

Accounting and control for sustainability and CSR

Session 16

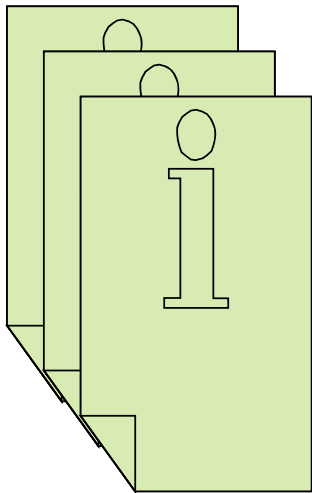
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13 December 2018

Strategic management accounting - A.Y. 2018/2019

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Sustainability disclosure: the main documents



- ✓ Annual report integrated with environmental and social indicators
 - ✓ Environmental report
 - ✓ Social report
 - ✓ Sustainability report
 - ✓ Non financial reporting directive
 - ✓ **Integrated reporting**
- ✓ Sustainability managerial reporting

Standards on sustainability / CSR measurement and reporting

International standards for sustainability report

- Global Reporting Initiative – GRI
- UN Global Compact
- Accountability 1000, AA1000
- Prince's Accounting for Sustainability Project (A4S)
- International Integrated Reporting Council (IIRC)

• ...

Standards for the social report

- Standards for the social report: GBS (Gruppo sul Bilancio Sociale – Italian research group on social report)
- ...

International standards for the environmental report

- IOW – Institute für Oekologische Wirtschaft (Institute for Ecological Economy Research) (IÖW) - standards for the environmental reporting
- FEEM – Fondazione Enrico Mattei (standards for the environmental reporting)
- ...

Prince's Accounting for Sustainability Project (A4S) International Integrated Reporting Council (IIRC)

- Prince's Accounting for Sustainability Project (A4S) and Global Reporting Initiative (GRI) established International Integrated Reporting Committee (IIRC) (August 1^o, 2010)
- IIRC's main aim is to develop a globally recognized standard for Accounting for Sustainability.
- IIRC's mission is to “create the globally accepted International <IR> Framework that elicits from organizations material information about their strategy, governance, performance and prospects in a clear, concise and comparable format. The Framework will underpin and accelerate the evolution of corporate reporting, reflecting developments in financial, governance, management commentary and sustainability reporting. The IIRC will seek to secure the adoption of <IR> by report preparers and gain the recognition of standard setters and investors”.

Prince's Accounting for Sustainability Project (A4S)

International Integrated Reporting Council (IIRC)

The principal role of the IIRC is to:

- reach a consensus among governments, listing authorities, business, investors, accounting bodies and standard setters for the best way to tackle the challenges of Integrated Reporting;
- identify priority areas where additional work is needed and provide a plan for development ;
- develop an overarching Integrated Reporting framework, which sets out the scope and key components of Integrated Reporting;
- consider whether standards in this area should be voluntary or mandatory;
- promote the adoption of Integrated Reporting by relevant regulators and report preparers.

Prince's Accounting for Sustainability Project (A4S) - International Integrated Reporting Council (IIRC)

- An Integrated Report should be a single report which is the organization's primary report – in most jurisdictions the Annual Report or equivalent.
- Central to Integrated Reporting is the challenge facing organisations to create and sustain value in the short, medium and longer term. Each element of an Integrated Report should provide insights into an organization's current and future performance.
- A framework which brings together financial, environmental, social and governance information in a clear, concise, consistent and comparable format - put briefly, in an “integrated” format.
- The intention is to help with the development of more comprehensive and comprehensible information about an organization's total performance, prospective as well as retrospective, to meet the needs of the emerging, more sustainable, global economic model.

Integrated Reporting: key facts

- Publication of One Report, by Krzus and Eccles (March 2010)
- GRI bi-annual conference (May 18-21, 2010)
- Mandated integrated reporting for all listed companies in South Africa from King III (June 1, 2010)

On 1 March 2010 the Johannesburg Stock Exchange (JSE) adopted the King III principles as part of its listing requirements. Listed companies in South Africa have to apply King III principles, which recommend Integrated Reporting and hence the requirements for listed companies to issue integrated reports. South Africa is leading the way internationally with regard to IR, being the first country in the world to take on integrated reporting on scale.

- London Steering Committee meeting deciding to launch the International Integrated Reporting Committee (IIRC) (July 16, 2010)
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- The IIRC will publish the International <IR> Framework in December 2013.

IR: guiding principles

Strategic focus and future orientation

An integrated report should provide insight into the organization's strategy, and how it relates to the organization's ability to create value in the short, medium and long term and to its use of and effects on the capitals

Connectivity of information

An integrated report should show a holistic picture of the combination, interrelatedness and dependencies between the factors that affect the organization's ability to create value over time

Stakeholder relationships

An integrated report should provide insight into the nature and quality of the organization's relationships with its key stakeholders, including how and to what extent the organization understands, takes into account and responds to their legitimate needs and interests

Materiality

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

Conciseness

An integrated report should be concise

Reliability and completeness

An integrated report should include all material matters, both positive and negative, in a balanced way and without material error

Consistency and comparability

The information in an integrated report should be presented: (a) on a basis that is consistent over time; and (b) in a way that enables comparison with other organizations to the extent it is material to the organization's own ability to create value over time

IR: content elements

Organizational overview and external environment

What does the organization do and what are the circumstances under which it operates

Governance

How does the organization's governance structure support its ability to create value in the short, medium and long term

Business model

What is the organization's business model

Risks and opportunities

What are the specific risks and opportunities that affect the organization's ability to create value over the short, medium and long term, and how is the organization dealing with them

Strategy and resource allocation

Where does the organization want to go and how does it intend to get there

Performance

To what extent has the organization achieved its strategic objectives for the period and what are its outcomes in terms of effects on the capitals

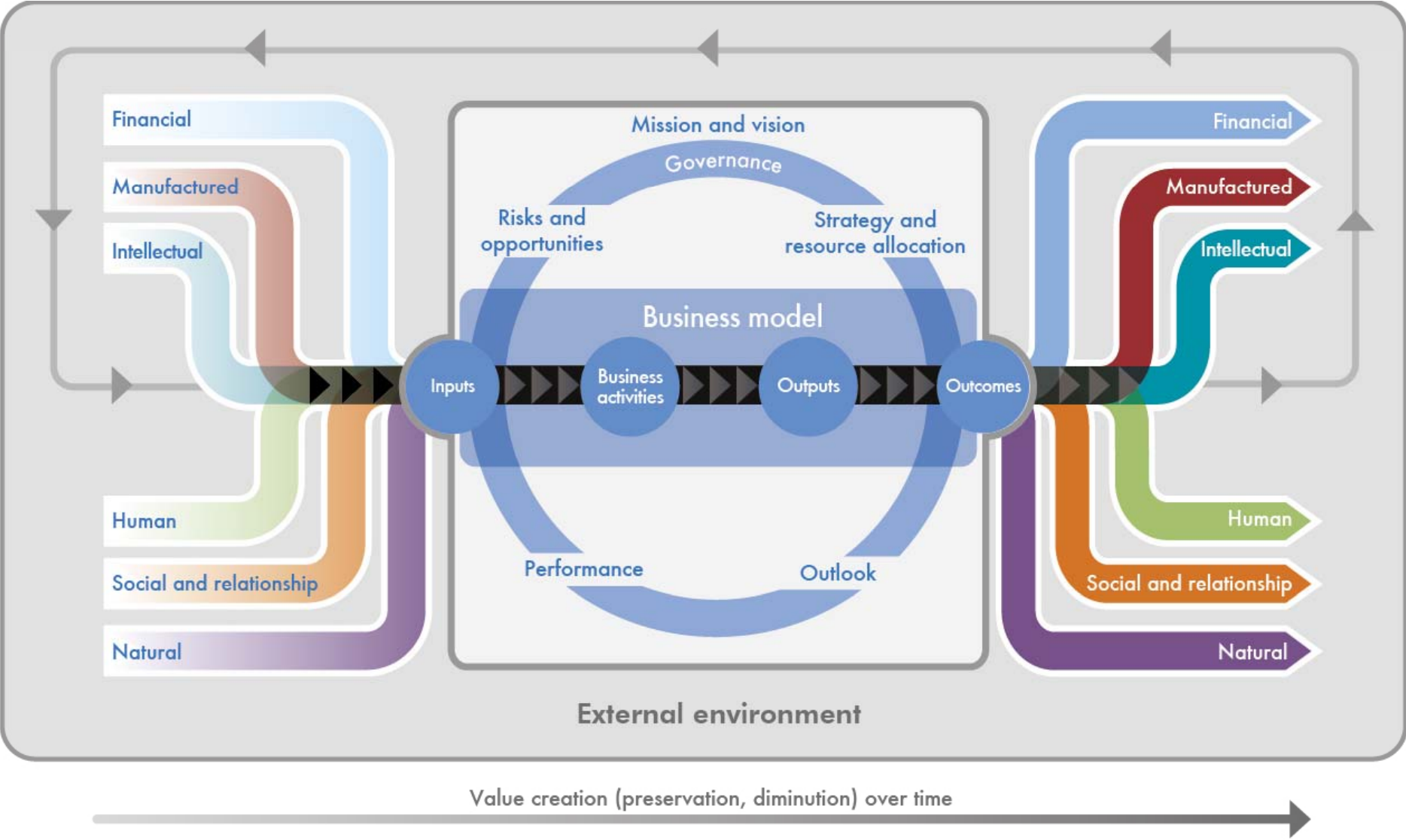
Outlook

What challenges and uncertainties is the organization likely to encounter in pursuing its strategy, and what are the potential implications for its business model and future performance

Basis of presentation

How does the organization determine what matters to include in the integrated report and how are such matters quantified or evaluated

IR: the framework



The IR framework: a wide vision of integration

The IR framework developed by the IIRC is based on a wide concept of integration.



- the company performance is interpreted as the result of the combined use of different kinds of capital provided by the different stakeholders: human capital, technical, intellectual, social and environmental capital;
- the framework requires to explicit the relations between the firm's strategy and its performance;
- the wished integration is not only looked for in the structure and in the content of the report but it is also pursued through the characteristics of the organizational processes and procedures;
- the framework promotes the integrated thinking and a strong collaboration among functions in order to improve the firm's value creation in the long run.
- the value creation process, indeed, is not only an internal result of the firm's activities but it is pursued through the various relations built with the different stakeholder categories and it is significantly influenced by external factors that define the context in which it operates, such as economic conditions, technological innovations, social and environmental issues.

6.1 RELATION BETWEEN INTEGRATED REPORTING AND SUSTAINABILITY REPORTING

Sustainability reporting is a process that assists organizations in setting goals, measuring performance and managing change towards a sustainable global economy – one that combines long term profitability with social responsibility and environmental care. Sustainability reporting – mainly through but not limited to a sustainability report – is the key platform for communicating the organization’s economic, environmental, social and governance performance, reflecting positive and negative impacts. The Aspects that the organization deems to be material, in response to its stakeholders’ expectations and interests, drive sustainability reporting. Stakeholders can include those who are invested in in the organization as well as those who have other relationships with the organization.

Integrated reporting is an emerging and evolving trend in corporate reporting, which in general aims primarily to offer an organization’s providers of financial capital with an integrated representation of the key factors that are material to its present and future value creation.

Integrated reporters build on sustainability reporting foundations and disclosures in preparing their integrated report. Through the integrated report, an organization provides a concise communication about how its strategy, governance, performance and prospects lead to the creation of value over time. Therefore, the integrated report is not intended to be an extract of the traditional annual report nor a combination of the annual financial statements and the sustainability report. However, the integrated report interacts with other reports and communications by making reference to additional detailed information that is provided separately.

Although the objectives of sustainability reporting and integrated reporting may be different, sustainability reporting is an intrinsic element of integrated reporting. Sustainability reporting considers the relevance of sustainability to an organization and also addresses sustainability priorities and key topics, focusing on the impact of sustainability trends, risks and opportunities on the long term prospects and financial performance of the organization. Sustainability reporting is fundamental to an organization’s integrated thinking and reporting process in providing input into the organization’s identification of its material issues, its strategic objectives, and the assessment of its ability to achieve them and create value over time.





The antecedents of IR (1)

The IR framework developed by IIRC may be viewed as a proposal that merges approaches and contents coming from other previous voluntary disclosure tools



The antecedents of IR (2)



- ✓ The King's III Principles  Holistic and integrated representation of the company's performance in terms of both its finances and its sustainability
- ✓ The disclosure on risks  Measurement of risk factors and risk drivers, risk assessment
- ✓ The disclosure on intangibles  Identify and understand the role of intangibles among the drivers of firm value and define appropriate key performance indicators.
- ... but also
- ✓ The managerial performance measurement and management  Development of financial and non-financial KPIs set aligned with business and CSR strategy

Main challenges to face in developing the IR

The main practical implementation issues:

- ✓ high costs for the project implementation: the firm has to redesign its reporting procedure. The main requested investments will be: technological investment, internal coordination costs, control costs in order to assure quality and reliability data;
- ✓ need of a cultural change in order to develop a new approach with reference to performance measurement:
 - capacity of communicating the firm's strategy and its strategic options without fear of competitor and market reactions
 - cultural change related to the way the information are represented in the IR. The numbers are not the only way to communicate; some information can be better explained in other forms like some stories.
 - It is important to reduce the distance between the cognitive model mainly based on numbers, typical of the finance department, and the cognitive model mainly focused on the narrative dimension peculiar of the CSR department.

Main challenges to face in developing the IR

- ✓ Need to provide forward looking information: it requires a different view of the firm performance, more oriented to the medium and long term, able to identify the critical variables that can influence the activities and their results in the long run;
- ✓ Need for external certifications of data, measurement and elaboration processes;
- ✓ Important challenges are related to the decisional processes. The IR require a better diffused knowledge and competencies about the sustainability issues in order to properly evaluate the global impacts (financial, social and environmental) of the different decisional streams.

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Empirical analysis

Limited diffusion of IR

Notwithstanding numerous initiatives sponsored by IIRC (IR Business Network, Pilot Programme Business Network) the IR is scarcely diffused



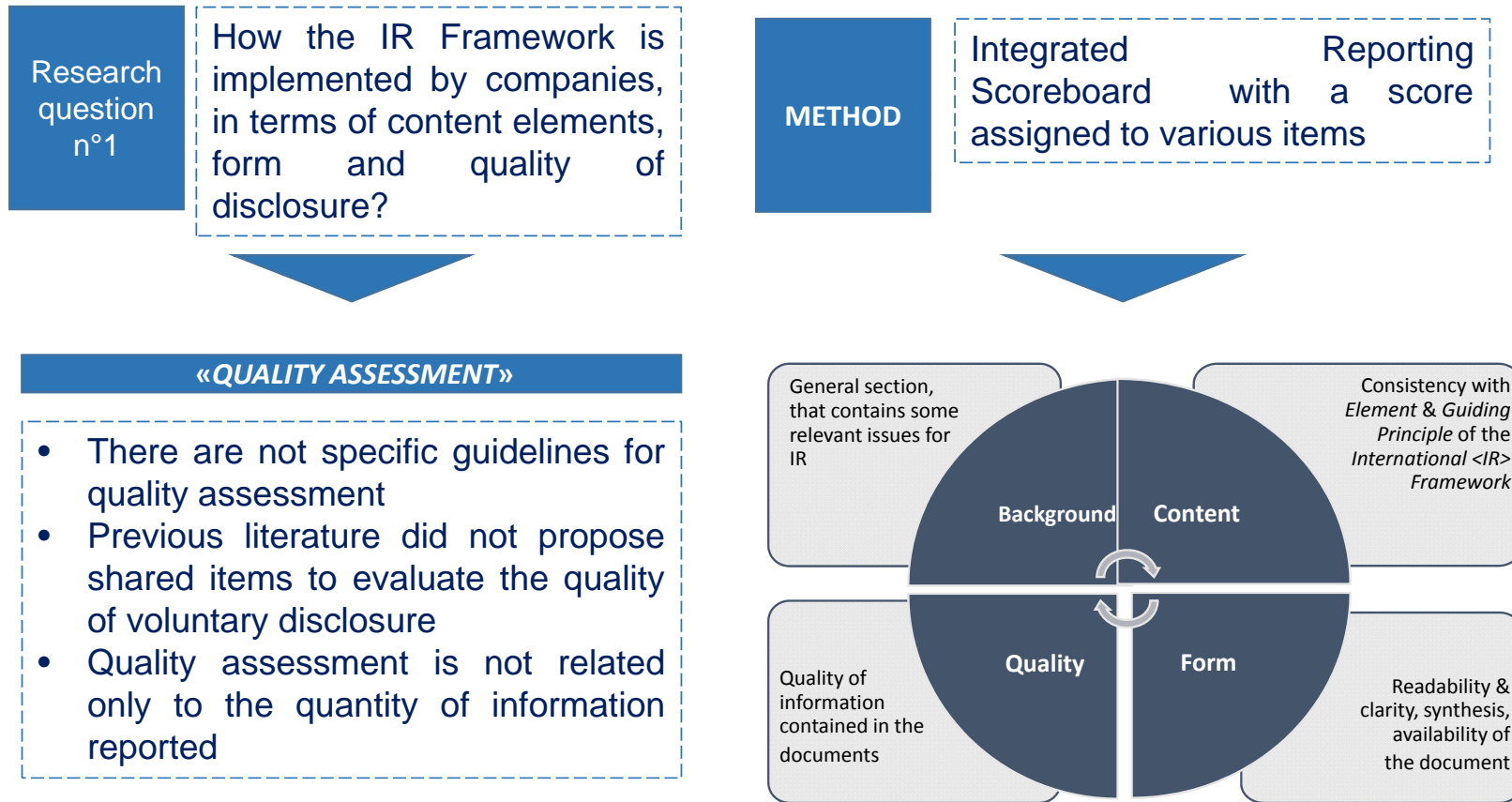
RESEARCH QUESTIONS

- 1 How the IR Framework is implemented by companies, in terms of content elements, form and quality of disclosure?
- 2 Is the implementation of the IR based on an integrated thinking that encompasses strategic, organizational and cultural integrations?

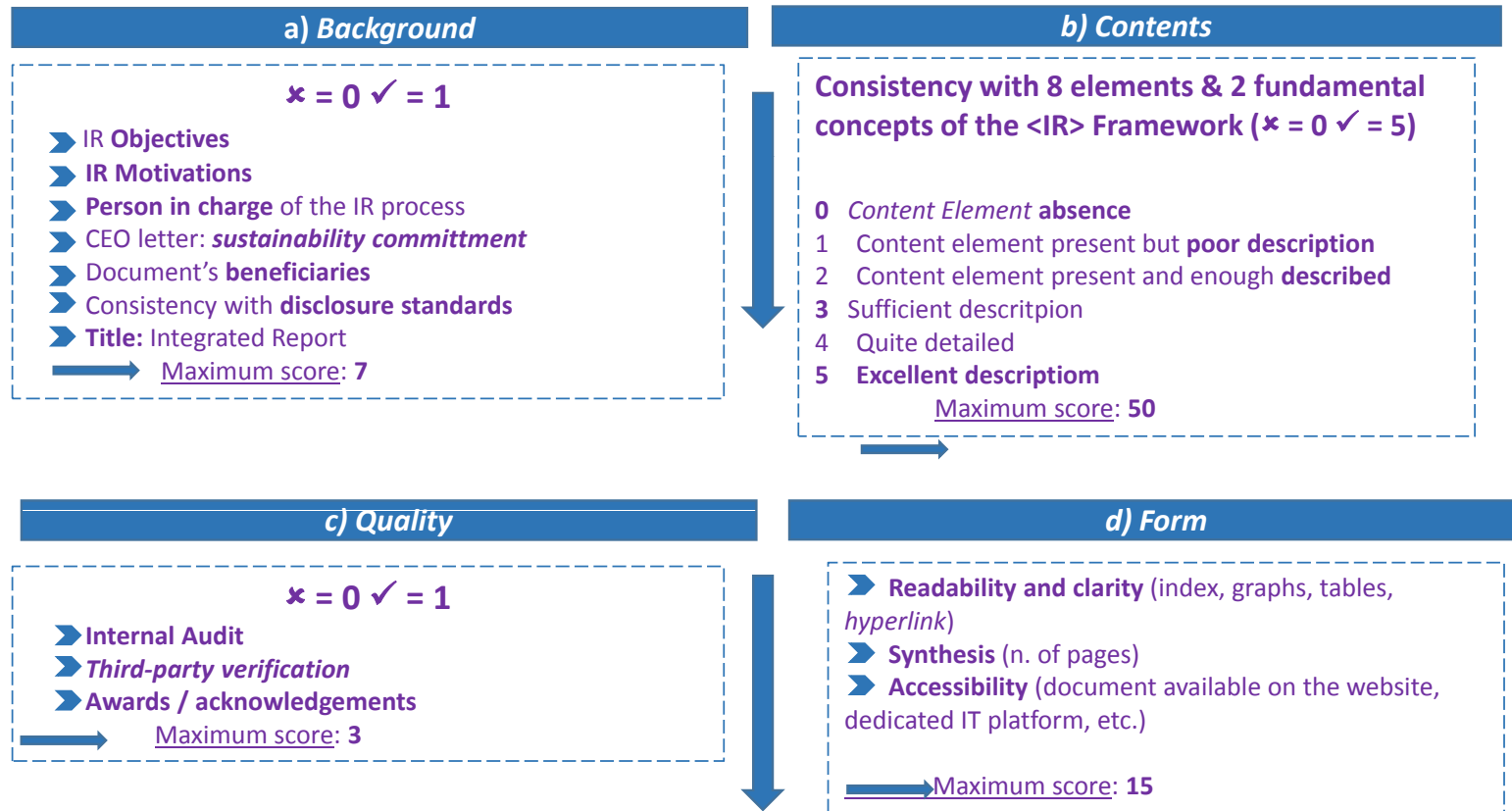


Pistoni A., Songini L., Bavagnoli F. 2017, Integrated Reporting quality: An empirical analysis, Corporate Social Responsibility and Environmental Management, DOI 10.1002/csr-1474

Empirical analysis: methodology



Integrated Reporting Scoreboard: scoring system



Conclusions

Usually firms follow the IR framework

BUT



- ✓ Scarce information is disclosed on relevant aspects such as capitals, the business model, the strategic priorities and the value creation process.
- ✓ A quite limited connectivity among various element of the framework emerged from the analysis, that does not allow to understand the relations among capitals, processes, strategy, performance and value creation in the medium-long term.
- ✓ An inadequate depth of analysis usually characterizes all sections of the integrated report.

Conclusions

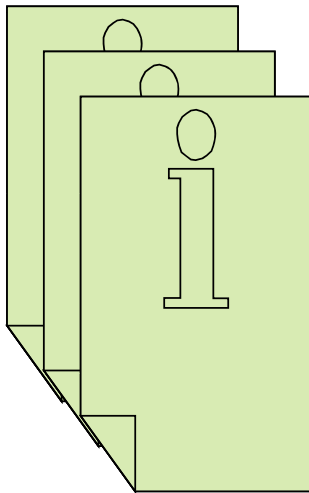
The research findings suggest that:

- ✓ a strong commitment of top management towards IR is needed, in order to favor the organizational change that the IR implementation implies,
- ✓ a stronger cooperation amongst functions and departments is needed
- ✓ investments in training, IT systems, stakeholder engagement are required



A debate has to begin among companies, professionals, associations and institutions on why the majority of firms seem not interested in adopting IR, what are positive impacts, real benefits versus costs, but also risks in terms of disclosing strategic and confidential information to competitors, etc.

Sustainability disclosure: the main documents



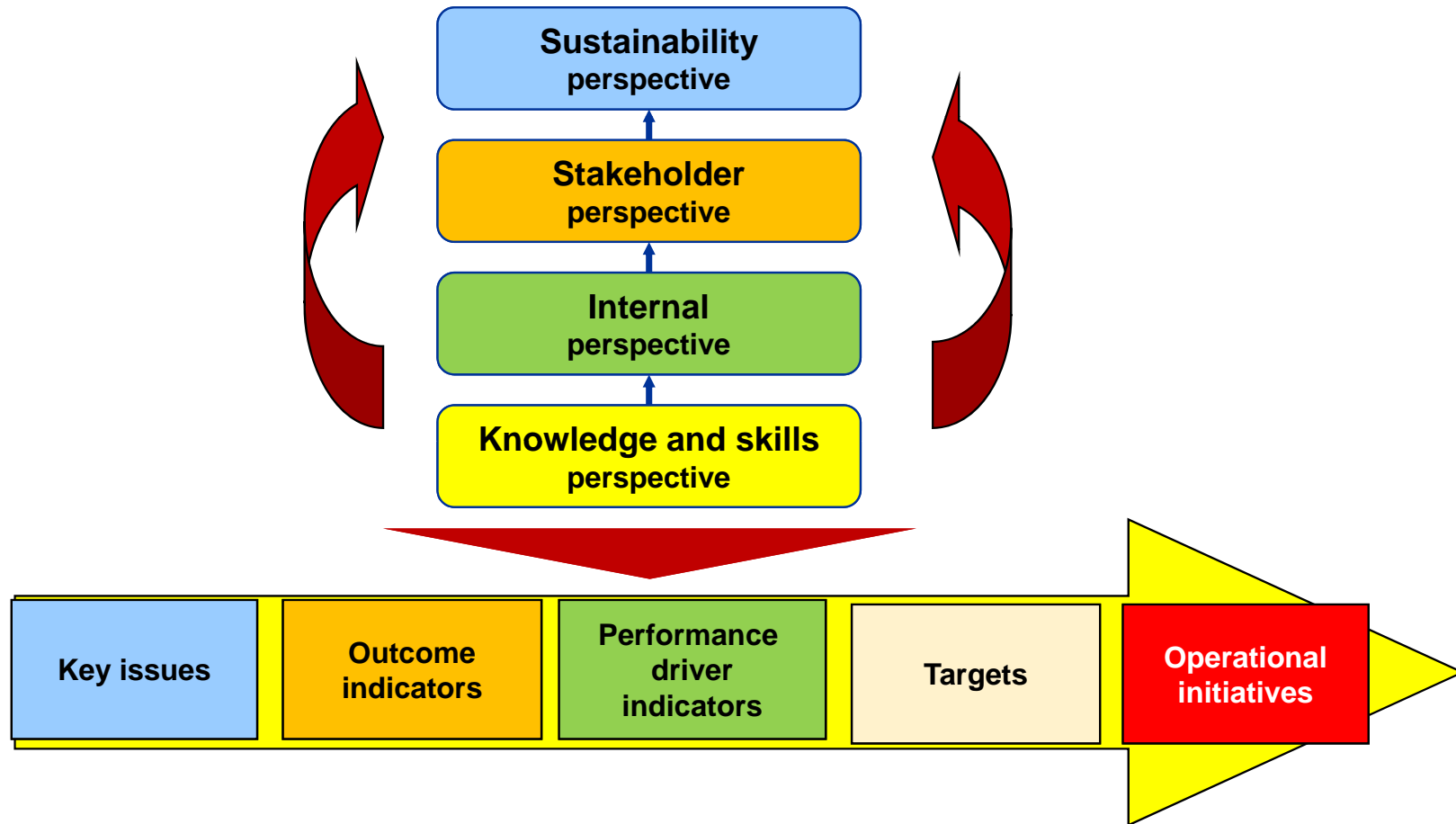
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✓ Sustainability managerial reporting

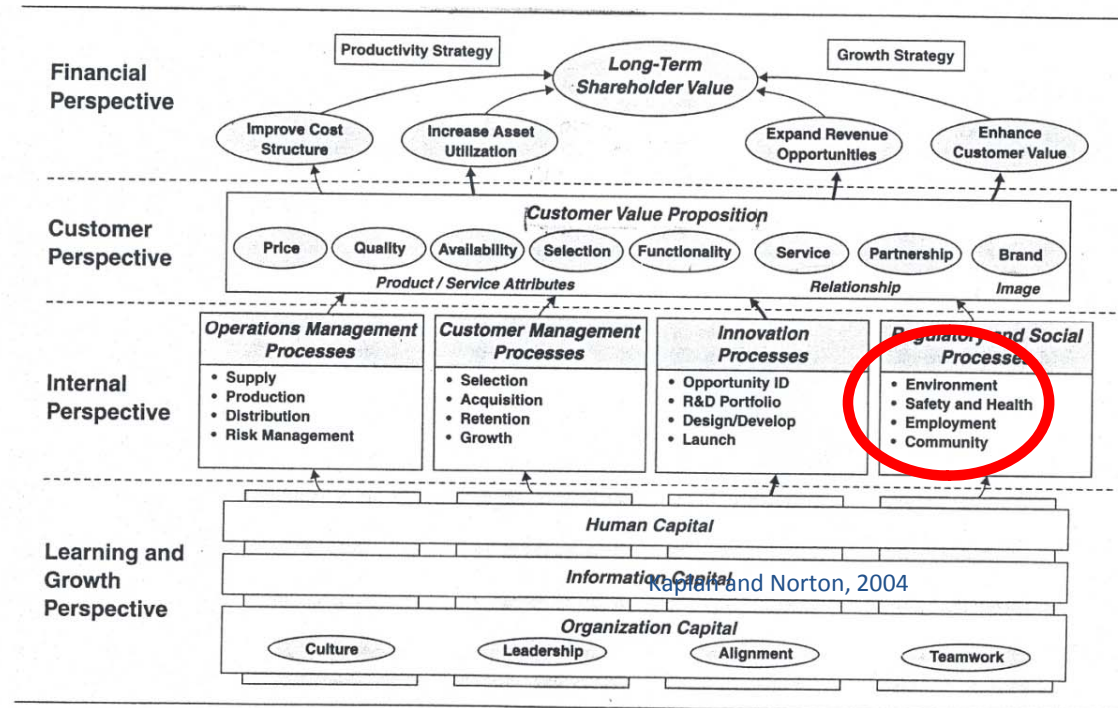
Performance measurement systems (PMSs) oriented to sustainability and CSR

- ✓ CSR e sustainability KPIs (Keeble et al, 2003; Clift, 2003; Hervani et al. 2005; Searcy, 2009; Ramos and Caeiro, 2010);
- ✓ Comparative Business Scorecard (Kanji, 1998; Kanji, Moura and Sa, 2002)
- ✓ Ethical Performance Scorecard (Spiller, 2000)
- ✓ Performance Prism (Neely et al., 2002)
- ✓ **SIGMA Sustainable Scorecard (Sigma Project)**
- ✓ Integral Framework for Performance Measurement (Rouse and Putterill, 2003)
- ✓ Responsive Business Scorecard, (Woerd and Brink, 2004)
- ✓ Thematic Balanced Scorecard (Dias-Sardinha and Reijnders, 2005)
- ✓ Corporate Sustainability Performance Pyramid (Epstein and Wisner, 2006)
- ✓ Dartboards and Clovers of Sustainability Model (Bonacchi and Rinaldi, 2007)
- ✓ **Sustainable Balanced Scorecard** (Kaplan and Norton, 2004 Epstein and Wisner, 2001, Figge et al. 2002, Epstein and Roy, 2003)

SIGMA Project: SIGMA sustainability scorecard

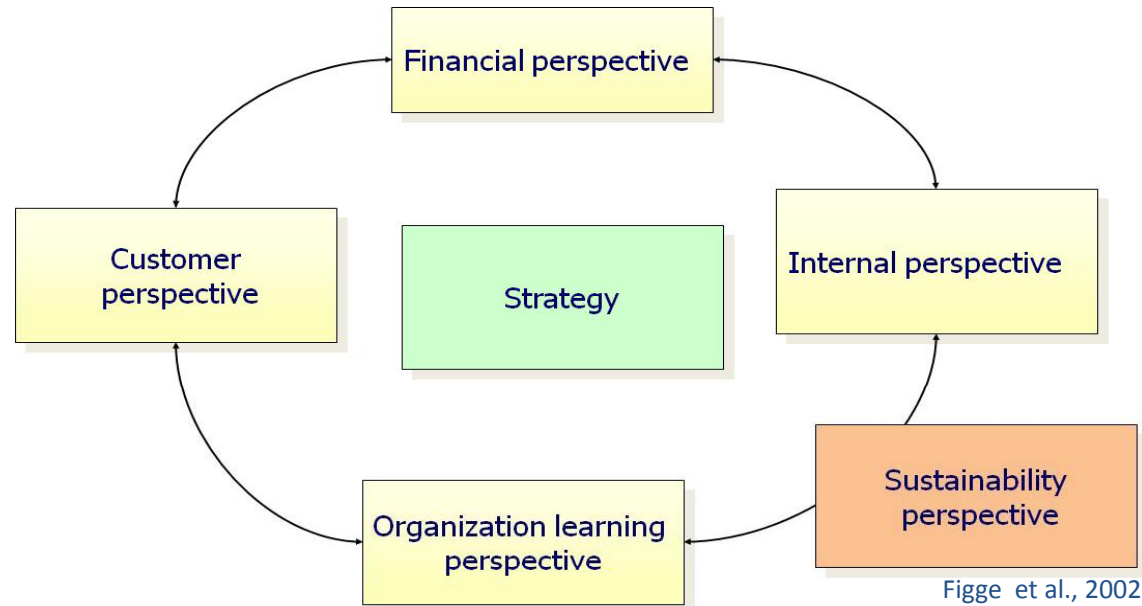


Sustainable Balanced Scorecard: option #1



- Key performance indicators (KPIs) on sustainability are introduced in the “Environment, Health and Safety” area.
- Social strategies and objectives are considered instrumental to business strategy and competitive and financial goals.

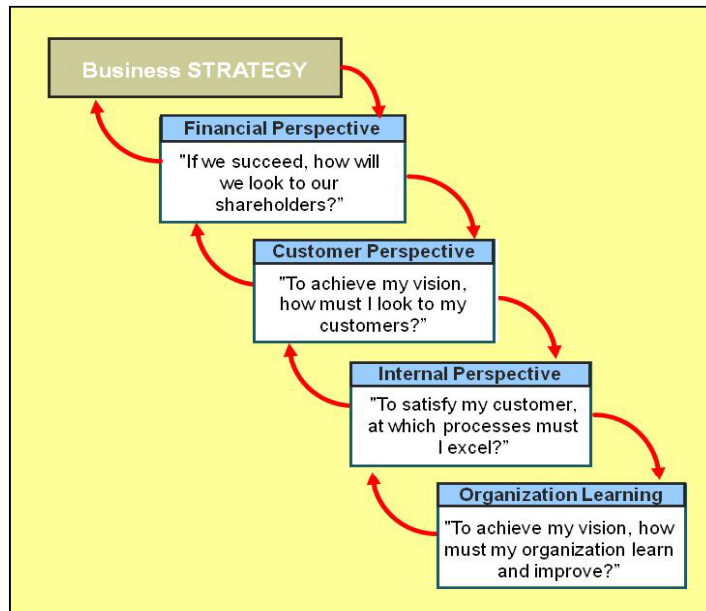
Sustainable Balanced Scorecard: option #2



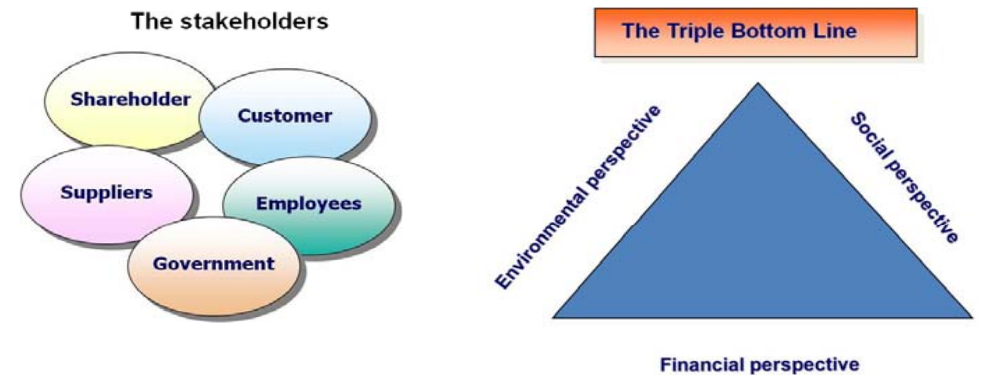
- A fifth perspective, the so called “non-market” perspective, is added to the traditional four perspectives.
- Sustainability is embedded into firm goals, but it is not linked to financial goals.
- Business strategy and social strategy remain separated.
- This option is chosen by firms which have been involved into sustainability recently or which would like to maintain separated the financial/competitive perspective from the sustainability perspective.

Sustainable Balanced Scorecard: option #3

The business BSC

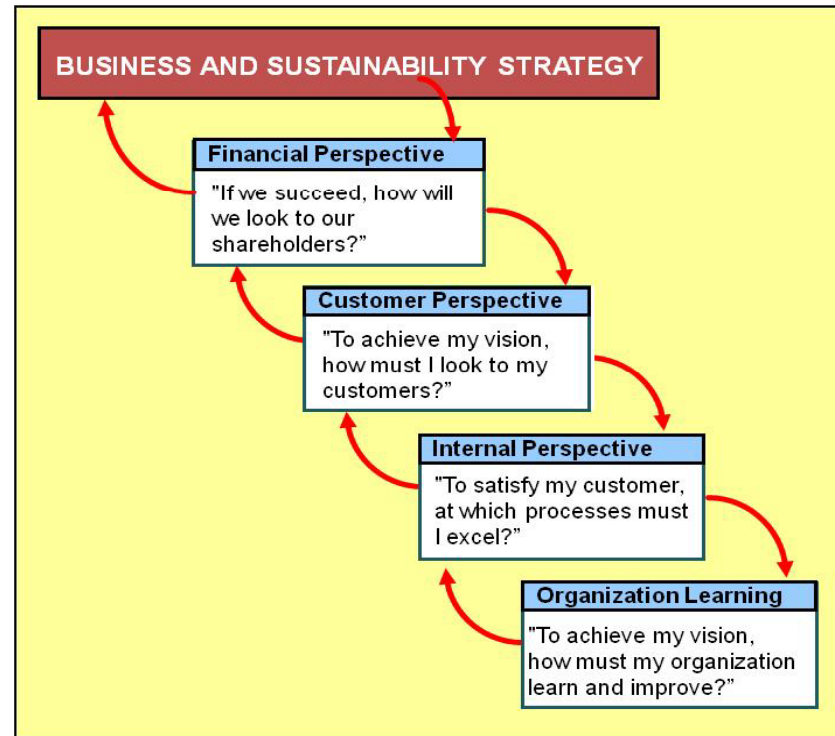


The sustainable BSC



- The sustainable balanced scorecard is separated from the traditional balanced scorecard
- The sustainable balanced scorecard is designed either following a triple bottom line approach or a multi-stakeholder perspective.
- Social strategy is separated from business strategy (Epstein and Wisner, 2001)

Sustainable Balanced Scorecard: option #4



- CSR and sustainability perspectives are pervasively introduced in all four perspectives of traditional BSC.
- There is a coincidence between business strategy and social strategy (Epstein and Manzoni, 1999)

Sustainable BSC: strengths and weaknesses

- ✓ The Sustainable Balanced Scorecard is perceived as a complex and an expensive mechanism, not balanced in terms of costs and benefits.
- ✓ The Sustainable Balanced Scorecard can contribute to implement social strategy in the first phases of the transition toward a more responsible and sustainable approach and in the short term.
- ✓ In the medium-long term firms tend to adopt formal PMSs to support the implementation of social strategy, but more flexible and simplified than the Sustainable Balanced Scorecard (i.e. KPIs).
- ✓ The Accounting and control department plays a relevant role: when the CFO and controller are the sponsors of the sustainable BSC this mechanisms is more used.

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