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NON-FINANCIAL DISCLOSURE AND INTEGRATED REPORTING: PRACTICES AND CRITICAL ISSUES

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INTRODUCTION

NON-FINANCIAL DISCLOSURE AND INTEGRATED REPORTING: PRACTICES AND CRITICAL ISSUES

Lucrezia Songini, Anna Pistoni, Pierre Baret and
Martin H. Kunc

The financial crisis of 2008 and its economic and social aftermath have highlighted the limits and risks of an increasingly global and embedded economy. They have also weakened society's trust in organizations and institutions and have led to calls for new strategic paradigms that focus more on the ethical conduct of organizations in the broader economy, transparency in reporting the social and environmental impact of business activities, and duties and responsibilities of the organizations toward all stakeholders.

In this context, the landscape of performance measurement and reporting is changing quickly, with calls for more integrated reporting (IR) and compulsory non-financial disclosures. Keeping up with those issues represents a significant concern for managers in many organizations.

On March 1, 2010, the Johannesburg Stock Exchange adopted the King III principles as part of its listing requirements. Since 2010 listed companies in South Africa have been asked to apply King III principles, which recommend IR and hence the requirements for listed companies to issue integrated reports.

In December 2013, the International Integrated Reporting Council (IIRC) generated the International IR framework with the aim to help the development of more comprehensive and comprehensible information about an organization's global, prospective as well as retrospective, performance to meet the needs of an emerging, more sustainable, and global economic model.

Even though there are numerous benefits for stakeholders and organizations, and the great number of studies and evidence on best practices in IR adoption,

IR is still not so much diffused among companies. The main reason can be traced to difficulties that companies find on implementing the IR framework.

Thus, a debate between academia and practitioners concerning whether the IR must be a compulsory or non-mandatory requirement for companies has emerged in recent years. Attention has been paid by the researchers to issues in IR, particularly, role and objectives, critical issues in its implementation, and the relationship with corporate social responsibility (CSR) and sustainability disclosure and reporting. More recently, the focus has been shifted to the determinants of the adoption of IR and its quality.

In the last few years, to cope with the effects of financial crisis, big interest toward non-financial disclosure has been emerged at the institutional level. In 2014, the European Union issued the Directive 2014/95/EU concerning mandatory disclosure of non-financial and diversity information by public-interest entities. The EU requires all European countries to consistently adopt this directive in their legislation. Since January 1, 2017, all large public-interest organizations with more than 500 employees, listed corporations, and financial institutions have been forced to disclose their Annual Report non-financial information concerning environmental protection, social responsibility and treatment of employees, respect for human rights, anti-corruption and bribery, and diversity on company boards.

The literature on the implementation and effects of the Directive 2014/95/EU on disclosure practices of European enterprises is still limited, but it seems to confirm the relevant role that institutions and regulation have in improving the quality of non-financial disclosure. However, many critical issues emerge in the measurement and communication of non-financial performance, which have negative impact on the quality of such a disclosure. They mainly refer to the relevance, the breadth, the reliability, the comparability, the standardization and harmonization of non-financial indicators, and the need that non-financial disclosure allows significant comparisons of performance of different companies during the particular time. The relationship between compulsory non-financial disclosure and voluntary CSR and sustainability disclosure tools, such as sustainability reporting and environmental reporting, as well as the role of well-established and recognized standards such as global reporting initiative, remains an open question.

This volume critically reviews and advances theorization and empirical research about new trends in disclosure. It will help bridge the outlined gaps in the literature and practice by focusing on the effectiveness, quality and practical issues in non-financial disclosure, and IR. It will shed new light on many of the critical topics in these areas, such as the determinants of disclosure quality; the identification of appropriate metrics for non-financial information; the relationship among the different disclosure mechanisms and between voluntary and mandatory disclosure and more.

The analyzed topics are very relevant for managers in organizations, academics and those in other institutions (e.g., governments and regulators). The topics in this volume will address prominent concerns in practice that managers are seeking guidance on, and a focus of research in many different fields of study.

As such, this volume will appeal to managers in organizations who are interested and involved in the development and implementation of IR and non-financial disclosure; scholars considering research related to non-financial disclosures and IR; and policy-makers in institutions who develop standards and regulations on these issues.

In particular, the volume is attractive to:

- Top and middle management teams in charge of non-financial disclosure, CSR and sustainability performance measurement, and IR, belonging to the following organizational departments: communication, accounting and control, and investor relations.
- Listed firms and multinational companies with operations that affect sustainability.
- Consultants and practitioners involved in accounting, financial communication, and performance measurement.
- Academics and others in research fields that study CSR, sustainability, financial accounting, managerial accounting, strategic planning, and communication.

According to the objectives pursued, the book is divided in two parts: the first one is devoted to highlight some critical issues in non-financial performance measurement and disclosure, while the second part deals with emerging and relevant topics concerning IR. Both conceptual and empirical contributions are presented using various methodologies and drawing on different kinds of organizations and geographical contexts.

A summary of the main contents of the different chapters is provided in the following.

The first part, “Key Issues and Practices in Non-financial Performance Measurement,” develops the topic with three contributions focusing on different issues.

Chapter 1, “Desperately Seeking a Standard Metric for Corporate Social Performance,” by Marco Masip aims at understanding why, despite all attempts proposed in the literature to measure corporate social performance (CSP), a standard metric is still missing. A wide sample of metrics (69), which have been developed in 51 papers in the last four decades and used as a measure of CSP, has been examined by the author with the purpose of analyzing if socially related corporate performance metrics developed so far in the literature can be used as an agreed common standard. Research findings show that none of the metrics are standard for CSP, highlighting a gap in CSP research. A need to develop measures for the social performance of companies, with a wide orientation to the society, emerges from the analysis. Such a metric should consider a societal point of view, and be applied to most organizations regardless of their size, industry and origin, and with a true integration of the interests and needs of all stakeholders.

Chapter 2, “Evolution of Non-financial Reporting in France: The Innovative Adaptation of a Cognac Producer,” by Pierre Baret and Vincent Helfrich aims

at studying the main stakes of non-financial reporting and revealing its possible pitfalls. Especially, the case study presents some innovative and particular practices in terms of non-financial reporting that can represent the guidelines of an “ideal” non-financial reporting strategy that can simultaneously conciliate three stakes: CSR, non-financial reporting, and expectations of the company with a non-financial reporting tool.

Chapter 3, “The Effect of Mandatory Publication of Nonfinancial Disclosure in Europe on Sustainability Reporting Quality: First Insights about Italian and German Companies,” by Giorgio Mion and Cristian R. Loza Adauí aims to explore and evaluate the impact of the Directive 2014/95/EU on the sustainability reporting quality in two countries that have recently adopted the EU Directive, and to compare the two different institutional frameworks. Through the analysis of listed companies on the Italian and German Stock Exchanges, the authors show that the mandatory disclosure has a widely predictable effect on the number of sustainability reports published while it has no significant effect on the number of companies developing IR. With reference to the quality of sustainability reporting practices adopted by organizations, two different effects can be outlined: on the one side mandatory disclosure does not have any significant impact on the quality of sustainability reports, on the other hand it contributes in leveling and harmonizing the sustainability reporting practices between the two analyzed countries, thereby favoring a reduction of the effects of the two institutional frameworks.

The second part, “Key Issues and Practices in Integrated Reporting,” develops the topic with four contributions focused on IR.

In Chapter 4, “Mapping Circular Economy Processes in Integrated Reporting: A Dynamic Resource-based Approach,” Martin H. Kunc, Federico Barnabè, and Maria Cleofe Giorgino propose to adopt the Dynamic Resource-based View (DRBV) approach to IR in order to improve its usefulness as both a management and governance tool. The authors, using a multiple case-study methodology, demonstrate how a combined approach of IR and DRBV is able to move IR from the simple communication tool to represent the business system and evaluate the performance of the organizations with the aim of supporting managerial decision processes and combining integrated thinking and integrated management practices.

Chapter 5, “Integrated Reporting and Social Disclosure: True Love or Forced Marriage? A Multidimensional Analysis of a Contested Concept,” by Sergio Paternostro aims at critically analyzing the relationship between IR and social/sustainability disclosure. In particular, the chapter studies if the IR can contribute to improve the sustainability disclosure of the company, compared to the traditional separation between financial and social disclosure and to understand the nature and type (natural or forced) of the link between IR and social disclosure. The analysis has been carried out considering three different perspectives: academics’ point of view, which has been traced by an in depth literature review, soft-regulators’ perspective identified through a critical content analysis of IIRC

framework and companies, and finally the organizations' perspective which has been drawn by developing four case studies.

A particular focus on the relationship between environmental, social, and governance (ESG) performance and the content and semantic properties of IR is provided in Chapter 6, "Tone at Top in Integrated Reporting: The Role of Non-financial Performance," by Valentina Beretta, Maria Chiara De Martini, and Sara Trucco. The chapter investigates the extent to which the optimistic tone of intellectual capital disclosure (ICD) found in integrated reports is affected by the company's ESG performance. Hypotheses based on the "tone and the top" were conceptually developed and empirically tested through the content and tone analysis of 79 integrated reports issued by European listed firms from 2011 to 2016. The results show that, among the three main ESG performance pillars, governance is the most relevant in contributing to optimistic tone in ICD and particularly the integration between vision and strategy. Workforce health and safety, with reference to social performance, and eco-efficient product innovation, with regard to the environmental performance, play a positive role in enhancing optimistic tone of ICD.

Finally, the quality of IR is approached in Chapter 7, "Integrated Reporting Quality: An Analysis of Key Determinants," by Lucrezia Songini, Anna Pistoni, Francesco Bavagnoli, and Valentina Minutiello. In particular, the authors used the IR scoreboard recently proposed in the literature to assess the quality of 165 integrated reports provided by 55 international firms during the period 2013–2015. The quality score was defined considering the level of compliance of the IR content with the IR framework proposed by IIRC. On the basis of the literature review, four main determinants of IR quality have been identified: industry, region (where the firm is established), firm size, and mandatory adoption of IR. Findings show that firms located in Europe and in countries where IR is mandatory have higher IR quality. Conversely, industry and firm size seem not to have any impact on IR quality.

Some concluding remarks are proposed in the last chapter of the book. Particularly, the chapters in this book show important advances in determining the usefulness of non-financial disclosure and in particular IR in improving reporting, corporate performance and disclosing the actions of companies related with CSR, sustainability, and other non-financial aspects. While further research is underway, managers should start accepting that non-financial disclosure and IR provide a solid foundation to generate positive contributions to society. For researchers, the implications of the findings indicate the usefulness of adopting multiple methodologies, for example, case studies, regression analysis, etc., to uncover the impact of non-financial disclosure and IR in companies and activities of CSR.

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PART I

KEY ISSUES AND PRACTICES IN NON-FINANCIAL PERFORMANCE MEASUREMENT

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