>
<tbody>
<tr>
<td>Approves strategic plans and budgets and reviews forecasts. Monitors corporate performance.</td>
<td>Review and approve organization’s sustainable business strategy</td>
<td>Develop, execute and monitor organization’s sustainable business strategy and policies</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>BOARD COMMITTEES</th>
</tr>
</thead>
<tbody>
<tr>
<td>Audit Committee</td>
</tr>
<tr>
<td>• Understand risk and provide challenge on control environment pertaining to sustainability performance reporting</td>
</tr>
<tr>
<td>• Review and approve integrated reports</td>
</tr>
<tr>
<td>• Oversee compliance with regulations relating to sustainability</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Remuneration Committee</th>
<th>Sustainability Committee</th>
<th>Risk Management Committee</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Align remuneration policies and incentive compensation plans with sustainability goals that are challenging and lead to the creation of long term social, environmental and financial value</td>
<td>• Contribute to organization’s strategic plan ensuring it reflects long term factors and constitutes a sustainable business model</td>
<td>• Monitor the organization’s aggregate exposure to sustainability risks</td>
</tr>
<tr>
<td></td>
<td>• Assess organization’s performance against sustainability aspects of integrated strategy</td>
<td>• Oversee the organization’s risk management and business resilience policies</td>
</tr>
</tbody>
</table>
3. Setting a structure for accountable strategic planning, budgeting and monitoring

**ROLES AND RESPONSIBILITIES FOR SUSTAINABILITY IN A TYPICAL ORGANIZATION**

**BOARD LEVEL**
- Approves strategic plans and budgets, and reviews forecasts.
- Monitors corporate performance.

<table>
<thead>
<tr>
<th>Non Executives</th>
<th>Executives</th>
</tr>
</thead>
<tbody>
<tr>
<td>Approves strategic plans and budgets, and reviews forecasts.</td>
<td>Develop and execute sustainable business strategy, as well as set the tone of the organization and the level of sustainable business ambition</td>
</tr>
<tr>
<td>Monitors corporate performance.</td>
<td>Drive all corporate operations, performance, compliance and management of stakeholders</td>
</tr>
</tbody>
</table>

**FINANCE FUNCTION**
- Lead the strategic planning, budgeting and forecasting processes.
- Essential in integrating non monetary value into budgeting and forecasting processes.
- Integrate sustainability within performance management and financial reporting processes.
- Embed sustainability data within management information platforms.
- Advise on financial impact and risks from sustainability issues in decision making activities.

**Key finance skills at play are strategic financial planning, data and information analysis, preparation and communication of budgeting guidelines.**

**OTHER FUNCTIONS**
- Assess individual functional unit responsibilities in light of the strategic objectives, relevant capabilities, available resources and budgeting guidelines. Determine opportunities to enhance non monetary value through functional roles. Identify suitable non monetary budgets and targets for the function. Provide input, validation, and agreement on assumptions and functional targets in strategic plans, budgets and forecasts.

<table>
<thead>
<tr>
<th>Operations</th>
<th>Commercial</th>
<th>Sales and Marketing</th>
<th>Legal</th>
<th>Human Resources</th>
<th>Corporate Affairs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Improve business resilience by building sustainable value chains</td>
<td>Integrate sustainability factors into strategic research and development, and innovation activities</td>
<td>Improve customer value proposition by integrating sustainability within selling, distribution and promotional activities</td>
<td>Assess impact of emerging and existing sustainability focused legislation</td>
<td>Embed sustainability in performance evaluation and remuneration practices</td>
<td>Define and protect the organization’s brand and reputation through strong sustainability policies and performance</td>
</tr>
<tr>
<td>Maximize operational efficiency to minimize use of energy and non renewable resources</td>
<td>Ensure that business development activities contribute to sustainable business growth</td>
<td>Contribute to delivery of sustainable performance objectives by influencing customer behaviour</td>
<td>Provide legal support to business for strategic changes, e.g. new commercial arrangements and contracts or/and corporate communications</td>
<td>Determine value of human capital and implement enhancement and protection plan</td>
<td>Communicate the organization’s position on sustainability issues to external stakeholders</td>
</tr>
<tr>
<td>Secure renewable energy sources</td>
<td>Partner with suppliers to help deliver sustainable performance objectives</td>
<td>Build wellbeing and diversity and inclusion into business as usual</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
## 3. Setting a structure for accountable strategic planning, budgeting and monitoring

### THE ROLE OF FINANCE IN RELATION TO SUSTAINABILITY

<table>
<thead>
<tr>
<th>FINANCE FUNCTION</th>
<th>Treasury and Commercial Finance</th>
<th>Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Planning and Analysis</td>
<td>Lead the setting of strategic sustainability budgets and forecasts.</td>
<td>Work with finance providers (both equity and debt) to communicate the sustainable business model and long term resilience of the organization, with a view to accruing long term investors and finance at attractive rates.</td>
</tr>
<tr>
<td></td>
<td>Extend financial structure and rigour of strategic planning, budgeting and forecasting process to natural, social and human capital.</td>
<td>Use capital management financing decisions to attract/accommodate new sources of potentially lower cost finance.</td>
</tr>
<tr>
<td></td>
<td>Work with the business to understand performance variances.</td>
<td>Work with Financial Planning and Analysis team to develop and implement a shadow pricing mechanism.</td>
</tr>
<tr>
<td></td>
<td>Drive scenario analysis process, incorporating significant sustainability risks and opportunities, e.g. climate risk.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Work with the Commercial Finance team to develop and implement shadow pricing mechanism.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Advise business units on the financial impact and risks from sustainability issues when developing strategic plans and budgets.</td>
<td>Advise business units on the financial impact and risks from sustainability issues when developing strategic plans and budgets.</td>
</tr>
<tr>
<td></td>
<td>Analyse and interpret complex data streams and influence business partners to integrate the sustainability approach into the business and into partnerships with other organizations.</td>
<td>Perform strategic analysis of sustainability related risks and opportunities.</td>
</tr>
<tr>
<td></td>
<td>Engage business units in developing relevant budgets (e.g. carbon, water) and including sustainability related targets in the budgeting and forecasting processes.</td>
<td>Ensure sustainability factors are considered when assessing the commercial rationale for mergers and acquisitions, joint ventures, strategic alliances and other non organic growth strategies.</td>
</tr>
</tbody>
</table>

### Business Partnering

- Analyse and interpret complex data streams and influence business partners to integrate the sustainability approach into the business and into partnerships with other organizations.
- Engage business units in developing relevant budgets (e.g. carbon, water) and including sustainability related targets in the budgeting and forecasting processes.

### Financial Reporting

- Interpret integrated and sustainability reporting standards, developing business reporting policies and manuals.
- Develop effective control environment for social and environmental data.
- Ensure reporting platform enables timely measurement of performance against sustainability targets set out in strategic plans, budgets and forecasts.
- Own the integrated reporting process for the business, for both internal and external reporting.
- Work with Investor Relations, Treasury and Commercial Finance teams to engage with investors.

### Corporate Development and Mergers and Acquisitions

- Perform strategic analysis of sustainability related risks and opportunities.
- Ensure sustainability factors are considered when assessing the commercial rationale for mergers and acquisitions, joint ventures, strategic alliances and other non organic growth strategies.
- Ensure sustainability factors are included in due diligence activities when executing strategic transactions.
- Assess impact of M&A activity on achievement of sustainability targets.
GOVERNANCE: REPORTING FRAMEWORKS

4. Transparent integrated management reporting

THE INTEGRATED MANAGEMENT REPORTING CYCLE

Finance systems and processes can form an initial framework upon which to build a transparent integrated management reporting framework by:

- Ensuring sufficiently robust control environment to drive complete and accurate reporting
- Evaluating integrated data and overview of supporting control environment for Board attention
- Performing internal audit over integrated control environment to independently test design and operating effectiveness of the controls and report findings to audit committee

The key phases of the integrated management reporting cycle are:

1. Reporting framework
2. Develop control environment
3. Reporting and developing insights

Extend the current reporting framework to support integrated strategic and operational decision making
Ensure the control environment is sufficiently robust to provide complete and accurate reporting under the framework
Produce consistent and accurate integrated performance reports which develop insight and enhance decision making

These will be explored in more depth in the forthcoming A4S Essential Guide to Integrated Management Reporting.

PRACTICAL EXAMPLE

At Sainsbury’s we use simple and visual integrated management reporting to increase the ability of the PLC and OPS Board to make quick, accurate decisions about future developments. An example is our refurbishing stores workstream where reporting of waste and store energy performance (before and after refit) is reported alongside sales and other key store metrics. To enhance decision making there are three cuts of energy data, one looking at a store level, a contractor summary, and a works type summary. These enable performance management to be put in place for both stores and contractors, with both being held accountable for their performance.

See full case study for further information
5. Defining decision authority, delegations and processes

MAKING COMPLEX DECISIONS

Strategic decision making in relation to sustainability factors can be complex, often incorporating input from both inside and outside the finance function by:

- Facilitating cross functional decision making with committees and steering groups
- Defining authorities, delegations and supporting processes to ensure these work effectively
- Determining a suitable approach to decision making depending on the choice of actions, and the method of evaluating the possible outcomes
- Putting safeguards in place to minimize unconscious bias or preference that may lead to unsustainable decisions

Business decisions can be strategic, tactical or operational, with strategic actions having an impact on long term outcomes. These influence how subsequent decisions are made and consequently often require an investment of time to make the right decision.

<table>
<thead>
<tr>
<th>LESS GOVERNANCE REQUIRED</th>
<th>MORE GOVERNANCE REQUIRED</th>
</tr>
</thead>
<tbody>
<tr>
<td>Structured</td>
<td>Unstructured</td>
</tr>
<tr>
<td>Low risk</td>
<td>High risk</td>
</tr>
</tbody>
</table>

Increasing complexity of decision

PRACTICAL EXAMPLE

At Sainsbury’s, our governance model reinforces and highlights the significance of integrating sustainability into every aspect of our business. Our Corporate Responsibility and Sustainability Committee is a Board level body chaired by a non executive director and oversees the company’s performance against our 20x20 Sustainability Plan, which is an integral part of our corporate strategy. In addition, there is a Corporate Responsibility and Sustainability Steering Group chaired by our CEO. This in turn encompasses smaller Value Steering Groups, each of which supports one of the company’s five value areas.

See full case study for further information
5. Defining decision authority, delegations and processes

**COMMON ISSUES IN DECISION MAKING**

Decision bias and the psychology associated with making decisions can cause inappropriate business decisions to be made, i.e. decisions which are irrational given the information available at the time. Given the often long term and unfamiliar nature of decisions relating to sustainability, they may be particularly prone to psychological bias. Here are some factors to be aware of when making decisions that may impact accounting for sustainability.

<table>
<thead>
<tr>
<th>Decision making ability</th>
<th>Illustrative scenarios</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overconfidence – Most people are overconfident of their own decision making ability.</td>
<td>Insufficient impact analysis is performed in choosing between two strategic social capital initiatives. The decision is based on a quick analysis and mostly instinctive. The social return on investment potential is not achieved and social capital is devalued.</td>
</tr>
<tr>
<td>Status quo bias – People disproportionately stick with the status quo rather than consider or select alternative options.</td>
<td>Strategic options about new innovations, initiatives or approaches that work towards a sustainable business model are not embraced because no significant issues have arisen yet with the way things have always been done in the past. Competitors working on lower resource solutions gain market share.</td>
</tr>
<tr>
<td>Optimism bias – People tend to overestimate the probability of positive events and underestimate the probability of negative events. Optimism bias also occurs when estimating how long things will take, and how much they will cost.</td>
<td>The probability of significant flood events is underweighted, thus scenario analysis is not considered necessary. Insufficient capital is invested in flood prevention and when preventable flooding does occur, the impact and cost are high.</td>
</tr>
<tr>
<td>Sunk cost bias – The more you invest in something the harder it becomes to abandon it, even if it’s no longer the rational option.</td>
<td>Significant infrastructure investment has been made in the past in a carbon intense process. Budget required to maintain the infrastructure is low, replacement budget is high but the forecast carbon and financial savings meet the investment criteria. There is a reluctance to write off the value of the current asset and invest more capital, despite this being a rational option.</td>
</tr>
<tr>
<td>Fooled by experience – Decisions based on experience are inherently biased. This can lead people to reapply a previous decision despite circumstances or surrounding context being sufficient to warrant separate consideration.</td>
<td>Project tenders have always followed a standard budgeting approach, with a market leading success rate. The market context is changing, with increasing emphasis in the customer base on carbon reduction. Based on experience, the decision is made by commercial finance to keep the current, successful low cost budgeting approach. Business is lost to a competitor with a higher financial budget, but who introduced a carbon budget into their standard approach.</td>
</tr>
</tbody>
</table>
GOVERNANCE: DECISION MAKING POWER AND PROCESS

5. Defining decision authority, delegations and processes

### Potential issue

**Uncertainty avoidance** – Risk appetite can be impacted by cultural preference, with some cultures preferring to avoid uncertainty. Decision making processes may need to be adapted in some regions to account for this.

**Group think** – This occurs when a group prefers harmony over critical evaluation, i.e. there is a reluctance to challenge a proposed idea. This is increasingly likely in collectivist societies.

**Loss aversion** – People tend to prefer avoiding losses to acquiring equivalent gains. Changing the reference point so options are seen as losses as opposed to gains, or vice versa, will often change the decision made.

**Instinctive decisions** – When making quick decisions, subconscious intuitive simplifications are common and not always helpful.

**Temporal discounting** – The idea that a negative outcome in the future is not perceived as badly as a more immediate negative outcome. The further away the negative outcome, the less negatively it is perceived.

**Consideration of future consequences** – People vary in the extent to which they consider the future outcomes of their current behaviour depending on their personality.

### Illustrative scenarios

**Group finance is encouraging innovation in cost effective ways to transition to low carbon across their global business.** Country level management have autonomy over what they implement and how they allocate budget to do so. Some countries try ambitious, bold new options and make significant savings; others are much more conservative, investment is low and reductions are limited.

**The operations director proposes strategic plans for a new gas fuelled CHP plant, forecasting opex savings of 15% and carbon savings of 10%.** The instinctive view of the Board is to proceed with the investment; all agree as it saves money and carbon, what is not to like? The plan is not critiqued in detail and opportunities for significantly greater savings were missed.

**In setting a carbon budget for a specific project, division management believe a level of 70% of former levels is achievable. In submitting the carbon budget to group finance, there is debate in the team whether to submit a budget of 60% of former levels (a stretch target, unlikely to be fully achieved), 70% of former levels (their best estimate) or 80% of former levels (an easy target, with low risk of failure). 80% was set, and slightly exceeded. The incentive and opportunity for greater savings were lost.**

**Climate change is generally perceived as a long term risk. This makes it easier not to act now despite knowledge of the likely consequences (some of which may be short term). Some people find it easier to ignore than others.**
COMMON ISSUES IN DECISION MAKING

Organizations tend to have structured approaches for key decisions. This is relevant for strategic decisions, particularly where significant budgets need to be allocated for large investment decisions. The role of governance is to determine and define what structures are appropriate, and standardize where necessary, e.g. requiring use of multi criteria decision analysis. In this way the risk that inappropriate, irrational or erroneous decisions are made can be reduced. This is especially important where organizations, or individuals, can be held accountable for decisions and/or there is a risk of litigation.

Being able to demonstrate that a decision followed a formal process and was justified on the basis of the information available at the time can be very important.

Some potential ways to mitigate these factors include:

- Have someone disruptive in the team to bring ‘opposite thinking’
- Get people to focus on possible failures and provide prospective hindsight
- Look at prospective outcomes from both a gain and a loss perspective
- Involve diverse stakeholders in decision making. This can be done by:
  - involving them directly in the process
  - using members of the team to role play as if they were specific stakeholders
  - engaging separately on potential options, e.g. in stakeholder workshops
- Be conscious of ‘do nothing’ decisions, e.g. not updating the strategy to a sustainable business model. Ensure an appropriate amount of rigour is applied to ‘do nothing’ decisions in the same way as to other key decisions. Is ‘do nothing’ justified?
GOVERNANCE: RISK MANAGEMENT FRAMEWORKS

6. Managing risk and uncertainty

Identification and mitigation of risk plays a significant part in responding to sustainability factors. Organizations should:

- Integrate sustainability risk into the corporate governance processes
- Incorporate oversight into the Audit Committee or Risk Management Committee agendas to enable them to play a key role in ensuring risks attributable to sustainability factors are appropriately identified, understood and managed

The key phases of the integrated risk process cycle are:

1. Risk identification
   - Ensure the risk horizon is broad enough to incorporate long term risks, reputational risks and those due to changing socio economic and environmental factors. Consider using tools such as SWOT to do so.

2. Gain an understanding
   - Involve sustainability specialists to assist in gaining an understanding of the risks, the likelihood and potential impact. Perform scenario analysis to support this process and assess resilience of the strategy.

3. Integrate into decision making
   - Assign clear accountability for managing and monitoring risks arising from macro sustainability trends in line with normal risk procedures. Embed risk factors and mitigations into decision making processes.

See the A4S Essential Guide to Managing Future Uncertainty for further guidance.
GOVERNANCE: PRACTICAL EXAMPLES

<table>
<thead>
<tr>
<th>STRATEGIC MANAGEMENT</th>
<th>ALIGNING BUSINESS GOALS</th>
<th>ORGANIZATIONAL STRUCTURE AND OVERSIGHT</th>
<th>REPORTING FRAMEWORKS</th>
<th>DECISION MAKING POWER AND PROCESS</th>
<th>MANAGING RISK AND UNCERTAINTY</th>
</tr>
</thead>
<tbody>
<tr>
<td>Danone: Our Manifesto to building a healthier future</td>
<td>Yorkshire Water: Creating a culture of understanding, alignment and agreement among teams</td>
<td>Anglian Water: Using cross functional involvement in strategic plans to strengthen the sustainability agenda</td>
<td></td>
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</tbody>
</table>
Almost 20 years ago, we began to refocus our operations onto a much more sustainable and responsible footing in response to sustainability megatrends that we felt presented a significant opportunity – and threat if we didn’t respond. We have moved away from fossil fuel based petrochemical businesses and turned to health, nutrition and materials sciences.

At the heart of our mission is the core value of sustainability and a commitment to helping create a more sustainable world. As part of our 2010-2015 strategy, the company took sustainability to the next level. In addition to fulfilling our own responsibilities towards society, we have successfully developed sustainability as a strategic growth driver.

For us, sustainability is a key differentiator and value driver in our markets. We are uniquely positioned to capitalize on the many opportunities this presents across the value chain. As an integral part of the company’s operations, strategic actions and decisions, sustainability guides the activities of our global business groups. They are charged with continuously developing innovative science based products and solutions that contribute to a brighter future for people, while helping to increase our profitability.

In order to have commitment from shareholders for this business model, DSM focused on those investors who take the long term view.

Excerpts from 2014 Capital Markets Day Analyst presentation.
Danone: Our Manifesto to building a healthier future

Danone is a global food company providing fresh dairy products, bottled water, and both medical and baby nutritional products. Our mission is to bring health through food to as many people as possible. Our cofounder and long time CEO, Antoine Riboud, said in 1972: ‘We only have one Planet Earth’. This ethos has been at the heart of the company’s culture for a long time. Since the early 1970s Danone has operated under what we refer to as ‘a dual project’, having both economic and social objectives has embedded nature into Danone’s genes.

In 2015 we published a new Manifesto which will be a guiding star to build a healthier future, and to enshrine the principles of co creation, local adaptation and continuous improvement. This Manifesto, which captures the ethos of Danone, is part of what drives Danone’s finance team and their cross functional colleagues to work together to find innovative, financially sound solutions for healthier customers and a healthier planet.

This Manifesto belongs to every Danoner. By living our Manifesto, we carry forward our mission to “bring health through food to as many people as possible” and our dual project for business success and social progress, while reflecting our values of Humanism, Openness, Proximity and Enthusiasm. This Manifesto embodies our commitment to lead an Alimentation Revolution by supporting people to adopt healthier choices and lifestyles, and by caring about the health and wellness of Danone and Danoners, of our communities and our planet, of current and future generations.

“We drafted a manifesto for alimentation that summarizes our convictions and commitments, spelling out our goals and staging just how we plan to act on our mission and work with all of our stakeholders.”

Emmanuel Faber, Chief Executive Officer
GOVERNANCE: STRATEGIC MANAGEMENT PRACTICAL EXAMPLES

Yorkshire Water: Creating a culture of understanding, alignment and agreement among teams

In 2010 Yorkshire Water launched a new company vision that incorporated sustainability at its heart: “Taking responsibility for the water environment for good”. To encourage embedding the vision into our culture, we launched a communication programme that helped us to empower our colleagues to take personal ownership and accountability for our goals.

We integrated our vision and Strategic Business Objectives into performance management and reporting by developing a framework of short, medium and long term projects and targets which encompass all of our sustainability priorities, with progress linked to colleague reward incentives. We monitor and drive delivery of this framework through our scorecards, quarterly updates to the leadership team and through our integrated annual report.

Mission, vision and strategy to enhance long term stakeholder value
GOVERNANCE: STRATEGIC MANAGEMENT PRACTICAL EXAMPLES

Anglian Water: Using cross functional involvement in strategic plans to strengthen the sustainability agenda

When the 2014 Water Industry Regulatory Price Review (‘PR14’) came into effect, Anglian Water had to deliver a five year strategic plan that included a wide range of non monetary measures including those relevant to sustainability. The project was company wide and, though the end plan was already based on our existing strategy, communicating the new approach that incorporated sustainability issues in such way that it would drive behavioural change was a challenging task.

To overcome this, Anglian Water created a PR14 Programme Board that reported to the Board, and beneath which various sub groups were operating to provide details and implementation proposals.

This approach resulted in strong buy in from various leaders across the organization, who played a key role in disseminating the message across the business. It also enabled cross functional involvement and ownership of the strategic plans, which strengthened the organization’s commitment to driving the strategic sustainability agenda forward.

The Finance team engaged in the PR14 Business Plan at every level and at every stage of the development and decision making process. At a high level this included explaining in detail to the shareholders/investors the impact on the business of the plan and the Final Determination. At a more granular level the finance team ensured that the strategic intent in the plan was costed and included such that the business could have confidence that the intent set out in words and desired outcomes would be financially deliverable. The Finance team played a vital role in challenging the business to ensure its plans would meet the strategic financial and non financial outcomes as well as developing the financing, tax and insurance strategies.

PR14 Programme Board

<table>
<thead>
<tr>
<th>Senior Executive Officers</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Treasury</td>
</tr>
<tr>
<td>• Tax</td>
</tr>
<tr>
<td>• Capital Investments</td>
</tr>
<tr>
<td>• Operations</td>
</tr>
<tr>
<td>• Asset Management</td>
</tr>
<tr>
<td>• Water Resources</td>
</tr>
<tr>
<td>• Customer Services</td>
</tr>
<tr>
<td>• Regulation</td>
</tr>
<tr>
<td>• Corporate Communications</td>
</tr>
</tbody>
</table>
GOVERNANCE: ALIGN BUSINESS GOALS PRACTICAL EXAMPLES

Unilever: Setting strategic goals to help our business grow

WHAT
In 2012 we set our four strategic goals to be:

• **Grow the Business**: By 2020 our goal is to double sales by the business compared to 2010
• **Improve Health and Wellbeing**: By 2020 we will help more than a billion people take action to improve their health and wellbeing
• **Reduce Environmental Impact**: By 2030 our goal is to halve the environmental footprint from making and using of our products as we grow our business
• **Enhance Livelihoods**: By 2020 we will enhance the livelihoods of millions of people as we grow our business

WHY
At Unilever, we have a simple but clear purpose – to make sustainable living commonplace. We believe this is the best long term way for our business to grow. Our purpose and operating expertise will help us to realize our vision of accelerating growth, reducing our environmental footprint and increasing our positive social impact. We recognize this is ambitious, but it is consistent with changing consumer attitudes and expectations. Our unswerving commitment to sustainable living is increasingly delivering:

• more trust from customers; and
• a strong business for shareholders, with lower risks and consistent, competitive and profitable long term growth.

HOW
Defining our purpose and our vision were key to setting our strategic goals. We believe profitable growth should also be responsible growth. That approach lies at the heart of the development of our strategic goals.

In developing our goals there were a number of priorities that were important to us:

• Customer and consumer trust
• A strong business for shareholders
• A better, healthier and more confident future for children
• A better future for the planet
• A better future for farming and farmers

We developed our goals as a path towards achieving our vision, incorporating these priorities through a process of actively engaging with governments, intergovernmental organizations, regulators, customers, suppliers, investors, civil society organizations, academics and our consumers. The detail on how we intend to deliver our goals is captured in the Unilever Sustainable Living Plan. It guides our approach to how we do business and how we meet the growing consumer demand for brands that act responsibly in a world of finite resources. Our Plan is distinctive in three ways:

1. It spans our entire portfolio of brands and all countries in which we sell our products.
2. It has a social and economic dimension: our products make a difference to health and wellbeing and our business supports the livelihoods of many people.
3. When it comes to the environment, we work across the whole value chain, from the sourcing of raw materials, to our factories and the way consumers use our products.
When we launched our new strategy, sustainability was identified as a key business and growth driver. To be able to track our performance against the 2015 vision we developed a set of Key Performance Indicators (KPIs) that incorporated our sustainability aspirations. These were developed to be reported externally as well as to be used internally to steer the business. A selection of these KPIs that are well established within the business are used in performance management and are linked to the variable pay of the management Board and employees.

*The development of the KPIs, management confidence in them (i.e. reliability and accuracy) as well regular internal management reporting means that we can use them as part of our performance management processes.*

Bert Steinbusch, Project Director Finance Transformation, Royal DSM

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### DSM Managing Board Total Direct Compensation (on target)

<table>
<thead>
<tr>
<th>Element</th>
<th>Vehicle</th>
<th>Performance targets &amp; measures</th>
<th>Target pay-out (% of ABS)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed</td>
<td>Annual base salary (ABS)</td>
<td>Cash</td>
<td>N/A</td>
</tr>
</tbody>
</table>
| Variable                       | Short Term Incentive (STI) (minimum performance threshold for STI pay-out set by Supervisory Board) | Cash* | 1. Financial:  
  • Adjusted EBITDA  
  • Gross Free Cash Flow  
  • Organic Net Sales Growth | 12.5%  
  10%  
  2.5%                     |
|                                |               | 2. Sustainability:  
  • Brighter Living Solutions  
  • Employee Engagement Index  
  • Safety Performance | 5%  
  5%  
  5%                     |
|                                |               | 3. Individual | 10%                     |
|                                | Long Term Incentive (LTI) | Performance Shares | 1. Financial:  
  • Relative Total Shareholder Return (TSR)  
  • Return On Capital Employed (ROCE) growth | 25%  
  25%                     |
|                                |               | 2. Sustainability:  
  • Energy Efficiency Improvement (EEI)  
  • Greenhouse-Gas Emissions (GHGE) Efficiency improvement | 25%  
  25%                     |

*STI deferral into shares: A mandatory (25%) and a voluntary proportion (up to a total maximum of 50%) of the actual STI amount earned in a year is deferred into DSM shares with a three year holding period. This is linked to a one-for-one matching award on the total deferred amount under the condition that predefined performance targets and measures are met at the end of the three year vesting period.*
GOVERNANCE: REPORTING FRAMEWORKS PRACTICAL EXAMPLES

Sainsbury’s: Using simple and visual integrated management reporting

‘Respect for the Environment’ is one of our five core values that underpin our business. It is all about doing the right thing by enhancing operational efficiency, which is both good for business and the environment. Part of this programme is a focus on reducing operational carbon by 30% by 2020 versus a 2005/06 baseline. A key work stream that focuses on this commitment is looking at refurbishing stores to enable them to use less energy, which has a positive impact on both the environment and the profit and loss account.

Sitting behind the implementation of this programme is a key management report that increases the ability of the PLC and OPS Board to make quick, accurate decisions about future developments. These reports are delivered under the usual governance of Investment Board papers and Post Implementation Review papers post investment. The report looks at store energy performance both during and after works have taken place, measuring the energy savings compared to targets. It is reported and reviewed in the same manner as other key store metrics such as sales and waste. To enhance decision making there are three cuts of data, one looking at a store level, a contractor summary and a works type summary. These enable performance management to be put in place for both stores and contractors, with both being held accountable for their performance.

Our summary of the different implementation activities available is key in decision making as it provides a view on the return on investment of different options. This is used to then influence future decisions about the level of investment for additional stores.

A key benefit of the report is that the OPS and Investment Boards have been able to make decisions more quickly about future works. This has enabled more savings to be realized as changes can be implemented in a timely manner rather than having to be discussed in detail. Annual performance is also used to assess the level of investment for the next financial year. This enables the level of capital required to be accurately forecasted, and therefore enhancing the budgeting process.

TOP TIPS

- Ensure Board level accountabilities are clearly agreed and that the governance structure and processes allow for balanced decision making and speedy escalation.

- Integrated management reporting needs to be simple and visual, with clear ‘line of sight’ through the business from front line operations right up to the Board.

- Achievement of effective cross business working is facilitated by alignment and communication of organization wide targets and incentives.
Sainsbury’s: Integrating sustainability into our governance model

Achieving our strategic goals and objectives requires having leadership buy-in, engagement from experts throughout our business and strong governance. Our governance model reinforces and highlights the significance of integrating sustainability into every aspect of our business.

Our Corporate Responsibility and Sustainability Committee is a Board level body chaired by a non-executive director and oversees the company’s performance against our 20x20 Sustainability Plan, which is an integral part of our corporate strategy.

In addition, there is a Corporate Responsibility and Sustainability Steering Group chaired by our CEO. This in turn encompasses smaller Value Steering Groups, each of which supports one of the company’s five value areas. Our Value Steering Groups bring together a cross-functional team once a quarter and are chaired by the accountable member of our Operating Board.

Our steering groups not only give strategic direction, but also measure our progress against the plans defined, deal with new or emerging issues, and provide context for external reporting.

We keep reviewing any sustainability issues that might be an impediment to our strategic objectives and actively engage with our stakeholders to ensure we adapt as required.

We have a clear plan of activity for our commitments every year, clearly linked to our budgets and forecasts.

We routinely monitor our performance and reward process, and we communicate our results and challenges to all our stakeholders for transparency.

“We believe we have a responsibility to improve the world around us and I know that we’ll continue to challenge ourselves to set ambitious targets”

Jean Tomlin, OBE, Chair of Corporate Responsibility and Sustainability committees, Sainsbury’s
GOVERNANCE: DECISION MAKING
POWER AND PROCESS PRACTICAL EXAMPLES

Sainsbury’s: Integrating sustainability into our governance model

J Sainsbury plc Board
Chair

CR&S STEERING GROUP
Established 2001, meets twice annually
Chair: Chief Executive

- Living healthier lives
  Owner: Marketing Director

- Sourcing with integrity
  Owner: Food Commercial Director

- Respect for our environment
  Owner: Chief Financial Officer

- Making a positive difference to our community
  Owner: Director of non-food operations

- A great place to work
  Owner: Group HR Director

CORPORATE RESPONSIBILITY AND SUSTAINABILITY COMMITTEE
Established January 2007, meets twice annually
Chair: Non-Executive Director

- Health Steering Group
- Product Forum
- Environment Steering Group
- Community Steering Group
- A Great Place to Work Steering Group
PERFORMANCE MANAGEMENT

STRATEGIC PLANNING, BUDGETING AND FORECASTING
Performance management is a set of processes that enables an organization to monitor its performance against the strategy. This includes both performance metrics (KPIs) and the employees’ behaviours and incentives when working to achieve the strategy.

Successful organizational performance depends on collective, individual performance of the employees. Therefore, developing the right metrics to measure and monitor employee performance is an important part of managing organizational performance.

Building the foundations for an environment where all employees can achieve their potential, to ensure a balanced, fair and equitable basis for accountable performance appraisal and KPI-based remuneration frameworks.

Employee performance and organizational performance are inherently linked, therefore it makes sense for KPIs for both to be aligned.

The collective skills of finance and HR will be valuable to develop and measure employee performance.

Culture and behaviour standards are the bedrock of employee performance, with strategy and values the bedrock for organizational performance. The two are inherently interlinked.

What did organizations say were their key performance management challenges?

How will this guide help?
PERFORMANCE MANAGEMENT: KEY CHALLENGES

**Organizations said...**

“Developing the right incentives and mechanisms to integrate sustainability factors into the organization’s performance management processes requires a structured approach.”

“The communication between finance teams and sustainability specialists is not transparent, and the information is not always available to gauge performance appropriately.”

“Short term financial pressures are an impediment to the successful delivery of long term goals and progress with sustainability issues and opportunities.”

“There is no guidance on how to link sustainability to financial impacts and benefits, resulting in us developing methods that might not treat sustainability as an integral part of our goals.”

“There is no ongoing tracking of initiatives and their benefits/costs to the company in terms of sustainability.”

**We need...**

Guidance on how to identify who can influence sustainability within the organization, and how they build this into, and track performance in, their appraisal. Remuneration can then be structured to incentivize the right behaviour.

Common terms and agreement on the right performance metrics, based on what is material to the business.

Guidance on how to link short term results to longer term performance and value.

Guidance on how to assess impacts and outcomes for sustainability and how this links to the overall strategic goals.

Guidance on how to measure and track benefits on sustainability initiatives.
What do I need to consider when monitoring organizational performance against the strategy and including corresponding metrics within my employee incentives?

At the strategic level, performance management is ensuring the right culture, structures and processes are in place to support delivery of the strategy.

### Areas to Consider

<table>
<thead>
<tr>
<th>1. Employee performance</th>
<th>2. Organizational performance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><strong>Culture and behaviour standards</strong> – clearly define and communicate behavioural expectations, with sustainability at the heart.</td>
</tr>
<tr>
<td></td>
<td><strong>Skills and capabilities</strong> – perform a sustainable business skills and capabilities audit, develop strategy for gaps and long term growth.</td>
</tr>
<tr>
<td></td>
<td><strong>Personal objectives and KPI based remuneration frameworks</strong> – align objectives and frameworks with corporate values, strategy and behaviour standards and using outputs and insights from activities above.</td>
</tr>
<tr>
<td></td>
<td><strong>Diversity and inclusion</strong> – assess diversity profile and pay gaps, for employee base, by grade, and for recruitment and promotion. Understand barriers to inclusion. Define business case and strategy for diversity and inclusion management.</td>
</tr>
<tr>
<td></td>
<td><strong>Empowerment, influence and autonomy</strong> – agree empowerment approach, e.g. employee innovation programme, performance roadshows, identify influencers and agree autonomy guidelines.</td>
</tr>
<tr>
<td></td>
<td><strong>Employee engagement</strong> – perform regular engagement survey, understand engagement shortfalls and barriers, agree strategic response.</td>
</tr>
<tr>
<td></td>
<td><strong>Strategy and values</strong> – clearly define and communicate corporate strategy, culture and values, with sustainability at the heart.</td>
</tr>
<tr>
<td></td>
<td><strong>Leadership and communications</strong> – align corporate and communication strategies, include communications to both internal and external stakeholders.</td>
</tr>
<tr>
<td></td>
<td><strong>Organizational and governance structures</strong> – set structure, oversight responsibility and accountability. Consider whether a separate sustainability committee is appropriate.</td>
</tr>
<tr>
<td></td>
<td><strong>Operational frameworks</strong> – align operations philosophy with culture and set corresponding principles, practices and KPIs.</td>
</tr>
<tr>
<td></td>
<td><strong>Reporting frameworks and systems</strong> – agree balanced scorecard; assess suitability of current IT systems and specification shortfall.</td>
</tr>
<tr>
<td></td>
<td><strong>Control environment</strong> – agree a recognized controls framework to use, e.g. the COSO framework, including for non monetary KPIs.</td>
</tr>
<tr>
<td></td>
<td><strong>Collaboration practices and tools</strong> – agree practices and tools to facilitate cross functional and geographically remote collaboration.</td>
</tr>
<tr>
<td></td>
<td><strong>Business plan targets</strong> – ensure targets are ethical, realistic, aligned with strategy and defensible to a wide range of stakeholders.</td>
</tr>
<tr>
<td></td>
<td><strong>Decision making processes</strong> – define authorities, delegations and supporting processes across the relevant committees.</td>
</tr>
<tr>
<td></td>
<td><strong>Project appraisal and management practices</strong> – agree methodology to embed sustainability into project appraisals and practices.</td>
</tr>
<tr>
<td></td>
<td><strong>Asset management</strong> – agree long term time horizon for asset management strategy to span, e.g. 20, 40, 50 years.</td>
</tr>
<tr>
<td></td>
<td><strong>Innovation</strong> – define innovation ambition and set strategy and budgets accordingly.</td>
</tr>
</tbody>
</table>
PERFORMANCE MANAGEMENT

1. Employee performance

- Employee wellbeing
- Employee engagement
- Empowerment, influence and autonomy
- Diversity and inclusion
- Personal objectives and KPI based remuneration
- Skills and capabilities
- Culture and behaviour standards

See full Performance Management diagram

See the next page for further guidance on how to select key influencers within the organization

See the A4S Essential Guide to Social and Human Capital Accounting for further guidance

See the forthcoming A4S Essential guide to Finance culture for further guidance

PRACTICAL EXAMPLE: EMPLOYEE WELLBEING

At National Grid, we measured our return on investment from our employee wellbeing programme.

See full case study for further information

PRACTICAL EXAMPLE: PERSONAL OBJECTIVES AND KPI BASED REMUNERATION

At SSE, see our remuneration structure includes performance against sustainability related KPIs.

See full case study for further information

PRACTICAL EXAMPLE: PERSONAL OBJECTIVES AND KPI BASED REMUNERATION

At Sainsbury's we have incorporated our Sustainability Plan values into our Board remuneration policy.

See full case study for further information
**PERFORMANCE MANAGEMENT**

### 1. Employee performance

**ALIGN SUSTAINABILITY CHANGE AGENTS WITH PERFORMANCE MEASURES**

To encourage progress towards an organization’s strategic objectives, key change agents within the organization should be identified and aligned with sustainability targets through annual objective setting and remuneration frameworks.

Sustainability champions and influencers should be determined based on their ability to enact change in the organization and should be aligned with sustainability targets through goal setting and remuneration incentives. Each department (including Finance) should have at least one sustainability champion; if sustainability is truly embedded throughout the organization some members of the sustainability team should sit within the various functional teams as well as having a central sustainability hub. An increasing number of organizations are also emphasising the role of Finance Director – Sustainability or Sustainability accountant to embed finance skills within the sustainability team and drive integration and collaboration across finance and sustainability teams.

<table>
<thead>
<tr>
<th>ABILITY TO INFLUENCE AND ENACT CHANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>HIGH</strong></td>
</tr>
<tr>
<td><strong>INFLUENCERS</strong></td>
</tr>
<tr>
<td>Sustainability targets are highly integrated with individual performance objectives based on ability to influence or enact change</td>
</tr>
<tr>
<td><strong>EXAMPLES</strong></td>
</tr>
<tr>
<td>Finance Director, Financial Controller, Property Finance Director, Head of Financial Planning and Analysis</td>
</tr>
</tbody>
</table>

| **LOW**                                |
| **CHAMPIONS**                          |
| Sustainability targets are integrated with individual performance objectives based on the performance of their business area |
| **EXAMPLES**                           |
| Finance Manager, Treasury Manager      |

| **MID**                                |
| **CONTRIBUTORS**                       |
| Sustainability targets are integrated where individuals can impact through part of their role |
| **EXAMPLES**                           |
| Tax Analyst, Financial Accountant      |

| **MID**                                |
| **OBSERVERS**                          |
| Sustainability targets are integrated where possible within individual performance objectives |
| **EXAMPLES**                           |
| Accounts Payable, Accounts Receivable Clerk |
PERFORMANCE MANAGEMENT

2. Organizational performance

- Innovation
- Asset management
- Project appraisal and management
- Decision making processes
- Business plan targets
- Collaboration practices and tools
- Control environment
- Reporting frameworks and systems
- Operational frameworks
- Organizational and governance structures
- Leadership and communications
- Strategy and values

PRACTICAL EXAMPLE: STRATEGY AND VALUES
At The Crown Estate, we define our values with sustainability at the heart.
See full case study for further information

PRACTICAL EXAMPLE: ORGANIZATIONAL AND GOVERNANCE STRUCTURES
At Sainsbury’s, we set our governance structure with accountability for Corporate Responsibility and Sustainability.
See full case study for further information

PRACTICAL EXAMPLE: PROJECT APPRAISAL AND MANAGEMENT
At Yorkshire Water, we linked sustainability to monetary and non-monetary impacts and benefits, and developed our Total Impact and Value Assessment.
See full case study for further information

See the next page for further guidance

See full Performance Management diagram
2. Organizational performance

OVERCOME SHORT TERM PERFORMANCE PRESSURES AND THEIR IMPACT ON LONG TERM VALUE

For many companies, short term financial pressures often preclude sustainability considerations from being incorporated into strategic plans, budgets and forecasts. Such ‘short termism’ can result in sustainability being treated as a secondary issue, rather than a core priority. To overcome short term pressures, organizations should retain sufficient focus on the long term value that is derived from integrating sustainability within their strategy and business model, as well as understanding short term benefits.

Short term pressures

- Investors and analysts expect quarterly earnings targets to be met, resulting in increases in share price and dividends in the short term.
- Suppliers are seeking to pass on higher prices of production and raw materials to their customers.
- Customers are leveraging their increased access to information to search for products and services delivering the best value for money.
- Employees and organized labour groups are constantly seeking concessions from management on wages, benefits, and working conditions.

Long term value

- Results presented to investors should be in the context of longer term performance and value. Actively seek to build an investor base with shared values.
- Building a more sustainable supply chain can result in more efficient operations, lower costs of procurement, and fewer disruptions to the flow of supplies – work with members of the value chain to create innovative solutions to business challenges.
- Promote the work done on sustainability and wider societal impact to create and increase brand awareness amongst all stakeholders.
- Sustainable business practices can improve the safety, wellbeing, productivity and engagement of employees while fostering a stronger corporate culture.

PERFORMANCE MANAGEMENT

2. Organizational performance

REPORTING FRAMEWORKS AND SYSTEMS: TRACK BENEFITS AND COSTS OF SUSTAINABILITY INITIATIVES

Regular monitoring of benefits and costs of sustainability initiatives helps to build greater visibility between the sustainability agenda and its impact on business performance. This also allows for effective performance incentives to be determined and implemented.

TOP TIPS FOR TRACKING BENEFITS AND COSTS

- Formalize the governance and reporting processes by documenting, standardizing and communicating key activities to the Finance team.
- Build the tracking of benefits and costs into business as usual activities and processes, rather than treating tracking activities as ‘added work’.
- Determine the frequency of benefits and costs tracking that makes sense for the organization.
- Use visualization tools and dashboards to help all parts of the organization better interpret and understand the benefits and costs of sustainability initiatives.
# PERFORMANCE MANAGEMENT: PRACTICAL EXAMPLES

## EMPLOYEE PERFORMANCE
- **National Grid:** Strengthening our licence to operate and saving costs through our employee wellbeing programme
- **SSE:** Incentivizing directors through a balanced range of performance measures
- **Royal DSM:** The role of KPIs and remuneration in frameworks in setting ownership in setting ownership and accountability for sustainability
- **Sainsbury’s:** Incorporating our Sustainability Plan values into our Board remuneration policy

## ORGANIZATIONAL PERFORMANCE
- **The Crown Estate:** Defining values, with sustainability at the heart
- **Sainsbury’s:** Integrating sustainability into our governance model
- **Yorkshire Water:** Linking sustainability to monetary and non-monetary impacts and benefits, and developing our Total Impact and Value Assessment
- **Anglian Water:** Agreeing outcomes with predetermined performance levels, framed around both business and sustainability benefits
PERFORMANCE MANAGEMENT:
PRACTICAL EXAMPLES

National Grid: Strengthening our licence to operate and saving money through our employee wellbeing programme

National data indicates that the average business cost of poor mental health is £1,029 per employee. This has broader personal and societal impacts, as well as being a cost and a risk to business continuity, our reputation with our employees and our stakeholders.

We developed a tailored programme to support employees with occupational health and wellbeing advice and support, and rehabilitation services for physical and mental health issues.

For every £1 investment in these services, we are seeing at least a £2 return in reduced sickness absence costs. The combination of the health and support services we provide has positive outcomes, for example employees return ahead of their predicted return to work date.

The predicted return to work date is based on independent international data covering age, work type, sex, type and degree of injury and or illness.

For every £1 investment in our occupational health and wellbeing services, we are seeing at least a £2 return in reduced sickness absence costs.

See the A4S Essential Guide to Social and Human Capital Accounting for further guidance.
PERFORMANCE MANAGEMENT: PRACTICAL EXAMPLES

SSE: Incentivizing directors through a balanced range of performance measures

At SSE, executive directors are incentivized through a balanced range of performance measures reflecting financial, customer, team working and personal performance.

REMUNERATION PRINCIPLES AND STRATEGY

The Remuneration Committee believes it is important that overall remuneration policy is strongly aligned to the purpose and strategy through the following approach:

<table>
<thead>
<tr>
<th>Simplicity</th>
<th>Customer focus</th>
<th>Balance</th>
<th>Delivery</th>
<th>Stewardship</th>
</tr>
</thead>
<tbody>
<tr>
<td>Executive Directors’ pay is made up of just four elements: base salary and benefits, pension, an annual incentive and a long term incentive</td>
<td>Customer service measures are included in both the annual incentive and Performance Share Plan (PSP)</td>
<td>A balanced range of measures used to ensure all aspects of Executive Directors’ overall performance are covered</td>
<td>Dividends and Total Shareholder Return (TSR) measures align Executive Directors’ interests with shareholders</td>
<td>Executive Directors are expected to look to the long term and build and maintain significant personal shareholdings in the business</td>
</tr>
</tbody>
</table>
PERFORMANCE MANAGEMENT: PRACTICAL EXAMPLES

SSE: Incentivizing directors through a balanced range of performance measures

The Committee considers that using a balanced range of performance measures is aligned to SSE's objectives. The performance measures and weightings for the Annual Incentive Plan and the Performance Share Plan will be as detailed below:

<table>
<thead>
<tr>
<th>Annual Incentive Plan</th>
<th>Performance Share Plan</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>PERFORMANCE MEASURE</strong></td>
<td><strong>WEIGHTING</strong></td>
</tr>
<tr>
<td>Financial</td>
<td>50%</td>
</tr>
<tr>
<td>Customer</td>
<td>15%</td>
</tr>
<tr>
<td>Team working</td>
<td>20%</td>
</tr>
<tr>
<td>Personal</td>
<td>15%</td>
</tr>
</tbody>
</table>

**FINANCIAL (50%)**

Financial performance is measured based on Adjusted PBT, DPS Growth and cash flow.

**CUSTOMER (15%)**

Service performance is measured based on the principle of treating customers fairly, with measures taken from a variety of trusted parties for the quality of our service. This includes: the Ombudsman for Energy Service reports, the Citizens Advice Energy Suppliers Performance Reports, Which? and the Institute of Customer Service. The performance measure also reflects the number and duration of power cuts.

**TEAM WORKING (20%)**

Team working measures performance against the ‘SSE SET’ of core values; Safety, Service, Efficiency, Sustainability, Excellence and Teamwork. It incorporates: Accident Frequency Rate, Total Recordable Injury Rate, Energy Supply customer surveys, debt reduction, carbon intensity of electricity generation, connection of renewable sources to the transmission system, Living Wage implementation and employee engagement.

**PERSONAL (15%)**

Performance against individual objectives based on: delivery of customer, safety and operational performance; effective communication channels with key stakeholders; plans for investment and growth; development of effective cost control and efficiency programmes; maintenance of a strong balance sheet; and ensuring that employees remained engaged and motivated to deliver for SSE.
PERFORMANCE MANAGEMENT: PRACTICAL EXAMPLES

Royal DSM: The role of KPIs and remuneration frameworks in setting ownership and accountability for sustainability

When we launched our new strategy, sustainability was identified as a key business and growth driver. To be able to track our performance against the 2015 vision we developed a set of Key Performance Indicators (KPIs) that incorporated our sustainability aspirations. These were developed to be reported externally as well as to be used internally to steer the business. A selection of these KPIs that are well established within the business are used in performance management and are linked to the variable pay of the management Board and employees.

DSM Managing Board Total Direct Compensation (on target)

<table>
<thead>
<tr>
<th>Element</th>
<th>Vehicle</th>
<th>Performance targets &amp; measures</th>
<th>Target pay-out (% of ABS)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed</td>
<td>Annual base salary (ABS)</td>
<td>Cash</td>
<td>N/A</td>
</tr>
<tr>
<td>Variable</td>
<td>Short Term Incentive (STI) (minimum performance threshold for STI pay-out set by Supervisory Board)</td>
<td>Cash</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1. Financial:</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Adjusted EBITDA</td>
<td></td>
<td>12.5%</td>
</tr>
<tr>
<td></td>
<td>• Gross Free Cash Flow</td>
<td></td>
<td>10%</td>
</tr>
<tr>
<td></td>
<td>• Organic Net Sales Growth</td>
<td></td>
<td>2.5%</td>
</tr>
<tr>
<td></td>
<td>2. Sustainability:</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Brighter Living Solutions</td>
<td></td>
<td>5%</td>
</tr>
<tr>
<td></td>
<td>• Employee Engagement Index</td>
<td></td>
<td>5%</td>
</tr>
<tr>
<td></td>
<td>• Safety Performance</td>
<td></td>
<td>5%</td>
</tr>
<tr>
<td></td>
<td>3. Individual</td>
<td></td>
<td>10%</td>
</tr>
<tr>
<td>Long Term Incentive (LTI)</td>
<td>Performance Shares</td>
<td>1. Financial:</td>
<td>25%</td>
</tr>
<tr>
<td></td>
<td>• Relative Shareholder Return (TSR)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Return on Capital Employed (ROCE) growth</td>
<td></td>
<td>25%</td>
</tr>
<tr>
<td></td>
<td>2. Sustainability:</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Energy Efficiency Improvement (EEI)</td>
<td></td>
<td>25%</td>
</tr>
<tr>
<td></td>
<td>• Greenhouse Gas Emissions (GHGE) Efficiency improvement</td>
<td></td>
<td>25%</td>
</tr>
</tbody>
</table>

*STI deferral into shares: A mandatory (25%) and a voluntary proportion (up to a total maximum of 50%) of the actual STI amount earned in a year is deferred into DSM shares with a three year holding period. This is linked to a one-for-one matching award on the total deferred amount under the condition that predefined performance targets and measures are met at the end of the three year vesting period.

"The development of the KPIs, management confidence in them (i.e. reliability and accuracy) as well regular internal management reporting means that we can use them as part of our performance management processes."

Bert Steinbusch, Project Director Finance Transformation, Royal DSM
PERFORMANCE MANAGEMENT: PRACTICAL EXAMPLES

Sainsbury’s: Incorporating our Sustainability Plan values into our Board remuneration policy

REMUNERATION PRINCIPLES

Sainsbury’s colleagues are central to the company’s ongoing success and the company’s overall reward strategy supports this. Our objective is to have a fair, equitable and competitive total reward package that supports our vision of being the most trusted retailer where people love to work and shop, encourages colleagues to perform in the ways that deliver great service for customers, drives sales and provides opportunities for colleagues to share in Sainsbury’s success. This overall reward strategy is the foundation for the remuneration policy for senior executives.

The over arching objectives of the remuneration policy are to ensure rewards are performance based and encourage long term shareholder value creation. The remuneration policy for senior executives is based on these five principles.

Sainsbury’s values are:
- A great place to work
- Respect for our environment
- Sourcing with integrity
- Living healthier lives
- Making a positive difference to our community

Linked to business strategy

Supports Sainsbury’s values

Drives long term growth

Secures high calibre leaders

Encourages share ownership

- Specifically built around our strategy
- Aligned to the Company’s values as outlined in our Sustainability Plan
- Encourages the right behaviours to deliver long term growth
- Recruit and retain high calibre leaders who can deliver operational excellence
- Enables executives to become shareholders in the Company

Personal objectives and KPI based remuneration frameworks
PERFORMANCE MANAGEMENT: PRACTICAL EXAMPLES

Sainsbury’s: Incorporating our Sustainability Plan values into our Board remuneration policy

PERFORMANCE RELATED PAY

The Committee believes it is important that a significant portion of the Executive Directors’ package is performance related and the performance conditions applying to incentive arrangements support the delivery of the Company’s strategy and the long term sustainable success of the Company. The specific metrics incorporated into the annual bonus, Deferred Share Award and Future Builder are built around the overall strategy and our key priorities. Remuneration for Executive Directors is made up of the following:

- Base salary
- Benefits
- Pension
- Annual bonus
- Deferred Share Award
- Long Term Incentive Plan

The Annual Bonus and Deferred Share Award include elements that incorporate sustainability performance.

Further enhance our differentiated food proposition

Grow General Merchandise and Clothing and deliver synergies

Diversify and grow Sainsbury’s Bank

Continue cost savings and maintain balance sheet strength

See the next page for further information on A, B, C
## Performance Management: Practical Examples

### Sainsbury’s: Incorporating our Sustainability Plan values into our Board remuneration policy

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>A</strong> Customer focused and individual performance</td>
<td>The customer focused measure is based on a customer satisfaction index, which is a survey operated by a third party, that assesses the satisfaction of Sainsbury’s customers shopping in store or online. Individual performance objectives are set annually for each Executive Director and are reviewed by the Committee. These objectives cover a variety of financial and operational targets that contribute to the achievement of longer term strategic goals; some of these objectives relate, either directly or indirectly, to the company’s value.</td>
</tr>
<tr>
<td><strong>B</strong> Deferred Shared Award</td>
<td>The Deferred Share Award (‘DSA’) is used to drive performance against a diverse range of key financial and strategic scorecard measures and rewards Executive Directors for achieving the short term objectives that will directly lead to building the sustainable, long-term growth of the Company and support Sainsbury’s values. Executive Directors can achieve a bonus of up to 35% - 40% of salary depending on combined performance of the customer focused and individual performance measures. They can earn up to 90% -110% of salary based on combined performance across the DSA measures.</td>
</tr>
</tbody>
</table>
| **C** Strategic Goals | The Strategic Goals measure incorporates: proposition, channels, price, customers, colleagues and values. Some examples of performance highlights which were taken into account for Executive Directors DSA reward in 2016/17 are:  
- We were named Grocer 33 Store of the Week 17 times in the year, the most of any of the 'big four' supermarkets  
- We were awarded a third consecutive Investors in People Gold accreditation |
PERFORMANCE MANAGEMENT: PRACTICAL EXAMPLES

The Crown Estate: Defining values, with sustainability at the heart

WHO WE ARE

The Crown Estate is a £13bn real estate business, which specialises in commercial property in central London, prime regional retail and offshore wind. Established by an Act of Parliament, as an independent commercial business, it returns 100% of its annual profits to the Treasury for the benefit of the public finances. This has totalled £2.6bn over the last ten years.

OUR PURPOSE AND VALUES

Our purpose, creating brilliant places through conscious commercialism, sits at the heart of everything we do. It is what drives us to take a long term view, to see the bigger picture, identify opportunities for growth and create environments that are relevant, attractive and profitable. Our purpose, in turn reflects our three values: commercialism, integrity and stewardship.

Commercialism
We are a business driven by a strong set of values. We mean them, we are proud of them and we are respected for them by the people we work with and in the wider community.

Integrity
Integrity and trust are behaviours more important than ever in today’s business world, and across our four portfolios we deliver commercial return with integrity.

Stewardship
Stewardship is deeply engrained in our culture; because of our history and because of our heritage, we act at all times as good stewards of the properties we manage. So our commercial approach is supported by a clear recognition of our stewardship responsibilities.

Our values provide the backbone of how we measure our performance, which we do using what we call our Total Contribution methodology. Total Contribution demonstrates the value we create by measuring the impact of our activity on the capitals on which we depend.
UNDERSTANDING OUR TOTAL CONTRIBUTION

Sustainable growth is central to our business resilience; it underpins our competitive advantage and outperformance of our benchmark. To enable us to understand the economic, social and environmental contribution that our business delivers to the UK, we developed our Total Contribution methodology.

Total Contribution equips us with a better understanding of the wider impacts of our activities, both positive and negative, and the broader value we create. This includes how our decisions affect our capitals, which are the factors the business draws upon to deliver its commercial performance, such as our financial and physical resources, our know how and our networks. This helps us to build trust and strengthen our relationships as well as improve decision making.

WHAT WE RELY ON

When we launched our first Total Contribution report in 2013, we reported against a limited number of indicators across the triple bottom line. They each had different units of measurement (e.g. tonnes of CO₂e and ㎥ of water). We realized that to understand better our value we needed to increase the number of both positive and negative indicators and find a common unit of measurement to provide consistency and a means of comparability.

In our second Total Contribution report, published in 2017, we reported on the impacts of our activity on six capitals:

- **Financial resources**: available to us to run and grow our business
- **Physical resources**: property, plant and equipment we own and use
- **Natural resources**: that we manage and use
- **Our people**: the skills, competencies and experience of our employees
- **Our know how**: our collective expertise and processes
- **Our networks**: our relationships with all of our stakeholders including customers, communities and business partners

These all link directly back to our values. We report on direct activity (carried out by ourselves), indirect activity (commissioned by us but carried out by our supply chain) and enabled activity (carried out by our customers on our land).

THE VALUE WE CREATE

We consistently create significant value for the UK taxpayer, and tangible, long term value for all of our stakeholders. We use Total Contribution methodology to measure our value:

- **Financial resources**: £320m
- **Physical resources**: £118m
- **Natural resources**: £27m
- **Our people**: £1m
- **Our know how**: £370m
- **Our networks**: £15m

See the Total Contribution Report for further details
PERFORMANCE MANAGEMENT: PRACTICAL EXAMPLES

Yorkshire Water: Linking sustainability to monetary and non-monetary impacts and benefits, and developing our Total Impact and Value Assessment

VALUING THE BENEFITS OF MANAGING THE WATER QUALITY CATCHMENT AREA

Yorkshire Water undertook a natural capital valuation to inform the choice of investment solutions that would most effectively ensure drinking water quality for our customers—the choices were either capital investment in a water treatment works or operational investment to help address the problem at source in the catchment. It was determined that monetary valuation would most effectively facilitate options analysis and integration into cost benefit analysis. The quality of some of Yorkshire Water’s important water sources has deteriorated over recent years due to land management practices, wildfires and air pollution. This has required the introduction of capital and energy intensive processes to provide extra treatment to the raw water, with associated financial and environmental costs.

We worked in partnership with Natural England on a pilot project to assess the potential financial benefits and costs both to the company and society of different investment solutions to help identify the most sustainable, long term approach.

The project sought to estimate the economic value of the benefits provided under a range of land management scenarios. The study used government guidelines on valuation (Value Transfer Guidelines) to assess quantitatively the different scenarios.

Research literature was used to identify financial values for the benefits and how these would change under the different scenarios. Three ‘benefits’ were considered based on their likely materiality and because they were more readily quantifiable—these were the ability of the land to: store carbon; protect water quality and maintain levels of biodiversity.

The findings helped shape our planned capital investment programme by providing evidence to show that catchment management is a cost beneficial method for protecting drinking water quality. The results revealed that for every £1 spent by Yorkshire Water to improve the land, society would benefit by an estimated £3 through lower water costs and improved carbon storage, and for every £1 not spent (or ‘saved’), society was likely to lose an estimated £6.61. The pilot study also informed the UK government’s approach to assessing ecosystem services.

Building on the learning we took from this catchment management valuation, we have continued to work with a range of maturing ‘sustainable accounting’ techniques. By bringing ecosystem services assessments together with other techniques, like our early adoption of environmental profit and loss accounting and the Natural Capital Protocol, we are working to develop and embed a practical approach that helps advance how we monitor, report, manage and enhance our impact and value to the society we serve. We call this Total Impact and Value Assessment. By looking at a range of economic, environmental and social issues, we are considering our impacts and associated economic value like never before. For us, this is about considering value beyond the traditional financial perspective to help business focus on what really matters to people.

“Whilst more development is needed, I am confident that we and others can start to deploy these maturing sustainable accounting approaches to inform decision making that enhances value for customers, shareholders and other stakeholders. In fact, I see an imperative for us and others to broaden our understanding of value creation, and develop new approaches that can effectively ensure the sustainability of our businesses and the society we serve.”

Liz Barber, Group Director of Finance and Regulation, Kelda Group (Yorkshire Water)
Anglian Water: Agreeing outcomes with predetermined performance levels, framed on both business and sustainability benefits

Anglian Water’s goals are aligned to ten outcomes agreed with customers, which reflect both business and sustainability outcomes. Each outcome has a predetermined committed performance level. Exceeding the committed performance level can lead to reputational or financial rewards, whereas underachieving can lead to reputational or financial penalties.

Examples of impacts and benefits measurements set out by the outcome are shown on the right.

The benefits of this approach are that the interaction and agreement with customers gives us good insight into what is important to our customers, and decision making can be aligned to factors that are priorities for both the business and customers.

OUTCOME DELIVERY INCENTIVE (ODI) REWARDS AND PENALTIES

Our ODIs are financial, reputational, or relate to special schemes we must deliver. The diagram below shows the impact that each ODI contributes to the total reward or penalty we could face over the asset management period.

**Relative ODI Rewards/Penalties (Total)**

- Intermittence
- Pressure
- Flooding
- Water quality contact
- Internal flooding
- Water quality contact
- External flooding

**Top 10 by financial impact**
- Serviceability
- Service incentive mechanism (SIM)
- Interruptions to supply
- Leakage
- Pollution incidents
- Bathing waters
- Low pressure
- Internal flooding
- Water quality contacts
- External flooding

**Other financial, lower impact**
- Per property water use
- Mean zonal compliance
- Value for money perception (water)
- Value for money perception (sewerage)
- Fairness of bills perception
- Affordability perception
- Single supplies

**Special case (financial impact)**
- Sustainable sewerage schemes
- Qualitative SIM
- Customer Satisfaction Index
- Hosepipe bans
- Security of supply index (SOSI) dry year
- Security of supply index (SOSI) critical year
- Favourable Sites of Special Scientific Interest
- Operational carbon
- Embodied carbon
- Community perception

**TOTAL MAXIMUM PENALTY – £632M**

**TOTAL MAXIMUM REWARD – £153M**
TECHNOLOGY AND DATA

STRATEGIC PLANNING, BUDGETING AND FORECASTING
TECHNOLOGY AND DATA

In order for organizations to track their performance successfully, and to allow effective strategic planning, budgeting and forecasting, they need to define data requirements based on materiality and the levels of frequency, granularity and accuracy required. Most organizations have an abundance of data, much of which is not used to help inform business decisions. Having the right technology and system capability also helps to reduce manual working within the finance team and across the business.

Finance teams tend to be very familiar with finance and accounting modules of ERP systems, but less so with systems or modules that have the capability to collate and analyse sustainability related data. In order to account for sustainability effectively, finance teams need access to the right data on a timely basis. Market options include sustainability modules for ERP systems or stand alone sustainability data systems, with a variety of functionalities. IT, finance and sustainability teams need to work together to ensure that relevant, accurate data is available to support strategic planning, budgeting, forecasting and decision making.

Presented below is a structural approach to help finance teams navigate the concept of integrated data and systems. Guidance and case studies are presented on the following pages.

DATA REQUIREMENTS
1. Determine data requirements for setting strategic priorities and monitoring progress against them
2. Consider opportunities, risks and challenges of implementing a big data approach

SYSTEM AND FUNCTIONALITY REQUIREMENTS
3. Establish system and functionality requirements for efficient access to required data

CURRENT SYSTEMS
4. Assess your current systems and determine what changes are needed

COMMON PITFALLS
5. Avoid common pitfalls in collecting information and overcome common challenges in integration

What did organizations say were their key technology and data challenges?
How will this guide help?
## TECHNOLOGY AND DATA: KEY CHALLENGES

<table>
<thead>
<tr>
<th>Organizations said…</th>
<th>We need…</th>
</tr>
</thead>
<tbody>
<tr>
<td>“We struggle to find sufficient available external information with enough</td>
<td>Guidance on how to unlock strategically valuable data, for example through</td>
</tr>
<tr>
<td>granularity to help inform strategic planning.”</td>
<td>access to internal and external big data.</td>
</tr>
<tr>
<td>“We find ourselves focusing on metrics that are easiest to measure rather than</td>
<td>Guidance on how to assess what is most material to the business from a</td>
</tr>
<tr>
<td>those that are most important.”</td>
<td>sustainability perspective.</td>
</tr>
<tr>
<td>“We struggle with integration due to lack of, or abundance of, data with no</td>
<td>Guidance on how to define and develop the right KPIs for the business, and</td>
</tr>
<tr>
<td>meaningful filtering or analytical ability.”</td>
<td>how to model cost information for the budgeting process.</td>
</tr>
<tr>
<td>“Integrating data is currently a very manual process. Adapting or upgrading</td>
<td>Suggestions for criteria which should be considered when upgrading or</td>
</tr>
<tr>
<td>systems would be a challenging undertaking. The business case to invest in new</td>
<td>selecting a new system.</td>
</tr>
<tr>
<td>systems is not straightforward – it’s not seen as critical, and even once agreed,</td>
<td></td>
</tr>
<tr>
<td>managing change is never easy.”</td>
<td></td>
</tr>
<tr>
<td>“There is a lack of a standard approach or framework to support the collation and</td>
<td>Guidance on how to develop an approach for collecting and reporting</td>
</tr>
<tr>
<td>reporting of sustainability information.”</td>
<td>sustainability information.</td>
</tr>
<tr>
<td>“We are not sure how we can better improve the quality of our data and enable</td>
<td>Guidance on how to break information down at business unit level, and</td>
</tr>
<tr>
<td>meaningful benchmarking between business units along our value chain, and against</td>
<td>determine the level of accuracy, granularity and timeliness required for</td>
</tr>
<tr>
<td>our peers.”</td>
<td>different types of data.</td>
</tr>
</tbody>
</table>
TECHNOLOGY AND DATA

1. Determine data requirements for setting strategic priorities and monitoring progress against them

**KEY STEPS**

1. Start with strategic priorities and identify the key corresponding internal stakeholders and decision makers.

2. Determine material factors, including operations, initiatives, innovations, risks, opportunities and competitive advantages relevant to the strategic priorities.

3. Consider internal, value chain and market data requirements for strategic planning, performance management and decision making in relation to these, including monetary and non-monetary data.

4. Determine the different data requirements for the different decision making levels and agree balanced scorecards to meet the needs of each.

**PRACTICAL EXAMPLE**

At Sainsbury’s, we defined the measures and metrics required to evaluate and assess our performance. See full case study for further information.

Also consider whether the following should be incorporated:
- Future data requirements (if these can be predicted)
- Data from strategically important stakeholder groups

See page 146 for further guidance on establishing and treating relative data importance.
**TECHNOLOGY AND DATA**

1. Determine data requirements for setting strategic priorities and monitoring progress against them

**PRIORITIZE AND FILTER THE DATA**

An abundance of data can make it difficult for an organization to distinguish the most relevant metrics from the ‘noise’. An organization’s business data (including sustainability data) should be prioritized based on its criticality to the execution of organizational strategy and the management of business performance.

**Importance of data**

- **Essential to strategy development and execution**
- **Essential to managing business performance**
- **Highly useful to strategy development and execution**
- **Highly useful to managing business performance**
- **Useful to strategy development and execution**
- **Useful in managing business performance**
- **Not essential to strategy development and execution**
- **Useful in managing business performance**

**Treatment of data**

- **Ensure immediate, on demand availability to users**
- **Ensure a robust control environment and treat material sustainability data in line with financial data**
- **Prioritize integrity and accuracy of data based on materiality**
- **Integrate fully with core performance management and reporting systems**
- **Ensure timely availability to users**
- **Safeguard integrity and accuracy of data**
- **Integrate substantially with core performance management and reporting systems**
- **Ensure availability at defined intervals to users**
- **Review integrity and accuracy of data**
- **Integrate as appropriate with core performance management and reporting systems**
- **Ensure availability on as needed basis**
- **Consider integrity and accuracy of data**
- **Integrate as appropriate with core performance management and reporting systems**
TECHNOLOGY AND DATA

2. Consider opportunities, risks and challenges of implementing a big data approach

WHAT IS BIG DATA?

The term “Big Data” has been rising in popularity in recent years, but the boundaries of what can be considered big data can be easily blurred.

Big Data isn’t so called on size alone but instead is characterized by the “three V’s”: velocity, volume and variety. These three characteristics make big data hard to manage with traditional data management techniques. However, by utilizing new technologies, the rewards of successfully understanding big data can be unlocked.

A REVOLUTION IN DATA

The explosion of big data is due to the incredible leaps forward in technology and processing power. New developments have created the so called Internet of Things (for example smart phone data and internet clickstream data) and this adds to the complexity and quantity of data that is readily available.

Effectively collecting and processing relevant data can lead to greater insights, increased efficiency and enhanced risk management.

BIG DATA AND SUSTAINABILITY

To understand how big data can enhance integration of sustainability into financial decision making, it is useful to consider how big data is being used in other areas of the organization. There are generally three main uses of big data.

TO GAIN INSIGHT
Better understand current activities

TO PREDICT THE FUTURE
Better understand how future events will affect the company

TO AID AUTOMATION
Automate decision making and reduce workload

These activities can be used to add value to an integrated strategic planning, budgeting and forecasting process.

EXAMPLE
Complex supply chains with complex data from many different sources can be understood and visualized for use by decision makers

EXAMPLE
To analyse and visually map assets exposed to physical climate risk, to estimate value and operations at risk across different geographies

EXAMPLE
Installing smart appliances coupled with a smart power grid that can “talk” to each other and create efficiencies with automated control
## TECHNOLOGY AND DATA

### 2. Consider opportunities, risks and challenges of implementing a big data approach

#### OPPORTUNITIES AND RISKS

<table>
<thead>
<tr>
<th>OPPORTUNITIES</th>
<th>RISKS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Easier integration and analysis of financial and sustainability data for planning and performance management purposes.</td>
<td>Data can be easy to misinterpret, e.g. misrepresentation of data population, variation in data accuracy or suitability for predictive use.</td>
</tr>
<tr>
<td>Visualization of big data can provide greater insights from and links between financial and sustainability data to aid decision making.</td>
<td>Data protection risk is increased by the breadth of data that is harvested through big data initiatives.</td>
</tr>
<tr>
<td>Big data from supply chains can enhance monitoring of social and environmental data relevant to supply agreements and associated commercial decisions.</td>
<td>Use of some types of big data can be inconsistent with the values of the organization. For example, in relation to customer and user privacy or the social implications of the use of artificial intelligence.</td>
</tr>
<tr>
<td>Complex networks of social, environmental and financial data, often with many variables and interdependencies (e.g. where harvested from the internet of things) can be analysed quickly and accurately to provide insights, aid decision making and/or obtain competitive advantage.</td>
<td>Bespoke big data infrastructure can be costly.</td>
</tr>
</tbody>
</table>

There can also be risks associated with not using big data. For example, regulators are increasingly using big data to analyse companies against certain sustainability criteria. This may mean that key stakeholders have better data about the organization than the organization itself.

*Systems that can process some forms of complex big data are readily available from accounting application providers, for example, HANA by SAP and Oracle Big Data.*
TECHNOLOGY AND DATA

2. Consider opportunities, risks and challenges of implementing a Big Data approach – Practical application

VISUALIZATION: ILLUSTRATIVE EXAMPLE

Many organizations have a wide geographical spread of assets and infrastructure for their own operations and key supply chain partners. These will be exposed to physical climate risk to varying degrees, e.g. those in coastal regions or close to river flood plains will often be at higher risk. Big data visualization applications can be used to analyse climate data across the key operational geographies to determine and visualize value at risk. The illustrative example below is for an organization’s assets in the Hellenic region, showing exposure to climate risk and value at risk in the three key areas of operation.

PRACTICAL EXAMPLE

We have used big data to develop our Cost of Production model, aimed at protecting dairy farm businesses from input and output market volatility. The finance and commercial teams have actively led the Cost of Production (COP) initiative in conjunction with the agriculture team. The model is a financially open book cost based approach, based on data collected from the 320 Sainsbury’s Dairy Development Group farms. The COP model has served to halve price volatility for our farmers and the data collected evidences that despite our cows producing more milk, they are healthier.

See full case study for further information

Exposure to hazard
- High
- Medium
- Low
TECHNOLOGY AND DATA

3. Establish system and functionality requirements for efficient access to required data

There are a number of factors that can be useful to consider, depending on the strategic importance of the data and needs of the business.

**RELIABILITY**
- Embedded preventative and monitoring controls
- Password protection and tiered access security
- Certified data security
- Audit trail and auditor access
- Data integrity checks
- System reliability
- Embedded accountability

**FUNCTIONALITY**
- Ability to manage qualitative, quantitative and monetary data, and present in an integrated manner
- Multiple year data and target setting functionality
- Configurable outputs for different audiences
- Data analysis with customizable charts, tables, dashboards and reports
- Shadow pricing platform
- Monetization of social, human and natural capital
- Live stream and on demand data availability
- Forecasting, scenario and sensitivity analysis functionality
- Ability to modify measurement metrics
- Advanced analytical capability for ‘big data’

**COMPATIBILITY**
- Integration with existing in house systems, including finance
- Integration with suppliers’ and customers’ systems, where appropriate
- Ability to export to CSV, Excel etc.
- Integration with investor platform

**SUSTAINABILITY**
- Green IT across IT infrastructure

Determine which factors are critical or desirable, and which are non essential.

See page 151 for further guidance

See page 152 for further guidance

See page 153 for further guidance

See page 156 for further guidance
TECHNOLOGY AND DATA

3. Establish system and functionality requirements for efficient access to required data

**IMPROVE DATA QUALITY**

Improving the quality of sustainability related data inputs into finance systems and processes allows organizations to build more robust planning, budgeting, and forecasting capabilities. Organizations can adopt various measures to enhance data quality, set out in this diagram.

**DATA QUALITY**

- **TIMELINESS**
  Understand timing of users’ information needs, and ensure data can be delivered when needed.

- **RELIABILITY**
  Establish automated validation rules, perform periodic audits of data accuracy and reduce need for, or frequency of, manual interventions.

- **UNDERSTANDABILITY**
  Consider whether the data is meaningful to the audience and use plain language to communicate the definitions of data elements to users.

- **COMPLETENESS**
  Capture specific data requirements with business users and check the information collated for errors, outliers and missing data.

- **COMPARABILITY**
  Be consistent in the collection of data to enable comparisons and benchmarking of performance between business units and reporting periods. Use recognized standards whenever feasible to facilitate comparison with peers and enhance usefulness to investors and other external stakeholders.
3. Establish system and functionality requirements for efficient access to required data

HOW DIFFERENT DATA TYPES CAN IMPACT FUNCTIONALITY CONSIDERATIONS

Collation of data, and monitoring and analysing performance, is more reliable if performed within a well controlled IT environment, incorporating tiered access controls, integrity checks and instant analysis functionality. Where an impact or performance measure can be presented in financial terms, this can provide additional valuable information for the business.

From a strategic planning, budgeting and forecasting perspective, quantitative and monetary data is often most valuable, and thus the reliability and accessibility of data becomes very important. Accurate and timely data and analysis are essential to support many strategic and budgetary decision making processes, and for monitoring progress against those decisions.

<table>
<thead>
<tr>
<th>QUALITATIVE</th>
<th>QUANTITATIVE</th>
<th>MONETARY</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Useful for:</strong></td>
<td><strong>Useful for:</strong></td>
<td><strong>Useful for:</strong></td>
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<tr>
<td>Written explanations describing importance, progress or improvement</td>
<td>Quantitative measurement</td>
<td>Developing a business case for an investment decision</td>
</tr>
<tr>
<td>Qualitative measurement</td>
<td>Comparison against targets and non monetary budgets</td>
<td>Making trade offs between different areas of impact</td>
</tr>
<tr>
<td>Accountable review comments</td>
<td>Forecasting and projections</td>
<td>Assessing the financial impact of risks and opportunities</td>
</tr>
<tr>
<td>Examples:</td>
<td>Scenario analysis</td>
<td>Comparison against financial budgets</td>
</tr>
<tr>
<td>Red, amber, green ratings</td>
<td>Greenhouse gas emissions</td>
<td>Cost benefit analysis</td>
</tr>
<tr>
<td>Supplier audit outcomes</td>
<td>Resource use</td>
<td>Forecasting and projections</td>
</tr>
<tr>
<td>Social value outcomes</td>
<td>Social value outputs</td>
<td>Scenario analysis</td>
</tr>
<tr>
<td><strong>Functionality considerations:</strong></td>
<td><strong>Functionality considerations:</strong></td>
<td><strong>Functionality considerations:</strong></td>
</tr>
<tr>
<td>Red, amber, green rating collation and analysis</td>
<td>Real time data analysis</td>
<td>Real time data analysis</td>
</tr>
<tr>
<td>Narrative fields</td>
<td>Data integrity checks</td>
<td>Advanced analytical capability for 'big data'</td>
</tr>
<tr>
<td>Issue escalation</td>
<td>Advanced analytical capability for 'big data'</td>
<td>Performance variance analysis</td>
</tr>
<tr>
<td>Qualitative trend analysis</td>
<td>Performance variance analysis</td>
<td>Year on year comparisons</td>
</tr>
<tr>
<td>Modular integration with suppliers</td>
<td>Visual analysis e.g. graphs and maps</td>
<td>Visual analysis e.g. graphs and maps</td>
</tr>
<tr>
<td>Visualization</td>
<td>Scenario analysis</td>
<td>Shadow pricing platform</td>
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</tbody>
</table>
TECHNOLOGY AND DATA

3. Establish system and functionality requirements for efficient access to required data

SUSTAINABLE ERP SYSTEMS

The ability to access and analyse key sustainability data alongside financial data is vital if strategic planning, budgeting and forecasting decisions are to integrate sustainability effectively. Traditional ERP systems may not be able to manage the rich variety of data relevant for an integrated approach. One path to an integrated information system, which will collect, integrate, automate and monitor sustainability information, is a Sustainable ERP (S-ERP) system.

An S-ERP system can integrate sustainability considerations across the value chain, configured to the organization’s strategic and operational requirements. For example, a strategic objective to improve supply chain resilience may require an S-ERP system’s procurement module to incorporate data relating to the provenance and certification of raw materials, climate risk by geography of key suppliers, social considerations such as risk of child labour or modern slavery, and/or embodied carbon arising from extraction, manufacturing and transportation. This data is all relevant for effective decisions relating to the management of the corresponding procurement budgets and forecasts. The same logic can be applied to every module of a traditional ERP system, using integrated data and analysis to drive effective financial and operational decision making.

An integrated information system allows organizations to:

- Take a proactive approach to ensure ongoing and early consultation at the early stages of business requirements analysis
- Link environmental and social management to the economic success of the organization
- Incorporate sustainability into new products’ requirements
- Meet integrated data requirements for finance teams to support strategic planning, budgeting, forecasting and decision making

PRACTICAL EXAMPLE

At Unilever, we use S-ERP to support our sustainable supply chain programme.

See full case study for further information

PRACTICAL EXAMPLE

At Danone, we use S-ERP to manage sustainability data collection, reporting and analytics.

See full case study for further information
4. Assess your current systems and determine what changes are needed

There are a number of factors to consider at the strategic planning and budgeting level to identify if significant changes to IT systems are needed:

**Ease of compatibility with current systems**
- Consider the compatibility of current systems with the potential solution(s)

**Budget**
- Establish the budget available for system changes
- Determine if access to wider budgets can be unlocked
- Identify potential financing options

**Transition costs**
- Incorporate transfer of data, implementation, integration and training into the budgeted costs

**Critical and desirable factors**
- Determine which critical factors are already in place
- Identify what potential options there are to fill the gaps
- Analyse where these options provide desirable factors

**Change management**
- Consider the transitional impact of the change. Will it mean short term disruption? How will it fit into the annual cycle?

**Skills**
- Consider whether there are the necessary skills in house for:
  - Specification and selection of the IT system changes
  - Managing bespoke build or outsourcing, as needed

**BUSINESS CASE** Build the business case for IT system integration

See page 147 for practical considerations to feed into selection criteria
### TECHNOLOGY AND DATA

#### 4. Assess your current systems and determine what changes are needed

**PRACTICAL CONSIDERATIONS TO FEED INTO SELECTION CRITERIA**

Once critical requirements of reliability, functionality, compatibility and sustainability have been satisfied, there are a number of practical requirements to consider.

<table>
<thead>
<tr>
<th>Selection criteria</th>
<th>Key considerations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scalability and changeability</td>
<td>• Determine whether the system is capable of supporting the growth of the organization and responding to changes in the business environment, including adapting to evolving environmental and social factors</td>
</tr>
<tr>
<td>Ease of implementation</td>
<td>• Determine whether a turnkey solution meets the organization’s monetary and non monetary (e.g. environmental and social) data requirements</td>
</tr>
<tr>
<td></td>
<td>• Assess the extent to which a customized solution would require modifications to meet the organization’s monetary and non monetary data requirements</td>
</tr>
<tr>
<td>Ease of use</td>
<td>• Evaluate a solution’s user friendliness and interface intuitiveness, including whether monetary and non monetary data can be efficiently accessed, analysed, and manipulated</td>
</tr>
<tr>
<td>Vendor support</td>
<td>• Consider the extent to which the vendor is able to provide implementation and post implementation support, including whether the vendor has experience and capabilities in integrating sustainability data</td>
</tr>
</tbody>
</table>
**TECHNOLOGY AND DATA**

## 4. Assess your current systems and determine what changes are needed

### A POTENTIAL APPROACH TO GREEN IT

As part of an overall energy and greenhouse gas reduction programme, implementing a Green IT strategy can have significant merit. From a financial perspective, the project can be treated as any other Capex project (for further guidance see the *A4S Essential Guide to Capex*) and will have financial outlays as well as financial, energy and greenhouse gas savings. The tool below suggests some factors to consider:

<table>
<thead>
<tr>
<th>Baseline assessment</th>
<th>Potential actions</th>
<th>Appraising options</th>
<th>Measuring impact</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Set scope</strong></td>
<td><strong>IT environment examples:</strong></td>
<td><strong>The organization will need to determine which initiatives bring the greatest cost effective benefit, with lowest detrimental impact (e.g. IT waste, processing speeds).</strong></td>
<td><strong>In measuring impact, consider the:</strong></td>
</tr>
<tr>
<td>PCs, laptops, tablets, phones, photocopiers, printers, multifunction devices, servers, datacentres, IT equipment cooling, IT waste (in house and outsourced)</td>
<td>• Retiring legacy systems</td>
<td>• Capital expenditure outlay</td>
<td></td>
</tr>
<tr>
<td><strong>Determine performance:</strong></td>
<td>• System and data centre consolidation</td>
<td>• Operating expenditure savings (absolute, relative and per kWh, tCO₂e)</td>
<td></td>
</tr>
<tr>
<td>• Energy use</td>
<td>• Landscape virtualization</td>
<td>• NPV, IRR and payback period</td>
<td></td>
</tr>
<tr>
<td>• GHG emissions</td>
<td>• Archiving of legacy data</td>
<td>• Energy savings</td>
<td></td>
</tr>
<tr>
<td>• Energy cost</td>
<td>• Digitalization of paper based processes</td>
<td>• Greenhouse gas savings</td>
<td></td>
</tr>
<tr>
<td>• Cost incl. shadow carbon price</td>
<td>• Sustainable IT asset procurement and disposal</td>
<td>• Carbon intensity of energy</td>
<td></td>
</tr>
<tr>
<td>• Processing speed</td>
<td>• Video conferencing</td>
<td>• Renewable energy generated/ sourced</td>
<td></td>
</tr>
<tr>
<td><strong>Consider:</strong></td>
<td><strong>Energy and GHG examples:</strong></td>
<td>• Resource recovery/ IT waste from the project</td>
<td></td>
</tr>
<tr>
<td>• Embedding energy metering to pull consumption data from devices</td>
<td>• Renewable energy generation/sourcing</td>
<td>• Changes in processing speeds (if relevant)</td>
<td></td>
</tr>
<tr>
<td>• Understanding how hosting providers allocate energy use between customers</td>
<td>• Cooling optimization</td>
<td>• Relative success of initiatives, e.g. behavioural change</td>
<td></td>
</tr>
<tr>
<td>• Where standardized estimation techniques may be useful</td>
<td>• Configuring power management on devices</td>
<td>• Geographical variations</td>
<td></td>
</tr>
</tbody>
</table>

The treatment of IT waste will have financial and resource recovery/waste elements.
5. Avoid common pitfalls in collecting information and overcome common challenges in integration

COMMON PITFALLS IN IDENTIFYING, COLLECTING AND INTEGRATING DATA IN STRATEGIC PLANNING, BUDGETING AND FORECASTING

- Large quantities of sustainability data are collected without first understanding their relevance to the organization’s strategic objectives and desired outcomes.
- The IT team generally lack awareness of the organization’s key sustainability performance measures and are therefore not actively engaged in the identification and integration of sustainability data into strategic planning, budgeting and forecasting processes.
- Sustainability data parameters are neither clearly defined, nor clearly communicated, throughout the organization, resulting in a lack of transparency to users of the data.
- The sustainability information collection process does not fully leverage the automation and integration functionality of existing systems and software, often resulting in data that resides outside of the core data and systems infrastructure.
- Information requirements for the strategic planning, budgeting and forecasting processes are not regularly reviewed, resulting in employees collecting unnecessary information or reviewing, processing and creating unnecessary documents.
- System selection does not consider flexibility of the system to meet future needs of the business.
- Project management for the implementation/integration is not clearly scoped, or effectively managed.
- Collaboration between IT, sustainability and finance is insufficient in specifying system requirements and selecting solutions.
- Weaknesses in the control environment prior to data input into the system and/or where data is extracted from the system and manipulated.
- Insufficient integration of systems, prohibiting efficient integrated management reporting.
TECHNOLOGY AND DATA: PRACTICAL EXAMPLES

DETERMINE DATA REQUIREMENTS FOR MONITORING PROGRESS ON STRATEGIC PRIORITIES AND DECISION MAKING
Sainsbury's: Defining the measures and metrics required to evaluate and assess our performance

CONSIDER OPPORTUNITIES, RISKS AND CHALLENGES OF IMPLEMENTING A BIG DATA APPROACH
Sainsbury's: Utilizing a big data approach to streamline our existing supply chain

ESTABLISH SYSTEM AND FUNCTIONALITY REQUIREMENTS FOR EFFICIENT ACCESS TO REQUIRED DATA
Danone: Using S-ERP to manage sustainability data collection, reporting and analytics
Unilever: Using S-ERP to support our sustainable supply chain programme
Sainsbury’s: Defining the measures and metrics required to evaluate and assess our performance

At Sainsbury’s our strategy is underpinned by five main strategic elements, and our values are a core part of our business as they incorporate our sustainability objectives. Our values play an important role for our long term strategy for growth and value creation for our customers, suppliers, colleagues and shareholders.

We disaggregated our long term targets and commitments into milestones to enable us to better manage progress. We ensured that our reporting suites incorporated all sustainability aspects of our activity in monetary and non monetary terms, taking into account the way that our executive team supports the delivery of our strategic objectives.

To ensure we can evaluate and assess our performance appropriately within our governance model, we defined the right measures and metrics required, considering whether these are quantifiable and the level of ease in collating the data and information required.

The diagram shows examples of monetary and non monetary measures we used.

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**TECHNOLOGY AND DATA: PRACTICAL EXAMPLES**

**SOURCING WITH INTEGRITY**
- Number of key raw materials with sustainability standards
- Quantity of raw materials sourced from supply chains working within our independent sustainability standards
- Sales of fairly traded products
- Value of investment for projects involving Sainsbury’s in British farming

**RESPECT FOR OUR ENVIRONMENT**
- Number of stores with Food Donation Partners for surplus food
- Investment in Waste less, Save more
- % change in carbon emissions
- % change in water use in our operations (absolute and relative) v 2005/6 baseline

**LIVING HEALTHIER LIVES**
- Healthy products sold as a proportion of total sales volume
- Total investment in our Active Kids scheme

**MAKING A POSITIVE DIFFERENCE TO OUR COMMUNITY**
- Number of stores supporting their Local Charity of the Year partner through awareness raising, fundraising and volunteering

**A GREAT PLACE TO WORK**
- Colleague reward vs National Living Wage
- Number of apprentices trained
- Number of colleagues employed through our You Can scheme since 2008
THE MODEL

Our Cost of Production (COP) model is aimed at protecting dairy farm businesses from market volatility, both with respect to the price paid for their milk and the major input costs to the farms. The model moves dairy pricing away from standard market pricing to a financially open book cost based approach, based on data independently collected from the 320 Sainsbury’s Dairy Development Group (SDDG) farms. The COP model took 18 months’ work with the SDDG farmers and an independent dairy accounting specialist. In March 2012, 86% of the SDDG voted in favour of adopting the COP model. Every SDDG farm provides financial data which is then compiled into an average pence per litre for the group. All costs apart from the 3Fs (feed, fuel and fertilizer) are fixed for 12 months. On a quarterly basis, the 3Fs are adjusted to account for the actual market fluctuations.

The COP model has served to halve price volatility for our farmers. The variance in market price has been 13.22 pence per litre (ppl) versus a COP variance of 7.12ppl.
THE ROLE OF BIG DATA

As well as collating financial data from the 320 farms in the Group, a significant amount of data is collected on herd health and efficiency. Each of the farms is incentivized to drive continual improvement using our ‘Herd Health and Efficiency Matrix’ which scores farms using a 100 point system. Submitted scores and declarations are subject to independent audit. The matrix scores are then used to reward excellence: the greater the score, the greater the farm’s bonus.

Data is also collected to support our Bovine Viral Diarrhoea (BVD) Control Scheme, aimed at eradicating BVD from our herds. This covers 250 farms, 20,000 heads of cattle and the results of over 2,500 blood samples.

The data collected evidences that despite our cows producing more milk, they are healthier.

TECHNOLOGY AND DATA: PRACTICAL EXAMPLES

Sainsbury’s: Utilizing a big data approach to streamline our existing supply chain
FINANCE TEAM INVOLVEMENT

The finance and commercial teams have actively led the Cost of Production initiative in conjunction with the agriculture team at Sainsbury’s, who are responsible for the day to day interaction with farmers. There has been a contraction in the British dairy industry with large numbers of farmers going out of business, and there was therefore a clear commercial imperative to safeguard the milk supplies in the UK market. The challenge and opportunity was to give our dairy farmers the stability and confidence to invest in the future of their businesses and protect them from market volatility. In doing so we have ensured consistent, resilient milk supplies whilst also ensuring a sustainable future for the SDDG farmers. The implications that implementing the COP model had for our business and the SDDG farmers was significant. We have decoupled our price negotiation from the market and linked our costs to a different set of volatile inputs beyond our control. Farmers have also decoupled their price negotiation from the market. This required strong buy in from the Operating Board at Sainsbury’s and our SDDG farmers. It was only the quality of the financial model, its data, governance and the processes that underpin it that was able to give the confidence and establish the trust within and across the businesses involved. The independence of our finance team internally and the independent nature of the dairy accounting specialist externally further supported this approach, working closely with SDDG farmers and our commercial, technical and agriculture teams throughout the process.

THE BENEFITS

The COP model serves to strengthen the long term commitment we have made to the SDDG as it guarantees them a sustained business margin which is something a market price is unable to do. The business margin element is a fundamental part of the model as it encourages investment and profitability. Our business recognizes that the most important part of sustainability is financial sustainability, which this model now secures. Financial certainty gives our farmers the confidence to invest in farm buildings, handling equipment and proactive herd health planning with their vet. These investments have already resulted in improvements to cow comfort which is contributing to us delivering our 2020 commitment to higher animal welfare standards on farm. These improvements ultimately lead to increased production efficiencies, which in the long term will bring the cost of producing a litre of milk down and reducing its environmental impact but, as the model secures a business margin, farms will remain profitable. Since January 2014 our COP price has been below the market milk price. Farmers have accepted this because it is based on data that is derived from their own businesses. The model, its data and governance gives the trust that the farms are still making a business margin. However, the market has now started to take a downward turn from which the SDDG will be protected which in turn will also protect our business from the negative PR that market volatility can generate.

TECHNOLOGY AND DATA: PRACTICAL EXAMPLES

Sainsbury’s: Utilizing a big data approach to streamline our existing supply chain
Danone: Using S-ERP to manage sustainability data collection, reporting and analytics

Danone’s Executive Board sees sustainability as a strategic priority. We have adopted a measured approach to integrating sustainable business practices across our 160 plants on five continents in over 120 countries. We’ve established carbon reduction as a guiding principle, and have appointed a ‘Vice President for Nature’. Senior management has elevated carbon reduction to coequal status with business targets, and also works hard to optimize water usage, which is key to operations. Transparency to consumers and retailers, as well as support for new standards and legislation in the countries where we operate, are foundational to our strategy of growth driven by sustainability.

To help achieve this transformation, we have partnered with SAP to help make sustainability an integral part of how we do business every day. The two companies are united by a shared commitment to innovative IT strategies that will meet our promises to consumers and the challenges of today’s environment, as well as comply with changing country regulations. In a resource constrained world where consumers want to make better choices, both companies know sustainability is not only about conservation or recycling. Real change can only occur by taking a measured business approach to determine the cost of materials and products across the supply chain, from sourcing to production to delivery and beyond.

As a result, Danone implemented SAP ERP to collect, measure, analyse and reduce our carbon footprint across our entire 35,000 product line. Relying on several SAP modules, the process captures highly detailed, monthly assessments of our product line by stock keeping unit (SKU) across the entire lifecycle, from sourcing through production, transport, retail distribution, consumption and end of lifecycle. Full integration with SAP ERP allows us to automatically retrieve information including bills of materials, production and delivery orders and intercompany transportation. We can easily assess a range of product footprints, and incorporate allocation of emissions and costs generated by each process.

We also use SAP ERP to help holistically manage data collection, reporting and analytics across all social, environmental and economic initiatives. Danone is also working with suppliers so they can directly enter their data into SAP ERP, saving time and boosting information quality. Future plans include enhanced reporting beyond SKU carbon footprint tracking. We will report emissions by product, factory, division, country, brand, customer and time interval, then set benchmarks based on the intelligence. Executives envision a monthly ‘sustainability closing’, much like a financial closing, for greater transparency and stronger competitive advantage.

Implementing SAP software solutions has helped to drive employee engagement. Employees have a deeper sense of pride in their work since every staff member is held accountable for the quality of carbon data in their business area. Specialists in lifecycle management collect and assess information from the supply chain, such as site specific emission factors for components used during the raw pack process. People with job titles like Carbon Master and Master Data Manager, along with users in manufacturing, purchasing and transport units, provide additional input for things like emissions factors by transport types or energy consumption to complete the process. Teams perform calculations for insight and visibility into the carbon measurements at a product level via multidimensional modelling and analysis. Using SAP software reports and dashboards, employees can display the product carbon footprint intensity as grams of CO2e per kilogram or litre of product, as well as in absolute terms of metric tonnes of CO2e emissions.
Unilever: Using S-ERP to support our sustainable supply chain programme

Unilever is committed to growing our businesses sustainably. Working with Oracle, we are contributing to a more sustainable supply chain through streamlining shipping, improving communication with providers, and helping reduce CO2 emissions. We undertook an ambitious programme to implement Oracle across the global network of Unilever logistics, making Oracle an important part of Unilever’s daily operations and assisting us on our journey to be a sustainable business.

We have integrated Oracle with several other business critical applications including: our warehouse management system, enterprise resource planning applications, electronic data interchange and transportation rate system, as well as interfacing with carriers and third party logistics providers.

We have used Oracle solutions to:

- help ensure high performance and 24/7 management support for the business critical transportation management platform while freeing IT team members for other priorities;
- expand use of cross docking and load consolidation model to support just in time delivery, reduce the number of trucks required, cut carbon and reduce inventory requirements; and
- reduce invoice rework thanks to real time information on freight costs and accessorail charges, cutting paper use and time spent generating and analysing logistics data.

In recognition of our efforts towards greater sustainability, Unilever won the 2014 Oracle Sustainability Innovation Award, which honours organizations that have reduced their environmental footprint while reducing costs using green business practices and Oracle technology.
MATURITY AND REFERENCES

STRATEGIC PLANNING, BUDGETING AND FORECASTING
### Maturity Map

**Sustainability factors integrated into strategic planning, budgeting and forecasting to enhance decision making**

Does your strategic planning process position your organization to respond to major environmental and social trends? If sustainability is considered at a strategic level, does this flow through into budgeting and forecasting processes? If not, what is preventing this?

<table>
<thead>
<tr>
<th>Strategy</th>
<th>Elements of sustainability integrated into strategic planning, budgeting and forecasting</th>
<th>Sustainability is fully integrated into strategic planning, budgeting and forecasting</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginner</td>
<td>- Information is retained by the departments involved in the sustainability planning process&lt;br&gt;- Information to support the integration of sustainability factors is collected through a mixture of manual and automated systems&lt;br&gt;- A limited number of sustainability related objectives are actively managed through the formal budgeting and forecasting process&lt;br&gt;- A limited number of sustainability factors are integrated within the overall strategic planning process&lt;br&gt;- A 'totex' approach is used rather than separate opex and capex budgets&lt;br&gt;- Non monetary budgets (e.g. carbon budgets) are used alongside financial budgets and integrated into decision making</td>
<td>Sustainability factors are within the remit of Board level governance bodies&lt;br&gt;- Sustainability is fully integrated into the corporate strategy which flows through into performance management frameworks&lt;br&gt;- Sustainability related objectives are actively managed through the formal budgeting and forecasting process&lt;br&gt;- Short and long term incentive plans are aligned with sustainability aims</td>
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</tbody>
</table>
TOP TIPS

Understand the sustainability factors that impact the business drivers or business model of your organization.

Ensure there is effective governance and strong commitment from the leadership team to deliver integrated planning, budgeting and forecasting.

Align integrated planning, budgeting and forecasting activities with the rest of the organization’s performance management framework, including reporting, performance appraisal and remuneration activities.

Prioritize the most relevant and meaningful data by assessing the data’s importance to strategy and business performance.
CASE STUDY INDEX: PROCESS

**STRATEGIC PLANNING**
- Yorkshire Water: Identifying long term risks and opportunities
- Anglian Water: Water resource scenario planning
- Anglian Water: Introducing sustainability factors into strategic planning, budgeting and forecasting
- BHP: Climate change scenario planning
- The Crown Estate: A strategic approach to success and future proofing our business
- SSE: Assessing total impact to benefit strategic planning decisions

**BUDGETING**
- Crossrail: Developing a budgeting structure which puts long term benefits at the centre
- Microsoft: Implementing an organization wide carbon fee model
- Asda: Setting monetary budgets in line with strategic sustainability objectives
- Bupa: Ring fencing funding for low carbon and renewable energy projects
- SSE: Standardized and transparent community fund
- SSE: Local supplier portal
- City, University of London: Using a marginal abatement model to budget for emissions reduction options
- Royal DSM: Setting a shadow carbon price
- South West Water: Integrating sustainability throughout strategic planning, budgeting and forecasting processes

**FORECASTING**
- Yorkshire Water: Integrating carbon forecasting into operational and financial forecasts
- City, University of London: Forecasting carbon emissions savings
- Siemens: Anchoring our Environmental Portfolio into strategic planning, budgeting and forecasting processes
- Sainsbury’s: Delivering financial and sustainability benefits hand in hand
- Danone: Combining financial and carbon savings
- Coca-Cola Hellenic: Introducing science backed carbon reduction targets and water usage efficiency
- Royal DSM: Setting a shadow carbon price
- South West Water: Integrating sustainability throughout strategic planning, budgeting and forecasting processes
- Danone: Moving away from a traditional annual budgeting cycle
## CASE STUDY INDEX: GOVERNANCE

<table>
<thead>
<tr>
<th>STRATEGIC MANAGEMENT</th>
<th>ALIGNING BUSINESS GOALS</th>
<th>ORGANIZATIONAL STRUCTURE AND OVERSIGHT</th>
<th>REPORTING FRAMEWORKS</th>
<th>DECISION MAKING POWER AND PROCESS</th>
<th>MANAGING RISK AND UNCERTAINTY</th>
</tr>
</thead>
<tbody>
<tr>
<td>Royal DSM: Transitioning towards a sustainable business model</td>
<td>Royal DSM: The role of KPIs and remuneration frameworks in setting ownership and accountability for sustainability</td>
<td>Royal DSM: Setting strategic goals to help our business grow</td>
<td>Sainsbury’s: Using simple and visual integrated management reporting</td>
<td>Sainsbury’s: Integrating sustainability into our governance model</td>
<td>The A4S Essential Guide to Managing Future Uncertainty</td>
</tr>
<tr>
<td>Danone: Our Manifesto to building a healthier future</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Yorkshire Water: Creating a culture of understanding, alignment and agreement among teams</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Anglian Water: Using cross functional involvement in strategic plans to strengthen the sustainability agenda</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
# CASE STUDY INDEX: PERFORMANCE MANAGEMENT

<table>
<thead>
<tr>
<th>EMPLOYEE PERFORMANCE</th>
<th>ORGANIZATIONAL PERFORMANCE</th>
</tr>
</thead>
<tbody>
<tr>
<td>National Grid: Strengthening our licence to operate and saving costs through our employee wellbeing programme</td>
<td>The Crown Estate: Defining values, with sustainability at the heart</td>
</tr>
<tr>
<td>SSE: Incentivizing directors through a balanced range of performance measures</td>
<td>Sainsbury’s: Integrating sustainability into our governance model</td>
</tr>
<tr>
<td>Royal DSM: The role of KPIs and remuneration in frameworks in setting ownership in setting ownership and accountability for sustainability</td>
<td>Yorkshire Water: Linking sustainability to monetary and non monetary impacts and benefits, and developing our Total impact and Value Assessment</td>
</tr>
<tr>
<td>Sainsbury’s: Incorporating our Sustainability Plan values into our Board remuneration policy</td>
<td>Anglian Water: Agreeing outcomes with predetermined performance levels, framed on both business and sustainability benefits</td>
</tr>
</tbody>
</table>
## CASE STUDY INDEX: TECHNICAL AND DATA

<table>
<thead>
<tr>
<th>Requirement</th>
<th>Sainsbury's: Defining the measures and metrics required to evaluate and assess our performance</th>
<th>Sainsbury's: Utilizing a Big Data approach to streamline our existing supply chain</th>
<th>Danone: Using S-ERP to manage sustainability data collection, reporting and analytics</th>
<th>Unilever: Using S-ERP to support our sustainable supply chain programme</th>
</tr>
</thead>
<tbody>
<tr>
<td>DETERMINE DATA REQUIREMENTS FOR MONITORING PROGRESS ON STRATEGIC PRIORITIES AND DECISION MAKING</td>
<td>CONSIDER OPPORTUNITIES, RISKS AND CHALLENGES OF IMPLEMENTING A BIG DATA APPROACH</td>
<td>ESTABLISH SYSTEM AND FUNCTIONALITY REQUIREMENTS FOR EFFICIENT ACCESS TO REQUIRED DATA</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

- **Introduction**
- **Process**
- **Governance**
- **Performance management**
- **Technology and Data**
- **Maturity and reference**
  - Maturity map
  - Top tips
  - Case study
  - References
The Prince’s Accounting for Sustainability Project was established by HRH The Prince of Wales in 2004 “to help ensure that we are not battling to meet 21st century challenges with, at best, 20th century decision making and reporting systems”.

**A4S MISSION STATEMENT**

To inspire action by finance leaders to drive a fundamental shift towards resilient business models and a sustainable economy.

The A4S Chief Financial Officer Leadership Network was launched by HRH The Prince of Wales at St James’s Palace in December 2013.

The Network brings together a group of leading CFOs from large businesses seeking to embed the management of environmental and social issues into business processes and strategy. The CFO Leadership Network is the first grouping of its kind globally.

The Network is looking at each area of finance function activity to identify how positive business returns can be achieved through integration of environmental, social and economic considerations. The focus is on sharing insights into what works and what does not. The Network aims to create open source guidance, which members of the Network commit to adopt and share. These insights are also discussed with bodies involved in the training and education of the finance and accounting community to scale up action.

Finance professionals from Network members’ organizations undertake a range of projects to develop practical guidance on specific areas of financial decision making, including this guide on strategic planning, budgeting and forecasting.
THE A4S ESSENTIAL GUIDE SERIES

The A4S Essential Guide Series has been produced by the A4S CFO Leadership Network to help organizations embed social and environmental considerations into their strategy, culture and processes. In other words, they support the adoption of integrated thinking and management. They are developed by finance teams for finance teams, but will also be of interest to others seeking to understand current approaches for integrating sustainability into financial practices and decision making.

LEAD THE WAY

Developing a strategic response to macro sustainability trends
- Finance Culture*
- Managing Future Uncertainty
- Incentivizing Action*
- Engaging the Board and Mobilizing Action*

MEASURE WHAT MATTERS

Developing measurement and valuation tools
- Natural and Social Capital Accounting
- Social and Human Capital Accounting

TRANSFORM YOUR DECISIONS

Integrating material sustainability factors into decision making
- Strategic Planning, Budgeting and Forecasting
- Integrated Management Reporting*
- Capex

ACCESS FINANCE

Engaging with finance providers on the drivers of sustainable value
- Enhancing Investor Engagement
- Debt Finance*

* Coming soon

See the A4S Essential Guide Series
REFERENCES


WE WOULD ALSO LIKE TO THANK

Fiona Wild, BHP Billiton
Jason Clarke, City, University of London
Gerhard Seidl, Coca-Cola Hellenic
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Tamara DiCaprio, Microsoft
Stuart Bailey, National Grid
Beth Hart, Sainsbury's
Mark Carlin and Ian Bowman, Siemens
George Cobb, SSE
Claire Burgess, The Crown Estate
Sabrina Mistry, Unilever
Gordon Rogers, Yorkshire Water
Chris Tuppen, A4S Expert Panel Chair
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