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Improve Sustainability Reporting through Integrated Reporting: Evidence from Italy

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Abstract: *This study aims to analyze the connections between integrated reporting (IR) and sustainability reporting (SR), in order to verify whether the IR can contribute to improving the SR prepared according to the Global Reporting Initiative (GRI) standards. In particular, this study considers the topic from the point of view of the SR to understand the benefits that it could obtain from the information disclosed through the IR. To this end, the study analyzes the integrated reports relating to the 2021 financial year of two listed Italian companies operating in the financial sector. The research has highlighted that some areas of sustainability, especially relating to the economic and environmental dimensions, are actually enhanced by integrated reporting, while the information benefits regarding the social dimension are less evident. The study can help indicate the advantages and possible improvements of the connections between SR and IR.*

1. INTRODUCTION

This study aims to analyze the contribution that integrated reporting (IR) can offer to the improvement of sustainability reporting (SR). In fact, the two accounting tools, although structured on different conceptual bases, have many areas in common thanks to which they are potentially able to reinforce each other.

Since the 1970s (Larrinaga & Bebbington, 2020), sustainability reporting has assumed increasing importance as a tool through which companies disclose information relating to the economic, social and environmental impact of their business, in favor of shareholders and stakeholders (O'Dwyer *et al*., 2005). In the Italian context, sustainability reporting remained optional until 2016 and became mandatory starting from 2017, following the transposition of EU Directive 95/2014, which introduced the obligation of non-financial reporting for large public interest entities.

This study analyzes the sustainability reporting prepared according to the Global Reporting Initiative (GRI) Standards, which today represent one of the reporting tools most used by companies (Christofi *et al*., 2012; Nikolaeva & Bicho, 2011). Integrated reporting is aimed at illustrating how the business strategy and future prospects of the company can preserve, create or destroy value in the short, medium and long term (Busco *et al*., 2013).

The purpose of this research is to verify whether the IR, as future-oriented, is able to enhance the SR which – by definition – is aimed at highlighting the company's ability to act in the present without jeopardizing the future. In this sense, according to the effective and well-known definition of the World Commission on Environment and Development (1987) sustainable development is "*development that meets the needs of the present without compromising the ability of future generations to meet their own needs*" (p. 54).

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In order to analyze the relationships between IR and SR, the research examined the integrated financial statements of two Italian listed companies belonging to the financial sector. Through a content analysis of the 2021 integrated reports, the disclosure on the six capitals – financial, manufactured, intellectual, human, social and relationship, and natural – on which the IR is based was analyzed. At the same time, the non-financial data produced according to the GRI standards were examined and the points of contact between the two sets of information were highlighted.

In particular, the goal of the content analysis was to verify whether the information provided for the purposes of sustainability reporting had connections with that provided for the purposes of IR and it was not simply an addition without relationships.

The research has highlighted how, in theory, there are many commonalities between the two types of reporting, mainly linked to the presence of areas dealing with the same issues. However, in the context of the reports analyzed, the IR is not always closely linked to the SR. In particular, this research has identified a ranking according to which the areas of sustainability that are most integrated with the IR are, in order, the environmental, the economic and, finally, the social ones.

This study contributes to the literature dedicated to the analysis of the most suitable accounting tools to improve sustainability reporting, in a context, such as the current one, in which social and environmental issues are acquiring maximum centrality, also due to the legal pressure deriving from the mandatory of the non-financial disclosure.

In addition, the analysis of the two business cases helps to highlight both the strengths of the IR and the points still subject to improvement, and thus it is useful for the research aimed at enhancing sustainability reporting.

2. THE SUSTAINABILITY REPORTING ACCORDING TO GRI STANDARDS

The Global Reporting Initiative is an independent international organization, founded in Boston in 1997 to support companies and entities – both public and private – in the preparation of their sustainability reports.

The GRI standards are adopted voluntarily and are the result of an elaboration process that began in 2000 with the issue of the first version of the GRI guidelines G1, followed by the G2 guidelines of 2002, the guidelines G3 of 2006 and the guidelines G4 of 2013. In 2016, the transition from the GRI guidelines to the GRI standards took place.

The version applicable to the 2021 financial year consists of 33 topic-specific standards, divided into three main sections – economic, environmental and social.

The widespread use of GRI standards by companies is due to a number of reasons.

First of all, the GRI standards constitute a structured and complete reporting framework useful for guiding the process of disclosure of non-financial information (Hedberg & Von Malmborg, 2003). In this sense, the adoption of GRI standards can help improve the rigor, quality and usefulness of sustainability reporting.

Secondly, the GRI standards provide a sustainability reporting framework characterized by a multi-stakeholder perspective (Islam *et al*., 2011) and try to satisfy the information needs not only of shareholders, but of a wide audience of subjects directly or indirectly involved in business dynamics.

With reference to the financial sector, it is important to remember that its credibility was severely threatened by the 2008 international financial crisis which in many respects can be attributed to the responsibility of the banks and the excessive risk they were willing to take in lending policies. Thus, the adoption of GRI standards has represented for this sector a useful tool for recovering market credibility, improving the image and building a new identity through legitimate behaviors (del Mar Alonso-Almeida *et al*., 2014).

However, it is necessary to consider that the literature has also highlighted the limitations of GRI standards. A first limitation concerns the possibility that non-financial reports are incomplete or not sufficiently transparent, above all due to the flexibility of standardization (Knebel & Seele, 2015). A further limitation of the GRI framework concerns the absence of specific indicators and guides on well-being, despite the fact that it provides a large amount of information regarding indicators on social, human rights, labor practices and environment.

Furthermore, the GRI framework adopts a retrospective approach and uses a structure built according to the same logic of financial reporting (Fonseca *et al*., 2014).

Finally, the GRI framework obscures the achievement of a unified vision by excluding the development of integrated indicators and places the three dimensions of sustainability –economic, environmental and social – on the same level of importance, without considering their relationships (Moneva *et al*., 2006).

This study draws its inspiration from this last criticism and seeks to identify the relationships between the different financial and non-financial dimensions disclosed by companies, in order to highlight the interconnection that could strengthen them.

3. THE INTEGRATED REPORTING ACCORDING TO THE INTERNATIONAL INTEGRATED REPORTING COUNCIL

The purpose of integrated reporting is to combine financial and non-financial information, in order to offer stakeholders as complete a picture of the company as possible, not only referring to the past but also oriented to the future.

The conceptual framework for the drafting of integrated reports was developed by the International Integrated Reporting Council (IIRC), formed in August 2010 in order to create a globally accepted model for communicating the processes of value creation over time.

Integrated reporting must be concise, clear, comprehensive and comparable and must be focused on the strategic objectives of the organization, its governance and its business model.

The conceptual core of integrated reporting is represented by the disclosure of the effects of the six capitals on the creation of value over time. These capitals are: financial capital, manufactured capital, intellectual capital, human capital, social and relationship capital, and natural capital.

Integrated reporting must be future-oriented and must reflect the interconnections between the environment, social, governance and financial factors, highlighting the link between sustainability and economic value. In this sense, integrated reporting can be seen as the latest evolution of reporting on environmental and social aspects related to the activity of an organization as it encourages integrated thinking as a new way of conceiving corporate success (De Villiers and Maroun, 2017). But at the same time, it can also be considered as an evolution of financial reporting, rather than a development of sustainability reporting (Mio, 2016).

If we consider the two perspectives above together, we can see integrated reporting as a form of reporting focused on the financial dimension of the company which also contains information on the sustainability dimension.

Before analyzing the relationships between IR and SR it is important to underline that the two models have different functions and contents. According to Adams (2015), sustainability reporting:

- is aimed at a wider audience of stakeholders than IR, which mainly involves providers of financial capital;
- focuses on the economic, environmental and social impacts of the organization's activity, while IR focuses on creating value through capital.

Given the above, this study is based on the idea that although the SR has aims and recipients in part different from the IR and it is not fungible with the latter, there are still possible connections between the two, thanks to which the information on the economic, environmental and social impact of businesses can be enhanced.

The following section explains these connections through the analysis of the 2021 integrated reports published by two listed Italian companies.

4. EMPIRICAL ANALYSIS

4.1. Methodology

To analyze the integrated reports, the study developed the analysis model (Table 1), in which the possible connections between SR according to GRI standards and integrated reporting according to IIRC are identified.

Table 1. GRI standards and Integrated Reporting frameworks

GRI standards	Integrated Reporting
Economic impact	Financial capital Manufactured capital Intellectual capital Human capital
Environmental impact	Natural capital
Social impact	Social and relationship capital

Source: Author's elaboration

In particular, the connections in Table 1 have been identified based on the following considerations.

- Economic impact. The economic impact identified by the GRI standards was linked to the four capitals – financial, manufactured, intellectual and human – of the IR since they, taken together, define the system of corporate resources directly at the service of production and therefore directly influencing economic performance.

- Environmental impact. The environmental impact identified by the GRI standards has been linked to the natural capital of the IR, since the main areas of disclosure – air, water, materials and biodiversity – are almost the same in both frameworks.
- Social impact. The social impact identified by the GRI standards was linked to the social and relationship capital of the IR since the two frameworks present, as their main common aspect, relations with communities.

It is important to emphasize that the aforementioned connections represent the thematic areas common to the two frameworks, while the approach to reporting followed by each of them, as well as their objectives of disclosure, remain different.

However, this last consideration does not at all exclude that the information on sustainability may be improved once, inserted in the context of integrated reporting; it is used and interpreted also according to the ability of capital to create value. In other words, this study believes that, although different, the two approaches – GRI and IR - are not only not incompatible, but can also reinforce each other.

In particular, the merger between financial and non-financial information can represent an effective tool capable of enhancing the content of reporting and its value for stakeholders, in compliance with the specificities and objectives of each framework.

To verify whether the SR has improved in the context of the IR, the study carried out a content analysis of the integrated reports of two listed Italian companies.

In particular, for each area of the GRI standards, the study verified the presence or absence of information relating to the contribution given by the six company capitals.

To this end, the contents were analyzed on the basis of the three parameters summarized in Table 2.

Table 2. Analysis parameters of the integrated reports

Framework	Evaluation Parameter
IR framework	Presence of disclosure on corporate capitals
GRI framework	Presence of disclosure on sustainability areas (economic, environmental and social)
Merger between IR and GRI framework	Presence of disclosure on relationships between corporate capitals and economic, environmental and social areas

Source: Author's elaboration

Similar to previous studies (Morhardt *et al*., 2002) each parameter was assigned a score, according to the following scale: 0 if disclosure is absent; 1 if the disclosure is summary; 2 if the disclosure is broad and detailed.

Since this operation was carried out for each of the three areas – economic, environmental and social – the maximum score obtainable by each company is equal to 18 (two points for each parameter, for each area), for a total of 36 points (18 points for each company).

4.2. Empirical Findings

The results of the study are summarized in Table 3.

Table 3. Integrated reporting, GRI standards and their merger in two Italian listed companies

Evaluation parameter	Economic area	Environmental area	Social area	Total
Presence of disclosure on specific corporate capitals among the six capitals	4	4	4	12
Presence of disclosure on specific sustainability area (economic, environmental and social)	4	4	4	12
Presence of disclosure on relationships between corporate capital and specific sustainability area	1	2	0	3
Total	**9**	**10**	**8**	**27**

Source: Author's elaboration

The results of Table 3 allow us to make some relevant observations.

First of all, for each of the three sustainability areas, the disclosure is broad (maximum score) both with respect to the integrated reporting framework and with respect to the GRI framework. This result confirms that the overall information provided by the two companies is complete and detailed for both the financial and the non-financial dimensions, considered separately.

Secondly, from the point of view of the individual sustainability areas, the most satisfactory score is obtained from the environmental area while the lowest is for the social area.

As for the environment, this result is mainly due to the fact that the notion of natural capital on which the IR is based has many aspects in common with the environmental dimensions identified by the GRI standards. It follows that natural capital that is able to create value for the environment is at the same time able to produce relevant results also from the perspective of the GRI standards. From this point of view, it is possible to conclude that sustainability reporting can concretely benefit from integrated reporting, since the merger of the information allows to combine the financial and non-financial aspects of the same phenomenon, providing stakeholders with a more complete disclosure.

Otherwise, as regards the social and relationship capital on which the IR is based, the connections with the GRI framework are less evident and this may be due jointly to two factors.

First of all, it is necessary to consider the objective heterogeneity of the areas relevant to the IR and those significant for the SR. In fact, while in the first case the relations between the communities focus mainly on the stakeholders and on aspects concerning the company, such as the brand and the reputation, within the GRI framework the social dimension, although referring to the communities, is more concentrated on work, employment, human rights and non-discrimination.

Secondly, it is important to take into account the propensity or ability of those who draw up the IR to prepare a disclosure capable of combining these two different, but contiguous perspectives, for example by highlighting how social and relationship capital can also create value promoting the well-being of workers.

Finally, in relation to the economic area, the score is intermediate to that of the two previous areas as the study found that the main and almost the only link between capitals and sustainability is represented by the disclosure of the distribution of added value.

5. CONCLUSION

This study aimed to analyze the relationships between integrated reporting and sustainability reporting in order to identify the presence of improvement areas through which to enhance sustainability disclosure.

In this regard, the study highlighted on the one hand that the disclosure provided to stakeholders by the two companies examined is significantly broad and complete, since it combines a large number of financial and non-financial data.

However, as described above, there are areas of sustainability, and in particular the social one, for which IR provides little information on the relationship between labor policies and value creation.

In this regard, an enhancement of disclosure on the social area – which the study highlighted as weaker – could be implemented not only through the reporting of human capital in terms of skills, abilities, experience and motivations, but also through the presentation of the effects on the value creation generated by the policies on employment, health and safety, training and education relevant for GRI standards.

In general, if on the one hand, it is clear that the IR and the SR have different objectives and adopt different reporting approaches, on the other hand, they can reinforce each other, without losing their specificities.

In this sense, rather than a sum of information, the IR should create an information system based on a unitary and comprehensive vision of the economic, environmental and social factors that contribute to the creation, conservation or destruction of value over time.

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