Theoretical Insights on Integrated Reporting: The Inclusion of Non-Financial Capitals in Corporate Disclosures

By **Mark Anthony Camilleri**[1]

This is a pre-publication version.

How to Cite: Camilleri, M.A. (2018). Theoretical Insights on Integrated Reporting: The Inclusion of Non-Financial Capitals in Corporate Disclosures. Corporate Communications: An International Journal. DOI 10.1108/CCIJ-01-2018-0016

Purpose

Corporations and large entities are increasingly disclosing material information on their financial and non-financial capitals in integrated reports (IR). The rationale behind their IR is to improve their legitimacy with institutions and stakeholders, as they are expected to communicate on all aspects of their value-creating activities, business models and strategic priorities. In this light, this contribution traces the theoretical underpinnings that have led to the organizations' environmental, social and governance (ESG) disclosures, and to explain the purpose of integrated thinking and reporting.

Design / Methodology

Following a review of relevant theories in business and society literature, this contribution examines the latest developments in corporate communication. This research explores the GRI's latest Sustainability Reporting Standards as it sheds light on IIRC's <IR> framework. Afterwards, it investigates the costs and benefits of using IR as a vehicle for the corporate disclosures on financial and non-financial performance.

Findings:

This contribution sheds light on the latest developments that have led to the emergence of the organizations' integrated thinking and reporting as they include financial and non-financial capitals in their annual disclosures. The findings suggest that the investors and the other financial stakeholders remain the key stakeholders of many organizations; it explains that they still represent the primary recipients of the corporate reports. However, the integrated disclosures are also helping practitioners to improve their organizational stewardship and to reinforce their legitimacy with institutions and other stakeholders in society, as they embed ESG information in their IR.

Research Limitations / Implications:

This paper has discussed about the inherent limitations of the accounting, reporting and auditing of the organizations' integrated disclosures. It pointed out that the practitioners may risk focusing their attention on the form of their reports, rather than on the content of their integrated reports. Moreover, this contribution implies that the report preparers (and their stakeholders) would benefit if their IR is scrutinized and assured by independent, externally-recognized audit firms.

Originality / Value:

This contribution has addressed a gap in academic literature along two lines of investigation. Firstly, it linked key theoretical underpinnings on the agency, stewardship, institutional and legitimacy theories, with the latest developments in corporate communication. Secondly, it critically evaluated the regulatory instruments, including; GRI's Sustainability Reporting Standards and the <IR>'s framework, among others; as these institutions are supporting organizations in their integrated thinking and reporting.

Keywords: Integrated Reporting, Non-Financial Reporting, Corporate Reporting, Legitimacy Theory, Institutional Theory, Stewardship Theory.

---

[1] Department of Corporate Communication, Faculty of Media and Knowledge Sciences, University of Malta, Msida, MSD2080, MALTA.

Introduction

Several public-interest entities, including listed businesses are already disclosing non-financial information in their corporate reports (Ioannou and Serafeim, 2016; Adams, 2015; Lueg, Lueg, Andersen and Dancianu 2016). They may be driven by an increased awareness of corporate social responsibility (CSR) issues (Elving, Golob, Podnar, Ellerup-Nielsen and Thomson, 2015). Alternatively, they could be influenced by institutions and stakeholder expectations about the role of business in society (Golob, Podnar, Elving, Ellerup Nielsen, Thomsen and Schultz, 2013; Brammer, Jackson and Matten, 2012). The report preparers are often combining financial as well as material information on their environmental, social and governance (ESG) performance in their integrated reporting (IR). Their corporate communications are stimulating 'integrated thinking' (Knauer and Serafeim, 2014) as report preparers gather information on their organizations' governance, performance and prospects from strategic and operational departments (Flower, 2015; de Villiers, Rinaldi and Unerman, 2014). Therefore, they may employ other institutions' regulatory tools and instruments, including standards or frameworks to support them in their internal planning and control purposes (Lueg et al., 2016). The internationally recognized standards, approaches and principles gave led to significant improvements in the organizations' dialogue with a growing variety of stakeholders (Lai, Melloni and Stacchezzini, 2018; Camilleri, 2015, Eccles and Krzus, 2010), and are helping them to increase their accountability for the broad bases of financial and non-financial capitals (Lueg et al., 2016; IIRC, 2013).

There is a wide plethora of possible disclosure formats that may be used for the corporations' ESG disclosures, including the UN Global Compact, OECD guidelines for multinational enterprises, ISO 26000, Global Reporting Initiative (GRI), and the International Integrated Reporting Council (IIRC), among others. These regulatory instruments are intended to address the shortcomings in corporate communications (Dumay, Bernardi, Guthrie and Demartini, 2016; IIRC, 2013), as former stand-alone, financial or social responsibility reports have failed to account for the interconnections between financial and ESG performance (Eccles and Krzus, 2010). Notwithstanding, international and local institutional frameworks can(not) facilitate the organizations' sustainability reporting (Stacchezzini, Melloni and Lai, 2016; Golob, et al., 2013; Jensen and Berg, 2011). As a result, entities may decide to incorporate robust economic, environmental and social performance metrics in support of their overall vision for integrated thinking, as IR provides a holistic picture of their businesses' vallue-creating activities (Maroun, 2018; Simnett and Huggins, 2015; Adams, 2015, Milne and Gray, 2013). The report preparers communicate about their financial as well as on their non-financial performance that is consistent with their corporate strategy. IR presumes that the businesses are willing to engage with different stakeholders, not just financial capital providers (Adams, 2015). Hence, it brings about the socialization of financial and ESG performance, as businesses respond to their stakeholders' legitimate needs and interests (Lai et al., 2018; Higgins, Stubbs and Love, 2014, p. 1102; IIRC, 2013).

Research Question

This contribution addresses a research gap in academia along two lines of investigation. Firstly, it links key theoretical underpinnings from business ethics literature with the ongoing developments in corporate communication. The stewardship, institutional and legitimacy theories have contributed to the advancement of the organizations' responsible and sustainable behaviors that are often reflected in their integrated reporting (de Villiers et al., 2014; Ioannou and Serafeim, 2012; Brammer et al., 2012; Muth and Donaldson, 1998; Davis, Schoorman and Donaldson, 1997; Eisenhardt, 1989). Indeed, the legitimacy theory (Beck, Dumay and Frost, 2015; Deegan, 2002; Suchman, 1995) has often been used to interpret the content of corporate reporting, including CSR communications (Elving et al., 2015; Golob et al., 2013). Thus, this research adds value to the extant literature by exploring the emergence of non-financial reporting within a broader legitimation strategy. It suggests that the organizations' integrated disclosures of material information appertaining to financial, manufactured, intellectual, human, social and natural capitals will help them forge relationships with stakeholders as they improve their legitimacy with institutions and other interested parties. Moreover, the institutional theory, and its related concepts of isomorphism (Dacin, 1997; Deephouse, 1996) and isopraxism (Adams, Potter, Singh and York, 2016) elucidates our interpretation on why corporate reporting approaches are (not) converging toward integrated reporting. Secondly, it critically analyzes specific aspects of GRI's latest Sustainability Reporting Standards and sheds light on the IIRC's <IR> framework. It also investigates the costs and benefits of using integrated reporting for the corporate disclosures on financial and non-financial performance.

The rationale for this contribution is to further consolidate the 'integrated thinking and reporting' of the organizations' capitals in clear, concise and comparable communications (Perego Kennedy and Whiteman, 2016; Knauer and Serafeim, 2014). This paper is a useful complement to the latest empirical studies that explore the causal relationships between the corporate disclosures of ESG performance and organizational legitimacy. In addition, it links key theoretical underpinnings on corporate sustainability and social responsibility literature to the contemporary practices in corporate communication.

Literature Review

Relevant academic literature suggests that the practicing organizations' underlying motive behind their non-financial disclosures is to maximize their financial capital and profit. This argumentation is synonymous with many conceptual theories in academic literature that seek to justify the rationale for voluntary, integrated reporting:

The Agency Theory

In the twentieth century, corporations were clearly distinguishing the difference between the ownership and control of wealth. The business owners were considered as principals as they employed executives (agents) to manage their firms. The executives acted as agents for the principals, and they were morally responsible to maximize their shareholders' wealth (i.e. the principals' wealth). The executives accepted their agents' status because they perceived the opportunity to maximize their own utility. The agency theory suggested that the company executives and their principals are motivated by opportunities for their own personal gain (Eisenhardt, 1989). Rightly so, the principals invest their wealth in profitable companies and will probably design governance systems in ways that will maximize their investments. On the other hand, agents accept the responsibility of managing their principals' undertakings to secure their employment prospects. However, at times, there may be divergences between the managers and their principals. There may be situations where the agents may feel constrained by their principals' imposed structures and controlling mechanisms (Davis et al., 1997). This matter may lead to unproductivity outcomes and could ultimately bring significant losses to the principals themselves. The crux of the agency theory is that the principals are expected to delegate authority to agents to act on their behalf. It is this delegated responsibility that at times allows agents to opportunistically build their own utility at the expense of their principals' utility. This happens when there are unaligned objectives; where managers may be motivated by their individualistic, self-serving goals, rather than by being good stewards for their principals (Eisenhardt, 1989).

The Stewardship Theory

The stewardship theory is the collective-serving model of behavior that is driven by the organizations' intrinsic values. In this case, the organization would do what is best for society and the planet (Donaldson and Davis, 1991). The stewardship behaviors benefit principals through the positive effects of profits on corporate dividends and share prices. Consequently, the stewards place higher value on cooperation, rather than defection (these terms are also found in the game theory), because they perceive greater utility in collaborative behaviors. Stewardship theorists assume that there is a strong relationship between successful organizations and their principals' satisfaction. The stewards protect and maximize their shareholders' wealth because by so doing, they maximize their utility functions toward principals.

Stewards who successfully improve their organizational performance will also satisfy other stakeholder groups who will have their own vested interests. Therefore, pro-organizational stewards are motivated to maximize organizational performance, whilst satisfying the competing interests of shareholders. The utility that they gain from pro-organizational behaviors is higher than the utility that could be gained through individualistic, self-serving behaviors. This theory suggests that stewards believe that their interests are aligned with those of the corporation that engaged them (Muth and Donaldson, 1998). In practice, this theory's ideals are evidenced in IIRC's <IR> Framework as it emphasizes the stewardship of multiple capitals, including; financial, manufactured, intellectual, human, social and natural capital (IR, 2013). In the past, the accountability of social and environmental capitals has often been found to be completely lacking in corporate disclosures (Adams et al., 2016; GRI, 2017). The companies were not always presenting a true and fair view of their externalities, as they were reluctant to promote their responsible and sustainable behaviors (Ioannou and Serafeim, 2017; Eccles and Krzus, 2010). This may be due to a lack of awareness on the business case for such activities (Camilleri, 2015). The organizations' motivations for undertaking the stewardship behaviors, including the ESG initiatives seem to fall into two converging camps: doing good practices (this is consistent with the predictions of the stewardship theory) or doing well (this is consistent with the institutional and legitimacy theories).

The Institutional Theory

Organizations react to the institutional pressures by adopting rules and procedures (Suchman 1995). Different components of the institutional theory explain how certain processes become established as authoritative guidelines for societal behaviors. Very often, structures and institutions are created, diffused, adopted, and adapted over space and time; and eventually they may also fall into decline and disuse. This theory acknowledges that individuals and organizations have the capacity to create, maintain, and change institutions through various mechanisms (Meyer and Rowan 1977). Unlike the efficiency-based theories which focus on profit maximization, or on the interactions between markets and governments; the institutional theory considers a wider range of variables that could influence the decision-making processes in organizations, including; their span of control, job programmability and compensation policy, among others (Eisenhardt, 1988). The situational variables arising from the immediate job context and the broader organizational culture could influence the organizations' normative structures and reinforcement contingencies, including; the individual employees' obedience to authority, and their pressures to accept responsibility for their behaviors.

The institutional theory clarifies how firms respond to their surrounding environments where they operate. Stakeholders, including; governments, regulatory authorities, NGOs, and other organizations within the supply chain can exert their influence on businesses. Organizations must conform to the institutional norms and rules that are prevailing in their operating environment. As a result, their compliance with the formal regulations will earn them legitimacy among stakeholders (Beck et al., 2015; Hahn and Lülfs, 2014; Dacin, 1997; Deephouse, 1996; Suchman, 1995). Further research is showing how the institutions effect organizational behaviors, particularly on CSR disclosure issues (Adams, 2015). Historically, the notion of CSR has emerged from the institutionalized forms of social solidarity that have emerged from liberal market economies. Therefore, the institutional theory offers promising ways of investigating what lies at the heart of the publics' concern as the corporations are influenced by the institutions' ethos, voluntary principles, policies and programs (Camilleri, 2015). Their responsible behaviors have often been triggered by socio-political forces and pressure groups (Elving et al., 2015). In this case, CSR practice and its reporting rests on the dichotomy between the corporations' voluntary engagement and their socially-binding responsibilities (Brammer et al., 2012). The fact that CSR disclosures remained a 'voluntary' practice in many contexts, is a clear reflection of the organizations' institutional context (De Villiers, Venter and Hsiao, 2017; Stacchezzini, Melloni and Lai, 2016; Camilleri, 2015). Numerous institutions have played a dynamic role, both individually and collectively in the development of integrated reporting (Jensen and Berg, 2012; Jackson and Apostolakou, 2010). While governments have been the primary force for the promotion of financial reporting standards through security exchange commissions; other institutions like the UN Global Compact, OECD, ISO, GRI and IIRC, among others, as they have facilitated the growth and diffusion of non-financial reporting mechanisms (Camilleri, 2015; Adams, 2015).

Isomorphism and Isopraxisim

Isomorphism has been constructed in conjunction with the applications of the institutional theory (Dacin, 1997). This concept has been propagated through cultural and associational processes that arise when ideas or innovations travel, and are adopted in different contexts (Dacin, 1997; Deephouse, 1996). For example, in this day and age, a previously-isolated island society that makes contact with the rest of the globe, would quickly take on standardized forms of economic forces, power relationships, and cultures that are similar to other nation-states around the world. Similarly, the notion of isopraxism refers to ideas that are translated and modified by different actors to suit their own needs. Isomorphism and its related notion, isopraxism are potentially helpful to framing our interpretation of why integrated reporting approaches may converge (or not) over time.

For example, the principles-based and non-mandatory <IR> Framework could potentially create explicit and implicit reporting norms that could encourage the organizations' non-financial disclosures through integrated reporting. Humphrey, O'Dwyer and Unerman (2016) argued that IIRC has claimed an institutional space which consists of competing, non-integrated, sets of corporate reporting initiatives. They suggested that the <IR> framework offers something to 'everyone' as it may appeal to new, enlightened long-term investors. In this sense, isomorphism may be useful to understand how and why the disclosures of ESG content can become widely accepted across companies, over time (Adams et al., 2016; Deephouse, 1996). In a similar vein, isopraxism has been used to describe instances where identifiable institutional forces may lead to new and different actions within specific organizational and social instances. Therefore, isopraxism suggests that the legitimate organizations may be intrigued to move toward more integrated approaches to reporting.

The Legitimacy Theory

Organizations prepare integrated reports in an attempt to maintain and repair their legitimacy among stakeholders (De Villiers et al., 2017). Their sustainability accounting and disclosures will usually reflect the institutional environments' values and expectations (Camilleri, 2015). As a result, responsible organizations become legitimate entities; particularly, if they comply with the relevant societal rules and norms (Beck et al., 2015; Deegan, 2002). The organizations' stakeholders will probably appraise the legitimate organizations who uphold their social contract, when "their actions are desirable, proper, or appropriate within some socially-constructed system of norms, values, beliefs, and definitions" (Suchman, 1995, p. 574). Therefore, the drivers of the institutional legitimacy may be influenced by the organizations' external environment; according to the culturally-defined values and beliefs in society. On the other hand, stakeholders will severely sanction irresponsible organizations when they do not respect the societal norms and ethical values.

Suchman (1995) described the concept of legitimacy as an operational resource assuming a “high level of managerial control over legitimization processes” (p. 576). Similarly, Hedberg and Malmborg (2003) contended that legitimate companies increased their credibility of their CSR engagement among stakeholders. These authors used the GRI guidelines as a vehicle for their organizational legitimacy. Other researchers suggested that legitimacy is strategic as it emanates from recurring conflicts between management and stakeholders (Dacin, Oliver and Roy, 2007; Suchman 1995). Arguably, the organizational legitimacy can be achieved by forging strong relationships with stakeholders. For this reason, organizations ought to adapt their corporate disclosures according to their stakeholders’ expectations, to garner their trust and achieve legitimacy (Hahn and Lülfs, 2014). However, any changes in corporate reporting should be driven by the organizations’ internal decisions on materiality (Eccles and Krzus, 2014). Hence, the managers’ agenda is to strategically enhance their organizational legitimacy by reporting material information on their financial and non-financial performance.

The Corporations’ Non-Financial Disclosures

The American Institute of Certified Public Accountants’ Jenkins Report may be considered as one of the major documents that has provided the foundations for non-financial disclosures (Rivera-Arrubla, Zorio-Grima and García-Benau, 2017). Notwithstanding, there were other guidelines that were developed by other non-governmental organizations (NGOs), including; the Global Reporting Initiative, AccountAbility, Accounting for Sustainability (A4S), the World Intellectual Capital Initiative (WICI), the Enhanced Business Reporting Consortium, the CDP (formerly known as the Carbon Disclosure Project), the International Corporate Governance Network, the Sustainability Reporting Standards Board and the Climate Disclosure Standards Board, among others. The International Standards Organization (ISO), Forest Stewardship Council (FSC), Greenpeace, Rainforest Alliance and Home Depot Certifiable, Fair Trade and the US Department of Agriculture’s USDA Organic Labelling, among others, have formulated uncertifiable, multi-stakeholder standards and instruments (Castka and Corbett, 2016) to support organizations in their CSR communication. In addition, certain listed corporations are adopting Fortune’s reputation index, the KLD Social index or RepTrak (Camilleri, 2017). Such measures require corporate executives to assess the extent to which their organization behaves responsibly towards the environment and the community.

Despite the development of these guiding principles and indices, their appropriateness remains doubtful (Camilleri, 2017; Adams, 2015).

In 2010, the development of ISO 26000 had represented a significant milestone in integrating socially and environmentally responsible behaviors into management processes (Toppinen, Virtanen, Mayer, and Tuppura, 2015; Hahn, 2013). ISO 26000 was developed through a participatory multi-stakeholder process as the International Labor Organization (ILO) had established a Memorandum of Understanding (MoU) to ensure that ISO’s social responsibility standard is consistent with its own labor standards. In fact, ISO 26000’s core subject on ‘Labor Practices’ is based on ILOs’ conventions on labor practices, including; Human Resources Development Convention, Occupational Health and Safety Guidelines, Forced Labor Convention, Freedom of Association, Minimum Wage Fixing Recommendation and the Worst Forms of Child Labor Recommendation, among others. Moreover, ISO’s core subject on ‘human rights’ is based on the Universal Declaration of Human Rights (that was adopted by the UN General Assembly in 1948). On the other hand, many academic commentators argue that ISO 26000 has never been considered as a management standard (Camilleri, 2017). The certification requirements have not been incorporated into ISO 26000’s development and reinforcement process, unlike other standards, including ISO 9000 and ISO 14001 (Hahn, 2013). Notwithstanding, ISO 14001 belongs to a larger set of ISO 14000 certifications that conform with the European Union's Eco-Management and Audit Scheme (EMAS) (Lueg et al, 2016).

The European Union (EU) has developed its non-binding guidelines for the non-financial disclosures of large, public-interest entities that engage more than 500 employees (Stubbs and Higgins, 2015; EU, 2014). The European Parliament mandated Directive 2014/95/EU on non-financial reporting; that was subsequently ratified by the European member states. Therefore, large undertakings are expected to disclose material information on their ESG behaviors. These entities are required to explain any deviations from their directive’s recommendations in their annual declaration of conformity, as per the EU’s “Comply or Explain” principle (Camilleri, 2015; EU, 2014). Their non-financial disclosures include topics, such as; social dialogue with stakeholders, information and consultation rights, trade union rights, health and safety and gender equality, among other issues. Moreover, the organizations’ environmental reporting could cover; material disclosures on energy efficiencies, the monitoring of efficiency levels their energy generation capacities, assessments on the co-generation of heating facilities, the use of renewable energy, greenhouse gas emissions, water and air pollution prevention and control from the production and processing of metals, mineral industry, chemical industry, waste management, livestock farming, etc. (EU, 2014). Therefore, large undertakings are expected to bear responsibility for the prevention and reduction of pollution. The EU recommends that the large organizations implement ILO’s Tri-partite Declaration of Principles on Multinational Enterprises and Social Policy, as well as other conventions that promote the fair working conditions of employees. It also makes reference to the OECD Guidelines for Multinational Enterprises, the 10 principles of the UN Global Compact, the UN Guiding Principles on Business and Human Rights, and mentions ISO 26000 Guidance Standard on Social Responsibility (EU, 2014). Following, the EU’s mandate for non-financial reporting, it is expected that 6,000 European public interest entities will be publishing their sustainability reports in 2018, covering financial year 2017-2018 (GRI, 2017).

Sustainability Reporting

In the past two decades, many entities started to incorporate economic, environmental and social performance indicators that were reinforced and institutionalized through GRI’s sustainability reporting guidelines (Stacchezzini et al., 2016; Simnett and Huggins, 2015; Milne and Gray, 2013). The Global Reporting Initiative (GRI) was one of the earliest proponents of sustainability reporting (Hahn and Lülfs, 2014; Hedberg and Von Malmborg, 2003). GRI was formed in 1997 by two United States-based non-governmental organizations, namely; Coalition for Environmentally Responsible Economies (Ceres) and Tellus Institute, in collaboration with the United Nations Environment Program (UNEP). In 2000, GRI released its Sustainability Reporting Guidelines during the World Summit for Sustainable Development in Johannesburg. In 2013, GRI’s Sustainability Reporting Guidelines were promoted as the G4 guidelines. Eventually, the G4 Guidelines were superseded by the GRI Sustainability Reporting Standards (GRI Standards) on the 1st July 2018.

GRI claims that its latest Standards represent global best practice for the public reporting on a range of economic, environmental and social impacts. The GRI report preparers are expected to provide material information about their organizations’ positive or negative contributions to sustainable development. Their sustainability report should include three Universal Standards, namely; GRI 101 (foundation), GRI 102 (general disclosures) and GRI 103 (management approach).

GRI 101 is the starting point for using GRI standards as it presents the Reporting Principles that define the content and quality of the disclosures. It explains the basic processes and the fundamental requirements for the reporting of material topics. GRI 102 describes the contextual information on the organization's profile, strategy, ethics (and integrity), governance, stakeholder engagement practices, and reporting process. This section provides the context for subsequent, more detailed reporting on the organizations' economic, environmental and social impacts. GRI 103 provides narrative information of how organizations identify, analyze and respond for their economic, environmental and social impacts. Whilst GRI 200 (Economic), GRI 300 (Environmental) or GRI 400 (Social) Standards have been designed to enhance the global comparability and quality of information on the organizations' impacts, thereby enabling greater transparency and accountability of practitioners (GRI, 2016).

The sustainability disclosures have a lengthy tradition of voluntary reporting, unlike the corporations' financial statements (Stubbs 2015). The proponents of the voluntary reporting argue that the businesses respond to their stakeholders' requirements, by being accountable and transparent about their sustainability. While the businesses may willing to embed sustainable practices in their operations, many stakeholders may question the reliability of the voluntary sustainability reports. While it may appear that businesses may support the voluntary approaches, relevant research suggests that in some contexts they may support mandatory approaches (de Villiers and van Staden, 2011). Beck et al. (2017) reported that the organizations' relationship with external guidelines has evolved from their compliance as a means of seeking external legitimation to the present pragmatic position, where their ESG disclosures are informed by the organization's strategic positioning, and not constrained by the promulgation of voluntary guidelines.

Very often, the practitioners' sustainable performance is not independently verified or assured (Stubbs, 2015). GRI prescribed the threshold for the definition of the material topics whilst describing the context of the reporting organization. In a similar vein, AccountAbility recommends the materiality tests, as practitioners are expected to communicate on their transparent processes of stakeholder engagement. Organizations are subjected to external assurance mechanisms, that examine the process and the results (Maroun, 2018). However, in practice, the report preparers are not always adopting all of the standard setters' guidelines (Eccles and Krzus, 2014). This argumentation strengthens the case for the regulatory approaches to address the lack of enforcement mechanisms as enforceable rules can foster compliance and credible report assurance practices (Maroun, 2018). The regulations will only provide the minimum norms with which corporations have to comply (Ioannou and Serafeim, 2014). Lately, the sustainability reporting is evolving to include more interdependencies with the financial information (Camilleri, 2017) as environmental, social and governance issues are embedded into the organizational strategy (Jensen and Berg, 2012).

Integrated Reporting

An increasing number of academics, governments, audit firms, interest groups and businesses are advocating the publication of integrated disclosures that link financial and ESG performance in one report (de Villiers and Maroun, 2017; Beck et al., 2017; Adams, 2015; Eccles and Krzus, 2010). The organizations' ethical behaviors are often equated with their obligation to disclose a true and fair view of their financial and non-financial performance (Maniora, 2015; Simnett and Huggins, 2015; Adams, 2015; EU, 2014).

In the aftermath of the global economic and financial crisis of 2007–2008, many policy makers, regulatory authorities and leading financial institutions were willing to improve the content of their corporate reporting. At the same time, there was an increased awareness on how the communication of ESG issues could help them enhance their corporate reputation and image (Camilleri, 2015). As a result, in 2010, the Prince of Wales' Accounting for Sustainability Project together with the Global Reporting Initiative (GRI), and the International Federation of Accountants (IFAC) established the International Integrated Reporting Committee (IIRC). Subsequently, it changed its name to International Integrated Reporting Council. The IIRC's <IR> framework has somewhat addressed the perennial criticisms and shortcomings of sustainability reporting, as it considered all of the organizational capitals (Stacchezzini et al., 2016; Jensen and Berg, 2012). Other major changes brought about by IIRC was an increased emphasis on materiality (Montecalvo, Farneti and de Villiers, 2018).

An Appraisal on Integrated Reporting

IIRC's <IR> framework has aligned financial and non-financial capital allocations with specific corporate behaviors (Fasan and Mio, 2017; Camilleri, 2017). It has categorized different stocks of value, including; Financial Capital; Manufactured Capital; Intellectual Capital; Human Capital; Social (and Relationship) Capital; as well as Natural Capital (IR, 2013). IIRC explains how industry and firm-level characteristics (including; board size and diversity) can play a significant role in the determination of material, non-financial disclosures. Therefore, the concept of materiality is fundamental to its audit and assurance (Eccles, and Krzus, 2014). García-Sánchez and Noguera-Gámez (2017) suggested that IIRC's <IR> tool can help to mitigate agency problems and can also improve the quality of material information for investors. IR facilitates corporate decision-making as it breaks down operational and reporting silos, resulting in improved systems and processes (Stubbs and Higgins, 2015).

The <IR> framework's strategic focus calls for both internalization and externalization processes. Internalization is a process through which the organization's human resources adopt the framework's external ideas, opinions, views or concepts, as their own. This process starts with learning about the reporting framework. Afterwards, the report preparers will be in a position to understand how its implementation makes sense to their organization, as a whole. The internal stakeholders will probably experience a process of adaptation until they finally accept that their organization's integrated reporting of financial and non-financial capitals creates value for them, over time. Thus, the internalization process can be understood as a process of acceptance of a new set of norms and working practices that could ultimately improve the organization's holistic performance in the long term. The organizations' internal transformation may lead to significant changes in 'integrated thinking', as they embed ESG performance with their strategic and operational processes.

The organizations' non-financial disclosures will shed light on the externalities that affect their stakeholders, the environment and other unrelated parties. In other words, through integrated reporting; the internal effects of integrated reporting are finally externalized outside the organizations' boundaries. At times, organizations may intentionally or unintentionally conceal ESG information from their corporate reporting. Such unethical practices may result from conscious or unconscious organizational behaviors, or from corporate misconduct when dealing with extensive information outputs. Hence, IIRC's <IR> framework encourages organizations to report both positive and negative behaviors that substantively affect their ability to create value over the short, medium and long term. Practitioners are also expected to provide adequate and sufficient contextual information about their capitals in their corporation communication. Nevertheless, despite the increased proliferation of integrated disclosures, only a few scholars have taken an optimistic stance on IR (Lai et al., 2018; Maroun, 2018; Flower, 2015; Stubbs and Higgins, 2014).

A Critique on Integrated Reporting

A few commentators argued that IIRC's framework focuses on the information demands of capital providers, and did not address the decision-making and accountability needs of other stakeholders (Brown and Dillard, 2014). Rensburg and Botha (2014) suggested that the integrated reports should be simplified and made comprehensible to a wider stakeholder audience. They maintained that this report should be easily understood by the general public. Stubbs and Higgins (2014) argued that IR focuses on the 'supply side', namely, the preparers of the corporate statements, whilst leaving out the 'demand side', i.e. the market stakeholders. These authors held that there was a significant gap between the information that was supplied by the reporting companies and the information that was sought by the financial markets. De Villiers et al. (2014) contended that the close connections between the report preparers and the investors can limit its potential to help other stakeholders to better understand the non-financial impacts of their organization.

Other researchers maintained that the IIRC's framework comprised ambiguous meanings and assessments of non-financial capitals, that have inevitably led to complexities in the assurance mechanisms of integrated reports (Maroun, 2018; Cheng, Green, Conradie, Konishi and Romi, 2014). Notwithstanding, the integrated disclosures are not scrutinized by externally-recognized assurance mechanisms. Rivera-Arrubla et al. (2016) reported that the level of the corporate disclosures is significantly associated with the specific contextual environment (i.e. region and industry) of the practitioners. Therefore, the report preparers ought to identify the recipients (i.e. the users) of their integrated reports (Adams et al., 2016). Pistoni, Songini and Bavagnoli (2018) noticed that the IR reports were not disclosing appropriate information on their business model, strategic priorities, and on their companies' value creation processes; as more attention was devoted to the form of the IR disclosures, rather than on their content. Flower (2015) posited that investors and societal stakeholders have different needs and expectations. A number of criticisms have been levelled at IR, particularly on its emphasis to satisfy the financial capital providers, to the detriment of other key stakeholders (Cheng et al., 2014).

Businesses tend to focus on creating value through profit maximization for their capital providers (Rowbottom and Locke, 2016; Flower, 2015; Adams, 2015; Van Bommel, 2014; Eisenhardt, 1989). Therefore, IR offers a limited approach to ensure the corporate accountability toward stakeholders (Brown and Dillard, 2014; Flower, 2015). Whilst, investors and creditors require financial information regarding their future profitability, external stakeholders expect broad-based information, irrespective of corporate interest. These stakeholders, including the organizations' customers (and prospects), suppliers, regulatory authorities, and the community at large, hold different views on what capital should be emphasized (Van Bommel, 2014). Flower (2015) argued that report preparers had no obligation to disclose their externalities (on the environment), where there is no subsequent impact on their firm. Similarly, Perego et al. (2016) hinted that the report preparers made different value judgments when anchoring the effects of their ESG information. It is very unlikely that they trade-off different forms of financial and non-financial capital, in line with the requirements of IIRC's framework (de Villiers et al., 2017).

By adopting key financial reporting conventions, and linking materiality to value creation, IR might not extend the accountability of the organizations' capitals (Deegan, 2013). Moreover, Brown and Dillard (2014) claimed that IR actually centers more on stakeholder management rather than on stakeholder accountability. Such argumentation suggests that academia is not convinced that IR has successfully improved the corporate accountability on financial and non-financial performance. Perhaps, the accountancy profession should exercise its authority over the institutional processes in order to bring a fundamental shift in framing the accountability, reporting and assurance of the organizations' ESG performance (Lai et al., 2018; Beck et al., 2017).

Conclusions and Future Research Avenues

The practice of sustainability and integrated reporting has evolved because of the stakeholders' needs for corporate communication. Relevant academic literature has yielded many recommendations, ideas and concepts that have surely improved the quality of corporate reporting. A critical review of different regulatory tools and voluntary instruments for the organizations' financial and non-financial disclosures suggests that the practice of integrated reporting represents a new strand for the communication of corporate responsible and sustainable behaviors. Therefore, this research adds value to academic knowledge by linking key conceptual developments from the business ethics literature with the contemporary developments in corporate communication. This contribution explains that the agency, stewardship, institutional and legitimacy theories have anticipated the development of the sustainability standards and led to the organizations' integrated reporting of financial and non-financial capitals. The author has presented an appraisal and a critique of GRI's latest Sustainability Reporting Guidelines and of IIRC's <IR> framework, and its content elements. Businesses and other entities can use IR to communicate about the strategic positioning of their financial and non-financial capitals to stakeholders. The investors and the other financial stakeholders remain the key stakeholders of many organizations, and they continue to represent the primary recipients of the corporate reports. However, other stakeholders are also putting pressure on corporations and public interest entities to disclose more information on social issues and on matters relating to governance, environmental sustainability in their annual statements. This is in line with the aim of IR, as both financial and non-financial stakeholders have basic, convergent expectations about the companies' strategies (IIRC, 2013). Therefore, the integrated disclosures of material information appertaining to financial and non-financial performance will help them forge important relationships with different stakeholders, as they improve their stewardship and legitimacy with institutions and other interested parties.

The findings of this paper suggest that IR has provided a passive avenue for the legitimization of corporations and large entities (Maroun, 2018; de Villiers et al., 2017; Adams et al., 2015; Beck et al., 2015; Dacin et al., 2007; Brown and Deegan, 1998) among stakeholders, as responsible organizations can disclose material information on their financial, manufactured, intellectual, human, social and natural capitals. Despite the critiques and the inherent limitations of IR that were duly covered in this paper, the researcher believes that in future organizations should be encouraged to disclose a true and fair view of their holistic activities, by including material aspects on their non-financial performance. This implies that the report preparers may require a dynamic process of adaptation, learning and action, as they have to redesign, implement and control their strategic and operational procedures that lead to "integrated thinking". Hence, they will be in a position to incorporate financial and non-financial capitals in their IR disclosures.

In conclusion, this contribution implies that there is scope for organizations to consolidate their 'integrated thinking and reporting' in clear, concise and comparable communications. It suggests that the integrated disclosures of the organizations' capitals and their value-creating activities could catalyze positive behavioral changes in society and the environment. Therefore, future research could investigate the difficulties in the corporate accounting of non-financial capitals, as well as the audit and assurance of their integrated reports. To date, there is still scant empirical evidence on how IR can be used for the corporate communication of the businesses' holistic activities, and little is known about the effectiveness of IR for organizational stewardship and legitimacy.

Acknowledgements

The author declares that he does not have any potential conflict of interest. He was not supported by third parties.

References

Adams, C.A. (2015), "The international integrated reporting council: a call to action", *Critical Perspectives on Accounting*, Vol. 27, pp. 23-28.

Adams C.A., Potter, B., Singh, P.J. and York J (2016), "Exploring the implications of integrated reporting for social investment (disclosures)", *British Accounting Review,* Vol. 48, No. 3, pp. 283-296.

Beck, C., Dumay, J. and Frost, G. (2015), "In pursuit of a 'single source of truth': from threatened legitimacy to integrated reporting", *Journal of Business Ethics*, Vol. 141, No. 1, pp.191-205.

Brammer, S., Jackson, G. and Matten, D. (2012), "Corporate social responsibility and institutional theory: New perspectives on private governance", *Socio-economic review*, Vol. 10, No. 1, pp. 3-28.

Brown, N. and Deegan, C. (1998). "The public disclosure of environmental performance information—a dual test of media agenda setting theory and legitimacy theory", *Accounting and business research*, Vol. 29, No. 1, pp. 21-41.

Brown, J. and Dillard, J. (2014), "Integrated reporting: On the need for broadening out and opening up", *Accounting, Auditing and Accountability Journal*, Vol. 27, No. 7, pp. 1120-1156.

Camilleri, M. A. (2015), "Environmental, social and governance disclosures in Europe", *Sustainability Accounting, Management and Policy Journal*, Vol. 6, Bo. 2, pp. 224-242.

Camilleri, M.A. (2017), "Measuring the corporate managers' attitudes towards ISO's social responsibility standard", *Total Quality Management and Business Excellence*, available at: DOI: 10.1080/14783363.2017.1413344 (Accessed 12th May, 2018).

Castka, P. and Corbett, C. J. (2016), "Governance of eco-labels: Expert opinion and media coverage", *Journal of Business Ethics*, Vol. 135, No. 2, pp. 309-326.

Cheng, M., Green, W., Conradie, P., Konishi, N. and Romi, A. (2014), "The international integrated reporting framework: key issues and future research opportunities", *Journal of International Financial Management and Accounting*, Vol. 25, No. 1, pp. 90-119.

Churet, C. and Eccles, R. G. (2014), “Integrated reporting, quality of management, and financial performance”, *Journal of Applied Corporate Finance*, Vol. 26, No. 1, pp. 56-64.

Dacin, M. T. (1997), “Isomorphism in context: The power and prescription of institutional norms”, *Academy of management journal*, Vol. 40, No. 1, pp. 46-81.

Dacin, M. T., Oliver, C. and Roy, J. P. (2007), “The legitimacy of strategic alliances: An institutional perspective”, *Strategic Management Journal*, Vol. 28, No. 2, pp. 169-187.

Davis, J. H., Schoorman, F. D. and Donaldson, L. (1997), “Toward a stewardship theory of management”, *Academy of Management review*, Vol. 22, No. 1, pp. 20-47.

Deegan, C. (2002). “Introduction: The legitimising effect of social and environmental disclosures–a theoretical foundation”, *Accounting, Auditing and Accountability Journal*, Vol. 15, No. 3, pp. 282-311.

Deegan, C. (2013), “The accountant will have a central role in saving the planet… really? A reflection on green accounting and green eyeshades twenty years later”, *Critical Perspectives on Accounting*, Vol. 24, No. 6, pp. 448-458.

Deephouse, D. L. (1996), “Does isomorphism legitimate?”, *Academy of management journal*, Vol. 39, No. 4, pp. 1024-1039.

de Villiers, C. and van Staden, C. (2011), “Shareholder requirements for compulsory environmental information in annual reports and on websites”, *Australian Accounting Review*, Vol. 21, No. 4, pp. 317-326.

de Villiers, C., Rinaldi, L. and Unerman, J. (2014), “Integrated Reporting: Insights, gaps and an agenda for future research”, *Accounting, Auditing and Accountability Journal*, Vol. 27, No. 7, pp. 1042-1067.

de Villiers, C. and Maroun, W. (2017), “Introduction to sustainability accounting and integrated reporting”, In *Sustainability Accounting and Integrated Reporting* Routledge, Oxford, UK, pp. 13-24.

de Villiers, C., Venter, E. R. and Hsiao, P. C. K. (2017), “Integrated reporting: background, measurement issues, approaches and an agenda for future research”, *Accounting and Finance*, Vol. 57, No. 4, pp. 937-959.

Donaldson, L. and Davis, J. H. (1991), “Stewardship theory or agency theory: CEO governance and shareholder returns”, *Australian Journal of management*, Vol. 16, No. 1, pp. 49-64.

Dumay, J., Bernardi, C., Guthrie, J. and Demartini, P. (2016), “Integrated reporting: a structured literature review”, *Accounting Forum*, Vol. 40, No. 3, pp. 166-185.

Eccles, R.G. and Krzus, M.P. (2010), *One report: Integrated reporting for a sustainable strategy*, John Wiley and Sons, Hoboken, NJ, USA.

Eccles, R.G. and Krzus, M.P. (2014), *The integrated reporting movement: Meaning, momentum, motives, and materiality*, John Wiley and Sons, Hoboken, NJ, USA.

Eisenhardt, K.M. (1988), “Agency-and institutional-theory explanations: The case of retail sales compensation”, *Academy of Management journal*, Vol. 31, No. 3, pp. 488-511.

Eisenhardt, K.M. (1989), “Agency theory: An assessment and review”, *Academy of management review*, Vol. 14, No. 1, pp. 57-74.

Elving, W. J., Golob, U., Podnar, K., Ellerup-Nielsen, A., & Thomson, C. (2015), “The bad, the ugly and the good: new challenges for CSR communication”, *Corporate Communications: An International Journal*, Vol. 20, No. 2, pp. 118-127.

EU (2014), “Non-financial reporting”, available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32014L0095 (accessed 15th June 2018).

EU (2015), “Implementing the UN Guiding Principles on Business and Human Rights - State of Play”, Commission Staff Working Document SWD (2015)144 final, available at: http://ec.europa.eu/DocsRoom/documents/11621/attachments/1/translations/ (accessed 15 May 2018).

Fasan, M. and Mio, C. (2017), “Fostering stakeholder engagement: The role of materiality disclosure in Integrated Reporting”, *Business Strategy and the Environment*, Vol. 26, No. 3, pp. 288-305.

Flower, J. (2015), “The international integrated reporting council: a story of failure”, *Critical Perspectives on Accounting*, Vol. 27, pp. 1-17.

García-Sánchez, I. M. and Noguera-Gámez, L. (2017), “Integrated Reporting and Stakeholder Engagement: The Effect on Information Asymmetry”, *Corporate Social Responsibility and Environmental Management*, Vol. 24, No. 5, pp. 395-413.

Golob, U., Podnar, K., Elving, W. J., Ellerup Nielsen, A., Thomsen, C., & Schultz, F. (2013), CSR communication: quo vadis?. *Corporate Communications: An International Journal*, Vol. 18, No. 2, pp. 176-192.

GRI (2016), “GRI Standards Download Centre”, available at: https://www.globalreporting.org/standards/gri-standards-download-center/ (Accessed 14th June, 2018).

GRI (2017), “Member State Implementation of Directive 2014/95/EU”, available at: https://www.globalreporting.org/resourcelibrary/NFRpublication%20online_version.pdf (accessed 12th June, 108)

Hahn, R. (2013), “ISO 26000 and the standardization of strategic management processes for sustainability and corporate social responsibility”, *Business Strategy and the Environment*, Vol. 22, No. 7, pp. 442-455.

Hahn, R. and Lülfs, R. (2014), “Legitimizing negative aspects in GRI-oriented sustainability reporting: A qualitative analysis of corporate disclosure strategies”, *Journal of Business Ethics*, Vol. 123, No. 3, pp. 401-420.

Hedberg, C.J. and Von Malmborg, F. (2003), “The global reporting initiative and corporate sustainability reporting in Swedish companies”, *Corporate social responsibility and environmental management*, Vol. 10, No. 3, pp. 153-164.

Higgins, C., Stubbs, W. and Love, T. (2014), “Walking the talk (s): Organizational narratives of integrated reporting”, *Accounting, Auditing and Accountability Journal*, Vol. 27, No. 7, pp. 1090-1119.

Humphrey, C., O’Dwyer, B. and Unerman, J. (2016), “Re-theorizing the configuration of organizational fields: The IIRC and the pursuit of ‘Enlightened’ corporate reporting”, *Accounting and Business Research*, Vol. 47, No. 1, pp. 1–34.

Ioannou, I. and Serafeim, G. (2012), “What drives corporate social performance? The role of nation-level institutions”, *Journal of International Business Studies*, Vol. 43, No. 9, pp. 834-864.

Ioannou, I., & Serafeim, G. (2017). The consequences of mandatory corporate sustainability reporting. Available at: https://papers.ssrn.com/soL3/papers.cfm?abstract_id=1799589 (accessed 15th June, 2018).

IIRC (2013), “International IR Framework, International Integrated Reporting Council”, available at: http://integratedreporting.org/wp-content/uploads/2013/12/13-12-08-THE-INTERNATIONAL-IR-FRAMEWORK-2-1.pdf (accessed 16 May, 2018).

Jackson, G. and Apostolakou, A. (2010), “Corporate social responsibility in Western Europe: an institutional mirror or substitute?”, *Journal of Business Ethics*, Vol. 94, No. 3, pp. 371-394.

Jensen, J. C. and Berg, N. (2012), “Determinants of traditional sustainability reporting versus integrated reporting. An institutionalist approach”, *Business Strategy and the Environment*, Vol. 21, No. 5, pp. 299-316.

Lai, A., Melloni, G. and Stacchezzini, R. (2018), “Integrated reporting and narrative accountability: the role of preparers”, *Accounting, Auditing and Accountability Journal*, available at: https://doi.org/10.1108/AAAJ-08-2016-2674 (Accessed on the 5th June 2018).

Knauer, A. and Serafeim, G. (2014), “Attracting Long-Term Investors Through Integrated Thinking and Reporting: A Clinical Study of a Biopharmaceutical Company”, *Journal of Applied Corporate Finance*, Vol. 26, No. 2, pp. 57-64.

Lueg, K., Lueg, R., Andersen, K. and Dancianu. V. (2016), "Integrated reporting with CSR practices: a pragmatic constructivist case study in a Danish cultural setting." *Corporate Communications: An International Journal,* Vol. 21, No. 1, pp. 20-35.

Maniora, J. (2015), Is integrated reporting really the superior mechanism for the integration of ethics into the core business model? An empirical analysis. *Journal of Business Ethics*, Vol. 140, No. 4, pp. 755-786.

Maroun, W. (2018), “Modifying assurance practices to meet the needs of integrated reporting: the case for interpretive assurance”, *Accounting, Auditing and Accountability Journal,* available from: *https://www.emeraldinsight.com/doi/abs/10.1108/AAAJ-10-2016-2732* (Accessed 14th June 2018).

Meyer, J. W., & Rowan, B. (1977). Institutionalized organizations: Formal structure as myth and ceremony. *American journal of sociology*, *83*(2), 340-363.

Milne, M. J. and Gray, R. (2013), "W(h)ither ecology? The triple bottom line, the global reporting initiative, and corporate sustainability reporting", *Journal of Business Ethics*, Vol. 118, No. 1, pp. 13-29.

Montecalvo, M., Farneti, F. and de Villiers, C. (2018), "The potential of integrated reporting to enhance sustainability reporting in the public sector", *Public Money and Management*, Vol. 38, No. 5, pp. 365-374.

Muth, M. and Donaldson, L. (1998), "Stewardship theory and board structure: A contingency approach", *Corporate Governance: An International Review*, Vol. 6, No. 1, pp. 5-28.

Perego, P., Kennedy, S. and Whiteman, G. (2016), "A lot of icing but little cake? Taking integrated reporting forward", *Journal of Cleaner Production*, Vol. 136, pp. 53-64.

Pistoni, A., Songini, L. and Bavagnoli, F. (2018), "Integrated Reporting Quality: An Empirical Analysis", *Corporate Social Responsibility and Environmental Management*, available at: https://doi.org/10.1002/csr.1474 (accessed 19th May, 2018).

Rensburg, R. and Botha, E. (2014), "Is integrated reporting the silver bullet of financial communication? A stakeholder perspective from South Africa", *Public Relations Review*, Vol. 40, pp. 44-152.

Reuter, M., and Messner, M. (2015), "Lobbying on the integrated reporting framework: an analysis of comment letters to the 2011 discussion paper of the IIRC", *Accounting, Auditing and Accountability Journal*, Vol. 28, No. 3, pp. 365-402.

Rivera-Arrubla, Y. A., Zorio-Grima, A. and García-Benau, M. A. (2017), "Integrated Reports: Disclosure level and Explanatory Factors", *Social Responsibility Journal*, Vol. 13, No. 1, pp. 155-176.

Rowbottom, N. and Locke, J. (2016), "The emergence of <IR>. *Accounting and business research"*, Vol. 46, No. 1, pp. 83-115.

Simnett, R. and Huggins, A. L. (2015), "Integrated reporting and assurance: where can research add value?", *Sustainability Accounting, Management and Policy Journal*, Vol. 6, No. 1, pp. 29-53.

Stacchezzini, R., Melloni, G. and Lai, A. (2016), "Sustainability management and reporting: the role of integrated reporting for communicating corporate sustainability management", *Journal of Cleaner Production*, Vol. 136, pp. 102-110.

Stubbs, W. and Higgins, C. (2014), "Integrated reporting and internal mechanisms of change", *Accounting, Auditing and Accountability Journal*, Vol. 27, No. 7, pp. 1068-1089.

Stubbs, W., and Higgins, C. (2015). "Stakeholders' perspectives on the role of regulatory reform in integrated reporting", *Journal of Business Ethics*, Vol. 147, No.3, pp. 489-508.

Suchman, M. C. (1995), "Managing legitimacy: Strategic and institutional approaches", *Academy of management review*, Vol. 20, No. 3, pp. 571-610.

Toppinen, A., Virtanen, A., Mayer, A., and Tuppura, A. (2015), “Standardizing social responsibility via ISO 26000: Empirical insights from the forest industry”, *Sustainable Development*, Vol. 23, No. 3, pp. 153-166.

Van Bommel, K. (2014), “Towards a legitimate compromise? An exploration of Integrated Reporting in the Netherlands”, *Accounting, Auditing and Accountability Journal*, Vol. 27, No. 7, pp. 1157–1189.