CSR: The EU Directive on the Disclosure of Non-Financial and Diversity Information and Integrated Reporting

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New regulation:
EU directive 2014/95/EU

- Requires CSR information as part of annual reports
- Soon to come into effect - 2017
- EU member nations will specify
  - which firms/organizations have to report
  - what they have to report

- Large European companies (average of 500+ employees)
- Publish a non-financial report as part of the annual report
- On environment, social, human rights, bribery/corruption, impact of activities
- Likely to permeate through the supply chain and affect SMEs

Further to
EU directive 2014/95/EU

- EU member states should clarify certain matters in the directive by end 2016
- Large firms (500 employees), which are seen as public interest enterprises are included
- Public interest enterprises include listed firms, banks, insurance firms
- Member nations can add more types of enterprises to the list
- Large defined as 500 employees, 20 million Euro assets, 40 million Euro sales
- Are governmental institutions included? Should be, because in public interest
- Are NGOs included? Should be, because in public interest
- Exactly what should be included in the non-financial reporting required? Currently left open
- So, discretion left to companies
- And discretion left to EU member nations
- E.g., member states may permit the omission of information if deemed to hurt competitiveness
- Member nations may require assurance of non-financial information

EU directive 2014/95/EU
Italian development

- Must follow a standard of reporting Can be chosen by companies
- Standard companies choose must be explicitly stated
- If the methodology is the company's own - provide a detailed description
- Many will choose GRI (also possible to choose Integrated Reporting)
- Mandatory attestation of the correctness of the non-financial information
- This is the draft – therefore may change

Is Social and Environmental Reporting New?

- Started during the 1960s and 1970s with social changes and changing demands
- Companies started to report on SOCIAL and ENVIRONMENTAL issues VOLUNTARILY
- Known by various names:
  - Social and Environmental reporting
  - CSR reporting
  - Sustainability reporting
  - ESG reporting (Environment, Social, Governance)
  - Integrated reporting

What is Social and Environmental Accounting?

- Social includes accountings regarding and for:
  - employees,
  - customers,
  - society, local communities,
  - other stakeholder groups,
  - Investors – governance information
- Accounting includes:
  - reporting (or disclosure)
  - management control system to support reporting (including internal reporting)
  - assurance of reports

Global Reporting Initiative (GRI) reporting guidelines/standards

- The leading sustainability reporting guideline
- Used to have levels of reporting 10, 30, 50+ for C, B, and A level reporting
- Then core and comprehensive
- Now changed to 'standards'
- Have now moved away from expecting all companies to disclose all items
- Companies now have to decide on their important impacts
- In consultation with their stakeholders
- Then report on these important items

GRI standards

- The GRI Standards are the first global standards for sustainability reporting. They feature a modular, interrelated structure, and represent the global best practice for reporting on a range of economic, environmental and social impacts.
- **GRI 101: Foundation 2016** is the starting point for using the GRI Standards. GRI 101 can be used by an organization of any size, type, sector, or geographic location that wants to use the GRI Standards to report about its economic, environmental, and/or social impacts.
- **GRI 102: General Disclosures 2016** sets out reporting requirements on contextual information about an organization and its sustainability reporting practices. This Standard can be used by an organization of any size, type, sector or geographic location.
- **GRI 103: Management Approach 2016** sets out reporting requirements about the approach an organization uses to manage a material topic. This Standard can be used by an organization of any size, type, sector or geographic location.
- https://www.globalreporting.org/standards?dm_i=4J5,4JZIT,IX9W8,GVZWH,1

  the information above was taken from this website

GRI – how to get started

- Consult the GRI’s standards
- https://www.globalreporting.org/standards?dm_i=4J5,4JZIT,IX9W8,GVZWH,1
- Contact your financial auditor and find out whether they assist with GRI implementation
- Read the report of a company that is considered a ‘good’ GRI reporter
- Examples can be found on the GRI website at:
- https://www.globalreporting.org/services/Communication/featured-reports-service/featured-reports/Pages/default.aspx
- Choose a company from this website that is in your industry

What is integrated reporting?

A concise report

that integrates financial and non-financial information

that tells an organisation’s future value creation story

with reference to the business model and strategy

employed to extract value from the six capitals:

financial, manufactured, intellectual, human, social and relationship, and natural capital

The story may include destroying some of the capitals, while creating value in other capitals

Where does Integrated Reporting come from?

- Started in practice – around 2002 NovoZymes – part of Novo Nordysk
- Calls for IR followed
- Included in the King III Corporate Governance rules in South Africa (2009)
- IIRC (international Integrated Reporting Council) established in 2010
- IR framework published in December 2013
- Many companies internationally now publish an IR
- Some publish a One Report that does not necessarily subscribe to the IIRC guideline
- The GRI guidelines 'require' integrated reporting – and the GRI is very popular as a sustainability reporting framework

Integrated Reporting – how to get started

- Consult the IIRC’s Integrated Reporting framework
- http://integratedreporting.org/wp-content/uploads/2013/12/13-12-08-THE-INTERNATIONAL-IR-FRAMEWORK-2-1.pdf
- Contact your financial auditor and find out whether they assist with IR implementation
- Read an Integrated Report of a company that is considered a ‘good’ IR reporter
- Perhaps Generali is a good example?
- http://www.generali.com/it/who-we-are/discovering-generali/Integrated-report.html

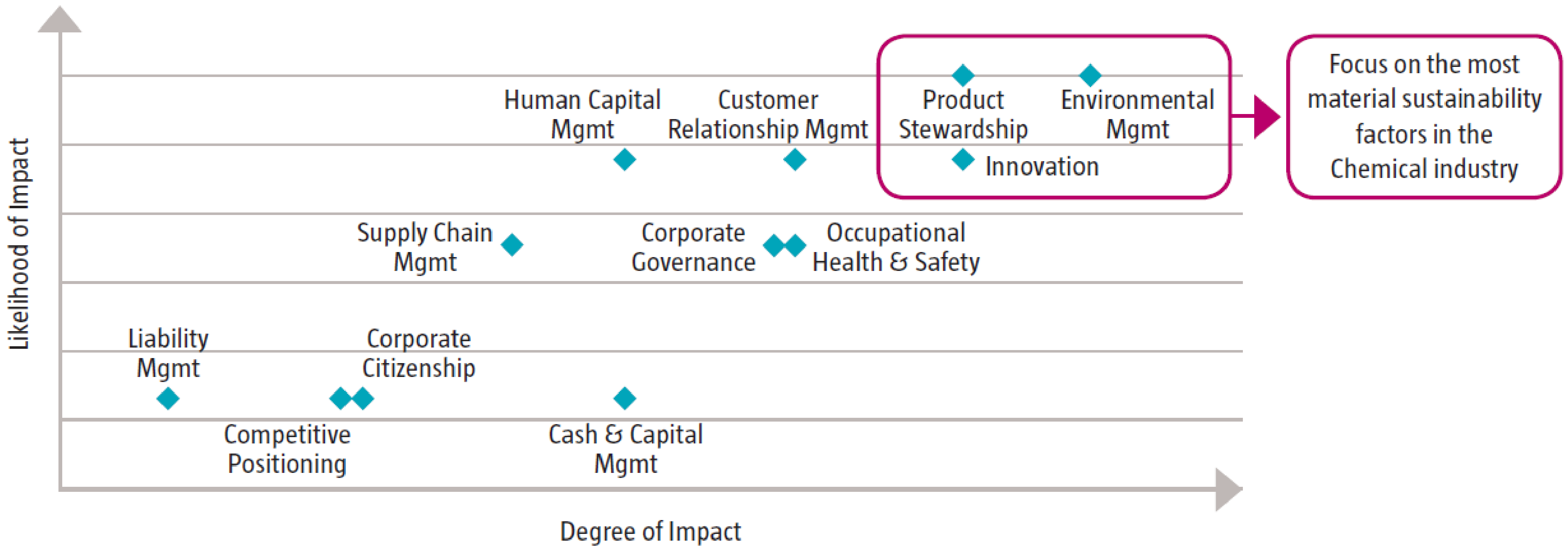
ESG (or CSR) has gone mainstream
Environment, Social, Governance (ESG)

- ESG has long been used by stakeholders
- ESG has not always been used by investors
- ESG is now increasingly used – even by investors

Investors think in terms of Risks & Returns

- Returns
  - Expected future cash flows
  - ESG related opportunities
- Risks
  - Risks associated with future cash flows
  - ESG related risks

Figure 4: Materiality matrix for the Chemical industry



Source: RobecoSAM

Figure 5: Company performance on the three most financially material sustainability criteria

Material Sustainability factor	Company's sustainability performance	Impact on value drivers
Innovation	Environmental targets for 80% of all product innovations. Product innovation (Eco+ products) revenue target = 45% of all revenues by 2015	++
Product Stewardship	Lifecycle assessment on 90% products > than peer average of 40%	+
Environmental Management	Lower CO_2 intensity than peers	+

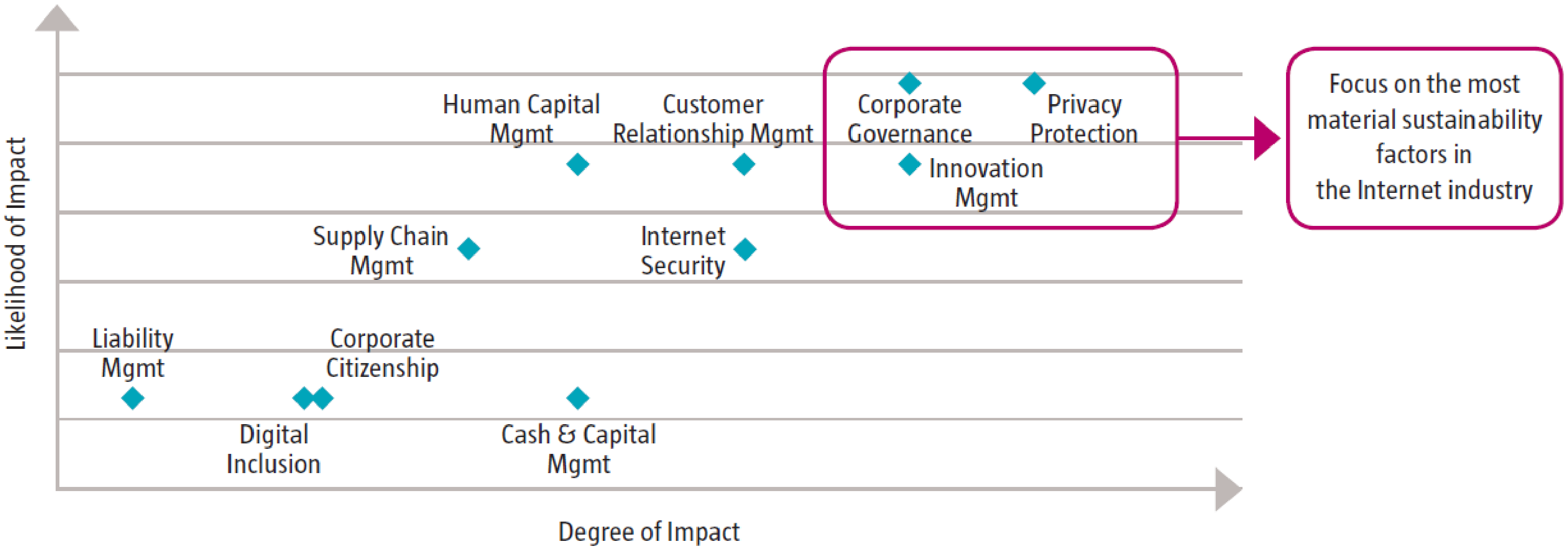
Source: RobecoSAM

Figure 6: Integrated valuation analysis of chemicals company

Drivers	Sales growth	Margins	Cost of Capital (Discount Rate)	Fair Value
	4.0%	13.7%	8%	
Valuation (ex-Sustainability)		EU recovery: > 200bps		€ 57
Sustainability factors	++ Innovation + 1%	+ Environmental Management + Product Stewardship + 1%		**+** € 10 (+ 17.5%)
Total	**5.0%**	**17% by 2017**	**8%**	**€ 67**

Source: RobecoSAM

Figure 7: Materiality matrix IT Services & Internet Software and Services industry



Source: RobecoSAM

Figure 8: Company performance on four of the most financially material sustainability criteria

Material Sustainability factor	Company's sustainability performance	Impact on value drivers
Innovation	Large investments in innovations	++
	Innovation culture	++
Human Capital Management	Ability to attract and retain highly skilled labor	+
Privacy Protection	Risk of more stringent privacy laws	–
Corporate Governance	Unbalanced voting rights	– –

Source: RobecoSAM

Figure 9: Integrated valuation analysis of internet company

Drivers	Sales growth	Margins	Cost of Capital (Discount Rate)	Fair Value
	15% (10-year estimate)	35%	8%	
Valuation (ex-Sustainability)				$ 105
Sustainability risk factors			- Privacy Protection -- Corporate Governance + 1%	- $ 15 (- 14.3%)
Total	**15%**	**35%**	**9%**	**$ 90**

Source: RobecoSAM

A few of the things we have learnt through research

- Major predictors of disclosure:
  - Industry and size, also profitability, and performance (bad perf. disclose more)
- Consequences of disclosure:
  - Lower cost of capital, higher share prices
- Where companies disclose:
  - Legitimacy crises (e.g. environmental) – websites
  - Long-standing bad (environmental) performance – annual reports
- Shareholder needs:
  - They want social and environmental disclosure
  - They are even willing to pay for it (with lower returns)
- Board characteristics influence environmental performance

Practical implication for business

- Analysts and investors use CSR information in investment decisions
- CSR reporting influence cost of capital and share prices
- The disclosure of more CSR information is potentially good for a company's cost of capital and share price
- EU directive will ensure that more companies will disclose CSR
- However, the amount and quality of the disclosure is not mandated
- To stand out from other companies and benefit – CONSIDER DISCLOSING MORE AND BETTER

Conclusion for practitioners

- Non-financial reporting
  - is happening voluntarily
  - is increasingly legislated
  - e.g. the EU directive coming into force in 2017
- Large companies will have to
  - disclose social and environmental information
  - Use a standard or guideline (GRI and IR are options)
- SMEs will have to provide SEA information to their large corporate customers

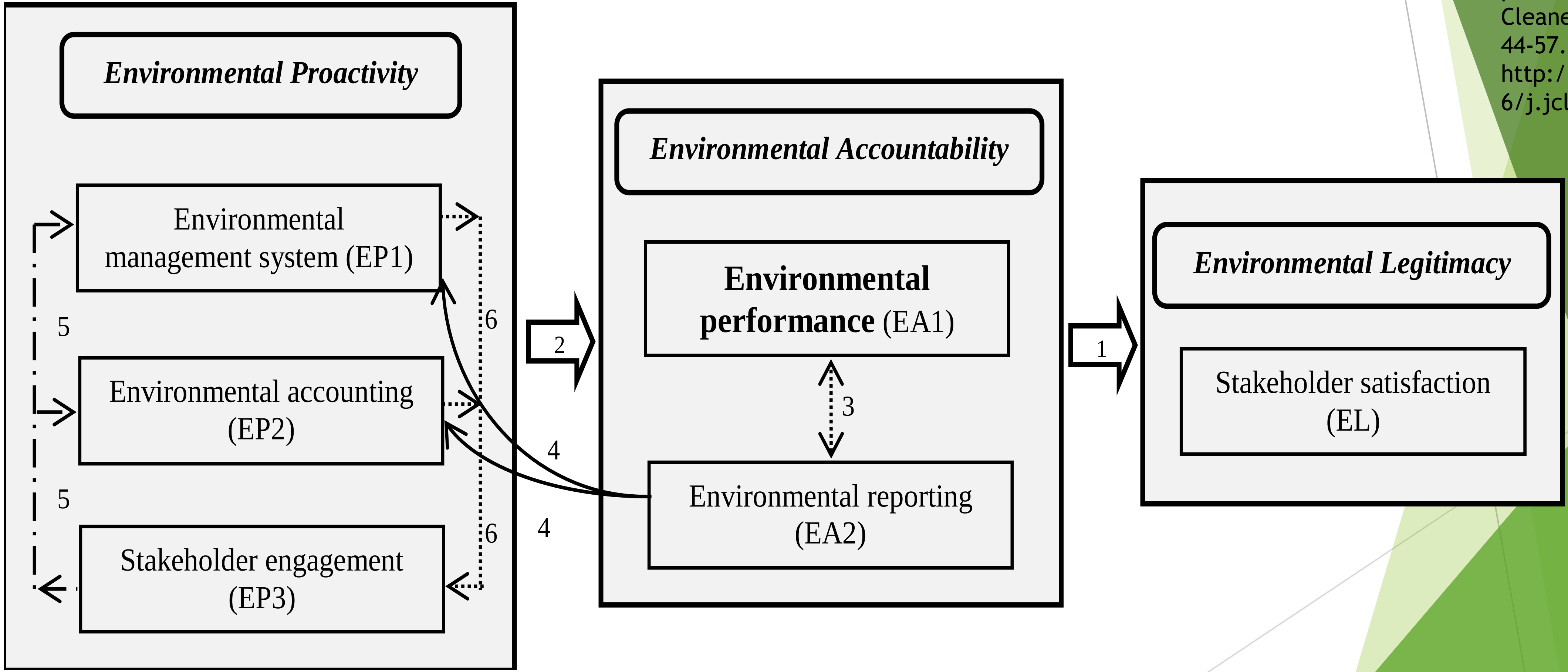
Investors think RISKS and RETURNS
Researchers think about causality

- WHAT CAUSES WHAT?

- One way to think about it is:
  - determinants and
  - consequences

Modelling influences towards sustainability

Source:
Alrazi, B., De Villiers, C. & Van Staden, C. 2015. A comprehensive literature review on, and the construction of a framework for, environmental legitimacy, accountability and proactivity. Journal of Cleaner Production, 102, 44-57. http://dx.doi.org/10.1016/j.jclepro.2015.05.022



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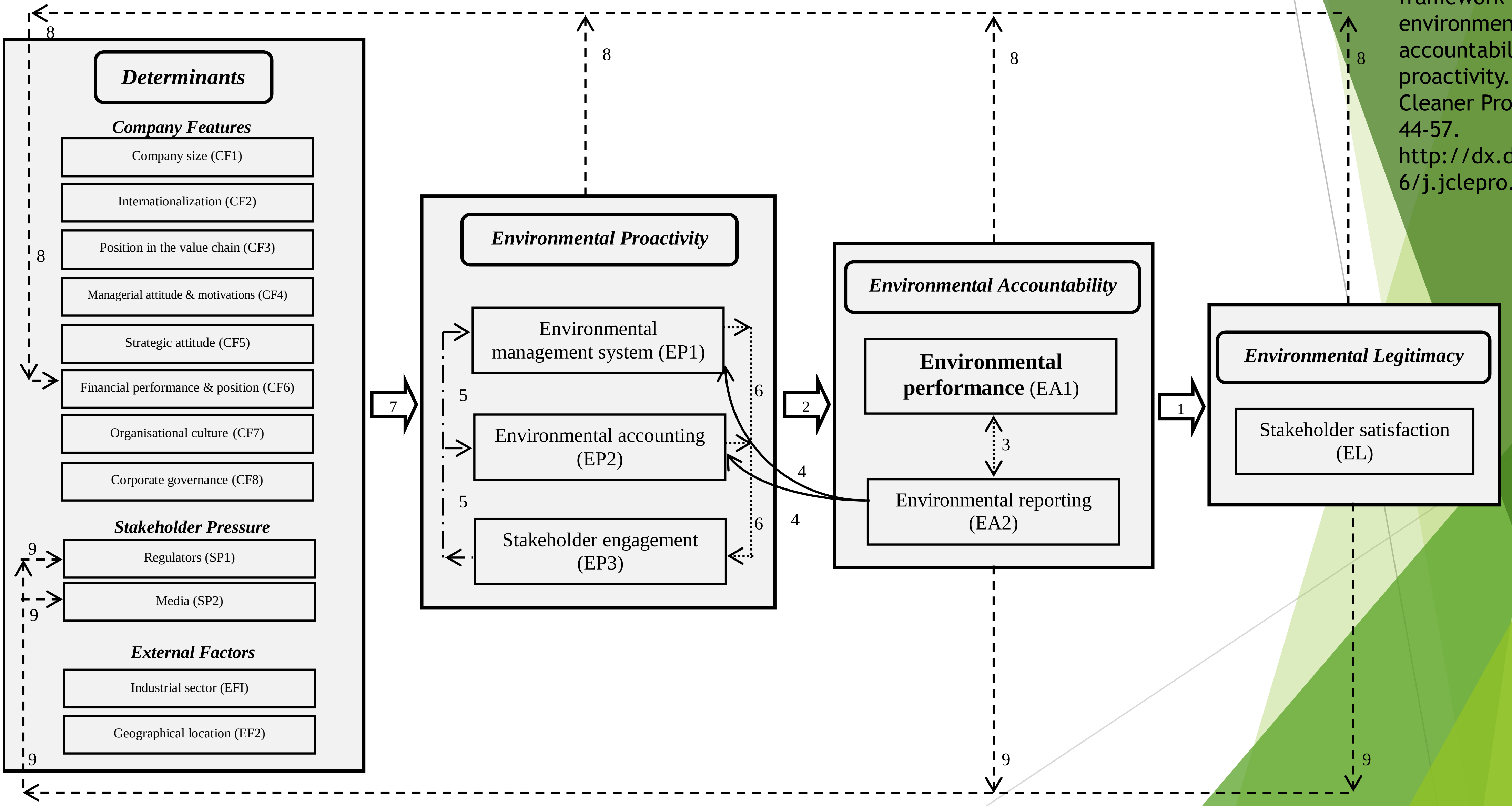

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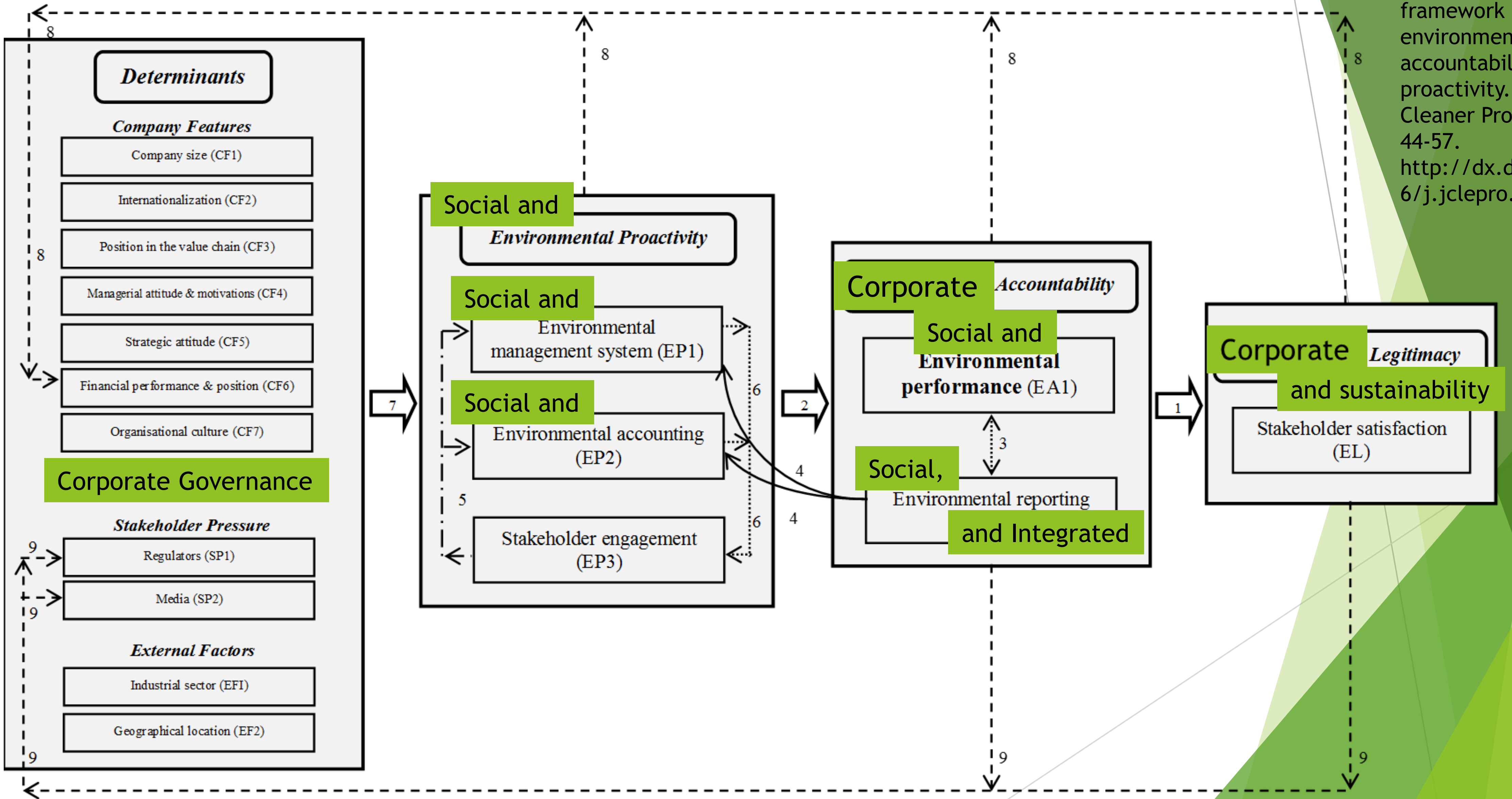

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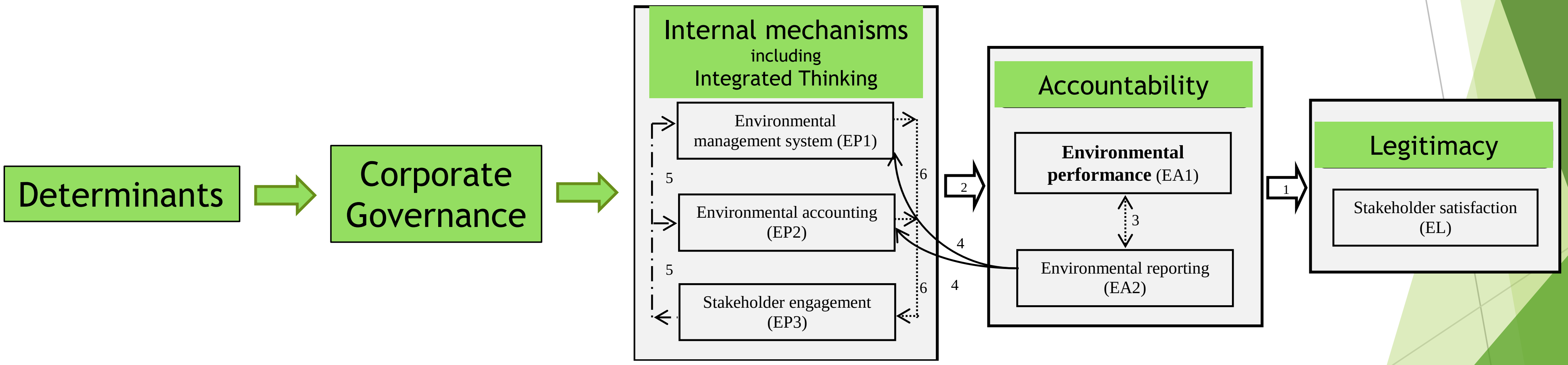
Modified model



In terms of research

- Several interesting opportunities for research
- Into CSR, SEA, Sustainability, Integrated reporting
  - Already exist
  - Will be opened up by the EU directive

- Where to start?

Integrated Reporting research opportunities – read these articles

De Villiers, C., Rinaldi, L. & Unerman, J. 2014. Integrated Reporting: Insights, gaps and an agenda for future research. *Accounting, Auditing & Accountability Journal*, 27(7), 1042-1067.

De Villiers, C., Venter, E. & Hsiao, P. 2016. Integrated reporting: Background, measurement issues, approaches and an agenda for future research, *Accounting & Finance*, forthcoming.

Case study insights from IR implementation, *Accounting, Auditing & Accountability Journal* special issue, forthcoming in 2017/8.

My list of interesting areas of research to consider in Sustainability Accounting (and Integrated Reporting)

Why companies report

- Agency theory arguments
- Legitimacy/Stakeholder theory arguments
- Institutional theory arguments

What happens to reporting after a (economic/ environmental) crisis?

Where companies report/ Performance versus disclosure

Board characteristics' influence on sustainability performance

Stakeholder requirements for corporate disclosure

Modelling the influences towards sustainability

Integrated Reporting

Internal management control mechanisms integrated with external reporting

Carbon mitigation

Accounting professions' influence on academe

Advice on article writing and construction

Some of my publications

Why companies report

- Agency theory arguments

    De Villiers, C. & Marques, A. 2015. Corporate social responsibility, country-level predispositions, and the consequences of choosing a level of disclosure. Accounting and Business Research, forthcoming. http://dx.doi.org/10.1080/00014788.2015.1039

    Cahan, S., De Villiers, C., Jeter, D., Naiker, V. & Van Staden, C. 2015. Are CSR Disclosures Value Relevant? Cross-Country Evidence. European Accounting Review, forthcoming. http://dx.doi.org/10.1080/09638180.2015.1064009

    De Klerk, M., De Villiers, C. & Van Staden, C. 2015. The influence of corporate social responsibility disclosure on share prices: Evidence from the United Kingdom. Pacific Accounting Review, 27(2): 208 - 228.

    De Klerk, M. & De Villiers, C. 2012. The Value Relevance of Corporate Responsibility Reporting by South African Companies. Meditari Accountancy Research, 20(1): 21-38.

- Legitimacy/Stakeholder theory arguments

    De Villiers, C. & Van Staden, CJ. 2006. Can less environmental disclosure have a legitimising effect? Evidence from Africa. Accounting, Organizations and Society, 31(8): 763-781.

- Institutional theory arguments

    De Villiers, C. & Alexander, D. 2014. The institutionalisation of corporate social responsibility reporting, British Accounting Review, 46: 198-212. http://dx.doi.org/10.1016/j.bar.2014.03.001

    De Villiers, C., Low, M. & Samkin, G. 2014. The institutionalisation of mining company sustainability disclosures. Journal of Cleaner Production, 84: 51-58. http://dx.doi.org/10.1016/j.jclepro.2014.01.089

What happens to reporting after a (economic/ environmental) crisis?

Pinto, S., De Villiers, C. & Samkin G. 2014. Corporate social responsibility disclosures during the global financial crisis: New Zealand evidence. NZ Journal of Applied Business Research, 12(2): 33-49.

Summerhays, K. & De Villiers, C. 2012. Oil Company Annual Report Disclosure Responses to the 2010 Gulf of Mexico Oil Spill. Journal of the Asia-Pacific Centre for Environmental Accountability, 18(2): 103-130.

Where companies report/ Performance versus disclosure

De Villiers, C. & Van Staden, C. 2011. Where firms choose to disclose voluntary environmental information. Journal of Accounting and Public Policy, 30(6): 504-525, http://dx.doi.org/10.1016/j.jaccpubpol.2011.03.005

Board characteristics' influence on performance

De Villiers, C., Naiker, V. & Van Staden, C. 2011. The Effect of Board Characteristics on Firm Environmental Performance, Journal of Management, 37(6): 1636-1663, http://dx.doi.org/10.1177/0149206311411506

Stakeholder requirements for corporate disclosure

De Villiers, C. & Van Staden, C. 2010. Shareholders' requirements for corporate environmental disclosures: a cross country comparison. British Accounting Review, 42(4): 227-240.

De Villiers, C. & Van Staden, C. 2010. Why do shareholders require corporate environmental disclosure? South African Journal of Economic and Management Sciences, 13(4): 436-445.

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Integrated Reporting

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Internal management control mechanisms integrated with external reporting

Kerr, J., Rouse, P. & De Villiers, C. 2015. Sustainability reporting integrated into management control systems. Pacific Accounting Review, 27(2): 189 - 207.

Carbon mitigation

De Villiers, C., Chen, S., Jin, C. & Zhu, Y. 2014. Carbon sequestered in the trees on a university campus: a case study. Sustainability Accounting, Management and Policy Journal, 5(2): 149 - 171.

Accounting professions' influence on academe

Venter, E. & De Villiers, C. 2013. The accounting profession's influence on academe: South African evidence. Accounting, Auditing & Accountability Journal, 26(8): 1246-1278.

Advice on article writing and construction

De Villiers, C. & Dumay, J. 2013. Construction of research articles in the leading interdisciplinary accounting journals. Accounting, Auditing & Accountability Journal, 26(6): 876 - 910.

De Villiers, C. & Dumay, J. 2014. Writing an article for a refereed accounting journal. Pacific Accounting Review, 26(3): 324-350.

Articles mapped against the model

Why companies report

EA2/8/CF6
- Agency theory arguments
  - De Villiers, C. & Marques, A. 2015. Corporate social responsibility, country-level predispositions, and the consequences of choosing a level of disclosure. Accounting and Business Research, forthcoming. http://dx.doi
  - De Klerk, M., De Villiers, C. & Van Staden, C. 2015. The influence of corporate social responsibility disclosure on share prices: Evidence from the United Kingdom. Pacific Accounting Review, 27(2): 208 - 228.
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5/2/1/9
- Legitimacy/Stakeholder theory arguments
  - De Villiers, C. & Van Staden, CJ. 2006. Can less environmental disclosure have a legitimising effect? Evidence from Africa. Accounting, Organizations and Society, 31(8): 763-781.

7/2/EA2
- Institutional theory arguments
  - De Villiers, C. & Alexander, D. 2014. The institutionalisation of corporate social responsibility reporting, British Accounting Review, 46: 198-212. http://dx.doi.org/10.1016/j.bar.2014.03.001
  - De Villiers, C., Low, M. & Samkin, G. 2014. The institutionalisation of mining company sustainability disclosures. Journal of Cleaner Production, 84: 51-58. http://dx.doi.org/10.1016/j.jclepro.2014.01.089

SF6/7/2
1/9/7/2 or 3
3

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CF8/7/2

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SP/EP/EL

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- De Villiers, C. & Van Staden, C. 2010. Why do shareholders require corporate environmental disclosure? South African Journal of Economic and Management Sciences, 13(4): 436-445.

n/a

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  http://dx.doi.org/10.1016/j.jclepro.2015.05.022

EA2

Integrated Reporting
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EP1/2/EA2

Internal management control mechanisms integrated with external reporting
- Kerr, J., Rouse, P. & De Villiers, C. 2015. Sustainability reporting integrated into management control systems. Pacific Accounting Review, 27(2): 189 - 207.

EA1

Carbon mitigation
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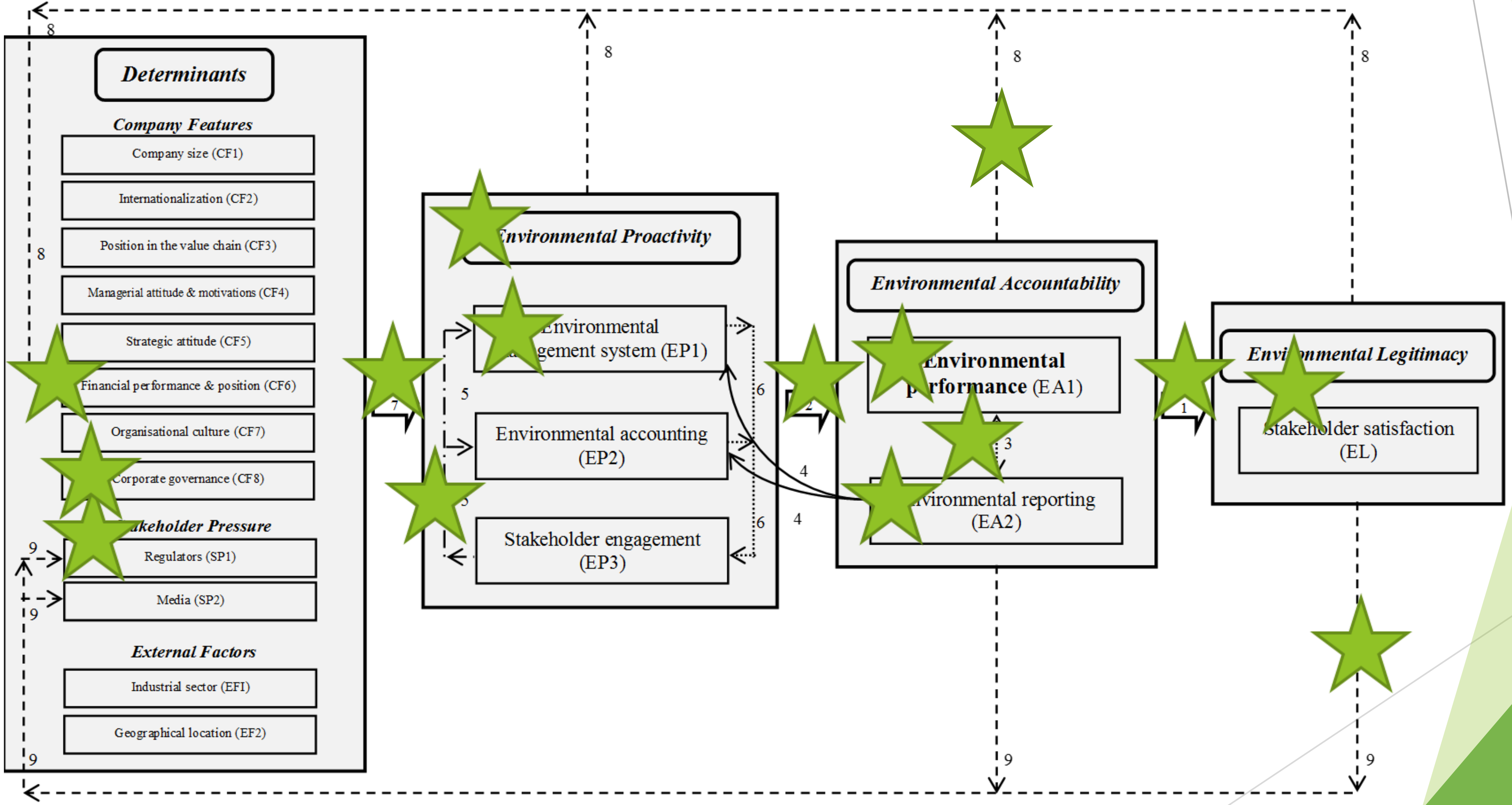
What has been covered (a little)?



So the model can be useful to:

- Identify areas of interest to research
  - E.g. the arrows marked 4 the model – the influence of reporting on management systems and accounting, i.e. the fact that companies report creates the need for additional controls and accounting

- Identify influences that needs to be thought about/controlled for when designing a research study
  - E.g. in regression analyses, the need to control for the factors in the 'determinants' box
  - E.g. in structured interviews, the need to explore the influence of stakeholder pressure (in the 'determinants' box) on the concepts in boxes towards the right

- Another possibility – do a (really) comprehensive literature review using the model as an organising framework

Thank you for the opportunity to present

Any questions or comments?